BANK MELLI IRAN BAKU BRANCH

The International Financial Reporting Standards
Financial Statements and
Independent Auditors' Report
For the Year Ended December 31, 2017

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2017

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the independent auditors' report set out on pages 2 and 3, is made with a view to distinguishing the respective responsibilities of the management and those of the independent auditors in relation to the financial statements of Bank Melli Iran Baku Branch ("Bank").

Management is responsible for the preparation of the financial statements that present fairly the financial position of the Bank as at December 31, 2017, the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

In preparing the financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating weather IFRS have been followed, subject to any material departures disclosed and explained in the financial statements; and
- Preparing the financial statements on a going concern basis, unless it is inappropriate to presume that the Bank will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Bank;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Bank, and which enable them to ensure that the financial statements of the Bank comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Bank; and
- Detecting and preventing fraud, errors and other irregularities.

The financial statements for the year ended December 31, 2017 were authorized for issue on March 2, 2018 by the Management of the Bank.

On behalf of the Management Board:

BANK MELLI IRAN BAKI FILIALI BAKU BRANCH BANK MELLI IRAN

Najafimarganmaskan Asghar Khalil	**Mirheydarov Vugar Mirfazil**
Deputy Branch Manager	**Chief Accountant**
March 2, 2018	March 2, 2018
Baku, the Republic of Azerbaijan	Baku, the Republic of Azerbaijan

INDEPENDENT AUDITORS' REPORT

To the Shareholders and the Board of Management of Bank Melli Iran Baku Branch:

Opinion

We have audited the financial statements of Bank Melli Iran Baku Branch ("Bank"), which comprise the statement of financial position as at December 31, 2017, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

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

Emphasis of matter

We draw your attention to Note 11- Other Assets which is integral part of financial statements. That note describes Recognition and Measurement of receivable from governmental organization for court claim. Our opinion is not qualified in respect of this matter.

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 have no realistic alternative but to do so.

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

Auditors' 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 auditors' 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 skepticism throughout the audit. We also:

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control;
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management;
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' 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 auditors' 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.

Nexia EA LLC

NEXIA EA

March 2, 2018
Baku, the Republic of Azerbaijan

BANK MELLI IRAN BAKU BRANCH

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 31, 2017
(In Azerbaijani Manats)

	Notes	December 31, 2017	December 31, 2016
ASSETS			
Cash and current placements with other banks	6	52,271,679	35,127,191
Due from banks and other financial institutions	7	2,476,426	3,659,374
Loans to customers	8	3,355,298	7,161,773
Investment securities held to maturity	9	18,347,899	12,436,730
Premises and equipment	10	3,608,285	3,708,168
Intangible assets	10	50,198	38,083
Other assets	11	20,387,890	18,336,271
TOTAL ASSETS		**100,497,675**	**80,467,590**
LIABILITIES			
Due to banks and other financial institutions	12	28,153,414	55,092,450
Customer accounts	13	2,661,778	2,359,310
Deferred tax liabilities	21	285,445	30,025
Other liabilities	14	112,127	1,079,211
Subordinated debt	15	18,276,300	-
TOTAL LIABILITIES		**49,489,064**	**58,560,996**
EQUITY			
Share capital	16	73,611,171	51,433,671
Revaluation surplus		12,036	17,403
Accumulated deficit		(22,614,596)	(29,544,480)
TOTAL EQUITY		**51,008,611**	**21,906,594**
TOTAL EQUITY AND LIABILITIES		**100,497,675**	**80,467,590**

On behalf of the Management Board:

BANK MELLI IRAN BAKU BRANCH

Najafimarganmaskan Asghar Khalil
Deputy Branch Manager

March 2, 2018
Baku, the Republic of Azerbaijan

Mirheydarov Vugar Mirfazil
Chief Accountant

March 2, 2018
Baku, the Republic of Azerbaijan

The notes on pages 9-46 form an integral part of these financial statements.

BANK MELLI IRAN BAKU BRANCH

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER 31, 2017

(In Azerbaijani Manats)

	Notes	Year ended December 31, 2017	Year ended December 31, 2016
Interest income	17	2,970,943	3,260,948
Interest expense	17	(53,702)	(43,736)
Net interest income		**2,917,241**	**3,217,212**
Reversal of provision / (Provision for impairment), net		1,676,394	(30,895,622)
Reversal of accrued interest expense	12	4,073,158	-
Net interest profit/(loss) after provision for loan impairment		**8,666,793**	**(27,678,410)**
Gain from operations in foreign currencies - less losses	18	208,960	363,993
Fee and commission income	19	199,077	135,382
Fee and commission expense	19	(67,655)	(44,298)
Realized loss on trade securities designated at fair value through profit or loss		-	(8,395)
Other income		3,567	1,776
Operating income/(loss)		**9,010,742**	**(27,229,952)**
Operating expenses	20	(1,830,806)	(2,042,207)
Profit before income tax		**7,179,936**	**(29,272,159)**
Income tax (expenses) / benefit	21	(256,761)	1,667
NET PROFIT/(LOSS) FOR THE YEAR		**6,923,175**	**(29,270,492)**
Transferring revaluation surplus to retained earnings		-	6,709
Net changes in retained earnings		**6,923,175**	**(29,263,783)**
Comprehensive income			
Gains on property revaluation		-	-
Income tax benefit relating to components of other comprehensive income		1,342	1,342
Other comprehensive income for the year		**1,342**	**1,342**
Transferring revaluation surplus to retained earnings		-	(6,709)
Net changes in other reserves		**1,342**	**(5,367)**
TOTAL COMPREHENSIVE INCOME / (LOSS) FOR THE YEAR		**6,924,517**	**(29,269,150)**

On behalf of the Management Board:

Najafimarganmaskan Asghar Khalil

Deputy Branch Manager

March 2, 2018

Baku, the Republic of Azerbaijan

Mirheydarov Vugar Mirfazil

Chief Accountant

March 2, 2018

Baku, the Republic of Azerbaijan

The notes on pages 9-46 form an integral part of these financial statements.

BANK MELLI IRAN BAKU BRANCH

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2017
(In Azerbaijani Manats)

	Share Capital	Accumulated deficit	Other Reserves	Total Equity
Balance at December 31, 2015	**51,433,671**	**(280,697)**	**22,770**	**51,175,744**
Net loss for the year	-	(29,270,492)	-	**(29,270,492)**
Other comprehensive income	-	-	1,342	**1,342**
Transfer of revaluation surplus	-	6,709	(6,709)	-
Balance at December 31, 2016	**51,433,671**	**(29,544,480)**	**17,403**	**21,906,594**
Net profit for the year	-	6,923,175	-	**6,923,175**
Other comprehensive income	-	-	1,342	**1,342**
Additional capital contribution	22,177,500	-	-	**22,177,500**
Transfer of revaluation surplus	-	6,709	(6,709)	-
Balance at December 31, 2017	**73,611,171**	**(22,614,596)**	**12,036**	**51,008,611**

On behalf of the Management Board:

Najafimarganmaskan Asghar Khalil
Deputy Branch Manager

March 2, 2018
Baku, the Republic of Azerbaijan

Mirheydarov Vugar Mirfazil
Chief Accountant

March 2, 2018
Baku, the Republic of Azerbaijan

The notes on pages 9-46 form an integral part of these financial statements.

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2017
(In Azerbaijani Manats)

	Notes	Year ended December 31, 2017	Year ended December 31, 2016
CASH FLOW FROM OPERATING ACTIVITIES			
Profit/(loss) before income tax		7,179,936	(29,272,159)
Adjustments for:			
Provision expense		(5,749,552)	30,895,622
Amortisation and depreciation expense		117,225	116,546
Translation gain on foreign exchange operations		44,702	(425,189)
Cash flow from operating activities before changes in operating assets and liabilities		**1,592,311**	**1,314,820**
(Increase)/decrease in operating assets:			
Due from banks and other financial institutions		903,438	7,382,636
Loans to customers		4,347,607	2,719,464
Financial assets held for trading		-	5,419,218
Investment securities		(5,911,548)	(12,436,730)
Other assets		(154,727)	292,683
Increase/(decrease) in operating liabilities:			
Due to banks and other financial institutions		(1,444,059)	2,290,942
Subordinated debt		17,556,300	-
Customer accounts		366,345	(594,882)
Other liabilities		(937,417)	1,031,756
Cash inflow from operating activities before taxation:		**16,318,250**	**7,419,907**
Income tax paid		-	-
Net cash generated from operating activities		**16,318,250**	**7,419,907**
CASH FLOW FROM INVESTING ACTIVITIES			
Purchase of premises and equipment		(10,957)	(24,227)
Purchase of intangible assets		(18,500)	(10,050)
Net cash used in investing activities		**(29,457)**	**(34,277)**
CASH FLOW FROM FINANCING ACTIVITIES			
Increase of share capital		-	-
Net cash used in financing activities		**-**	**-**

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2017
(In Azerbaijani Manats)

Effect of changes in foreign exchange rates on cash and cash equivalents		855,695	2,019,628
NET INCREASE IN CASH AND CASH EQUIVALENTS		**17,144,488**	**9,405,258**
CASH AND CASH EQUIVALENTS, beginning of the year	6	**35,127,191**	**25,721,933**
CASH AND CASH EQUIVALENTS, end of the year	6	**52,271,679**	**35,127,191**

On behalf of the Management Board:

Najafimarganmaskan Asghar Khalil
Deputy Branch Manager

March 2, 2018
Baku, the Republic of Azerbaijan

Mirheydarov Vugar Mirfazil
Chief Accountant

March 2, 2018
Baku, the Republic of Azerbaijan

The notes on pages 9-46 form an integral part of these financial statements.

1 INTRODUCTION

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended December 31, 2017 for Bank Melli Iran Baku Branch (the "Bank"), which was incorporated in Azerbaijan in 1993. The Bank's principal business activity is commercial and retail banking operations.

Basic activities.The Bank's primary business consists of bank services for legal and individual persons. The Bank is regulated by the Central Bank of the Republic of Azerbaijan (the "CBAR") and conducts its business under general license number 124.

As at December 31, 2017, the following shareholders owned the issued shares of the Bank:

Shareholders	**Country**	**December 31, 2017** %	**December 31, 2016** %
"Bank Melli Iran"	Iran Islamic Republic	100	100

Registered address and place of business. The Bank's registered address is:

Nobel ave. 23, AZ 1025, Baku, the Republic of Azerbaijan

Presentation currency. These financial statements are presented in Azerbaijani Manats ("AZN"). The Azerbaijani Manat ("AZN") is the official currency of Republic of Azerbaijan.

2 OPERATING ENVIRONMENT OF THE BANK

The Republic of Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks towards the market economy. The future stability of Azerbaijan's economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

Major indicators of the Azerbaijan economy were influenced by a number of negative factors. Considering significant drop in crude oil prices starting from the second half of 2014, there continues to be uncertainty regarding the economic growth, access to capital and cost of capital in the Republic of Azerbaijan, because Azerbaijan produces and exports large volumes of oil and gas, its economy is particularly dependent on the price of oil and gas. Economic growth slowed down in 2014 and 2015 approximately 2% and 1.1%, respectively and turned negative 3% in 2016. These factors aggravated the economic slowdown to shift from prosperity to recession economy with high inflation and unemployment and decreasing GDP.

The future economic direction of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory and political developments. The Management is unable to predict, all developments in the economic environment which would have an impact on the Bank's operations and consequently what effect, if any, they could have on the financial position of the Bank.

Decreasing revenues from oil exports made the CBAR abandon its peg policy to the basket of US dollars and euros. In addition, CBAR devalued the Azerbaijani Manat by approximately 34% on 21 February 2015 and further on 21 December 2015 introduced a floating exchange rate that resulted in one-time devaluation of the AZN against US dollars and other major currencies by approximately 48%. The devaluation of Azerbaijani Manat continued in 2016 and resulted in 14% fall against US dollars and 9% fall against Euro by 31 December 2016. During 2017 there was no any significant changes in foreign currency rates. In January 2016, Standard & Poor's, international credit agency, downgraded long-term and short-term foreign and national currency sovereign rating to the speculative level. Starting from February, 2016 the CBAR has gradually increased refinancing rate from 3% to 15% and the minimum capital adequacy ratio was lowered from 12% to 10%. In addition, CBAR prevented speculations in the currency market by setting a limit on the currency exchange rate corridor within 4% of the official rate which was revoked in 2017 and introduced limits on the amount of foreign currency exchange.

Amidst the ongoing crisis, the government of Azerbaijan shifted its oil-oriented economic policy, dominated for two decades, to the diversification of the economy. For that purpose, a "national strategic roadmap" was adopted to formulate a correct development strategy. The implementation of the "national strategic roadmap" was assigned to the newly formed "Center for Analysis of Economic Reforms and Communications", the aim of which is analyzing the effectiveness of conducted reforms and making new proposals. Another important structural reform was the establishment of the "Financial Market Supervisory Authority" to reinforce more strict, transparent and flexible control over the financial sector by improving the regulation and fighting against illegal financial activities.

Significant measures have been taken in custom services and taxation as well. As of 1 August, 2016, new regulations to ensure more operative and transparent custom clearance (a "green corridor" and other access systems) were implemented. The new simplified procedures will stimulate imports and will provide favorable conditions for business and external trade. As a continuation of reforms in customs, the reception of e-declarations to avoid the "official-citizen contact" is being carried out. In order to amend the existing tax system, the decree approving the "Directions of Reforms in Taxation for 2016" was signed. The presidential decree requires the Ministry of Taxes to ensure that on-site and off-tax audits are performed within short periods of time and extend the coverage of electronic tax audits to limit face-to-face contacts with taxpayers. Another important amendment on monopolistic actions was made to the Criminal Code. Besides, the latest changes in December 2016 to Taxes Code there will be applied "transfer pricing" against artificially exaggerated expenses and "voluntary tax disclosure" which highly practicable in greatest economies. Furthermore, in order to prevent additional exposure of financial sanctions by tax authority because of wrongly calculated tax liability, the mechanism of "determination of tax liability in advance" will be activated. Along with them, implementation of electronic invoices will play an important role in prevention of tax evasion and will impact on positively on tax system optimization. Banks, acting as tax agents, are obliged to assess and to remit 18% VAT to the State Budget at the expense of funds being transferred by the person, not registered with the Azerbaijani tax authorities, being a buyer of e-commerce works or services from non-residents having no VAT registration in the Republic of Azerbaijan, as well as by the person, not registered with the tax authorities, being a participant of online lotteries, online contests and online competitions organized outside of the Republic of Azerbaijan. Supply of non-performing (toxic) assets by banks, which have become insolvent, within the framework of restructuring and bailout measures is exempt from VAT until January 1, 2020. The toxic assets supply rules are yet to be set forth by the Financial Market Supervisory Authority. Amendments made to the Tax Code now require banks operating in the Republic of Azerbaijan and the national postal service operator to withhold simplified tax at a rate of 1% on withdrawals of cash by legal entities and individual entrepreneurs. The tax must be remitted to the State Budget and reported by the entity withholding it no later than the 20th of the following month.

It is expected that recession to be short-lived, recovering to economic growth in 2017, partly due to positive effects of investments in gas projects. It is expected the GDP will grow 1.4% and the non-oil sector about 2.4%. Over the long term, Azerbaijan will benefit from production from the new gas fields, which is expected to come online in 2018.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation. These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention. The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Financial statements prepared in compliance with the requirements of the Azerbaijan Republic law and financial markets Supervision Chamber. There was no significant difference between financial statements prepared in accordance with local accounting requirements and International Financial Reporting Standards.

The existing differences mainly are arises due to following:

- Accrued interest income in IFRS financial statements classified as Loans to customers, in prudential reports as other assets.
- In IFRS financial statements ordinary reserves are deducted from assets, but in prudential report classified as ordinary reserves under capital section.

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

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair value is the current bid price for financial assets and current asking price for financial liabilities which are quoted in an active market. For assets and liabilities with offsetting market risks, the Bank may use mid-market prices as a basis for establishing fair values for the offsetting risk positions and apply the bid or asking price to the net open position as appropriate.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange or other institution and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Valuation techniques such as discounted cash flows models or models based on recent arms length transactions or consideration of financial data of the investees are used to fair value certain financial instruments for which external market pricing information is not available.

Valuation techniques may require assumptions not supported by observable market data. Disclosures are made in these financial statements if changing any such assumptions to a reasonably possible alternative would result in significantly different profit, income, total assets or total liabilities.

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

Amortized cost is the amount at which the financial instrument was recognized at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortization of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortized discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related balance sheet items.

The effective interest method is a method of allocating interest income or interest expense over the relevant period so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest reprising date except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortized over the whole expected life of the instrument.

The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate (refer to income and expense recognition policy).

Initial recognition of financial instruments. Trading securities, derivatives and other financial instruments at fair value through profit or loss are initially recorded at fair value. All other financial instruments are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Bank commits to deliver a financial asset. All other purchases are recognized when the entity becomes a party to the contractual provisions of the instrument. Following their initial recognition, the financial assets and financial liabilities are subsequently measured at amortized cost using the effective interest rate method.

Derecognition of financial assets. The Bank derecognizes financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control.

Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

Cash and cash equivalents. Cash and cash equivalents are items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Funds restricted for a period of more than three months on origination are excluded from cash and cash equivalents. Cash and cash equivalents are carried at amortized cost.

Mandatory cash balances with the CBAR. Mandatory cash balances in AZN and foreign currency held with the CBAR are carried at amortized cost and represent non-interest bearing mandatory reserve deposits, which are not available to finance the Bank's day-to-day operations.

Due from other banks. Amounts due from other banks are recorded when the Bank advances cash and cash equivalents to counterparty banks with no intention of trading the resulting unquoted non-derivative receivable due on fixed or determinable dates and the Bank has no intention of trading unquoted non-derivative receivables. Amounts due from other banks are carried at amortized cost.

Loans and advances to customers. Loans and advances to customers are recorded when the Bank advances money to purchase or originate an unquoted non-derivative receivable from a customer due on fixed or determinable dates and has no intention of trading the receivable. Loans and advances to customers are carried at amortized cost.

Impairment of financial assets carried at amortized cost. Impairment losses are recognized in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of the financial asset and which have an impact on the amount or timing of the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

If the Bank determines that no objective evidence exists that impairment was incurred for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. The primary factors that the Bank considers whether a financial asset is impaired is its overdue status and reliability of related collateral, if any.

The following other principal criteria are also used to determine that there is objective evidence that an impairment loss has occurred:

- Any installment is overdue and the late payment cannot be attributed to a delay caused by the settlement systems;
- The borrower experiences a significant financial difficulty as evidenced by the borrower's financial information that the Bank obtains;
- The borrower considers bankruptcy or a financial reorganization;
- There is an adverse change in the payment status of the borrower as a result of changes in the national or local economic conditions that impact the borrower; or
- The value of collateral significantly decreases as a result of deteriorating market conditions.

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 the terms of an impaired financial asset held at amortized cost are renegotiated or otherwise modified because of financial difficulties of the borrower or issuer, impairment is measured using the original effective interest rate before the modification of terms.

Impairment losses are always recognized through an allowance account to write down the asset's carrying amount to the present value of expected cash flows (which exclude future credit losses that have not been incurred) discounted at the original effective interest rate of the asset. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

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

Uncollectible assets are written off against the related impairment loss provision after all the necessary procedures to recover the asset have been completed and the amount of the loss has been determined.

Credit related commitments. The Bank enters into credit related commitments, including letters of credit and financial guarantees. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognized at their fair value, which is normally evidenced by the amount of fees received. This amount is amortized on a straight line basis over the life of the commitment, except for commitments to originate loans if it is probable that the Bank will enter into a specific lending arrangement and does not expect to sell the resulting loan shortly after origination; such loan commitment fees are deferred and included in the carrying value of the loan on initial recognition. At each balance sheet date, the commitments are measured at the higher of (i) the remaining unamortized balance of the amount at initial recognition and (ii) the best estimate of expenditure required settling the commitment at the balance sheet date.

Premises and equipment. Premises are stated at revalued amounts, as described below, less accumulated depreciation and provision for impairment, where required. All other items of premises and equipment are stated at cost less accumulated depreciation and impairment losses, if any.

The costs of minor repairs and maintenance are expensed when incurred. The cost of replacing major parts or components of premises and equipment items are capitalized and the replaced part is retired.

If impaired, premises and equipment are written down to the higher of their value in use and fair value less costs to sell. The decrease in carrying amount is charged to profit or loss to the extent it exceeds the previous revaluation surplus in equity. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognized as profit or loss from disposal of fixed assets.

Depreciation. Depreciation on other items of premises and equipment is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives as follows:

Premises	2%
Computers and communication equipment	20%
Furniture, fixtures and othe	20%
Vehicles	15%
Other fixed assets	20%

The residual value of an asset is the estimated amount that the Bank would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.The residual value of an asset is nil if the Bank expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Intangible assets. All of the Bank's intangible assets have definite useful life and primarily include capitalized computer software.

Acquired computer software licenses are capitalized based on the costs incurred to acquire and bring to use the specific software. Development costs that are directly associated with identifiable and unique software controlled by the Bank are recorded as intangible assets if the inflow of incremental economic benefits exceeding costs is probable. Capitalized costs include staff costs of the software development team and an appropriate portion of relevant overheads. All other costs associated with computer software, e.g. its maintenance, are expensed when incurred. Capitalized computer software is amortized on a straight line basis over expected useful lives of 10 years.

Due to other banks. Amounts due to other banks are recorded when money or other assets are advanced to the Bank by counterparty banks. The non-derivative liability is carried at amortized cost.

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

Customer accounts. Customer accounts are non-derivative liabilities to individuals, state or corporate customers and are carried at amortized cost.

Other borrowed funds. Other borrowed funds include loans from resident and non-resident financial institutions with fixed maturities and fixed or floating interest rates. Term borrowings are carried at amortised cost.

Subordinated debt. Subordinated debt includes long-term non-derivative liabilities to Bank Melli Iran Head Office and is carried at amortised cost. Debt is classified as subordinated debt when its repayment debt ranks after all other creditors in case of liquidation. Subordinated debt is included in "Tier 2 capital" of the Bank.

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

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

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

In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit.Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilized. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available, against which the deductions can be utilized.

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

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

When loans and other debt instruments become doubtful of collection, they are written down to the present value of expected cash inflows and interest income is thereafter recorded for the unwinding of the present value discount based on the asset’s effective interest rate which was used to measure the impairment loss. All other fees, commissions and other income and expense items are generally recorded on an accrual basis by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Foreign currency translation. Institutions of the Bank's functional currency of the primary economic environment in which the entity is the currency. The Bank’s functional and presentation currency is the national currency of the Republic of Azerbaijan, Azerbaijani Manats (“AZN”).

Monetary assets and liabilities are translated into entity’s functional currency at the official exchange rate of the CBAR at the respective balance sheet dates. Foreign exchange gains and losses resulting from the settlement of transactions and from the translation of monetary assets and liabilities into Bank’s functional currency at year-end official exchange rates of the CBAR are recognized in profit or loss. Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

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

	December 31, 2017	December 31, 2016
USD/AZN	1.7001	1.7707
EUR/AZN	2.0307	1.8644

Offsetting. Financial assets and liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognized amounts, and there is an intention to either settle on a net basis, or to realize the asset and settle the liability simultaneously.

Earnings per share. Preference shares are not redeemable and are considered to be participating shares. Earnings per share is determined by dividing the profit or loss attributable to owners of the Bank by the weighted average number of participating shares outstanding during the reporting year.

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

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES

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

Impairment losses on loans and advances. The Bank regularly reviews its loan portfolios to assess impairment. In determining whether an impairment loss should be recorded in the statement of comprehensive income the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group.

Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Initial recognition of related party transactions. In the normal course of business the Bank enters into transactions with its related parties. IAS 39 requires initial recognition of financial instruments based on their fair values. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analysis. Terms and conditions of related party balances are disclosed in Note 27.

Tax legislation. Azerbaijani tax, currency and customs legislation is subject to varying interpretations.

5 STANDARDS AND INTERPRETATIONS ISSUED AND NOT YET ADOPTED

At the date of authorization of these financial statements, other than the Standards and Interpretations adopted by the Bank in advance of their effective dates, the following Interpretations were in issue but not yet effective.

Annual Improvements to IFRS Standards 2014–2016 Cycle contains amendments to three International Financial Reporting Standards (IFRSs) as result of the IASB's annual improvements project.

Standard	Subject of amendment
IFRS 1 "First-time Adoption of International Financial Reporting Standards"	Deletion of short-term exemptions for the first-time adopters: The amendments delete the short-term exemptions in IFRS 1 that relate to IFRS 7, IAS 19, IFRS 12 and IAS 27
IFRS 12 "Disclosure of Interests in Other Entities"	Clarification of the scope of the Standard: IFRS 12 states that an entity need not provide summarised financial information for interests in subsidiaries, associates or joint ventures that are classified as held for sale. The amendment clarifies that this is the only concession from disclosure requirements of IFRS 12 for such interests.
IAS 28 "Investments in Associates and Joint Ventures"	Measuring an associate or joint venture at fair value: The amendments clarify that the election to measure at fair value through profit or loss an investment in an associate or a joint venture that is held by an entity that is a venture capital organisation, or other qualifying entity, is available for each investment in an associate or joint venture on an investment-by-investment basis, upon initial recognition.

The amendments to IFRS 1 and IAS 28 are effective for annual periods begin on or after January 1 2018.

The IASB and FASB have issued their joint revenue recognition standard, IFRS 15 "Revenue from Contracts with Customers", which replaces all existing IFRS and US GAAP revenue requirements. IFRS 15 specifies how and when an IFRS reporter will recognize revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard provides a single, principles based five-step model to be applied to all contracts with customers. IFRS 15 was issued in May 2014 and applies to an annual reporting period beginning on or after January 1, 2018. Earlier application is permitted.

Amendments to IAS 40 "Transfers of Investment Property" are intended to clarify that an entity can only reclassify a property to/from investment property when, and only when, there is evidence that a change in the use of the property occurred.The amendments are effective for periods beginning on or after January 1, 2018. Earlier application is permitted. An entity applies the amendments to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. Retrospective application is also permitted if that is possible without the use of hindsight.

IFRIC 22 "Foreign Currency Transactions and Advance Consideration" addresses foreign currency transactions or parts of transactions where:

- there is consideration that is denominated or priced in a foreign currency;
- the entity recognizes a prepayment asset or a deferred income liability in respect of that consideration, in advance of the recognition of the related asset, expense or income; and
- the prepayment asset or deferred income liability is non-monetary.

The Interpretations Committee came to the following conclusion that the date of the transaction, for the purpose of determining the exchange rate, is the date of initial recognition of the non-monetary prepayment asset or deferred income liability. If there are multiple payments or receipts in advance, a date of transaction is established for each payment or receipt. The interpretation applies to annual reporting periods beginning or after January 1, 2018. Earlier adoption is permitted.

IFRS 9 "Financial Instruments" issued in November 2009 and amended in October 2010 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for de-recognition.

- IFRS 9 requires all recognized financial assets that are within the scope of IAS 39 "Financial Instruments: Recognition and Measurement" to be subsequently measured at amortized cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair values at the end of subsequent accounting periods;
- The most significant effect of IFRS 9 regarding the classification and measurement of financial liabilities relates to the accounting for changes in fair value of a financial liability (designated as at fair value through profit or loss) attributable to changes in the credit risk of that liability. Specifically, under IFRS 9, for financial liabilities that are designated as at fair value through profit or loss, the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is recognized in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit and loss accounts. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit and loss accounts. Previously, under IAS 39, the entire amount of the change in the fair value of the financial liability designated as at fair value through profit and loss accounts was recognized in profit and loss accounts.

IFRS 9 is effective for annual periods beginning on or after January 1, 2018.

Amendments to IFRS 2 "Share-Based Payment" – The IASB have published final amendments to IFRS 2 "Share-based Payment" that clarify the classification and measurement of share-based payment transactions. Classification and Measurement of Share-based Payment Transactions contains the following clarifications and amendments:

Accounting for cash-settled share-based payment transactions that include a performance condition

Until issue of these amendments, IFRS 2 contained no guidance on how vesting conditions affect the fair value of liabilities for cash-settled share-based payments. IASB has now added guidance that introduces accounting requirements for cash-settled share-based payments that follows the same approach as used for equity-settled share-based payments.

Classification of share-based payment transactions with net settlement features

The IASB has introduced an exception into IFRS 2 so that a share-based payment where the entity settles the share-based payment arrangement net is classified as equity-settled in its entirety provided the share-based payment would have been classified as equity-settled had it not included the net settlement feature.

Accounting for modifications of share-based payment transactions from cash-settled to equity-settled

Until issue of these amendments, IFRS 2 did not specifically address situations where a cash-settled share-based payment changes to an equity-settled share-based payment because of modifications of the terms and conditions. The IASB has introduced the following clarifications:

- On such modifications, the original liability recognized in respect of the cash-settled share-based payment is derecognized and the equity-settled share-based payment is recognized at the modification date fair value to the extent services have been rendered up to the modification date;
- Any difference between the carrying amount of the liability as at the modification date and the amount recognized in equity at the same date would be recognized in profit and loss immediately.

The amendments are effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted.

IFRS 16 "Leases", which specifies how and IFRS reporter will recognise, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17.

IFRS 16 was issued in January 13, 2016 and applies to an annual reporting period beginning on or after January 1, 2019.

The Management is considering the implications of these standards, their impact on the financial statements and the timing of its adoption by the Bank.

6 CASH AND CURRENT PLACEMENTS WITH OTHER BANKS

	December 31, 2017	December 31, 2016
Cash on hand	1,391,222	2,360,808
Cash balances with the CBAR	25,398,018	19,251,876
Correspondent accounts and overnight placements with other banks:		
- The Republic of Azerbaijan	7,362	518,122
- Other countries	25,732,401	13,132,864
Less: provision for imapirment	(257,324)	(136,479)
Total cash and current placements with other banks	**52,271,679**	**35,127,191**

The analysis by credit quality of cash and current placements with other banks at December 31, 2017 is as follows:

	Cash on hand	Cash balances with the CBAR	Correspondent accounts and overnight placements with other banks	Total
Current and not impaired				
- Cash on hand	1,391,222	-	-	**1,391,222**
- The Republic of Azerbaijan	-	25,398,018	7,320	**25,405,338**
- Other countries	-	-	25,475,119	**25,475,119**
Total current and not impaired	**1,391,222**	**25,398,018**	**25,482,439**	**52,271,679**
Total cash and current placements with other banks	**1,391,222**	**25,398,018**	**25,482,439**	**52,271,679**

The analysis by credit quality of cash and current placements with other banks at December 31, 2016 is as follows:

	Cash on hand	Cash balances with the CBAR	Correspondent accounts and overnight placements with other banks	Total
Current and not impaired				
- Cash on hand	2,360,808	-	-	**2,360,808**
- The Republic of Azerbaijan	-	19,251,876	512,972	**19,764,848**
- Other countries	-	-	13,001,535	**13,001,535**
Total current and not impaired	**2,360,808**	**19,251,876**	**13,514,507**	**35,127,191**
Total cash and current placements with other banks	**2,360,808**	**19,251,876**	**13,514,507**	**35,127,191**

7 DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

	December 31, 2017	December 31, 2016
Short-term deposits in Resident banks	14,202,420	17,894,769
Short-term deposits in non-Resident banks	-	934,556
Less: provision for imapirment	(11,725,994)	(15,169,951)
Total due from banks and other financial institutions	**2,476,426**	**3,659,374**

The balance values of the amounts due from banks as of December 31, 2017 and December 31, 2016 approximate their fair values. The approximate fair value of the amounts due from banks as of December, 31 2017 is AZN 2,476,426 (2016: AZN 3,659,374).

During 2017 the Bank has not placed any deposits.

Other deposits placed in the previous years:

In 2016, the Bank placed a deposit in the amount of EUR 500,000 in Mir Business Bank at an annual interest rate of 1.0 % for a period of 6 months. During 2017 deposit fully recovered by Bank.

In 2015, the Bank placed two deposits in the total amount of AZN 5,000,000 in Texnikabank OJSC at an annual interest rate of 7.0 % for a period of 6 months. Later these deposits were prolonged to another six-month period.

In 2015, the Bank placed a deposit in the amount of AZN 1,000,000 in Texnikabank OJSC at an annual interest rate of 5.0 % for a period of 6 months.

As at 31 December 2017 total deposit in Texnikabank OJSC amounted to AZN 6,067,778 (AZN 6,000,000 principal and AZN 67,778 accrued interest).

In 2015, the Bank placed two deposits in the total amount of AZN 2,000,000 in Atrabank OJSC at an annual interest rate of 6.0 % for a period of 6 months. Later these deposits were prolonged to another six-month period. As at 31 December 2017 total deposit in AtraBank OJSC amounted to AZN 2,009,000 (AZN 2,000,000 principal and AZN 9,000 accrued interest).

As at December 31, 2017 amount in current accounts of Texnikabank OJSC and Atrabank OJSC represent AZN 11,478 and AZN 2,119,051 respectively (Texnikabank USD 431 and EUR 5,291 and Atrabank USD 513,261 and EUR 613,806).

The licenses of Texnikabank OJSC and Atrabank OJSC were cancelled by the CBAR in 2016. As at 31 December 2017 impairment loss provision against the deposits placed and current accounts with these banks amount to AZN 8,517,907 (2016:AZN7,345,732).

The Bank placed two deposits in the total amount of EUR 2,000,000 in Zaminbank OJSC at an annual interest rate of 5.0 % for a period of 6 months. Zaminbank's license was cancelled by the Central Bank of Azerbaijan in 2016. As at December 31, 2016, the Bank's provision for impairment against these deposits was amounting to 100%. Collateral for this deposit was different immovable properties. In December 2017, the bank acquired legal ownership over these properties and the properties has been evaluated and taken on the balance of Bank. The deposit was derecognized in profit and loss statement during 2017.

As at December 31, 2017, the Bank's term deposits with Royal Bank amount to AZN 3,998,288. Royal Bank provided collateral against these deposits which was valued at a market value of AZN 4,300,000 by an appraiser firm in June, 2013. As at December 31, 2017, the Bank's provision for impairment against these deposits amounts to 100% (2016: 100%).

The Bank placed deposits in the total amount of USD 12,500,000 in Birlikbank OJSC whose license cancelled by the Central Bank of Azerbaijan in 2011. Collateral for this deposit was 3rd floor of the AMAY shopping center with administrative offices with area of 13103 m2. In December 2016, the bank acquired legal ownership over this property and the property has been evaluated and taken on the balance of Bank. The deposit was derecognized in profit and loss statement during 2016.

8 LOANS TO CUSTOMERS

	December 31, 2017	December 31, 2016
Individuals	4,512,127	8,514,432
Legal entities	254,175	596,025
Loans to customers (gross)	**4,766,302**	**9,110,457**
Less - provision for impairment	(1,411,004)	(1,948,684)
Loans to customers (net)	**3,355,298**	**7,161,773**

Total loans to customers amount to AZN 3,355,298 at December 31, 2017 (December 31, 2016: AZN 7,161,773).

The movement in the provision for loan impairment during 2017 is as follows:

	Leagal entities	Individuals	Total
Provision for impairment at 1 January 2017	**147,206**	**1,801,478**	**1,948,684**
Provision for impairment during the year	-	-	**-**
Reversal of provision for impairment during the year	(86,686)	(445,962)	**(532,648)**
Amounts repaired/(written off) during the year	-	(5,032)	**(5,032)**
Provision for impairment at 31 December 2017	**60,520**	**1,350,484**	**1,411,004**

The movement in the provision for loan impairment during 2016 is as follows:

	Leagal entities	Individuals	Total
Provision for impairment at 1 January 2016	**7,348,652**	**1,582,862**	**8,931,514**
Provision for impairment during the year	80,920	388,102	**469,022**
Reversal of provision for impairment during the year	-	(59,280)	**(59,280)**
Amounts repaired/(written off) during the year	(7,282,366)	(110,206)	**(7,392,572)**
Provision for impairment at 31 December 2016	**147,206**	**1,801,478**	**1,948,684**

Economic sector risk concentrations within the loans to customers is as follows:

	December 31, 2017	December 31, 2016
Legal entities	254,175	596,025
Repair of Apartment	2,431,854	4,103,295
Trade and services	703,823	979,695
Consumer loans	802,014	1,626,784
Car purchase	474,778	1,731,063
Manufacturing	99,658	73,595
Total loans (gross)	**4,766,302**	**9,110,457**

The Bank applied the portfolio provisioning methodology prescribed by IAS 39, Financial Instruments: Recognition and Measurement, and created portfolio provisions for impairment losses that were incurred but have not been specifically identified with any individual loan by the balance sheet date. The Bank's policy is to classify each loan as 'current and not impaired' until a specific objective evidence of impairment of the loan is identified.

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

The main types of collateral obtained are as follows:
- residential real estate;
- movable property;
- deposits;
- and guarantor.

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

The carrying value of each class of loans and advances to customers approximates fair value at December 31, 2017 and December 31, 2016.

9 INVESTMENTS

As at December 31, 2017 and December 31, 2016 the Bank's balances of investment securities held to maturity are as follows:

	Interest to nominal %	December 31, 2017	Interest to nominal %	December 31, 2016
Ministry of Finance of RA - bonds no. IS0102025514	-	-	17.30	528,547
Ministry of Finance of RA - bonds no. AZ0102023519	-	-	16.00	525,627
Ministry of Finance of RA - bonds no. AZ0104021511	-	-	14.89	223,586
Ministry of Finance of RA - bonds no. AZ0102012512	-	-	10.80	1,025,459
Ministry of Finance of RA - bonds no. AZ0102009518	-	-	11.00	1,539,599

Ministry of Finance of RA - bonds no. IS0102005516	-	-	8.92	1,119,390
Ministry of Finance of RA - bonds no. IS0102005516	-	-	7.94	1,518,477
Ministry of Finance of RA - bonds no. IS0104013492	-	-	13.96	776,273
Ministry of Finance of RA - bonds no. IS0104010498	-	-	11.32	649,928
Ministry of Finance of RA - bonds no. IS0104010498	-	-	13.03	1,099,922
Ministry of Finance of RA - bonds no. IS0104010498	-	-	13.96	2,217,852
Cenral Bank of RA - notes no. 50100652S	-	-	14.57	1,212,070
Ministry of Finance of RA - bonds no. AZ0104001547	18.39	2,107,896	-	-
Ministry of Finance of RA - bonds no. AZ0105001553	15.00	200,859	-	-
Ministry of Finance of RA - bonds no. AZ0104007544	17.99	1,508,349	-	-
Ministry of Finance of RA - bonds no. AZ0104007544	16.32	2,287,214	-	-
Ministry of Finance of RA - bonds no. AZ0104007544	17.37	709,375	-	-
Ministry of Finance of RA - bonds no. AZ0104009540	17.90	134,770	-	-
Ministry of Finance of RA - bonds no. AZ0104009540	17.97	708,027	-	-
Ministry of Finance of RA - bonds no. AZ0104014540	13.50	989,464	-	-
Ministry of Finance of RA - bonds no. AZ0104014540	13.00	1,074,068	-	-
Ministry of Finance of RA - bonds no. AZ0104014540	13.41	408,651	-	-
Ministry of Finance of RA - bonds no. AZ0105006552	15.00	359,249	-	-
Ministry of Finance of RA - bonds no. AZ0104022543	9.98	725,374	-	-
Ministry of Finance of RA - bonds no. AZ0102023543	7.50	508,218	-	-
Ministry of Finance of RA - bonds no. AZ0105008558	15.00	202,059	-	-
Ministry of Finance of RA - bonds no. AZ0105003641	12.00	3,012,286	-	-
Ministry of Finance of RA - bonds no. AZ0102001630	11.00	1,814,001	-	-
Ministry of Finance of RA - bonds no. AZ0104002636	12.50	1,006,179	-	-
Cenral Bank of RA - notes no. 50100166S	10.01	67,026	-	-
Cenral Bank of RA - notes no. 50100166S	10.01	186,494	-	-
SOCAR - bonds no. AZ2001019895	5.00	338,340	-	-
Total investment securities held to maturity		**18,347,899**		**12,436,730**

10 PREMISES, EQUIPMENT AND INTANGIBLE ASSETS

	Premises	Furniture and Fixtures	Computers and Communication Equipment	Vehicles	Other fixed assets	Total Premises and Equipments	Software and Licences	Total
Balance as at January 1, 2016	**3,682,681**	**8,036**	**24,121**	**80,189**	**-**	**3,795,027**	**33,493**	**3,828,520**
Additions	-	21,235	2,992	-	-	**24,227**	10,050	**34,277**
Revaluation	-	-	-	-	-	**-**	-	**-**
Disposals/Sale	-	(17,363)	(910)	-	-	**(18,273)**	-	**(18,273)**
Depreciation/amortisation charge	(83,460)	(5,520)	(8,267)	(13,839)	-	**(111,086)**	(5,460)	**(116,546)**
Elimination of accumulated deprecation	-	17,363	910	-	-	**18,273**	-	**18,273**
Balance as at December 31, 2016	**3,599,221**	**23,751**	**18,846**	**66,350**	**-**	**3,708,168**	**38,083**	**3,746,251**
Additions	-	5,127	5,830	-	-	**10,957**	18,500	**29,457**
Revaluation	-	-	-	-	-	**-**	-	**-**
Disposals/Sale	-	(381)	(2,228)	-	-	**(2,609)**	-	**(2,609)**
Depreciation/amortisation charge	(83,460)	(7,068)	(6,473)	(13,839)	-	**(110,840)**	(6,385)	**(117,225)**
Elimination of accumulated deprecation	-	381	2,228	-	-	**2,609**	-	**2,609**
Balance as at December 31, 2017	**3,515,761**	**21,810**	**18,203**	**52,511**	**-**	**3,608,285**	**50,198**	**3,658,483**
Cost at December 31, 2016	4,173,009	457,251	143,244	89,410	18,097	**4,881,011**	148,879	**5,029,890**
Accumulated depreciation	(573,788)	(433,500)	(124,398)	(23,060)	(18,097)	**(1,172,843)**	(110,796)	**(1,283,639)**
Balance as at December 31, 2016	**3,599,221**	**23,751**	**18,846**	**66,350**	**-**	**3,708,168**	**38,083**	**3,746,251**
Cost at December 31, 2017	4,173,009	461,997	146,846	89,410	18,097	**4,889,359**	167,379	**5,056,738**
Accumulated depreciation	(657,248)	(440,187)	(128,643)	(36,899)	(18,097)	**(1,281,074)**	(117,181)	**(1,398,255)**
Balance as at December 31, 2017	**3,515,761**	**21,810**	**18,203**	**52,511**	**-**	**3,608,285**	**50,198**	**3,658,483**

11 OTHER ASSETS

	December 31, 2017	December 31, 2016
Sundry debtors	-	10,528
Receivable from governmental organizations for court claim	9,295,981	9,296,171
Total other financial assets	**9,295,981**	**9,306,699**
Immovables received in satisfaction of non-performing loans	10,912,895	8,993,708
Advances for different services	24,450	15,852
Deferred expenses	13,670	20,012
Tax receivable	140,894	-
Total other assets	**20,387,890**	**18,336,271**

In accordance with the decree of the Major of Baku dated November 18, 2014 on the construction of the new park, the Bank's building in the net book value of AZN 9,295,981 was dismantled. This fact amounted to receivable balances from unsettled regular-way trades. The parties cannot negotiate on the compensation. However, the Management of the Bank believes that their terms will apply.

The Bank did not make any impairment loss provision for receivable from Governmental Organization in accordance with IAS 39 - Financial Instruments: Recognition and Measurement. This matter is in court proceedings and final court decision to be expected in 2018. Bank will make appropriate adjustments to its financial statements based on the final court decision.

Currently, the Bank is taking action in order to receive the compensation for the damage. The case is heard at Baku Administrative-Economical Court No.1. The Bank claims the amount equal to the net book value of the building at the date of the dismantling, which is revalued value less accumulated depreciation. The building was revalued by an Independent Firm of Valuers on 3rd July, 2013. The basis used for the appraisal was the composition of the replacement cost, the discounted cash flow and the market value. The fair value of the building after valuation amounted to AZN 9,400,000.The building was previously pledged by Royal Bank as collateral for the deposit received from the Bank. The collateral was accrued to the Bank as a compensation for impairment loss provision based on the court decision in 2013 and was recognized as premises and equipment and measured at revalued amount at initial recognition.

As at December 31, 2017 and December 31, 2016 fair value of other assets amount to AZN 20,387,890 and AZN 18,336,271 respectively.

12 DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

	December 31, 2017	December 31, 2016
Melli Iran Bank Head Office	25,626,803	54,089,202
Export Development Bank of Iran	2,513,875	986,307
Correspondent accounts and overnight placements of other banks	9,849	14,927
Short-term amounts owed to other insurance companies	2,887	2,014
Total due to banks and other financial institutions	**28,153,414**	**55,092,450**

The balance amount of due to banks approximates their fair values as of December 31, 2017 and December 31, 2016. At December 31, 2017 the estimated fair value of due to banks and funds borrowed was AZN 28,153,414 (2016: AZN 55,092,450).

Due to Banks and funds borrowed consists of AZN 25,626,803 amount in 2017 (2016: AZN 54,089,202) which are blocked accounts and correspondent accounts of Bank Melli Iran Head Office in USD and EUR.

AZN 2,513,875 amount in 2017 (2016: AZN 986,307) consists of correspondent accounts of Export Development Bank of Iran in USD and EUR.

During 2017 interest expense accrual on Loan from Head office in the amount of AZN 4,073,158 (USD 2,295,772) was written down in accordance with agreement with head office and recognized in profit or loss statement for the year.

There were no any financial covenants with regard to these borrowings that the Bank should have complied with.

13 CUSTOMER ACCOUNTS

	December 31, 2017	December 31, 2016
State Owned Enterprises and Public Organizations	**228,050**	**181,098**
- Current Accounts	227,780	180,995
- Closed Customer Accounts	270	103
Other legal entities	**744,048**	**64,232**
- Current Accounts	714,392	37,712
- Closed Customer Accounts	29,656	26,520
Individuals	**1,689,680**	**2,113,980**
- Current Accounts	1,624,362	2,083,189
- Term Deposits	35,803	-
- Closed Customer Accounts	29,515	30,791
Total Customer accounts	**2,661,778**	**2,359,310**

Economic sector concentrations within customer accounts are as follows:

	December 31, 2017		December 31, 2016	
	Amount	%	Amount	%
Individuals	1,689,680	63.48	2,113,980	89.60
Other Institutions of Foreign Governments	59,760	2.25	87,718	3.72
Embassies and Consulates	167,783	6.30	92,850	3.94
Trade and Services	184,332	6.93	15,480	0.66
Manufacturing and industry	499,655	18.77	19,247	0.82
Public Organisations	506	0.02	530	0.02
Construction and Real Estate	19,642	0.74	1,111	0.05
Agriculture and Recycling	2,349	0.09	1,756	0.07
Transportation or Communication	111	-	115	-
Other	37,960	1.42	26,523	1.12
Total Customer accounts	**2,661,778**	**100.00**	**2,359,310**	**100.00**

The balance amount of customer accounts is their fair values as of December 31, 2017 and December 31, 2016. The fair value of customer accounts is AZN 2,661,778 as of December 31, 2017 (2016: AZN 2,359,310).

14 OTHER LIABILITIES

Other liabilities comprise the following:

	December 31, 2017	December 31, 2016
Items in Course of Settlement	4,859	497,865
Other financial liabilities	8,120	27,949
Total other financial liabilities	**12,979**	**525,814**
Tax payable	92,928	89,300
Payable for guarantees	-	451,529
Sundry creditors	6,220	12,568
Total other liabilities	**112,127**	**1,079,211**

15 SUBORDINATED DEBT

On 9 February 2017, the Bank signed Subordinated Debt Agreement with the Bank Melli Iran Head Office, registered in Tehran, the Iran Islamic Republic, for obtaining funds in the amount of EUR 9,000,000 to raise its capital via Tier-2 with the maturity till 30 December 2024. This borrowingis not guarenteed by any assets of Bank Melli Iran Baku branch and that the balance bears no interest and is repayable in five equal semi-annual instalments with a first instalment due on 30 December 2020.
At 31 December 2017, the estimated fair value of subordinated debt was AZN 18,276,300 (2016: AZN nil).
The repayment of Bank's subordinated debt ranks after all other creditors in case of liquidation of the Bank, even; before the maturity if the Branch experiences good financial position.

16 SHARE CAPITAL

Total registered and paid shares of the Bank amounted to AZN 73,611,171 as of December 31, 2017. The movement of shares is as follows:

	Share capital
At December 31, 2016	**51,433,671**
- increase in share capital	22,177,500
At December 31, 2017	**73,611,171**

According to agreement with Head office, on 9 february 2017 loan to head office in the amount of AZN 22,177,500 (USD 12,500,000) was transferred to share capital.
100% of share capital owned by Bank Melli Iran Head Office.

17 INTEREST INCOME AND EXPENSE

	Year ended December 31, 2017	Year ended December 31, 2016
Interest income comprises:		
Interest income on assets at amortised cost		
-interest income on assets with recognized provision	2,865,813	3,210,426
Interest income on financial assets held for trading	105,130	50,522
Total interest income	**2,970,943**	**3,260,948**
Interest income		
Loans and advances to:		
-customers	1,074,426	2,026,924
-banks and other financial institutions	2,300	336,637
	1,076,726	**2,363,561**
- financial assets held for trading	105,130	50,522
-investment securities held-to-maturity	1,789,087	846,865
Total interest income	**2,970,943**	**3,260,948**
Interest expense comprises:		
-interest on liabilities recorded at amortized cost	(5,487)	(802)
Total interest expense	**(5,487)**	**(802)**
Interest expense		
-deposits due to customers	(803)	-
-deposits due to banks	(4,684)	(802)
-other	(48,215)	(42,934)
Total interest expenses	**(53,702)**	**(43,736)**
Net interest income prior to provisions	**2,917,241**	**3,217,212**

18 GAIN FROM OPERATIONS IN FOREIGN CURRENCIES – LESS LOSSES

Gain on foreign exchange operations - less losses comprises:

	Year ended December 31, 2017	Year ended December 31, 2016
Dealing operations	253,662	(61,196)
Revaluation	(44,702)	425,189
Net losses	**208,960**	**363,993**

19 FEE AND COMMISSION INCOME AND EXPENSE

	Year ended December 31, 2017	Year ended December 31, 2016
Fee and commission income comprises:		
-cash operations	27,217	38,496
-settlements	171,560	85,662
-other operations	300	11,224
Total fee and commission income	**199,077**	**135,382**
Fee and commission expense comprises:		
-settlements	(49,573)	(36,059)
-cash operations	(7,122)	(1,536)
-other operations	(10,960)	(6,703)
Total fee and commission expenses	**(67,655)**	**(44,298)**
Net fee and commission income	**131,422**	**91,084**

20 OPERATING EXPENSES

	Year ended December 31, 2017	Year ended December 31, 2016
Salaries and wages	965,570	917,766
Taxes, other than income tax	197,129	310,510
Legal fees	2,305	303,200
Depreciation expenses	117,225	116,546
Premises Security	63,651	63,299
Insurance expenses	49,718	42,940
Communications	40,936	42,127
Repair and maintenance	63,117	39,157
SWIFT expenses	24,485	45,554
Utilities	14,005	24,106
Professional Services	25,312	29,378
Membership	196,000	33,000
Printing and office supplies	7,766	11,962
Rent expense	6,466	6,083
Advertising	8,503	-
Miscellanous	48,618	56,579
Total operating expenses	**1,830,806**	**2,042,207**

21 INCOME TAX

Income tax expense comprises the following:

	Year ended December 31, 2017	Year ended December 31, 2016
Taxable/(deductible) temporary differences		
-premises and equipments and other assets	(1,427,225)	(150,127)
Net taxable/(deductible) temporary differences	**(1,427,225)**	**(150,127)**
Net deferred tax liability at the end of the year (at the statutory tax rate of 20%)	(285,445)	(30,025)
Net deferred tax (liability)/asset at the beginning of the year	(30,025)	(33,034)
Change in the deferred tax for the year charged to profit	**(255,420)**	**3,009**
Deferred income/(expense) charged to equity	1,342	1,342
Deferred income/(expense) charged to profit	(256,761)	1,667

	Year ended December 31, 2017	Year ended December 31, 2016
Profit/(loss) before income tax	6,923,175	(29,270,761)
Tax at the statutory tax rate	(1,384,635)	5,854,152
Tax effect of permanent differences	-	-
Unrecognised carry forward tax losses for the year	1,127,874	(5,852,485)
Utilisation of previous year carry forward losses	-	
Income tax (expense)/benefit	**(256,761)**	**1,667**
Current income tax expense	-	-
Change in the deferred income tax	(256,761)	1,667
Income tax (expense) / benefit	**(256,761)**	**1,667**

Differences between IFRS and Azerbaijani statutory taxation regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases.

22 FINANCIAL RISK MANAGEMENT

The risk management function within the Bank is carried out in respect of financial risks, operational risks and legal risks. Financial risk comprises market risk (including currency risk, interest rate risk and other price risk), credit risk and liquidity risk.

The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimise operational and legal risks.

Credit risk. The Bank takes on exposure to credit risk which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises as a result of the Bank's lending and other transactions with counterparties giving rise to financial assets.

In addition, there are certain limits introduced and regularly monitored by the CBAR which are also mandatory to comply for all financial institutions of Azerbaijan. The following sub-limits are applied by the Bank:

(1) the maximum loan amount for one borrower or related borrowers is, as follows:

(i) 20 per cent of the Bank's tier 1 capital if the market value of the collateral is at least equal to 100 per cent of the value of the loan and less if there is no 150 per cent of the value of the loan collateralized by real estate; and

(ii) 7 per cent of the Bank's tier 1 capital if the market value of the collateral is at least equal to 100 per cent of the value of the loan and less if there is no 150 per cent of the value of the loan collateralized by real estate; and

(2) All large loans in aggregate must not exceed 8 times in total of the Bank's total equity;

(3) the total maximum amount of the Bank's loans to related parties must not exceed:

(i) 20 per cent of the Bank's total equity for all such loans; and

(ii) 10 per cent of the Bank's equity per legal person; or

(iii) 3 per cent of the Bank's equity per physical person.

The serates are calculated based on the figures from the Bank's financial statements prepared in accordance with local standards.

The limits, other than the limits of the CBAR are developed and revised by the Risk Management Department on a quarterly basis. In the case of material change to the market environment, the limits may also be reviewed. A proposal for any change to the limits is first provided to the Credit Committee and subsequently to the Management Board of Bank Melli Iran for approval.

The Credit department reviews the adherence to all limits on a regular basis and some of the limits (maximum exposure to a single borrower or group of related borrowers, maximum exposure to related parties) are checked prior to the issue of any new loan.

The Credit Policy of the Bank regulates the authorities and responsibilities of each body of the Bank involved in lending process and determine the limits for credit granting approval the rules for monitoring of loans, the principles of rating system implemented by the bank, lending procedures etc.

Loan Approval Procedure and Delegation. The loan approval process is conducted in accordance with the procedures described in Lending Policy of the Bank. The delegation of authorities for loan granting approval process has been defined within the limits set by Head office by Credit Committee of the Bank.

Delegation of authorities for credit granting approval. Credit Committee monitors and approves all loans within set limits. Limits on loans are as follows:

- Business loans (36 months) – withcollateral of real estate - maximum limit USD 150,000;

- Loans to individuals (36 months) – with collateral of real estate - maximum limit USD 50,000;

- According to deposits - maximum limit USD 400,000;

- Loans to individuals who works in offices of Iran Islamic Republic in Azerbaijan's governmental institutions - maximum limit USD 20,000;

- Loans to individuals with guarant or maximum limit USD 10,000;

- Loans for the purpose of car purchase with collateral of car - maximum limit USD 10,000;

The Bank performs a detailed evaluation of potential borrowers before granting loans. This analysis is based on their financial situation, position on the market, type and value of collateral provided for secure the loan and on credit history of the potential borrower.

Monitoring is implemented on a regular basis during the whole duration of a loan. As the interest payments under the majority of the loans are made on a monthly basis it gives the Bank additional indicators of the borrower's financial condition. In case of overdue repayments, an extraordinary monitoring is executed by the Problem Cases Department which executes all types of loans' monitoring for the purpose of ensuring the security of Bank's assets and minimising possible credit risks and losses, and the results of it are to be formulated in special monitoring report presented for consideration to the Credit Committee of the Bank. The Bank aims for all loans to be secured by guarantees and various forms of collateral (real estate, vehicles, deposits, etc).

The appraisal of the collateral value provided to secure a loan is conducted by independent qualified companies and by the Bank's professional staff depending on type of collateral and amount of credit granted.

Credit risk for off-balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract. The Bank uses the same credit policies in making conditional obligations as it does for on-balance sheet financial instruments through established credit approvals, risk control limits and monitoring procedures

.***Maximum exposure to credit risk.*** The Bank's maximum exposure to credit risk for balance sheet items is usually presented in the balance sheet value of the financial assets in the statement of financial position. The ability of the interchange of assets and liabilities is significant to reduce potencial credit risk.

For off-balance sheet items, especially letters of credit and guarantees the maximum exposure of credit risk represents total amount of liabilities. The Bank's credit risk for off-balance sheet items is disclosed in Note 23 "Contingencies and Commitments"

Credit risk for off-balance sheet financial instruments is defined as the possibility of sustaining a loss as a result of another party to a financial instrument failing to perform in accordance with the terms of the contract.

The Bank uses the same credit policies in making conditional obligations as it does for on-balance sheet financial instruments through established credit approvals, risk control limits and monitoring procedures.

					December 31, 2017
	Maximum exposure	**Offset**	**Net exposure after offset**	**Collateral pledged**	**Net exposure after offset and collateral**
Cash and current placements with other banks	50,880,457	-	50,880,457	-	50,880,457
Due from banks and other financial institutions	2,476,426	-	2,476,426	2,476,426	-
Loans to customers	3,355,298	-	3,355,298	3,355,298	-
Investment securities held to maturity	18,347,899	-	18,347,899	-	18,347,899

					December 31, 2016
	Maximum exposure	**Offset**	**Net exposure after offset**	**Collateral pledged**	**Net exposure after offset and collateral**
Cash and current placements with other banks	32,766,383	-	32,766,383	-	32,766,383
Due from banks and other financial institutions	3,659,374	-	3,659,374	2,727,174	932,200
Loans to customers	7,161,773	-	7,161,773	7,161,773	-
Investment securities held to maturity	12,436,730	-	12,436,730	-	12,436,730

The banking industry is generally exposed to credit risk through its financial assets and contingent liabilities. Credit risk exposure of the Bank is concentrated within the Azerbaijan Republic. The exposure is monitored on a regular basis to ensure that the credit limits and credit worthiness guidelines established by the Bank's risk management policy are not breached

Market risk. The Bank takes on exposure to market risks. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements. Management sets limits on the value of risk that may be accepted, which is monitored on a daily basis. However, the use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

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

At the end of the reporting period the Bank's exposure to foreign currency exchange rate risk is presented in the table below:

	AZN	USD	EUR	Other	December 31, 2017 Total
ASSETS					
Cash and current placements with other banks	396,796	19,826,681	31,939,689	108,513	52,271,679
Due from banks and other financial institutions	2,476,426	-	-	-	2,476,426
Loans to customers	2,926,532	359,956	68,810	-	3,355,298
Financial assets held for trading	-	-	-	-	-
Investment securities held to maturity	18,006,149	341,750	-	-	18,347,899
Premises and equipment	3,608,285	-	-	-	3,608,285
Intangible assets	50,198	-	-	-	50,198
Other assets	20,387,890	-	-	-	20,387,890
TOTAL ASSETS	**47,852,276**	**20,528,387**	**32,008,499**	**108,513**	**100,497,675**
LIABILITIES					
Due to banks and other financial institutions	2,533	14,516,313	13,634,568	-	28,153,414
Customer accounts	241,608	1,474,059	946,111	-	2,661,778
Deferred tax liabilities	285,445	-	-	-	285,445
Other liabilities	108,897	3,230	-	-	112,127
Subordinated debt	-	-	18,276,300	-	18,276,300
TOTAL LIABILITIES	**638,483**	**15,993,602**	**32,856,979**	**-**	**49,489,064**
NET BALANCE SHEET POSITION	**47,213,793**	**4,534,785**	**(848,480)**	**108,513**	**51,008,611**

	AZN	USD	EUR	Other	December 31, 2016 Total
ASSETS					
Cash and current placements with other banks	804,299	17,122,327	17,193,085	7,480	35,127,191
Due from banks and other financial institutions	1,608,534	-	2,050,840	-	3,659,374
Loans to customers	7,067,592	94,181	-	-	7,161,773
Investment securities held to maturity	12,436,730	-	-	-	12,436,730
Premises and equipment	3,708,168	-	-	-	3,708,168
Intangible assets	38,083	-	-	-	38,083
Income tax assets	-	-	-	-	-
Deferred tax assets	-	-	-	-	-
Other assets	18,336,271	-	-	-	18,336,271
TOTAL ASSETS	**43,999,677**	**17,216,508**	**19,243,925**	**7,480**	**80,467,590**
LIABILITIES					
Due to banks and other financial institutions	1,536	33,996,804	21,094,110	-	55,092,450
Customer accounts	342,398	1,818,162	198,750	-	2,359,310
Deferred tax liabilities	30,025	-	-	-	30,025
Other liabilities	132,912	945,465	834	-	1,079,211
TOTAL LIABILITIES	**506,871**	**36,760,431**	**21,293,694**	**-**	**58,560,996**
NET BALANCE SHEET POSITION	**43,492,806**	**(19,543,923)**	**(2,049,769)**	**7,480**	**21,906,594**

Currency risk sensitivity. The Risk Management Department of the Bank daily monitors and regulates foreign currency risk related to commercial bank operations as follows:

i. Holding the open currency position limits determined by the CBAR for every foreign currency;

ii. Monitoring of the reciprocal relation between currency position level and liquidity level for every foreign currency;

iii. Forecasting of change trends in foreign currency exchange rates as USD and EUR;

iv. Analysis of activity of the Bank's large customers engaged in export-import operations and bank operations.

Open positions in foreign currencies. Exposure to foreign exchange risk faced by the Bank is also limited by the CBAR normative requirements, which place a 10% of capital limit on open positions in any single foreign currency and a 20% open limit on all foreign currencies.

As at December 31, 2017 the Bank was in compliance with open currency limits determined by local legislation, as open currency position in single foreign currency was maximim 8,8% of the total capital.

The Bank's open currency position determined by local legislation is calculated based on the Bank's statements prepared in compliance with local standards and this calculation may materially differ from the information given in the Bank's current financial statements.

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

Impact on profit before tax:

	As at December 31, 2017		**As at December 31, 2016**	
	Interest rate 1%	**Interest rate -1%**	**Interest rate 1%**	**Interest rate -1%**
Assets:				
Due from banks and other financial institutions	24,764	(24,764)	36,594	(36,594)
Loans to customers	33,553	(33,553)	71,618	(71,618)
Investment securities held to maturity	183,479	(183,479)	124,367	(124,367)
Liabilities:				
Due to banks and other financial institutions	(281,534)	281,534	(550,925)	550,925
Subordinated debt	(182,763)	182,763	-	-
Net impact on profit before tax	**(222,501)**	**222,501**	**(318,346)**	**318,346**

Geographical concentration

The geographical concentration of financial assets and liabilities as of December 31, 2017 is set out below:

	Azerbaijan Republic	OECD countries	Non-OECD countries	Total
Financial assets				
Cash and current placements with other banks	26,796,560	-	25,475,119	52,271,679
Due from banks and other financial institutions	2,476,426	-	-	2,476,426
Loans to customers	3,355,298	-		3,355,298
Investment securities held to maturity	18,347,899	-	-	18,347,899
Other financial assets	9,295,981	-	-	9,295,981
Total financial assets	**60,272,164**	**-**	**25,475,119**	**85,747,283**
Financial liabilities				
Due to banks and other financial institutions	8,986	-	28,144,428	28,153,414
Customer accounts	1,230,580	-	1,431,198	2,661,778
Other financial liabilities	12,979	-	-	12,979
Subordinated debt	-	-	18,276,300	18,276,300
Total financial liabilities	**1,252,545**	**-**	**47,851,926**	**49,104,471**
Net balance sheet position	**59,019,619**	**-**	**(22,376,807)**	**36,642,812**

The geographical concentration of assets and liabilities as of December 31, 2016 is set out below:

	Azerbaijan Republic	OECD countries	Non-OECD countries	Total
Financial assets				
Cash and current placements with other banks	22,125,656	-	13,001,535	35,127,191
Due from banks and other financial institutions	2,734,163	-	925,211	3,659,374
Loans to customers	7,161,773	-	-	7,161,773
Investment securities held to maturity	12,436,730	-	-	12,436,730
Other financial assets	9,306,699	-	-	9,306,699
Total financial assets	**53,765,021**	**-**	**13,926,746**	**67,691,767**
Financial liabilities				
Due to banks and other financial institutions	13,498	-	55,078,952	55,092,450
Customer accounts	734,528	-	1,624,782	2,359,310
Other financial liabilities	525,814	-	-	525,814
Total financial liabilities	**1,273,840**	**-**	**56,703,734**	**57,977,574**
Net balance sheet position	**52,491,181**	**-**	**(42,776,988)**	**9,714,193**

Assets, liabilities and loan liabilities are classified according to the counterparts' operation country. Cash, precious metals, and equipments are classified according to the holding countries.

Other risk concentrations. The Management determines risk concentrations based on the evaluation of quantitative indexes for the risks within the reporting period. This disclosure is based on the information presented to key management personnel and represents currency, credit and interest rate risk concentration analysis.

Liquidity risk. Liquidity risk exists when the maturities of assets and liabilities do not match. The Bank everyday incurs risks related to the usage of the monetary funds intended for operations with overnight placements, customer accounts, repayment of deposits, granting loans, payments on guarantees and derivative financial instruments. The Bank doesn't hold enough monetary funds to meet all the obligations shown above at the same time, as it is possible to forecast exactly the necessary level of the monetary funds amount intended for meeting these obligations based on the experience. The liquidity risk is controlled by the management of the Bank.

The Bank seeks to maintain a stable funding base comprising primarily amounts due to other banks, corporate and retail customer deposits and debt securities and invest the funds in diversified portfolios of liquid assets, in order to be able to respond quickly and smoothly to unforeseen liquidity requirements.

The liquidity management of the Bank requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring balance sheet liquidity ratios against regulatory requirements.

The Bank calculates its instant liquidity ratio on a monthly basis in accordance with the requirement of the Central Bank of Azerbaijan Republic.

In accordance with the directions of the CBAR, the Bank calculates the quick ratio as a ratio of weighted daily assets to weighted daily liabilities. This ratio is calculated based on the balances from the Bank's financial statements prepared in accordance with local standards.

Risk Management Departament obtains the information on the liquidity profiles related to financial assets and liabilities, monitors the liquidity position every day and regularly do testings of sensitivity for liquidity based on different scenarious which include standard and unfavorable market conditions. After this, Management maintains adequacy of short-term liquid assets which include short-term debt securities for sale, short-term placements with other banks for the purpose of maintenance enough liquidity in the Bank.

The functions of Risk Management Department are set out below:

i. Compliance with the minimum liquidity requirements of the CBAR (As a percentage of assets and liabilities should not be less than 30%);

ii. Reporting to the Bank's director and assistant director on the forecast levels of cash flows;

iii. Monitoring of large deposit concentrations;

iv. Monitoring of cash flows related to the Bank's credit activity;

v. Control complience with OPFC currency limits.

The Bank controls maturities and liquidity shortage summarized as follows at December 31, 2017:

	Up to 1 month	1 month to 3 months	3 months to 1 year	More than 1 year	Total
Assets					
Cash and current placements with other banks	52,271,679	-	-	-	52,271,679
Due from banks and other financial institutions	2,476,426	-	-	-	2,476,426
Loans to customers	322,554	601,205	1,782,083	649,456	3,355,298
Investment securities held to maturity	253,520	2,308,755	11,873,690	3,911,934	18,347,899
Other financial assets	-	-	-	9,295,981	9,295,981
Total financal assets	**55,324,179**	**2,909,960**	**13,655,773**	**13,857,371**	**85,747,283**
Liabilities					
Due to banks and other financial institutions	28,153,414	-	-	-	28,153,414
Customer accounts	2,661,778	-	-	-	2,661,778
Other financial liabilities	12,979	-	-	-	12,979
Subordinated debt	-	-	-	18,276,300	18,276,300
Total financial liabilities	**30,828,171**	**-**	**-**	**18,276,300**	**49,104,471**
Liquidity gap as at December 31, 2017	**24,496,008**	**2,909,960**	**13,655,773**	**(4,418,929)**	**36,642,812**
Cumulative liquidity gap as at December 31, 2017	**24,496,008**	**27,405,968**	**41,061,741**	**36,642,812**	

The Bank controls maturities and liquidity shortage summarized as follows at December 31, 2016:

	Up to 1 month	1 month to 3 months	3 months to 1 year	More than 1 year	Total
Assets					
Cash and current placements with other banks	35,127,191	-	-	-	35,127,191
Due from banks and other financial institutions	2,724,818	934,556	-	-	3,659,374
Loans to customers	616,422	1,170,781	3,673,607	1,700,963	7,161,773
Investment securities held to maturity	3,871,060	2,294,750	6,270,920	-	12,436,730
Other financial assets	10,528	-	-	9,296,171	9,306,699
Total financal assets	**42,350,019**	**4,400,087**	**9,944,527**	**10,997,134**	**67,691,767**

Liabilities					
Due to banks and other financial institutions	28,716,396	-	-	26,376,054	55,092,450
Customer accounts	2,359,310	-	-	-	2,359,310
Other financial liabilities	525,814	-	-	-	525,814
Total financial liabilities	**31,601,520**	**-**	**-**	**26,376,054**	**57,977,574**
Liquidity gap as at December 31, 2016	**10,748,499**	**4,400,087**	**9,944,527**	**(15,378,920)**	**9,714,193**
Cumulative liquidity gap as at December 31, 2016	**10,748,499**	**15,148,586**	**25,093,113**	**9,714,193**	

The matching and/or controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest and exchange rates.

The management considers that although the great part of customer accounts has "demand" status, diversification of these deposits by number and type of depositors, and the past experience of the Bank would indicate that these customer accounts provide a long-term and stable source of funding for the Bank.

23 COMMITMENTS AND CONTINGENCIES

Legal proceedings. From time to time and in the normal course of business, claims against the Bank can be received. On the basis of its own estimates and both internal and external professional advice the

Bank's management is of the opinion that no material losses will be incurred in respect of claims and accordingly no provision has been made in these financial statements.

Tax legislation. Azerbaijani tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation, as applied to the transactions and activity of the Bank, may be challenged by the relevant state authorities. Recent events within the Republic of Azerbaijan suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Capital expenditure commitments. At December 31, 2017, the Bank had no significant contractual capital expenditure commitments in respect of premises and equipment, or in any other areas.

Operating lease commitments. At December 31, 2017, the Bank had no significant operating lease commitments (2016: nil).

Compliance with covenants. The Management has made judgments during interpretation of local legislation requirements and determination of the Bank's compliance with special covenants in credit facility agreements. These judgments comprise calculation methods and impact of such potential contradictions on the Bank. The Management based on the rules it uses believes that the determination of the impact of the current contradictions on the financial statements was properly accomplished. If proof that, management's approach is not the correct, penalties or other sanctions may be imposed against the Bank.

Obligations related to credits. The main purpose of these financial instruments is to maintain providing financial assets to customers.

Commitments for granting credits comprise unused part of the amounts not approved by the Management for granting credits as loans, guarantees or letters of credit. The Bank incurs risks of loss which equals to the total amount of potential unused commitments when the unused amounts should be used due to the credit commitments. However, as the great part of credit related commitments depends on some requirements concerning customer's payment ability, the estimated amount of loss is less than the amount of unused commitments. Due to the fact that long-term liabilities usually have higher credit risk comparing to short-term liabilities, the Bank monitors the period untill the maturity date of the credit related commitments. The commitments related to credits comprise the following.

The total outstanding contractual amount of un-drawn credit lines, letters of credit, and guarantees does not necessarily represent future cash requirements, as these financial instruments may expire or terminate without being funded.

24 MANAGEMENT OF CAPITAL

The Bank's objectives when managing capital are to comply with the capital requirements set by the CBAR, to safeguard the Bank's ability to continue as a going concern and to maintain a sufficient capital base to achieve a capital adequacy ratio of at least 10%. Compliance with capital adequacy ratios set by the Central Bank of Azerbaijan is monitored monthly with reports outlining their calculation reviewed and signed by the Bank's director and assistant director, Chief Accountant and Head of Internal Audit Department. Other objectives of capital management are evaluated annually.

Under the current capital requirements set by the CBAR banks have to: (a) hold the minimum level of share capital of AZN 50,000 thousand; (b) maintain a ratio of regulatory capital to risk weighted assets ("statutory capital ratio") at or above a prescribed minimum of 10% and (c) maintain a ratio of tier-1 capital to the risk-weighted assets (the 'Tier-1 capital ratio') at or above the prescribed minimum of 5%.

CBAR capital adequacy ratio

The CBAR requires banks to maintain a minimum capital adequacy ratio of 10% (2016: 10%) of risk-weighted assets for regulatory capital. As at 31 December 2017 and 2016 the Bank's capital adequacy ratio on this basis was as follows:

	December 31, 2017	December 31, 2016
Tier 1 capital	44,066,691	21,889,191
Tier 2 capital	25,501,659	212,466
Less: deductions from capital	(50,198)	(38,083)
Total regulatory capital	**69,518,152**	**22,063,574**
Risk-weighted assets	**53,010,556**	**46,377,906**
Capital adequacy ratio	**131%**	**47%**
Tier 1 capital adequacy ratio	**83%**	**47%**

The Management Board of the Central Bank of the Republic of Azerbaijan decided to keep the minimum level of capital for banks in the amount of AZN 50 million. The effective date of this decision was January 1, 2015.

As at December, 31 2017 total regulatory capital was amounted to AZN 69,518,152, which is in compliance with CBAR's requirements.

As at December, 31 2016 total regulatory capital was amounted to 22,063,574, which is not in compliance with CBAR's requirements. Capital of Bank Melli Iran Baku Branch significantly decreased during 2016 as a result of 100% provision on deposits placed at some commercial banks (Royal Bank, Zamin Bank, Texnika Bank,Atra Bank and Birlik Bank) in Azerbaijan. In this regard, on February 9, 2017 the bank increased its capital in the amount of AZN 22,177,500. Additionally Bank achquired subordinated debt from head office in the amount of EUR 9,000,000 for the 8 years period,which also element of tier-2 capital.

Management believes that the Bank is in compliance with the other statutory requirements of the CBAR at December 31, 2017.

25 FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair values of financial instruments carried at amortized cost are as follows:

	December 31, 2017		December 31, 2016	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets				
Cash and current placements with other banks	52,271,679	52,271,679	35,127,191	35,127,191
Due from banks and other financial institutions	2,476,426	2,476,426	3,659,374	3,659,374
Loans to customers	3,355,298	3,355,298	7,161,773	7,161,773
Investment securities held to maturity	18,347,899	18,347,899	12,436,730	12,436,730
Other financial assets	9,295,981	9,295,981	9,306,699	9,306,699
Total financial assets carried at amortised cost	**85,747,283**	**85,747,283**	**67,691,767**	**67,691,767**

	December 31, 2017		December 31, 2016	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Financial liabilities				
Due to banks and other financial institutions	28,153,414	28,153,414	55,092,450	55,092,450
Customer accounts	2,661,778	2,661,778	2,359,310	2,359,310
Other financial liabilities	12,979	12,979	525,814	525,814
Subordinated debt	18,276,300	18,276,300	-	-
Total financial liabilities carried at amortised cost	**49,104,471**	**49,104,471**	**57,977,574**	**57,977,574**

26 PRESENTATION OF FINANCIAL INSTRUMENTS BY MEASUREMENT CATEGORY

For the purposes of measurement, IAS 39, Financial Instruments: Recognition of Measurement, classifies financial assets into the following categories: (a) loans and receivables; (b) available for sale financial assets; (c) financial assets held to maturity and d) financial assets at fair value through profit or loss ("PLFV"). "Financial assets at fair value through profit or loss" category is divided into two sub-categories: (i) During the initial accounting part of this category of assets and (ii) financial assets for trading.

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

	Loans and receivables	**Available-for-sale assets**	**Total**
Financial assets			
Cash and current placements with other banks	52,271,679	-	52,271,679
Cash on hand	1,391,222	-	1,391,222
Cash and balances with the CBAR	25,398,018	-	25,398,018
Correspondent accounts	25,482,439	-	25,482,439
Due from banks and other financial institutions	2,476,426	-	2,476,426
Loans to customers	3,355,298	-	3,355,298
Individuals	4,512,127	-	4,512,127
Legal entities	254,175	-	254,175
Provision for impairment	(1,411,004)	-	(1,411,004)
Investment securities held to maturity	18,347,899	-	18,347,899
Other financial assets	9,295,981	-	9,295,981
Total financial assets	**85,747,283**	**-**	**85,747,283**
Non-financial assets	**14,750,392**	-	**14,750,392**
Total assets	**100,497,675**	-	**100,497,675**

The following table provides a reconciliation of classes of financial assets with these measurement categories as at December 31, 2016:

	Loans and receivables	Available-for-sale assets	Total
Financial assets			
Cash and current placements with other banks	35,127,191	-	35,127,191
Cash on hand	2,360,808	-	2,360,808
Cash and balances with the CBAR	19,251,876	-	19,251,876
Correspondent Accounts	13,514,507	-	13,514,507
Due from banks and other financial institutions	3,659,374	-	3,659,374
Loans to customers	7,161,773	-	7,161,773
Legal entities	596,025	-	596,025
Individuals	8,514,432	-	8,514,432
Provision for impairment	(1,948,684)	-	(1,948,684)
Investment securities held to maturity	12,436,730	-	12,436,730
Other financial assets	9,306,699	-	9,306,699
Total financial assets	**67,691,767**	**-**	**67,691,767**
Non-financial assets	**12,775,823**	-	**12,775,823**
Total assets	**80,467,590**	-	**80,467,590**

27 TRANSACTIONS WITH RELATED PARTIES

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

	December 31, 2017		December 31, 2016	
	Related party balances	Total category as per financial statements caption	Related party balances	Total category as per financial statements caption
Loans to customers		**4,766,302**		**9,110,457**
- entities with joint control or significant influence over the entity	-		-	
- key management personnel of the entity or its close relatives	6,491		155,596	
Allowance for impairment losses		**(1,411,004)**		**(1,947,684)**
- entities with joint control or significant influence over the entity	-		-	
- key management personnel of the entity or its close relatives	(65)		(1,556)	
Customer accounts		**2,661,778**		**2,359,310**
- entities with joint control or significant influence over the entity	-		-	
- key management personnel of the entity or its close relatives	47,511		20,577	

As at December 31, 2017 and December 31, 2016 benefits to key management personnel were as follows:

	Year ended December 31, 2017	**Year ended December 31, 2016**
Short-term benefits – salaries and bonuses	168,294	162,836
Total	**168,294**	**162,836**

During the year ended December 31, 2017 key management's compensation, comprising salaries and benefits of the Bank's director and assistant director are classified as short-term payments in accordance IAS 19 "Employee Benefits".

28 EVENTS AFTER THE REPORTING PERIOD

No significant events have occured after reporting period.