პროკრედიტ ბანკი
ProCredit Bank
Georgia

Pillar 3 Report 2018

JSC ProCredit Bank Georgia

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1 About the Pillar 3 report

The Pillar 3 report is prepared in full compliance with the internal control processes agreed with the Supervisory Board of ProCredit Bank. The present report meets the requirements of the “Rule about the disclosure of information by commercial banks within the Pillar 3”, stipulated by the National Bank of Georgia. The Pillar 3 Report and the accuracy and reliability of the information contained in this report are confirmed by the Board of Directors of ProCredit Bank.

2 Introduction

ProCredit Bank focuses on small and medium-sized enterprises (SMEs) in Georgia. The business model focuses on the core activities comprising classical banking.

Our corporate strategy and our activities are guided by the objective of making a sustainable contribution to economic, social and environmental development in the country, and in doing so achieving an appropriate return on investment for our shareholders. In this respect, we see good potential in Georgia. ProCredit’s business strategy is based on the formation of long-term relationships with our clients and staff and on careful risk management.

It is the goal of the ProCredit Bank to play a leading role as the “Hausbank” for SMEs. We offer the full range of banking services in terms of financing, account operations, payments and deposit business. Through our long-term support for sound SMEs, we make a contribution to creating jobs, enhancing capacity for innovation, and encouraging investments in ecological and social projects. We focus on innovative companies showing dynamic growth and stable, formalised structures. Furthermore, we place an emphasis on promoting local production.

In addition to serving SMEs, the ProCredit Bank also pursues a Direct Banking strategy for private clients, a completely different banking experience that provides the full package of banking services through electronic media. Simple services, a flat fee, permanent access to banking services with Internet Banking and access to multi-functional 24/7 self-service zones are the main advantages that customers can enjoy with Direct Banking. Thanks to the diversity of remote channels and the investments the bank has made in them, clients can now carry out nearly 99% of banking operations independently, whenever and wherever they like. The bank’s official website has been updated, with its modern, simple design making it more convenient for customers to use. Customers have continuous access to the banking services they need using Internet Banking.

The most prominent component of our support for private clients comprises account management and savings services. We also provide financing to enable such clients to purchase real estate and make other selected investments. We do not actively pursue consumer lending.

All ProCredit clients enjoy a range of innovative service channels centering around user-friendly online banking. In addition, our outlets are equipped with 24-hour self-service areas where the entire package of payment transactions can be completed. By means of these two channels, nearly all transactions have been fully automated. Our clients have access to personalised advice in our branches and through our contact center.

The ProCredit Bank is a member of the ProCredit (banking) group which is supervised by the German Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht, or BaFin) and the Deutsche Bundesbank. ProCredit Holding is responsible for the strategic management, capital

adequacy, reporting, risk management and proper business organisation of the ProCredit (banking) group pursuant to Section 25a of the German Banking Act (KWG). The ProCredit Holding shares are traded on the Prime Standard segment of the Frankfurt Stock Exchange.

With this Pillar 3 report, ProCredit Bank complies with the disclosure requirements for the ProCredit Bank as of 31 December 2018, stipulated in the “Rule about the disclosure of information by commercial banks within the Pillar 3” by the National Bank of Georgia, Capital Requirements Regulation (CRR) - (EU) No. 575/2013 and Basel Committee requirements regarding disclosure of information. Legally protected or confidential information is generally excerpted from disclosure.

The information disclosed is based on the audited financial statements of ProCredit Bank and ProCredit Properties LLC as reported in the 2018 report. As a supplement to this Pillar 3 report, information on the ProCredit Bank is available in ProCredit Bank’s 2018 Financial Statements and Independent Auditors’ Report, which is published on the website.

The Pillar 3 report has been approved by the Management of ProCredit Bank.

This report contains summed figures and percent calculations that may, due to rounding, contain minor deviations.

3 Scope of consolidation

This Pillar 3 report is prepared on the basis of the companies in the ProCredit group which have been consolidated under IFRS; this includes ProCredit Properties LLC, an institution which carries out property management activities and over which ProCredit Bank exercises a controlling influence. The reports for regulatory purposes are prepared on standalone bank’s financial data.

Consolidation by entities

	Name of Entity	Method of Accounting consolidation	Method of regulatory consolidation				Description
			Full Consolidation	Proportional Consolidation	Neither consolidated nor deducted	Deducted	
1	ProCredit Property	Full Consolidation				x	Georgia, Tbilisi; Real Estate management; Assets - 8 991 692.21 ₾; Capital - 8 824 298.14 ₾

Table 1

4 Key ratios

Key metrics

in Lari

N		31/12/2018	30/09/2018	30/06/2018	31/03/2018	31/12/2017
	Regulatory capital (amounts, GEL)					
	Based on Basel III framework					
1	Common Equity Tier 1 (CET1)	169,150,627	162,771,322	186,457,106	179,007,000	170,795,357
2	Tier 1	169,150,627	162,771,322	186,457,106	179,007,000	170,795,357
3	Total regulatory capital	225,112,407	223,305,529	230,596,153	222,229,810	217,192,975
	Risk-weighted assets (amounts, GEL)					
4	Risk-weighted assets (RWA) (Based on Basel III framework)	1,265,298,589	1,246,086,716	1,143,607,669	1,109,187,542	1,187,966,918
	Capital ratios as a percentage of RWA					
	Based on Basel III framework					
5	Common equity Tier 1 ratio >=9.34%	13.37%	13.06%	16.30%	16.14%	14.38%
6	Tier 1 ratio >=11.63%	13.37%	13.06%	16.30%	16.14%	14.38%
7	Total regulatory capital ratio >=15.89%	17.79%	17.92%	20.16%	20.04%	18.28%
	Income					
8	Total Interest Income /Average Annual Assets	6.39%	6.51%	6.54%	6.55%	6.35%
9	Total Interest Expense / Average Annual Assets	2.48%	2.37%	2.31%	2.31%	2.36%
10	Earnings from Operations / Average Annual Assets	2.45%	2.53%	2.47%	2.86%	2.25%
11	Net Interest Margin	3.91%	4.14%	4.23%	4.24%	3.98%
12	Return on Average Assets (ROAA)	2.14%	2.28%	2.44%	2.54%	1.55%
13	Return on Average Equity (ROAE)	15.50%	15.74%	16.71%	17.83%	11.38%
	Asset Quality					
14	Non Performed Loans / Total Loans	2.70%	2.64%	2.43%	2.73%	3.07%
15	LLR/Total Loans	3.21%	3.26%	3.18%	3.34%	3.43%
16	FX Loans/Total Loans	77.27%	77.88%	79.03%	79.20%	80.44%
17	FX Assets/Total Assets	73.34%	73.86%	71.49%	72.24%	73.65%
18	Loan Growth-YTD	3.78%	0.41%	-4.85%	-7.09%	15.35%
	Liquidity					
19	Liquid Assets/Total Assets	26.33%	24.80%	20.46%	19.52%	21.26%
20	FX Liabilities/Total Liabilities	83.76%	84.57%	85.36%	86.37%	86.68%
21	Current & Demand Deposits/Total Assets	30.37%	27.30%	28.95%	28.59%	31.46%
	Liquidity Coverage Ratio*					
22	Total HQLA	348,156,938	302,901,732	226,617,945	205,001,537	248,201,149
23	Net cash outflow	203,278,852	157,168,525	148,542,114	163,896,085	182,086,960
24	LCR ratio (%)	171%	193%	153%	125%	136%

Table 2

* LCR calculated according to NBG's methodology which is more focused on local risks than Basel framework. Commercial banks are required to comply with the limits by coefficients calculated according to NBG's methodology. The numbers calculated within Basel framework are given for illustratory purposes.

Liquidity Coverage Ratio

in Lari

		Total unweighted value			Total weighted values according to NBG's methodology*			Total weighted values according to Basel methodology		
		GEL	FX	Total	GEL	FX	Total	GEL	FX	Total
High-quality liquid assets										
1	Total HQLA				65,695,084	237,025,191	302,720,274	47,511,849	196,681,933	244,193,782
Cash outflows										
2	Retail deposits	42,808,668	324,423,250	367,231,918	8,587,480	59,130,345	67,717,826	2,042,346	14,726,833	16,769,179
3	Unsecured wholesale funding	130,352,980	716,751,873	847,104,853	32,826,143	63,604,072	96,430,215	30,535,572	65,308,581	95,844,153
4	Secured wholesale funding	0	0	-	-	-	-	-	-	-
5	Outflows related to off-balance sheet obligations and net short position of derivative exposures	36,159,904	35,698,722	71,858,625	6,739,813	8,445,277	15,185,091	2,627,445	2,912,071	5,539,516
6	Other contractual funding obligations			-			-			-
7	Other contingent funding obligations	11,129,092	12,071,531	23,200,623	2,443,274	5,240,483	7,683,757	2,443,274	5,240,483	7,683,757
8	**TOTAL CASH OUTFLOWS**	220,450,644	1,088,945,376	1,309,396,020	50,596,711	136,420,178	187,016,889	37,648,637	88,187,968	125,836,605
Cash inflows										
9	Secured lending (eg reverse repos)	758,967	0	758,967	-	-	-	-	-	-
10	Inflows from fully performing exposures	233,695,070	828,655,839	1,062,350,910	5,972,959	10,666,688	16,639,647	24,156,194	94,121,593	118,277,787
11	Other cash inflows	115,558	0	115,558	115,558	-	115,558	115,558	-	115,558
12	**TOTAL CASH INFLOWS**	234,569,595	828,655,839	1,063,225,435	6,088,517	10,666,688	16,755,205	24,271,751	94,121,593	118,393,344
					Total value according to NBG's methodology (with limits)			Total value according to Basel methodology (with limits)		
13	Total HQLA				86,434,087	261,722,851	348,156,938	71,168,486	199,782,875	270,951,361
14	Net cash outflow				51,864,602	151,414,250	203,278,852	22,432,067	28,172,766	39,086,393
15	Liquidity coverage ratio (%)				166.65%	172.85%	171.27%	317.26%	709.13%	693.21%

Table 3

Capital Adequacy Requirements *in Lari*

		31/12/2018		31/12/2017	
	Minimum Requirements	**Ratios**	**Amounts (GEL)**	**Ratios**	**Amounts (GEL)**
1	**Pillar 1 Requirements**				
1.1	Minimum CET1 Requirement	≥4,5%	56,938,437	≥4,5%	53,458,511
1.2	Minimum Tier 1 Requirement	≥6%	75,917,915	≥6%	71,278,015
1.3	Minimum Regulatory Capital Requirement	≥8%	101,223,887	≥8%	95,037,353
2	**Combined Buffer**				
2.1	Capital Conservation Buffer	≥2,5%	31,632,465	≥2,5%	29,699,173
2.2	Countercyclical Buffer	≥0%	-	≥0%	-
2.3	Systemic Risk Buffer	≥0%	-	≥0%	-
	Existing Ratios/Amounts	**Ratios**	**Amounts (GEL)**	**Ratios**	**Amounts (GEL)**
4	CET1	13.4%	**169,150,627**	14.4%	**170,795,357**
5	Tier 1	13.4%	**169,150,627**	14.4%	**170,795,357**
6	Total regulatory Capital	17.8%	225,112,407	18.3%	217,192,975

Table 4

Additional factors which influenced the capital and liquidity level of the bank are the following:

- In the middle of 2018, the bank repaid dividends in amount of GEL 30.3 m.
- The Tier 1 capital was increased by GEL 29 m.

5 Balance sheet

Balance Sheet *in Lari*

N	Assets	31/12/2018 GEL	31/12/2018 FX	31/12/2018 Total	31/12/2017 GEL	31/12/2017 FX	31/12/2017 Total
1	Cash	22,040,128	29,688,695	51,728,823	23,993,488	25,467,757	49,461,245
2	Due from NBG	20,669,481	171,492,340	192,161,821	11,573,376	126,740,358	138,313,735
3	Due from Banks	15,265,601	105,865,914	121,131,515	14,000,181	56,779,188	70,779,369
4	Dealing Securities	0	0	0	0	0	0
5	Investment Securities	29,584,522	0	29,584,522	27,544,988	0	27,544,988
6.1	Loans	237,196,326	806,312,106	1,043,508,432	196,706,742	808,832,609	1,005,539,351
6.2	Less: Loan Loss Reserves	-6,357,124	-27,142,636	-33,499,760	-5,416,141	-29,123,258	-34,539,399
6	Net Loans	**230,839,201**	**779,169,471**	**1,010,008,672**	**191,290,601**	**779,709,351**	**970,999,952**
7	Accrued Interest and Dividends Receivable	2,077,200	3,716,102	5,793,302	1,563,730	4,112,025	5,675,755
8	Other Real Estate Owned & Repossessed Assets	0	X	0	0	X	0
9	Equity Investments	6,298,572	50,657	6,349,229	6,298,572	51,223	6,349,795
10	Fixed Assets and Intangible Assets	62,278,978	X	62,278,978	70,058,581	X	70,058,581
11	Other Assets	10,319,090	8,907,854	19,226,944	10,186,659	3,427,931	13,614,590
12	**Total assets**	**399,372,774**	**1,098,891,032**	**1,498,263,806**	**356,510,176**	**996,287,832**	**1,352,798,009**
	Liabilities						
13	Due to Banks	0	122,963,800	122,963,800	0	86,985,600	86,985,600
14	Current (Accounts) Deposits	94,628,321	130,338,628	224,966,949	82,992,069	125,245,181	208,237,251
15	Demand Deposits	54,342,049	175,724,413	230,066,462	40,060,359	177,267,190	217,327,549
16	Time Deposits	22,534,059	213,372,831	235,906,890	21,381,186	178,467,650	199,848,835
17	Own Debt Securities			0			0
18	Borrowings	30,614,358	363,717,800	394,332,158	0	370,700,740	370,700,740
19	Accrued Interest and Dividends Payable	1,046,810	8,016,812	9,063,621	941,435	7,423,065	8,364,500
20	Other Liabilities	11,443,003	10,623,147	22,066,150	11,094,455	7,050,457	18,144,912
21	Subordinated Debentures	0	82,265,500	82,265,500	0	64,805,000	64,805,000
22	**Total liabilities**	**214,608,600**	**1,107,022,931**	**1,321,631,531**	**156,469,504**	**1,017,944,883**	**1,174,414,387**
	Equity Capital						
23	Common Stock	88,914,815	X	88,914,815	88,914,815	X	88,914,815
24	Preferred Stock	0	X	0	0	X	0
25	Less: Repurchased Shares	0	X	0	0	X	0
26	Share Premium	36,388,151	X	36,388,151	36,388,151	X	36,388,151
27	General Reserves	0	X	0	0	X	0
28	Retained Earnings	51,329,308	X	51,329,308	53,080,655	X	53,080,655
29	Asset Revaluation Reserves	0	X	0	0	X	0
30	**Total Equity Capital**	176,632,275	X	176,632,275	178,383,622	X	178,383,622
31	**Total liabilities and Equity Capital**	**391,240,875**	**1,107,022,931**	**1,498,263,806**	**334,853,126**	**1,017,944,883**	**1,352,798,009**

Table 5

Besides the above mentioned factors, the balance sheet reflects the following movements:

- Customer funds increased by GEL 65.5 m.
- Subordinated debts increased by GEL 17.4 m.

6 Income statement

Income statement *in Lari*

N		31/12/2018 GEL	31/12/2018 FX	31/12/2018 Total	31/12/2017 GEL	31/12/2017 FX	31/12/2017 Total
	Interest Income						
1	Interest Income from Bank's "Nostro" and Deposit Accounts	2,007,780	853,856	2,861,637	2,932,842	299,682	3,232,524
2	Interest Income from Loans	23,228,068	57,127,594	80,355,663	18,757,313	57,423,219	76,180,532
2.1	from the Interbank Loans	347,018	0	347,018	813,632	0	813,632
2.2	from the Retail or Service Sector Loans	17,245,769	37,585,232	54,831,001	13,551,246	38,858,555	52,409,801
2.3	from the Energy Sector Loans	39,913	104,979	144,892	290	90,575	90,865
2.4	from the Agriculture and Forestry Sector Loans	602,115	1,870,357	2,472,472	324,991	1,395,412	1,720,403
2.5	from the Construction Sector Loans	1,944,329	2,652,856	4,597,184	720,186	1,928,475	2,648,661
2.6	from the Mining and Mineral Processing Sector Loans	165,962		1,240,791	133,781	658,627	792,408
2.7	from the Transportation or Communications Sector Loans	339,442	1,127,643	1,467,084	182,795	1,129,019	1,311,813
2.8	from Individuals Loans	1,492,473	9,882,596	11,375,069	2,156,370	10,092,966	12,249,336
2.9	from Other Sectors Loans	1,051,049	2,829,103	3,880,152	874,023	3,269,590	4,143,613
3	Fees/penalties income from loans to customers	213,325	588,129	801,453	245,707	785,115	1,030,822
4	Interest and Discount Income from Securities	1,262,336	0	1,262,336	1,700,977	0	1,700,977
5	Other Interest Income			0			0
6	**Total Interest Income**	26,711,509	58,569,579	85,281,088	23,636,839	58,508,016	82,144,855
	Interest Expense						
7	Interest Paid on Demand Deposits	1,940,750	2,007,271	3,948,021	1,779,176	2,677,719	4,456,895
8	Interest Paid on Time Deposits	1,881,742	5,898,369	7,780,111	2,324,427	6,762,817	9,087,243
9	Interest Paid on Banks Deposits	3,121	3,372,979	3,376,100	287	383,426	383,713
10	Interest Paid on Own Debt Securities	0	0	0	0	0	0
11	Interest Paid on Other Borrowings	813,024	17,216,220	18,029,243	0	16,660,147	16,660,147
12	Other Interest Expenses	0	0	0	0	0	0
13	**Total Interest Expense**	4,638,637	28,494,838	33,133,475	4,103,890	26,484,109	30,587,999
14	**Net Interest Income**	22,072,872	30,074,741	52,147,613	19,532,949	32,023,907	51,556,856
	Non-Interest Income						
15	Net Fee and Commission Income	-205,080	3,887,043	3,681,963	-641,270	3,126,219	2,484,949
15.1	Fee and Commission Income	5,682,496	5,578,174	11,260,670	4,811,397	5,212,160	10,023,558
15.2	Fee and Commission Expense	5,887,576	1,691,131	7,578,707	5,452,667	2,085,942	7,538,609
16	Dividend Income	0	15,473	15,473	0	15,834	15,834
17	Gain (Loss) from Dealing Securities			0			0
18	Gain (Loss) from Investment Securities		0	0		0	0
19	Gain (Loss) from Foreign Exchange Trading	9,254,563		9,254,563	9,847,475		9,847,475
20	Gain (Loss) from Foreign Exchange Translation	1,280,099		1,280,099	-4,863,562		-4,863,562
21	Gain (Loss) on Sales of Fixed Assets	123,059		123,059	1,035,345		1,035,345
22	Non-Interest Income from other Banking Operations	1,832,824	517,330	2,350,154	1,500,471	591,723	2,092,194
23	Other Non-Interest Income	1,097,339	205,876	1,303,215	475,171	114,142	589,314
24	**Total Non-Interest Income**	13,382,803	4,625,723	18,008,526	7,353,631	3,847,918	11,201,549
	Non-Interest Expenses						
25	Non-Interest Expenses from other Banking Operations	2,086,037	5,261,584	7,347,621	3,058,554	4,392,479	7,451,033
26	Bank Development, Consultation and Marketing Expenses	3,892,948	2,316,329	6,209,276	3,181,293	1,749,450	4,930,742
27	Personnel Expenses	13,400,333		13,400,333	14,391,650		14,391,650
28	Operating Costs of Fixed Assets	186,203		186,203	157,156		157,156
29	Depreciation Expense	4,919,317		4,919,317	6,092,196		6,092,196
30	Other Non-Interest Expenses	3,966,092	5,222	3,971,315	4,446,286	15,360	4,461,646
31	**Total Non-Interest Expenses**	28,450,931	7,583,134	36,034,065	31,327,135	6,157,289	37,484,423
32	**Net Non-Interest Income**	-15,068,127	-2,957,412	-18,025,539	-23,973,503	-2,309,371	-26,282,874
33	**Net Income before Provisions**	7,004,745	27,117,329	34,122,074	-4,440,554	29,714,536	25,273,982
34	Loan Loss Reserve	-109,296	X	-109,296	3,411,681	X	3,411,681
35	Provision for Possible Losses on Investments and Securities	0	X	0	0	X	0
36	Provision for Possible Losses on Other Assets	858,278	X	858,278	-1,166,781	X	-1,166,781
37	**Total Provisions for Possible Losses**	748,983	0	748,983	2,244,900	0	2,244,900
38	**Net Income before Taxes and Extraordinary Items**	6,255,762	27,117,329	33,373,092	-6,685,455	29,714,536	23,029,082
39	Taxation	4,867,266		4,867,266	2,867,409		2,867,409
40	**Net Income after Taxation**	1,388,497	27,117,329	28,505,826	-9,552,864	29,714,536	20,161,673
41	Extraordinary Items	85,834		85,834	-101,746		-101,746
42	**Net Income**	1,474,331	27,117,329	28,591,660	-9,654,609	29,714,536	20,059,927

Table 6

The comparison of income statements between 2017 and 2018 shows that net income has increased by 43% in 2018. The main factors which influenced income and expenses are:

- The increase of the total interest income by 5%, mainly from financing of medium and small sector loans;

- The high quality of the loan portfolio, which effected in low provisioning expenses;
- The increase of total non-interest income approximately by 61%, out of which the fee and commission income had the biggest effect (48%);
- Decrease of the total non-interest expenses by 4% which was achieved due to the automation and online availability of banking services.

7 Corporate governance

7.1 Shareholder structure

ProCredit Holding AG & Co. KGaA owns 100% of ProCredit Bank's shares.

ProCredit Holding AG & Co. KGaA, the superordinated company of the ProCredit group, has the legal form of a partnership limited by shares. ProCredit Holding is managed by the members of the Management Board of ProCredit General Partner AG. The Management Board of the general partner is responsible for managing ProCredit Holding in accordance with the requirements established in the law, in the Articles of Association and in the internal rules of procedure for ProCredit General Partner AG, as defined by its Supervisory Board.

The General Meeting of Shareholders is the highest authority in decision-making.

The rights, tasks and responsibilities of the management authorities are stipulated in the charter of the bank, final amendments to which are approved at the Shareholders' meeting on 19 December 2018.

The shareholders of the bank carry out their execution rights and decision-making on the General Meeting of Shareholders. The General Meeting of Shareholders reviews and discusses reports about the bank's activities provided by the Supervisory Board of the bank, approves the audited annual financial statements of the bank, makes decisions regarding profit distribution, provisioning, capital increase/decrease and selling of assets.

The General Meeting of Shareholders is authorized to free the members of the Supervisory Board of the bank with simple majority of votes.

	List of Shareholders owning 1% and more of issued capital, indicating Shares	
1	Prokredit holdingi (ProCredit Holding AG & Co. KGaA)	100%
	List of bank beneficiaries indicating names of direct or indirect holders of 5% or more of shares	
1	Zeitinger Invest GmbH	17.0%
2	KfW - Kreditanstalt für Wiederaufbau	13.2%
3	DOEN Paticipaties BV	12.5%
4	IFC - International Finance Corporation	10.0%
5	TIAA-Teachers Insurance and Annuity Association	8.6%

Table 7[1]

7.2 Supervisory Board of ProCredit Holding

The bank's immediate and ultimate parent company is ProCredit Holding AG & Co. KGaA.

[1] Starting from 4th quarter of 2018, the Pillar 3 report discloses the information about the exact shares of beneficiary owners.

ProCredit Holding AG & Co. KGaA ("ProCredit Holding") is a company listed on the Frankfurt Stock Exchance, which places emphasis on transparent corporate governance and open communication with all stakeholders. This approach and its development-oriented mission are supported by its international shareholders. The values upon which we have successfully built the ProCredit group include personal integrity and commitment, social responsibility and tolerance, open communication and transparency, as well as high professional standards. These principles pervade all aspects of how the ProCredit group is governed. Corporate Governance is an important chapter in the ProCredit Holding 2017 Impact Report, which is available on the ProCredit Holding website (https://www.procredit-holding.com/wp-content/uploads/2019/03/ProCredit_Impact_Report_2018_L.pdf).

The Supervisory Board of ProCredit Holding (the "Supervisory Board") has six members. The responsibilities of the Supervisory Board are defined in the German Stock Corporation Act (Aktiengesetz – "AktG") and German Banking Law (specifically Kreditwesengesetz – KWG § 25d). In addition, ProCredit Holding complies with the German Corporate Governance Code, except in circumstances outlined in the holding's Corporate Governance Report, which can be found in the ProCredit Holding Annual Report which is available on the ProCredit Holding website.

The main function of the Supervisory Board is the supervision of the management of ProCredit Holding, provided by ProCredit General Partner AG ("General Partner"). The General Partner also has a supervisory board made up of the same individuals as the Supervisory Board of ProCredit Holding.

With regard to the independence of its supervisory board members, ProCredit Holding follows the definition and provisions set out in Articles 5.4.1 and 5.4.2 of the German Corporate Governance Code.

Currently, all Supervisory Board members fulfill the Corporate Governance Code's definition of independence.

The composition of the Supervisory Board and its Internal Rules of Procedure generally reflect the requirements of Article 25d of the German Banking Act (Kreditwesengesetz – "KWG") and the relevant provisions of the German Corporate Governance Code (apart from the recommendation to have a regular limit to Supervisory Board members' term of office).

The Supervisory Board has determined that the composition of the Supervisory Board should duly represent members who apart from good knowledge of banking have:

- a good understanding of and interest in the group's focus region of operations
- the time and interest to travel to the region to understand and assess the operations of ProCredit subsidiaries, and ideally a seat on at least one supervisory board of a subsidiary
- a good understanding of and interest in development finance and sustainability aspects.

The Supervisory Board believes that it complies with the specified concrete objectives regarding its composition.

The Supervisory Board respects diversity when proposing members for appointment to the Supervisory Board. One member of the six-person Supervisory Board is a woman. The ProCredit Holding Disclosure Report, available on the website (https://www.procredit-holding.com/wp-content/uploads/2019/03/2018_PCH_Disclosure_Report_L.pdf) outlines how members of the Supervisory Board are appointed by the Annual General Meeting of Shareholders, with consideration given to the balanced and comprehensive knowledge, skills and experience of all Supervisory Board members and taking account of the requirements established in Section 25d KWG.

The Supervisory Board of ProCredit Holding typically takes no decisions which relate directly and specifically to ProCredit Bank Georgia. The role of the Supervisory Board is to supervise the Management of ProCredit Holding in the context of the overall performance and risk profile of the ProCredit Group. At the group level, Management reports to the Supervisory Board on the business and risk strategies of the group at least once per year and routinely reports on the status of implementation of the strategies. The Supervisory Board receives at least quarterly a Group Risk Report and a Group Audit Report. All ProCredit banks operate within the tight business and risk management framework thereby set by ProCredit Holding.

In the fiscal year 2018, the Supervisory Board held four routine in-person meetings and four telephone votes. Attendance and details of discussions in each meeting can be found in the Supervisory Board Report, published in the ProCredit Holding Annual Report.

The Supervisory Board examines the efficiency and effectiveness of its activities on a regular basis, and at least once in every calendar year.

7.3 Supervisory Board of the bank

The bank's business activities are supervised by the Supervisory Board, whose members are appointed by the General Meeting of Shareholders. For good reason, members of the Supervisory Board may be freed at any time by the General Meeting of Shareholders. Members of the Supervisory Board may not be at the same time bank's employees.

Based on ¾ of present votes, the Supervisory Board defines the bank's business strategy, approves policy guidelines, approves the annual business plan (including the annual operating budget) presented by the Board of Directors of the bank, discusses and approves the business operations report presented by the Board of Directors during the financial year and prepares the bank's annual report for submitting to the Shareholders' General Meeting.

Based on its discretionary right, the Supervisory Board appoints and releases the members of the Board of Directors of the bank at any time. The Supervisory Board appoints and dismisses the members of the Audit Committee.

The Supervisory Board makes decisions on sources for refinancing of the bank, issuance of bonds, loans from international financial institutions. The Supervisory Board delegates the relevant decisions regarding the borrowings to the Board of Directors of the bank.

The Supervisory Board approves the policy on conflict of interests and changes in policy. The Supervisory Board approves any transaction, which is permitted by the Georgian legislation, between the bank and a member of the Board of Directors or a member of the Supervisory Board.

	Members of Supervisory Board
1	Ilir I. Aliu
2	Jovanka Joleska Popovska
3	Sandrine Massiani
4	Wolfgang Bertelsmeier
5	Marcel Zeitinger

Table 8

The term of membership of the Bank's Supervisory Board is fixed for a period of 4 years or a shorter-term which is determined by the General Meeting of Shareholders. It is possible to re-appoint a member of the Supervisory Board. However, the termination is only in force when a new candidate is appointed. Upon

the dismissal of a member of the Supervisory Board, the candidate shall be appointed before the next meeting of the Supervisory Board.
The Supervisory Board appoints the chairperson from its members by a simple majority of votes. The chairperson is appointed for the same term as a member of the Supervisory Board. The Chairman of the Supervisory Board can be re-elected.
The Supervisory Board meetings are held at least once a quarter. At the Supervisory Board meeting, the quorum is composed of at least two thirds of the Supervisory Board members. Decisions on the Supervisory Board meetings are considered by a simple majority of votes presented. The decisions made by the Supervisory Board shall be summarized by a bank representative or a member of the Supervisory Board, which is signed by the Chairman of the Supervisory Board after consideration. The minutes of the Supervisory Board meetings are available to the shareholders for a review.
At the Supervisory Board meetings, the Board of Directors present and discuss pre-agreed issues, including but not limited to: loan portfolio development and customer funds, other funding sources, loan portfolio quality and other key risk indicators, key financial indicators, overview of banking products and market trends.

7.4 Board of Directors of the bank

The Board of Directors of the bank leads and performs activities related to the daily functioning of the bank in accordance with the business strategy defined by the Supervisory Board.
The members of the Board of Directors are appointed and dismissed by the Supervisory Board at any time by its discretion.

The Board of Directors of the bank is represented by 3 (three) Directors. The number of directors must be at least three in accordance with the charter of the bank. The Board of Directors shall make decisions by a simple majority of votes presented. The Board of Directors shall be appointed for a maximum period of four years or a shorter term which the Supervisory Board defines, with the right to re-appointment.

Members of Board of Directors
1 Ketevan Khuskivadze
2 Alex Matua
3 Natia Tkhilaishvili

Table 9[2]

Members of the Board of Directors meet the requirements of the Law of Georgia on "Activities of Commercial Banks" (Criteria for the Shareholders and Administrators of Commercial Banks) as well as the requirements set in the order of the President of the National Bank of Georgia 50/04 "Requirements for Administrators of Commercial Bank" (the Criteria for the Administrators of Commercial Banks). The members of the Board of Directors have many years of experience working in various departments in the bank. Each director has completed a full course of ProCredit Academy Management (Furth, Germany).

The Board of Directors delegates fulfillment of certain tasks within the scope of its competence, taking into consideration allocation of liability to the Bank's employees, if this does not contradict the legislation of Georgia. The bank operates a system of responsibility delegation, which is regularly monitored through the committees operating in the bank. At least 2 members of the Board of Directors are present at the

[2] Additional information about the members of the Board of Directors of ProCredit bank is presented on the bank's web site: www.procreditbank.ge.

committees. Attendance of the member of the Board of Directors which is responsible for the specific field is obligatory.

Members of the board of directors of the bank are responsible for the specific areas of their education and professional experience:

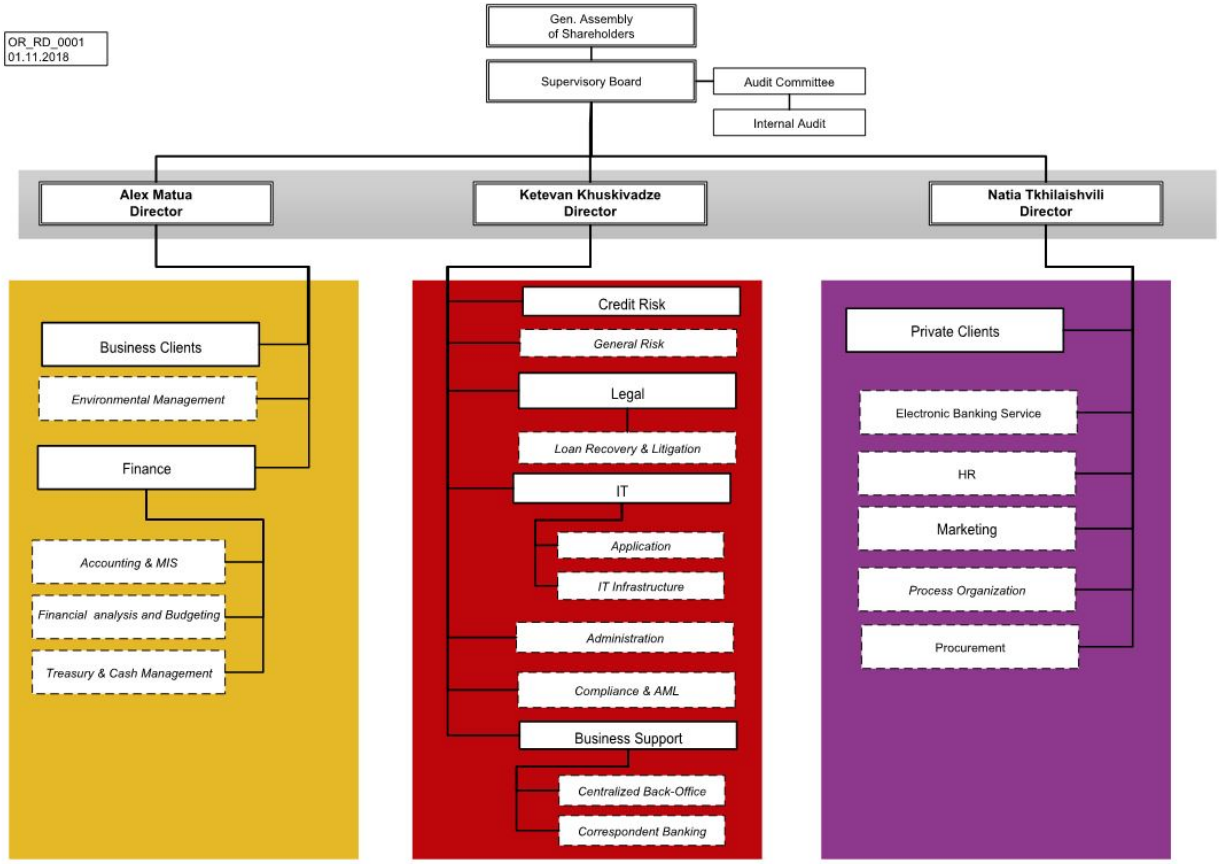


Table 10

7.5 Flow of information concerning risk

The Management of the bank is provided with regular daily, monthly and quarterly risk reports in a timely manner after the respective reporting date. Furthermore, escalation mechanisms and ad-hoc reporting are implemented in the event of new risks, non-compliance with existing limits or, for known risks, in case of a significant increase in the probability of occurrence or the loss amount.

The Management of ProCredit Bank works closely together with the Supervisory Board to achieve the goals of the company. The Management reports to the Supervisory Board in a regular, timely and complete manner concerning all matters which are of particular significance for the bank. This includes all relevant issues in regard to planning, business development, the risk situation, risk management and compliance. Information which is of material importance from a risk point of view is provided without delay to the Supervisory Board, independent of the regular quarterly reports on the risk situation. The Management of the bank and the Supervisory Board determine the strategic orientation of the company in consultation and discuss at regular intervals regarding the implementation status of the strategy. The

Supervisory Board must be informed of any changes in the management of risk control function, in the internal audit function or in the compliance officer position.

8 Risk management

8.1 Risk strategy

The ProCredit Bank's risk strategy and business strategy are updated annually. While the business strategy lists the objectives of the bank for all material business activities and presents measures to be taken to achieve them, the bank's risk strategy addresses the material risks arising from the implementation of the business strategy and defines the objectives and measures of risk management. The risk strategy is broken down into strategies for all material risks in the bank. Both the risk strategy and business strategy are approved by the Management of ProCredit Bank following discussions with the Supervisory Board.

An informed and transparent approach to risk management is a central component of ProCredit's socially responsible business model. This is also reflected in our risk culture, resulting in decision-making processes that are well-balanced from a risk point of view. The Code of Conduct, which is binding for all staff, plays a key role in this respect as it describes these principles.

In accordance with our simple, transparent and sustainable business strategy, our risk strategy is a conservative one. By following a consistent group-wide approach to managing risks, the aim is to ensure that the liquidity and capital adequacy of the bank continues to be appropriate at all times no matter if external conditions are volatile, as well as to achieve steady results.

The principles of our business activity, as listed below, provide the foundation for our risk management. The consistent application of these principles significantly reduces the risks to which the bank is exposed.

i. Focus on core business

The ProCredit Bank focuses on the provision of financial services to small and medium-sized businesses as well as to private clients. Accordingly, income is generated primarily in the form of interest income on customer loans and fee income from account operations and payments. All of the bank's other operations are performed mainly in support of the core business. ProCredit Bank assumes mainly credit risk, currency risk, interest rate risk, liquidity risk and operational risk in the course of its day-to-day operations.

ii. High degree of transparency, simplicity and diversification

ProCredit's focus on small and medium-sized businesses entails a very high degree of diversification in both customer loans and customer deposits. In terms of client groups, this diversification spans economic sectors, client groups (SMEs and private clients) and income groups. The diversification of the loan portfolio is an integral part of the bank's credit risk management policy. A further characteristic of our approach is that we seek to provide our clients with simple, easily understandable services. This leads to a high degree of transparency not only for the respective client, but also from a risk management point of view. Both the high degree of diversification and our simple, transparent services and processes result in a significant reduction of the bank's risk profile.

iii. Careful staff selection and intensive training

Responsible banking is characterised by long-term relationships not only with clients, but also with staff. This is why we select our staff very carefully and have invested heavily in staff training over many years. Besides high levels of technical professionalism, the result of our training efforts is above all an open and transparent communication culture. From a risk perspective, well-trained employees who are accustomed to voicing their opinions openly are an important factor for managing and reducing risk, specifically operational risk and fraud risk.

Key elements of risk management

Risk management comprises identifying, quantifying, managing, monitoring, controlling and reporting risks. In managing risks, the ProCredit Bank takes account of the respective regulations of the National Bank of Georgia, of the "Minimum Requirements for Risk Management" (MaRisk) stipulated by the German regulator, of relevant publications by national and international regulatory authorities and of our knowledge of the market acquired over many years. The mechanisms designed to hedge and mitigate risks are monitored regularly to ensure their appropriateness and effectiveness, and the procedures and methods used to manage risks are subject to ongoing further development. The key elements of risk management in the ProCredit Bank are presented below.

- ProCredit Bank applies a single common risk management framework, which is based on group-wide minimum standards and incorporates requirements set by the National Bank of Georgia. The risk management policies and standards are approved by the Management of ProCredit Bank and are updated at least annually. These specify the responsibilities and establish minimum requirements for managing, monitoring and reporting.
- All risks assumed are managed by ensuring at all times an adequate level of regulatory and internal capital of the bank.
- The annually conducted risk inventory ensures that all material and non-material risks are identified and, if necessary, considered in the strategies and risk management processes.
- Early warning indicators (reporting triggers) and limits are set and monitored for all material risks.
- Regular stress tests are performed for all material risks; stress tests are carried out for each individual risk category as well as across all risk categories.
- Regular and ad hoc reporting is carried out on the risk profile, including detailed descriptions and commentaries.
- Monitoring and control of risks and possible risk concentrations is carried out using comprehensive analysis tools for all material risks.
- The effectiveness of the chosen measures, limits and methods is continuously monitored and controlled.
- All new or significantly changed services undergo a thorough analysis before being used for the first time (New Risk Approval process). This ensures that new risks are assessed and all necessary preparations and tests are completed prior to implementation.

These key elements of risk management in the ProCredit Bank are based on the substantial experience we have gained over the past 20 years in the country and on a precise understanding of both our clients and the risks we assume. Although the operating environment in the country has improved over the last ten years, it is still characterised by relatively volatile macroeconomic and geopolitical environments. The

diversification of our business activities, combined with our comprehensive experience, provide a solid foundation for us to manage these risks.

8.2 Organisation of risk management and risk reporting

Risk management in the ProCredit Bank is the overall responsibility of the Management of the Bank, which regularly analyses the risk profile of the bank and decides on appropriate measures.

The Management of ProCredit Bank is supported by various committees.

- The Credit Risk Management Committees[3] monitor the credit risk profile of the bank. This includes the monitoring of individual risk positions, limit compliance, and the internal and regulatory requirements regarding the credit risk.
- The General Risk Management Committee monitors the overall risk profile of the bank, limit compliance and the internal and regulatory capital adequacy. The committee defines the risk tolerance limits within the limits set by the group-wide risk management framework and the National Bank of Georgia. It supports and advises the Management in connection with market risks, operational risks including fraud prevention and information security risk.
- The Asset and Liability Committee (ALCO) is responsible for monitoring the liquidity reserve and liquidity management of the bank, for setting interest rates on loans and deposits, co-ordinating measures aimed at securing funding for the ProCredit Bank and reporting on material developments in financial markets.
- Compliance and AML Committee supports and advises the Management in connection with the ongoing monitoring of the bank's risk profile regarding money laundering and compliance, as well as in the adoption of suitable measures to prevent AML risks. The committee is a forum for evaluating compliance risks, discussing the impact of changes in legal regulations and prioritising identified compliance risks.
- The Audit Committee supports and advises the Management in the approval of annual internal audit plans and in monitoring the timely implementation of measures to resolve the findings of internal and external auditors. Moreover, this body aims to achieve ongoing improvement in the Internal Audit Policy.

- The HR Committee is responsible for the approval of annual staffing and training plan, analyzing the development of the staff structure, staff turnover and the recruitment process, monitoring the staff assessment process and taking the appropriate action based on the results, annually reviewing the salaries and deciding on changes, approving staff transfers, changes of position, promotions, calls to attention, warning letters and periodically reviewing the bank's remuneration practice.

- The Eco Committee supports and advises the Management in connection with environmental impact improvement/mitigation resulted from lending activity, positioning of the bank as environmentally responsible organization and strengthening its reputation, increasing the level of the bank energy efficiency and encouraging rational use of natural resources, hereby reduction of costs, mitigation of risks resulted from negative environmental impact, raising awareness and the level of knowledge about environmental and energy efficiency topics among the bank staff and clients.

[3] Credit Risk and Business Committee, Loan Loss Provisions Committee, Portfolio Management and Analysis Committee, Arrears Committee, Litigation Committee.

The bank has an effective compliance management system which is supported by our Code of Conduct and our approach to staff selection and training. Compliance with the Code of Conduct is compulsory for all staff members. The compliance and risk management functions which bear responsibility for adhering to national banking regulations report regularly and on an ad-hoc basis to the Management of the bank and to the Group's responsible departments. Any conduct, which is inconsistent with the established rules, can be reported anonymously to an e-mail address established for the bank.

Internal Audit is an independent functional area within the bank who functionally reports to the Supervisory Board of the bank via an Audit Committee, which is subordinate to and appointed by the Supervisory Board. It provides support in determining what constitutes appropriate risk management and an appropriate internal control system within the bank. Once per year, the internal audit department of the ProCredit Bank carries out risk assessment of bank's activities in order to arrive at a risk-based annual audit plan. The Group Audit team monitors the quality of the audits conducted in ProCredit bank and provides technical guidance.

The Internal Audit Department audits and assesses the following:

1. The viability, effectiveness, efficiency and suitability of the internal control systems;
2. The application, viability, effectiveness and suitability of the risk management and control systems, the reporting and information systems and the financial and accounting systems;
3. The observance of existing legal and banking supervisory provisions as well as other regulations;
4. Compliance with operational guidelines, instructions and rules;
5. Compliance of all operational and business procedures with legal requirements and generally accepted standards and principles; the rules observed and the precautions taken to protect assets.

In principle, the Internal Audit Department is looking at the full set of processes, using a risk-based approach to identify review priorities.

Ad hoc audits might be undertaken as and when deemed appropriate by the Internal Audit Department.

In accordance with the banking legislation, the bank undergoes an external audit on an annual basis. The selection of external auditor is performed through the tender procedure. Based on the recommendations prepared by the Tender Committee, the Supervisory Board takes the final decision on appointing an external auditor.

The external audit process is always performed by so-called "Big 4" audit firms. However, in order to maintain impartiality of auditors, the bank consistently follows the practice of rotating audit firms.

In the bank, adequate processes and procedures for an effective internal control system are in place. The system is built around the principles of segregation of duties, dual control and, for all risk-relevant operations, the separation of front and back office up to the management level; this ensures that risk management and risk control are performed independently of front-office functions.

Risk management and risk controlling function of the bank is designed to define, measure, and monitor the risks in the operations of the bank, organise and coordinate the processes designed to control these risks in cooperation with the respective subdivisions of the bank. The main tasks are:

1. Analysis of existing and potential risks with the purpose of developing measures, methods and procedures for evaluating, controlling and monitoring them; definition of the degree of the bank's vulnerability to these risks;
2. Measurement of the current risks facing the bank;
3. Conducting market risk analysis based on the stress testing/scenario and gap analysis;
4. Ensuring the adequate design of the early warning system if required by internal/external regulations and/or bank's Management;
5. Monitoring of risks by preparing reports for the committees, the Management and the Supervisory Board of the bank;
6. Drafting decisions aimed at mitigation of risks for further consideration and approval by the Board of Directors and/or the respective committees of the bank;
7. Preparation and implementation of the measures for Heads of the bank departments/units with the purpose of improving the risk management efficiency within the field of their responsibilities, and increasing the awareness of the bank's management and employees about the banking risks threatening their activities;
8. Checking compliance of branches/service centres with operational rules and procedures by conducting on-site monitoring of branches/service centres and preparing reports.

Risk positions are analysed regularly, discussed intensively and documented in standardised reports. Each month ProCredit Bank prepares risk reports for the Group Risk Management Committee / bank's ALCO; on a quarterly basis, risk reports are delivered to the Supervisory Board of the bank, Audit Committee and bank's Risk Management Committees. Monitoring of risk situation and the overall risk profile of the bank is carried out through a review of these reports and of additional information generated by the responsible staff. If necessary, additional topic-specific ad hoc reporting occurs. The aim is to achieve transparency on the material risks and to be aware at an early stage if potential problems might be arising.

The risk department of the bank reports regularly to the different risk functions at ProCredit Holding, and the respective supervisory board is informed on at least a quarterly basis about all risk-relevant developments.

8.3 Risk statement and risk profile

The risk management processes of the ProCredit Bank have been designed in a suitable manner considering the nature, scale, complexity and riskiness of the business activities as well as the business strategy and the risk strategy of the bank. MaRisk, Basel Committee standards and relevant publications of national and international regulatory authorities are taken into account at all times during this process.

The processes for risk management take account of all material risks defined in the risk inventory; these processes were found to be appropriate and approved by the Management of the bank, and are subject to ongoing further development. As the business strategy of the ProCredit Bank focuses on SMEs, the credit risk associated with serving this client group constitutes the material item in the bank's risk profile.

A comprehensive set of early warning indicators (reporting triggers) and limits is used to measure, manage and limit risks. The limit system is the operational counterpart of the principles established in the risk policies, and it represents the risk tolerance level (risk appetite) defined by the Management. In addition to the limits for specific types of risk, e.g. limits for each borrower, limits for all material risks are set in the framework of the internal capital adequacy calculation. Ongoing monitoring is performed in order to identify potential concentrations within risk categories or between risk types; if necessary, decisions are taken on measures to reduce any risk concentrations.

Key risk indicators, which provide a comprehensive overview of the risk profile of the bank, are presented in the individual sections of the Pillar 3 report on the material risks and in the explanations regarding capital adequacy.

9 Credit risk

The ProCredit Bank defines credit risk as the risk that losses will be incurred if the party to a transaction cannot fulfil its contractual obligations at all, not in full or not on time. Within overall credit risk we distinguish between customer credit risk and counterparty risk (including issuer risk). Credit risk is the most significant risk facing the ProCredit Bank, and customer credit exposures account for the largest share of that risk.

9.1 Customer credit risk

9.1.1 Strategy and principles

The key objectives of our credit risk management are to achieve high loan portfolio quality, low risk concentrations within the loan portfolio and appropriate coverage of credit risks with loan loss provisions. For our lending operations with clients, we apply the following principles:

- intensively analysing the debt capacity of credit clients (the bank doesn't apply any scoring model)
- carefully documenting credit risk analyses and processes conducted during lending operations, ensuring that the analyses performed can be understood by knowledgeable third parties
- strictly avoiding over-indebtedness of bank's clients
- building a personal and long-term client relationship and maintaining regular contact
- strictly monitoring the repayment of credit exposures
- customer-oriented, intensified loan management in the event of past due loans
- collateral collection in the event of insolvency

The bank's framework for managing customer credit risk is presented in the relevant policies and standards. The policies define, among other things, the responsibilities for managing credit risk at the bank level, the principles for organising lending business, the principles of granting loans, and the framework for evaluating loan collateral. The standards contain detailed explanations of the bank's lending operations with business clients and private clients and of the range of credit facilities offered. They also set forth rules for restructuring, risk provisioning and write-offs. Thus, the policies and standards define risk-mitigating measures for the pre-disbursement phase (credit risk assessment) and the post-disbursement phase (e.g. regular monitoring of the financial situation, review of early warning indicators, and both intensified and problem loan management).

The ProCredit group divides its credit exposures into three categories: small and medium-sized business credit exposures and credit exposures to private clients. Small exposures are typically between USD 30,000 and USD 270,000, and medium exposures are above USD 270,000. The largest portion of loan portfolio is attributed to the clients with exposures between USD 50 000 and USD 250 000. Depending on the client category to which the respective credit exposure is assigned, different credit risk assessment processes are applied. These processes differ from one another in terms of the following attributes: degree of segregation of duties, type of information that provides the basis for the credit analysis, criteria for credit decisions, and collateral requirements. A strict separation of front- and back-office functions up to the management level is applied for risk-relevant credit exposures.

The experience of the ProCredit Bank has shown that a thorough creditworthiness assessment constitutes the most effective form of credit risk management. The credit decisions of the ProCredit Bank are therefore based on an analysis of the client's financial situation and creditworthiness. Regular on-site visits are performed for all clients to ensure an adequate consideration of their specific features and needs.

All credit decisions in the ProCredit Bank are taken by a credit committee. Its members have approval limits that reflect their expertise and experience. All decisions on medium credit exposures are taken by credit committees at the bank's head office. If the exposures are particularly significant for the bank, the decision is taken by the Supervisory Board, usually following a positive vote issued by the responsible team at ProCredit Holding.

Setting appropriate credit limits, deciding which services correspond to the financial needs of clients and determining the proper structure of the credit exposure form an integral part of the discussion process within the credit committee. In this context, the following general principles apply: The lower the amount of the credit exposure, the more meaningful the documentation provided by the client, the shorter the term of the credit exposure, the longer the client's history with the bank and the higher the account turnover of the client with the bank, the lower the collateral requirements will be.

The bank's credit risk management policies limit the possibility for unsecured credit operations. Depending on the riskiness and the term of the exposure, loans may also be issued without being fully collateralised. As a general rule, credit exposures with a higher risk profile are covered with collateral security, mostly through mortgages.

The early detection of increases in credit risk at the level of individual credit exposures is incorporated into all lending-related processes, resulting in a fast and efficient assessment of the degree of financial difficulty faced by clients. The respective indicators are developed and implemented for the early identification of risks based on quantitative and qualitative risk features. These include, but are not limited to, declining account turnover or volume, high usage of granted credit lines and overdrafts over a longer period of time, and arrears. The responsible member of staff checks whether there are indications of increased risk of default, and, if necessary, ensures that additional steps are taken in accordance with the policies. Reports on the affected portfolio are regularly given to the branch manager, the bank's head office and in aggregated form to the respective units at group level. The early warning indicators and the close monitoring of clients allow for appropriate tracking of increases in credit risk related to individual credit exposures (migration risk).

Once a higher risk of default is detected for a credit exposure, it is placed under intensified management. This centres around close communication with the client, identification of the source of higher credit default risk and close monitoring of the client's business activities. Decisions on measures to reduce the credit default risk for individual credit exposures are taken by the authorised decision-making bodies for the credit exposures in question. In addition, specialised recovery officers may be called in to support the intensified management of the credit exposure.

When a loan is classified as a problem credit exposure, recovery officers take over responsibility for dealings with the client. The bank generally considers an exposure to be problematic when there is strong doubt that the client will be able to meet his/her contractual obligations, e.g. in the case of bankruptcy or arrears exceeding 90 days. If necessary, the recovery officers are supported by litigation officers (legal department) and/or specialists in the sale of assets or collateral.

Credit risk at the portfolio level is assessed on a monthly basis and, if necessary, more frequently. This includes an analysis of portfolio structure and quality, restructured exposures, write offs, the coverage ratio (risk provisions in relation to past due portfolio) and concentration risk. For the ProCredit Bank, important indicators of loan portfolio quality are the shares of the portfolio that are past due by more than 30 days (PAR>30) or more than 90 days (PAR>90). We also track the degree to which credit exposures past due by more than 30 days and 90 days are covered with loan loss provisions, as an indicator of the adequate provisioning of our loan portfolio. The portfolio of restructured credit exposures, the corresponding provisions and the level of write offs are also closely monitored.

In addition, three asset quality indicators have been introduced, on the basis of which the bank's loan portfolio is divided into the categories: performing, underperforming and defaulted. The process of assigning exposures to these categories is based on a risk classification system and on additional risk characteristics of the exposures (e.g. whether a loan has been restructured). The indicators allow for a clear overview of the quality of the bank's portfolio and provide support for the credit risk management process.

Concentration risk in the customer loan portfolio is effectively limited by a high degree of diversification. This diversification is a consequence of lending to small and medium-sized businesses in various economic sectors and regions. In addition, the ProCredit Bank limits the concentration risk of loan portfolio by means of the following requirements: Large credit exposures (those exceeding 10 % of regulatory capital of the bank) require the approval of the Group Risk Management Committee. No individual large credit exposure may exceed 25 % of regulatory capital of the bank, and the sum of all large credit exposures of the bank may not exceed 150 % of its regulatory capital.

9.2 Counterparty risk, including issuer risk

The ProCredit Bank defines counterparty risk, including issuer risk, as the risk that a counterparty/issuer cannot fulfil its contractual obligations at all, not in full or not on time. Counterparty risk in the ProCredit Bank mainly arises from keeping highly liquid assets for the purpose of managing liquidity. There are also structural exposures towards the National Bank of Georgia in the form of mandatory minimum reserves.

Counterparty risk is managed according to the principle that our liquidity must be placed securely and in a manner which is as diversified as possible. While the bank tries to generate some income from these assets, the overriding objective is to ensure secure placement and timely availability, i.e. risk considerations predominate. For this reason, we only work with carefully selected, reliable banks which normally have high credit ratings, we typically place our money for short terms (up to one month, but typically shorter) and we use only a very limited number of simple financial instruments.

Issuer risk is likewise managed according to these principles. The ProCredit Bank is prohibited from engaging in speculative trading. As a matter of principle, only highly liquid papers are bought, typically with a maximum maturity of one year. Liquidity in local currency is predominantly invested in the papers of the NBG or bonds issued by the Ministry of Finance of Georgia. EUR or USD, on the other hand, are generally placed with banks in the OECD countries. The impact of market price changes on the bank is limited. The reasons are that the volume of securities is rather low, their maturities are short and issuers are carefully selected based on conservative risk criteria.

Typically, our counterparties are the National Bank of Georgia, the Georgian State and commercial banks. The main types of exposure are account balances, short-maturity term deposits, highly liquid securities, and, on a very limited scale, simple derivative instruments for liquidity management and hedging purposes (particularly foreign currency swaps).

We effectively limit counterparty and issuer risk through our conservative investment strategy. Due to mandatory minimum reserves, a concentration exists with regard to exposures towards the National Bank of Georgia. Since 2010 the ProCredit group has insured the mandatory reserves in foreign currency with guarantees from the Multilateral Investment Guarantee Agency (MIGA).

The exposure towards counterparties and issuers is managed on the basis of a limit system, as is the case for customer credit risk. ProCredit Bank concludes transactions only with counterparties that have previously been carefully analysed and for which a limit has been approved. The total limit towards a non-OECD bank or banking group may not exceed 10 % of the ProCredit Bank's CRR capital without prior additional approval from Group ALCO or the Group Risk Management Committee. For an OECD bank, the threshold is 25 %. The typical maximum maturity of our term deposits is one month; longer maturities than 3 months must be approved by Group ALCO or the Group Risk Management Committee. Approval is likewise required before any investments in securities, except for NBG papers in the local currency with a remaining maturity of up to three months.

In order to avoid risk concentrations, an additional maximum limit towards each banking group and each state group (total exposure towards central bank, government and state-owned entities) exists.

9.3 Default risk arising from derivative positions

In the ProCredit Bank, derivatives are utilised to an extremely limited extent. They are only used to hedge foreign currency; the bank may not be engaged in for the purposes of proprietary or speculative trading. The following derivatives are relevant for the ProCredit Bank:

- FX swaps

For derivative exposures, the same risk classification, limit-setting and monitoring processes apply as for counterparty risk. The bank conducts FX swaps only with ProCredit Bank Germany.

Due to the type of counterparty and low volume of derivatives in the ProCredit Bank, possible correlations between counterparty/issuer risk and market risks are negligible.

9.4 Use of external ratings and credit risk mitigation techniques in the credit risk standardised approach

The ProCredit Bank exclusively uses the standardised approach to determine its exposure to credit risk. The bank has nominated the rating agency Fitch Ratings for the exposure classes "central governments or central banks", "institutions" and "institutions and corporates with a short-term credit assessment". Since our customers are usually not rated, ProCredit Bank does not use ratings for the exposure class "corporates" and "retail".

For exposures where an external credit assessment is available, risk weighting is determined on the basis of that external rating. For unrated exposures, risk weighting of the respective parent company is taken. In all other cases, the exposure is treated as unrated.

10 Market risks

Market risks comprise the risk of potential losses from shifts in market prices, such as exchange rates or other parameters which influence prices. Relevant market risks for ProCredit Bank are foreign currency risk and interest rate risk in the banking book. ProCredit Bank manages market risks in such a way that their impact is as limited as possible from an overall risk perspective. In accordance with the bank's risk

strategy, foreign currency risk and interest rate risk may not be incurred for speculative purposes; foreign currency derivatives and interest rate derivatives may only be used for hedging purposes or to obtain liquidity. ProCredit bank is strictly a non-trading book institution.

10.1 Foreign currency risk

We define foreign currency risk as the risk that an institution incurs losses or is negatively affected by exchange rate fluctuations. Foreign currency risk can have adverse effects on income and can lead to a decline in regulatory capital ratios.

Results are impacted negatively when the volume of its assets and liabilities denominated in foreign currencies do not match and the exchange rates move unfavourably (depreciation of the local currency). The key risk indicator that captures the balance sheet discrepancy for each currency is the open currency position (OCP). The total OCP is limited to 10 % of the bank's CRR capital, unless deviation from this limit has been approved by the Group ALCO or Group Risk Management Committee. A threshold of 7.5 % of a ProCredit bank's CRR capital has been defined as an early warning indicator for the total OCP, and ±5 % for each individual currency OCP.

Foreign currency risk can reduce regulatory capital ratios as the capital of the bank is held in the local currency while many of the assets it supports are denominated in foreign currency. In that case, local currency depreciation can result in a significant deterioration of capital adequacy if the foreign currency assets appreciate (from a local perspective) and the bank therefore has higher risk-weighted assets but the capital remains unchanged. To mitigate this risk, the bank aims to increase the share of assets in the local currency. At least quarterly, currency risk stress tests are performed within the capital adequacy forecasting process that depict the effects of unfavourable exchange rate developments on the bank's capital ratios.

10.2 Interest rate risk in the banking book

Interest rate risk is the risk of incurring losses driven by changes in market interest rates and arises from structural differences between the repricing maturities of assets and liabilities. It is measured on a regular basis, at least quarterly.

In order to manage interest rate risk, ProCredit Bank focuses on issuing variable-rate loans. In this way, the repricing maturities of assets can be better matched to the repricing maturity of liabilities, even when liabilities have shorter maturities than loans. In order to grant variable-rate loans in a transparent manner, the bank uses a publicly available interest rate as a benchmark when adjusting the interest rates (LIBOR, EUROBOR, the NBG refinancing rate). Financial instruments to mitigate interest rate risk (hedges) are not available in local currency.

The bank's approach used to measure, monitor and limit interest rate risk is based on repricing gap analyses. The assets and liabilities are distributed across time buckets according to the terms of the underlying contractual agreements. The bank measures the interest rate risk based on two indicators: EVI – economic value impact, a longer-term perspective, and IEI – interest earnings indicator, 12 months perspective.

We assume a parallel shift of the interest rate curve. For EUR and USD the interest rate shock is ± 200 basis points, whereas for local currency the magnitude of the shock is derived on the basis of a historical analysis. Sight deposits and savings accounts are included in the gap analyses according to their expected repricing maturities. These maturities are derived from an analysis of historical developments. The economic value impact (EVI) when simulating a simultaneous detrimental (upward or downward)

interest rate shock across all currencies must not exceed 15 % of the bank's CRR capital, unless approved by the Group Risk Management Committee; the early warning indicator for each currency is set at 10 % (non-netted in each case). The P&L effect is deemed significant if it exceeds 5% of the bank's CRR capital (early warning indicator). The P&L effect must not exceed 10 % of the bank's CRR capital (non-netted in each case).

11 Liquidity risks

11.1 Liquidity and funding risk

Liquidity and funding risk addresses the ProCredit Bank's short- and long-term ability to meet its financial obligations in a complete and timely manner, even in stress situations.

In general, liquidity and funding risk is limited in the bank by the fact that we primarily issue instalment loans with monthly repayments, financed largely by customer deposits. Our deposit-taking operations focus on our target group of business clients and savers, with whom we establish strong relationships. The financial crisis has shown that our customer deposits are a stable and reliable source of funding. As of end-December 2017, the largest funding source was customer deposits.

We measure our short-term liquidity risk using a liquidity gap analysis, among other instruments, and monitor this risk based on a 30-day liquidity indicator (Sufficient Liquidity Indicator, SLI), as well as in accordance with the minimum liquidity ratios stipulated by the National Bank of Georgia (NBG Liquidity Coverage Ratio, LCR) and CRR (CRR Liquidity Coverage Ratio, LCR). The SLI measures whether the institution has sufficient liquidity for the expected inflows and outflows of funds in the next 30 days. The calculation applies outflows derived from historical analyses of deposit movements in the banks. Liquidity Coverage Ratios indicate whether the bank has sufficient liquidity to cover the net outflows expected in the next 30 days, even in the event of a specified severe economic shock scenario. Additionally, the bank conducts regular analysis of the liquidity needs for longer stress periods (up to 3 months) and maintains respective limits.

In addition, early warning indicators are defined and monitored. A key indicator in this respect is the deposit concentration indicator, which ensures that the bank holds sufficient highly liquid assets at all times to be able to pay out deposits of a higher volume.

Market-related, combined and longer-term stress tests are conducted monthly and ad hoc to make sure that ProCredit Bank keeps sufficient liquid funds to meet its obligations, even in difficult times. Moreover, the bank has a liquidity contingency plan. If unexpected circumstances arise and the bank proves not to have sufficient liquid funds, the ProCredit group has also developed a liquidity contingency plan and ProCredit Holding would step in as a "lender of last resort". ProCredit Holding keeps an adequate liquidity reserve available for this purpose. The amount of the liquidity reserve is determined on the basis of group stress tests and monitored on a regular basis.

The liquidity of the bank is managed on a daily basis by the treasury department based on cash flow projections which are approved by the ALCO and monitored by the risk management department on a daily basis.

Funding risk is the danger that additional funding cannot be obtained, or can only be obtained at significantly higher costs. It therefore covers parts of the non-systemic effect of interest rate changes. This risk is mitigated by the fact that we finance our lending operations primarily through retail customer

deposits, supplemented by long-term funds from international financial institutions (IFIs). We make little use of interbank and financial markets.

ProCredit Bank manages, measures and limits funding risk through business planning, maturity gap analysis and relevant indicators. The funding needs of the bank, identified in the business planning process, are monitored and regularly reviewed at group level, as well. Group ALCO and bank's ALCO monitor the progress of all individually significant transactions with external funding providers, especially international financial institutions. ProCredit Holding and the ProCredit Bank Germany also offer bridge financing in the event that a funding project is delayed. Two indicators additionally restrict the level of funding from the interbank market to a low level.

11.2 Encumbered and unencumbered assets

Assets are deemed to be encumbered when they have been pledged or are committed to collateral agreements or agreements to improve the credit assessment of on- or off-balance sheet transactions and it is not possible to withdraw these assets from the terms of such agreements (e.g. pledges for funding purposes).

The ProCredit Bank has a limited amount of encumbered assets, as the bank largely funds its activities through deposits. The encumbered assets comprise primarily assets in local currency which are committed to collateral agreements with the National Bank of Georgia in case the bank will take 7-days refinancing loan from the NBG. In order to be pledged with the NBG, these assets shall comply with certain criteria which are stipulated in the respective decree of the National Bank of Georgia.

12 Operational risk

In line with CRR, we define operational risk as the risk of loss resulting from inadequate or failed internal processes, people or systems or from external events. This definition includes fraud risk, IT and information security risks, legal risk, reputational risk and outsourcing risk. Policies on operational risk management have been implemented since 2009; they have been approved by the Management of the bank and are updated annually. The principles set forth in the policies are in compliance with the requirements for the standardised approach for operational risk pursuant to CRR, the operational risk management regulations of the National Bank of Georgia and international best practices.

The aim of operational risk management is to detect risks at an early stage and to avoid recurrence of loss events. The main tools utilised are the group-wide Risk Event Database (RED), the annual risk assessments of operational and fraud risks, established Key Risk Indicators (KRI) and the analysis of all new services and processes in a structured procedure, the New Risk Approval (NRA) process.

The Risk Event Database was developed to ensure that all operational risk events identified in the ProCredit group are documented, analysed and communicated effectively. All ProCredit banks document their risk events using the provided framework, which ensures that adequate attention is paid to the implementation of necessary corrective or preventive measures for reducing or avoiding operational and fraud risk.

In contrast to the ex-post analysis of risk events as recorded in the Risk Event Database, annual risk assessments are systematically performed in order to identify and evaluate key risks and assess the adequacy of the control environment. These two tools complement each other and provide an overall picture of the operational risk profile for ProCredit Bank.

Risk indicators are also used to identify elevated fraud risk in specific areas of banking operations or specific outlets that could be used by potential fraudsters. These indicators are analysed regularly and where needed preventive measures are agreed on.

To complete the management of operational risk, all new services need to be analysed to identify and manage potential risks before implementation (NRA process).

In order to limit IT risks, the ProCredit group has defined standards for IT infrastructure, business continuity and information security. At bank level, ProCredit Bank incorporates the requirements from the National Bank of Georgia into the IT/information security risk management framework. Regular controls of information security and business continuity are part of existing processes and procedures. The bank carries out a classification of its information assets and conducts an annual risk assessment on its critical information assets. The business continuity framework implemented in the bank ensures that these risks are understood by all members of staff that critical processes are identified and that resources are allocated to restore operations, in line with the prioritisation of processes.

Information about historical operational losses *in Lari*

		31/12/2018	30/09/2018	30/06/2018
1	Total amount of losses	33,138	15,496	29,951
2	Total amount of losses, exceeding GEL 10,000	17,599	0	12,126
3	Number of events with losses exceeding GEL 10,000	1	0	1
4	Total amount of 5 biggest losses	33,126	15,218	28,583

Table 11

13 Risks arising from money laundering, terrorist financing and other acts punishable by law

The prevention of money laundering and terrorist financing is a key function of the bank. The business ethics and strong corporate values of the ProCredit group and of ProCredit bank play a key role in this regard. PCBG consistently applies the Know Your Customer (KYC) principle to all customers. Furthermore, in addition to complying with national rules and regulations, ProCredit Group and ProCredit Bank implement the requirements stipulated by the German Money Laundering Act, as well as the requirements applicable at the European level.
In order to consistently monitor accounts and transactions, the bank uses specialized software to detect conspicuous activities and identify business relationships involving money from dubious sources. The system brings conspicuous activity to the attention of the AML Officer of the bank, who then researches the background of the respective transaction or business relationship.
The AML framework of the bank ensures that:

- the bank appoints an AML Officer who regularly reports to the Management Board as well as to the Group AML Officer at ProCredit Holding
- the bank applies a strict Know Your Customer and Know Your Correspondent approach in its customer due diligence and correspondent banking procedures
- Group AML and the bank annually assesses the risk of money laundering and terrorist financing throughout the ProCredit group on the basis of a distinct risk model.
- the bank staff members receive AML training when they first join the institution and thereafter on an ongoing basis within the framework of the training plan
- the bank maintains a risk classification of its customers to prevent money laundering and terrorist financing and applies due diligence and monitoring procedures accordingly

- The bank applies consistent standards for data and transaction monitoring and adheres to international sanctions and embargoes.

14 Capital adequacy

14.1 Capital management

Capital management in the ProCredit group is guided by the principle that neither a ProCredit bank nor the ProCredit group as a whole may at any time incur greater risks than they are able to bear. This principle is monitored using different indicators for which early warning indicators and limits have been established. The indicators for ProCredit bank include, in addition to regulatory standards of the National Bank of Georgia, a capital adequacy calculation in accordance with CRR requirements, a Tier 1 leverage ratio in accordance with CRR and an internal capital adequacy assessment.

The capital management framework has the following objectives:

- compliance with regulatory capital requirements
- ensuring internal capital adequacy
- compliance with the internally defined capital requirements and creation of a sufficient capital buffer to ensure the bank's capacity to act
- support for the bank in implementing its plans for continued growth

Whereas the Pillar 1 capital requirements for the ProCredit group are imposed and monitored by BaFin and by the Supervisory College pursuant to Section 8a KWG, the ProCredit Bank is subject to the requirements imposed by the national supervisory authority.

In Georgia, the implementation of the new combined regulation based on Basel II and Basel III came into force in 2014. On 28 October 2013, the National Bank of Georgia (NBG) published the "Regulation on Capital Adequacy Requirements for Commercial Banks" (Decree N100/04 of the President of the National Bank of Georgia), which is in turn based on the three Pillars as defined by the internationally accepted capital adequacy framework of the Basel Committee on Banking Supervision, Capital Requirements Regulation – (EU) 575/2013 (CRR) and Capital Requirements Directive 2013/36/EUR (CRD IV).

14.2 Pillar 1 and combined buffer

Starting from December 2017, the NBG reviewed the minimum Pillar 1 and Pillar 2 capital requirements and defined additional capital buffers. The minimum requirements for Common Equity Tier 1, Tier 1 and total regulatory capital have been decreased and minimums of 4.5 %, 6 % and 8 %, respectively (7 %, 8.5 %, 10.5 % previously) have been established, excluding additional capital buffers. JSC ProCredit Bank, Georgia is required to hold own funds, which are at all times greater than or equal to the above capital requirements.

Furthermore, banks are required to hold additional combined buffer through Common Equity Tier 1. The combined buffer consists of the conservation, the countercyclical and the systemic buffers. The rate for the conservation buffer has been set at 2.5 % of risk-weighted assets, while a rate of 0 % has been set for the countercyclical buffer for all banks. The countercyclical buffer can vary within the range from 0 % to 2.5 % and shall be reviewed periodically, based on the financial and macroeconomic environment. For systemically important commercial banks, the systemic buffer has been introduced. PCB Georgia is not considered a systemic bank; therefore, 0 % for systemic buffers is required from the bank.

14.3 Pillar 2

In accordance with Basel III framework, commercial banks within the framework of Pillar 2, should hold capital adequacy buffers for those risks that aren't sufficiently covered under Pillar 1. With the objective to formalize and establish this framework National Bank of Georgia introduced "Rule on Additional Capital Buffer Requirements for Commercial Banks within of Pillar 2".

In accordance with this rule, Pillar 2 capital requirements include requirements for unhedged currency induced credit risk buffer, which was previously integrated in Pillar 1.

Besides abovementioned buffer, Pillar 2 framework determines capital buffer for credit portfolio concentration risk (single name as well as sectoral concentration risk), net stress-test buffer based on supervisory stress-test results and net GRAPE buffer set determined through the supervisory process - General Risk Assessment Program (GRAPE) by NBG.

It's important to note, that capital buffers under Pillar 2 should be proportionately incorporated in capital requirements (Common Equity Tier 1 4.5%, Tier 1 capital 6% and Total Regulatory Capital 8%). Therefore, 56 % of capital required under Pillar 2 should be held through Common Equity Tier 1, while 75% through Tier 1 capital instruments (table 12).

		Common Equity Tier 1	Tier 1	Total Regulatory Capital
Pillar 1	Basel III min requirements	4.50%	6.00%	8.00%
	Conservation buffer	2.50%	2.50%	2.50%
	Countercyclical buffer	[0%-2.5%]	[0%-2.5%]	[0%-2.5%]
	Systemic buffers	n%	n%	n%
Pillar 2	Unhedged currency induced credit risk buffer	n x (min)56%	n x (min)75%	n%
	Name concentration risk buffer	n x (min)56%	n x (min)75%	n%
	Sectoral concentration risk buffer	n x (min)56%	n x (min)75%	n%
	Net stress-test buffer	n x (min)56%	n x (min)75%	n%
	Net GRAPE buffer	n x (min)56%	n x (min)75%	n%

Table 12

For the purpose of complying with these requirements commercial banks have been given appropriate timeframes (table below).

GRAPE buffer distribution among capital elements	31-01-18	31-12-18	31-12-19	31-12-20	31-12-21 and after
Common Equity Tier 1	0%	15%	30%	45%	56%
Tier 1	0%	20%	40%	60%	75%
Total Regulatory Capital	100%	100%	100%	100%	100%

Table 13

As a result of the amendments to capital adequacy requirements, when a commercial bank breaches new total capital requirement it will be considered that combined buffer requirement is breached first. In such case, in accordance with updated "Regulation on Capital Adequacy Requirements for Commercial Banks" distribution of own equity instruments, including distributions of dividends, are prohibited.

14.4 Regulatory capital

Common Equity Tier 1 represents the main portion of bank’s Regulatory Capital (GEL 169m after the regulatory adjustments). The bank does not have the Additional Tier 1 capital. Tier 2 capital is also part of the Regulatory Capital, which consists of subordinated debts and general reserves (GEL 56m).

N	Regulatory capital	*in Lari*
1	**Common Equity Tier 1 capital before regulatory adjustments**	**176,632,275**
2	Common shares that comply with the criteria for Common Equity Tier 1	88,914,815
3	Stock surplus (share premium) of common share that meets the criteria of Common Equity Tier 1	36,388,151
4	Accumulated other comprehensive income	0
5	Other disclosed reserves	0
6	Retained earnings (loss)	51,329,308
7	**Regulatory Adjustments of Common Equity Tier 1 capital**	**7,481,648**
8	Revaluation reserves on assets	0
9	Accumulated unrealized revaluation gains on assets through profit and loss to the extent that they exceed accumulated unrealized revaluation losses through profit and loss	0
10	Intangible assets	1,287,076
11	Shortfall of the stock of provisions to the provisions based on the Asset Classification	0
12	Investments in own shares	0
13	Reciprocal cross holdings in the capital of commercial banks, insurance entities and other financial institutions	0
14	Cash flow hedge reserve	0
15	Deferred tax assets not subject to the threshold deduction (net of related tax liability)	0
16	Significant investments in the common equity tier 1 capital (that are not common shares) of commercial banks, insurance entities and other financial institutions that are outside the scope of regulatory consolidation	0
17	Holdings of equity and other participations constituting more than 10% of the share capital of other commercial entities	6,194,572
18	Significant investments in the common shares of commercial banks, insurance entities and other financial institutions (amount above 10% limit)	0
19	Investments in the capital of commercial banks, insurance entities and other financial institutions where the bank does not own more than 10% of the issued share capital (amount above 10% limit)	0
20	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	0
21	The amount of significant Investments and Deferred Tax Assets which exceed 15% of common equity tier 1	0
22	Regulatory adjustments applied to Common Equity Tier 1 resulting from shortfall of Tier 1 and Tier 2 capital to deduct investments	0
23	**Common Equity Tier 1**	**169,150,627**
24	**Additional tier 1 capital before regulatory adjustments**	**0**
25	Instruments that comply with the criteria for Additional tier 1 capital	0
26	Including:instruments classified as equity under the relevant accounting standards	0
27	Including: instruments classified as liabilities under the relevant accounting standards	0
28	Stock surplus (share premium) that meet the criteria for Additional Tier 1 capital	0
29	**Regulatory Adjustments of Additional Tier 1 capital**	**0**
30	Investments in own Additional Tier 1 instruments	0
31	Reciprocal cross-holdings in Additional Tier 1 instruments	0
32	Significant investments in the Additional Tier 1 capital (that are not common shares) of commercial banks, insurance entities and other financial institutions	0
33	Investments in the capital of commercial banks, insurance entities and other financial institutions where the bank does not own more than 10% of the issued share capital (amount above 10% limit)	0
34	Regulatory adjustments applied to Additional Tier 1 resulting from shortfall of Tier 2 capital to deduct investments	0
35	**Additional Tier 1 Capital**	**0**
36	**Tier 2 capital before regulatory adjustments**	**55,961,780**
37	Instruments that comply with the criteria for Tier 2 capital	42,116,500
38	Stock surplus (share premium) that meet the criteria for Tier 2 capital	0
39	General reserves, limited to a maximum of 1.25% of the bank's credit risk-weighted exposures	13,845,280
40	**Regulatory Adjustments of Tier 2 Capital**	**0**
41	Investments in own shares that meet the criteria for Tier 2 capital	0
42	Reciprocal cross-holdings in Tier 2 capital	0
43	Significant investments in the Tier 2 capital (that are not common shares) of commercial banks, insurance entities and other financial institutions	0
44	Investments in the capital of commercial banks, insurance entities and other financial institutions where the bank does not own more than 10% of the issued share capital (amount above 10% limit)	0
45	**Tier 2 Capital**	**55,961,780**

Table 14

Common Equity Tier 1 is subject to regulatory adjustments. Intangible assets and equity and other participations constituting more than 10% of the share capital of other commercial entities are deducted from Common Equity.

General reserves, which form Tier 2 capital, are limited to a maximum of 1.25% of the bank's credit risk-weighted exposures. As of December 2018, the bank's total general reserves exceed the 1.25% of credit

risk-weighted exposures and, as the results, the reserves in volume of GEL 13.8 m, which are included into Tier 2 capital, represent 1.25% of credit risk-weighted exposures.

Table below shows the reconciliation of balance sheet to regulatory capital.

Reconciliation of balance sheet to regulatory capital — *in Lari*

N	On-balance sheet items per standardized regulatory report	Carrying values as reported in published stand-alone financial statements per local accounting rules	linkage to capital table
1	Cash	51,728,823	
2	Due from NBG	192,161,821	
3	Due from Banks	121,131,515	
4	Dealing Securities	0	
5	Investment Securities	29,584,522	
6.1	Loans	*1,043,508,432*	
6.2	*Less: Loan Loss Reserves*	*-33,499,760*	
6.2.1	*Of which Loan Loss General Reserves*	*-13,845,280*	*Table 14 (Capital), N39*
6	Net Loans	1,010,008,672	
7	Accrued Interest and Dividends Receivable	5,793,302	
8	Other Real Estate Owned & Repossessed Assets	0	
9	Equity Investments	6,349,229	
9.1	*Of which above 10% equity holdings in financial institutions*	*6,194,572*	*Table 14 (Capital), N17*
9.2	*Of which significant investments subject to limited recognition*	*0*	
9.3	*Of which below 10% equity holdings subject to limited recognition*	*0*	
10	Fixed Assets and Intangible Assets	62,278,978	
10.1	*Of which intangible assets*	1,287,076	*Table 14 (Capital), N10*
11	Other Assets	19,226,944	
12	**Total assets**	**1,498,263,806**	
13	Due to Banks	122,963,800	
14	Current (Accounts) Deposits	224,966,949	
15	Demand Deposits	230,066,462	
16	Time Deposits	235,906,890	
17	Own Debt Securities	0	
18	Borrowings	394,332,158	
19	Accrued Interest and Dividends Payable	9,063,621	
20	Other Liabilities	22,066,150	
20.1	*Of which off-balance elements Loss General Reserves*	781,998	
21	Subordinated Debentures	82,265,500	
21.1	*Of which tier II capital qualifying instruments*	*42,116,500*	*Table 14 (Capital), N37*
22	**Total liabilities**	**1,321,631,531**	
23	Common Stock	88,914,815	*Table 14 (Capital), N2*
24	Preferred Stock	0	
25	Less: Repurchased Shares	0	
26	Share Premium	36,388,151	*Table 14 (Capital), N3*
27	General Reserves	0	
28	Retained Earnings	51,329,308	*Table 14 (Capital), N6*
29	Asset Revaluation Reserves	0	
30	**Total Equity Capital**	**176,632,275**	

Table 15

14.5 Risk weighted assets

The total risk weighted assets consists of risk weighted assets for credit risk, market risk and for operational risk.

Risk weighted assets for credit risk includes as on-balance, as well off-balance elements and counterparty credit risk.

Table below shows the linkages between financial statement assets and balance sheet items subject to credit risk weighting.

Linkages between financial statement assets and balance sheet items subject to credit risk weighting *in Lari*

N	Account name of standardazed supervisory balance sheet item	Carrying values as reported in published stand-alone financial statements per local accounting rules	Carrying values of items	
			Not subject to capital requirements or subject to deduction from capital	Subject to credit risk weighting
1	Cash	51,728,823	-	51,728,823
2	Due from NBG	192,161,821	-	192,161,821
3	Due from Banks	121,131,515	-	121,131,515
4	Dealing Securities	-	-	-
5	Investment Securities	29,584,522	-	29,584,522
6.1	Loans	*1,043,508,432*	-	1,043,508,432
6.2	*Less: Loan Loss Reserves*	*(33,499,760)*	-	(33,499,760)
6	Net Loans	1,010,008,672	-	1,010,008,672
7	Accrued Interest and Dividends Receivable	5,793,302	-	5,793,302
8	Other Real Estate Owned & Repossessed Assets	-	-	-
9	Equity Investments	6,349,229	6,194,572	154,657
10	Fixed Assets and Intangible Assets	62,278,978	1,287,076	60,991,903
11	Other Assets	19,226,944	-	19,226,944
	Total exposures subject to credit risk weighting before adjustments	**1,498,263,806**	**7,481,648**	**1,490,782,158**

Table 16

6.2m GEL represents investments in equities, particularly in ProCredit Properties LLC and Creditinfo Georgia JSC, out of which 6.1m GEL is investment in ProCredit Properties LLC (the bank owns 100% of its shares). This amount is deducted from Common Equity Tier 1 during the regulatory adjustments. Accordingly, this amount is not subject to weighting for credit risk.

Additionally, the amount of intangible assets, which also is deducted from Common Equity Tier 1, does not participate in weighting for credit risk.

Off-balance elements' volume is reduced by the special reserve – through the credit-converse factor.

The following table will describe the off-balance sheet items per standardized regulatory report:

Off-balance sheet items per standardized regulatory report *in Lari*

N	Off-balance sheet items per standardized regulatory report	31/12/2018		
		GEL	FX	Total
1	**Contingent Liabilities and Commitments**	37,835,314	27,466,406	65,301,719
1.1	Guarantees Issued	25,324,818	13,757,205	39,082,023
1.2	Letters of credit Issued	0	0	0
1.3	Undrawn loan commitments	12,510,496	13,709,201	26,219,697
1.4	Other Contingent Liabilities	0	18,201	18,201
2	**Guarantees received as security for liabilities of the bank**	30,614,358	220,563,483	251,177,841
3	**Assets pledged as security for liabilities of the bank**	2,870,000	0	2,870,000
3.1	Financial assets of the bank	2,870,000	0	2,870,000
3.2	Non-financial assets of the bank			0
4	**Guarantees received as security for receivables of the bank**	102,015,116	352,554,565	454,569,680
4.1	Surety, joint liability	71,400,757	131,991,081	203,391,839
4.2	Guarantees			0
5	**Assets pledged as security for receivables of the bank**	305,141,466	1,069,450,754	1,374,592,220
5.1	Cash	5,304,085	6,283,846	11,587,931
5.2	Precious metals and stones	0	0	0
5.3	Real Estate:	235,499,560	1,007,819,697	1,243,319,257
5.3.1	*Residential Property*	70,496,212	285,840,138	356,336,350
5.3.2	*Commercial Property*	103,449,992	562,260,569	665,710,561
5.3.3	*Complex Real Estate*	0	0	0
5.3.4	*Land Parcel*	61,524,108	158,537,762	220,061,870
5.3.5	*Other*	29,248	1,181,228	1,210,476
5.4	Movable Property	28,808,682	53,539,176	82,347,858
5.5	Shares Pledged	32,119,200	463,052	32,582,252
5.6	Securities	0	0	0
5.7	Other	3,409,939	1,344,984	4,754,922
6	**Derivatives**	0	111,851,756	111,851,756
6.1	Receivables through FX contracts (except options)		56,589,956	56,589,956
6.2	Payables through FX contracts (except options)		55,261,800	55,261,800
6.3	Principal of interest rate contracts (except options)			0
6.4	Options sold			0
6.5	Options purchased			0
6.6	Nominal value of potential receivables through other derivatives			0
6.7	Nominal value of potential payables through other derivatives			0
7	**Receivables not recognized on-balance**			0
7.1	Principal of receivables derecognized during last 3 month	145,278	822,044	967,322
7.2	Interest and penalty receivable not recognized on-balance or derecognized during last 3 month	108,783	506,367	615,150
7.3	Principal of receivables derecognized during 5 years month (including last 3 month)	6,072,612	34,411,777	40,484,388
7.4	Interest and penalty receivable not recognized on-balance or derecognized during last 5 years (including last 3 month)	2,169,850	11,436,087	13,605,937
8	**Non-cancelable operating lease**	4,841	279,633	284,474
8.1	Through indefinit term agreement			0
8.2	Within one year	4,841	279,633	284,474
8.3	From 1 to 2 years			0
8.4	From 2 to 3 years			0
8.5	From 3 to 4 years			0
8.6	From 4 to 5 years			0
8.7	More than 5 years			0
9	**Capital expenditure commitment**			0

Table 17

The following table shows the differences between carrying values per standardized balance sheet used for regulatory reporting purposes and the exposure amounts used for capital adequacy calculation purposes:

	Differences between carrying values per standardized balance sheet used for regulatory reporting purposes and the exposure amounts used for capital adequacy calculation purposes	*in Lari*
1	**Total carrying value of balance sheet items subject to credit risk weighting before adjustments**	1,490,782,158
2.1	Nominal values of off-balance sheet items subject to credit risk weighting	65,319,473
2.2	Nominal values of off-balance sheet items subject to counterparty credit risk weighting	56,589,956
3	**Total nominal values of on-balance and off-balance sheet items before any adjustments used for credit risk weighting purposes**	1,612,691,587
4	Effect of provisioning rules used for capital adequacy purposes	19,891,564
5.1	Effect of credit conversion factor of off-balance sheet items related to credit risk framework	-18,177,183
5.2	Effect of credit conversion factor of off-balance sheet items related to counterparty credit risk framework (table CCR)	-55,458,157
6	Effect of other adjustments	
7	**Total exposures subject to credit risk weighting**	1,558,947,811

Table 18

The nominal value of off-balance positions, the nominal value of the counterparty related off-balance elements and the general reserve is added to the nominal value of the balance sheet items. In order to get the total RWAs for credit risk, the adjustments are made by using the credit conversion factor for off-balance and for counterparty related elements.

The bank uses a standardized approach to calculate the amount of the risk weighted assets for credit risk. Each risk position belongs to a certain class of risk positions. The risk weights to the risk positions are assigned in accordance with the Regulation on the Requirements for Capital Adequacy of Commercial Banks (The Order No. 100/04 of the President of the National Bank of Georgia).

The risk weighted assets for credit risk before credit risk mitigation are calculated according to the risk position class.

Table 19 shows the total balance and off-balance sheet values of the bank according to risk position classes and corresponding weights.

The table shows that the bank's largest risk position classes are "unconditional and conditional retail requirements", "unconditional and conditional requirements for corporate clients", "unconditional and conditional requirements for central governments and central banks" (the main part is mandatory reserves) and "unconditional and conditional requirements for commercial banks".

Credit Risk Weighted Exposures (On-balance items and off-balance items after credit conversion factor) *in Lari*

N	Risk weights / Exposure classes	0%		20%		35%		50%		75%		100%		150%		250%		Risk Weighted Exposures before Credit Risk Mitigation
		On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	On-balance sheet amount	Off-balance sheet amount	
1	Claims or contingent claims on central governments or central banks	50,443,013	0	0	0	0	0	0	0	0	0	171,494,187	0	0	0	0	0	171,494,187
2	Claims or contingent claims on regional governments or local authorities	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
3	Claims or contingent claims on public sector entities	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
4	Claims or contingent claims on multilateral development banks	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
5	Claims or contingent claims on international organizations/institutions	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
6	Claims or contingent claims on commercial banks	0	0	102,382,346	0	0	0	19,399,648	0	0	0	0	0	0	0	0	0	30,176,293
7	Claims or contingent claims on corporates	0	0	0	0	0	0	0	0	0	0	543,658,109	47,142,290	0	0	0	0	590,800,399
8	Retail claims or contingent retail claims	0	0	0	0	0	0	0	0	462,204,745	0	0	0	0	0	0	0	346,653,559
9	Claims or contingent claims secured by mortgages on residential property	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
10	Past due items	0	0	0	0	0	0	0	0	0	0	6,162,556	0	0	0	0	0	6,162,556
11	Items belonging to regulatory high-risk categories	0	0	0	0	0	0	0	0	0	0	0	0	23,412,739	0	5,401,285	0	48,622,321
12	Short-term claims on commercial banks and corporates	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
13	Claims in the form of collective investment undertakings ('CIU')	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	-
14	Other items	51,728,823	0	0	0	0	0	0	0	0	0	74,386,270	0	0	0	0	0	74,386,270
	Total	**102,171,836**	**0**	**102,382,346**	**0**	**0**	**0**	**19,399,648**	**0**	**462,204,745**	**0**	**795,701,123**	**47,142,290**	**23,412,739**	**0**	**5,401,285**	**0**	**1,268,295,586**

Table 19

The largest part of loan portfolio has been assigned to the risk position class of "claims or contingent retail claims" with the risk weight of 75%, as the bank's business operations focus on the segments of small and medium businesses.

The second largest category is the risk position class of "claims or contingent claims on corporates" with the risk weight of 100%. This class includes guarantees and letters of credit, as well as unused part of credit lines and business overdrafts.

The class "claims and contingent claims for central governments and central banks" includes both, balance and off-balance positions.

The table also shows that class "claims and contingent claims for commercial banks" have a 20% risk weight. Risk weight in the above-mentioned class depends on the credit rating of a commercial bank. The bank places the excess liquidity in banks with high credit ratings, and therefore the lowest weight (20%) has been awarded to the largest part of this class.

The main components of the class "other items" (GEL 74 m out of GEL 52 m) are the fixed assets.

Standardized approach - Effect of credit risk mitigation *in Lari*

N	Asset Classes	On-balance sheet exposures	Off-balance sheet exposures		RWA before Credit Risk Mitigation	RWA post Credit Risk Mitigation	RWA Density f=e/(a+c)
			Off-balance sheet exposures - Nominal value	Off-balance sheet exposures post CCF			
1	Claims or contingent claims on central governments or central banks	221,937,201	0	0	171,494,187	54,986,507	25%
2	Claims or contingent claims on regional governments or local authorities	0	0	0	0	0	0%
3	Claims or contingent claims on public sector entities	0	0	0	0	0	0%
4	Claims or contingent claims on multilateral development banks	0	0	0	0	0	0%
5	Claims or contingent claims on international organizations/institutions	0	0	0	0	0	0%
6	Claims or contingent claims on commercial banks	121,781,994	0	0	30,176,293	30,176,293	25%
7	Claims or contingent claims on corporates	543,658,109	65,319,473	47,142,290	590,800,399	556,589,445	94%
8	Retail claims or contingent retail claims	462,204,745	0	0	346,653,559	336,604,862	73%
9	Claims or contingent claims secured by mortgages on residential property	0	0	0	0	0	0%
10	Past due items	6,162,556	0	0	6,162,556	6,162,556	100%
11	Items belonging to regulatory high-risk categories	28,814,024	0	0	48,622,321	48,490,119	168%
12	Short-term claims on commercial banks and corporates	0	0	0	0	0	0%
13	Claims in the form of collective investment undertakings ('CIU')	0	0	0	0	0	0%
14	Other items	126,115,093	0	0	74,386,270	74,386,270	59%
	Total	**1,510,673,722**	**65,319,473**	**47,142,290**	**1,268,295,586**	**1,107,396,054**	**71%**

Table 20

14.6 Credit risk mitigation techniques

The bank applies the following techniques (instruments) to reduce credit risk when calculating the capital requirements for credit risk:

- Guarantee
- Cash deposit as collateral

The bank applies the guarantee obtained from the Multilateral Investment Guarantee Agency (MIGA). MIGA is a member of the World Bank Group and can be classified as a multilateral development bank. Its purpose is to promote direct investments in developing countries, which it does by offering guarantees to secure against political risks. MIGA's risk position is 0 percent according to the Capital Adequacy Regulation of the National Bank of Georgia. The amount of the guarantee, which was introduced in November 2015 and whose purpose is to mitigate credit risk, is EUR 40.5 m (GEL 116.5 m). The bank applies this guarantee to the USD and EUR exposure with the National Bank of Georgia, i.e. the mandatory reserves.

Starting November 2018, the bank applies the InnovFin guarantee (issued within the Agreement of Deep and Comprehensive Free Trade Area) facility which decreased the volume of RWAs by GEL 37 m. The

EU-supported guarantee is provided to selected financial institutions to cover 50-75% of the Defaulted Amounts (which include principal and accrued interest up to 90 days net of recoveries from loans to SMEs).

Cash deposits as collateral have also been used since November 2015 to mitigate on- and off-balance sheet exposures, specifically client loans and guarantees (see the positions corporate loans, retail loans and guarantees in the table below). The main criteria for cash collateral mitigation are:

- the currency of the loan/guarantee must be the same as the currency of the cash deposit
- the mitigated exposure is only the portion which is covered by cash collateral

The total credit risk mitigation concentration is low. The mitigated exposure as at December 2018 was approximately GEL 160 m, which is equivalent to 12 % of the total on- and off-balance sheet RWAs.

The table below shows used mitigation types according to the risk classes:

Credit Risk Mitigation On-balance and Off-balance elements

in Lari

		Funded Credit Protection									
N		On-balance sheet netting	Cash on deposit with, or cash assimilated instruments	Debt securities issued by central governments or central banks, regional governments or local authorities, public sector entities, multilateral development banks and international organizations/institutions	Debt securities issued by regional governments or local authorities, public sector entities, multilateral development banks and international organizations/institutions	Debt securities issued by other entities, which securities have a credit assessment, which has been determined by NBG to be associated with credit quality step 3 or above under the rules for the risk weighting of exposures to corporates.	Debt securities with a short-term credit assessment, which has been determined by NBG to be associated with credit quality step 3 or above under the rules for the risk weighting of short term exposures	Equities or convertible bonds that are included in a main index	Standard gold bullion or equivalent	Debt securities without credit rating issued by commercial banks	Units in collective investment undertakings
1	Claims or contingent claims on central governments or central banks	0	0	0	0	0	0	0	0	0	0
2	Claims or contingent claims on regional governments or local authorities	0	0	0	0	0	0	0	0	0	0
3	Claims or contingent claims on public sector entities	0	0	0	0	0	0	0	0	0	0
4	Claims or contingent claims on multilateral development banks	0	0	0	0	0	0	0	0	0	0
5	Claims or contingent claims on international organizations/institutions	0	0	0	0	0	0	0	0	0	0
6	Claims or contingent claims on commercial banks	0	0	0	0	0	0	0	0	0	0
7	Claims or contingent claims on corporates	0	6,189,916	0	0	0	0	0	0	0	0
8	Retail claims or contingent retail claims	0	712,327	0	0	0	0	0	0	0	0
9	Claims or contingent claims secured by mortgages on residential property	0	0	0	0	0	0	0	0	0	0
10	Past due items	0	0	0	0	0	0	0	0	0	0
11	Items belonging to regulatory high-risk categories	0	132,202	0	0	0	0	0	0	0	0
12	Short-term claims on commercial banks and corporates	0	0	0	0	0	0	0	0	0	0
13	Claims in the form of collective investment undertakings	0	0	0	0	0	0	0	0	0	0
14	Other items	0	0	0	0	0	0	0	0	0	0
	Total	**0**	**7,034,445**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**

in Lari

		Unfunded Credit Protection						
N		Central governments or central banks	Regional governments or local authorities	Multilateral development banks	International organizations / institutions	Public sector entities	Commercial banks	Other corporate entities that have a credit assessment, which has been determined by NBG to be associated with credit quality step 2 or above under the rules for the risk weighting of exposures to corporates
1	Claims or contingent claims on central governments or central banks	0	0	116,507,680	0	0	0	0
2	Claims or contingent claims on regional governments or local authorities	0	0	0	0	0	0	0
3	Claims or contingent claims on public sector entities	0	0	0	0	0	0	0
4	Claims or contingent claims on multilateral development banks	0	0	0	0	0	0	0
5	Claims or contingent claims on international organizations/institutions	0	0	0	0	0	0	0
6	Claims or contingent claims on commercial banks	0	0	0	0	0	0	0
7	Claims or contingent claims on corporates	0	0	28,021,037	0	0	0	0
8	Retail claims or contingent retail claims	0	0	9,336,369	0	0	0	0
9	Claims or contingent claims secured by mortgages on residential property	0	0	0	0	0	0	0
10	Past due items	0	0	0	0	0	0	0
11	Items belonging to regulatory high-risk categories	0	0	0	0	0	0	0
12	Short-term claims on commercial banks and corporates	0	0	0	0	0	0	0
13	Claims in the form of collective investment undertakings	0	0	0	0	0	0	0
14	Other items	0	0	0	0	0	0	0
	Total	**0**	**0**	**153,865,087**	**0**	**0**	**0**	**0**

in Lari

N		Total Credit Risk Mitigation - On-balance sheet	Total Credit Risk Mitigation - Off-balance sheet	Total Credit Risk Mitigation
1	Claims or contingent claims on central governments or central banks	116,507,680	0	116,507,680
2	Claims or contingent claims on regional governments or local authorities	0	0	0
3	Claims or contingent claims on public sector entities	0	0	0
4	Claims or contingent claims on multilateral development banks	0	0	0
5	Claims or contingent claims on international organizations/institutions	0	0	0
6	Claims or contingent claims on commercial banks	0	0	0
7	Claims or contingent claims on corporates	28,849,353	5,361,600	34,210,953
8	Retail claims or contingent retail claims	10,048,696	0	10,048,696
9	Claims or contingent claims secured by mortgages on residential property	0	0	0
10	Past due items	132,202	0	0
11	Items belonging to regulatory high-risk categories	0	0	132,202
12	Short-term claims on commercial banks and corporates	0	0	0
13	Claims in the form of collective investment undertakings	0	0	0
14	Other items	0	0	0
	Total	**155,537,931**	**5,361,600**	**160,899,532**

Table 21

Counterparty credit risk is related to counterparty default risk before the transaction is realized. The bank have SWAP transaction only with its sister bank – ProCredit Bank, Germany. Generally, SWAP's maturity is up to 3 months and, accordingly, it is weighted in 2% according to the NBG regulation.

Counterparty credit risk

in Lari

N		Nominal amount	Percentage	Exposure value	0%	20%	35%	50%	75%	100%	150%	250%	Counterparty Credit Risk Weighted Exposures
1	**Counterparty credit risk**	56,589,956		1,131,799	0	1,131,799	0	0	0	0	0	0	226,360
1.1	Maturity less than 1 year	56,589,956	2.0%	1,131,799	0	1,131,799	0	0	0	0	0	0	226,360
1.2	Maturity from 1 year up to 2 years	0	5.0%	0	0	0	0	0	0	0	0	0	0
1.3	Maturity from 2 years up to 3 years	0	8.0%	0	0	0	0	0	0	0	0	0	0
1.4	Maturity from 3 years up to 4 years	0	11.0%	0	0	0	0	0	0	0	0	0	0
1.5	Maturity from 4 years up to 5 years	0	14.0%	0	0	0	0	0	0	0	0	0	0
1.6	Maturity over 5 years	0			0	0	0	0	0	0	0	0	0
2	**Interest rate contracts**	0		0	0	0	0	0	0	0	0	0	0
2.1	Maturity less than 1 year	0	0.5%	0	0	0	0	0	0	0	0	0	0
2.2	Maturity from 1 year up to 2 years	0	1.0%	0	0	0	0	0	0	0	0	0	0
2.3	Maturity from 2 years up to 3 years	0	2.0%	0	0	0	0	0	0	0	0	0	0
2.4	Maturity from 3 years up to 4 years	0	3.0%	0	0	0	0	0	0	0	0	0	0
2.5	Maturity from 4 years up to 5 years	0	4.0%	0	0	0	0	0	0	0	0	0	0
2.6	Maturity over 5 years	0			0	0	0	0	0	0	0	0	0
3	**Total**	**56,589,956**		**1,131,799**	0	1,131,799	0	0	0	0	0	0	**226,360**

Table 22

Risk Weighted Assets for Market Risk is the volume of total open currency position. The bank, according to the foreign currency risk management policy, does not carry out speculative transactions and tries to maintain open currency position within strict internal limits.

The bank is required to maintain capital for operational risk. For calculating the risk weighted assets for operational risk the bank applies to the method of basic indicator.

Operational risks - basic indicator approach

in Lari

N		2018	2017	2016	Average of sums of net interest and net non-interest income during last three years	Risk Weighted asset (RWA) for operational risk
1	Net interest income	52,147,613	51,556,856	64,654,951		
2	Total Non-Interest Income	18,008,526	11,201,549	22,587,114		
3	*less: income (loss) from selling property*	123,059	1,035,345	-301,194		
4	**Total income (1+2-3)**	70,033,080	61,723,060	87,543,259	**73,099,800**	**137,062,124**

Table 23

The table below shows the risk weighted assets after mitigation applied:

Risk Weighted Assets *in Lari*

N		31/12/2018	30/09/2018
1	Risk Weighted Assets for Credit Risk	1,107,622,414	1,076,992,572
1.1	Balance sheet items	1,065,615,364	1,039,745,359
1.1.1	Including: amounts below the thresholds for deduction (subject to 250% risk weight)	0	0
1.2	Off-balance sheet items	41,780,690	37,186,136
1.3	Counterparty credit risk	226,360	61,077
2	Risk Weighted Assets for Market Risk	20,614,051	20,132,419
3	Risk Weighted Assets for Operational Risk	137,062,124	148,961,725
4	**Total Risk Weighted Assets**	**1,265,298,589**	**1,246,086,716**

Table 24

14.7 Differences between accounting and regulatory scopes of consolidation

Differences between accounting and regulatory scopes of consolidation — *in Lari*

Assets (as reported in published IFRS financial statements)	Carrying Values as reported in published IFRS financial statements	Carrying Values per IFRS under scope of regulatory consolidation (stand-alone)	Carrying values as reported in published stand-alone financial statements per local accounting rules (stand-alone)	Reconciliation with standardized regulatory reporting format													
				1	2	3	4	5	6.1	6.2	6	7	8	9	10	11	12
				Cash	Due from NBG	Due from Banks	Dealing Securities	Investment Securities	Total Loans	Less: Loan Loss Reserves	Net Loans	Accrued Interest and Dividends Receivable	Other Real Estate Owned & Repossessed Assets	Equity Investments	Fixed Assets and Intangible Assets	Other Assets	**TOTAL ASSETS**
Cash and balances with the NBG	167,841,524	167,841,524	167,961,674	51,728,823	21,533,144	94,511,367						1,610				186,729	**167,961,674**
Mandatory reserve deposits with NBG	170,805,544	170,805,544	170,628,677		170,628,677												**170,628,677**
Investments in debt securities	29,767,196	29,767,196	29,767,196					29,584,522				182,674					**29,767,196**
Due from other banks	32,142,568	32,140,336	32,160,933			26,620,148						7,927				5,532,859	**32,160,933**
Financial assets at fair value through profit or loss	-	-	0														**0**
Loans and advances to customers	1,023,256,057	1,023,256,057	1,015,609,762						1,043,508,432	-33,499,760	1,010,008,672	5,601,090					**1,015,609,762**
Current tax assets	-	-	3,251,885													3,251,885	**3,251,885**
Investment Properties	6,984,552	5,401,285	5,401,285												5,401,285		**5,401,285**
Intangible assets	1,287,076	1,287,076	1,287,076												1,287,076		**1,287,076**
Property, plant and equipment	55,590,618	55,590,618	55,590,618												55,590,618		**55,590,618**
Deferred tax assets	-	-	391,386													391,386	**391,386**
Other assets	11,232,524	14,168,792	16,213,314											6,349,229		9,864,085	**16,213,314**
Total assets	**1,498,907,658**	**1,500,258,427**	**1,498,263,806**	**51,728,823**	**192,161,821**	**121,131,515**	**0**	**29,584,522**	**1,043,508,432**	**-33,499,760**	**1,010,008,672**	**5,793,302**	**0**	**6,349,229**	**62,278,978**	**19,226,944**	**1,498,263,806**

Liabilities (as reported in published IFRS financial statements)	Carrying Values as reported in published IFRS financial statements	Carrying Values per IFRS under scope of regulatory consolidation (stand-alone)	Carrying Values per local accounting rules under scope of regulatory consolidation (stand-alone)	Reconciliation with standardized regulatory reporting format									
				13	14	15	16	17	18	19	20	21	22
				Due to Banks	Current (Accounts) Deposits	Demand Deposits	Time Deposits	Own Debt Securities	Borrowings	Accrued Interest and Dividends Payable	Other Liabilities	Subordinated Debentures	**Total Liabilities**
Due to other banks	71,608,225	71,608,225	71,008,150	65,511,700						893,286	4,603,164		**71,008,150**
Financial liabilities at fair value thr	223,530	223,530	0										**0**
Customers accounts	696,378,375	699,695,122	699,215,797		224,966,949	230,066,462	235,906,890			2,160,686	6,114,810		**699,215,797**
Borrowing from international financial institutions	457,233,613	457,233,613	457,168,004	57,452,100					394,332,158	5,383,746			**457,168,004**
Subordinated debt	82,977,903	82,977,903	82,891,403							625,903		82,265,500	**82,891,403**
Current tax liabilities	1,775,228	1,775,228	5,027,114								5,027,114		**5,027,114**
Other liabilities	1,320,722	1,197,926	3,909,499								3,909,499		**3,909,499**
Provisions	812,649	812,649	1,454,043								1,454,043		**1,454,043**
Deferred tax liabilities	638,876	638,876	957,521								957,521		**957,521**
Total liabilities	**1,312,969,122**	**1,316,163,073**	**1,321,631,531**	**122,963,800**	**224,966,949**	**230,066,462**	**235,906,890**	**0**	**394,332,158**	**9,063,621**	**22,066,150**	**82,265,500**	**1,321,631,531**

Equity (as reported in published IFRS financial statements)	Carrying Values as reported in published IFRS financial statements	Carrying Values per IFRS under scope of regulatory consolidation (stand-alone)	Carrying Values per local accounting rules under scope of regulatory consolidation (stand-alone)	Reconciliation with standardized regulatory reporting format							
				23	24	25	26	27	28	29	30
				Common Stock	Preferred Stock	Less: Repurchased Shares	Share Premium	General Reserves	Retained Earnings	Asset Revaluation Reserves	**Total Equity Capital**
Subscribed capital	88,914,815	88,914,815	88,914,815	88,914,815							**88,914,815**
Capital reserve	36,388,151	36,388,151	36,388,151				36,388,151				**36,388,151**
Retained earnings	60,635,569	58,792,387	51,329,308						51,329,308		**51,329,308**
Total equity	**185,938,536**	**184,095,354**	**176,632,275**	**88,914,815**	**0**	**0**	**36,388,151**	**0**	**51,329,308**	**0**	**176,632,275**

Table 25

Main differences between accounting and regulatory scopes of consolidation are formed by the following reasons:

- Assets

  The balances on nostro accounts are considered as “Cash and balances with NBG” according to the IFRS, but the regulatory scope puts these amounts into “Due from other banks”. As of December 2018, the volume of the bank’s nostro accounts was approximately GEL 94m, therefore this is the difference between “Cash and balances with NBG” and “Due from other banks”;

  The account “Net loans” represents the loan portfolio netted by loan loss provision. The volume of loan loss provision according to the regulatory purposes is higher than IFRS loan loss provision (the difference is approximately GEL7m). Additionally, the accrued interest on loans is also included in the “Net loans” account. According to the regulatory accounting, the accrued interest is accumulated for one month, according to the IFRS – throughout the whole period until the loan is written off. The IFRS accrued interest volume is higher by GEL 1.8m.

- Liabilities

  According to the regulatory accounting, the deposit from ProCredit Holding is in account “Due to other banks”, while according to the IFRS it is reported under “Borrowing from international financial institutions” which causes a difference of GEL 57m.

- Equity

  The difference in account “Retained earnings” in amount of GEL 9m is mainly caused by different loan loss provisioning.

14.8 Internal capital adequacy

Ensuring that the bank has sufficient internal capital at all times is a key element of ProCredit’s group-wide risk management and internal capital adequacy assessment process. In the context of the internal capital adequacy assessment, the capital needs arising from our specific risk profile are compared with the available capital resources to assure that the ProCredit Bank’s capitalisation is at all times sufficient to match our risk profile. It is an ongoing process that raises group/bank-wide awareness of our capital requirements and exposure to risks.

The methods we use to calculate the amount of economic capital required to cover the different risks the bank is exposed to are based on statistical models, provided that appropriate models are available. The guiding principle for our internal capital adequacy assessment is that the bank is able to withstand strong shock scenarios. In our view, the crisis years 2009 and 2010 underscored the necessity for a conservative approach to managing risks and capital, and the developments during that time proved the strength of the ProCredit group as well as of ProCredit Bank in dealing with a difficult economic environment. Throughout this period, the bank showed strong levels of capital, leaving ample scope for additional loss absorption had the economic conditions further deteriorated.

According to the internal capital adequacy concept, we are committed to being able to meet our non-subordinated obligations at all times in the event of unexpected losses, both in normal and in stress scenarios. The internal capital adequacy of the bank was sufficient at all times during 2018.

When calculating the economic capital required to cover risk exposures we apply a one-year risk assessment horizon. The included material risks and the limits set for each risk reflect the specific risk profile of the bank and are based on the annually conducted risk inventory.

Stress tests

Stress tests are performed regularly, at least once per month and ad hoc, to test the bank's resilience. Various types of analysis are performed, from simple sensitivity analysis for individual risk types to scenario analyses in which multiple or all risk factors are stressed simultaneously. Our analysis of the impact of stress scenarios includes an analysis of a severe economic downturn.

The scenarios apply to both historical and hypothetical stress situations. They include, among other things, assumptions depicting significant deterioration of macroeconomic conditions and simultaneous massive economic downturn. The selection of the scenarios takes account for the bank's strategic orientation and the economic environment.

The results of stress testing show that the risks to which the bank would be exposed in a severe stress event would not exceed the RAtCR, meaning that the internal capital adequacy of the bank would be sufficient at all times, even under stress conditions. Our analysis of the ProCredit bank's internal capital adequacy thus confirms that the bank would have an adequate level of capitalisation even under extremely adverse conditions.

15 Remuneration

15.1 Principles of remuneration

The overall aims of the bank's staff management approach are to establish long-term relationships between our staff and the ProCredit institution and to promote responsible behaviour among staff. ProCredit Holding sets the framework for the bank's remuneration structure and organises a regular exchange of experience on these topics. ProCredit Bank is responsible for the implementation of the standards.

The ProCredit Bank's remuneration system is in line with our sustainable business and risk strategy and does not encourage excessive risk taking by our employees. The remuneration structure of the ProCredit Bank has the following objectives:

- to attract and retain staff and managers who have the requisite social and technical skills and have the willingness to engage
- to encourage staff to assume responsibility, to effectively manage the operations of the bank and to work together as a team
- to support the development and maintenance of long-term working relationships
- to ensure that the remuneration is perceived to be transparent and fair in order to encourage staff to perform their duties in line with the conservative risk profile of the ProCredit Bank

The remuneration approach in ProCredit Bank aims to provide a long-term perspective to our staff and managers. A transparent salary structure with fixed salaries is a key aspect in this context; as a general rule, salaries are not dependent on performance. Variable remuneration is restricted and under no circumstances contractually guaranteed. For most of the staff, the remuneration reflects market averages. For managers, however, the remuneration we offer is directly not comparable with that of our competitors.

This is primarily due to the variable remuneration elements which are paid to managers at other institutions.

In addition to a fair salary, we offer every ProCredit staff member comprehensive training and professional development opportunities that represents a significant benefit for our staff. ProCredit Bank invests significant amounts in training, and the expenditures for training measures are a substantial part of the bank's overall personnel expenses. Other important factors which build long-term relationships between our staff and ProCredit are the interesting jobs we offer, flat hierarchies, transparent promotion opportunities since our management staff predominantly come from within the bank, independent responsibilities for duties as well as a stimulating and professional working environment.

15.2 Structure of remuneration

When defining the remuneration for its staff and managers, ProCredit Bank applies the group's standardised salary structure which has 22 salary levels. The bank defines the exact salary amounts in each step according to the market conditions, assigning its staff to one of the salary steps. This is carried out on the basis of the individual's position, the responsibilities they hold and their performance.

The ProCredit salary scheme applies to all ProCredit banks. The purpose of this salary structure is to ensure that positions with comparable responsibility within the ProCredit group are also compensated according to the same principles. This salary scheme defines which professional development programmes an employee must have successfully completed in order to be appointed to the various positions. The salary structure applicable throughout the group is reviewed and approved yearly by the Management of ProCredit Holding and presented to the Supervisory Board of ProCredit Holding. The salary scheme specific to the bank is likewise subject to annual review; the Management Board of the bank examines the salary scheme and it is approved by the Supervisory Board. A review of the allocation of staff within the ProCredit Bank to one of the 22 salary steps is also carried out annually on the basis of extensive staff evaluations and feedback discussions carried out by the HR committee.

The framework of the remuneration systems in the ProCredit Bank presented above also apply to staff whose professional activities have a material impact on the risk profile of the bank and the ProCredit group. As variable remuneration elements are not permitted in the remuneration structure of the bank described above, our remuneration system provides no incentives to assume particular risks.

15.3 Communication and approval of remuneration schemes

The remuneration structure and particularly the salary scheme in the bank is communicated to staff in a transparent manner. The management board of the ProCredit Bank reports annually to the supervisory board of the bank on the remuneration structure. The salary scheme in the bank is approved by the Management or the Supervisory Board of the bank, following discussions with the respective function at ProCredit Holding; however, the Management is permitted to delegate this responsibility to a Human Resources Committee. The Human Resources Committee is the bank's body responsible for taking decisions regarding the professional development of staff members and reviewing the bank's remuneration practices. The committee meets at least quarterly.

Remuneration for the Management of the bank is approved by the bank's supervisory board, after discussion with the Management of ProCredit Holding.

ProCredit Holding is managed by the members of the Management Board of ProCredit General Partner AG. As the remuneration structure which has been selected is simple, the Supervisory Board of ProCredit

General Partner AG decided to retain responsibility for determining the amount and composition of Management remuneration, instead of delegating this decision-making authority to a remuneration committee.

15.4 Remuneration 2018

The remuneration of all staff in ProCredit Bank whose professional activities have a material impact on the risk profile is given below. In particular, this includes the management of the bank and staff with management responsibilities (pursuant to Delegated Regulation (EU) No. 604/2014).

Remuneration is presented separately for staff whose professional activities have an impact on the risk profile and for members of the Management. As a general rule, the heads of the following units are classified as staff whose professional activities have an impact on the risk profile: risk management, finance, legal, internal audit, compliance, IT, as well as branch managers. Overall, we consider around 15% of all staff to be risk takers.

Remuneration awarded during the reporting period

		Board of Directors	Supervisory Board	Other material risk takers
Fixed remuneration	Number of employees	4		40
	Total fixed remuneration (3+5+7)	1,069,447	0	2,504,964
	Of which cash-based	1,066,597		2,477,604
	Of which: deferred			
	Of which: shares or other share-linked instruments			
	Of which deferred			
	Of which other forms	2,850		27,360
	Of which deferred			
Variable remuneration	Number of employees			
	Total variable remuneration (11+13+15)	0	0	0
	Of which cash-based			
	Of which: deferred			
	Of which shares or other share-linked instruments			
	Of which deferred			
	Of which other forms			
	Of which deferred			
Total remuneration		1,069,447	0	2,504,964

Table 26

The members of the bank's Supervisory Board are not included in the table above as they are not compensated by the bank.

ProCredit Bank does not have special or referred and retained remuneration payments.

There is no share in ownership of the Management of the bank, as well as of other risk takers.