JSC MICROFINANCE ORGANISATION

EURO CREDIT

FINANCIAL STATEMENTS

Together with Independent Auditors’ Report

For the year ended 31 December 2018

CONTENTS:

INDEPENDENT AUDITOR'S REPORT 3

FINANCIAL STATEMENTS

STATEMENT OF COMPREHENSIVE INCOME 5
STATEMENT OF FINANCIAL POSITION 6
STATEMENT OF CHANGES IN EQUITY 7
STATEMENT OF CASH FLOWS 8

NOTES TO THE FINANCIAL STATEMENTS

1. General information 9
2. Basis of preparation 9
3. Summary of significant accounting policies 11
4. Critical accounting estimates and judgements 20
5. Effects of changes in accounting policies 21
6. Prior period adjustments 21
7. Other contributions by owners 22
8. Other income 22
9. Financial services 22
10. General and administrative expenses 23
11. Salaries and other employee benefits 23
12. Taxation 23
13. Cash and cash equivalents 24
14. Loans to customers 24
15. Borrowings and subordinated borrowings 26
16. Other liabilities 27
17. Share capital 27
18. Commitments and contingencies 27
19. Financial instruments – risk management 28
20. Management of capital 31
21. Transactions with related parties 31
22. Events after the reporting period 32

INDEPENDENT AUDITOR'S REPORT

To the Shareholders and Management of JSC MICROFINANCE ORGANISATION EURO CREDIT

Qualified Opinion

We have audited the financial statements of **JSC MICROFINANCE ORGANISATION EURO CREDIT** (hereinafter - the Organisation), which comprise the statement of financial position as at 31 December 2018, and the statement of comprehensive income, changes in equity and 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 matters 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 Organisation 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 (IFRSs).

Basis for Qualified Opinion

Effective interest rate was not used for loans to customers which were overdue during 2017. Instead, the original schedules of repayments were used for interest accruals, which constitutes a departure from IFRSs. The extrapolated effect of the abovementioned departure from IFRSs amounted to GEL607,658. Our audit opinion on the financial statements for the period ended 31 December 2017 was modified accordingly. Our opinion on the current period's financial statement is also modified because of the possible effect of this matter on the comparability of the current period's figures and the corresponding figures.

As disclosed in Note 15, the Organisation received borrowings from related parties under common control. As at 31 December 2018, 2017 and 1 January 2017 borrowings are stated in the statement of financial position with amounts GEL14,434,665, GEL62,245,777 and GEL24,786,856, respectively. We did not receive sufficient appropriate audit evidence whether those borrowings were recognised using effective interest rate as at 31 December 2018, 2017 and 1 January 2017. Because of this matter, we were unable to determine whether any adjustments might have been found necessary in respect of borrowings and the elements making up the financial statements.

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Organisation in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Georgia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

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

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 Organisation'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 Organisation or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organisation'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 Organisation's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Organisation to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of 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.

The engagement partner responsible for the audit resulting in this independent auditor's report is:

Ivane Zhuzhunashvili (Registration # SARAS-A-720718)

For and on behalf of BDO LLC

Tbilisi, Georgia

24 September 2019

BDO

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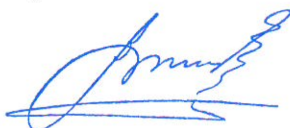

Ivane Zhuzhunashvili (Registration # SARAS-A-720718)

For and on behalf of BDO LLC

Tbilisi, Georgia

24 September 2019

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2018

(In Georgian Lari)

	Note	2018	2017 Restated
Interest income		35,175,167	28,669,914
Interest expense		(10,701,137)	(9,684,411)
Net interest income before impairment		**24,474,030**	**18,985,503**
Loan impairment charge	14	(3,157,081)	-
Net interest income		**21,316,949**	**18,985,503**
Other income	8	7,580,418	3,740,299
Financial services	9	(133,550)	(5,190,656)
General and administrative expenses	10	(6,758,171)	(2,628,421)
Salaries and other employee benefits	11	(5,087,334)	(3,041,892)
Net loss on foreign exchange operations		(2,622,427)	(2,124,509)
Profit before income tax		**14,295,885**	**9,740,324**
Income tax expense	12	(3,110,756)	(1,359,379)
Total comprehensive income		**11,185,129**	**8,380,945**

The financial statements for the year ended 31 December 2018 were approved on behalf of the management on 24 September 2019 by:

Director ____________________ Mikheil Nonikashvili

Financial Manager ____________________ Guja Tsintsadze

The notes on pages 9-32 form an integral part of these financial statements.

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(In Georgian Lari)

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Financial Manager Guja Tsintsadze

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As at 31 December 2018

(In Georgian Lari)

	Note	31 December 2018	31 December 2017 Restated	1 January 2017
Assets				
Cash and cash equivalents	13	2,341,764	1,120,403	964,685
Loans to customers	14	39,933,649	69,013,753	22,609,956
Property and equipment		288,505	31,898	-
Other assets		158,669	24,110	-
Deferred tax asset	12	103,242	146,518	196,711
Total assets		**42,825,829**	**70,336,682**	**23,771,352**
Liabilities				
Borrowings	15	14,434,665	62,245,777	24,786,856
Subordinated borrowings	15	7,148,561	-	-
Other liabilities	16	1,379,614	595,193	270,657
Taxes Payable		1,727,944	400,928	-
Total liabilities		**24,690,784**	**63,241,898**	**25,057,513**
Equity				
Share capital	17	500,000	250,000	250,000
Retained earnings/(Accumulated losses) and other reserves		17,635,045	6,844,784	(1,536,161)
Total equity		**18,135,045**	**7,094,784**	**(1,286,161)**
Total liabilities and equity		**42,825,829**	**70,336,682**	**23,771,352**

The notes on pages 9-32 form an integral part of these financial statements.

	Share capital	Retained earnings/(Accumulated losses) and other reserves	Total
At 1 January 2017	**250,000**	**(1,536,161)**	**(1,286,161)**
Total comprehensive income (restated)	-	8,380,945	**8,380,945**
At 31 December 2017	**250,000**	**6,844,784**	**7,094,784**
Change in accounting policy – IFRS 9 Financial Instruments	-	(16,673,107)	**(16,673,107)**
At 1 January 2018 as restated	**250,000**	**(9,828,323)**	**(9,578,323)**
Transactions with owners	-	16,541,397	**16,541,397**
Increase of share capital	250,000	-	**250,000**
Dividend	-	(263,158)	**(263,158)**
Total comprehensive income	-	11,185,129	**11,185,129**
At 31 December 2018	**500,000**	**17,635,045**	**18,135,045**

*Information about transactions with owners is disclosed in Note 7.

STATEMENT OF CASH FLOWS

For the year ended 31 December 2018

(In Georgian Lari)

	Note	2018	2017 Restated
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income tax		14,295,885	9,740,324
Adjustments for:			
Change in interest accruals, net		3,548,925	2,685,595
Loan impairment charge	14	3,157,081	-
Depreciation		40,566	-
Net loss on foreign exchange operations		2,622,427	2,124,509
Cash flows from operating activities before changes in operating assets and liabilities		23,664,884	14,550,428
Movements in working capital:			
Increase in loans to customers		(1,720,043)	(35,029,724)
Increase in other assets		(135,067)	(56,008)
Increase in other liabilities		780,037	355,389
Increase in tax liabilities		533,982	-
Cash flows from operating activities before taxation		23,123,793	(20,179,915)
Income tax paid		(2,274,446)	(908,259)
Net cash inflow/(outflow) from operating activities		20,849,347	(21,088,174)
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property and equipment		(297,173)	(31,898)
Cash outflow from investing activities		(297,173)	(31,898)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from borrowings		2,814,738	26,920,863
Repayment of borrowings		(22,097,405)	(5,450,072)
Increase in share capital		250,000	-
Dividends		(263,158)	-
Net cash inflow/(outflow) from financing activities		(19,295,825)	21,470,791
Net increase in cash and cash equivalents		1,256,349	350,719
Cash and cash equivalents at the beginning of the year	13	1,120,403	964,685
Effect of changes in foreign exchange rate on cash and cash equivalents		(34,988)	(195,001)
Cash and cash equivalents at the end of the year	13	2,341,764	1,120,403

Interest paid and received by the Organisation during the year ended December 31, 2018 amounted to GEL263,048 and GEL28,286,003, respectively.

Interest received by the Organisation during the year ended December 31, 2017 amounted to GEL21,671,098.

1. GENERAL INFORMATION

A) ORGANISATION

JSC MFO EURO CREDIT is a Joint Stock Company (the "Organisation") which was registered on 22 November 2011 at tax department office in Tbilisi, Georgia with the registration number 404919102. However, the first transaction was conducted in 2014 (contribution to Share capital), the same year when the Organisation was registered as Micro Finance Organisation.

The Organisation changed their legal form from Limited Liability Company to Joint Stock Company on 25 December 2018.

The Organisation conducts its business under the Law of Microfinance Activity and is regulated by the National Bank of Georgia ("NBG").

As its principal business activity, the Organisation provides micro and small loans (secured by the automobiles) to customers in Georgia.

The Organisation's governing body is the general meeting of shareholders. Daily activities in each branch are supervised by the branch manager appointed by the Organisation's supervisory board and nominated by the CEO.

The Organisation had 9 branches in major cities of Georgia as at 31 December 2018.

The shareholders of the organisation as at 31 December 2018, 2017 and 1 January 2017 can be presented as follows:

Shareholders	31 December 2018	31 December 2017	1 January 2017
Zuk China Stone Works Limited	75.51%	75.51%	75.51%
Mody Import & Marketing Ceramics LTD	7.99%	7.99%	7.99%
Iosef Reuven Grenikas	6.5%	9.5%	9.5%
Uri Zuk	5%	5%	5%
Oren Duanias	3%	-	-
Eyal Duanias	2%	2%	2%
Total	**100%**	**100%**	**100%**

Moshe Zuk was the ultimate controlling party of the Organisation as at 31 December 2018, 2017 and 1 January 2017.

The Organisation's office is located at 11 Saakadze street, 2nd pass, Tbilisi, Georgia.

B) CHANGES IN GEORGIAN LEGISLATION

According to the decision of the President of Georgia, from 1 September 2018 after granting loan to customer, effective interest rate between the parties should not exceed 50% during the year (instead of 100% as it was stated previously).

2. BASIS OF PREPARATION

STATEMENT OF COMPLIANCE

These financial statements have been prepared in accordance with International Financial Reporting Standards, International Accounting Standards and Interpretations (collectively IFRSs).

The Organisation maintains its records and prepares financial statements in Georgian Lari (GEL), which is also the Organisation's functional currency.

The reporting period for the Organisation is the calendar year from January 1 to December 31.

Amounts in the financial statements are presented without rounding, unless otherwise stated.

The preparation of financial statements in compliance with adopted IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in applying The Organisation's accounting policies. The areas where significant judgments and estimates have been made in preparing the financial statements and their effect are disclosed in Note 4.

2. BASIS OF PREPARATION (CONTINUED)

BASIS OF MEASUREMENT

These financial statements have been prepared under the historical cost basis.

GOING CONCERN

These financial statements have been prepared on the assumption that the Organisation is a going concern and will continue its operations for the foreseeable future. The management believes that the going concern assumption is appropriate for the Organisation.

ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

a) New standards, interpretations and amendments effective from 1 January 2018

New standards impacting the Organisation that will be adopted in the annual financial statements for the year ended 31 December 2018, and which have given rise to changes in the Organisation's accounting policies are:

- IFRS 9 - Financial Instruments (IFRS 9); and
- IFRS 15 - Revenue from Contracts with Customers (IFRS 15)

The Organisation adopted IFRS 9 and IFRS 15 with a transition date of 1 January 2018. The Organisation has chosen not to restate comparatives on adoption of IFRS 9 and IFRS 15, therefore changes are not reflected in the restated prior year financial statements. Rather, these changes have been processed at the date of initial application (i.e. 1 January 2018) and recognised in the opening equity balances.

The Organisation has not made any adjustments for adopting IFRS 15, as new standard has no significant impact on the opening equity balances, while adoption differences for IFRS 9 brings fundamental changes to the accounting for financial assets. Details are disclosed in Note 3 and Note 4.

b) New standards, interpretations and amendments not yet effective

There are a number of standards, amendments to standards, and interpretations which have been issued by the IASB that are effective in future accounting periods that the Organisation has decided not to adopt early. The most significant of these is:

- IFRS 16 Leases (mandatorily effective for periods beginning on or after 1 January 2019)

The Organisation has progressed its projects dealing with the implementation of this key new accounting standard and is able to provide the following information regarding its likely impact:

IFRS 16 Leases

Adoption of IFRS 16 will result in the Organisation recognising right-of-use assets and lease liabilities for all contracts that are, or contain, a lease. For leases currently classified as operating leases, under current accounting requirements the Organisation does not recognise related assets or liabilities, and instead spreads the lease payments on a straight-line basis over the lease term, disclosing in its annual financial statements the total commitment.

The Board has decided it will apply the modified retrospective adoption method in IFRS 16, and, therefore, will only recognise leases on balance sheet as at 1 January 2019. In addition, it has decided to measure right-of-use assets by reference to the measurement of the lease liability on that date. This will ensure there is no immediate impact to net assets on that date. However, further work still needs to be carried out to determine whether and when extension and termination options are likely to be exercised, which will result in the actual liability recognised being higher than this.

Instead of recognising an operating expense for its operating lease payments, the Organisation will recognise interest on its lease liabilities and amortisation on its right-of-use assets.

The Organisation is currently assessing the possible impact of the new standard on its financial statements.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

FINANCIAL INSTRUMENTS

The Organisation has adopted IFRS 9 as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which resulted in accounting policies and adjustments to the amounts previously recognized in the financial statements. The Organisation did not early adopt any of IFRS 9 in previous periods.

As permitted by the transitional provisions of IFRS 9, the Organisation elected not to restate comparative figures. Any adjustments to the carrying amounts of financial assets and liabilities at the date of transition were recognized in the opening retained earnings and are disclosed in Note 5.

Consequently, for notes disclosures, the consequential amendments to IFRS 7 disclosures have also only been applied to the current period. Accounting policies under IAS 39 relating to 2017 financial year can be found in the previous year Financial Statements.

The adoption of IFRS 9 has resulted in Changes in the Organisation's accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

IFRS 9 replaces the 'incurred loss' (CL) model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments. Under IFRS 9, credit losses are recognised earlier than under IAS 39.

INITIAL RECOGNITION OF FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are recognised in the Organisation's financial position when the Organisation becomes a party to the contractual provisions of the instrument.

When financial instruments are recognised initially, they are measured at fair value, adjusted, in the case of instruments not at fair value through profit or loss, for directly attributable fees and costs.

If the transaction price differs from fair value at initial recognition, the Organisation accounts for such difference as follows:

- if the fair value is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique that uses only data from observable markets, the Organisation recognises the difference between the fair value at initial recognition and the transaction price as a gain or loss;
- in all other cases, the initial measurement of the financial instrument is adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, the Organisation recognises that deferred difference as a gain or loss only when the inputs become observable, or when the instrument is derecognised.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FINANCIAL ASSETS

Classification and subsequent measurement

On initial recognition, a financial asset is classified into one of the following measurement categories: amortised cost; fair value through other comprehensive income (FVOCI); or fair value through profit or loss (FVTPL).

FINANCIAL ASSETS AT AMORTISED COST

Financial asset at amortised cost is the most relevant measurement category to the Organization. The Organization measures financial assets at amortised cost if both of the following conditions are met:

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest (“SPPI”) on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

A financial asset is measured at fair value through other comprehensive income if it meets both of the following conditions and is not designated as at fair value through profit or loss:

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

All financial assets not classified as measured at amortised cost or FVOCI as described above are measured at FVTPL. This includes all derivative financial assets.

The Organisation’s all financial assets are measured at amortised cost, except Derivative financial assets.

BUSINESS MODEL ASSESSMENT

There are three business models available under IFRS 9:

- Hold to collect: It is intended to hold the asset to maturity to earn interest, collecting repayments of principal and interest form the counterparty.
- Hold to collect and sell: this model is similar to the hold to collect model, except that the entity may elect to sell some or all of the assets before maturity as circumstances change or to hold the assets for liquidity purposes.
- Other: all those models that do not meet the ‘hold to collect’ or ‘hold to collect and sell’ qualifying criteria.

The assessment of business model requires judgment based on facts and circumstances at the date of the assessment. The business model is not assessed on an instrument-by-instrument basis, but at a higher level of aggregated portfolios per instrument type and is based on observable factors.

The Organisation has considered quantitative factors and qualitative factors such as how the performance of the business model and the financial assets held within that business model are evaluated and reported to the key management personnel; the risks that affect the performance of the business model and, in particular, the way those risks are managed; and how managers of the business are compensated.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial assets that are held for trading or are managed and whose performance is evaluated on a fair value basis are measured at FVTPL, because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

SOLELY PAYMENTS OF PRINCIPAL AND INTEREST (SPPI)

If a financial asset is held in either to a Hold to Collect or a Hold to Collect and Sell business model, then assessment to determine whether contractual cash flows are solely payments of principal and interest on the principal amount outstanding at initial recognition is required to determine the classification. The SPPI test is performed on an individual instrument basis.

Contractual cash flows, that represent solely payments of principal and Interest on the principal amount outstanding, are consistent with basic lending arrangement. Interest is consideration for the time value of money and the credit risk associated with the principal amount outstanding during a particular period of time. It can also include consideration for other basic lending risks (e.g. liquidity risk) and costs (e.g. administrative costs) associated with holding the financial asset for a particular period of time, and a profit margin that is consistent with a basic lending arrangement.

In assessing whether the contractual cash flows are SPPI, the Organisation considers whether the contractual terms of the financial asset contain a term that could change the timing or amount of contractual cash flows arising over the life of the instrument which could affect whether the instrument is considered to meet the SPPI test.

If the SPPI test is failed, such financial assets are measured at FVTPL with interest earned recognised in other interest income.

DERECOGNITION OF FINANCIAL ASSETS

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Organisation's statement of financial position) when:

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

IMPAIRMENT OF FINANCIAL ASSETS

Changes to the impairment estimation

The adoption of IFRS 9 has fundamentally changed the Organisation's accounting for loan loss impairment by replacing IAS 39's incurred loss approach with forward-looking expected credit loss (ECL) approach. IFRS 9 requires the Organisation to record ECL on all of its debt financial assets at amortised cost or FVOCI. The allowance is based on the ECL associated with the probability of default in the next 12 months unless there has been a significant increase in credit risk since origination, in which case the allowance is based on the ECL over the life of the asset. If the financial asset meets the definition of purchased or originated credit impaired, the allowance is based on the change in the lifetime ECL.

From 1 January 2018 the Organisation recorded the allowance for expected credit loss for all debt instruments that are measured at amortised cost.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The determination of impairment losses and allowance moves from an incurred credit loss model whereby credit losses are recognised when a defined loss event occurs under IAS 39, to an expected credit loss model under IFRS 9, where provisions are taken upon initial recognition of the financial instruments. Under IFRS 9, the Organisation first evaluates individually whether objective evidence of impairment exists for loans that are individually significant. It then collectively assesses loans that are not individually significant and loans which are significant but for which there is no objective evidence of impairment available under the individual assessment.

Collectively assessesed loans are grouped on the basis of shared credit risk characteristics and collateral type.

Three stage approach

IFRS 9 introduces a three stage approach to impairment for Financial Instruments that are performing at the date of origination or purchase. This approach is summarised as follows:

Stage 1: The Organisation recognizes a credit loss allowance at an amount equal to 12-month expected credit losses. This represents the portion of lifetime expected credit losses from default events that are expected within 12 months of the reporting date, assuming that credit risk has not increased significantly after initial recognition. For those financial assets with a remaining maturity of less than 12 months, a PD is used that corresponds to the remaining maturity.

Stage 2: The Organisation recognizes a credit loss allowance at an amount equal to lifetime expected credit losses for those Financial Instruments which are considered to have experienced a significant increase in credit risk since initial recognition. This requires the computation of ECL based on lifetime probability of default that represents the probability of default occurring over the remaining lifetime of the Financial Instrument. Allowance for credit losses are higher in this stage because of an increase in credit risk and the impact of a longer time horizon being considered compared to 12 months in Stage 1. Financial Instruments in stage 2 are not yet deemed to be credit-impaired.

Stage 3: If the Financial Instrument is credit-impaired, it is then moved to stage 3. The Organisation recognizes a loss allowance at an amount equal to lifetime expected credit losses, reflecting a Probability of Default (PD) of 100 % for those Financial Instruments that are credit-impaired.

INTEREST INCOME RECOGNITION

For Financial Instruments in Stage 1 and Stage 2, the Organisation calculates interest income by applying the Effective Interest Rate (EIR) to the gross carrying amount. Interest income for financial assets in Stage 3 is calculated by applying the EIR to the amortised cost (i.e. the gross carrying amount less credit loss allowance). For Financial Instruments classified as purchased or originated credit-impaired only, interest income is calculated by applying a credit adjusted EIR to the amortised cost of these purchased or originated credit-impaired assets.

Definition of default

The Organisation recognizes default in the following cases:

- Arrears including restructured loans >90 days
- Decease of a client
- Force majeure, when a client becomes insolvent due to external factors beyond the control

The definition of default is in line with relevant regulations taking into account the 90 days past due cap presumption IFRS 9.

The loans for which the Organisation recognizes default are credit-impaired loans.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Organisation considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Organisation's historical experience and expert credit assessment and including forward-looking information.

The quantitative information is a primary indicator of significant increase in credit risk and is based on the change in lifetime PD by comparing:

- the remaining lifetime PD at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated based on facts and circumstances at the time of initial recognition of the exposure.

As a backstop, the Organisation considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due.

The Organisation monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- The criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- The criteria do not align with the point in time when an asset becomes 30 days past due; and
- There is no unwarranted volatility in loss allowance from transfers between 12-months PD (probability of default) and lifetime PD.

Forward-looking information

Under IFRS 9, the allowance for credit losses is based on reasonable and supportable forward looking information obtainable without undue cost or effort, which takes into consideration past events, current conditions and forecasts of future economic conditions.

The Organisation incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL.

The Organisation has identified and documented the key drivers of credit risk and credit losses for the portfolio using an analysis of historical data, has assessed impact of macro-economic variables on probability of default and recovery rate. The following macro-economic variables were analysed:

- Real growth rate of GDP of Georgia;
- Inflation rate;

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- Probability of default (PD);
- Loss given default (LGD);
- Exposure at default (EAD).

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Probability of default (PD)

PD estimates are estimates at a certain date, which are calculated based on statistical rating models.

If a counterparty or exposure migrates between ratings classes, then this will lead to a change in the estimate of the associated PD. PDs are estimated considering the contractual maturities of exposures and estimated prepayment rates.

PDs are calculated based on three-year average and then 1-year and lifetime PDs are derived by extrapolating using migration matrices.

Exposure at default (EAD)

Exposure of default (EAD) represents an estimate of the exposure to credit risk at the time of a potential default occurring during the life of a financial asset. It represents the cash flows outstanding at the time of default, considering expected repayments, interest payments and accruals discounted at the EIR.

Loss given default (LGD)

LGD is defined as the likely loss in case of a counterparty default. The Organisation estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD model considers cash recoveries only. LGD is calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

FINANCIAL LIABILITIES

The Organisation classifies its financial liabilities into one of two categories, depending on the purpose for which the liability was acquired. On 1 January 2018 (the date of initial application of IFRS 9), the Organisation has classified all financial as liabilities within “Other financial liabilities” category. Other financial liabilities include the following items: borrowings and other short-term monetary liabilities.

Other financial liabilities are initially recognised at fair value net of any transaction costs directly attributable to the issue of the instrument. Such interest-bearing liabilities are subsequently measured at amortised cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the statement of financial position. For the purposes of each financial liability, interest expense includes initial transaction costs and any premium payable on redemption, as well as any interest or coupon payable while the liability is outstanding.

DERECOGNITION OF FINANCIAL LIABILITIES

The Organisation derecognises financial liabilities when, and only when, the Organisation’s obligations are discharged, cancelled or they expire. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable is recognised in profit and loss.

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 recognised amounts, and there is an intention to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FOREIGN CURRENCY TRANSLATION

Items included in the financial statements are measured using the currency of the primary economic environment in which The Organisation operates ('the functional currency'). Financial statements are presented in thousands of Georgian Lari (GEL), which is the Organisation's functional and presentation currency.

Monetary assets and liabilities are translated into the Organisation's functional currency at the official exchange rate of the National Bank of Georgia.

Foreign exchange gains and losses resulting from the settlement of transactions and from the translation of monetary assets and liabilities into Organisation's functional currency at year-end official exchange rates are recognised in the statement of comprehensive income. 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.

Table below presents the closing exchange rates by the National Bank of Georgia as at 31 December 2018, 2017 and 1 January 2017:

	USD / GEL	EUR / GEL
Exchange rate as at 31 December 2018	2.6766	3.0701
Exchange rate as at 31 December 2017	2.5922	3.1044
Exchange rate as at 1 January 2017	2.6468	2.7940

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. Cash and cash equivalents include cash on hand, and all bank placements or receivables with original maturities of less than three months. Funds restricted for a period of more than three months on origination are excluded from cash and cash equivalents.

LOANS TO CUSTOMERS AND OTHER RECEIVABLES

Loans to customers and other receivables included in other assets in the statement of financial position are non-derivative financial assets measured at amortised cost. Loans to customers and other receivables are initially measured at fair value and subsequently at their amortised cost using the effective interest method.

PROPERTY AND EQUIPMENT

Property and equipment are carried at historical cost less accumulated depreciation and recognized impairment loss, if any. Depreciation is charged on the carrying value of property and equipment and is designed to write off assets over their useful economic lives. Depreciation is calculated on a straight-line basis at the following useful lives:

Historical cost	Useful life (years)
Leasehold improvements	10
Office equipment	5
Furniture and fixtures	5

The carrying amounts of property and equipment are reviewed at each reporting date to assess whether they are recorded in excess of their recoverable amounts. The recoverable amount is the higher of fair value less costs to sell and value in use.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

BORROWINGS AND SUBORDINATED BORROWINGS

Borrowings are initially recognised at fair value. Subsequently they are stated at amortised cost and any difference between net proceeds and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings, using the effective interest method.

The subordinated borrowings represent the obligations that rank lower than all other loans and securities with respect to the claim on a firm's assets. Therefore, if the borrower defaults, the creditors of subordinated debt will be compensated after all other debt holders are paid in full.

SHARE CAPITAL

Ordinary shares with discretionary dividends are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium in equity.

DIVIDENDS

Dividends are recorded in equity in the period in which they are declared. Any dividends declared after the end of the reporting period and before the financial statements are authorised for issue, are disclosed in the subsequent events note.

TAXATION

The tax expense for the year comprises current and deferred tax. Tax is recognized in the statement of comprehensive income, except to the extent that it relates to items recognized in other comprehensive income or directly in equity. In this case the tax is also recognized in other comprehensive income or directly in equity, respectively.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in Georgia and generates taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit and loss. Deferred income tax is determined using tax rate (and laws) that has been enacted or substantially enacted by the balance sheet date and is expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilized. Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity where there is an intention to settle the balances on a net basis.

SALARIES AND OTHER EMPLOYEE BENEFITS

Wages, salaries, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Organisation.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

PROVISIONS

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

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

EVENTS AFTER THE REPORTING PERIOD

The Organisation makes certain estimates and assumptions regarding the future. Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may deviate from these estimates and assumptions. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Organisation makes certain estimates and assumptions regarding the future. Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may deviate from these estimates and assumptions. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

MEASUREMENT OF EXPECTED CREDIT LOSSES

The following are key estimations that the management have used in the process of applying the Organisation's accounting policies and that have the most significant effect on the loss allowances for expected credit losses:

- Probability of default: PD constitutes a key input in measuring ECL. PD is an estimate of the likelihood of default over a given time horizon, the calculation of which includes historical data, assumptions and expectations of future conditions.
- Loss Given Default: LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, taking into account cash flows from collateral and integral credit enhancements.
- Establishing forward-looking scenarios: When measuring ECL the Organisation uses reasonable and supportable forward-looking information, which is based on assumptions for the future movement of different economic drivers and how these drivers will affect each other.

INCOME TAXES

During the ordinary course of business, there are many transactions and calculations for which the ultimate tax determination is uncertain. As a result, the Organisation recognizes tax liabilities based on estimates of whether additional taxes and interest will be due. These tax liabilities are recognized when, despite the Organisation's belief that its tax return positions are supportable, the Organisation believes that certain positions are likely to be challenged and may not be fully sustained upon review by tax authorities. As a result, the Organisation minimizes the risks related to this fact. The Organisation believes that its accruals for tax liabilities are adequate for all open audit years based on its assessment of many factors including past experience and interpretations of tax law. This assessment relies on estimates and assumptions and may involve a series of complex judgments about future events.

5. EFFECTS OF CHANGES IN ACCOUNTING POLICIES

The measurement category and the carrying amount of financial assets and liabilities in accordance with IAS 39 and IFRS 9 at 1 January 2018 are compared as follows:

				Remeasurment			
	Note	**Original classification under IAS 39**	**Original Carrying amount under IAS 39**	**ECL***	**Other**	**New Carrying amout under IFRS 9**	**New classification under IFRS 9**
Cash and cash equivalents	13	Amortised cost (loans and receivables)	1,120,403	-	-	1,120,403	Amortised cost
Loans to customers	14	Amortised cost (loans and receivables)	69,013,753	(16,673,106)	-	52,340,647	Amortised cost
Total financial assets			**70,134,156**	**(16,673,106)**	**-**	**53,461,050**	
Borrowings	15	Amortised cost (loans and receivables)	62,245,777	-	-	62,245,777	Amortised cost
Other liabilities	17	Amortised cost (loans and receivables)	595,193	-	-	595,193	Amortised cost
Total financial liabilities			**62,840,970**	**-**	**-**	**62,840,970**	

* Re-measurement in the above table includes the effect of ECL in the amount of GEL16,306,269 and effect of interest accrual on 3 stage GEL366,837.

6. PRIOR PERIOD ADJUSTMENTS

For the presentation purposes of 2018, the following adjustments were made on 2017 figures:

	As per prior year	**Adjustment**	**After adjustment**
Borrowings	58,465,477	3,780,300	62,245,777
Gain /(loss) from exchange rate difference	1,655,791	(3,780,300)	(2,124,509)

7. OTHER CONTRIBUTIONS BY OWNERS

	2018
Income from sale of portfolio	**34,134,929**
Cost of sale:	**17,593,532**
Gross portfolio	34,134,929
Impairment	(11,994,007)
Other (interest income adjustment according IFRS 9)	(4,547,390)
Gain from sale of portfolio	**16,541,397**

On 30 November 2018 Organisation sold the loan portfolio with total amount of GEL34,124,929 to related party – Euro Credit + LLC. Euro Credit + repaid its payable by offsetting the borrowings (with amount of selling price) with the Organisation (see note 15). The major part of sold portfolio was comprised by overdue loans.

8. OTHER INCOME

	2018	2017
Penalties and fines	6,641,720	3,389,683
Income from EP Commission	266,303	243,859
Other	672,395	106,757
Total other income	**7,580,418**	**3,740,299**

9. FINANCIAL SERVICES

On 15 January 2016 the agreement was signed between the Organisation and EC+ LLC with the subject to provide financial services related to the operational activities of the Organisation.

EC+ LLC is experienced entity to run the same type of business, which generally includes client application, analysis of user data, risk assessment, determination of loan terms and decision making on loan issuance.

Financial services also included process of collecting money from clients such as:

- Daily/monthly/yearly relationship with borrowers using different communications channels (phone, email, etc.);
- Having negotiation with the clients in order to restructure or refinance the loans in case of necessity;
- Collecting the money based on Georgian Legislation and the loan agreement in case of overdue loans.

10. GENERAL AND ADMINISTRATIVE EXPENSES

	2018	2017
Legal fees	(1,073,733)	(701,360)
Rent expenses	(997,387)	(449,270)
Marketing cost	(995,287)	(548,671)
Expenses related with repossessed vehicles	(694,146)	(49,873)
Consulting and other professional services*	(663,890)	(102,735)
Office expense	(395,839)	(62,308)
Application inspection fees	(376,512)	(199,109)
IT consulting service and software support fees	(308,350)	(51,595)
Fuel	(257,414)	(93,087)
Business trips	(253,545)	(23,186)
Communication	(165,693)	(38,817)
Utilities	(56,627)	(51,572)
Bank fees	(44,795)	(132,811)
Other	(474,953)	(124,027)
Total general and administrative expenses	**(6,758,171)**	**(2,628,421)**

*Consulting services include audit fees with total amount of GEL69,686 for the years ended 31 December 2016 and 2017.

11. SALARIES AND OTHER EMPLOYEE BENEFITS

	2018	2017
Salaries	(4,583,163)	(2,700,082)
Bonuses	(351,791)	(275,862)
Other employee benefits	(152,380)	(65,948)
Total salaries and other employee benefits	**(5,087,334)**	**(3,041,892)**

12. TAXATION

Temporary differences at a rate of 15% due to:	Balance at 1 January 2017	Credited (charged) to the Income Statement	Balance at 31 December 2017	(Charged)/ credited to equity*	Balance at 1 January 2018	Credited (charged) to the Income Statement	Balance at 31 December 2018
Loans to customers	83,644	62,874	146,518	2,445,940	2,592,458	(1,364,005)	1,228,453
Property and equipment	-	-	-	-	-	(43,276)	(43,276)
Tax loss carry forward	113,067	(113,067)	-	-	-	-	-
Deferred tax asset	**196,711**	**(50,193)**	**146,518**	**2,445,940**	**2,592,458**	**(1,407,281)**	**1,185,177**
Unrecognised Temporary differences							
Loans to customers	-	-	-	-	(2,445,940)	1,364,005	(1,081,935)
Net deferred tax asset	**196,711**	**(50,193)**	**146,518**	**2,445,940**	**146,518**	**(43,276)**	**103,242**

* Change due to implementation of IFRS 9.

12. TAXATION (CONTINUED)

Income tax expense comprises the following:

	2018	2017
Current income tax	(3,067,480)	(1,309,186)
Effect of temporary differences	(43,276)	(50,193)
Income tax expense	**(3,110,756)**	**(1,359,379)**

The tax effects of the movements in temporary differences recorded at the rate of 15% are as follows:

	2018	2017
Profit before income tax	**30,837,282**	**9,740,324**
Applicable tax rate	15%	15%
Theoretical Income tax expense	**(4,625,592)**	**(1,461,049)**
Effect of unrecognised tax asset	(1,081,935)	-
Effect of permanent differences	2,596,772	101,670
Income tax expense	**(3,110,756)**	**(1,359,379)**

13. CASH AND CASH EQUIVALENTS

	31 December 2018	31 December 2017	1 January 2017
Cash on hand in Georgian Lari	6,504	94,608	90,895
Cash on hand in foreign currencies	2,492	44	358,684
Cash in bank in Georgian Lari	2,117,893	755,588	73,030
Cash in bank in foreign currencies	74,349	130,209	442,076
Cash in transit	140,526	139,954	-
Total cash and cash equivalents	**2,341,764**	**1,120,403**	**964,685**

Cash and cash equivalents distribution by currency is disclosed in Note 19.

14. LOANS TO CUSTOMERS

	31 December 2018	31 December 2017	1 January 2017
Gross loans to customers	47,193,403	69,013,753	22,609,956
Less: allowance for impairment losses	(7,259,754)	-	-
Total loans to customers	**39,933,649**	**69,013,753**	**22,609,956**

Analysis by credit quality of the originated loans to customers according to the agreement as at 31 December 2018, 2017 and 1 January 2017 is as follows:

	31 December 2018		
Credit quality of loans to customers	**Gross Loan**	**ECL**	**Net Loan**
Loans without individual sign of impairment	23,459,451	(2,099,102)	21,360,349
Less than 30 days overdue	7,009,575	(850,825)	6,158,750
30 to 60 days overdue	2,687,813	(470,279)	2,217,534
60 to 90 days overdue	1,645,119	(387,755)	1,257,364
Over 90 days	5,610,798	(2,540,645)	3,070,153
Restructured (Less than 90)	5,302,165	(260,416)	5,041,749
Restructured (Over 90 Days)	1,478,482	(650,732)	827,750
Total as at 31 December 2018	**47,193,403**	**(7,259,754)**	**39,933,649**

14. LOANS TO CUSTOMERS (CONTINUED)

	31 December 2017		
Credit quality of loans to customers	**Gross Loan**	**CL**	**Net Loan**
Loans without individual sign of impairment	34,510,623	-	34,510,623
Less than 30 days overdue	6,976,411	-	6,976,411
30 to 60 days overdue	3,951,074	-	3,951,074
60 to 90 days overdue	2,456,834	-	2,456,834
Over 90 days	18,099,846	-	18,099,846
Restructured (Less than 90)	2,714,376	-	2,714,376
Restructured (Over 90 Days)	304,589		304,589
Total as at 31 December 2017	**69,013,753**	**-**	**69,013,753**

	1 January 2017		
Credit quality of loans to customers	**Gross Loan**	**CL**	**Net Loan**
Loans without individual sign of impairment	12,906,572	-	12,906,572
Less than 30 days overdue	6,531,108	-	6,531,108
30 to 60 days overdue	1,999,969	-	1,999,969
60 to 90 days overdue	564,468	-	564,468
Over 90 days	544,309	-	544,309
Restructured (Less than 90)	63,530	-	63,530
Restructured (Over 90 Days)	-		-
Total as at 1 January 2017	**22,609,956**	**-**	**22,609,956**

The Organisation has established internal policy for issuing collateralized loans. Loans are pledged with vehicles. Requirements for collateral is determined by using LTV (Loan to Value) ratio (Maximum ratio is 85% as of NBG). This ratio is referred to the collateral's market value, which is maximum 80% of fair value of pledged collateral.

Movements in the loan impairment allowance for the year ended 31 December are as follows:

Reconciliation – Loan Impairment	**Stage 1**	**Stage 2**	**Stage 3**	
	12-month ECL	Lifetime ECL- not credit-impaired	Lifetime ECL- credit-impaired	**Total**
Balance at 1 January 2018 by IAS 39				-
Adjustment due to IFRS 9 application				16,306,268
Balance at 1 January 2018 by IFRS 9	**4,933,500**	**1,515,472**	**9,857,296**	**16,306,268**
Transfer to Stage 1	109,284	(91,957)	(17,327)	-
Transfer to Stage 2	(593,455)	593,598	(143)	-
Transfer to Stage 3	(2,043,584)	(4,797)	2,048,381	-
Loan impairment charge for the year	734,096	(1,083,780)	3,506,765	3,157,081
Write off for the year	-	-	(209,588)	(209,588)
Sold Loans During the year	-	-	(11,994,007)	(11,994,007)
Balance at 31 December 2018	**3,139,841**	**928,536**	**3,191,377**	**7,259,754**

15. BORROWINGS AND SUBORDINATED BORROWINGS

	31 December 2018	31 December 2017	1 January 2017
Originated borrowings	12,487,537	50,946,419	23,514,294
Accrued interest	1,947,128	11,299,358	1,272,562
Total borrowings	**14,434,665**	**62,245,777**	**24,786,856**

Borrowings by current and non-current portions for 31 December 2018, 2017 and 1 January 2017 can be presented as follows:

				31 December 2018			
				Current		Non-Current	
	Interest rate	Maturity date	Currency	Principal amount	Accrued Interest	Principal amount	Accrued Interest
Euro Credit +	24%	3-Feb-20	USD	-	1,947,127	12,487,537	-
Total borrowings				**-**	**1,947,127**	**12,487,537**	**-**

				31 December 2017			
				Current		Non-Current	
	Interest rate	Maturity date	Currency	Principal amount	Accrued Interest	Principal amount	Accrued Interest
Euro Credit +	24%	3-Feb-19	USD	-	11,177,640	50,260,282	-
W.G.H Georgia Investments JSC	24%	31-Dec-18	USD	-	121,718	674,679	-
Zuk China Stone Works JSC	24%	31-Dec-18	GEL	-	-	11,458	-
Total borrowings				**-**	**11,299,358**	**50,946,419**	**-**

				1 January 2017			
				Current		Non-Current	
	Interest rate	Maturity date	Currency	Principal amount	Accrued Interest	Principal amount	Accrued Interest
Euro Credit +	24%	3-Feb-19	USD	-	1,272,562	23,502,836	-
Zuk China Stone Works JSC	24%	31-Dec-18	GEL	-	-	11,458	-
Total borrowings				**-**	**1,272,562**	**23,514,294**	**-**

Borrowed funds are with credit line term. Based on signed loan agreement interest accrued during the period should be paid at the end of each reporting year.

Subordinated borrowings for 31 December 2018, 2017 and 1 January 2017 can be presented as follows:

				31 December 2018			
				Current		Non-Current	
	Interest rate	Maturity date	Currency	Principal amount	Accrued Interest	Principal amount	Accrued Interest
Euro Credit +	24%	1-Dec-25	USD	-	-	3,502,879	71,401
Euro Credit +	24%	1-Dec-25	USD	-	-	3,502,879	71,401
Total subordinated borrowings				**-**	**-**	**7,005,758**	**142,802**

15. BORROWINGS AND SUBORDINATED BORROWINGS (CONTINUED)

Changes in borrowings and subordinated borrowings arising from financing activities, including both changes arising from cash flows and non-cash changes can be presented as follows:

	2018	2017
At the beginning of the year	62,245,777	24,786,856
Cash flows	(19,557,542)	21,470,791
Non-cash flows:		
Interest accruing in period	10,701,137	10,026,798
Other liabilities converted into borrowings	-	5,190,656
Offsetting borrowings and loan portfolio (Note 7)	(34,134,929)	-
Effects of foreign exchange	2,328,783	770,676
At the end of the year	**21,583,226**	**62,245,777**

16. OTHER LIABILITIES

	31 December 2018	31 December 2017	1 January 2017
Financial other liabilities			
Trade payables	1,147,308	434,000	226,635
Salary payables	8,901	34,108	18,384
Other	223,405	127,085	25,638
Total other liabilities	**1,379,614**	**595,193**	**270,657**

17. SHARE CAPITAL

Shareholders	Percent	31 December 2018	Percent	31 December 2017	Percent	1 January 2017
Zuk China Stone Works JSC	75.51%	377,550	75.51%	188,775	75.51%	188,775
Mody Import&Marketing Ceramics LTD	7.99%	39,950	7.99%	19,975	7.99%	19,975
Iosef Reuven Grenikas	6.50%	32,500	9.50%	23,750	9.50%	23,750
Uri Zuk	5.00%	25,000	5.00%	12,500	5.00%	12,500
Oren Duanias	3.00%	15,000	0.00%	-	0.00%	-
Eyal Duanias	2.00%	10,000	2.00%	5,000	2.00%	5,000
Total share capital	**100%**	**500,000**	**100%**	**250,000**	**100%**	**250,000**

18. COMMITMENTS AND CONTINGENCIES

LITIGATION

In the ordinary course of business, organisations are usually subject to legal actions and complaints.

Legal proceedings against Organisation's customers unable to repay loans

Following the Organisation's customer's failure to meet loan repayment obligations the Organisation is involved in legal disputes against such customers. The highest possible outcome from such legal disputes is the amount of loans receivable from such customers (including accrued interest and other charges).

As it is not certain that all the customers will meet the repayment obligations, the Organisation recognises provision for impairment for such loans, as disclosed in Note 14.

19. FINANCIAL INSTRUMENTS – RISK MANAGEMENT

As a financial institution, the Organisation is exposed to risks that arise from its use of financial instruments. This note describes the Organisation's objectives, policies and processes for managing those risks and the methods used to measure them. Further quantitative information in respect of these risks is presented throughout these financial statements.

Financial assets and financial liabilities that are liquid or have a short-term maturity it is assumed that the carrying amounts approximate to their fair value.

GENERAL OBJECTIVES, POLICIES AND PROCESSES

The management has overall responsibility for the determination of the Organisation's risk management objectives and policies and, whilst retaining ultimate responsibility for them, it has delegated the authority for designing and operating processes that ensure the effective implementation of the objectives and policies to the Organisation's finance function.

The overall objective of the management is to set polices that seek to reduce risks as far as possible without unduly affecting the Organisation's competitiveness and flexibility. Further details regarding these policies are set out below. Through its operations, the Organisation is exposed to the following financial risks:

- Credit risk
- Liquidity risk
- Market risk:
  - Currency risk
  - Interest rate risk

CREDIT RISK

Credit risk 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 lending and other transactions with counterparties giving rise to financial assets.

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting dates was:

	31 December 2018	31 December 2017	1 January 2017
Cash and cash equivalents (excluding cash on hand)	2,332,768	1,025,751	515,106
Loans to customers	39,933,649	69,013,753	22,609,956
Total credit risk exposure	**42,266,417**	**70,039,504**	**23,125,062**

LIQUIDITY RISK

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

In order to manage liquidity risk, the Organisation performs regular monitoring of future expected cash flows, which is a part of assets/liabilities management process. An analysis of the liquidity and interest rate risks is presented in the following tables. The presentation below is based upon the information provided by key management personnel of the Organisation.

Liquidity of financial liabilities as at 31 December 2018 can be presented as follows:

Financial liabilities	Up to 1 year	1 year to 5 years	Over 5 years	Total
Borrowings	4,944,379	12,759,533	-	17,703,912
Subordinated Borrowings	1,824,185	6,730,134	10,230,326	18,784,645
Other liabilities	1,379,614	-	-	1,379,614
Total financial liabilities	**8,148,178**	**19,489,667**	**10,230,326**	**37,868,171**

19. FINANCIAL INSTRUMENTS – RISK MANAGEMENT (CONTINUED)

Liquidity of financial liabilities as at 31 December 2017 can be presented as follows:

Financial liabilities	Up to 1 year	1 year to 5 years	Total
Borrowings	24,212,184	51,350,861	**75,563,045**
Other liabilities	595,193	-	**595,193**
Total financial liabilities	**24,807,377**	**51,350,861**	**76,158,238**

Liquidity of financial liabilities as at 1 January 2017 can be presented as follows:

Financial liabilities	Up to 1 year	1 year to 5 years	Total
Borrowings	6,915,993	29,667,696	**36,583,689**
Other liabilities	270,657	-	**270,657**
Total financial liabilities	**7,186,650**	**29,667,696**	**36,854,346**

MARKET RISK

Market risk is the risk that the fair value of a financial instrument will decrease because of changes in market factors. Market risk arises from the Organisation's use of interest bearing and foreign currency financial instruments. It is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates (currency risk) and interest rates (interest rate risk).

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

Currency risk of financial assets and liabilities as at 31 December 2018 can be presented as follows:

Financial assets	GEL	USD	Total
Cash and cash equivalents	2,264,924	76,840	**2,341,764**
Loans to customers	39,534,000	399,649	**39,933,649**
Total financial assets	**41,798,924**	**476,489**	**42,275,413**
Financial liabilities			
Other liabilities	1,246,064	133,550	**1,379,614**
Borrowings	-	14,434,665	**14,434,665**
Subordinated Borrowings	-	7,148,561	**7,148,561**
Total financial liabilities	**1,246,064**	**21,716,776**	**22,962,840**
Open balance sheet position	**40,552,860**	**(21,240,287)**	**19,312,573**

19. FINANCIAL INSTRUMENTS – RISK MANAGEMENT (CONTINUED)

Currency risk of financial assets and liabilities as at 31 December 2017 can be presented as follows:

Financial assets	GEL	USD	Total
Cash and cash equivalents	990,150	130,253	**1,120,403**
Loans to customers	60,703,850	8,309,903	**69,013,753**
Total financial assets	**61,694,000**	**8,440,156**	**70,134,156**
Financial liabilities			
Other liabilities	595,193	-	**595,193**
Borrowings	11,458	62,234,319	**62,245,777**
Total financial liabilities	**606,651**	**62,234,319**	**62,840,970**
Open balance sheet position	**61,087,349**	**(53,794,163)**	**7,293,186**

Currency risk of financial assets and liabilities as at 1 January 2017 can be presented as follows:

Financial assets	GEL	USD	Total
Cash and cash equivalents	163,993	800,692	**964,685**
Loans to customers	3,752,783	18,857,173	**22,609,956**
Total financial assets	**3,916,776**	**19,657,865**	**23,574,641**
Financial liabilities			
Other liabilities	270,657	-	**270,657**
Borrowings	11,458	24,775,398	**24,786,856**
Total financial liabilities	**282,115**	**24,775,398**	**25,057,513**
Open balance sheet position	**3,634,661**	**(5,117,533)**	**(1,482,872)**

The following table details the Organisation's sensitivity to a 20% increase and decrease in the foreign currency exchange rates against GEL and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the year for a 20% change in foreign currency rates. Impact on the statement of comprehensive income and equity based on financial instrument values as at 31 December 2018 and 2017 can be presented as follows:

	(GEL / USD)	
Sensitivity of the fluctuation of the market exchange rates	**2018**	**2017**
20% increase	(4,248,057)	(10,758,833)
20% decrease	4,248,057	10,758,833

- **INTEREST RATE RISK**

Interest rate risk arises from potential changes in market interest rates that can adversely affect the fair values of the financial assets and liabilities of the Organisation. This risk can arise from maturity mismatches of assets and liabilities, as well as from the re-pricing characteristics of such assets and liabilities.

19. FINANCIAL INSTRUMENTS – RISK MANAGEMENT (CONTINUED)

The table below summarises the Organisation's exposure to interest rate risks. The table presents the aggregated amounts of the Organisation's interest-bearing financial assets and interest bearing financial liabilities at carrying amounts as at 31 December 2018, 2017 and 1 January 2017:

	31 December 2018	31 December 2017	1 January 2017
Total interest bearing financial assets	47,193,403	69,013,753	22,609,956
Total interest bearing financial liabilities	21,583,226	62,245,777	24,786,856
Net interest sensitivity gap	**25,610,177**	**6,767,976**	**(2,176,900)**

Organisation's all interest-bearing assets and liabilities are at fixed interest rates. Therefore, market interest rate fluctuations do not affect Organisation's income or expenses.

20. MANAGEMENT OF CAPITAL

The Organisation's objectives when maintaining capital are:

- To safeguard the Organisation's ability to continue as a going concern, so that it can continue to operate sufficiently; and
- To comply with the capital requirements set by NBG.
- To provide an adequate return to shareholders.

The Organisation sets the amount of capital it requires in proportion to risk. The Organisation manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets.

21. TRANSACTIONS WITH RELATED PARTIES

Related parties or transactions with related parties, as defined by IAS 24 "Related party disclosures", could be one or more of the followings:

a) Parties that directly, or indirectly through one or more intermediaries: control, or are controlled by, or are under common control with, the Organisation (this includes parents, subsidiaries and fellow subsidiaries); have an interest in the Organisation that gives then significant influence over the Organisation; and that have joint control over the Organisation;

b) Members of key management personnel of the Organisation or its parent;

c) Close members of the family of any individuals referred to in (a) or (b);

d) Parties that are entities controlled, jointly controlled or significantly influenced by, or for which significant voting power in such entity resides with, directly or indirectly, any individual referred to in (c) or (b);

In considering each possible related party relationship, attention is directed to the substance of the relationship, and not merely the legal form. Details of transactions between the Organisation and other related parties are disclosed below.

21. TRANSACTIONS WITH RELATED PARTIES (CONTINUED)

Transactions with related parties as at 31 December 2018 can be presented as follows:

Financial Statement caption	Shareholders	Entity under common control
Borrowings	-	14,434,665
Subordinated borrowings	-	7,148,561
Other liabilities	-	995,526
General and administrative expenses	(160,985)	(695,548)
Salaries and other employee benefits	(396,368)	-
Interest expense	-	(10,701,137)
Financial service	(133,550)	-

In 2018 loan portfolio was sold to related party (detailed information is disclosed in Note 7).

Transactions with related parties as at 31 December 2017 can be presented as follows:

Financial Statement caption	Entity under common control
Borrowings	62,245,777
Other liabilities	434,000
Salaries and other employee benefits	(614,521)
Interest expense	(9,684,411)
Financial service	(5,190,656)

Transactions with related parties as at 1 January 2017 can be presented as follows:

Financial Statement caption	Entity under common control
Borrowings	24,786,856
Interest expense	(1,106,433)
Financial service	(3,781,313)

22. EVENTS AFTER THE REPORTING PERIOD

According to the Order #281/04 Of the President of the National Bank of Georgia new regulations came into force from 1 January 2019. Due to the new regulations MFO is not permitted to grant loans without analysing the solvency of customer. The purpose of new regulation is to ensure stable and sustainable operation of the financial system of Georgia and to encourage healthy lending.