JSC Liberty Bank and Subsidiaries

Consolidated Financial Statements

Year ended 31 December 2012
Together with Independent Auditor's Report

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Independent auditors' report

To the Shareholders and Supervisory Board of JSC Liberty Bank -

We have audited the accompanying consolidated financial statements of JSC Liberty Bank and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2012, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated 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 consolidated financial statements

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

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated 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 whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2012, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ERNST & YOUNG LLC

1 April 2013

Consolidated statement of financial position

As of 31 December 2012

(Thousands of Georgian Lari)

	Notes	2012	2011
Assets			
Cash and cash equivalents	6	232,954	136,715
Amounts due from credit institutions	7	2,673	23,463
Loans to customers	8	378,118	324,240
Investment securities:			
- available-for-sale		2	411
- held-to-maturity	9	59,159	100,805
Investment properties	10	4,793	25,021
Property and equipment	11	126,095	97,201
Intangible assets	12	9,280	6,155
Current income tax assets	13	637	637
Deferred income tax assets	13	-	762
Prepayments	14	9,586	7,028
Other assets	14	15,635	9,934
Total assets		**838,932**	**732,372**
Liabilities			
Amounts due to credit institutions	15	28,173	21,212
Amounts due to customers	16	696,417	604,976
Deferred tax liabilities	13	3,746	-
Contingent capital participation notes		-	19,150
Other liabilities	14	11,934	14,258
Total liabilities		**740,270**	**659,596**
Equity	17		
Share capital		53,284	42,708
Additional paid-in capital		42,559	32,809
Preferred shares		893	-
Accumulated losses		(18,839)	(24,504)
Other reserves		20,765	21,763
Total equity		**98,662**	**72,776**
Total liabilities and equity		**838,932**	**732,372**

Signed and authorised for release on behalf of the Management Board of the Bank:

Vladimer Gurgenidze Executive Chairman and Chief Executive Officer

Zurab Tsulaia Chief Financial Officer

1 April 2013

The accompanying notes on pages 6 to 45 are an integral part of these consolidated financial statements.

Consolidated income statement

For the year ended 31 December 2012

(Thousands of Georgian Lari)

	Notes	2012	2011
Interest income			
Loans to customers		109,892	79,347
Investment securities		11,380	11,989
Amounts due from credit institutions		2,937	2,923
		124,209	**94,259**
Interest expense			
Amounts due to customers		(66,617)	(45,352)
Amounts due to credit institutions		(3,283)	(4,268)
Contingent capital participation notes		(2,264)	(2,792)
Other		(110)	(30)
		(72,274)	**(52,442)**
Net interest income		**51,935**	**41,817**
Loan impairment charge	8	(12,504)	(17,702)
Net interest income after loan impairment charge		**39,431**	**24,115**
Net fee and commission income	19	28,855	34,328
Net gains from disposal of subsidiaries		-	461
Net gains/(losses) from foreign currencies:			
- Dealing		6,056	5,056
- Translation differences		(77)	(529)
Share of (loss)/income from associates		(63)	23
Other income	20	4,880	4,562
Non-interest income		**39,651**	**43,901**
Personnel expenses	21	(37,605)	(30,742)
General and administrative expenses	21	(18,900)	(17,712)
Depreciation, amortisation and impairment		(10,005)	(9,382)
Other operating expenses		(1,902)	(1,484)
Other impairment and provisions	14	(885)	(183)
Non-interest expense		**(69,297)**	**(59,503)**
Profit before income tax expense		**9,785**	**8,513**
Income tax expense	13	**(4,601)**	**(875)**
Profit for the year		**5,184**	**7,638**
Income per share:	17		
- Basic income per share (in full amount)		0.00111	0.00237
- Diluted income per share (in full amount)		0.00110	0.00234

The accompanying notes on pages 6 to 45 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income

For the year ended 31 December 2012

(Thousands of Georgian Lari)

	Notes	2012	2011
Profit for the year		**5,184**	**7,638**
Other comprehensive income			
Impairment of the building due to fire loss		(608)	-
Unrealised losses on investment securities available-for-sale	17	-	(238)
Revaluation of buildings	17	-	(138)
Income tax relating to components of other comprehensive income	13, 17	91	27
Other comprehensive income for the year, net of tax		**(517)**	**(349)**
Total comprehensive income for the year		**4,667**	**7,289**

The accompanying notes on pages 6 to 45 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

For the year ended 31 December 2012

(Thousands of Georgian Lari)

	Attributable to shareholders of the Bank						
	Share capital	***Additional paid-in capital***	***Preferred Shares***	***Treasury shares***	***s Accumulate d losses***	***Other reserves***	***Total***
31 December 2010	**28,858**	**19,113**	**-**	**(3,371)**	**(32,692)**	**22,702**	**34,610**
Total comprehensive income/(loss) for the year	-	-	-	-	7,638	(349)	7,289
Depreciation of revaluation reserve (Note 17)	-	-	-	-	483	(483)	-
Transfer of revaluation reserve of sold asset	-	-	-	-	107	(107)	-
Issue of share capital (Note 17)	13,850	13,696	-	-	-	-	27,546
Dividends of subsidiaries	-	-	-	-	(40)	-	(40)
Sale of treasury shares (Note 17)	-	-	-	3,371	-	-	3,371
31 December 2011	**42,708**	**32,809**	**-**	**-**	**(24,504)**	**21,763**	**72,776**
Total comprehensive income/(loss) for the year	-	-	-	-	5,184	(517)	4,667
Depreciation of revaluation reserve (Note 17)	-	-	-	-	481	(481)	-
Share based payments (Note 17)	-	1,712	-	-	-	-	1,712
Issue of share capital (Note 17)	10,576	8,038	-	-	-	-	18,614
Issue of preferred shares (Note 17)	-	-	893	-	-	-	893
31 December 2012	**53,284**	**42,559**	**893**	**-**	**(18,839)**	**20,765**	**98,662**

The accompanying notes on pages 6 to 45 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

For the year ended 31 December 2012

(Thousands of Georgian Lari)

	Notes	2012	2011
Cash flows from operating activities			
Interest received		129,929	85,359
Interest paid		(70,512)	(50,658)
Fees and commissions received		33,147	38,924
Fees and commissions paid		(4,503)	(4,422)
Net realised gains from dealing in foreign currencies		6,183	5,098
Recoveries of assets previously written off	8, 14	163	106
Other income received	20	4,388	3,811
Personnel expenses paid		(36,711)	(29,692)
General, administrative and other operating expenses paid		(20,664)	(18,894)
Cash flows from operating activities before changes in operating assets and liabilities		**41,420**	**29,632**
Net (increase)/decrease in operating assets			
Amounts due from credit institutions		20,711	(16,156)
Loans to customers		(75,058)	(180,485)
Other assets		(10,304)	(1,944)
Net increase/(decrease) in operating liabilities			
Amounts due to credit institutions		6,724	(56,082)
Amounts due to customers		89,999	223,413
Other liabilities		(1,416)	1,928
Net cash flows from operating activities before income tax		**72,076**	**306**
Income tax paid		-	(182)
Net cash from operating activities		**72,076**	**124**
Cash flows from investing activities			
Proceeds from disposal of subsidiaries and associates		-	860
Proceeds from redemption of investment available-for-sale		-	367
Purchase of investment securities		(121,730)	(65,859)
Proceeds from redemption of investment securities		165,598	53,394
Purchase of intangibles, property and equipment		(20,373)	(17,362)
Proceeds from sale of property and equipment		-	577
Net cash used in investing activities		**23,495**	**(28,023)**
Cash flows from financing activities			
Proceeds from issue of share capital		-	13,850
Increase in additional paid in capital		-	13,690
Sale of treasury shares		-	3,371
Proceeds from issue of preferred shares		893	-
Dividends paid by subsidiaries		-	(40)
Net cash from financing activities		**893**	**30,871**
Effect of exchange rates changes on cash and cash equivalents		(225)	(5,528)
Net increase/(decrease) in cash and cash equivalents		**96,239**	**(2,556)**
Cash and cash equivalents, beginning	6	**136,715**	**139,271**
Cash and cash equivalents, ending	6	**232,954**	**136,715**

The accompanying notes on pages 6 to 45 are an integral part of these consolidated financial statements.

(Thousands of Georgian Lari)

1. Principal activities

JSC Liberty Bank (the "Bank") is a joint stock company, formed on the basis of the former State Bank AgromretsvBank. By the Decree number 288 of the Cabinet of Ministers of Georgia, dated 14 April 1993, and the Ordinance of the President of Georgia number 178, dated 29 May 1994, the organisational forms of state owned banks and enterprises were transformed into Joint Stock Companies. The Bank operates under a general banking license issued by the National Bank of Georgia (the "NBG"), the central bank of Georgia, on 10 February 1993, as well as licenses for foreign currency operations.

The Bank accepts deposits from the public and extends credit, transfers payments in Georgia and abroad, exchanges currencies and provides commercial and broker-dealer services to its commercial and retail customers. Its main office is in Tbilisi, Georgia and it had as of 31 December 2012, 434 (31 December 2011: 253) branches, service centers, distribution outlets and mobile banking units operating in Georgia. The Bank's registered legal address is Liberty Tower, 74 I. Chavchavadze Avenue, 0162 Tbilisi, Georgia.

As of 31 December 2012 and 2011, the following shareholders owned more than 1% of the outstanding ordinary shares. Other shareholders owned less than 1% individually of the outstanding ordinary shares.

Shareholder	***2012*** Ownership interest, %	***2011*** Ownership interest, %
Liberty Holdings Georgia LLC (former Liberty Capital LLC)	72.44%	76.46%
BNY Limited (Nominees)	11.71%	13.53%
JSC Liberty Capital	8.05%	-
Stichting Liberty ESOP*	3.16%	3.89%
Other shareholders (individually holding less than 1%)	4.64%	6.12%
Total	**100.00%**	**100.00%**

**Ordinary shares sold on a deferred payment basis to Stichting Liberty ESOP as the trustee for the share based compensation programme Note 17.*

The Bank is a publicly traded company and its ordinary shares are traded on the Georgian Stock Exchange. Free float amounted to 19.5% as of 31 December 2012. (31 December 2011: 23.1%)

The Bank is the parent company of the group (the "Group") which consists of the following entities consolidated in the financial statements:

Name	**Country of incorporation**	**The Group ownership interest** 31 December 2012	31 December 2011	**Date of incorporation**	**Activities**
Bus Stop LLC	Georgia	100.00%	100.00%	27 August 2009	Outdoor advertising
JSC Smartex (a)	Georgia	21.47%	22.24%	5 January 2009	Courier services/ Start-up incubator.

(a) 21.47% held by the Bank and 78.53% held by JSC Liberty Capital. It is not consolidated in the Group's financial statements and is recognised under the equity method of accounting.

The majority equity interest of the Group is ultimately beneficially owned and controlled by Dan Costache Patriciu.

2. Basis of preparation

General

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

The Bank and its subsidiaries maintain their accounting records in accordance with IFRS.

The consolidated financial statements have been prepared under the historical cost convention except for derivative financial instruments, investment properties, buildings and available-for-sale securities as disclosed in the accounting policies below.

These consolidated financial statements are presented in thousands of Georgian Lari ("GEL"), except per share amounts and unless otherwise indicated.

(Thousands of Georgian Lari)

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS during the year ended 31 December 2012:

Amendments to IFRS 7 "Financial Instruments: Disclosures"

The Amendments were issued in October 2010 and are effective for annual periods beginning on or after 1 July 2011. The amendment requires additional disclosure about financial assets that have been transferred but not derecognised to enable the user of the Group's financial statements to understand the relationship with those assets that have not been derecognised and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognised assets to enable the user to evaluate the nature of, and risks associated with, the entity's continuing involvement in those derecognised assets. The amendment has no impact on the Group's disclosures, financial position or performance.

Other amendments resulting from Improvements to the following standards did not have any impact on the accounting policies, financial position or performance of the Group:

- IAS 12 Income Taxes (Amendment) – Deferred Taxes: Recovery of Underlying Assets
- IFRS 1 First-Time Adoption of International Financial Reporting Standards (Amendment) – Severe Hyperinflation and Removal of Fixed Dates for First-Time Adopter

Basis of consolidation

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated in full; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognises the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognises the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognised in other comprehensive income to profit or loss.

Investments in associates

Associates are entities in which the Group generally has between 20% and 50% of the voting rights, or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognised at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Group's share of net assets of the associate. The Group's share of its associates' profits or losses is recognised in the consolidated income statement, and its share of movements in reserves is recognised in other comprehensive income. However, when the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognise further losses, unless the Group is obliged to make further payments to, or on behalf of, the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Financial assets

Initial recognition

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

Date of recognition

All regular way purchases and sales of financial assets are recognised on the trade date i.e. the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Financial assets (continued)

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Group has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period are not included in this classification. Held-to-maturity investments are subsequently measured at amortised cost. Gains and losses are recognised in the consolidated income statement when the investments are impaired, as well as through the amortisation process.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognised in other comprehensive income until the investment is derecognised or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is reclassified to the consolidated income statement. However, interest calculated using the effective interest method is recognised in the consolidated income statement.

Determination of fair value

The fair value for financial instruments traded in active market at the reporting date is based on their quoted market price or dealer price quotations (bid price for long positions and ask price for short positions), without any deduction for transaction costs.

Determination of fair value (continued)

For all other financial instruments not listed in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include net present value techniques, comparison to similar instruments for which market observable prices exist, options pricing models and other relevant valuation models.

Offsetting

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the consolidated statement of financial position.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the NBG, excluding obligatory reserves, and amounts due from credit institutions that mature within ninety days of the date of origination and are free from contractual encumbrances.

Amounts due from credit institutions

In the normal course of business, the Group maintains advances or deposits for various periods of time with other banks. Amounts due from credit institutions are initially recognised at fair value and are subsequently measured at amortised cost using the effective interest method. Amounts due from credit institutions are carried net of any allowance for impairment losses.

Derivative financial instruments

In the normal course of business, the Group enters into various derivative financial instruments including forwards and swaps in the foreign exchange and capital markets. Such financial instruments are held for trading and are recorded at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in the consolidated income statement as net gains/(losses) from trading securities or net gains/(losses) from foreign currencies dealing, depending on the nature of the instrument.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to credit institutions, amounts due to customers and debt securities issued. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method. Gains and losses are recognised in the consolidated income statement when the borrowings are derecognised as well as through the amortisation process.

If the Group purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is recognised in the consolidated income statement.

Leases

i. Finance - Group as lessee

The Group recognises finance leases as assets and liabilities in the consolidated statement of financial position at the date of commencement of the lease term at amounts equal to the fair value of the leased property or, if lower, at the present value of the minimum lease payments. In calculating the present value of the minimum lease payments the discount factor used is the interest rate implicit in the lease, when it is practicable to determine; otherwise, the Group's incremental borrowing rate is used. Initial direct costs incurred are included as part of the asset. Lease payments are apportioned between the finance charge and the reduction of the outstanding liability. The finance charge is allocated to periods during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

The costs identified as directly attributable to activities performed by the lessee for a finance lease, are included as part of the amount recognised as an asset under the lease.

ii. Operating - Group as lessee

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

iii. Operating - Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset. Lease income from operating leases is recognised in the consolidated income statement on a straight-line basis over the lease term as other income. The aggregate cost of incentives provided to lessees is recognised as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

Impairment of financial assets

The Group assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Amounts due from credit institutions and loans to customers

For amounts due from credit institutions and loans to customers carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated income statement. Interest income continues to be accrued on the reduced carrying amount based on the original effective interest rate of the asset. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the consolidated income statement.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

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

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Held-to-maturity financial investments

For held-to-maturity investments the Group assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated income statement.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, any amounts formerly charged are credited to the consolidated income statement.

Available-for-sale financial investments

For available-for-sale financial investments, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the consolidated income statement – is reclassified from other comprehensive income to the consolidated income statement. Impairment losses on equity investments are not reversed through the consolidated income statement; increases in their fair value after impairment are recognised in other comprehensive income.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in the consolidated income statement. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the consolidated income statement, the impairment loss is reversed through the consolidated income statement.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due.

The accounting treatment of such restructuring is conducted in 2 basic scenarios:

- If the loan restructuring is not caused by the financial difficulties of the borrower but the cash flows were renegotiated, the loan is not recognized as impaired. The loan is not derecognised but the new effective interest rate is determined based on the remaining cash flows under the loan agreement till maturity. If the new effective interest rate is below the market rate at the date of restructuring, the new carrying amount is calculated as the fair value of the loan after restructuring, being the present value of the future cash flows discounted using the market rate at the date of restructuring. In this case, the difference between the carrying amount before restructuring and the fair value of the loan after restructuring is recognized as a loss on loans restructuring.

- If the loan is impaired after restructuring, the Group uses the original effective interest rate in respect of new cash flows to estimate the recoverable amount of the loan. The difference between the recalculated present value of the new cash flows taking into account collateral and the carrying amount before restructuring is included in loan impairment charge for the period.

Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- the rights to receive cash flows from the asset have expired;
- the Group has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- the Group either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

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, and the difference in the respective carrying amounts is recognised in the consolidated income statement.

Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, in 'Other liabilities', being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of the expenditure that is required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the consolidated income statement. The premium received is recognised in the consolidated income statement on a straight-line basis over the life of the guarantee.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Taxation

The current income tax expense is calculated in accordance with the regulations of Georgia. It represents the sum of the current and deferred tax expenses.

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

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

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

Georgia also has various operating taxes, which are assessed on the Group's activities. These taxes are included as a component of other operating expenses.

Property and equipment

Property and equipment, except for buildings, is carried at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Following initial recognition at cost, buildings are carried at a revalued amount, which is the fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Valuations are performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount.

Accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Any revaluation surplus is credited to the revaluation reserve for property and equipment included in other comprehensive income, except to the extent that it reverses a revaluation decrease of the same asset previously recognised in the consolidated income statement, in which case the increase is recognised in the consolidated income statement. A revaluation deficit is recognised in the consolidated income statement, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the revaluation reserve for property and equipment.

An annual transfer from the revaluation reserve for property and equipment to retained earnings is made for the difference between depreciation based on the revalued carrying amount of the assets and depreciation based on the assets original cost. Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis at the following annual prescribed rates:

Buildings and other real estate	2%-5%
Furniture and fixtures	15%-20%
Computer and office equipment	20%-25%
Motor vehicles	20%-25%
Leasehold improvements	10%-25%

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalisation.

Leasehold improvements are amortized over the life of the related leased asset

Assets under construction comprise costs directly related to construction of property and equipment including an appropriate allocation of directly attributable variable and fixed overheads that are incurred in construction. Depreciation of these assets, on the same basis as similar property assets, commences when the assets are put into operation.

Compensation from third parties for items of property, plant and equipment that were impaired, lost or given up is included in other income when the compensation becomes receivable.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Investment properties

The Group holds certain properties as investments to earn rental income, generate capital appreciation or both. Investment properties are measured initially at cost, including subsequent costs. Subsequent to initial recognition, investment properties are stated to fair values. Gains or losses arising from changes in fair values of investment properties are included in the consolidated income statement in other income or other operating expenses lines.

Intangible assets

Intangible assets include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. The useful lives of intangible assets are assessed to be finite. Intangible assets with finite lives are amortised over the useful economic lives of 5 to 10 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired.
Costs associated with maintaining computer software programs are recorded as an expense as incurred.

Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Assets classified as held-for-sale

The Group classifies a non-current asset as held-for-sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the non-current asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable.

The sale qualifies as highly probable if the Bank's management is committed to a plan to sell the non-current asset (or disposal group) and an active program to locate a buyer and complete the plan must have been initiated. Further, the non-current asset (or disposal group) must have been actively marketed for a sale at price that is reasonable in relation to its current fair value and in addition the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification of the non-current asset (or disposal group) as held for sale.

The Group measures an asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Group recognises an impairment loss for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell if events or changes in circumstance indicate that their carrying amount may be impaired.

Equity

Share capital and additional paid in capital

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

Treasury shares

Where the Bank purchase the Bank's shares, the consideration paid, including any attributable transaction costs, net of income taxes, is deducted from total equity as treasury shares until they are cancelled, sold or reissued. Where such shares are subsequently sold or reissued, any consideration received is included in equity. Treasury shares are stated at weighted average cost.

Dividends

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

Segment reporting

The Group's segment reporting is based on the following operating segments: Retail Banking, Corporate and SME (Small & Medium Size) Banking, Private Banking and Corporate Centre functions.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Contingencies

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

Retirement and other benefit obligations

The Group does not have any pension arrangements separate from the state pension system of Georgia. In addition, the Group has no post-retirement benefits.

Share-based payment transactions

Employees (including senior executives) of the bank receive remuneration in the form of share–based payment transactions, whereby employees render services as consideration for equity instruments ('equity–settled transactions').

Equity–settled transactions

The cost of equity settled transactions with employees is measured by reference to the fair value at the date on which they are granted.

The cost of equity–settled transactions is recognised, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('the vesting date'). The cumulative expense recognised for equity–settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Bank's best estimate of the number of equity instruments that will ultimately vest. The income statement expense or credit for a period is recorded in 'Personnel expenses' and represents the movement in cumulative expense recognised as at the beginning and end of that period.

Where the terms of an equity–settled award are modified, the minimum expense recognised in 'Personnel expenses' is the expense as if the terms had not been modified. An additional expense is recognised for any modification which increases the total fair value of the share–based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Where an equity–settled award is cancelled, it is treated as if it had vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non–vesting conditions within the control of either the entity or the counterparty are not met. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of diluted earnings per share (Note 17).

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

For all financial instruments measured at amortised cost and interest bearing securities classified as trading or available-for-sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the original effective interest rate applied to the new carrying amount.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Fee and commission income

The Group earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- *Fee income earned from services that are provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan.

- *Fee income from providing transaction services*

Fees arising from negotiating or participating in the negotiation of a transaction for a third party – such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses – are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Dividend income

Revenue is recognised when the Groups' right to receive the payment is established.

Foreign currency translation

The consolidated financial statements are presented in Georgian Lari, which is the Bank's and subsidiaries' functional and presentation currency. Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognised in the consolidated income statement as gains less losses from foreign currencies - translation differences. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the NBG exchange rate on the date of the transaction are included in gains less losses from dealing in foreign currencies.

The exchange rates used by the Group in the preparation of the consolidated financial statements as at 31 December 2012 and 31 December 2011 are as follows:

	2012	*2011*
GEL/1 US Dollar	1.6567	1.6703
GEL/1 Euro	2.1825	2.1614

Future changes in accounting policies

Standards and interpretations issued but not yet effective

Up to the date of approval of the consolidated financial statements, certain new standards, interpretations and amendments to existing standards have been published that are not yet effective for the current reporting period and which the Group has not early adopted, as follows:

IFRS 9 "Financial Instruments"

IFRS 9, as issued, reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard was initially effective for annual periods beginning on or after 1 January 2013, but Amendments to IFRS 9 mandatory Effective Date of IFRS 9 and Transition Disclosures, issued in December 2011, moved the mandatory effective date to 1 January 2015. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The Group will quantify the effect of the adoption of the first phase of IFRS 9 in conjunction with the other phases, at the time the other phases are issued issued, to present a comprehensive picture.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Future changes in accounting policies (continued)

IFRS 10 Consolidated Financial Statements

IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require management to exercise significant judgement to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27. In addition IFRS 10 introduces specific application guidance for agency relationships. IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. It also includes the issues raised in SIC-12 Consolidation — Special Purpose Entities. It is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The Group is currently evaluating the possible effect of the adoption of IFRS 10 on its financial position and performance.

IFRS 11 Joint Arrangements

IFRS 11 removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method. IFRS 11 supersedes IAS 31 Interests in Joint Ventures and SIC-13 Jointly Controlled Entities—Non-monetary Contributions by Venturers and is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The Group expects that adoption of IFRS 11 will have no effect on its financial position and performance.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 is effective for annual periods beginning on or after 1 January 2013. IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required. In particular, the Group will need to disclose more information about the consolidated and unconsolidated structured entities with which it is involved or which it has sponsored. However, the standard will have no impact on Group's financial position or performance.

IFRS 13 Fair Value Measurement

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. IFRS 13 is effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted. The adoption of the IFRS 13 may have effect on the measurement of the Group's assets and liabilities accounted for at fair value. The Group is currently evaluating the possible effect of the adoption of IFRS 13 on its financial position and performance. However, currently the Bank is assessing the impact of this change.

IAS 27 Separate Financial Statements (as revised in 2011)

As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. The amendment becomes effective for annual periods beginning on or after 1 January 2013.

IAS 28 Investments in Associates and Joint Ventures (as revised in 2011)

As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates. The amendment becomes effective for annual periods beginning on or after 1 January 2013.

Standards and interpretations issued but not yet effective (continued)

Amendments to IAS 19 Employee Benefits

The IASB has published amendments to IAS 19 Employee Benefits, effective for annual periods beginning on or after 1 January 2013, which involve major changes to the accounting for employee benefits, including the removal of the option for deferred recognition of changes in pension plan assets and liabilities (known as the "corridor approach"). In addition, these amendments will limit the changes in the net pension asset (liability) recognised in profit or loss to net interest income (expense) and service costs. The Group expects that these amendments will have no impact on the Group's financial position.

(Thousands of Georgian Lari)

3. Summary of accounting policies (continued)

Future changes in accounting policies (continued)

Amendments to IAS 1 Changes to the Presentation of Other Comprehensive Income

The amendments to IAS 1 change the grouping of items presented in other comprehensive income. Items that could be reclassified (or recycled) to profit or loss at a future point in time (for example, net losses or gains on available-for-sale financial assets) would be presented separately from items that will never be reclassified (for example, revaluation of buildings). The amendment affects presentation only and has no impact on the Group's financial position or performance. The amendment becomes effective for annual periods beginning on or after 1 July 2012.

Amendments to IFRS 7 Disclosures – Offsetting Financial assets and Financial Liabilities

These amendments require an entity to disclose information about rights to set-off and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The new disclosures are required for all recognized financial instruments that are set off in accordance with IAS 32 Financial Instruments: Presentation. The disclosures also apply to recognised financial instruments that are subject to an enforceable master netting arrangement or similar agreements, irrespective of whether they are set off in accordance with IAS 32. These amendments will not impact the Group's financial position or performance. These amendments will become effective for annual periods beginning on or after 1 January 2013.

Amendments to IAS 32 – Offsetting Financial Assets and Financial Liabilities

These amendments clarify the meaning of "currently has a legally enforceable right to set-off". It will be necessary to assess the impact to the Group by reviewing settlement procedures and legal documentation to ensure that offsetting is still possible in cases where it has been achieved in the past. In certain cases, offsetting may no longer be achieved. In other cases, contracts may have to be renegotiated. The requirement that the right of set-off be available for all counterparties to the netting agreement may prove to be a challenge for contracts where only one party has the right to offset in the event of default.

The amendments also clarify the application of the IAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. While many settlement systems are expected to meet the new criteria, some may not. As the impact of the adoption depends on the Group's examination of the operational procedures applied by the central clearing houses and settlement systems it deals with to determine if they meet the new criteria, it is not practical to quantify the effects.

These amendments become effective for annual periods beginning on or after 1 January 2014.

Amendment to IFRS 1 – Government loans

These amendments require first-time adopters to apply the requirements of *IAS 20 Accounting for Government Grants and Disclosure of Government Assistance*, prospectively to government loans existing at the date of transition to IFRS. The amendment will have no impact on the Group.

Improvements to IFRS

The amendments are effective for annual periods beginning on or after 1 January 2013 and will have no impact on the Group:

- IFRS 1 First-time Adoption of International Financial Reporting Standards: This improvement clarifies that an entity that stopped applying IFRS in the past and chooses, or is required, to apply IFRS, has the option to re-apply IFRS 1. If IFRS 1 is not re-applied, an entity must retrospectively restate its financial statements as if it had never stopped applying IFRS.
- IAS 1 Presentation of Financial Statements: This improvement clarifies the difference between voluntary additional comparative information and the minimum required comparative information. Generally, the minimum required comparative information is the previous period.
- IAS 16 Property Plant and Equipment: This improvement clarifies that major spare parts and servicing equipment that meet the definition of property, plant and equipment are not inventory.
- IAS 32 Financial Instruments, Presentation: This improvement clarifies that income taxes arising from distributions to equity holders are accounted for in accordance with IAS 12 Income Taxes.
- IAS 34 Interim Financial Reporting: The amendment aligns the disclosure requirements for total segment assets with total segment liabilities in interim financial statements. This clarification also ensures that interim disclosures are aligned with annual disclosures.

(Thousands of Georgian Lari)

4. Significant accounting judgments and estimates

The preparation of the Group's consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the balance sheet date and the reported amount of income and expenses during the year ended. Management evaluates its estimates and judgments on an ongoing basis. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. The following estimates and judgments are considered important to the Group's financial condition.

Allowance for impairment of loans

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

The Group 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 Group 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 Group uses management's judgment to adjust observable data for a group of loans to reflect current circumstances not reflected in historical data.

The Group considers the fair value of collateral when estimating the amount of impairment loss for collateralized loans and receivables and finance lease receivables. Management monitors market value of collateral on a regular basis. Management uses its experienced judgment or independent opinion to adjust the fair value to reflect current circumstances. The amount and type of collateral required depends on the assessment of credit risk of the counterparty.

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

Measurement of fair value of investment properties and buildings

Investment properties and buildings are stated at fair value. The fair value represents the amount at which the assets could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction at the date of valuation, in accordance with International Valuation Standards Committee standards.

Buildings of the Group are subject to revaluation on a regular basis. The date of latest revaluation was 31 December 2011. As at 31 December 2012 the Group analysed market prices for its premises and concluded that the market price of premises was not materially different from their carrying value. Refer to Note 11.

Fair value of investment properties was determined by independent professionally qualified appraisers as at 31 December 2012. Fair value was determined by applying income approach based on discounted cash flow method, supported by the terms of any existing lease and other contracts and, when available, by external evidence such as current market rents for similar properties in a comparable location and condition, and using discount rates that reflect current market assessments of the uncertainty in the amount and timing of the cash flows. The estimates of future cash flows include projections of cash outflows for rent or purchase of the land. The key assumptions used to determine the fair value of the investment properties, are further explained in Note 10.

The estimates described above are subject to change as new transaction data and market evidence become available.

Taxation

Tax legislation in Georgia is subject to varying interpretations, and changes can occur frequently. Management interpretation of such legislation and changes as applied to the transactions and activity of the Bank may be challenged by the relevant authorities. As such, additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for six years including the year of review. Management believes that as at 31 December 2012 its interpretation of the relevant legislation is appropriate and that the Bank's tax position will be sustained.

Management of the Bank believes that it is probable that sufficient taxable profits will be available to utilise the tax loss carry-forward before its expiration.

(Thousands of Georgian Lari)

5. Segment information

For management purposes, the Group is organised into the following operating segments based on products and service:

Retail Banking	Principally handling individual customers' deposits, and providing consumer loans, overdrafts, credit cards facilities and funds transfer facilities.
Corporate and SME Banking	Principally handling loans and other credit facilities and deposit and current accounts for corporate and institutional customers.
Private Banking	Principally providing private banking and wealth management services to high net worth individuals.
Corporate Centre	Principally providing treasury and back office services to all operating segments of the Bank.
Other	Segments not classified above, comprising non-banking operations.

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance, as explained in the table below, is measured differently from profit or loss in the consolidated financial statements. Income taxes are managed on a group basis and are not allocated to operating segments.

The Group operates in one geographical market – Georgia. Since the Group's assets are located in single geographical area, the Group's external income, total assets and capital expenditure are allocated to single location.

Transactions between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

Revenue from transactions with Social Service Agency amounted to GEL 8,499 (2011: GEL 17,199) representing 9.43% (2011: 20.0%) of the Group's total revenue for the year ended 31 December 2012.

2012	*Retail Banking*	*Corporate & SME Banking*	*Private Banking*	*Corporate Centre*	*Other*	*Adjustments & Eliminations*	*Total*
Revenue							
Net interest income	37,692	4,634	754	8,850	2	3	51,935
Net fee and commission income	17,360	7,737	72	3,730	(44)	-	28,855
Net gains from foreign currencies	1,196	896	119	3,768	-	-	5,979
Other income	400	3,660	47	573	443	(306)	4,817
Total revenue	**56,648**	**16,927**	**992**	**16,921**	**401**	**(303)**	**91,586**
Net impairment charge on interest-bearing assets	(2,707)	(5,549)	(55)	(4,691)	-	498	(12,504)
Personnel expenses	(27,816)	(5,886)	(372)	(3,510)	(21)	(0)	(37,605)
Depreciation and amortisation	(6,427)	(1,482)	-	(1,976)	(120)	(0)	(10,005)
Other impairment and provisions	(228)	(131)	(9)	(20)	-	(497)	(885)
General and administrative and other operating expenses	(12,334)	(4,025)	(315)	(4,072)	(350)	294	(20,802)
Segment results	**7,136**	**(146)**	**241**	**2,652**	**(90)**	**(8)**	**9,785**
Income tax expense	-	-	-	-	-	-	(4,601)
Profit for the year	-	-	-	-	-	-	**5,184**
Segment assets	747,590	54,134	14,649	23,353	930	(1,724)	838,932
Segment liabilities	252,360	406,558	53,692	27,638	179	(157)	740,270
Other segment information							
Investments in associates	-	-	-	171	-	-	**171**
Share of income of associates	-	-	-	(63)	-	-	**(63)**

(Thousands of Georgian Lari)

5. Segment information (continued)

2011	*Retail Banking*	*Corporate & SME Banking*	*Private Banking*	*Corporate Centre*	*Other*	*Adjustments & Eliminations*	*Total*
Revenue							
External							
Net interest income	30,034	4,301	634	6,850	-	(2)	41,817
Net fee and commission income	20,649	9,203	85	4,436	(44)	(1)	34,328
Net gains from foreign currencies	906	678	90	2,852	(1)	2	4,527
Other income	436	3,990	51	625	376	(432)	5,046
Total revenue	**52,025**	**18,172**	**860**	**14,763**	**331**	**(433)**	**85,718**
Net impairment charge on interest-bearing assets	(3,699)	(7,584)	(75)	(6,411)	-	67	(17,702)
Personnel expenses	(22,376)	(4,735)	(299)	(2,823)	(38)	(471)	(30,742)
Depreciation, amortisation and impairment	(6,028)	(1,390)	-	(1,854)	(110)	-	(9,382)
Other impairment and provisions	(65)	(38)	(3)	(6)	1	(72)	(183)
General and administrative and other operating expenses	(11,099)	(3,622)	(284)	(3,665)	(404)	(122)	(19,196)
Segment results	**8,758**	**803**	**199**	**4**	**(220)**	**(1,031)**	**8,513**
Income tax expense	-	-	-	-	-	-	(875)
Profit for the year	-	-	-	-	-	-	**7,638**
Segment assets	560,496	148,161	18,159	6,243	1,194	(1,881)	732,372
Segment liabilities	173,106	418,253	37,039	31,167	152	(121)	659,596
Other segment information							
Investments in associates	-	-	-	70	-	-	**70**
Share of income of associates	-	-	-	23	-	-	**23**

6. Cash and cash equivalents

Cash and cash equivalents comprise:

	2012	*2011*
Cash on hand	84,839	64,753
Current accounts with the NBG	46,867	42,442
Current accounts with other credit institutions	17,987	21,020
Time deposits with credit institutions up to 90 days	83,261	8,500
Cash and cash equivalents	**232,954**	**136,715**

As of 31 December 2012, GEL 11,527 (31 December 2011: GEL 15,705) was placed on current and time deposit accounts with internationally recognised OECD banks that are the counterparties of the Group in performing international settlements. As of 31 December 2012, GEL 83,261 (31 December 2011: GEL 8,500) was placed on short-term time and overnight deposits with the NBG. The interest rates on time deposits with credit institutions up to 90 days range between 2.5% - 5.0% per annum.

7. Amounts due from credit institutions

Amounts due from credit institutions comprise:

	2012	*2011*
Time deposits for more than 90 days	2,673	4,176
Obligatory reserve with the NBG	-	19,287
Amounts due from credit institutions	**2,673**	**23,463**

As of 31 December 2012, GEL 2,673 (31 December 2011: GEL 4,176) was placed on current accounts and inter-bank deposits with internationally recognised OECD banks, that are the main counterparties of the Group in performing international settlements. The interest rate on such deposits is between 0.1% - 2.5% per annum.

On 21 November 2012 the Bank obtained the Waiver from the NBG to maintain zero obligatory reserves with them for the period starting 22 November 2012 to 16 January 2013. Subsequent to the year end and after the expiration of the Waiver the Bank has maintained the obligatory reserves as required by the NBG.

(Thousands of Georgian Lari)

8. Loans to customers

	2012	*2011*
Loans to retail clients with regular inflows	260,038	228,763
Corporate & SME loans	38,446	78,646
Consumer loans	38,183	25,985
Micro loans	22,634	7,409
Gold pawn loans	20,215	5,033
Residential mortgage loans	19,428	14,540
Gross loans to customers	**398,944**	**360,376**
Less – allowance for impairment	(20,826)	(36,136)
Loans to customers	**378,118**	**324,240**

Allowance for impairment of loans to customers

A reconciliation of the allowance for impairment of loans to customers by class is as follows:

	Loans to retail clients with regular inflows 2012	*Corporate & SME loans 2012*	*Consumer loans 2012*	*Micro loans 2012*	*Residential mortgage loans 2012*	*Gold pawn loans 2012*	*Total 2012*
At 1 January 2012	**9,642**	**17,562**	**8,358**	**291**	**283**	**-**	**36,136**
Charge for the year	6,860	3,496	1,810	156	182	-	**12,504**
Recoveries	126	-	37	-	-	-	**163**
Amounts written off	(5,589)	(11,151)	(2,249)	-	-	-	**(18,989)**
Interest accrued on impaired loans	(720)	(5,722)	(2,546)	-	-	-	**(8,988)**
At 31 December 2012	**10,319**	**4,185**	**5,410**	**447**	**465**	**-**	**20,826**
Individual impairment	8,358	3,750	3,328	149	286	-	**15,871**
Collective impairment	1,961	435	2,082	298	179	-	**4,955**
	10,319	**4,185**	**5,410**	**447**	**465**	**-**	**20,826**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**8,358**	**5,012**	**3,328**	**149**	**286**	**-**	**17,133**

	Loans to retail clients with regular inflows 2011	*Corporate & SME loans 2011*	*Consumer loans 2011*	*Micro loans 2011*	*Residential mortgage loans 2011*	*Gold pawn loans 2011*	*Total 2011*
At 1 January 2011	**1,520**	**16,294**	**6,965**	**-**	**-**	**-**	**24,779**
Charge for the year	8,721	4,457	3,950	291	283	-	**17,702**
Recoveries	3	7	91	-	-	-	**101**
Amounts written-off	(501)	(2,985)	(2,254)	-	-	-	**(5,740)**
Interest accrued on impaired loans	(101)	(211)	(394)	-	-	-	**(706)**
At 31 December 2011	**9,642**	**17,562**	**8,358**	**291**	**283**	**-**	**36,136**
Individual impairment	8,184	17,352	6,511	216	140	-	**32,403**
Collective impairment	1,458	210	1,847	75	143	-	**3,733**
	9,642	**17,562**	**8,358**	**291**	**283**		**36,136**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**8,184**	**23,913**	**6,637**	**216**	**228**	**-**	**39,178**

(Thousands of Georgian Lari)

8. Loans to customers (continued)

Individually impaired loans

Interest income accrued on loans, for which individual impairment allowances have been recognised as at 31 December 2012 comprised GEL 2,356 (2011: GEL 8,727). Related allowance charges were recognised both in 2012 and 2011 and are recorded in consolidated income statement under net impairment charge on interest-bearing assets.

Collateral and other credit enhancements

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 lending to legal entities, charges over real estate properties, inventory and trade receivables,
- For retail lending, mortgages over residential properties and gold over gold pawns.

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 loan impairment.

Concentration of loans to customers

As of 31 December 2012, the concentration of loans granted by the Group to ten largest third party borrowers comprised GEL 16,096 accounting for 4.0% of the gross loan portfolio of the Group (2011: GEL 43,482 and 12.1%, respectively). An allowance of GEL 2,896 (2011: GEL 16,528) was established against these loans.

Loans have been extended to the following types of customers:

	2012	*2011*
Individuals	364,445	283,379
Private companies	34,215	73,457
State owned companies	284	3,540
Loans to customers, gross	**398,944**	**360,376**
Less - allowance for loan impairment	(20,826)	(36,136)
Loans to customers, net	**378,118**	**324,240**

Loans are made principally within Georgia in the following industry sectors:

	2012	*2011*
Individuals	364,445	283,379
Trade and service	26,722	57,413
Construction	2,941	3,631
Agriculture	61	-
Other	4,775	15,953
Loans to customers, gross	**398,944**	**360,376**
Less - allowance for loan impairment	(20,826)	(36,136)
Loans to customers, net	**378,118**	**324,240**

9. Investment securities held-to-maturity

Held-to-maturity securities comprise:

	2012	*2011*
Treasury bonds of the Ministry of Finance	52,184	69,198
Treasury bills of the Ministry of Finance	6,975	29,000
Corporate bonds of state owned Georgian Railway LLC	-	2,607
Held-to-maturity securities	**59,159**	**100,805**

(Thousands of Georgian Lari)

10. Investment properties

	2012	*2011*
At 1 January	25,021	21,115
Additions	-	74
Transfer (out) in	(20,204)	2,574
Net change in fair value	(24)	1,258
At 31 December	**4,793**	**25,021**

Investment properties primarily comprise of class B office space located in downtown Zugdidi with total rental space of 1,848 square meters and the warehouse building located in an industrial area of Tbilisi with storage space of 7,850 square meters; as well as several other properties located outside of Tbilisi.

The Bank transferred from investment properties the portion of Liberty Tower, which is a 19 storey building in a prime residential and commercial downtown area of Tbilisi and is wholly-owned by the Bank previously recorded as investment property. The primary reason being the fact that as the Bank has expanded its operations almost entire building has been occupied by the Bank and only immaterial portion is rented out.

Investment properties are stated at fair value, which has been determined based on valuation performed by GREMIC, an accredited independent appraiser, as at 31 December 2012. GREMIC is an industry specialist in valuing these types of investment properties. The fair value represents the amount at which the asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction at the date of valuation, in accordance with International Valuation Standards Committee standards. GREMIC used the income approach for the purposes of valuation of the investment properties.

The table below sets out the rental income and the direct operating expenses in respect of the investment properties:

	2012	*2011*
Rental income	210	512
Direct operating expenses	5	26

The entire amount of direct operating expenses participated in the generation of rental income during the respective periods.

11. Property and equipment

The movements in property and equipment were as follows:

	Land and buildings	*Furniture and fixtures*	*Computers and office equipment*	*Motor vehicles*	*Leasehold improvements*	*Assets under construction*	*Total*
Cost or revalued amount							
31 December 2011	**60,379**	**30,341**	**11,702**	**9,369**	**4,735**	**1,740**	**118,266**
Additions	5,080	6,598	3,868	2,589	722	437	**19,294**
Write offs	-	(623)	-	(492)	(590)	-	**(1,705)**
Transfers	1,001	-	-	-	95	(1,096)	**-**
Reclassification from Investment property	20,204	-	-	-	-	-	**20,204**
Impairment	(608)	-	-	-	-	-	**(608)**
31 December, 2012	**86,056**	**36,316**	**15,570**	**11,466**	**4,962**	**1,081**	**155,451**
Accumulated depreciation							
31 December , 2011	**171**	**9,696**	**7,436**	**3,380**	**382**	**-**	**21,065**
Depreciation charge	1,351	3,470	2,233	1,889	106	-	**9,049**
Write offs	-	(383)	-	(375)	-	-	**(758)**
31 December 2012	**1,522**	**12,783**	**9,669**	**4,894**	**488**	**-**	**29,356**
Net book value:							
31 December 2011	**60,208**	**20,645**	**4,266**	**5,989**	**4,353**	**1,740**	**97,201**
31 December 2012	**84,534**	**23,533**	**5,901**	**6,572**	**4,474**	**1,081**	**126,095**

(Thousands of Georgian Lari)

11. Property and equipment (continued)

	Land and buildings	*Furniture and fixtures*	*Computers and office equipment*	*Motor vehicles*	*Leasehold improvements*	*Assets under construction*	*Total*
Cost or revalued amount							
31 December 2010	**59,269**	**27,077**	**9,623**	**4,897**	**4,855**	**3,284**	**109,005**
Additions	3,900	4,670	2,110	4,557	987	318	**16,542**
Disposals	(677)	(64)	(33)	(33)	-	-	**(807)**
Write offs	(476)	-	(11)	(6)	-	-	**(493)**
Transfers	821	-	-	-	3	(824)	**-**
Reclassifications	2,031	(1,342)	13	(46)	(1,110)	(1,038)	**(1,492)**
Effect of revaluation	(4,489)	-	-	-	-	-	**(4,489)**
31 December, 2011	**60,379**	**30,341**	**11,702**	**9,369**	**4,735**	**1,740**	**118,266**
Accumulated depreciation							
31 December , 2010	**1,799**	**6,513**	**6,134**	**2,024**	**370**	**-**	**16,840**
Depreciation charge	1,181	2,873	1,805	1,360	83	-	**7,302**
Disposals	(68)	(2)	(4)	-	-	-	**(74)**
Write offs	(23)	-	-	(6)	-	-	**(29)**
Reclassifications	314	312	(499)	2	(71)	-	**58**
Effect of revaluation	(3,032)	-	-	-	-	-	**(3,032)**
31 December 2011	**171**	**9,696**	**7,436**	**3,380**	**382**	**-**	**21,065**
Net book value:							
31 December 2010	**57,470**	**20,564**	**3,489**	**2,873**	**4,485**	**3,284**	**92,165**
31 December 2011	**60,208**	**20,645**	**4,266**	**5,989**	**4,353**	**1,740**	**97,201**

Premises of the Group are subject to revaluation on a regular basis. The date of latest revaluation was 31 December 2011. As at 31 December 2012 the Group analysed market prices for its premises and concluded that the market price of the premises were not materially different from their carrying value.

If the buildings were measured using the cost model, the carrying amounts would be as follows:

	2012	*2011*
Cost	41,417	35,942
Accumulated depreciation and impairment	(4,418)	(3,590)
Net carrying amount	**36,997**	**32,352**

(Thousands of Georgian Lari)

12. Intangible assets

The movements in intangible assets, which comprised computer software and licenses, were as follows:

	Computer software and licenses
Cost	
31 December 2011	**8,689**
Additions	4,099
Disposals	(19)
31 December 2012	**12,769**
Accumulated amortisation	
31 December 2011	**2,534**
Amortisation charge	956
Disposals	(1)
31 December 2012	**3,489**
Net book value:	
31 December 2011	**6,155**
31 December 2012	**9,280**

	Computer software and licenses
Cost	
31 December 2010	**9,079**
Additions	1,562
Disposals	(1,952)
31 December 2011	**8,689**
Accumulated amortisation	
31 December 2010	**3,722**
Amortisation charge	762
Disposals	(1,950)
31 December 2011	**2,534**
Net book value:	
31 December 2010	**5,357**
31 December 2011	**6,155**

(Thousands of Georgian Lari)

13. Taxation

The corporate income tax expense comprised:

	2012	*2011*
Deferred tax charge – origination and reversal of temporary differences	4,601	875
Income tax expense	**4,601**	**875**

Georgian legal entities must file individual tax declarations. The tax rate for banks for profits other than on state securities was 15% for 2012 and 2011. The tax rate for interest income on state securities and the NBG deposits is 0%.

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	2012	*2011*
Profit before income tax	**9,785**	**8,513**
Statutory tax rate	15%	15%
Theoretical income tax expense at the statutory rate	**1,468**	**1,277**
Change in unrecognised deferred tax asset	5,072	1,309
Income from state securities at 0%	(2,038)	(1,985)
Non-taxableincome related to sale of subsidiary	-	128
Other	99	146
Income tax expense	**4,601**	**875**

Deferred tax assets and liabilities as of 31 December and their movements for the respective years comprise:

		Origination and reversal of temporary differences			Origination and reversal of temporary differences		
	2010	In the income statement	In other comprehensive income	**2011**	In the income statement	In other comprehensive income	**2012**
Tax effect of deductible temporary differences:							
Property and equipment	269	-	-	**269**	-	-	**269**
Tax loss carried forward	7,645	(507)	-	**7,138**	(1,309)	-	**5,829**
Loans to customers	1,163	123	-	**1,286**	430	-	**1,716**
Equity investments	1,030	(1)	-	**1,029**	44	-	**1,073**
Other assets	258	179	-	**437**	(233)	-	**204**
Other liabilities	(134)	481	-	**347**	64	-	**411**
Gross deferred tax assets	**10,231**	**275**	**-**	**10,506**	**(1,004)**	**-**	**9,502**
Unrecognised deferred tax asset	(269)	(1,309)	-	**(1,578)**	(4,048)	-	**(5,626)**
Deferred tax asset	**9,962**	**(1,034)**	**-**	**8,928**	**(5,052)**	**-**	**3,876**
Tax effect of taxable temporary differences:							
Property and equipment and intangible assets	(8,241)	57	20	**(8,164)**	451	91	**(7,622)**
Investment securities	(109)	102	7	**-**	-	-	**-**
Deferred tax liabilities	**(8,350)**	**159**	**27**	**(8,164)**	**451**	**91**	**(7,622)**
Net deferred tax assets/ (liabilities)	**1,612**	**(875)**	**27**	**764**	**(4,601)**	**91**	**(3,746)**

(Thousands of Georgian Lari)

13. Taxation (continued)

The Group has available GEL 38,858 (2011: GEL 47,582) of tax losses carried forward which begin to expire in 2013, if not utilised. The Group has recognised a tax loss carry forward related net deferred tax asset of GEL 473 (gross GEL 5,829 less allowance of GEL 5,356) and GEL 5,828 (Gross GEL 7,137 less allowance of GEL 1,309) in 2012 and 2011, respectively. During the year Bank utilised tax loss carry forward by GEL 1,892 (2011: GEL 3,380) and wrote off the expired portion of GEL 6,831 (2011: GEL 0), respective tax effect of utilisation amounted to GEL 285 (2011: GEL 507) and tax effect of write off amounted to GEL 1,024 (2011: GEL 0). The schedule of available tax loss carried forward with respective expiration dates is presented below:

Year of expiration	***2012***	***2011***
2012	-	8,724
2013	30,226	30,226
2014	6,310	6,310
2015	2,322	2,322
Tax loss carried forward, gross	38, 858	47,582
Unrecognised tax loss carried forward	(35,708)	(8,724)
Tax loss carried forward, net	**3,150**	**38,858**

14. Other assets, prepayments and other liabilities

Other assets comprise:

	2012	***2011***
Receivables from remittances systems operators	10,149	5,517
Guarantee deposits placed	1,388	1,374
Receivable from guarantees paid	794	801
Repossessed property	712	782
Prepaid taxes other than income tax	577	542
Receivable from documentary operations	231	133
Investment in associate	171	70
Other	2,985	2,316
	17,007	**11,535**
Less – allowance for impairment of other assets	(1,372)	(1,601)
Other assets	**15,635**	**9,934**

Receivables from remittances in the amount of GEL 10,149 (2011: GEL 5,517) represent money transfers made in advance toward the retail clients at the period end that were subsequently settled by the systems operators within several days in accordance with respective service contracts.

Guarantee deposits placed at 31 December 2012 primarily represent pledged funds at VISA Inc. and MasterCard Inc. in the amount of GEL 579 and GEL 757, respectively. (2011: VISA Inc. for GEL 560, MasterCard Inc. for GEL 763).

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Prepayments comprise:

	2012	***2011***
Prepayments for security services	4,401	-
Prepayments for fixed and intangible assets	3,698	5,485
Prepayments for professional services	203	453
Prepayments for office supplies	115	252
Prepaid insurance	107	126
Other	1,062	712
Total Prepayments	**9,586**	**7,028**

(Thousands of Georgian Lari)

14. Other assets, prepayments and other liabilities (continued)

Advances for security service represent a prepayment made to Legal Entity of Public Law (LEPL) Security Police Department (SPD). On 30 May 2012, the Bank signed a five year service agreement with SPD for 63 months until 1 September 2017 in the amount of GEL 5 million. According to the agreement, SPD provides security services at the Bank's head office, branches and other distribution outlets, as well as for vehicles used for cash transportation. In connection with this agreement, the Bank has recognised an expense in the amount of GEL 583 for the year ended 31 December 2012.

Other liabilities comprise:

	2012	*2011*
Funds pending settlements	4,690	7,757
Bonus accrual	1,884	1,785
Payables for intangible assets	1,498	-
Sundry creditors	766	1,316
Operating taxes payable	703	345
Derivative financial liabilities	272	144
Provision on guarantees and commitments	188	99
Share based payment accrual	-	1,437
Other	1,933	1,375
Other liabilities	**11,934**	**14,258**

The movements in other impairment allowances and provisions were as follows:

	Investment securities Available-for-sale	*Other assets*	*Guarantees and commitments*	*Total*
31 December 2011	**-**	**1,601**	**99**	**1,700**
Charge	408	388	89	**885**
Write-offs	-	(617)	-	**(617)**
31 December 2012	**408**	**1,372**	**188**	**1,968**

	Investment securities Available-for-sale	*Other assets*	*Guarantees and commitments*	*Total*
31 December 2010	**-**	**1,514**	**69**	**1,583**
Charge	42	111	30	**183**
Write-offs	(42)	(29)	-	**(71)**
Recoveries	-	5	-	**5**
31 December 2011	**-**	**1,601**	**99**	**1,700**

Provisions for claims, guarantees and commitments are recorded in other liabilities. Impairment of investment securities available-for-sale reduced the carrying value of respective asset.

15. Amounts due to credit institutions

Amounts due to credit institutions comprise:

	2012	*2011*
Current accounts	1,035	843
Time deposits and loans	27,138	20,369
Amounts due to credit institutions	**28,173**	**21,212**

(Thousands of Georgian Lari)

16. Amounts due to customers

The amounts due to customers include the following:

	2012	*2011*
Current accounts	452,766	473,481
Time deposits	243,651	131,495
Amounts due to customers	**696,417**	**604,976**
Held as security against guarantees issued	**3,215**	**1,982**

At 31 December 2012, amounts due to customers of GEL 214,250 (30.8%) were due to the ten largest customers (31 December 2011: GEL 214,870 (35.6%)).

Amounts due to customers include accounts with the following types of customers:

	2012	*2011*
State & public sector	323,963	326,704
Individuals	301,710	198,920
Private enterprises	70,744	79,352
Amounts due to customers	**696,417**	**604,976**

The amounts due customers by economic sector are as follows:

	2012	*2011*
State & public sector	323,963	326,704
Individuals	301,710	198,920
Trade	21,961	12,723
Real estate constructions	4,519	3,927
Transport and communication	4,119	2,902
Energy	3,054	2,115
Agriculture	1,120	11,858
Mining	116	1,304
Other	35,855	44,523
Amounts due to customers	**696,417**	**604,976**

17. Equity

Share capital

As of 31 December 2012, the authorised share capital of the Bank comprised 6,000,000,000 ordinary shares of which 5,918,670,396 were issued and 5,328,424,621 ordinary shares were fully paid (31 December 2011: 4,468,637,039 ordinary shares, of which 4,270,769,313 were issued and fully paid). Each share has nominal value of GEL 0.01.

Ordinary and preferred shares issued and outstanding, net of treasury shares and movements are described below:

	Number of shares		*Nominal amount*		
	Preferred	*Ordinary*	*Preferred*	*Ordinary*	*Total*
31 December 2010	**-**	**2,663,952**	**-**	**26,640**	**26,640**
Increase in share capital	-	1,384,152	-	13,842	**13,842**
Sale of treasury shares	-	221,815	-	2,218	**2,218**
Increase in share capital arising from ESOP	-	850	-	8	**8**
31 December 2011	**-**	**4,270,769**	**-**	**42,708**	**42,708**
Increase in share capital	893	1,057,655	893	10,576	**11,469**
31 December 2012	**893**	**5,328,424**	**893**	**53,284**	**54,177**

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

(Thousands of Georgian Lari)

17. Equity (continued)

For the year ended 31 December 2012, the Bank raised GEL 18,614 through the conversion of the Contingent Capital Participation Notes (The "CCPN") into 1,057,655,308 newly issued ordinary shares at the conversion price of GEL 0.0176 (resulting an increase of the nominal capital by GEL 10,576 and additional paid-in capital by GEL 8,038). Liberty Holdings Georgia LLC and JSC Liberty Capital held 95.7% of the CCPN, with the remainder held by certain minority shareholders.

On 30 December 2011, the Bank raised GEL 17,661 of new equity through the rights issue. Liberty Holdings Georgia LLC purchased 1,007,621,951 ordinary shares resulting in an increase of GEL 16,525 in the Bank's total shareholder's equity (comprising an increase of the nominal capital by GEL 10,076 and additional paid-in capital by GEL 6,449). The minority shareholders purchased 69,278,122 ordinary shares, resulting in an increase of GEL 1,136 in the Bank's shareholders' equity (comprising an increase of the nominal capital by GEL 693 and additional paid-in capital by GEL 443).

In addition to the rights issue, the Bank sold in 2011 529,067,126 ordinary shares to third parties, resulting in an increase of GEL 13,240 in the Bank's total shareholders' equity (comprising an increase of the nominal capital by GEL 5,291 and additional paid-in capital by GEL 7,950).

For the year ended 31 December 2010, the principal contribution to the Bank's shareholders' equity was made by Liberty Holdings Georgia LLC and JSC Liberty Capital. In February 2010, Liberty Holdings Georgia LLC purchased 975,000,000 ordinary shares resulting in an increase of GEL 17,160 in the Bank's shareholders' equity (comprising an increase of the nominal capital by GEL 9,750 and additional paid-in capital by GEL 7,410). Also, the Bank sold in 2010 151,508,589 ordinary shares to third parties, resulting in an increase of GEL 3,537 in the Bank's total shareholders' equity.

On 4 February 2010 and 18 September 2010 the authorised share capital of the Bank was increased by GEL 10,000 and GEL 20,000, respectively, from GEL 30,000 as of 31 December 2009 to GEL 60,000 by September 2010 comprising of 6,000,000,000 ordinary shares. The increase is in anticipation of the future increase in the share capital by way of selling newly issued ordinary shares to investors.

Preferred shares

In August 2012, the Bank issued and made available for sale to the general public in a public offer in Georgia 10,000,000 non-redeemable convertible Preferred Shares, of which 892,553 were outstanding and fully paid-up as of 31 December 2012, and the remainder available for sale through the public offer expiring on 30 June 2013. The Bank's Preferred Shares are not listed.

On 25 October 2012, Liberty Holdings Georgia LLC and JSC Liberty Capital purchased GEL 562 and GEL 68 of the convertible preferred shares issued by the Bank.

The dividend rate on the Preferred Shares is 17% per annum, payable annually, subject to the AGM approval in each given year. Preferred shares are non-cumulative. The conversion option was classified as equity component as of initial recognition date and its fair value comprised zero.

The ability to pay dividends is subject to the Bank's financial condition and results of operations and compliance with the prudential capital adequacy requirements and may be restricted by, among other things, applicable laws and regulations, financing arrangements and other agreements and commitments, and by the NBG.

Basic/diluted income per share

The 2012 net income attributable to ordinary shareholders of the Group comprised GEL 5,184 (2011: GEL 7,638). At 31 December 2012, the weighted average number of ordinary shares outstanding during the year was 4,653,621,404 (2011: 3,220,107,186), resulting in income per share of GEL 0.00111 (full amount) for 2012 (2011: GEL 0.00237). At 31 December 2012 the diluted number of ordinary shares was 4,701,071,753 (31 December 2011: 4,277,762,470), resulting in diluted income per share of GEL 0.00110 (full amount) for 2012 (2011: GEL 0.00234). The dilution includes the potential effect of dilution from the conversion of 892,553 preferred shares into ordinary shares.

ESOP Programme

The Bank has established a share based management compensation package (the "ESOP") entitling the beneficiaries to purchase allocated ordinary shares of the Bank at the nominal value of GEL 0.01 per share subject to vesting conditions. The effective date of the majority such awards is 1 January 2010 with a vesting period of three years, with one third of the respective nominal-cost option allocations vesting on each of 1 January 2011, 2012, 2013 and 2014 subject to the recipient being employed by the Bank on such vesting dates. The ordinary shares designated for the ESOP programme (174,678,856 newly issued ordinary shares) have been sold in 2010, on a deferred payment basis, to Stichting Liberty ESOP, a foundation incorporated under the laws of the Netherlands.

On 1 January 2012, the Bank awarded the nominal-cost option to purchase 18,661,977 ordinary shares to 10 senior employees, with the vesting period of one year. Subsequent to year end on 1 January 2013, the Bank awarded the nominal-cost options to purchase 9,825,243 ordinary shares to four senior employees, with the vesting period of one year.

(Thousands of Georgian Lari)

17. Equity (continued)

As of 31 December 2012 164,853,613 shares were granted to 30 eligible employees (31 December 2011: 168,128,732, to 48 employees) of the Bank. As of 31 December 2012, 3,275,119 (31 December 2011: 8,559,263) ordinary shares have been forfeited. During the year ended 2012, zero number of (2011: 849,357) nominal-cost option have been exercised.

In connection with the ESOP programme, the Bank has recognised an expense in the amount of GEL 275 for the year ended 31 December 2012 (31 December 2011: GEL 516). This expense is based on the weighted average price of GEL 0.0202 per share, determined on the basis of the quoted market prices at the respective actual dates such awards have been granted during the year.

Treasury shares

No treasury ordinary shares remained as of 31 December 2012 (31 December 2011: nil).

Dividends

The Bank has not paid any dividends on its ordinary shares for the years 2012 and 2011

Other reserves

Movements in other reserves were as follows:

	Revaluation reserve for property and equipment	***Unrealised gains/(losses) on investment securities available-for-sale***	***Total***
At 31 December 2010	**22,471**	**231**	**22,702**
Depreciation of revaluation reserve, net of tax	(483)	-	(483)
Reversal of revaluation reserve of sold asset, net of tax	(107)	-	(107)
Net unrealised losses on available-for-sale investments, net of tax	-	(238)	(238)
Revaluation of buildings, net of tax	(138)	-	(138)
Tax effect of property revaluation and securities available-for-sale, net of tax	20	7	27
At 31 December 2011	**21,763**	**-**	**21,763**
Depreciation of revaluation reserve, net of tax	(481)	-	(481)
Impairment loss as a result of fire, net of tax	(517)	-	(517)
At 31 December 2012	**20,765**	**-**	**20,765**

Nature and purpose of other reserves

Revaluation reserve for property and equipment

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

Unrealised gains/(losses) on investment securities available-for-sale

This reserve records fair value changes on available-for-sale investments.

18. Commitments and contingencies

Operating environment

Parliamentary elections of 1 October 2012 and the subsequent transition of power were largely peaceful and thus relieved political uncertainty. The credit rating agencies reconfirmed their ratings for Georgia with stable outlook. Georgia remains under precautionary (non-cash) stand-by arrangement with the IMF which ensures dialogue on all aspects of macro-fiscal and monetary decision-making. All Georgian sovereign and corporate Eurobonds traded on 31 December 2012 above their par value.

In the recent years, Georgia implemented far-reaching structural reforms. Georgia is No.9 in the World Bank Ease of Doing Business global rankings, far ahead of any other country in the broader neighbourhood. Supply-side economic reforms have contributed to the resilience and helped to contain Georgia's exposure to exogenous challenges stemming from the global financial and credit market conditions. After the relatively insignificant dip in 2009, the economy rebounded significantly growing by 6.3% and 7.0% in 2010 and 2011, respectively, with GDP growth projected to exceed 7% in 2012. Baseline 2013 growth forecast by the new government is at 6%.

(Thousands of Georgian Lari)

18. Commitments and contingencies (continued)

Fiscal decision-making has been generally conservative. In 2009-2012, Georgia went through steep fiscal consolidation, with overall budget deficit expected at below 3% of GDP estimated for in 2013. Significant emphasis on infrastructure development measures has allowed to sustain pronounced positive operating budget balances (calculated as revenues minus recurrent expenditure, at approximately 5% of GDP in 2012), with the bulk of the contribution to the overall deficit formation coming from capital expenditures. Proper fiscal-monetary interaction and prudent banking sector supervision allowed to sustain dynamics in the financial sector and to counter exchange rate and credit risks, providing for incremental loan book growth while keeping system-wide NPLs at a low level. The inflation rate has been negative through the most of 2012. Public debt as share of GDP is on the decline. The government and the NBG sustain sufficient liquidity – in the form of the government cash deposit at the NBG and in the form of the NBG's international reserves – to repay the IMF loan coming due in 2013. Non-IMF public debt amortisation profile remains flat and annual repayment instalments amount to insignificant shares of related annual budget revenues.

Georgia remains a small open economy, which is exposed to exogenous trends and pressures. Fiscal and monetary policies implemented in the recent years helped to create certain shield and policy space, although external capital market sentiment and choppiness of global credit conditions – if these transcend certain scale and depth – might trigger pass-through on the in-country consumer, lender and investment confidence. Relatively high unemployment in Georgia, reduced corporate liquidity and profitability, and corporate and personal insolvencies dating back to 2008 - 2009 continue to affect the Group's borrowers' ability to repay the amounts due to the Group. Changes in economic conditions are correlated with the value of collateral held against loans and other obligations. To the extent that information is available, the Group has reflected revised estimates of expected future cash flows in its impairment assessment.

Legal

In the ordinary course of business, the Group is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Group.

The Group's commitments and contingencies comprised the following:

	2012	*2011*
Credit related commitments		
Guarantees	27,318	28,012
Letters of credit	-	1,559
Undrawn loan commitments	23,200	20,999
	50,518	**50,570**
Operating lease commitments		
Not later than 1 year	2,911	2,812
Later than 1 year but not later than 5 years	7,400	6,867
Later than 5 years	4,872	3,999
	15,183	**13,678**
Capital expenditure commitments	455	1,045
Less – provisions (Note 14)	(188)	(99)
Commitments and contingencies (before deducting collateral)	**65,968**	**65,194**
Less – cash held as security against guarantees issued	(3,215)	(1,982)
Commitments and contingencies	**62,753**	**63,212**

As of 31 December 2012 and 31 December 2011, the Bank had Bankers Blanket Bond insurance, Directors and Officers liability insurance, Property and Vehicle insurance coverage.

(Thousands of Georgian Lari)

19. Net fee and commission income

Net fee and commission income comprised:

	2012	*2011*
Fee income received from the Social Service Agency and other State entities	8,738	17,237
Remittances	7,781	7,298
Settlements operations	5,098	5,020
Plastic card operations	4,731	5,980
Cash operations	2,044	1,142
Fee income received from utility payments	1,574	1,279
Guarantees and letters of credit	1,345	614
Other	1,892	376
Fee and commission income	**33,203**	**38,946**
Plastic card operations	(2,058)	(2,786)
Settlements operations	(2,053)	(1,651)
Guarantees and letters of credit	(197)	(176)
Cash operations	(40)	(5)
Fee and commission expense	**(4,348)**	**(4,618)**
Net fee and commission income	**28,855**	**34,328**

On 19 June 2012, the Bank renewed an agreement with the Legal Entity of Public Law (LEPL) Social Service Agency (the "Agency'). The Bank distributes the state pensions, welfare payments, state compensations and other public funds on behalf of the Agency and provides related basic banking services, such as the opening and maintenance of the beneficiary's current account and debit card and withdrawal of the public funds in the Bank's branches and ATMs free of any charge. The agreement expires on 31 December 2014. For the year ended 31 December 2012, fee income received from Agency comprised GEL 8,499 (31 December 2011: GEL 17,199)

20. Other income

	2012	*2011*
Income from penalty on late payments on customer loans & advances	2,634	1,485
Income from rent	737	549
Income from fire loss reimbursement from insurance	595	-
Income from advertising	144	91
Gain from sale of assets	80	43
Income from brokerage operations	-	60
Income from architectural works	-	97
Income from postal and courier services	-	515
Gain from revaluation of investment properties	-	1,258
Other	690	464
Total other income	**4,880**	**4,562**

21. Personnel and general and administrative expenses

Personnel and general and administrative expenses comprise:

	2012	*2011*
Salaries	33,165	27,336
Performance based discretionary bonus pool	2,297	1,785
Variable bonuses	1,868	1,105
Share based payment compensation	275	516
Personnel expenses	**37,605**	**30,742**

(Thousands of Georgian Lari)

21. Personnel and general and administrative expenses (continued)

	2012	2011
Occupancy and rent	3,931	4,010
Marketing and advertising	2,370	2,042
Office supplies	1,729	1,318
Utility expense	1,726	1,535
Operating taxes	1,320	1,367
Legal and other professional services	1,112	1,202
Security	1,111	1,356
Communication	983	918
Corporate hospitality and entertainment	626	682
Travel expenses	549	672
Insurance	425	382
Repair and maintenance	316	189
Personnel training and recruitment	75	100
Other	2,627	1,939
General and administrative expenses	**18,900**	**17,712**

22. Risk management

Introduction

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities. The Group is exposed to credit risk, liquidity risk and market risk. It is also subject to operating risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Group's strategic planning process.

Risk Management Structure

The Supervisory Board is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Management Board

The Management Board has the responsibility to monitor the overall risk process within the Group.

Audit Committee

The Audit Committee has the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits. It is responsible for the fundamental risk issues and manages and monitors relevant risk decisions.

Risk Management

The Risk Management Unit is responsible for implementing and maintaining risk related procedures to ensure an independent control process.

Bank Treasury

Group Treasury is responsible for managing the Group's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Group.

Internal Audit

Risk management processes throughout the Group are audited annually by the internal audit function, which examines both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee.

(Thousands of Georgian Lari)

22. Risk management (continued)

Introduction (continued)

Risk Measurement and Reporting Systems

The Group's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Group also runs worst case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Group. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept, with additional emphasis on selected industries.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Management Board, and the head of each business division. The report includes aggregate credit exposure, hold limit exceptions, liquidity ratios and risk profile changes. Senior management assesses the appropriateness of the allowance for credit losses on a monthly basis.

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

The Group actively uses collateral to reduce its credit risks (see below for more details).

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographical location.

Credit Risk

Credit risk is the risk that the Group will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The Group manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Group has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Actual exposure per borrower against limits is monitored on loans granted. The Credit Committee may initiate a change in the limits. Where appropriate, the Bank obtains collateral and corporate guarantees. The credit risks are monitored on a continuous basis and are subject to annual or more frequent reviews.

Credit-related Commitments Risks

The Group makes available to its customers guarantees which may require that the Group make payments on their behalf. Such payments are collected from customers based on the terms of the letter of credit. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

Credit quality per class of financial assets

The credit quality of financial assets is managed by the Group internal credit policies. The table below shows the credit quality by class of asset for loan-related lines in the statement of financial position, based on the categories specified in the tables.

(Thousands of Georgian Lari)

22. Risk management (continued)

Credit Risk (continued)

As at 31 December 2012	Notes	Neither past due nor impaired 2012	Past due but not impaired 2012	Individually impaired 2012	Total 2012
Amounts due from credit institutions	7	2,673	-	-	**2,673**
Loans to customers:	8				
Loans to retail clients with regular inflows		246,549	5,130	8,359	260,038
Corporate & SME loans		24,349	9,086	5,011	38,446
Consumer loans		31,793	3,062	3,328	38,183
Micro loans		22,382	103	149	22,634
Residential mortgage loans		18,338	804	286	19,428
Gold pawn loans		19,228	987	-	20,215
		362,639	**19,172**	**17,133**	**398,944**
Investment securities	9				
Held-to-maturity		59,159	-	-	**59,159**
		59,159	-	-	**59,159**
Total		**424,471**	**19,172**	**17,133**	**460,776**

As at 31 December 2011	Notes	Neither past due nor impaired 2011	Past due but not impaired 2011	Individually impaired 2011	Total 2011
Amounts due from credit institutions	7	23,463	-	-	**23,463**
Loans to customers:	8				
Loans to retail clients with regular inflows		217,459	3,120	8,184	228,763
Corporate & SME loans		53,159	1,574	23,912	78,645
Consumer loans		17,636	1,711	6,638	25,985
Micro loans		7,171	22	216	7,409
Residential mortgage loans		14,189	123	228	14,540
Gold pawn loans		4,960	74	-	5,034
		314,574	**6,624**	**39,178**	**360,376**
Investment securities	9				
Held-to-maturity		100,805	-	-	**100,805**
		100,805	-	-	**100,805**
Total		**438,842**	**6,624**	**39,178**	**484,644**

An analysis of past due loans, by age, is provided below. The majority of the past due loans are not considered to be impaired.

It is the Group's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of credit exposures across all lines of business, geographic regions and products. The rating system is supported by a variety of financial analytics, combined with processed market information to provide the main inputs for the measurement of counterparty risk. All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy. The attributable risk ratings are assessed and updated regularly.

(Thousands of Georgian Lari)

22. Risk management (continued)

Credit Risk (continued)

Aging analysis of past due but not impaired loans per class of financial assets

As at 31 December 2012	Notes	Less than 30 days 2012	31 to 60 days 2012	61 to 90 days 2012	More than 90 days 2012	Total 2012
Loans to customers:	8					
Loans to retail clients with regular inflows		3,690	1,078	362	-	**5,130**
Corporate & SME loans		2,711	1,094	695	4,586	**9,086**
Consumer loans		1,691	768	603	-	**3,062**
Micro loans		72	21	10	-	**103**
Residential mortgage loans		545	201	58	-	**804**
Gold pawn loans		634	163	68	122	**987**
Total		**9,343**	**3,325**	**1,796**	**4,708**	**19,172**

As at 31 December 2011	Notes	Less than 30 days 2011	31 to 60 days 2011	61 to 90 days 2011	More than 90 days 2011	Total 2011
Loans to customers:	8					
Loans to retail clients with regular inflows		2,280	522	318	-	**3,120**
Corporate & SME		606	274	-	694	**1,574**
Consumer loans		978	413	320	-	**1,711**
Micro loans		17	3	2	-	**22**
Residential mortgage loans		99	24	-	-	**123**
Gold pawn loans		72	1	1	-	**74**
Total		**4,052**	**1,237**	**641**	**694**	**6,624**

See Note 8 for more detailed information with respect to the allowance for impairment of loans to customers.

Carrying amount per class of financial assets whose terms have been renegotiated

The table below shows the carrying amount for renegotiated financial assets, by class.

	2012	2011
Loans to customers:		
Loans to retail clients with regular inflows	101	252
Corporate & SME loans	4,488	23,802
Consumer loans	8,805	4,044
Micro Loans	239	22
Residential Mortgage loans	143	180
Total	**13,776**	**28,300**

(Thousands of Georgian Lari)

22. Risk management (continued)

Credit Risk (continued)

Impairment assessment

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

Individually assessed allowances

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

Collectively assessed allowances

Allowances are assessed collectively for losses on loans to customers that are not individually significant (including credit cards, residential mortgages and unsecured consumer lending, payroll loans, pension advances) and for individually significant loans where there is not yet objective evidence of individual impairment. Allowances are evaluated on each reporting date with each portfolio receiving a separate review.
The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is no yet objective evidence of the impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the appropriate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired. Local management is responsible for deciding the length of this period which can extend for as long as one year. The impairment allowance is then reviewed by credit management to ensure alignment with the Group's overall policy.

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

The geographical concentration of the group's assets and liabilities is put out below:

	2012				*2011*			
	Georgia	*OECD*	*CIS and other foreign countries*	*Total*	*Georgia*	*OECD*	*CIS and other foreign countries*	*Total*
Assets:								
Cash and cash equivalents	215,312	11,527	6,115	**232,954**	116,566	15,705	4,444	**136,715**
Amounts due from credit institutions	80	2,593	-	**2,673**	19,287	4,176	-	**23,463**
Loans to customers	378,118	-	-	**378,118**	324,240	-	-	**324,240**
Investment securities:								
- available-for-sale	2	-	-	**2**	411	-	-	**411**
- held-to-maturity	59,159	-	-	**59,159**	100,805	-	-	**100,805**
All other assets	164,688	1,338		**166,026**	145,414	1,324	-	**146,738**
	817,359	**15,458**	**6,115**	**838,932**	**706,723**	**21,205**	**4,444**	**732,372**
Liabilities:								
Amounts due to credit institutions	28,173	-	-	**28,173**	21,018	194	-	**21,212**
Derivative financial liabilities	232	40	-	**272**	-	144	-	**144**
Amounts due to customers	667,798	7,814	20,805	**696,417**	592,303	3,758	8,915	**604,976**
Contingent capital participation notes	-	-	-	**-**	19,150	-	-	**19,150**
All other liabilities	15,408	-	-	**15,408**	14,114	-	-	**14,114**
	711,611	**7,854**	**20,805**	**740,270**	**646,585**	**4,096**	**8,915**	**659,596**
Net Assets / (Liabilities)	**105,748**	**7,604**	**(14,690)**	**98,662**	**60,138**	**17,109**	**(4,471)**	**72,776**

(Thousands of Georgian Lari)

22. Risk management (continued)

Liquidity risk and funding management

The tables below summarise the maturity profile of the Group's financial liabilities at 31 December 2012, 31 December 2011 based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

Financial liabilities As at 31 December 2012	***Less than 3 months***	***3 to 12 months***	***1 to 5 years***	***Over 5 years***	***Total***
Amounts due to credit institutions	1,411	26,933	-	-	**28,344**
Amounts due to customers	497,470	187,027	31,923	1,423	**717,843**
Other financial liabilities	-	-	-	-	**-**
Total undiscounted financial liabilities	**498,881**	**213,960**	**31,923**	**1,423**	**746,187**

Financial liabilities As at 31 December 2011	***Less than 3 months***	***3 to 12 months***	***1 to 5 years***	***Over 5 years***	***Total***
Amounts due to credit institutions	20,973	100	168	-	**21,241**
Amounts due to customers	503,547	98,760	10,603	645	**613,555**
Other financial liabilities	704	20,718	-	-	**21,422**
Total undiscounted financial liabilities	**525,224**	**119,578**	**10,771**	**645**	**656,218**

The table below shows the contractual expiry by maturity of the Group's financial commitments and contingencies. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

	Less than 3 months	***3 to 12 months***	***1 to 5 years***	***Over 5 years***	***Total***
2012	43,375	6,092	10,938	5,751	**66,156**
2011	37,088	9,963	13,362	4,880	**65,293**

The Group expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

The maturity analysis does not reflect the historical stability of current accounts. Their liquidation has historically taken place over a longer period than indicated in the tables above. These balances are included in amounts due in less than three months in the tables above.

Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchanges, and equity prices. The Bank has no significant concentration of market risk.

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments.

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held at 31 December. Since all the interest bearing assets and liabilities of the Bank are at fixed rates the Bank is not open to interest rate risk fluctuations on the existing interest bearing assets and liabilities.

(Thousands of Georgian Lari)

22. Risk management (continued)

Market Risk (continued)

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Management Board has set limits on positions by currency based on the NBG regulations. Positions are monitored on a daily basis.

The tables below indicate the currencies to which the Group had significant exposure at 31 December on its non-trading monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the currency rate against the GEL, with all other variables held constant on the income statement (due to the fair value of currency sensitive non-trading monetary assets and liabilities). The effect on equity does not differ from the effect on the income statement. A negative amount in the table reflects a potential net reduction in income statement or equity, while a positive amount reflects a net potential increase.

Currency	*Estimated appreciation/(depreciation) of the exchange rate of GEL against the respective currency in % 2012*	*Effect on profit before tax 2012*	*Estimated appreciation/(depreciation) of the exchange rate of GEL against the respective currency in % 2011*	*Effect on profit before tax 2011*
USD	0.81%	30	5.78%	(680)
EUR	-0.98%	(8)	8.03%	17

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 Group cannot expect to eliminate all operational risks, but a control framework and monitoring and responding to potential risks could be effective tools to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

23. Fair values of financial instruments

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

At 31 December 2012	*Level 1*	*Level 2*	*Level 3*	*Total*
Financial assets				
Investment securities – available-for-sale	-	2	-	2
	-	**2**	**-**	**2**
Financial liabilities				
Derivative financial instruments	-	272	-	272
	-	**272**	**-**	**272**

At 31 December 2011	*Level 1*	*Level 2*	*Level 3*	*Total*
Financial assets				
Investment securities – available-for-sale	-	411	-	411
	-	**411**	**-**	**411**
Financial liabilities				
Derivative financial instruments	-	144	-	144
	-	**144**	**-**	**144**

(Thousands of Georgian Lari)

23. Fair values of financial instruments (continued)

Financial instruments recorded at fair value

The following is a description of the determination of fair value for financial instruments which are recorded at fair value using valuation techniques. These incorporate the Group's estimate of assumptions that a market participant would make when valuing the instruments.

Investment securities available-for-sale

Investment securities available-for-sale valued using a valuation technique or pricing models primarily consist of unquoted equity and debt securities. These securities are valued using models which sometimes only incorporate data observable in the market and at other times use both observable and non-observable data. The non-observable inputs to the models include assumptions regarding the future financial performance of the investee, its risk profile, and economic assumptions regarding the industry and geographical jurisdiction in which the investee operates.

Fair value of financial assets and liabilities not carried at fair value

Set out below is a comparison by class of the carrying amounts and fair values of the Group's financial instruments that are not carried at fair value in the consolidated statement of financial position. The table does not include the fair values of non-financial assets and non-financial liabilities.

	Carrying value 2012	***Fair value 2012***	***Unrecognised gain/(loss) 2012***	***Carrying value 2011***	***Fair value 2011***	***Unrecognised gain/(loss) 2011***
Financial assets						
Cash and cash equivalents	232,954	232,954	-	136,715	136,715	-
Amounts due from credit institutions	2,673	2,673	-	23,463	23,463	-
Loans to customers	378,118	378,118	-	324,240	324,240	-
Investment securities:						
- held-to-maturity	59,159	61,130	1,971	100,805	103,946	3,141
Financial liabilities						
Amounts due to credit institutions	28,173	28,173	-	21,212	21,212	-
Amounts due to customers	696,417	696,417	-	604,976	604,976	-
Contingent capital participation notes	-	-	-	19,150	19,150	-
Total unrecognised change in unrealised fair value			**1,971**			**3,141**

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements.

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits and savings accounts without a specific maturity.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates offered for similar financial instruments. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and maturity.

(Thousands of Georgian Lari)

24. Maturity analysis of assets and liabilities

The table below shows an analysis of monetary assets and liabilities according to when they are expected to be recovered or settled.

	2012			*2011*		
	Within one year	***More than one year***	***Total***	***Within one year***	***More than one year***	***Total***
Cash and cash equivalents	232,954	-	232,954	136,715	-	136,715
Amounts due from credit institutions	2,673	-	2,673	23,463	-	23,463
Loans to customers	235,044	143,074	378,118	205,025	119,215	324,240
Investment securities:						
- available-for-sale	-	2	2	-	411	411
- held-to-maturity	18,412	40,747	59,159	81,036	19,769	100,805
Total	**489,083**	**183,823**	**672,906**	**446,239**	**139,395**	**585,634**
Amounts due to credit institutions	28,173	-	28,173	21,045	167	21,212
Amounts due to customers	268,963	427,454	696,417	382,268	222,708	604,976
Contingent capital participation notes	-	-	-	19,150	-	19,150
Other liabilities	274	-	274	164	-	164
Total	**297,410**	**427,454**	**724,864**	**422,627**	**222,875**	**645,502**
Net	**191,673**	**(243,631)**	**(51,958)**	**23,612**	**(83,480)**	**(59,868)**

Customer deposits diversification by number and type of depositors and the past experience of the Group indicate that such accounts and deposits provide a long term and stable source of funding, and as a result they are allocated per expected time of funds outflow in the gap analysis table on the basis of statistical data accumulated by the Group during the previous periods and assumptions regarding the "permanent" part of current account balances.

As of 31 December 2012 total Amounts due to customers amounted to GEL 696,417 (2011: GEL 604,976). The Bank conducts analysis of the stability of the Amounts due to customers for the period of the preceding two years on a monthly basis. These balances have not fallen below GEL 427,454 (2011: GEL 222,708) for the respective periods of the preceding 24 months. As such, it is reasonable to present these funds in Amounts due to customers in more than one year maturity range in the above schedule. If the contractual maturities of Amounts due to customers were considered, the cumulative liquidity gap within one year as of 31 December 2012 would have been negative GEL 208,747 (2011: GEL (189,845)).

The Group has utilized in full a standby facility from the NBG in the amount of GEL 40,000 to be drawn down until 30 November 2012 and maturing in equal monthly installments on 30 April 2013 (the facility has been fully repaid in 2013, for details see Note: 27). On 1 November 2012, Fitch Ratings affirmed the Bank's Long-Term Foreign Currency Issuer Default Rating (IDR) of 'B', Short-term IDR of 'B', Individual Rating of 'D/E', Support Rating of '4' and Support Rating Floor of 'B'. The Outlook for the Long-term IDR is Stable. (In 2010 Fitch Ratings assigned the Bank a Long-Term Foreign Currency Issuer Default Rating (IDR) of 'B', Short-term IDR of 'B', Individual Rating of 'D/E', Support Rating of '4' and Support Rating Floor of 'B'. The Outlook for the Long-term IDR is Stable).

As of 31 December 2012, the Bank had sufficient liquid collateral to additionally draw down GEL 54,622 (2011: GEL 16,169) from the NBG at immediate notice.

25. Related party disclosures

In accordance with IAS 24 "Related Party Disclosures", parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

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

(Thousands of Georgian Lari)

25. Related party disclosures (continued)

	2012				*2011*			
	Parent	***Entities with significant influence over the Group***	***Entities under common control***	***Key management personnel***	***Parent***	***Entities with significant influence over the Group***	***Entities under common control***	***Key management personnel***
Loans outstanding at 1 January, gross	**-**	**-**	**-**	**208**	**-**	**-**	**-**	**307**
Loans issued during the year	-	-	-	50	-	4,116	-	3
Loan repayments during the year	-	-	-	-	-	4,116	-	(102)
Loans outstanding at 31 December, gross	**-**	**-**	**-**	**258**	**-**	**-**	**-**	**208**
Less: allowance for impairment at 31 December	-	-	-	5	-	-	-	5
Loans outstanding at 31 December, net	**-**	**-**	**-**	**253**	**-**	**-**	**-**	**203**
Interest income on loans	-	-	-	29	-	156	-	11
Impairment charge for loans	-	-	-	-	-	-	-	4
Deposits at 1 January	-	-	-	30	-	17,784	-	177
Deposits received during the year	-	-	-	1,905	-	-	-	-
Deposits repaid during the year	-	-	-	217	-	17,784	-	147
Deposits at 31 December	**-**	**-**	**-**	**1,718**	**-**	**-**	**-**	**30**
Contingent capital participation notes at 31 December	-	-	-	-	17,815	-	-	-
Current accounts at 31 December	303	-	574	631	480	1,867	413	3,828
Interest expense on deposits	118	-	-	271	82	1,009	-	43
Interest expense on the CCPN	2,167			-	2,672	-	-	-
Commitments and guarantees issued	-	-	-	-	-	-	-	-
Fee and commission income	-	-	-	2	-	-	-	3
Other operating expenses	-	-	-	335	-	-	-	447

Entities under common control comprises of organizations in which shareholders of the Bank exercise control which represent related parties to the Bank.

The number of key personnel at 31 December 2012 was 12 (2011: 13):

	2012	*2011*
Salaries and other benefits	2,714	2,165
Share based payment compensation	211	323
Total key personnel compensation	**2,925**	**2,487**

(Thousands of Georgian Lari)

26. Capital adequacy

The Bank is regulated by the NBG. As such, the Bank submits to the NBG monthly reports of its financial position and operation (the "Monthly Supervision Report"), which, *inter alia*, contains the Bank's Tier I and Total Capital Adequacy Ratios, calculated in accordance with the methodology required by the NBG. The capital adequacy calculation methodology adopted by the NBG differs in certain material respects from the BIS (Basel I) framework, but has historically been more stringent, due, *inter alia*, to the higher market-risk weighting of the assets.

The Bank maintains an actively managed capital base to cover risks inherent in the business and aims at further enhancing its capital base. The adequacy of the Group's capital is monitored using, among other measures, the ratios established by the NBG and the ratios established by the Basel Capital Accord 1988 in supervising the Group.

The minimum Tier I and the Total Capital Adequacy Ratios required by the NBG are 8% and 12%, respectively, of the risk weighted assets. The Bank's Tier I and Total Capital Adequacy Ratios were above the minimum requirements as of 31 December 2012 and below the minimum requirements as of 31 December 2011. However, at the end of 2011 the Bank operated under the Waiver as explained below.

Prior to 21 September 2009, the Bank had violated established regulatory capital requirements. However, on 17 September 2009, the Bank obtained a written Waiver from the NBG, exempting the Bank from regulatory capital requirements for a three-year period ending 21 September 2012. According to the Waiver letter, the Bank's regulatory capital shall be treated as though it were increased from its current level by GEL 108,000. The amount shall be considered as core capital (Tier 1 capital) and shall be included in the calculation of the prudential ratios, including, without limitation, the capital adequacy ratios.

The Waiver expired on 21 September 2012. In order to enhance the Bank's capital base, Liberty Holdings Georgia LLC, its controlling shareholder, committed at the time of the purchase of a 91.2% equity interest in the Bank, to contribute USD 10 million equivalent in GEL in share capital within six months from the acquisition date. In October 2009, these funds were placed on deposit at the Bank and, in February 2010, were converted into share capital. In 2010 the Bank issued the CCPN in the amount of GEL 18,615 of which 95.7% was purchased by Liberty Holdings Georgia LLC, and the CCPN have been converted in to common equity in October 2012.. On 30 December 2011 Liberty Holdings Georgia LLC invested GEL 16,525 in the Bank's share capital through the rights issue..

NBG capital adequacy ratio

The NBG requires banks to maintain the minimum capital adequacy ratio of 12% of the RWA, as well as the minimum core capital (Tier 1 capital) adequacy ratio of 8% of the RWA, computed based on the Bank's stand-alone financial statements, prepared in accordance with the NBG requirements. As of 31 December 2012 and 31 December 2011, the Bank's capital adequacy ratios were as follows:

	2012	*2011*
Core capital	59,975	42,809
Supplementary capital	17,726	19,405
Less: deductions from capital	(1,458)	(1,458)
Total capital	**76,243**	**60,756**
Risk-weighted assets	**620,796**	**557,987**
Tier I capital adequacy ratio	**9.66%**	**7.67%**
Capital adequacy ratio	**12.28%**	**10.89%**

Capital adequacy ratio under Basel Capital Accord 1988

The Group's capital adequacy ratios, computed in accordance with the Basel Capital Accord 1988, with subsequent amendments including the amendment to incorporate market risks, as of 31 December 2012 and 31 December 2011, were as follows:

	2012	*2011*
Tier 1 capital	77,897	51,008
Tier 2 capital	27,618	27,779
Less: Deductions from capital	-	-
Total capital	**105,515**	**78,787**
Risk-weighted assets	**575,684**	**511,220**
Tier 1 capital adequacy ratio	**13.53%**	**9.98%**
Total capital adequacy ratio	**18.33%**	**15.41%**

(Thousands of Georgian Lari)

27. Events after the reporting period

In January 2013, the Bank early repaid the remaining balance of the NBG facility in the amount of GEL 26,666 that was drawn down in November 2012 and maturing in equal monthly installments on 30 April 2013.

In February 2013, the Bank sold additional preferred shares of GEL 3,300 to third party investors.