

HSBC Bank Armenia CJSC

Annual Report and Accounts 2016

The HSBC Group

HSBC Bank Armenia is a member of HSBC Group, one of the largest banking and financial services organisations in the world.

HSBC Group international network comprises around 4,000 offices over 70 countries and territories.

HSBC Bank Armenia CJSC

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Statement of management's responsibilities

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

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



Paul Edgar
Chief Executive Officer



Աստղիկ Դրամբյան
Chief Financial Officer / Deputy CEO

Statement of compliance

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

The financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2016, and its financial performance and its cash flows for the year then ended.

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

This opinion is prepared based on the results of internal audits and continuing monitoring completed by the Internal Audit function during 2016. It is confirmed that the function had appropriate resources for this activity.

Based on the above, in our opinion, the Bank's activity during 2016 was generally in compliance with legislative and regulatory requirements. Any identified issues with this regard have been escalated to the Board and management through internal audit reports. Appropriate management remediating actions have been agreed and either completed or are in progress.

Internal Audit Department

Business review and financial analysis

HSBC Bank Armenia CJSC (the “Bank”) continues to play its part in the Armenian financial sector, improved its risk management and control framework and continues to reinforce its standards of business conduct. It has also retained its strong capital position and market share in certain areas.

We provide banking and financial services to our customers and continuously strive to enhance the quality of the products we offer in Armenia. Throughout 2016 we continued to serve the needs of our customers through three of HSBC’s global businesses: Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets through our branches/offices and direct channels.

2016 will be remembered for its economic and political events both globally and in Armenia. The continuing macroeconomic crisis, economic downturn in the region, low GDP growth and decrease of foreign investments have deepened financial problems that our corporate clients faced, resulting in credit defaults and a drop in real estate prices.

These uncertainties along with the anticipated capital injections planned by majority of the local banks in order to comply with the new regulatory requirements, influenced investment activity, contributed to changing financial market conditions and tightened competition.

Against this background, the Bank’s performance in 2016 was poor; for the first time in 20 years we closed the year with a loss. This was largely due to higher impairment charges in our wholesale banking credit profiles. Additionally, we have chosen to apply more prudent approach in assessing these impairment charges.

Encouragingly, our retail business continued to be profitable and was stronger than expected, as individual customers responded positively to the marketing campaigns and activities. On the corporate side, we remained focused on internationally minded businesses - helping customers benefit from our network and expertise and connecting customers to opportunities. We remain one of the country’s leading international banks for trade finance and international cash management.

During the year we remained committed to our strategy of supporting foreign investments into Armenia, by referring lending opportunities to HSBC Bank plc, UK for direct lending to Armenian businesses. The loan portfolio of HSBC Bank plc, UK to Armenian businesses grew from USD 153 million as at 31 December 2015 to USD 170 million as at 31 December 2016, or by 11%, generating net interest income of equivalent to USD 6.1 million during 2016. These financial indicators are not part of the financial statements of the Bank, however these present the level of interest and engagement of HSBC Group in Armenia’s economy.

We are continuing to take concerted action to remediate anti-money laundering and sanctions compliance deficiencies and to implement Global Standards. We are safer today and better protected from the threat of financial crime because of the investments we have been making in our Global Standards programme. We remain fully committed to our work in this area in 2017 and beyond to enhance our financial crime risk controls and capabilities, and to meet our external commitments.

We are investing in innovation and technology to serve customers better and enhance security around financial transactions and customer data. Digital channels, including mobile banking, show increasing level of usage, necessary preparation works are completed to introduce contactless cards technology. The latter aims to enhance customer experience, align customer data collection to best international standards, enable us to better protect our customers and effectively meet their evolving needs.

How we do business is as important as what we do. We conduct our business intent on supporting the sustained success of the communities that we work in. In 2016, we contributed AMD 33 million to charitable programmes, and our employees volunteered in community activities during working days. In 2016, HSBC renewed its commitments to its two flagship global education programmes, the HSBC Youth Opportunities Programme and Junior Achievement More than Money, for another three years. These programmes help young people access education and realise their potential, in which we closely cooperate with the local JA office. Education of children at risk remains one of our corporate sustainability focus areas and comprises circa 80% of our total community investment in 2016. We have cooperated with non-profit organisations such as Orran Benevolent NGO, Tumo Centre for Creative Technologies, Junior Achievement of Armenia and Meghvik NGO.

As ever, we owe a huge thanks to our 420 colleagues who have delivered all of these at the same time as working tirelessly to meet the expectations of our 30 thousand customers. On behalf of the Management and Board, we want to thank them all for their dedication and commitment.

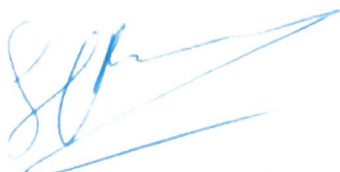
Financial review

The Bank's net loss after tax for the year was AMD 6,667 million compared to AMD 6,416 million profit in prior year. This is explained by higher impairment charges against loan portfolio due to new delinquencies and decline in real estate prices, driven by economic downturn. Another big driver of higher impairment charges is the more prudent approach implemented by the Bank in 2016 in assessing its impairment charges.


Operating income decreased to AMD 16,878 million, a 14% decrease from the previous year. This is mainly driven by reduction of margins due to deterioration of credit quality for corporate portfolio and increase in the number of bankruptcy cases, as well as lower portfolio size.

Impairment charges were AMD 16,887 million versus AMD 3,012 million in 2015. Personnel and other administrative expenses were AMD 8,037 million, a 4% decrease from the previous year.

Total assets as at 31 December 2016 were AMD 215 billion, a 22% decrease over the previous year. Loans to customer portfolio amounted to AMD 120 billion, a 26% decrease over last year. The gross corporate loan portfolio decreased by 23% and amounted to AMD 107 billion. The gross retail loan portfolio demonstrated 10% decrease amounting to AMD 24 billion.



Stephen Banner
Board Member



Ara Alexanian
Board Member



Independent Auditor's Report

To the Board of HSBC Bank Armenia CJSC

Our opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of HSBC Bank Armenia CJSC (the "Bank") as at 31 December 2016, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

What we have audited

The Bank's financial statements comprise:

- the statement of financial position as at 31 December 2016;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

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

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

Independence

We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements of the Auditor's Professional Ethics Code and Auditor's Independence Rules that are relevant to our audit of the financial statements in the Republic of Armenia. We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

Emphasis of Matter

We draw your attention to Note 1 to these financial statements. The operations of the Bank and those of other entities in Armenia have been affected and may continue to be affected in the foreseeable future by the continuing economic difficulties in Armenia. Our opinion is not qualified in respect of this matter.



Independent Auditor's Report (Continued)

Other information

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

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

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

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

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

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

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

Auditor's responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

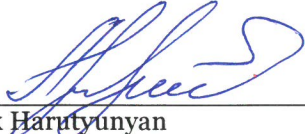


Independent Auditor's Report (Continued)

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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


Altai Tapia
Managing Partner


Hasmik Harutyunyan
Auditor

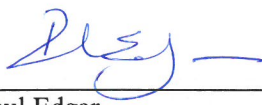
PricewaterhouseCoopers Armenia LLC.

21 April 2017
Yerevan, Republic of Armenia

Statement of Profit or Loss and Other Comprehensive Income for the year ended 31 December 2016

	Notes	2016 AMD'000	2015 AMD'000
Interest income	4	17,649,493	20,413,962
Interest expense	4	(5,304,386)	(6,260,855)
Net interest income		12,345,107	14,153,107
Fee and commission income	5	3,700,449	3,576,656
Fee and commission expense	6	(518,690)	(574,055)
Net fee and commission income		3,181,759	3,002,601
Net (loss)/gain on financial instruments at fair value through profit or loss	7	(3,214)	593,533
Net foreign exchange gain	8	1,617,896	1,715,025
Net gain on available-for-sale financial assets		2,742	42,662
Other operating income		82,262	227,636
Other operating expenses	9	(348,967)	(219,025)
Operating income		16,877,585	19,515,539
Impairment losses	10	(16,886,681)	(3,012,327)
Personnel expenses	11	(3,829,441)	(3,821,264)
Other general administrative expenses	12	(4,207,813)	(4,540,578)
(Loss)/Profit before income tax		(8,046,350)	8,141,370
Income tax credit/(expense)	13	1,379,496	(1,725,307)
(Loss)/Profit for the year		(6,666,854)	6,416,063
Other comprehensive income/(loss), net of income tax			
<i>Items that are or may be reclassified subsequently to profit or loss:</i>			
Revaluation reserve for available-for-sale financial assets:			
- Net change in fair value		634,362	(611,762)
- Net change in fair value transferred to profit or loss		2,194	34,130
<i>Items that will not be reclassified to profit or loss:</i>			
- Revaluation of land and buildings		-	233,772
Other comprehensive income/(loss) for the year, net of income tax		636,556	(343,860)
Total comprehensive (loss)/income for the year		(6,030,298)	6,072,203

The financial statements as set out on pages 12 to 78 were approved by the Board of the Bank. The financial statements were signed by the Management of the Bank on 21 April 2017.


 Paul Edgar
 Chief Executive Officer


 Astghik Drambayan
 Chief Financial Officer/Deputy CEO



The accompanying notes on pages 16 to 78 are an integral part of these financial statements.

Statement of Financial Position as at 31 December 2016

	Notes	2016 AMD'000	2015 AMD'000
ASSETS			
Cash and cash equivalents	14	54,076,716	73,286,515
Financial instruments at fair value through profit or loss			
- Held by the Bank	15	922,745	919,785
Available-for-sale financial assets			
- Held by the Bank	16	24,773,867	13,636,501
Loans and advances to banks	17	6,238,794	8,840,791
Loans to customers	18	119,590,354	161,206,360
Current tax asset		632,010	1,123,661
Property, equipment and intangible assets	19	3,418,325	3,904,258
Other assets	20	5,508,006	12,487,906
Total assets		215,160,817	275,405,777
LIABILITIES			
Deposits and balances from banks	21	11,595,885	45,445,776
Current accounts and deposits from customers	22	149,832,833	160,484,839
Deferred tax liability	13	899,429	2,329,575
Other liabilities	23	5,825,448	14,109,235
Total liabilities		168,153,595	222,369,425
EQUITY			
Share capital	24	18,434,350	18,434,350
Share-based payments reserve		94,788	96,063
Revaluation reserve for available-for-sale financial assets		257,091	(379,465)
Revaluation reserve for land and buildings		233,772	233,772
Retained earnings		27,987,221	34,651,632
Total equity		47,007,222	53,036,352
Total liabilities and equity		215,160,817	275,405,777

The accompanying notes on pages 16 to 78 are an integral part of these financial statements.

Statement of Cash Flows for the year ended 31 December 2016

	Notes	2016 AMD'000	2015 AMD'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Interest receipts		15,957,949	18,542,343
Interest payments		(5,514,233)	(6,710,428)
Fee and commission receipts		3,375,491	3,444,895
Fee and commission payments		(744,623)	(481,158)
Net (payments)/receipts from financial instruments at fair value through profit or loss		(118,436)	1,346,826
Net receipts from foreign exchange		1,429,979	2,072,392
Net other expense payments		(132,043)	(123,356)
Staff costs paid		(3,850,785)	(3,599,143)
Other general administrative expenses paid		(2,349,273)	(3,610,207)
(Increase)/decrease in operating assets			
Financial instruments at fair value through profit or loss		85,447	(216,232)
Available-for-sale financial assets		(9,818,910)	18,435,133
Loans and advances to banks		4,826,140	(3,260,490)
Loans to customers		22,733,540	14,977,665
Other assets		137,853	(112,981)
Increase/(decrease) in operating liabilities			
Deposits and balances from banks		(33,437,326)	(7,284,784)
Amounts payable under repurchase agreements		-	(11,999,961)
Current accounts and deposits from customers		(10,059,619)	(15,209,907)
Other liabilities		2,268	35,500
Net cash (used in)/from operating activities before income tax paid		(17,476,581)	6,246,107
Income tax paid		(851,915)	(1,738,468)
Cash flows (used in)/from operating activities		(18,328,496)	4,507,639
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchases of property, equipment and intangible assets		(527,831)	(663,697)
Sales of property, equipment and intangible assets		10,328	10,226
Cash flows used in investing activities		(517,503)	(653,471)
CASH FLOWS FROM FINANCING ACTIVITIES			
Repayments of subordinated debt		-	(2,882,000)
Cash flows used in financing activities		-	(2,882,000)
Net (decrease)/increase in cash and cash equivalents		(18,845,999)	972,168
Effect of changes in exchange rates on cash and cash equivalents		36,200	(542,368)
Cash and cash equivalents as at the beginning of the year		72,356,515	71,926,715
Cash and cash equivalents as at the end of the year	14	53,546,716	72,356,515

The accompanying notes on pages 16 to 78 are an integral part of these financial statements.

Statement of Changes in Equity for the year ended 31 December 2016

	Share capital	Share-based payments reserve	Revaluation reserve for available-for-sale financial assets	Revaluation reserve for land and buildings	Retained earnings	Total
AMD'000						
Balance as at 1 January 2015	18,434,350	92,466	198,167	-	28,235,419	46,960,402
Profit for the year	-	-	-	-	6,416,063	6,416,063
Other comprehensive loss						
Items that are or may be reclassified subsequently to profit or loss:						
Net change in fair value of available-for-sale financial assets, net of income tax	-	-	(611,762)	-	-	(611,762)
Net change in fair value of available-for-sale financial assets transferred to profit or loss, net of income tax	-	-	34,130	-	-	34,130
Items that will not be reclassified to profit or loss:						
Revaluation of land and buildings, net of income tax	-	-	-	233,772	-	233,772
Total other comprehensive loss	-	-	(577,632)	233,772	-	(343,860)
Total comprehensive income for the year	-	-	(577,632)	233,772	6,416,063	6,072,203
Transactions with owners, recorded directly in equity						
Share-based payments	-	3,597	-	-	150	3,747
Total transactions with owners	-	3,597	-	-	150	3,747
Balance as at 31 December 2015	18,434,350	96,063	(379,465)	233,772	34,651,632	53,036,352
Balance as at 1 January 2016	18,434,350	96,063	(379,465)	233,772	34,651,632	53,036,352
Loss for the year	-	-	-	-	(6,666,854)	(6,666,854)
Other comprehensive income						
Items that are or may be reclassified subsequently to profit or loss:						
Net change in fair value of available-for-sale financial assets, net of income tax	-	-	634,362	-	-	634,362
Net change in fair value of available-for-sale financial assets transferred to profit or loss, net of income tax	-	-	2,194	-	-	2,194
Total other comprehensive income	-	-	636,556	-	-	636,556
Total comprehensive income/(loss) for the year	-	-	636,556	-	(6,666,854)	(6,030,298)
Transactions with owners, recorded directly in equity						
Share-based payments	-	(1,275)	-	-	2,443	1,168
Total transactions with owners	-	(1,275)	-	-	2,443	1,168
Balance as at 31 December 2016	18,434,350	94,788	257,091	233,772	27,987,221	47,007,222

The accompanying notes on pages 16 to 78 are an integral part of these financial statements.

Notes to the Financial Statements

1 Background

(a) Organisation and operations

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

As at 31 December 2016 the Bank had 10 offices and branches. The average number of persons employed by the Bank during the year was 415 (2015: 388).

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

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

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

Related party transactions are detailed in Note 31.

(b) Operating environment of the Bank

The Bank’s operations are primarily located in Armenia. Consequently, the Bank is exposed to the economic and financial markets of Armenia which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue to develop and are subject to frequent changes and varying interpretations, refer to Note 29.

The economic environment of the Republic of Armenia is significantly influenced by the level of business activity in the Russian Federation and significant cash movements flow from the Russian Federation to the Republic of Armenia. Therefore, a decline in business activity, stock market volatility and other risks experienced in the Russian Federation could have a flow-on negative effect on the financial and corporate sectors of the Republic of Armenia. During 2016, the Russian economy was negatively impacted by low oil prices and on-going political tension in the region and international sanctions against certain Russian companies and individuals.

Borrowers of the Bank were adversely affected by the financial and economic environment in Armenia and in the Region, which in turn impacted their ability to repay the amounts owed. Deteriorating economic conditions for borrowers were reflected in revised estimates of expected future cash flows in impairment assessments.

The amount of provision for impaired loans is based on management's appraisals of these assets at the end of the reporting period after taking into consideration the cash flows that may result from foreclosure less costs for obtaining and selling the collateral.

The market in the Republic of Armenia for many types of collateral, especially real estate, has been affected by the economic downturn, resulting in a low level of liquidity for certain types of assets. As a result, the actual realisable value on future foreclosure may differ from the value ascribed in estimating allowances for impairment at the end of the reporting period. Under IFRS, impairment losses on financial assets expected as a result of future events, no matter how likely, cannot be recognised until such events arise.

2 Basis of preparation

(a) Statement of compliance

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

(b) Basis of measurement

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

(c) Functional and presentation currency

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

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

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

(d) Use of estimates and judgments

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

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

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

- Loan impairment estimates – Note 18;
- Revaluation of land and buildings – Note 19;
- Fair value of financial instruments – Note 32.

(e) Changes in presentation

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

3 Significant accounting policies

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

(a) Foreign currency translation and presentation of foreign currency items

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

At 31 December 2016, the principal rate of exchange used for translating foreign currency balances was USD 1 = AMD 483.94 (2015: USD 1 = AMD 483.75), EUR 1 = AMD 512.20 (2015: EUR1=AMD 528.69), GBP 1 = 595.54 (2015: GBP 1 = AMD 717.69).

(b) Cash and cash equivalents

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

3 Significant accounting policies (continued)

(c) Financial instruments

(i) Classification

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

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

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

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

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

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

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

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

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

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

3 Significant accounting policies (continued)

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

(ii) *Recognition*

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

(iii) *Measurement*

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

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

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

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

Cost is the amount of cash or cash equivalents paid or the fair value of the other consideration given to acquire an asset at the time of its acquisition and includes transaction costs. Measurement at cost is only applicable to investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured and derivatives that are linked to, and must be settled by, delivery of such unquoted equity instruments. Refer to Note 15.

(iv) *Amortised cost*

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

3 Significant accounting policies (continued)

(v) *Fair value measurement principles*

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

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

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

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

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

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

(vi) *Gains and losses on subsequent measurement*

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

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

3 Significant accounting policies (continued)

For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in profit or loss when the financial asset or liability is derecognised or impaired, and through the amortisation process.

(vii) Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability in the statement of financial position. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

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

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

In transfers where control over the asset is retained, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred assets.

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

The Bank writes off assets deemed to be uncollectible.

(viii) Repurchase and reverse repurchase agreements

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

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

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

3 Significant accounting policies (continued)

(ix) Derivative financial instruments

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

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

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

(x) Offsetting

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

(d) Property and equipment

(i) Owned assets

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

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

(ii) Revaluation

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

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

3 Significant accounting policies (continued)

(iii) Depreciation

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

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

(e) Intangible assets

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

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

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

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

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

- computer software	3 to 5 years
- other	10 years

(f) Repossessed collateral

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

(g) Impairment

(i) Financial assets carried at amortised cost

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

3 Significant accounting policies (continued)

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

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

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

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

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

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

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

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

3 Significant accounting policies (continued)

(ii) *Financial assets carried at cost*

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

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

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

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

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

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

(iv) *Non-financial assets*

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

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

3 Significant accounting policies (continued)

(h) Provisions

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

(i) Credit related commitments

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

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

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

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

Loan commitments are not recognised, except for the following:

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

(j) Share capital

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

(i) Dividends

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

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

(ii) General reserve

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

3 Significant accounting policies (continued)

(k) Taxation

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

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

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

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

(l) Income and expense recognition

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

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

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

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

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

(m) Employee benefits

Share-based payment transactions

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

3 Significant accounting policies (continued)

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

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

(n) Adoption of new or revised standards and interpretations

The following new standards and interpretations became effective for the Bank from 1 January 2016:

IFRS 14, Regulatory Deferral Accounts (issued in January 2014 and effective for annual periods beginning on or after 1 January 2016). IFRS 14 permits first-time adopters to continue to recognise amounts related to rate regulation in accordance with their previous GAAP requirements when they adopt IFRS. However, to enhance comparability with entities that already apply IFRS and do not recognise such amounts, the standard requires that the effect of rate regulation must be presented separately from other items. An entity that already presents IFRS financial statements is not eligible to apply the standard. The amendment had no material impact on the Bank's financial statements.

Accounting for Acquisitions of Interests in Joint Operations – Amendments to IFRS 11 (issued on 6 May 2014 and effective for the periods beginning on or after 1 January 2016). This amendment adds new guidance on how to account for the acquisition of an interest in a joint operation that constitutes a business. The amendment had no material impact on the Bank's financial statements.

Clarification of Acceptable Methods of Depreciation and Amortisation – Amendments to IAS 16 and IAS 38 (issued on 12 May 2014 and effective for the periods beginning on or after 1 January 2016). In this amendment, the IASB has clarified that the use of revenue-based methods to calculate the depreciation of an asset is not appropriate because revenue generated by an activity that includes the use of an asset generally reflects factors other than the consumption of the economic benefits embodied in the asset. The amendment had no material impact on the Bank's financial statements.

Agriculture: Bearer plants – Amendments to IAS 16 and IAS 41 (issued on 30 June 2014 and effective for annual periods beginning 1 January 2016). The amendments change the financial reporting for bearer plants, such as grape vines, rubber trees and oil palms, which now should be accounted for in the same way as property, plant and equipment because their operation is similar to that of manufacturing. Consequently, the amendments include them within the scope of IAS 16, instead of IAS 41. The produce growing on bearer plants will remain within the scope of IAS 41. The amendment had no material impact on the Bank's financial statements.

3 Significant accounting policies (continued)

Equity Method in Separate Financial Statements – Amendments to IAS 27 (issued on 12 August 2014 and effective for annual periods beginning 1 January 2016). The amendments will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. The amendment had no material impact on the Bank's financial statements.

Annual Improvements to IFRSs 2014 (issued on 25 September 2014 and effective for annual periods beginning on or after 1 January 2016). The amendments impact 4 standards. IFRS 5 was amended to clarify that change in the manner of disposal (reclassification from "held for sale" to "held for distribution" or vice versa) does not constitute a change to a plan of sale or distribution, and does not have to be accounted for as such. The amendment to IFRS 7 adds guidance to help management determine whether the terms of an arrangement to service a financial asset which has been transferred constitute continuing involvement, for the purposes of disclosures required by IFRS 7. The amendment also clarifies that the offsetting disclosures of IFRS 7 are not specifically required for all interim periods, unless required by IAS 34. The amendment to IAS 19 clarifies that for post-employment benefit obligations, the decisions regarding discount rate, existence of deep market in high-quality corporate bonds, or which government bonds to use as a basis, should be based on the currency that the liabilities are denominated in, and not the country where they arise. IAS 34 will require a cross reference from the interim financial statements to the location of "information disclosed elsewhere in the interim financial report". The amendment had no material impact on the Bank's financial statements.

Disclosure Initiative Amendments to IAS 1 (issued in December 2014 and effective for annual periods on or after 1 January 2016). The Standard was amended to clarify the concept of materiality and explains that an entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material, even if the IFRS contains a list of specific requirements or describes them as minimum requirements. The Standard also provides new guidance on subtotals in financial statements, in particular, such subtotals (a) should be comprised of line items made up of amounts recognised and measured in accordance with IFRS; (b) be presented and labelled in a manner that makes the line items that constitute the subtotal clear and understandable; (c) be consistent from period to period; and (d) not be displayed with more prominence than the subtotals and totals required by IFRS standards. The amendment had no material impact on the Bank's financial statements.

Investment Entities: Applying the Consolidation Exception Amendment to IFRS 10, IFRS 12 and IAS 28 (issued in December 2014 and effective for annual periods on or after 1 January 2016). The Standard was amended to clarify that an investment entity should measure at fair value through profit or loss all of its subsidiaries that are themselves investment entities. In addition, the exemption from preparing consolidated financial statements if the entity's ultimate or any intermediate parent produces consolidated financial statements available for public use was amended to clarify that the exemption applies regardless whether the subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with IFRS 10 in such ultimate or any intermediate parent's financial statements. The amendment had no material impact on the Bank's financial statements.

3 Significant accounting policies (continued)

(o) New accounting pronouncements

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2017 or later, and which the Bank has not early adopted.

IFRS 9 “Financial Instruments: Classification and Measurement” (amended in July 2014 and effective for annual periods beginning on or after 1 January 2018). Key features of the new standard are:

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
- Classification for debt instruments is driven by the entity’s business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets’ cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.
- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.
- IFRS 9 introduces a new model for the recognition of impairment losses – the expected credit losses (ECL) model. There is a ‘three stage’ approach which is based on the change in credit quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.
- Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

The standard is expected to have a significant impact on the Bank’s loan impairment provisions. The Bank is currently assessing the impact of the new standard on its financial statements.

3 Significant accounting policies (continued)

IFRS 16 "Leases" (issued in January 2016 and effective for annual periods beginning on or after 1 January 2019). The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Bank is currently assessing the impact of the new standard on its financial statements.

IFRS 15, Revenue from Contracts with Customers (issued on 28 May 2014 and effective for the periods beginning on or after 1 January 2018). The new standard introduces the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed. The Bank is currently assessing the impact of the new standard on its financial statements.

Disclosure Initiative - Amendments to IAS 7 (issued in 29 January 2016 and effective for annual periods beginning on or after 1 January 2017). The amended IAS 7 will require disclosure of a reconciliation of movements in liabilities arising from financing activities. The Bank will present this disclosure in its 2017 financial statements.

- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture - Amendments to IFRS 10 and IAS 28 (issued on 11 September 2014 and effective for annual periods beginning on or after a date to be determined by the IASB).
- Recognition of Deferred Tax Assets for Unrealised Losses - Amendments to IAS 12 (issued on 19 January 2016 and effective for annual periods beginning on or after 1 January 2017).
- Amendments to IFRS 15, Revenue from Contracts with Customers (issued on 12 April 2016 and effective for annual periods beginning on or after 1 January 2018).
- Amendments to IFRS 2, Share-based Payment (issued on 20 June 2016 and effective for annual periods beginning on or after 1 January 2018).
- Amendments to IFRS 4, Insurance Contracts (issued on 12 September 2016 and effective for annual periods beginning on or after 1 January 2018).

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

4 Net interest income

	2016 AMD'000	2015 AMD'000
Interest income		
Loans to customers	14,776,873	17,354,471
Available-for-sale financial assets	2,020,121	2,511,980
Loans and advances to banks	631,713	450,903
Cash and cash equivalents	148,710	41,565
Financial instruments at fair value through profit or loss	72,076	55,043
Total interest income	17,649,493	20,413,962
Interest expense		
Current accounts and deposits from customers	4,101,878	4,000,260
Deposits and balances from banks and other financial institutions	1,202,508	1,292,350
Amounts payable under repurchase agreements	-	968,245
Total interest expense	5,304,386	6,260,855

Included within loans to customers line under interest income for the year ended 31 December 2016 is a total of AMD 1,734,965 thousand (2015: AMD 528,546 thousand) accrued on impaired financial assets.

5 Fee and commission income

	2016 AMD'000	2015 AMD'000
Credit facilities	2,231,472	1,689,970
Letters of credits and guarantees	476,697	625,206
Remittances	381,849	502,035
Credit cards	345,200	382,510
Account services	156,257	219,728
ATM services	29,264	37,938
Insurance agency	17,965	18,486
Other	61,745	100,783
Total fee and commission income	3,700,449	3,576,656

The Credit facilities mainly represent the amounts of commission income received from loans provided to Armenian businesses by the HSBC Bank plc.

The Credit cards mainly represent the amounts of commission income received from fees charged for credit cards issuance and credit cards service.

6 Fee and commission expense

	2016 AMD'000	2015 AMD'000
Card transactions fees	320,404	307,291
Loans and borrowings	106,873	156,637
Settlement transactions	69,347	88,915
Other	22,066	21,212
Total fee and commission expense	518,690	574,055

7 Net (loss)/gain on financial instruments at fair value through profit or loss

	2016 AMD'000	2015 AMD'000
Debt financial instruments	99,987	(2,993)
Foreign currency contracts	(103,201)	596,526
Total net (loss)/gain on financial instruments at fair value through profit or loss	(3,214)	593,533

8 Net foreign exchange gain

	2016 AMD'000	2015 AMD'000
Gain on foreign exchange transactions	1,429,979	2,072,392
Net gain/(loss) from revaluation of financial assets and liabilities	187,917	(357,367)
Total net foreign exchange gain	1,617,896	1,715,025

9 Other operating expenses

	2016 AMD'000	2015 AMD'000
Payments to Deposit Guarantee Fund	209,300	219,025
Fines and penalties	139,667	-
Total other operating expenses	348,967	219,025

10 Impairment losses

	2016 AMD'000	2015 AMD'000
Loans to customers (Note 18)	16,629,881	3,012,327
Other assets (Note 20)	256,800	-
Total impairment losses	16,886,681	3,012,327

The 2016 results are driven largely by the Bank's more prudent approach in assessing its impairment charges considering the current economic downturn in the region, decrease of foreign investments and asset prices in the country (refer to Note 18).

11 Personnel expenses

	2016 AMD'000	2015 AMD'000
Employee compensation	3,829,441	3,821,264
Total personnel expenses	3,829,441	3,821,264

12 Other general administrative expenses

	2016 AMD'000	2015 AMD'000
HSBC Group IT support costs and other charges	1,552,976	1,955,860
Depreciation and amortisation (Note 19)	1,011,547	984,251
Rent of property	555,922	555,043
Communication and information services	114,631	108,345
Insurance	101,135	106,882
Advertising and marketing	89,409	87,365
Security	87,078	79,856
Repair and maintenance	77,073	70,977
IT related costs	76,551	80,654
Utilities	74,704	77,153
Professional services	73,941	68,051
Travel and entertainment expenses	52,694	50,829
Charity and sponsorship	32,581	45,002
Office supplies	29,475	34,252
Currency shipment charges	25,404	29,040
Other	252,692	207,018
Total other general administrative expenses	4,207,813	4,540,578

13 Income tax (credit)/expense

	2016 AMD'000	2015 AMD'000
Current tax expense		
Current year tax expense	-	300,000
Current tax expense under/(over) provided in prior years	209,789	(167,785)
Origination and reversal of temporary differences	(1,589,285)	1,593,092
Total income tax (credit)/expense	(1,379,496)	1,725,307

In 2016 the applicable tax rate for current and deferred tax is 20% (2015: 20%).

Reconciliation of effective tax rate:

	2016 AMD'000	%	2015 AMD'000	%
(Loss)/Profit before income tax	(8,046,350)		8,141,370	
Income tax (credit)/expense at the applicable tax rate	(1,609,270)	20.0	1,628,274	20.0
Non-deductible costs	19,985	(0.2)	264,818	3.3
Under/(Over) provided in prior years	209,789	(2.6)	(167,785)	(2.1)
Total income tax (credit)/expense	(1,379,496)	17.1	1,725,307	21.2

13 Income tax (credit)/expense (continued)

(a) Deferred tax asset and liability

Temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax liabilities as of 31 December 2016 and 2015.

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

Movements in temporary differences during the years ended 31 December 2016 and 2015 are presented as follows:

	Balance 1 January 2016	Recognised in profit or loss	Recognised in other comprehensive income	Balance 31 December 2016
AMD'000				
Cash and cash equivalents	39,473	(12,997)	-	26,476
Financial instruments at fair value through profit or loss	41,048	23,038	-	64,086
Available-for-sale financial assets	(94,866)	-	159,139	64,273
Loans and advances to banks	17,682	(14,850)	-	2,832
Loans to customers	2,698,653	(271,439)	-	2,427,214
Property and equipment	(51,433)	(22,430)	-	(73,863)
Other assets	14,469	40,907	-	55,376
Other liabilities	(335,451)	70,486	-	(264,965)
Tax loss carry forwards	-	(1,402,000)	-	(1,402,000)
Total movement	2,329,575	(1,589,285)	159,139	899,429

	Balance 1 January 2015	Recognised in profit or loss	Recognised in other comprehensive income	Balance 31 December 2015
AMD'000				
Cash and cash equivalents	55,035	(15,562)	-	39,473
Financial instruments at fair value through profit or loss	189,343	(148,295)	-	41,048
Available-for-sale financial assets	49,542	-	(144,408)	(94,866)
Loans and advances to banks	9,495	8,187	-	17,682
Loans to customers	1,037,614	1,661,039	-	2,698,653
Property and equipment	(148,530)	38,654	58,443	(51,433)
Other assets	27,254	(12,785)	-	14,469
Other liabilities	(397,305)	61,854	-	(335,451)
Total movement	822,448	1,593,092	(85,965)	2,329,575

13 Income tax (credit)/expense (continued)

(b) Income tax recognised in other comprehensive income

The tax effects relating to components of other comprehensive income for the years ended 31 December 2016 and 2015 comprise the following:

	2016			2015		
	Amount before tax	Tax expense	Amount net-of-tax	Amount before tax	Tax (expense)/ benefit	Amount net-of-tax
AMD'000						
Revaluation of land and buildings	-	-	-	292,215	(58,443)	233,772
Net change in fair value of available-for-sale financial assets	792,953	(158,591)	634,362	(764,702)	152,940	(611,762)
Net change in fair value of available-for-sale financial assets transferred to profit or loss	2,742	(548)	2,194	42,662	(8,532)	34,130
Other comprehensive income	795,695	(159,139)	636,556	(429,825)	85,965	(343,860)

14 Cash and cash equivalents

	31 December 2016 AMD'000	31 December 2015 AMD'000
Cash on hand	5,345,244	5,297,837
Nostro accounts with the CBA (net of credit card settlement deposit)	31,547,130	47,322,497
Deposit with the CBA	3,000,780	-
Nostro accounts with other banks		
- rated AA-	13,361,741	18,283,925
- rated from A- to A+	149,917	128,536
- rated BB-	-	2,245
Total nostro accounts with other banks	13,511,658	18,414,706
Cash equivalents		
Money market overnight placements		
- rated AA-	141,904	1,321,475
Total cash equivalents	141,904	1,321,475
Cash and cash equivalents in the statement of cash flows	53,546,716	72,356,515
Credit card settlement deposit with the CBA	530,000	930,000
Cash and cash equivalents in the statement of financial position	54,076,716	73,286,515

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

14 Cash and cash equivalents (continued)

The nostro accounts include mandatory minimum reserve deposits calculated in accordance with regulations promulgated by the CBA at 2% to 18% (31 December 2015: 2% to 20%) from the attracted funds depending on currency. Withdrawal of such reserves is not restricted; however, the Bank is subject to penalties if the required minimum average balance is not periodically maintained.

As at 31 December 2016, in addition to balances with the CBA, the Bank had one HSBC Group member bank (31 December 2015: one HSBC Group member bank) whose balance exceeded 10% of equity. The gross value of these balances as at 31 December 2016 is AMD 10,769,804 thousand (31 December 2015: AMD 16,374,837 thousand).

15 Financial instruments at fair value through profit or loss

	31 December 2016 AMD'000	31 December 2015 AMD'000
Held by the Bank		
ASSETS		
Debt and other fixed-income instruments		
Armenian Government treasury bills		
- rated B+	636,930	671,693
Derivative financial instruments		
Foreign currency contracts		
- rated AA-	285,815	248,092
Total financial instruments at fair value through profit or loss	922,745	919,785

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

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

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

Foreign currency contracts

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

15 Financial instruments at fair value through profit or loss (continued)

	Notional amount		Weighted average contractual exchange rates	
	31 December 2016 AMD'000	31 December 2015 AMD'000	31 December 2016 AMD'000	31 December 2015 AMD'000
Buy USD sell AMD				
Less than 3 months	3,212,739	1,852,372	476.0	480.0
Between 3 and 12 months	3,847,691	3,728,243	465.5	474.0
Buy USD sell EUR				
Less than 3 months	-	8,609,383	-	1.1
Buy USD sell AUD				
Less than 3 months	57,317	31,389	1.4	1.4
Buy USD sell RUB				
Less than 3 months	26,888	-	65.1	-
Buy USD sell CAD				
Less than 3 months	80,003	-	1.3	-
Buy RUB sell USD				
Less than 3 months	28,502	-	65.5	-
Buy AMD sell USD				
Less than 3 months	1,394,002	1,100,000	484.8	484.3

16 Available-for-sale financial assets

	31 December 2016 AMD'000	31 December 2015 AMD'000
Held by the Bank		
Debt and other fixed-income instruments		
Armenian Government treasury bills		
- rated B+	24,028,968	12,567,002
Corporate bonds		
International financial institutions		
- rated AAA	-	366,341
Other corporate bonds		
- Unrated	712,867	671,102
Total debt and other fixed-income instruments	24,741,835	13,604,445
Equity instruments – Unquoted		
ACRA credit reporting	19,140	19,140
Armenian Card	12,143	12,143
SWIFT	749	773
Total equity instruments – Unquoted	32,032	32,056
Total available-for-sale financial assets held by the Bank	24,773,867	13,636,501

16 Available-for-sale financial assets (continued)

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

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

As at 31 December 2016 and 31 December 2015 unrated corporate bonds are represented by the corporate bonds issued by local financial institution.

Investments without a determinable fair value

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

17 Loans and advances to banks

	31 December 2016 AMD'000	31 December 2015 AMD'000
Local banks	6,223,504	8,808,806
Rated AA-	15,290	31,985
Total loans and advances to banks	6,238,794	8,840,791

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

As at 31 December 2016 the Bank had one bank (2015: no banks) whose balances exceeded 10% of equity. These balances as at 31 December 2016 were AMD 4,823,076 thousand (2015: nil).

The loans and advances to local banks as at 31 December 2016 have been repaid by 31 January 2017 and 31 December 2015 were repaid by 31 January 2016.

The loans and advances to local banks in AMD 4,823,076 thousand are secured by Armenian government treasury bonds as at 31 December 2016. The amount excludes overcollateralization.

18 Loans to customers

	31 December 2016 AMD'000	31 December 2015 AMD'000
Loans to corporate customers		
Loans to large corporates	64,737,839	62,607,834
Loans to small and medium size companies	42,620,766	77,410,084
Total loans to corporate customers	107,358,605	140,017,918
Loans to retail customers		
Mortgage loans	15,034,500	16,811,261
Credit cards	2,503,302	2,601,981
Construction loans	484,722	641,714
Auto loans	328,228	586,045
Consumer loans	3,699,810	2,999,824
Other loans to retail customers	1,671,496	2,846,392
Total loans to retail customers	23,722,058	26,487,217
Gross loans to customers	131,080,663	166,505,135
Impairment allowance	(11,490,309)	(5,298,775)
Net loans to customers	119,590,354	161,206,360

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2016 are as follows:

	Loans to corporate customers AMD'000	Loans to retail customers AMD'000	Total AMD'000
Balance at the beginning of the year	5,221,615	77,160	5,298,775
Net charge	16,516,260	113,621	16,629,881
Net write-offs	(8,640,963)	(1,541)	(8,642,504)
Unwinding of discount on impairment allowance	(1,734,966)	-	(1,734,966)
Effect of foreign currency translation	(61,323)	446	(60,877)
Balance at the end of the year	11,300,623	189,686	11,490,309

During the year ended 31 December 2016 the Bank has written off the excess of loan amount outstanding over expected recoverable amount.

Movements in the loan impairment allowance by classes of loans to customers for the year ended 31 December 2015 are as follows:

	Loans to corporate customers AMD'000	Loans to retail customers AMD'000	Total AMD'000
Balance at the beginning of the year	3,125,760	72,277	3,198,037
Net charge	2,921,953	90,374	3,012,327
Net write-offs	(174,843)	(85,378)	(260,221)
Unwinding of discount on impairment allowance	(703,880)	-	(703,880)
Effect of foreign currency translation	52,625	(113)	52,512
Balance at the end of the year	5,221,615	77,160	5,298,775

18 Loans to customers (continued)

(a) Credit quality of loans to customers

The following table provides information on the credit quality of loans to customers as at 31 December 2016:

	Gross loans AMD'000	Impairment allowance AMD'000	Net loans AMD'000	Impairment allowance to gross loans %
Loans to corporate customers				
Loans to large corporates				
Loans without individual signs of impairment				
- not overdue	40,408,506	(1,732,278)	38,676,228	4.3
Overdue but not impaired loans				
- overdue less than 30 days	220,429	(35,539)	184,890	16.1
- overdue 30-89 days	1,693,090	(91,769)	1,601,321	5.4
- overdue 90-179 days	417,813	(67,404)	350,409	16.1
- overdue 180-359 days	869,322	(156,155)	713,167	18.0
- overdue more than 360 days	1,546,576	(10,396)	1,536,180	0.7
Total overdue but not impaired loans	4,747,230	(361,263)	4,385,967	7.6
Overdue and impaired loans				
- overdue less than 30 days	516,875	(211,177)	305,698	40.9
- overdue 30-89 days	6,489,488	(2,571,597)	3,917,891	39.6
- overdue 90-179 days	1,197,569	(202,015)	995,554	16.9
- overdue 180-359 days	2,451,187	(459,308)	1,991,879	18.7
- overdue more than 360 days	8,926,984	(928,377)	7,998,607	10.4
Total overdue and impaired loans	19,582,103	(4,372,474)	15,209,629	22.3
Total loans to large corporates	64,737,839	(6,466,015)	58,271,824	10.0
Loans to small and medium size companies				
Loans without individual signs of impairment				
- not overdue	24,064,673	(1,007,974)	23,056,699	4.2
Overdue but not impaired loans				
- overdue less than 30 days	74,572	-	74,572	-
- overdue 30-89 days	662,305	-	662,305	-
- overdue 90-179 days	2,298,484	-	2,298,484	-
- overdue 180-359 days	607,942	(8,207)	599,735	1.4
- overdue more than 360 days	1,980,377	(733)	1,979,644	0.0
Total overdue but not impaired loans	5,623,680	(8,940)	5,614,740	0.2
Overdue and impaired loans				
- overdue 90-179 days	3,753,229	(2,378,462)	1,374,767	63.4
- overdue 180-359 days	1,734,474	(381,349)	1,353,125	22.0
- overdue more than 360 days	7,444,710	(1,057,883)	6,386,827	14.2
Total overdue and impaired loans	12,932,413	(3,817,694)	9,114,719	29.5
Total loans to small and medium size companies	42,620,766	(4,834,608)	37,786,158	11.3
Total loans to corporate customers	107,358,605	(11,300,623)	96,057,982	10.5

18 Loans to customers (continued)

	Gross loans	Impairment allowance	Net loans	Impairment allowance to gross loans
	AMD'000	AMD'000	AMD'000	%
Loans to retail customers				
Mortgage loans				
- not past due	13,987,733	(28,160)	13,959,573	0.2
- overdue less than 30 days	47,424	(93)	47,331	0.2
- overdue 30-89 days	154,430	(5,071)	149,359	3.3
- overdue 90-179 days	301,739	(57,696)	244,043	19.1
- overdue 180-359 days	7,562	(14)	7,548	0.2
- overdue more than 360 days	535,612	(31,049)	504,563	5.8
Total mortgage loans	15,034,500	(122,083)	14,912,417	0.8
Credit cards				
- not past due	2,475,275	(38,373)	2,436,902	1.6
- overdue less than 30 days	9,279	(143)	9,136	1.5
- overdue 30-89 days	14,320	(222)	14,098	1.6
- overdue 90-179 days	4,428	(69)	4,359	1.6
Total credit cards	2,503,302	(38,807)	2,464,495	1.6
Construction loans				
- not past due	428,785	(844)	427,941	0.2
- overdue less than 30 days	3,361	(7)	3,354	0.2
- overdue more than 360 days	52,576	(41)	52,535	0.1
Total construction loans	484,722	(892)	483,830	0.2
Auto loans				
- not past due	326,433	(8,662)	317,771	2.7
- overdue more than 360 days	1,795	(48)	1,747	2.7
Total auto loans	328,228	(8,710)	319,518	2.7
Consumer loans				
- not past due	3,684,308	(6,911)	3,677,397	0.2
- overdue less than 30 days	7,696	(14)	7,682	0.2
- overdue 30-89 days	7,806	(14)	7,792	0.2
Total consumer loans	3,699,810	(6,939)	3,692,871	0.2
Other loans to retail customers				
- not past due	1,572,163	(12,036)	1,560,127	0.8
- overdue less than 30 days	3,853	(27)	3,826	0.7
- overdue 30-89 days	2,023	(14)	2,009	0.7
- overdue 90-179 days	47,475	(156)	47,319	0.3
- overdue more than 360 days	45,982	(22)	45,960	0.0
Total other loans to retail customers	1,671,496	(12,255)	1,659,241	0.7
Total loans to retail customers	23,722,058	(189,686)	23,532,372	0.8
Total loans to customers	131,080,663	(11,490,309)	119,590,354	8.8

18 Loans to customers (continued)

The following table provides information on the credit quality of loans to customers as at 31 December 2015:

	Gross loans	Impairment allowance	Net loans	Impairment allowance to gross loans
	AMD'000	AMD'000	AMD'000	%
Loans to corporate customers				
Loans to large corporates				
Loans without individual signs of impairment				
- not overdue	54,248,617	(300,828)	53,947,789	0.6
Overdue but not impaired loans				
- overdue less than 30 days	4,602,011	(5,004)	4,597,007	0.1
- overdue 90-179 days	3,021,454	(16,011)	3,005,443	0.5
Total overdue but not impaired loans	7,623,465	(21,015)	7,602,450	0.3
Overdue and impaired loans				
- overdue more than 360 days	735,752	(48,097)	687,655	6.5
Total overdue and impaired loans	735,752	(48,097)	687,655	6.5
Total loans to large corporates	62,607,834	(369,940)	62,237,894	0.6
Loans to small and medium size companies				
Loans without individual signs of impairment				
- not overdue	48,684,154	(263,653)	48,420,501	0.5
Overdue but not impaired loans				
- overdue less than 30 days	2,326,264	(2,529)	2,323,735	0.1
- overdue 30-89 days	1,905,720	(2,072)	1,903,648	0.1
- overdue 90-179 days	5,702,796	(9,174)	5,693,622	0.2
- overdue 180-359 days	1,941,257	(10,500)	1,930,757	0.5
Total overdue but not impaired loans	11,876,037	(24,275)	11,851,762	0.2
Overdue and impaired loans				
- overdue 90-179 days	2,098,819	(421,567)	1,677,252	20.1
- overdue 180-359 days	998,281	(334,596)	663,685	33.5
- overdue more than 360 days	13,752,793	(3,807,584)	9,945,209	27.7
Total overdue and impaired loans	16,849,893	(4,563,747)	12,286,146	27.1
Total loans to small and medium size companies	77,410,084	(4,851,675)	72,558,409	6.3
Total loans to corporate customers	140,017,918	(5,221,615)	134,796,303	3.7

18 Loans to customers (continued)

	Gross loans AMD'000	Impairment allowance AMD'000	Net loans AMD'000	Impairment allowance to gross loans %
Loans to retail customers				
Mortgage loans				
- not past due	15,861,527	(21,410)	15,840,117	0.1
- overdue less than 30 days	189,808	(204)	189,604	0.1
- overdue 30-89 days	163,048	(176)	162,872	0.1
- overdue 90-179 days	14,195	(15)	14,180	0.1
- overdue 180-359 days	250,159	(271)	249,888	0.1
- overdue more than 360 days	332,524	(6,932)	325,592	2.1
Total mortgage loans	16,811,261	(29,008)	16,782,253	0.2
Credit cards				
- not past due	2,572,935	(23,311)	2,549,624	0.9
- overdue less than 30 days	14,168	(128)	14,040	0.9
- overdue 30-89 days	7,806	(71)	7,735	0.9
- overdue 90-179 days	7,072	(64)	7,008	0.9
Total credit cards	2,601,981	(23,574)	2,578,407	0.9
Construction loans				
- not past due	590,586	(1,732)	588,854	0.3
- overdue less than 30 days	2,042	(4)	2,038	0.2
- overdue 30-89 days	2,627	(6)	2,621	0.2
- overdue 180-359 days	1,169	(2)	1,167	0.2
- overdue more than 360 days	45,290	(96)	45,194	0.2
Total construction loans	641,714	(1,840)	639,874	0.3
Auto loans				
- not past due	564,123	(9,708)	554,415	1.7
- overdue less than 30 days	6,619	(114)	6,505	1.7
- overdue 30-89 days	2,287	(39)	2,248	1.7
- overdue 180-359 days	1,650	(28)	1,622	1.7
- overdue more than 360 days	11,366	(4,492)	6,874	39.5
Total auto loans	586,045	(14,381)	571,664	2.5
Consumer loans				
- not past due	2,937,062	(2,015)	2,935,047	0.1
- overdue less than 30 days	4,098	(3)	4,095	0.1
- overdue 30-89 days	5,413	(4)	5,409	0.1
- overdue 90-179 days	7,270	(5)	7,265	0.1
- overdue more than 360 days	45,981	(32)	45,949	0.1
Total consumer loans	2,999,824	(2,059)	2,997,765	0.1
Other loans to retail customers				
- not past due	2,775,356	(6,189)	2,769,167	0.2
- overdue less than 30 days	12,330	(26)	12,304	0.2
- overdue 30-89 days	11,200	(24)	11,176	0.2
- overdue 90-179 days	47,506	(59)	47,447	0.1
Total other loans to retail customers	2,846,392	(6,298)	2,840,094	0.2
Total loans to retail customers	26,487,217	(77,160)	26,410,057	0.3
Total loans to customers	166,505,135	(5,298,775)	161,206,360	3.2

18 Loans to customers (continued)

All not overdue loans are assigned the same credit rating according to the Bank's internal policies and have no signs of downgrade as at 31 December 2016 and 31 December 2015.

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

(i) *Loans to corporate customers*

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

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

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

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

A modelling approach based on historic loss rate modelled allowance is used for portfolio provision, while in determining the individual impairment allowance for loans to corporate customers, management makes the following key assumptions:

- Historical Loss Rate of 4.63% (31 December 2015: 0.92%) determined based on the previous 60 months (31 December 2015: 60 months) credit losses.
- Estimated emergence periods of 7 months (31 December 2015: 5 months) is defined for whole portfolio.
- A discount up to 80% (31 December 2015: 30%) to the appraised value if the asset pledged is sold. The discount is computed based on several assumptions, including, but not limited to, collateral type, liquidity and location.
- A delay up to 24 months (31 December 2015: 12 to 24 months) in obtaining proceeds from the foreclosure of collateral for loans with individual signs of impairment.

Changes in these estimates could affect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by minus one percent, the impairment allowance on loans to corporate customers as at 31 December 2016 would be AMD 960,580 thousand higher (2015: AMD 1,347,963 thousand higher).

18 Loans to customers (continued)

(ii) *Loans to retail customers*

The Bank estimates loan impairment for loans to retail customers based on Historical Loss Rate (HLR) methodology for all unsecured loans and secured loans with up to 90 days delinquency and discounted cash-flow (DCF) methodology is applied for secured assets that are 90 or more days past due. The significant assumptions used in determining the impairment losses for loans to retail customers as at 31 December 2016 include:

- Historical annual loss rates of 0.25% (31 December 2015: 0.31%) for mortgage and other loans secured by real estate, 2.17% (31 December 2015: 1.9%) for auto loans, 0.38% (31 December 2015: 0.24%) for consumer loans and 0.98% (31 December 2015: 1%) for credit cards are determined based on the previous 60 months (31 December 2015: 60 months) loss data.
- Estimated emergence periods of 6 months (31 December 2015: 3 months) for mortgage and other loans secured by real estate, 8 months (31 December 2015: 6 months) for car loans, 9 months (31 December 2015: 6 months) for overdrafts and credit cards between occurrence of an impairment loss and identification of the loss.
- In case of DCF it is expected that the cash flow from the sale of the pledge will flow in 18 months' time (31 December 2015: 12 months' time). If property liquidation values provided by the valuation agency are available, then that value is used for discounting, otherwise the average market price per square meter is used by applying a reduction of 25% (31 December 2015: 20%) from market value.
- Unsecured loans overdue more than 180 days (31 December 2015: 180 days) are considered as a loss.

Changes in these estimates could affect the loan impairment provision. For example, to the extent that the net present value of the estimated cash flows differs by minus three percent, the impairment allowance on loans to retail customers as at 31 December 2016 would be AMD 705,971 thousand higher (2015: AMD 792,302 thousand higher).

18 Loans to customers (continued)

(c) Analysis of collateral and other credit enhancements

(i) Loans to corporate customers

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

31 December 2016	Loans to customers, carrying amount	Fair value of collateral assessed in the reporting period
AMD'000		
Loans without individual signs of impairment		
Borrower settlement account	3,739,650	-
Cash and deposits	1,604	1,604
Armenian Government treasury bills	2,426,994	2,426,994
Real estate	49,824,326	49,824,326
Motor vehicles	325,084	325,084
Equipment	370,687	370,687
Stock	2,099,710	2,099,710
Other collateral	68,251	68,251
Corporate guarantees (unrated)	1,197,034	1,197,034
No collateral or other credit enhancement – personal guarantees	1,679,587	-
Total loans without individual signs of impairment	61,732,927	56,313,690
Overdue but not impaired loans		
Real estate	9,262,705	9,262,705
Other	589,169	589,169
Corporate guarantees (unrated)	108,657	108,657
Stock	40,000	40,000
No collateral or other credit enhancement – personal guarantees	176	-
Total overdue but not impaired loans	10,000,707	10,000,531
Overdue and impaired loans		
Borrower settlement account	350,687	-
Real estate	20,782,424	20,782,424
Equipment	1,511,344	1,511,344
Other	1,020,886	1,020,886
Corporate guarantees (unrated)	584,286	584,286
No collateral or other credit enhancement – personal guarantees	74,721	-
Total overdue and impaired loans	24,324,348	23,898,940
Total loans to corporate customers	96,057,982	90,213,161

18 Loans to customers (continued)

31 December 2015	Loans to customers, carrying amount	Fair value of collateral assessed in the reporting period
AMD'000		
Loans without individual signs of impairment		
Borrower settlement account	4,568,506	-
Cash and deposits	17,249	17,249
Armenian Government treasury bills	3,328,752	3,328,752
Real estate	86,487,489	86,487,489
Motor vehicles	284,990	284,990
Equipment	2,065,393	2,065,393
Stock	2,046,317	2,046,317
Other collateral	183,812	183,812
State guarantees	907,413	907,413
Corporate guarantees (unrated)	367,199	367,199
No collateral or other credit enhancement – personal guarantees	2,111,170	-
Total loans without individual signs of impairment	102,368,290	95,688,614
Overdue but not impaired loans		
Real estate	16,783,139	16,783,139
Equipment	2,671,073	2,671,073
Total overdue but not impaired loans	19,454,212	19,454,212
Overdue and impaired loans		
Real estate	12,894,756	12,894,756
Equipment	27,500	27,500
Stock	51,545	51,545
Total overdue and impaired loans	12,973,801	12,973,801
Total loans to corporate customers	134,796,303	128,116,627

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

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

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

(ii) Loans to retail customers

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

The fair value of collateral is at least equal to carrying amounts of individual mortgage and construction loans as at 31 December 2016 and 2015.

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

Credit card loans are not secured.

18 Loans to customers (continued)

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

Consumer loans represent unsecured personal loans.

(d) Industry and geographical analysis of the loan portfolio

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

	31 December 2016	31 December 2015
	AMD'000	AMD'000
Trade	26,505,200	32,087,760
Construction	7,581,879	7,983,560
Food and beverages	25,700,992	29,581,779
Services	19,917,319	33,273,605
Energy	5,723,607	10,316,441
Manufacturing	10,312,291	11,177,583
Agriculture	2,760,077	2,829,786
Finance	2,427,026	3,329,278
Chemicals	-	204,716
Other	6,430,214	9,233,411
Loans to individuals	23,722,058	26,487,216
Total loans to customers (gross)	131,080,663	166,505,135
Impairment allowance	(11,490,309)	(5,298,775)
Total loans to customers (net)	119,590,354	161,206,360

(e) Significant credit exposures

As at 31 December 2016 the Bank had three borrowers or groups of connected borrowers (2015: three), whose loan balances exceeded 10% of equity. The gross value of these loans as at 31 December 2016 was AMD 15,508,372 thousand (2015: AMD 16,728,269 thousand).

19 Property, equipment and intangible assets

AMD'000	Land and buildings	Leasehold improvements	Vehicles	Computer equipment	Intangible assets	Other	Total
Cost/revalued amount							
Balance at 1 January 2016	1,498,401	2,979,924	158,746	1,632,631	3,583,200	1,393,495	11,246,397
Additions	1,517	8,844	44,000	71,463	357,618	44,077	527,519
Disposals/write-offs	-	(7,170)	(18,972)	(28,135)	(59,879)	(39,674)	(153,830)
Balance at 31 December 2016	1,499,918	2,981,598	183,774	1,675,959	3,880,939	1,397,898	11,620,086
Depreciation, amortisation and impairment losses							
Balance at 1 January 2016	-	(2,521,441)	(115,717)	(1,417,803)	(2,039,580)	(1,247,598)	(7,342,139)
Depreciation and amortisation charge	(101,394)	(134,530)	(16,122)	(96,764)	(591,025)	(71,712)	(1,011,547)
Disposals/write-offs	-	7,170	18,972	27,811	59,879	38,093	151,925
Balance at 31 December 2016	(101,394)	(2,648,801)	(112,867)	(1,486,756)	(2,570,726)	(1,281,217)	(8,201,761)
Carrying amount							
At 31 December 2016	1,398,524	332,797	70,907	189,203	1,310,213	116,681	3,418,325
Cost/revalued amount							
Balance at 1 January 2015	1,876,253	2,977,513	166,578	1,611,624	3,120,903	1,368,601	11,121,472
Additions	21,400	9,647	14,729	48,430	540,645	28,845	663,696
Disposals/write-offs	-	(7,236)	(22,561)	(27,423)	(78,348)	(3,951)	(139,519)
Revaluation	(399,252)	-	-	-	-	-	(399,252)
Balance at 31 December 2015	1,498,401	2,979,924	158,746	1,632,631	3,583,200	1,393,495	11,246,397
Depreciation, amortisation and impairment losses							
Balance at 1 January 2015	(693,290)	(2,298,489)	(121,456)	(1,301,170)	(1,657,355)	(1,184,165)	(7,255,925)
Depreciation and amortisation charge	(68,880)	(229,251)	(14,107)	(144,056)	(460,573)	(67,384)	(984,251)
Disposals/write-offs	-	6,299	19,846	27,423	78,348	3,951	135,867
Revaluation	762,170	-	-	-	-	-	762,170
Balance at 31 December 2015	-	(2,521,441)	(115,717)	(1,417,803)	(2,039,580)	(1,247,598)	(7,342,139)
Carrying amount							
At 31 December 2015	1,498,401	458,483	43,029	214,828	1,543,620	145,897	3,904,258

19 Property, equipment and intangible assets (continued)

Revalued assets

At 31 December 2016 land and buildings were revalued based on the results of an independent appraisal performed by an independent valuator. The resulting fair values were not materially different from the carrying value of the land and buildings and no revaluation impact was recorded in the financial statements.

At 31 December 2015 land and buildings were revalued based on the results of an independent appraisal performed by an independent valuator. The resulting fair values were materially different from the carrying value of the land and buildings. Revaluation impact have been recorded in the financial statements accordingly.

Due to the nature of the land and buildings and lack of comparable market data, the fair value of the land and buildings is estimated based on the income capitalisation method, where the value is estimated from the expected market rental income streams from similar properties and capitalisation yields. The method considers net income generated by comparable property, capitalised to determine the value for property which is subject to the valuation.

The principal assumptions underlying the estimation of the fair value are those relating to: the possible market rentals and appropriate discount rates. These valuations are regularly compared to actual market data and actual transactions by the Bank and those reported by the market.

The impact on the aggregate valuations of reasonably possible changes in these assumptions, with all other variables held constant, are as follows:

- The capitalisation rate was assumed to be 5%. Should this capitalisation rate increase / decrease by 1 percentage point, the carrying value of the land and buildings would be AMD 255,241 thousand lower / AMD 382,862 thousand higher.
- Should the rental income assumed in the valuation report increase / decrease by 10 percent, the carrying value of the land and buildings would be AMD 153,145 thousand higher / AMD 153,145 thousand lower.

The carrying value of land and buildings as of 31 December 2016, if the land and buildings would not have been revalued would be AMD 1,096,041 thousand (31 December 2015: AMD 1,166,194 thousand).

20 Other assets

	31 December 2016 AMD'000	31 December 2015 AMD'000
Other financial assets		
Receivables for letters of credit	4,068,524	11,714,685
Accrued commissions	569,210	259,473
Other	233,573	325,038
Total financial assets	4,871,307	12,299,196
Other non-financial assets		
Prepayments	36,592	138,562
Materials and supplies	27,369	50,148
Reposessed collateral	572,738	-
Total non-financial assets	636,699	188,710
Total other assets	5,508,006	12,487,906

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

Reposessed collateral represents real estate assets acquired by the Bank in settlement of overdue loans. The Bank expects to dispose of the assets in the foreseeable future. The transaction did not require the use of cash and cash equivalents and was excluded from the statement of cash flows.

No other assets are impaired.

Movements in the other assets impairment allowance for the year ended 31 December 2016 are as follows:

	Receivables for letters of credit AMD'000	Total AMD'000
Balance at the beginning of the year	-	-
Net charge	256,800	256,800
Net write-offs	(256,800)	(256,800)
Balance at the end of the year	-	-

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

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

21 Deposits and balances from banks

	31 December 2016 AMD'000	31 December 2015 AMD'000
Members of HSBC Group	10,933,412	33,648,748
Loans received from the CBA	545,949	-
Financial institutions	116,524	11,797,028
Total deposits and balances from banks	11,595,885	45,445,776

21 Deposits and balances from banks (continued)

As at 31 December 2016 the Bank had two banks (31 December 2015: three banks), whose balances exceeded 10% of equity. The gross value of these balances as at 31 December 2016 were AMD 10,928,102 thousand (2015: AMD 37,027,993 thousand).

Included in loans from financial institutions and the CBA are loans from international and governmental financial institutions and the CBA with arrangements to sub-lend these funds to borrowers for qualifying loans. The qualifying loans under these agreements are loans to small and medium size businesses and the energy efficiency sector.

22 Current accounts and deposits from customers

	31 December 2016 AMD'000	31 December 2015 AMD'000
Current accounts		
- Retail	38,717,213	43,378,569
- Corporate	28,459,594	35,886,526
Term deposits		
- Retail	68,373,927	64,094,850
- Corporate	14,184,018	17,052,305
Other	98,081	72,589
Total current accounts and deposits from customers	149,832,833	160,484,839

As at 31 December 2016, the Bank maintained customer deposit balances of AMD 1,185,818 thousand (31 December 2015: AMD 1,602,685 thousand) that served as collateral for loans and unrecognised credit instruments granted by the Bank.

As at 31 December 2016, the Bank had two customers (31 December 2015: one customer), whose balances exceeded 10% of equity. These balances as at 31 December 2016 were AMD 11,366,297 thousand (2015: AMD 5,873,383 thousand).

23 Other liabilities

	31 December 2016 AMD'000	31 December 2015 AMD'000
Other financial liabilities		
Payables for letters of credit	4,068,524	11,714,685
Deferred income	286,447	655,399
Accrued expenses	132,487	116,580
Foreign currency derivative contracts at fair value through profit or loss	2,328	25,169
Other	217,038	223,529
Total other financial liabilities	4,706,824	12,735,362
Other non-financial liabilities		
Accrued employee benefit costs	725,146	711,518
Deferred income	341,322	609,743
Payable to Deposit Guarantee Fund	52,156	52,612
Total other non-financial liabilities	1,118,624	1,373,873
Total other liabilities	5,825,448	14,109,235

24 Share capital

(a) Issued capital

The authorised, issued and outstanding share capital comprises 609,400 ordinary shares of AMD 30.25 thousand each (2015: 609,400 of AMD 30.25 thousand each).

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

(b) Dividends

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

No dividends were declared and paid during 2016 (2015: nil).

25 Risk management

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

25 Risk management (continued)

(a) Risk management policies and procedures

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

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

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

(b) Market risk

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

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

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

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

(i) *Interest rate risk*

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

25 Risk management (continued)

Interest rate gap analysis

Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the interest gap position for major financial instruments as at 31 December 2016 and 2015 is as follows:

AMD'000	Less than 3 months	3-12 months	1-5 years	More than 5 years	Non-interest bearing	Carrying amount
31 December 2016						
ASSETS						
Cash and cash equivalents	3,142,684	-	-	-	50,934,032	54,076,716
Financial instruments at fair value through profit or loss	636,930	-	-	-	285,815	922,745
Available-for-sale financial assets	6,887,425	12,675,945	5,085,463	93,002	32,032	24,773,867
Loans and advances to banks	6,238,794	-	-	-	-	6,238,794
Loans to customers	115,372,936	1,904,748	2,310,199	2,471	-	119,590,354
Other financial assets	-	-	-	-	4,871,307	4,871,307
Total financial assets	132,278,769	14,580,693	7,395,662	95,473	56,123,186	210,473,783
LIABILITIES						
Deposits and balances from banks	7,196,225	3,854,243	535,000	-	10,417	11,595,885
Current accounts and deposits from customers	55,087,416	29,288,904	1,564,812	-	63,891,701	149,832,833
Other financial liabilities	-	-	-	-	4,706,824	4,706,824
Total financial liabilities	62,283,641	33,143,147	2,099,812	-	68,608,942	166,135,542
Interest rate gap	69,995,128	(18,562,454)	5,295,850	95,473	(12,485,756)	44,338,241

25 Risk management (continued)

AMD'000	Less than 3 months	3-12 months	1-5 years	More than 5 years	Non-interest bearing	Carrying amount
31 December 2015						
ASSETS						
Cash and cash equivalents	1,321,475	-	-	-	71,965,040	73,286,515
Financial instruments at fair value through profit or loss	671,693	-	-	-	248,092	919,785
Available-for-sale financial assets	98,424	2,874,428	10,557,128	74,465	32,056	13,636,501
Loans and advances to banks	8,840,791	-	-	-	-	8,840,791
Loans to customers	157,321,282	2,398,144	1,483,660	3,274	-	161,206,360
Other financial assets	-	-	-	-	12,299,196	12,299,196
Total financial assets	168,253,665	5,272,572	12,040,788	77,739	84,544,384	270,189,148
LIABILITIES						
Deposits and balances from banks	34,829,525	9,329,573	-	-	1,286,678	45,445,776
Current accounts and deposits from customers	49,464,091	33,184,482	1,430,698	-	76,405,568	160,484,839
Other financial liabilities	-	-	-	-	12,735,362	12,735,362
Total financial liabilities	84,293,616	42,514,055	1,430,698	-	90,427,608	218,665,977
Interest rate gap	83,960,049	(37,241,483)	10,610,090	77,739	(5,883,224)	51,523,171

25 Risk management (continued)

Average interest rates

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

	2016			2015		
	Average effective interest rate, %			Average effective interest rate, %		
	AMD	USD	Other currencies	AMD	USD	Other currencies
Interest bearing assets						
Cash and cash equivalents	4.9	-	8.6	-	-	2.0
Financial instruments at fair value through profit or loss	12.4	-	-	14.4	-	-
Available-for-sale financial assets	10.3	-	-	11.5	-	-
Loans and advances to banks	5.7	-	-	9.6	6.3	-
Loans to customers	14.4	9.5	7.6	16.2	10.1	8.2
Interest bearing liabilities						
Deposits and balances from banks	9.3	1.5	1.6	9.3	2.7	-
Current accounts and deposits from customers						
- Current accounts and demand deposits	2.1	1.1	-	1.9	1.1	-
- Term deposits	11.5	4.3	1.2	10.4	4.1	0.9

Interest rate sensitivity analysis

The management of interest rate risk based on interest rate gap analysis is supplemented by monitoring the sensitivity of financial assets and liabilities. An analysis of sensitivity of profit or loss and equity (net of taxes) to changes in interest rates (repricing risk) based on a simplified scenario of a 100 basis point (bp) symmetrical fall or rise in all positions of interest-bearing assets and liabilities, excluding financial instruments at fair value through profit or loss and financial assets available-for-sale, existing as at 31 December 2016 and 2015 is as follows:

	2016		2015	
	Profit or loss AMD'000	Equity AMD'000	Profit or loss AMD'000	Equity AMD'000
100 bp parallel rise	848,854	848,854	935,650	935,650
100 bp parallel fall	(848,854)	(848,854)	(935,650)	(935,650)

25 Risk management (continued)

An analysis of sensitivity of profit or loss and equity as a result of changes in the fair value of financial instruments at fair value through profit or loss and financial assets available-for-sale due to changes in the interest rates based on positions existing as at 31 December 2016 and 2015 and a simplified scenario of a 100 bp symmetrical fall or rise in all yield curves is as follows:

	2016		2015	
	Profit or loss AMD'000	Equity AMD'000	Profit or loss AMD'000	Equity AMD'000
100 bp parallel rise	(21,190)	(130,574)	(19,373)	(160,430)
100 bp parallel fall	23,173	134,561	20,798	165,398

(ii) Currency risk

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

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

The following table shows the foreign currency exposure structure of financial assets and financial liabilities as at 31 December 2016:

	AMD	USD	EUR	Other currencies	Total
	AMD'000	AMD'000	AMD'000	AMD'000	AMD'000
ASSETS					
Cash and cash equivalents	31,048,882	17,508,833	3,477,281	2,041,720	54,076,716
Financial instruments at fair value through profit or loss	636,930	282,002	-	3,813	922,745
Available-for-sale financial assets	24,773,118	-	749	-	24,773,867
Loans and advances to banks	6,223,504	-	3,474	11,816	6,238,794
Loans to customers	29,352,709	74,835,804	15,295,697	106,144	119,590,354
Other financial assets	195,390	1,190,018	3,485,899	-	4,871,307
Total financial assets	92,230,533	93,816,657	22,263,100	2,163,493	210,473,783
LIABILITIES					
Deposits and balances from banks	672,889	5,787,184	5,135,812	-	11,595,885
Current accounts and deposits from customers	39,596,509	94,651,593	13,789,882	1,794,849	149,832,833
Other financial liabilities	373,266	758,073	3,434,187	141,298	4,706,824
Total financial liabilities	40,642,664	101,196,850	22,359,881	1,936,147	166,135,542
Net position as at 31 December 2016	51,587,869	(7,380,193)	(96,781)	227,346	44,338,241
The effect of derivatives held for risk management and regular way currency contracts	(5,666,428)	5,802,134	-	(135,706)	-

25 Risk management (continued)

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2015:

	AMD	USD	EUR	Other currencies	Total
	AMD'000	AMD'000	AMD'000	AMD'000	AMD'000
ASSETS					
Cash and cash equivalents	39,806,585	29,042,925	1,743,618	2,693,387	73,286,515
Financial instruments at fair value through profit or loss	919,785	-	-	-	919,785
Available-for-sale financial assets	13,635,728	-	773	-	13,636,501
Loans and advances to banks	7,360,603	1,465,586	1,262	13,340	8,840,791
Loans to customers	31,658,834	110,136,893	19,410,633	-	161,206,360
Other financial assets	299,994	5,286,166	6,713,036	-	12,299,196
Total financial assets	93,681,529	145,931,570	27,869,322	2,706,727	270,189,148
LIABILITIES					
Deposits and balances from banks	1,444,743	44,001,033	-	-	45,445,776
Current accounts and deposits from customers	33,674,979	111,907,420	12,871,233	2,031,207	160,484,839
Other financial liabilities	413,523	5,055,950	6,738,642	527,247	12,735,362
Total financial liabilities	35,533,245	160,964,403	19,609,875	2,558,454	218,665,977
Net position as at 31 December 2015	58,148,284	(15,032,833)	8,259,447	148,273	51,523,171
The effect of derivatives held for risk management and regular way currency contracts	(4,480,615)	13,121,387	(8,609,383)	(31,389)	-

A strengthening of the AMD, as indicated below, against the following currencies at 31 December 2016 and 2015 would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis is based on foreign currency exchange rate variances that the Bank considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

	2016		2015	
	Profit or loss AMD'000	Equity AMD'000	Profit or loss AMD'000	Equity AMD'000
10% depreciation of USD against AMD	157,770	157,770	191,145	191,145
10% depreciation of EUR against AMD	(9,678)	(9,678)	34,994	34,994

A weakening of the AMD against the above currencies at 31 December 2016 and 2015 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

25 Risk management (continued)

(c) Credit risk

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

The credit policy is in line with HSBC Group standards.

The credit policy establishes:

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

Corporate loan credit applications are originated by the relevant relationship managers via the Credit Approval and Relationship Management (the “CARM”) system and are then passed on for review to the Head of Wholesale Banking and approval to the Chief Risk Officer or Regional Credit and Risk team within the established credit approval limits. Analysis reports are based on a structured analysis focusing on the customer’s business and financial performance. All legal documents regarding credit facilities are prepared and amended based on the approved CARM application.

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

Retail loan credit applications are reviewed by the Retail Credit department through verification of application data with criteria set in the Retail Banking Wealth Management (the “RBWM”) Risk and Reward Plans (RRPs) approved by the Board of Directors.

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

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

25 Risk management (continued)

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

	2016 AMD'000	2015 AMD'000
ASSETS		
Cash and cash equivalents	48,731,472	67,988,678
Financial instruments at fair value through profit or loss	922,745	919,785
Available-for-sale debt assets	24,741,835	13,604,445
Loans and advances to banks	6,238,794	8,840,791
Loans to customers	119,590,354	161,206,360
Other financial assets	4,871,307	12,299,196
Credit related commitments and guarantees	30,295,009	33,875,988
Total maximum exposure	235,391,516	298,735,243

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

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

For the analysis of collateral held against loans to customers and of concentration of credit risk in respect of loans to customers refer to Note 18.

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

Offsetting financial assets and financial liabilities

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

- are offset in the Bank's statement of financial position; or
- are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments, irrespective of whether they are offset in the statement of financial position.

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

25 Risk management (continued)

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

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

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

The table below shows financial assets and financial liabilities subject to offsetting, enforceable master netting arrangements and similar arrangements as at 31 December 2016:

AMD'000 Types of financial assets/liabilities	Gross amounts of recognised financial asset/liability	Gross amount of recognised financial liability/asset offset	Net amount of financial assets/ liabilities	Related amounts not offset Financial Instruments (non-cash collateral)	Net amount
Reverse sale and repurchase agreements	7,244,091	-	7,244,091	(7,244,091)	-
Total financial assets	7,244,091	-	7,244,091	(7,244,091)	-

The table below shows financial assets and financial liabilities subject to offsetting, enforceable master netting arrangements and similar arrangements as at 31 December 2015:

AMD'000 Types of financial assets/liabilities	Gross amounts of recognised financial asset/liability	Gross amount of recognised financial liability/asset offset	Net amount of financial assets/ liabilities	Related amounts not offset Financial Instruments (non-cash collateral)	Net amount
Reverse sale and repurchase agreements	3,325,889	-	3,325,889	(3,325,889)	-
Total financial assets	3,325,889	-	3,325,889	(3,325,889)	-

25 Risk management (continued)

(d) Liquidity risk

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

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

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

The liquidity management policy requires:

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

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

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

25 Risk management (continued)

The following tables show the undiscounted cash flows on financial liabilities and credit-related commitments on the basis of their remaining contractual maturity. The total gross inflow and outflow disclosed in the tables is the contractual, undiscounted cash flow on the financial liability or commitment. For issued financial guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee can be called. The maturity analysis for financial liabilities as at 31 December 2016 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	Total
AMD'000						
Non-derivative liabilities						
Deposits and balances from banks	681,042	1,336,203	3,907,533	5,991,940	-	11,916,718
Current accounts and deposits from customers	75,902,131	10,963,715	42,334,889	24,195,803	1,350,982	154,747,520
Other financial liabilities	753,486	369,554	3,235,063	348,721	-	4,706,824
Total liabilities	77,336,659	12,669,472	49,477,485	30,536,464	1,350,982	171,371,062
Credit related commitments and letters of credit	26,872,328	-	-	-	-	26,872,328
Performance guarantees	2,368,969	-	-	-	-	2,368,969
Financial guarantees	846,257	-	-	-	-	846,257
Other commitments	207,455	-	-	-	-	207,455

The maturity analysis for financial liabilities as at 31 December 2015 is as follows:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	Total
AMD'000						
Non-derivative liabilities						
Deposits and balances from banks	13,665,190	665,564	9,410,763	23,149,770	-	46,891,287
Current accounts and deposits from customers	90,736,180	11,738,644	44,914,890	15,470,877	1,372,039	164,232,630
Other financial liabilities	1,960,911	589,502	7,045,398	3,139,551	-	12,735,362
Total liabilities	106,362,281	12,993,710	61,371,051	41,760,198	1,372,039	223,859,279
Credit related commitments and letters of credit	30,331,947	-	-	-	-	30,331,947
Performance guarantees	1,822,633	-	-	-	-	1,822,633
Financial guarantees	1,402,966	-	-	-	-	1,402,966
Other commitments	318,442	-	-	-	-	318,442

25 Risk management (continued)

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

- less than 1 month: AMD 7,007,535 thousand (2015: AMD 6,491,542 thousand);
- from 1 to 3 months: AMD 9,044,531 thousand (2015: AMD 9,466,932 thousand);
- from 3 to 12 months: AMD 32,508,309 thousand (2015: AMD 33,010,457 thousand);
- from 1 to 5 years: AMD 18,341,680 thousand (2015: AMD 13,640,558 thousand);
- more than 5 years: AMD 796,686 thousand (2015: AMD 843,960 thousand).

25 Risk management (continued)

The table below shows an analysis, by expected maturities, of the amounts recognised in the statement of financial position as at 31 December 2016:

AMD'000	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Overdue	Total
Cash and cash equivalents	54,076,716	-	-	-	-	-	-	54,076,716
Financial instruments at fair value through profit or loss	661,561	47,616	213,568	-	-	-	-	922,745
Available-for-sale financial assets	4,292,549	2,594,876	12,675,944	5,085,464	93,002	32,032	-	24,773,867
Loans and advances to banks	6,238,794	-	-	-	-	-	-	6,238,794
Loans to customers	7,248,550	8,408,918	29,037,394	51,746,739	8,342,165	-	14,806,588	119,590,354
Current tax asset	-	-	632,010	-	-	-	-	632,010
Property, equipment and intangible assets	-	-	-	-	-	3,418,325	-	3,418,325
Other assets	621,449	374,515	3,819,092	348,721	-	30,403	313,826	5,508,006
Total assets	73,139,619	11,425,925	46,378,008	57,180,924	8,435,167	3,480,760	15,120,414	215,160,817
Deposits and balances from banks	680,422	1,332,485	3,875,235	5,707,743	-	-	-	11,595,885
Current accounts and deposits from customers	75,879,628	10,896,877	40,825,866	21,429,539	800,923	-	-	149,832,833
Deferred tax liability	-	-	-	-	-	899,429	-	899,429
Other liabilities	837,327	1,150,213	3,356,736	481,155	17	-	-	5,825,448
Total liabilities	77,397,377	13,379,575	48,057,837	27,618,437	800,940	899,429	-	168,153,595
Net position as at 31 December 2016	(4,257,758)	(1,953,650)	(1,679,829)	29,562,487	7,634,227	2,581,331	15,120,414	47,007,222

25 Risk management (continued)

The table below shows an analysis, by expected maturities, of the amounts recognised in the statement of financial position as at 31 December 2015:

AMD'000	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Overdue	Total
Cash and cash equivalents	73,286,515	-	-	-	-	-	-	73,286,515
Financial instruments at fair value through profit or loss	689,589	26,923	203,273	-	-	-	-	919,785
Available-for-sale financial assets	29,759	68,665	2,874,428	10,557,128	74,465	32,056	-	13,636,501
Loans and advances to banks	8,840,791	-	-	-	-	-	-	8,840,791
Loans to customers	8,252,124	10,345,024	38,385,063	78,311,269	9,939,062	-	15,973,818	161,206,360
Current tax asset	-	-	1,123,661	-	-	-	-	1,123,661
Property, equipment and intangible assets	-	-	-	-	-	3,904,258	-	3,904,258
Other assets	1,583,426	601,440	7,072,127	3,176,799	-	54,114	-	12,487,906
Total assets	92,682,204	11,042,052	49,658,552	92,045,196	10,013,527	3,990,428	15,973,818	275,405,777
Deposits and balances from banks	1,919,918	12,303,828	9,361,195	21,860,835	-	-	-	45,445,776
Current accounts and deposits from customers	90,712,126	11,668,531	43,500,400	13,752,118	851,664	-	-	160,484,839
Deferred tax liability	-	-	-	-	-	2,329,575	-	2,329,575
Other liabilities	2,785,258	696,650	7,267,407	3,352,781	7,139	-	-	14,109,235
Total liabilities	95,417,302	24,669,009	60,129,002	38,965,734	858,803	2,329,575	-	222,369,425
Net position as at 31 December 2015	(2,735,098)	(13,626,957)	(10,470,450)	53,079,462	9,154,724	1,660,853	15,973,818	53,036,352

25 Risk management (continued)

As at 31 December 2016 the Bank has a liquidity gap of assets and liabilities on demand and up to 12 months. This liquidity gap arises from the fact that an important source of funding for the Bank as of 31 December 2016 were customer accounts on demand. Management believes that in spite of a substantial portion of customer accounts being on demand, diversification of these deposits by number and type of depositors, and the past experience of the Bank indicate that these customer accounts provide a long-term and stable source of funding for the Bank.

The key measures used by the Bank for managing liquidity risk and funding risk are liquidity coverage ratio, liquid asset buffer ratio, net stable funding ratio, depositor and term funding maturity concentrations, which are monitored and managed on daily basis. Liquidity and funding risk appetite is defined by the Bank in Risk appetite statement approved by the Board. The CBA sets and monitors liquidity requirements for the Bank. Under the current requirements set by the CBA, banks have to maintain the ratios of liquid assets to total assets and liquid assets to on demand liabilities above the prescribed minimum level. For this purpose liquid assets include cash and cash equivalents and Government treasury bills, which are not pledged or the use of which is not restricted in any way. As at 31 December 2016, this minimum level was 15% and 60% respectively. The Bank was in compliance with the statutory liquidity ratios as at 31 December 2016 and 2015 and over the periods.

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

	2016 AMD'000	2015 AMD'000
At 31 December		
Ratio of liquid assets to total assets	36%	31%
Ratio of liquid assets to on demand liabilities	116%	107%

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

26 Capital management

The CBA sets and monitors capital requirements for the Bank.

The Bank defines as capital those items defined by statutory regulation as capital for credit institutions. Under the current capital requirements set by the CBA, banks have to maintain a ratio of capital to risk weighted assets (statutory capital ratio) above the prescribed minimum level. As at 31 December 2016, this minimum level was 12%. The Bank was in compliance with the statutory capital ratio as at 31 December 2016 and 2015 and over the periods.

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

26 Capital management (continued)

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

	2016 AMD'000	2015 AMD'000
Tier 1 capital		
Share capital	18,434,350	18,434,350
Retained earnings	26,028,383	32,692,794
General Reserve (CBA)	1,958,838	1,958,838
Adjustment to CBA accounting principles	(10,504,088)	(11,404,127)
Other deductions	(3,059,590)	(527,698)
Total tier 1 capital	32,857,893	41,154,157
Tier 2 capital		
Revaluation reserve for available-for-sale financial assets, gross of tax	321,364	(474,331)
Revaluation reserve for land and buildings	292,215	292,215
Share-based payment reserve	94,788	96,063
Total tier 2 capital	708,367	(86,053)
Total capital	33,566,260	41,068,104
Risk weighted assets, combining credit, market and operational risks	202,361,504	258,419,940
Total capital ratio	16.6%	15.9%

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

27 Commitments

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

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

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

27 Commitments (continued)

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

	31 December 2016 AMD'000	31 December 2015 AMD'000
Contracted amount		
Loan and credit line commitments	16,030,728	22,380,609
Credit card commitments	4,682,468	4,959,254
Performance guarantees	2,368,969	1,822,633
Undrawn overdraft facilities	5,465,166	1,564,135
Letters of credit	693,966	1,427,949
Financial guarantees	846,257	1,402,966
Other commitments	207,455	318,442
Total commitments	30,295,009	33,875,988

The total outstanding contractual commitments above do not necessarily represent future cash requirements, as these commitments may expire or terminate without being funded. However, the majority of loan and credit line commitments do not represent an unconditional commitment by the Bank. The fair value of commitments was AMD 426,306 thousand as at 31 December 2016 (31 December 2015: AMD 620,917 thousand).

Of these commitments, AMD 13,587,656 thousand are to 10 customers as at 31 December 2016 (31 December 2015: AMD 15,486,844 thousand are to 10 customers).

28 Operating leases

Non-cancelable operating lease rentals are payable as follows:

	31 December 2016 AMD'000	31 December 2015 AMD'000
Less than 1 year	451,768	541,496
Between 1 and 5 years	1,411,892	1,097,665
More than 5 years	1,781	248,537
Total operating lease rentals payable	1,865,441	1,887,698

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

29 Contingencies

(a) Litigation

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

(b) Taxation contingencies

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

These circumstances may create tax risks in the Republic of Armenia that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Armenian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on the financial position, if the authorities were successful in enforcing their interpretations, could be significant.

30 Custody activities

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

31 Related party transactions

(a) Transactions with the members of the Board and the Key Management Personnel

Total compensation is as follows:

	2016 AMD'000	2015 AMD'000
Total remuneration	533,302	550,197
Benefits-in-kind	143,671	80,124
Total remuneration and benefits-in-kind	676,973	630,321
Share-based payments	8,245	25,267
Total compensation	685,218	655,588

31 Related party transactions (continued)

The outstanding balances and interest rates are as follows:

	2016 AMD'000	2015 AMD'000
Statement of financial position		
ASSETS		
Loans to customers (contractual interest rate: 4.0% - 19.0%)	639,900	558,698
LIABILITIES		
Current accounts and deposits from customers (contractual interest rate: 0.0% - 11.3%)	151,087	164,110

Amounts included in the statement of profit or loss and other comprehensive income are as follows:

	2016 AMD'000	2015 AMD'000
Profit or loss		
Interest income	42,560	39,970
Interest expense	(4,000)	(4,818)

(b) Transactions with other related parties

Other related parties include entities under common control of the Bank's ultimate controlling party and other related parties of key management personnel. The outstanding balances and the related interest rates are as follows:

	31 December 2016 AMD'000		31 December 2015 AMD'000	
	Entities under common control	Other related parties	Entities under common control	Other related parties
Cash and cash equivalents (contractual interest rate: 0.0% - 9.0%)	13,508,595	-	19,611,700	-
Loans to customers (contractual interest rate: 8.0 %- 22.0%)	-	3,054	-	196,241
Financial instruments at fair value through profit or loss	285,815	-	248,092	-
Deposits and balances from banks (contractual interest rate: 0.0% – 2.9%)	10,933,412	-	32,363,357	-
Current accounts and deposits from customers (contractual interest rate: 0.0% – 11.3%)	-	534,438	-	4,285,776
Other liabilities	4,021,702	-	12,097,200	-

31 Related party transactions (continued)

Amounts included into the statement of profit or loss and other comprehensive income are as follows:

	2016 AMD'000		2015 AMD'000	
	Entities under common control	Other related parties	Entities under common control	Other related parties
Interest income	37,827	5,756	54,034	10,398
Interest expense	(847,930)	(25,904)	(608,606)	(156,480)
(Loss)/Gain from foreign currency contracts	(104,613)	-	441,589	-
Fee and commission expense	(103,422)	-	(118,942)	-
Other operating income	27,177	5,593	70,299	4,006
Administrative and other operating expenses	(1,552,976)	-	(1,955,860)	-

Other rights and obligations with related parties are as follows:

	31 December 2016 AMD'000	31 December 2015 AMD'000
	Entities under common control	Entities under common control
Guarantees issued to the Group at the year-end	865,708	908,277
Unused credit facilities	14,518,200	5,286,900
Foreign currency contracts	8,620,254	15,321,386

32 Financial assets and liabilities: fair values and accounting classifications

(a) Accounting classifications

The table below sets out the carrying amounts of financial assets and financial liabilities as at 31 December 2016:

AMD'000	Trading	Loans and receivables	Available-for- sale	Other amortised cost	Total carrying amount
Cash and cash equivalents	-	54,076,716	-	-	54,076,716
Financial instruments at fair value through profit or loss	922,745	-	-	-	922,745
Available-for-sale financial assets	-	-	24,773,867	-	24,773,867
Loans and advances to banks	-	6,238,794	-	-	6,238,794
Loans to customers	-	119,590,354	-	-	119,590,354
Other financial assets	-	4,871,307	-	-	4,871,307
Total financial assets	922,745	184,777,171	24,773,867	-	210,473,783
Deposits and balances from banks	-	-	-	11,595,885	11,595,885
Current accounts and deposits from customers	-	-	-	149,832,833	149,832,833
Other financial liabilities	2,328	-	-	4,704,496	4,706,824
Total financial liabilities	2,328	-	-	166,133,214	166,135,542

32 Financial assets and liabilities: fair values and accounting classifications (continued)

The table below sets out the carrying amounts of financial assets and financial liabilities as at 31 December 2015:

AMD'000	Trading	Loans and receivables	Available-for-sale	Other amortised cost	Total carrying amount
Cash and cash equivalents	-	73,286,515	-	-	73,286,515
Financial instruments at fair value through profit or loss	919,785	-	-	-	919,785
Available-for-sale financial assets	-	-	13,636,501	-	13,636,501
Loans and advances to banks	-	8,840,791	-	-	8,840,791
Loans to customers	-	161,206,360	-	-	161,206,360
Other financial assets	-	12,299,196	-	-	12,299,196
Total financial assets	919,785	255,632,862	13,636,501	-	270,189,148
Deposits and balances from banks	-	-	-	45,445,776	45,445,776
Current accounts and deposits from customers	-	-	-	160,484,839	160,484,839
Other financial liabilities	25,169	-	-	12,710,193	12,735,362
Total financial liabilities	25,169	-	-	218,640,808	218,665,977

(b) Fair values and fair value hierarchy

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

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

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

32 Financial assets and liabilities: fair values and accounting classifications (continued)

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

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

The estimated fair values of all financial instruments except for unquoted equity securities available-for-sale approximate their carrying values. As at 31 December 2016 fair value of unquoted equity securities available-for-sale with a carrying value of AMD 32,032 thousand (2015: AMD 32,056 thousand) cannot be determined.

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

- discount rates of 5.7% (31 December 2015: 6.3%-9.6%) and 7.6%-14.4% (31 December 2015: 8.2%-16.2%) are used for discounting future cash flows from loans and advances to banks and loans to customers, respectively; discount rates of 1.1% - 11.5% (31 December 2015: 0.9%-10.4%) are used for discounting future cash flows for liabilities;
- the fair value of variable rate instruments is not materially different from carrying amount;
- the fair value of government bonds is estimated based on government bonds yield curve.

The table below analyses financial instruments measured at fair value for the years ended 31 December 2016 and 2015, by the level in the fair value hierarchy into which the fair value measurement is categorised:

	2016	2015
AMD'000	Level 2	Level 2
Financial instruments at fair value through profit or loss		
- Government treasury bills	636,930	671,693
- Derivative assets	285,815	248,092
- Derivative liabilities	(2,328)	(25,169)
Available-for-sale financial assets		
- Government treasury bills	24,028,968	12,567,002
- Corporate bonds	712,867	1,037,443

The following table analyses the fair value of financial instruments not measured at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised as at 31 December 2016:

32 Financial assets and liabilities: fair values and accounting classifications (continued)

AMD'000	Level 2	Level 3	Total fair values	Total carrying amount
ASSETS				
Cash and cash equivalents	54,076,716	-	54,076,716	54,076,716
Loans to banks	6,238,794	-	6,238,794	6,238,794
Loans to customers	-	119,590,354	119,590,354	119,590,354
Other financial assets	-	4,871,307	4,871,307	4,871,307
LIABILITIES				
Deposits and balances from banks	11,595,885	-	11,595,885	11,595,885
Current accounts and deposits from customers	67,176,807	82,656,026	149,832,833	149,832,833
Other financial liabilities	-	4,706,824	4,706,824	4,706,824

The following table analyses the fair value of financial instruments not measured at fair value, by the level in the fair value hierarchy into which each fair value measurement is categorised as at 31 December 2015:

AMD'000	Level 2	Level 3	Total fair values	Total carrying amount
ASSETS				
Cash and cash equivalents	73,286,515	-	73,286,515	73,286,515
Loans to banks	8,840,791	-	8,840,791	8,840,791
Loans to customers	1,853,283	159,353,077	161,206,360	161,206,360
Other financial assets	-	12,299,196	12,299,196	12,299,196
LIABILITIES				
Deposits and balances from banks	45,445,776	-	45,445,776	45,445,776
Current accounts and deposits from customers	79,265,095	81,219,744	160,484,839	160,484,839
Other financial liabilities	-	12,735,362	12,735,362	12,735,362

Management believes that the fair values of loans to customers as at 31 December 2016 and 31 December 2015 approximates its carrying values as the majority of loans to customers are at floating rates.

33 Events after the end of the reporting period

There were no events after the reporting period that may require adjustment of or disclosure in the Bank's financial statements for the year ended 31 December 2016.

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