Subsidiary Bank National Bank of Pakistan in Kazakhstan JSC

Financial statements

For the year ended 31 December 2018
prepared in accordance with IFRSs

Almaty 2019

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MOORE STEPHENS

INDEPENDENT AUDITORS' REPORT

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To the shareholder of Subsidiary Bank National Bank of Pakistan in Kazakhstan JSC

Qualified Opinion

We have audited the accompanying financial statements of Subsidiary Bank National Bank of Pakistan in Kazakhstan JSC (hereinafter – "the Bank"), which comprise the statement of financial position as at 31 December 2018, and the statement of total comprehensive loss, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, except for the effects of the matter described in the *Basis for Qualified Opinion* section of our report, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (hereinafter – "IFRSs").

Basis for Qualified Opinion

Impairment of loans to clients

As indicated in note 2(g), due to the fact that according to the Bank's management, most of the loans to clients will be repaid through the sale of collateral (distressed loans), the Bank assessed the impairment of these assets on an individual basis, calculating the amount of the allowance by analysing discounted cash flows that would be received from the sale of such collateral. The analysis assumes high level of subjectivity and dependence on the assumptions used in assessing the possible realisable value of collateral and the timing of its implementation.

During the audit, we paid special attention to the verification of the validity of the assessment approaches used, methods for collecting information, and also the validity of the main assumptions in determining the value of collateral. As a result, taking into account the real estate market situation in Kazakhstan, we were unable to obtain sufficient amount of relevant audit evidence to confirm the assumptions used by the Bank's management for the determination of the allowance. In the absence of stated evidence, we had a limitation on the scope of our audit procedures when evaluating the assumptions used by the Bank's management in determining the allowance. Accordingly, we were unable to determine whether any adjustments were necessary in respect of impairment losses, loans to clients and retained earnings for the year ended 31 December 2018.

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

Emphasis of Matter – Impairment of financial assets

Without qualifying our opinion, we draw attention to note 2(e) to the financial statements, which states that the Bank is not able to use the model of "expected credit losses" (hereinafter – "ECL model"), due to late agreement with the National Bank of the Republic of Kazakhstan. In this regard, despite the provisions of IFRS 9, when assessing losses from the impairment of financial assets, the Bank applied the previously approved model of incurred losses stipulated by IAS 39 instead of the model. The management believes that the impact of this aspect is insignificant, taking into account the peculiarities of financial assets Bank and its policies and procedures in credit risk management, which minimise the risk of losses. Our opinion does not contain reservations regarding this issue.

Key Audit Matters

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

In addition to the questions set out in the sections "Basis for expressing opinions with a reservation" and "Important circumstances – impairment of financial assets", we identified the following key question that needs to be reported in our report:

Materiality

The maximum tolerable error for the financial statements of the Bank as a whole was set at KZT 71,000 thousand. It was determined with reference to a benchmark of the Bank total assets which represents 1.5%. The total assets were taken as the calculation base because from the beginning of 2016 the Bank had stopped issuing loans due to significant problem loan portfolio.

We reported to the Bank's management all identified uncorrected misstatements exceeding KZT 3,600 thousand for the comprehensive loss items and other identified misstatements that warranted reporting on qualitative grounds.

Except for the effects of the matter described in the *Basis for Qualified Opinion,* the amount of identified uncorrected misstatements does not exceed the maximum tolerable error for the Bank's financial statements as a whole.

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

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

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

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

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 scepticism throughout the audit. We also:

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

Auditors' Responsibilities for the Audit of the Financial Statements, continued

- 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.

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Approve

Serik Kozhikenov
Certified auditor
Audit partner
Audit certificate №0000557 dated 24 December 2003
Chief Executive
Moore Stephens Kazakhstan LLP
11 February 2019

Aidar Aitov
Audit-partner

MOORE STEPHENS

General license No. 18021214 for audit activity issued 23 November 2018 by Ministry of Finance of the Republic of Kazakhstan

SB National Bank of Pakistan in Kazakhstan JSC
Statement of financial position
as at 31 December 2018

KZT'000	Note	2018	2017
Assets			
Cash	3	397,256	503,834
Amounts due from other banks		2,645	2,599
"Reverse REPO" receivables	4	2,686,686	2,655,764
Loans to clients	5	1,108,853	1,403,445
Corporate income tax prepaid		13,760	14,972
Assets held for sale	6	348,580	247,896
Other assets	7	63,377	79,962
Property, plant and equipment		9,724	4,200
Intangible assets	8	130,864	129,633
Total assets		**4,761,745**	**5,042,305**
Liabilities			
Correspondent accounts and amounts due to banks		747	523
Amounts due to clients	9	263,177	492,908
Other liabilities	10	53,990	29,692
Total liabilities		317,914	523,123
Equity			
Share capital	11(a)	4,325,000	4,325,000
Reserve capital	11(b)	79,620	79,620
Dynamic reserves	11(c)	–	86,255
Retained earnings		39,211	28,307
Total equity		4,443,831	4,519,182
Total equity and liabilities		**4,761,745**	**5,042,305**

These financial statements have been approved for issue on 11 February 2019 and signed on behalf of the Bank's management:

Arif Hussain
Deputy General Manager
Subsidiary Bank National Bank of Pakistan
in Kazakhstan JSC

Pirmaganbetova Akmaral
Chief Accountant
Subsidiary Bank National Bank of Pakistan
in Kazakhstan JSC

NATIONAL BANK OF PAKISTAN IN KAZAKHSTAN (Subsidiary Bank)

The notes on pages 5 to 26 are an integral part of these financial statements

KZT'000 (unless otherwise stated)	Note	2018	2017
Interest income	12	246,453	309,754
Interest expenses	13	(7,538)	(15,799)
Net interest income		**238,915**	**293,955**
Recovery (allowance) for loan impairment	5	20,844	(352,508)
Net interest income (loss) after allowance for loan impairment		**259,759**	**(58,553)**
Commission income		10,114	15,690
Commission expenses		(5,973)	(5,745)
Net gain from foreign currency transactions		19,000	2,377
Recovery (allowance) of provision for other assets	7	4,845	(19,913)
Operating profit (loss)		**287,745**	**(66,144)**
Administrative expenses	14	(363,096)	(448,011)
Loss before tax		**(75,351)**	**(514,155)**
Income tax recovery	15(a)	–	–
Loss for the year		**(75,351)**	**(514,155)**
Other comprehensive income		–	–
Total comprehensive expense for the year		**(75,351)**	**(514,155)**
Basic loss per share, tenge	11(d)	(8,711)	(62,801)

KZT'000	Note	2018	2017
Cash flow from operating activities:			
Interest received on loans to clients and amounts due from other banks	12	15,362	39,533
Interest received on "Reverse REPO"	12	231,091	270,221
Interest paid on amounts due to clients		(7,538)	(15,799)
Commission income received		10,114	15,690
Commission expenses paid		(5,973)	(5,745)
Net loss from foreign currency transactions		17,051	(877)
Administrative and other operating expenses paid		(360,460)	(440,041)
Cash flows from operating activities before changes in operating assets and liabilities		(100,353)	(137,018)
(Increase) decrease in amounts due from other banks		(46)	957
(Increase) decrease in "Reverse REPO" receivables		(30,922)	223,779
Decrease of loans to clients		315,436	136,898
Sale of assets held for sale	6	1,281	7,901
Increase in other assets		(80,535)	(22,697)
Decrease (increase) in correspondent accounts and amounts due from other banks		224	(44)
Decrease in amounts due to clients		(229,731)	(95,986)
Increase (decrease) in other liabilities		25,510	(9,522)
Net cash (used in) generated from operating activities		(99,136)	104,268
Cash flow from investing activities:			
Purchases of property, plant and equipment and intangible assets		(9,391)	(135,602)
Net cash used in investing activities		(9,391)	(135,602)
Cash flow from financing activities:			
Repayment of a subordinated loan		–	(214)
Net cash used in financing activities		–	(214)
Net decrease in cash		(108,527)	(31,548)
Effect of exchange rate changes on cash		1,949	3,254
Cash at the beginning of the year		503,834	532,128
Cash at the end of the year	3	**397,256**	**503,834**

Non-cash transactions:

The Bank conducted the following non-cash transactions:

- In 2018, due to the completion of state registration procedures other assets for the total amount of KZT 101,965 thousand were classified as assets held for sale (2017: KZT 89,140 thousand);
- In 2017, the subordinated loan in the amount of KZT 234,000 thousand was converted into ordinary shares of the Bank.

KZT'000	Share capital	Reserve capital	Dynamic reserves	Retained earnings	Total equity
At 1 January 2017	**4,091,000**	**79,620**	**86,255**	**542,462**	**4,799,337**
Net loss for the year	–	–	–	(514,155)	(514,155)
Issued shares	234,000	–	–	–	234,000
At 31 December 2017	**4,325,000**	**79,620**	**86,255**	**28,307**	**4,519,182**
Net loss for the year	–	–	–	(75,351)	(75,351)
Reclassification of dynamic reserves and retained earnings	–	–	(86,255)	86,255	–
At 31 December 2018	**4,325,000**	**79,620**	**–**	**39,211**	**4,443,831**

The notes on pages 5 to 26 are an integral part of these financial statements

1. General information

(a) Organisation and operation

Joint Stock Company Subsidiary Bank National Bank of Pakistan in Kazakhstan (hereinafter – the "Bank") is a joint stock company registered in the Republic of Kazakhstan in 2001. As at 31 December 2018 and 2017, the sole shareholder of the Bank is the National Bank of Pakistan, Karachi (hereinafter – the "Parent Bank"). The ultimate owner of the Bank is the State Bank of Pakistan with a share of 75.2% (2017: 75.2%).

The activity of the Bank is regulated by the National Bank of the Republic of Kazakhstan (hereinafter – the "NBRK"). The key activity of the Bank is banking operations carried out in the Republic of Kazakhstan. The Bank conducts its business under the license No. 252 for banking and other operations issued on 27 December 2007. The Bank is a member of Kazakhstan Deposit Insurance Fund JSC.

As at 31 December 2018 and 2017, the Bank has two branches in Almaty and Karaganda cities of the Republic of Kazakhstan. The number of employees as at 31 December 2018 was 54 persons (31 December 2017: 55 persons).

The legal address of the head office of the Bank: 27A Nauryzbai street, Kaskelen city, Almaty region, Republic of Kazakhstan.

(b) Kazakhstan economic environment

The Bank's activities are subject to economic, political and social risks inherent in doing business in Kazakhstan. These risks include the consequences of government policy decisions, economic conditions, the introduction or modification of tax claims and other legal regulations, currency fluctuations and the feasibility of contractual rights.

The accompanying financial statements reflect management's assessment of the impact of the economic environment in Kazakhstan on the operations and financial position of the Bank. Future economic conditions may differ from management's assessment.

2. Basis of preparation of financial statements

(a) Statement of compliance to IFRSs

Except for transition to IFRS 9 regarding impairment, these financial statements have been prepared in accordance with the International Financial Reporting Standards (hereinafter – "IFRSs") as issued by the International Accounting Standards Board (hereinafter – "IASB") and interpretations issued by the International Financial Reporting Interpretations Committee (hereinafter – "IFRIC") of the IASB. As described in note 2(e), the management of the Bank believes that the impact of this aspect is insignificant, given the characteristics of the Bank's financial assets and its credit risk management policies and procedures, which minimise the risk of loss.

(b) Going concern

These financial statements have been prepared on a going concern basis, accordingly, the Bank will continue to realise its assets and meet its liabilities in the ordinary course of business in the foreseeable future.

As at 31 December 2018, the Bank's retained earnings amounted to KZT 39,211 thousand, the loss for the year ended 31 December 2018 was KZT 75,351 thousand. Losses were formed a result of decrease in interest income on loans issued to clients due to suspending the issuance of new loans from March 2016.

In order to achieve sustainable financial results, the Bank's management plans to obtain permission for issuance of new loans to customers and conduct further systematic work to develop new loan products that provide a competitive advantage in the banking services market. The Bank's management believes that sufficient amount of own capital and a significant excess of highly liquid assets over liabilities will allow servicing current liabilities and introduce new loan products.

Therefore, the Bank's management believes that the accompanying financial statements do not require adjustments necessary in the event that the Bank could not continue its operations on a going concern basis.

(c) Basis of accounting

The financial statements have been prepared on a historical cost basis.

(d) Functional currency

The national currency of the Republic of Kazakhstan is the Kazakhstan tenge (hereinafter – "tenge" or "KZT"), which is the functional currency of the Bank and the currency in which these financial statements are presented. All financial information presented in tenge has been rounded to the nearest thousand (hereinafter – "KZT'000" or "KZT thousand").

2. Basis of preparation of financial statements, continued

(e) Adoption of standards and interpretations

In preparing the financial statements, the Bank has applied the following standards effective from 1 January 2018:

- IFRS 9 “Financial Instruments”. The new standard has been applied retrospectively but did not impact the Bank’s accounting policies for the recognition and measurement of financial assets and liabilities. The standard outlines a new “expected credit loss” model (hereinafter – "ECL model"), used to estimate the risk to the Bank’s financial assets. Taking into account the above, on 29 December 2018 the Bank developed and approved a new methodology for calculating allowance (reserves) in accordance with IFRS 9 (the ECL model) as per NBRK letter dated 23 December 2018, the coordination of which with the NBRK was only completed on 3 January 2019. Taking into account that the Bank was not able to apply the new methodology prior to its approval by the NBRK, the Bank used previously approved the IAS 39 model of incurred losses in assessing impairment losses of financial assets instead of the ECL model. At the same time, management believes that the impact of this aspect is insignificant, taking into account the peculiarities of the Bank’s financial assets and its credit risk management policies and procedures which control credit exposure and minimise the risk of loss.
- IFRS 15 “Revenue from Contracts with Customers”. In applying the transition requirements and provisions of the new standard, the Bank reviewed its contracts and assessed the nature of its performance obligations. The transition to the standard did not result in any classification or measurement adjustment or any restatement of comparative information.

The Bank has not early adopted any standards, interpretations or amendments that were issued but are not yet effective.

(f) New standards and interpretations not yet adopted

A number of new standards and interpretations have not yet entered into force, and their requirements have not been considered when preparing the financial statements:

- IFRS 16 “Leases”. The standard was issued in January 2016 with an effective date of 1 January 2019. The standard specifies how an entity will recognise, measure, present and disclose leases for lessees. The new standard’s approach to lessor accounting substantially unchanged. Based on the nature of the Bank’s activities, the adoption of the standard is not expected to have a material impact on the financial position or performance of the Bank.
- IFRS 17 “Insurance Contracts”. The standard was issued in May 2017 with an IASB effective date of 1 January 2021. IFRS 17 will replace IFRS 4 “Insurance Contracts” and applies to all types of insurance contracts (regardless of the type of entities that issue them), as well as to certain guarantees and financial instruments with discretionary participation features. This standard is not expected to have an impact on the financial position or performance of the Bank.
- IFRIC 23 “Uncertainty over Income Tax Treatments”: issued in June 2017 and effective from 1 January 2019. The interpretation provides additional guidance in the determination of taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates, when there is uncertainty over income tax treatments under IAS 12. This interpretation is not expected to have an impact on the financial position or performance of the Bank.
- Improvements to IFRSs: There are a number of amendments to certain standards following the 2016-2018 annual improvements project. These changes are not expected to have an impact on the Bank’s financial statements.

(g) Use of estimates and judgments

The Bank’s management has made a number of judgments, estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with IFRSs. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected. Below are the most significant cases of the use of judgments and estimates.

Fair value of financial instruments

If the fair value of financial assets and financial liabilities recorded in the statement of financial position cannot be determined based on prices in an active market, it is determined using different valuation models that include mathematical models. Note 16 provides details of key assumptions used in determining the fair value of financial instruments, as well as the detailed analysis of the sensitivity of estimates with respect to these assumptions. Management believes that the valuation techniques chosen and the assumptions used are appropriate to determine the fair value of financial instruments.

2. Basis of preparation of financial statements, continued

Impairment of loans to clients

The Bank regularly reviews its loans to clients for impairment. The Bank's reserves for the loan impairment are established to recognise incurred impairment losses in its loan portfolio. The Bank considers accounting estimates related to allowance for impairment of loans as a key source of estimation uncertainty because they are highly susceptible to changes from period to period as the assumptions on future default rates and valuation of potential losses relating to impaired loans are based on recent results, and any significant difference between the Bank's estimated losses and actual losses would require the Bank to record allowance which could have a significant impact on its financial statements in future periods.

The Bank uses management's judgment to estimate the amount of any impairment loss in cases where the borrower has financial difficulties and there are few sources of historical data relating for similar borrowers. Similarly, the Bank estimates changes in future cash flows based on the past experience, the borrower's past behaviour, the available data indicating negative change in the status of repayment by borrowers at the Bank, or national or local economic conditions that correlate with defaults on assets of the Bank. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the group of loans.

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

In determining the amount of allowance for loans to clients, management made the following assumptions:

- a decrease in the initial estimated value of the property pledged in case of sale is 30%;
- the delay in receipt of proceeds from the sale of collateral is 18 months.

Changes in the above estimates may affect the amount of the allowance for impairment of loans to clients.

Impairment of other receivables

The Bank regularly reviews other receivables for impairment and uses its subjective judgment in assessing impairment losses in situations where the debtor is experiencing financial difficulties and there is insufficient evidence of similar debtors. The Bank's management similarly estimates changes in future cash flows on the basis of observable data indicating an adverse change in the status of repayment of debtors' obligations or a change in state or local economic conditions that relates to incidents of default on assets within the Bank.

The Bank uses its subjective judgment when adjusting the observable data with respect to other receivables to reflect current circumstances.

Taxation

The management assesses the completeness of the recognition of various taxes applicable to the Bank, both to payment and reimbursement. The judgment was applied, in particular, with respect to corporate income tax, namely taxable losses. Professional judgment is critical because Kazakhstan's tax legislation is subject to various interpretations and changes that can occur frequently. The management's interpretation of such legislation applicable to transactions and activities of the Bank may be challenged by the relevant regional or state authorities. Thus, additional taxes, penalties and fines may be imposed.

(h) Comparative information

Where a change in the presentation format of the financial statements has been made during the year, comparative figures have been restated accordingly, to conform with the new presentation format.

3. Cash

KZT'000	2018	2017
"Nostro" accounts in other banks	325,381	340,885
Current accounts in NBRK	39,320	41,270
Cash on hand	32,555	121,679
	397,256	**503,834**

Minimum reserve requirements

In accordance with the regulations issued by the NBRK, the minimum reserve requirements are calculated as the total amount of certain ratios of different groups of bank liabilities. Banks are required to comply with these requirements by maintaining the average reserve assets (cash in the national currency and current accounts within the NBRK) equal to or greater than the average minimum requirements. As at 31 December 2018, the minimum reserve amount was KZT 10,768 thousand (2017: KZT 15,428 thousand). The Bank complies with the minimum reserve requirements for second-tier banks.

4. "Reverse REPO" receivables

As at 31 December 2018, there were unsettled "Reverse REPO" agreements in the amount of KZT 2,681,983 thousand (2017: KZT 2,653,003 thousand) between the Bank and Kazakhstan Stock Exchange JSC. As at 31 December 2018, accrued interest amounted to KZT 4,703 thousand (2017: KZT 2,761 thousand). The subject of these agreements were treasury notes of the Ministry of Finance of the Republic of Kazakhstan and the NBRK with annual interest rates ranging from 8% to 9% and maturing in January 2019 (2017: notes of the Ministry of Finance of the Republic of Kazakhstan, with rates ranging from 8% to 12%).

5. Loans to clients

KZT'000	2018	2017
Loans to legal entities	1,188,263	1,328,035
Loans to individuals	293,648	469,312
Gross loans to clients before allowance for impairment	**1,481,911**	**1,797,347**
Allowance for impairment	(373,058)	(393,902)
	1,108,853	**1,403,445**

Loans to individuals include loans granted to individual entrepreneurs.

As at 31 December 2018, the accrued interest amounted KZT 248,968 thousand (2017: KZT 283,039 thousand).

As at 31 December 2018, the Bank has a borrower which accounts for 22.76% of the maximum level of credit risk (2017: 18.77%).

Change in allowance for impairment of loans to clients is as follows:

KZT'000	Loans to legal entities	Loans to individuals	Total
At 1 January 2017	**31,021**	**10,373**	**41,394**
Accrued allowance	273,338	96,610	369,948
Recovered allowance	(13,058)	(4,382)	(17,440)
At 31 December 2017	**291,301**	**102,601**	**393,902**
Accrued allowance	21,388	29,652	51,040
Recovered allowance	(18,539)	(53,345)	(71,884)
At 31 December 2018	**294,150**	**78,908**	**373,058**

5. Loans to clients, continued

Quality of loans to clients

Analysis of loans by credit quality as at 31 December 2018 is provided bellow:

KZT'000	Loans to legal entities	Loans to individuals	Total
Non past due and unimpaired	–	63,494	63,494
Overdue:			
- past due less than 30 days	–	489	489
- past due from 30 to 90 days	–	–	–
- past due from 91 to 180 days	–	–	–
- past due from 181 to 365 days	–	31,829	31,829
- past due from more than one year	1,188,263	197,836	1,386,099
Total past due loans to clients	1,188,263	230,154	1,418,417
Gross loans to clients before allowance for impairment	**1,188,263**	**293,648**	**1,481,911**
Allowance for impairment	(294,151)	(78,907)	(373,058)
Total loans to clients	**894,112**	**214,741**	**1,108,853**

Analysis of loans by credit quality as at 31 December 2017 is provided bellow:

KZT'000	Loans to legal entities	Loans to individuals	Total
Non past due and unimpaired	10,484	130,559	141,043
Overdue:			
- past due less than 30 days	–	–	–
- past due from 30 to 90 days	–	622	622
- past due from 91 to 180 days	36,003	–	36,003
- past due from 181 to 365 days	–	–	–
- past due from more than one year	1,281,548	338,131	1,619,679
Total past due loans to clients	1,317,551	338,753	1,656,304
Gross loans to clients before allowance for impairment	**1,328,035**	**469,312**	**1,797,347**
Allowance for impairment	(291,301)	(102,601)	(393,902)
Total loans to clients	**1,036,734**	**366,711**	**1,403,445**

Collateral analysis

The following table represents analysis of carrying value of loans to clients by type of collateral:

KZT'000	**2018**	**2017**
Loans collateralised by real estate	1,376,297	1,689,498
Loans collateralised by inventory and equipment	55,698	55,698
Loans collateralised by vehicles	41,126	43,263
Unsecured loans	8,790	8,888
Gross loans to clients before allowance for impairment	**1,481,911**	**1,797,347**
Allowance for impairment	(373,058)	(393,902)
Total loans to clients	**1,108,853**	**1,403,445**

As at 31 December 2018, the fair value of collateral is KZT 2,704,442 thousand (2017: KZT 3,098,460 thousand).

5. Loans to clients, continued

Analysis of the loan portfolio by sectors of the economy

The structure of concentration of risk of the Bank's client loan portfolio according to sectors of economy is provided below:

KZT'000	2018	2017
Production	559,953	588,961
Rental services	498,147	508,647
Trade	235,552	282,850
Food services	–	93,919
Construction	55,698	55,698
Other	15,219	15,364
Individuals excluding private entrepreneurs	117,342	251,908
Gross loans to clients before allowance for impairment	**1,481,911**	**1,797,347**
Allowance for impairment	(373,058)	(393,902)
	1,108,853	**1,403,445**

6. Assets held for sale

These include collateral accepted by the Bank against overdue loans to clients, which as expected, would be realised within 12 months. The movement of the assets is as follows:

KZT'000	2018	2017
At 1 January	**247,896**	**166,657**
Transferred from other assets	101,965	89,140
Sold	(1,281)	(7,901)
At 31 December	**348,580**	**247,896**

Assets held for sale with a carrying value of KZT 61,215 thousand are in the custody of the borrower.

The Bank estimates fair value of assets held for sale at each reporting date to avoid a significant difference in the carrying amount of such assets from their fair value less costs to sell.

As at 31 December 2018, the Bank performed estimation of the value of assets held for sale and was satisfied that there were no material differences in their carrying amounts and fair values. The fair value at the date of such measurement was determined using a comparative approach that relates to level 2 in the fair value hierarchy.

7. Other assets

KZT'000	2018	2017
Assets held as repayment of overdue loans to clients	54,694	54,694
Prepayments for services	13,857	29,894
Other	27,732	33,125
	96,283	117,713
Allowance for impairment	(32,906)	(37,751)
	63,377	**79,962**

Assets held as repayment of overdue loans to clients consist of assets recovered by the court decisions for the total amount of KZT 41,788 thousand for which official registration procedures started in 2017 but haven’t been completed (2017: KZT 41,788 thousand), and assets in the possession of the third parties for the total of KZT 12,906 thousand (2017: KZT 12,906 thousand). The management of the Bank believes that all procedures will be completed in 2019.

7. Other assets, continued

The change in the allowance for impairment of other assets is as follows:

KZT'000	2018	2017
At 1 January	37,751	17,838
Accrued	1,292	20,434
Restored	(6,137)	(521)
At 31 December	**32,906**	**37,751**

8. Intangible assets

KZT'000	2018	2017
Cost		
At 1 January	159,522	25,885
Additions	1,629	133,637
At 31 December	161,151	159,522
Amortisation		
At 1 January	(29,889)	(23,996)
Amortisation charge	(398)	(5,893)
At 31 December	(30,287)	(29,889)
Net book value	**130,864**	**129,633**

In 2017, the Bank acquired the right to use the software complex of the integrated banking system RS-Bank V.6 for KZT 127,292 thousand. At the date of approval of the financial statements preparatory work on software integration has not been completed.

9. Amounts due to clients

KZT'000	2018	2017
Current accounts		
Legal entities	84,396	171,688
Individuals	75,912	139,773
	160,308	311,461
Deposits		
Legal entities	1,158	1,219
Individuals	101,711	180,228
	102,869	181,447
	263,177	**492,908**

As at 31 December 2018, the client's funds of the legal entity in the amount of USD 68,955 (2017: nil) are used as collateral for the fulfilment of obligations under the guarantee provided by the Bank for the equivalent amount.

In cases where the term deposit is returned to the depositor upon request before the expiry of the term, the fee is not paid, or is paid at a significantly lower interest rate, depending on the conditions stipulated in the agreement.

As at 31 December 2018 and 2017, the share of the Bank's ten major clients from total balance of amounts due to clients to 67% and 61%, respectively. The total balance of such obligations as at 31 December 2018 and 2017 amounted to KZT 175,299 thousand and KZT 300,976 thousand, respectively.

10. Other liabilities

KZT'000	2018	2017
Creditors for non-core activities	31,083	10,128
Taxes payable	11,139	5,831
Provision for vacation benefits	8,905	10,304
Creditors for banking activities	517	1,138
Other	2,346	2,291
	53,990	**29,692**

Taxes payable are not financial instruments, therefore, for the purposes of disclosure of the financial risk management policy, other liabilities amount to KZT 42,851 thousand (2017: KZT 23,861 thousand).

11. Equity

(a) Share capital

	2018	2017
Number of placed and fully paid shares	8,650	8,650
Nominal value of one share, tenge	500,000	500,000
Share capital, thousand tenge	**4,325,000**	**4,325,000**

As at 31 December 2018 and 2017, the announced number of shares remained the same and amounted to 30,000 ordinary shares. Each share entitles to one vote and an equal right to receive dividends.

In 2017, the increase in share capital was due to the conversion of a subordinated loan in the amount of KZT 234,000 thousand into ordinary shares of the Bank.

In 2018 and 2017, dividends were neither declared nor paid.

(b) Reserve capital

Until the entry into force of the Resolution of the Board of the NBRK No. 137 dated 27 May 2013 “On approval of the Rules for the formation by second-tier banks of the dynamic reserve and determination of the minimum size of the dynamic reserve, the amount of expected losses” the Bank, in accordance with the Resolution of the Board of the Agency of the Republic of Kazakhstan on Regulation and supervision of financial market and financial organisations No. 196 dated 31 January 2011 “On establishing a minimum size of reserve capital of second-tier banks” was obliged to create a reserve capital by transferring the amount from undistributed income to a reserve not subject to distribution.

In 2018 and 2017, transfers to the provision for general banking risk were not affected.

(c) Dynamic reserves

Since 1 January 2018, amendments to the Law of the Republic of Kazakhstan No. 2444 dated 31 August 1995 “On banks and banking activity in the Republic of Kazakhstan” came into force, according to which the requirement to form a dynamic reserve was excluded from this law, in this connection, the Bank reclassified the dynamic reserve to the retained earnings.

(d) Basic loss per share

Basic loss per share is determined by dividing the net loss for the year by the weighted average number of ordinary shares outstanding during the period. The Bank does not have dilutive shares.

	2018	2017
Net loss for the year, thousand tenge	(75,351)	(514,155)
Weighted average number of ordinary shares	8,650	8,187
Basic loss per share, tenge	**(8,711)**	**(62,801)**

12. Interest income

KZT'000	2018	2017
"Reverse REPO" receivables	231,091	270,221
Loans to clients	14,027	38,448
Amounts due from other banks	1,335	1,085
	246,453	**309,754**

13. Interest expenses

The item includes expenses on interest paid on amounts due to clients.

14. Administrative expenses

KZT'000	2018	2017
Payroll and related expenses	247,997	282,880
Office rent	29,711	38,617
Taxes other than income tax	26,751	44,641
Security	7,753	8,735
Transportation	6,755	10,793
Communication services	6,446	7,866
Professional services	3,751	2,464
Technical maintenance	2,647	5,889
Depreciation and amortisation	2,636	7,970
Travel expenses	2,616	2,165
Contributions to Kazakhstan deposit insurance fund	1,557	2,776
Insurance	1,207	1,539
Penalties	2	10,614
Other	23,267	21,062
	363,096	**448,011**

15. Income tax

(a) Income tax recovery

Reconciliation of income tax applicable to the accounting loss before taxation at the statutory income tax rate and income tax recovery at the effective income tax rate for the periods presented is shown below:

KZT'000	2018	2017
Loss before tax	(75,351)	(514,155)
Income tax rate	20.0%	20.0%
At statutory income tax rate	(15,070)	(102,831)
Change in unrecognised deferred tax assets	64,167	136,687
Tax effect non-taxable income and non-deductible expenses	(49,097)	(33,856)
Income tax recovery	**–**	**–**
Effective income tax rate	0.0%	0.0%

15. Income tax, continued

(b) Deferred tax assets and liabilities

KZT'000	2018	2017
Tax losses	292,064	226,187
Property, plant and equipment	(3,584)	(2,233)
Employee related accruals	1,781	2,061
Taxes payable	314	393
	290,575	226,408
Unrecognised deferred tax assets	(290,575)	(226,408)
	–	–

As at 31 December 2018 and 2017, deferred tax assets were not recognised, since it is not probable that sufficient taxable income will be available against which deductible temporary differences can be offset. These assets can be offset for a period of from 3 to 10 years.

16. Financial risk management objectives and policies

(a) Overview

Management of risks is at the core of banking activities and is an essential element of the Bank's operations. Risk management of the Bank is carried out in respect of financial risks (credit risk, liquidity risk and market risk), operational, geographical and legal risks. The main task of managing financial risks is to define risk limits and further ensure compliance with established limits. Management of operational and legal risks should ensure proper compliance with internal regulations and procedures in order to minimise operational and legal risks.

(b) Categories and fair values of financial assets and financial liabilities

Categories of financial assets and financial liabilities

The carrying amounts of financial assets and liabilities of the Bank are as follows:

KZT'000	Note	2018	2017
Financial assets carried at amortised cost			
Cash	3	397,256	503,834
Amounts due from other banks		2,645	2,599
"Reverse REPO" receivables	4	2,686,686	2,655,764
Loans to clients	5	1,108,853	1,403,445
		4,195,440	**4,565,642**
Financial liabilities carried at amortised cost			
Correspondent accounts and amounts due to banks		(747)	(523)
Amounts due to clients	9	(263,177)	(492,908)
Other liabilities	10	(42,851)	(23,861)
		(306,775)	**(517,292)**

Fair value measurement

The fair value of financial assets and liabilities includes the amount at which the instrument can be exchanged in current transactions between willing parties rather than in a forced sale or sale due to liquidation. The Bank does not have financial assets and liabilities that are measured at fair value.

The following methods and assumptions were used to estimate fair value:

- Cash is equal to book value due to the nature of this financial instrument;
- "Reverse REPO" receivables are approximately equal to their book value due to the short maturity of the instrument. They are assigned Level 1 in the fair value hierarchy;
- Loans to clients and term deposits of clients are approximately equal to their book value in view of the fact that the interest rate corresponds to the market rate;
- Amounts due to clients and other liabilities approximate their carrying value due to the short maturity of these instruments. They are assigned Level 3 in the fair value hierarchy.

16. Financial risk management objectives and policies, continued

(c) Credit risk

Credit risk is the risk that the Bank incurs a financial loss due to the failure of the borrower or counterparty to the financial instrument to fulfil its contractual obligations. The Bank manages its credit risk by setting a limit on the amount of risk that the Bank is prepared to accept for individual counterparties, geographical or sectoral concentrations of risk, and by monitoring compliance with established risk limits

The Bank has developed a credit quality verification procedure to ensure early detection of possible changes in the creditworthiness of counterparties, including periodic review of the amount of collateral. Limits on counterparties are determined using a credit risk classification system that assigns a credit rating to each counterparty. Ratings are regularly reviewed. The procedure for checking credit quality allows the Bank to estimate the amount of potential losses on the risks to which it is exposed and take the necessary measures.

Financial assets are classified based on current credit ratings assigned by internationally recognised rating agencies, such as Standard & Poor's Financial Services, Fitch Ratings and Moody's Investors Service. The highest possible rating is AAA.

The carrying amount of financial assets is the maximum exposure to credit risk. Below is information on the maximum exposure to credit risk of certain instruments in the context of credit ratings:

KZT'000	Rated from BB- to BB+	Rated from B- to B+	Rating not assigned	Total
2018				
Cash, excluding cash on hand	1,064	324,317	39,320	364,701
Amounts due from other banks	340	2,305	–	2,645
"Reverse REPO" receivables	–	–	2,686,686	2,686,686
Loans to clients	–	–	1,108,853	1,108,853
	1,404	**326,622**	**3,834,859**	**4,162,885**
2017				
Cash, excluding cash on hand	–	100,790	281,365	382,155
Amounts due from other banks	–	2,599	–	2,599
"Reverse REPO" receivables	–	–	2,655,764	2,655,764
Loans to clients	–	–	1,403,445	1,403,445
	–	**103,389**	**4,340,574**	**4,443,963**

Impairment losses

As indicated in note 2(e), the Bank creates an allowance for impairment of loans to clients, which is a calculated estimate of the amount of losses already incurred. The estimated value of the total loss is determined on the basis of management judgment regarding the recoverability of the assets.

	2018		**2017**	
KZT'000	Gross	Allowance	Gross	Allowance
Non past due and unimpaired	63,494	–	141,043	–
Overdue:				
- past due less than 30 days	489	–	–	–
- past due from 30 to 90 days	–	–	622	–
- past due from 91 to 180 days	–	–	36,003	–
- past due from 181 to 365 days	31,829	–	–	–
- past due from more than one year	1,386,099	373,058	1,619,679	393,902
	1,481,911	**373,058**	**1,797,347**	**393,902**

As at 31 December 2018 and 2017, ten major borrowers or groups of interrelated borrowers of the Bank accounted for 87.0% and 79.4% of the total loan portfolio, respectively, before allowance for impairment, which represents a significant concentration. The total debt of these loans as at 31 December 2018 and 2017 amounted to KZT 1,291,160 thousand and KZT 1,427,133 thousand, respectively.

16. Financial risk management objectives and policies, continued

Geographical concentration

The major part of the Bank's financial assets is in Kazakhstan. The Bank monitors its risk to the legal environment in all countries in which it owns assets and assesses the potential impact on the Bank's activities. In particular, the Bank monitors sovereign credit risk established by international credit rating agencies. A risk manager regularly monitors financial and political news in the international mass media to prevent any possible negative effect on the Bank's exposure to risk. This approach allows the Bank to minimise possible losses due to changes in investment climate in the countries where the Bank owns assets.

Information on geographical concentration of financial assets and liabilities as at 31 December 2018 and 2017 is presented below:

KZT'000	Kazakhstan	Other countries	Total
2018			
Cash, excluding cash on hand	40,385	324,316	364,701
Amounts due from other banks	2,645	–	2,645
"Reverse REPO" receivables	2,686,686	–	2,686,686
Loans to clients	1,108,853	–	1,108,853
Correspondent accounts and amounts due to banks	–	(747)	(747)
Amounts due to clients	(263,177)	–	(263,177)
Other liabilities	(42,851)	–	(42,851)
	3,532,541	**323,569**	**3,856,110**
2017			
Cash, excluding cash on hand	142,060	240,095	382,155
Amounts due from other banks	2,599	–	2,599
"Reverse REPO" receivables	2,655,764	–	2,655,764
Loans to clients	1,403,445	–	1,403,445
Correspondent accounts and amounts due to banks	–	(523)	(523)
Amounts due to clients	(492,908)	–	(492,908)
Other liabilities	(23,861)	–	(23,861)
	3,687,099	**239,572**	**3,926,671**

Credit–related commitments risks

The Bank makes available to its customers guarantees that may require that the Bank makes payments on their behalf and enters into commitments to extend credit lines to secure their liquidity needs. Letters of credit and guarantees (including standby letters of credit) commit the Bank to make payments on behalf of customers in the event of a specific act, generally related to the import or export of goods. Such commitments expose the Bank to similar risks to loans and are mitigated by the same control processes and policies.

(d) Liquidity risk and funding management

Liquidity risk is the risk of difficulties in obtaining the funds to meet deposit withdrawals and other financial commitments associated with financial instruments as they actually fall due.

The Committee on management of active – passive transactions and a risk manager control liquidity risk by means of maturity analysis, determining the Bank's strategy for the next financial period. Management of current liquidity is carried out by the Treasury that makes transactions in money markets to maintain the current liquidity and optimisation of cash flows.

In order to manage liquidity risk, the Bank performs daily monitoring of future expected cash flows on client and banking operations which is included in the process of asset and liability management. The Bank's management board sets limits in terms of minimum proportion of maturing funds available to meet deposit withdrawals, and on the minimum level of interbank and other borrowing facilities that should be in place to compensate withdrawals of deposits at unexpected levels.

16. Financial risk management objectives and policies, continued

Maturity of financial assets and liabilities

The following table provides an analysis of the Bank's financial assets and liabilities by expected maturity:

KZT'000	Due on demand	Less than 3 months	3 to 12 months	1 to 5 years	Total
2018					
Cash	397,256	–	–	–	397,256
Amounts due from other banks	2,305	–	340	–	2,645
"Reverse REPO" receivables	–	2,699,336	–	–	2,699,336
Loans to clients	–	–	81,259	1,079,420	1,160,679
Correspondent accounts and amounts due to banks	(747)	–	–	–	(747)
Amounts due to clients	(165,520)	–	(97,657)	–	(263,177)
Other liabilities	–	(33,946)	(8,905)	–	(42,851)
	233,294	**2,665,390**	**(24,963)**	**1,079,420**	**3,953,141**
2017					
Cash	503,834	–	–	–	503,834
Amounts due from other banks	605	1,994	–	–	2,599
"Reverse REPO" receivables	–	2,657,126	–	–	2,657,126
Loans to clients	–	–	63,889	1,357,640	1,421,529
Correspondent accounts and amounts due to banks	(523)	–	–	–	(523)
Amounts due to clients	(329,659)	(33,558)	(129,691)	–	(492,908)
Other liabilities	–	(13,557)	(10,304)	–	(23,861)
	174,257	**2,612,005**	**(76,106)**	**1,357,640**	**4,067,796**

“Reverse REPO” receivables and loans to clients include expected future interest payments calculated on the basis of interest rates effective on the balance sheet date.

(e) Operational risk

Operating risk is the risk arising from a systemic failure, personnel errors, fraud or external events. When the control system ceases to function, operating risks can damage reputation, have legal consequences or lead to financial losses. The Bank cannot claim that all operational risks have been eliminated, but through the monitoring system and by monitoring and responding to potential risks, the Bank can manage such risks. The control system stipulates effective segregation of duties, access rights, approval and reconciliation procedures, training of personnel, and evaluation procedures, including internal audit. The management is responsible for managing the operational risk inherent in the Bank's products, activities, procedures and systems. In the process of work, compliance officers monitor the consistency and effectiveness of control over the risk of non-compliance with the Bank's regulatory requirements.

(f) Market risk

Market risk is the risk that the fair value of future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, exchange rates and equity prices. Market risk is managed and monitored using sensitivity analysis.

The Bank manages market risk by setting limits on the open position in relation to the size of the portfolio for individual financial instruments, the timing of changes in interest rates, currency position, and loss limits. The Bank regularly monitors such positions, which are updated and approved by the Board and the Board of Directors of the Bank.

(g) Currency risk

Currency risk is the risk of losses arising from changes in foreign exchange rates when the Bank conducts its business. The risk of losses arises from the revaluation of the Bank's currency positions in monetary terms. The Bank has assets and liabilities denominated in several foreign currencies. Currency risk arises when the available or foreseen assets expressed in a foreign currency are greater or less than the amount of existing or forecasted liabilities in the same currency.

16. Financial risk management objectives and policies, continued

The Bank manages currency risk by setting limits on open positions of financial instruments, maturity and currency, which are monitored on a regular basis, reviewed and approved by the authorised body of the Bank.

The Bank monitors compliance with established currency limits on a daily basis.

Exposure to currency risk

The Bank's exposure to currency risk, based on conditional (nominal) values, was as follows:

KZT'000	KZT	EUR	USD	RUB	Total
2018					
Cash	54,302	11,475	330,682	797	397,256
Amounts due from other banks	340	–	2,305	–	2,645
"Reverse REPO" receivables	2,686,686	–	–	–	2,686,686
Loans to clients	1,108,853	–	–	–	1,108,853
Correspondent accounts and amounts due to banks	(747)	–	–	–	(747)
Amounts due to clients	(84,295)	(167,166)	(11,714)	(2)	(263,177)
Other liabilities	(42,851)	–	–	–	(42,851)
	3,722,288	**(155,691)**	**321,273**	**795**	**3,888,665**
2017					
Cash	104,373	19,739	378,646	1,076	503,834
Amounts due from other banks	605	–	1,994	–	2,599
"Reverse REPO" receivables	2,655,764	–	–	–	2,655,764
Loans to clients	1,403,445	–	–	–	1,403,445
Correspondent accounts and amounts due to banks	(523)	–	–	–	(523)
Amounts due to clients	(151,133)	(318,259)	(23,513)	(3)	(492,908)
Other liabilities	(23,861)	–	–	–	(23,861)
	3,988,670	**(298,520)**	**357,127**	**1,073**	**4,048,350**

Financial instruments denominated in tenge are not exposed to foreign currency risk and are provided for reconciliation of total amounts.

Sensitivity analysis

The weakening of tenge by 10 percent against the currencies listed below as at December 31 would have resulted in a (increase) decrease of loss before tax by the amounts indicated below, and the strengthening of tenge by the indicated 10 percent would have resulted in an equivalent but opposite effect. This analysis assumes that all other variables remain constant.

KZT'000	2018	2017
EUR	(15,569)	(29,852)
USD	32,127	35,713
RUB	80	107

(h) Interest rate risk

The Bank assumes the risk associated with the effect of adverse fluctuations in market interest rates on its financial position and cash flows. Such fluctuations may increase the level of interest margin, but in the event of unexpected changes in interest rates, interest margin may decrease and cause losses. Management sets limits on the acceptable level of discrepancies in interest rates and monitors compliance with established limits on a regular basis.

The Bank uses gap analysis to manage interest rate risk. The Bank groups financial assets and financial liabilities by maturity or interest rate repricing, whichever occurs first, and calculates the gap for each group. The positive value of the gap means that an increase in interest rates with a certain maturity will lead to an increase in net interest income (a decrease in interest rates will lead to a decrease in net interest income). The negative value of the gap means that an increase in interest rates with a certain maturity will result in a decrease in net interest income (a decrease in interest rates with a certain maturity will lead to an increase in net interest income).

16. Financial risk management objectives and policies, continued

When interest rates are expected to increase, the Bank increases the maturity of debt, reduces fixed-rate loans, reduces the maturity of the investment portfolio, reduces investment in securities and reduces credit lines. When interest rates are expected to fall, the Bank reduces the terms of debt repayment, increases loans with a fixed rate, increases the maturity of the investment portfolio and increases credit lines.

To manage the risk of interest rate effect on fair value, the Bank uses periodic assessment of potential losses that can be incurred as a result of negative changes in the market conditions. The risk department monitors the current financial performance of the Bank, assesses the Bank's vulnerability to the risk of the effect of the interest rate on fair value and impact on the Bank's income.

Sensitivity analysis

Increase in interest rates by 100 basis points in relation to the following items of the statement of financial position as at 31 December would result in a (decrease) increase in net loss for the amounts indicated below, and a decrease in interest rates on the 100 basis points indicated would have an equivalent, but opposite effect. This analysis assumes that all other variables remain unchanged.

KZT'000	2018	2017
Amounts due from other banks	26	26
"Reverse REPO" receivables	26,867	26,558
Loans to clients	11,089	14,034
Correspondent accounts and amounts due to banks	(7)	(5)
Amounts due to clients	(2,632)	(4,929)
	35,343	**35,684**

(i) Price risk

The Bank is not exposed to the price risk due to lack of transactions with financial instruments that are sensitive to changes in prices in the market.

17. Capital management

The Bank maintains an active management of adequacy of capital base for protection against risks inherent in the nature of its business. The Bank's sufficiency of capital is monitored using, amongst other measures, norms established by the legislation of the Republic of Kazakhstan.

The main purpose of capital management for the Bank is to ensure that the Bank adheres to external capital requirements and maintains a high credit rating and capital adequacy ratios required to carry out activities.

The Bank manages the structure of its capital and adjusts it to changes in economic conditions and risk characteristics of the activities. Compared to the previous year, there have been no changes for the purposes, policies and procedures of capital management, but the Board of Directors constantly pays attention to this issue.

In accordance with the effective capital requirements, set by the NBRK, the Bank must maintain a capital adequacy coefficient (k1-1) of not lower than 0.055, a Tier 1 capital adequacy coefficient (k1-2) of not lower than 0.065 and a capital adequacy coefficient (k2) of not lower than 0.08.

As at 31 December 2018, the Bank's capital adequacy coefficient values calculated in accordance with the NBRK's requirements exceeded the regulatory minimum and amounted to: k1-1 was equal to 1.009; k1-2 was equal to 1.009; k2 was equal to 1.009.

18. Commitments and contingencies

(a) Taxation contingencies in Kazakhstan

Inherent uncertainties in interpreting tax legislation

The Bank is subject to uncertainties relating to the determination of its tax liabilities. Tax legislation and practice in Kazakhstan are in a state of continuous development and, therefore, are subject to varying interpretations and changes.

The management interpretations of such legislation in applying it to business transactions of the Bank may be challenged by the relevant tax authorities and, as a result, the Bank may be claimed for additional tax payments, including fines, penalties and interest charges that could have a material adverse effect on the Bank's financial position and results of operations.

Period for additional tax assessments

The tax authorities are able to raise additional tax assessments for five years after the end of the relevant tax period concerning all taxes. In certain cases, as determined by the tax legislation, the terms could be extended for three years.

Possible additional tax liabilities

The management believes that the Bank is in compliance with the tax laws enacted in Kazakhstan and tax conditions of concluded contracts that affect its operations and no additional tax liabilities will arise. However, due to the reasons set out above, the risk remains that the relevant tax authorities may take a differing position with regard to the interpretation of contractual provisions or tax law.

The resulting effect of this matter is that additional tax liabilities may arise. However, due to the range of uncertainties described above in assessing any potential additional tax liabilities, it is not practicable for the management to estimate the financial effect in terms of the amount of additional tax liabilities, if any, together with any associated penalties and charges for which the Bank may be liable.

(b) Credit related commitments

The main purpose of these instruments is to ensure the provision of funds to customers as necessary. Commitments to extend loans include the unused portion of amounts approved by the authorised body of the Bank to provide borrowings in the form of loans, guarantees or letters of credit. With respect to loan commitments, the Bank is potentially exposed to the risk of incurring losses in an amount equal to the total amount of unused liabilities.

The Bank monitors the time remaining until maturity of credit related commitments, as usually longer-term liabilities have a higher level of credit risk than short-term liabilities.

As at 31 December 2018, the amount of the uncovered guarantee issued by the Bank was equal to USD 68,955 (equivalent to KZT 26,493 thousand), which was fully secured by the client's funds (see note 9).

(c) Obligations to the authorised body (the NBRK)

In accordance with the Resolution of the Board of the NBRK dated 29 February 2016 No. 69 "On the establishment of factors affecting the deterioration of the banking financial position of the and the banking conglomerate, as well as the approval of the rules for the application of early response measures and methods for determining factors affecting the deterioration of the banking financial position and banking conglomerate", one of the factors affecting the worsening of the Bank's financial position is the excess of the ratio of loans in arrears on principal and (or) accrued remuneration in excess of ninety (90) calendar days net of allowance, to the total loan portfolio net of allowance, that is, the NPL should not exceed 10%. During a comprehensive audit, the Bank's activities carried out by the NBRK in 2017, the NBRK indicated a significant excess of the NPL above the established standards. The Bank's management believes that the Bank has sufficient resources to reduce this indicator and, accordingly, agree on an action plan with the NBRK, and therefore the negative impact of these circumstances on the Bank's financial statements is unlikely.

(d) Insurance

The insurance industry in Kazakhstan is in a developing stage and many forms of insurance protection common in other parts of the world are not yet generally available. Available insurance programs may not provide full coverage in the event of a major loss.

(e) Legal commitments

In the ordinary course of business, the Bank is subject to legal actions and complaints. The management believes that the ultimate liability, if any, arising from such actions or complaints will not have a materially adverse effect on the financial condition or results of operations of the Bank. As at 31 December 2018 the Bank was not involved in any significant legal trials.

19. Related party disclosures

In accordance with IAS 24 “Related Party Disclosures”, parties are considered to be related, one of which is able to control or significantly affect the operating and financial decisions of the other party. When deciding whether the parties are related, the content of the relationship between the parties is taken into account, and not only their legal form.

Related parties may enter into transactions that are not conducted between unrelated parties. The prices and terms of such transactions may differ from the prices and terms of transactions between unrelated parties.

(a) Management remuneration

Remuneration received by key executives are included in personnel costs (see note 14) and amounted to KZT 97,414 thousand (2017: KZT 63,426 thousand).

(b) Transactions with related parties

KZT'000	Companies under common control	Key management personnel
2018		
Cash	324,316	–
Correspondent accounts and amounts due to banks	(747)	–
Amounts due to clients	–	(5,238)
2017		
Cash	240,095	–
Correspondent accounts and amounts due to banks	(523)	–
Amounts due to clients	–	(2,334)

The Bank does not have significant income and expenses related to transactions with related parties.

(c) Terms and conditions of transaction with related parties

Prices for related party transactions are determined by the parties on an ongoing basis depending on the nature of the transaction.

20. Significant accounting policies

The following significant accounting policies have been consistently applied in the preparation of the financial statements.

(a) Cash

Cash includes cash banknotes and coins, free balances (Nostro accounts) in the NBRK and other banks.

(b) Financial instruments

Date of recognition

Financial assets and liabilities, with the exception of loans and advances to customers and amounts due to clients, are initially recognised on the trade date, i.e., on the date when the Bank becomes a party to the contractual provisions of the instrument. Standard acquisitions or sales are the acquisitions or sales of financial assets that require delivery during a period, usually determined by the rules or regulations adopted in the market.

Loans and advances to customers are recognised when funds are transferred to the customers’ account. The Bank recognises due to customer balances when funds reach the Bank.

Recognition and measurement

Classification of financial instruments at initial recognition depends on the contractual terms and business model used to manage the instruments. Financial instruments are initially measured at fair value, including or excluding transaction costs, unless financial assets and financial liabilities are measured at fair value through profit or loss. Trade receivables are valued at the transaction price. If the fair value of financial instruments at initial recognition differs from the transaction price, the Bank considers the profit or loss of the first day, as described below.

20. Significant accounting policies, continued

Starting from 1 January 2018, the Bank classifies all its financial assets on the basis of the business model used for asset management and the contractual terms of the assets as assessed by:

- amortised value;
- fair value through other comprehensive income;
- fair value through income or loss.

Financial liabilities, other than commitments to provide loans and financial guarantees, are measured at amortised cost or at fair value through profit or loss if they are intended for trading and derivatives, or at the discretion of the organisation are classified as fair value.

Derecognition

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

- the rights to receive cash flows from the asset have expired;
- the Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- the Bank either has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has not transferred control of the asset.

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

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

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in profit or loss.

Impairment of financial assets

The Bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired.

A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred “loss event”) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulties, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

20. Significant accounting policies, continued

Day 1 profit or loss

When the transaction price differs from the fair value of other observable current market transactions in the same instrument, or based on a valuation technique with the variables including only data from observable markets, the Bank immediately recognises the difference between the transaction price and fair value (a Day 1 profit or loss) in profit or loss. In cases where fair value is determined using data which is not observable, the difference between the transaction price and model value is only recognised in profit or loss when the inputs become observable, or when the instrument is derecognised.

Determination of fair value

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

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

Offsetting

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position only if, there is a legally enforceable right to offset the recognised amounts and there is an intention to realise the asset and settle the liability simultaneously.

Reconstruction of loans

The Bank seeks to restructure loans rather than to take possession of collateral, for example, extending the payment arrangements and the agreement of new loan condition.

The accounting treatment of such restructuring is as follows:

- If the loan restructuring is not caused by the financial difficulties of the borrower, the Bank uses same approach as for financial liabilities described below;
- If the loan restructuring is due to the financial difficulties of the borrower and the loan is considered impaired after the restructuring the Bank recognises the difference between the present value of future cash flows under the new terms, discounted at the original effective interest rate and the carrying amount before restructuring as part of the allowance for impairment in the period. If the loan is not impaired as a result of the restructuring, the Bank recalculates the effective interest rate.

Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loan continues to be subject to individual or collective impairment assessment, calculated using the loan’s original or current effective interest rate.

(c) Property, plant and equipment

Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to a working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located, and capitalised borrowing costs

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Any gain (loss) on disposal of an item of property, plant and equipment is determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment, and is recognised net within other income (other expenses) in profit or loss.

Subsequent costs

The cost of replacing a component of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the component will flow to the Bank, and its cost can be measured reliably. The carrying amount of the replaced component is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in profit or loss as incurred.

20. Significant accounting policies, continued

Depreciation

Depreciation is charged to profit or loss on a straight-line basis over the estimated useful life of the individual asset to its estimated residual value:

- vehicles 6 – 7 years;
- computers 2 – 3 years;
- other 6 – 7 years.

Useful lives and residual values of property, plant and equipment are analysed at each reporting date.

(d) Intangible assets

Intangible assets include software and licenses. Intangible assets are recognised at acquisition at cost. After initial recognition, intangible assets are measured at cost less accumulated amortisation and accumulated impairment losses.

Intangible assets are amortised on a straight-line basis over their useful economic lives. The expected useful lives of the assets are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The estimated useful life of intangible assets is 5 – 7 years.

(e) Impairment of non-financial assets

The carrying amounts of non-current assets are reviewed for impairment if events or changes in circumstances indicate the carrying value may not be recoverable. If there are indicators of impairment, an exercise is undertaken to determine whether the carrying values are in excess of their recoverable amount. Such review is undertaken on an asset-by-asset basis, except where such assets do not generate cash flows independent of other assets, in which case the review is undertaken at the cash generating unit level.

If the carrying amount of an asset or its cash-generating unit exceeds the recoverable amount, an allowance is recorded to reflect the asset or cash-generating unit at the lower amount. Impairment losses are recognised in profit or loss.

Calculation of recoverable amount

The recoverable amount of assets is the greater of their value in use and fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. The Bank's cash-generating units are the smallest identifiable groups of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

Reversals of impairment

A previously recognised impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

(f) Non-current assets held for sale

Non-current assets (or disposal group's) classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell. Non-current assets (or disposal groups) are classified as held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition, management has committed to the sale, and the sale is expected to have been completed within one year from the date of classification.

(g) Provisions

Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Unwinding of discounts on provisions is recognised as finance costs.

20. Significant accounting policies, continued

(h) Retirement employee benefits

The Bank does not have any pension arrangements separate from the state pension system of the Republic of Kazakhstan, which requires current contributions by the employer and employee calculated as a percentage of current gross salary payments.

(i) Equity

Share capital

The share capital is recorded by the Bank as the total nominal value of issued and paid-up shares. Any amounts paid in excess of the par value of ordinary shares are recognised as share seigniorage benefits.

Assets contributed to share capital are recognised at fair value at the time of transaction. The amount of any excess of the fair value of funds received over the notional value of the contribution to the share capital at the time of its legal registration credited directly to equity as additional paid-in capital.

Dividends

Dividends are recognised as a liability and deducted from equity at the accounting date only if they are declared before the accounting date. Information on dividends is disclosed in the financial statements when they are proposed before the accounting date, also recommended or declared after the accounting date but before approval of the financial statement.

(j) Recognition of income and expenses

For all financial instruments measured at amortised cost, interest income or expense is recorded at the effective interest rate when discounting at which the expected future cash payments or receipts throughout the expected term of the financial instrument or during a shorter period of time, where appropriate, to exactly yield a net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, a right for early redemption) and commissions or additional expenses directly associated with the instrument, which are an integral part of the effective interest rate, but are not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

In the case of reduction disclosed in the financial statements value of the financial asset or group of similar financial assets due to impairment, interest income continues to be recognised using the original effective interest rate based on the new carrying value.

(k) Income tax

Income tax for the year comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items charged or credited directly to equity, in which case it is recognised in equity.

Current tax expense is the expected tax payable on the taxable income for the year and any adjustment to tax payable in respect of previous years.

Deferred tax is determined using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes, and the amounts used for taxation purposes.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on the tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred tax asset is recognised only to the extent that it is probable to receive taxable income in future, which can be utilised against this asset. Amount of deferred tax assets are reduced to the extent that it is not probable that appropriate tax savings would be used.

Deferred tax assets and liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

20. Significant accounting policies, continued

(l) Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency of the Bank at exchange rate ruling at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies are retranslated to the functional currency at the exchange ruling rate at the reporting date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate ruling at the date when their fair value was determined. Foreign currency differences arising on retranslation at the exchange rate on

the date of the transaction as well as those from retranslation of monetary assets and liabilities at the reporting date are recognised in profit or loss.

The following exchange rates were used in preparing the financial statements:

		2018		2017
	Year-end	Average	Year-end	Average
USD	384.20	344.71	332.33	326.00
EUR	439.37	406.66	398.23	368.32
RUB	5.52	5.50	5.77	5.59

21. Events after the balance sheet date

As disclosed in note 2(e), in January 2019, the Bank has completed the coordination procedure with the NBRK on the new methodology for calculating allowance (reserves) in accordance with IFRS 9.

In February 2019, the Bank has decided to change its legal address to 105 Dostyk Ave., Medeu district, Almaty and close its branch in Karaganda.