AzerTurkBank OJSC

International Financial Reporting Standards
Financial Statements and
Independent Auditor's Report

31 December 2012

CONTENTS

INDEPENDENT AUDIT OPINION

FINANCIAL STATEMENTS

Notes to Financial Statements

INDEPENDENT AUDITOR'S REPORT

INDEPENDENT AUDITOR'S REPORT

To the Shareholders and the Board of Directors of AZERTURKBANK OJSC

Auditor's report on the Financial Statements

We have audited the accompanying financial statements of AZERTURKBANK OJSC (hereinafter referred to as "the Bank") which comprise the statement of financial position as of 31 December 2012 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as of 31 December 2012, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Emphasis of matter

Without further qualifying our opinion, we draw attention to Note 2 to the accompanying financial statements "Going Concern", which indicates, due to various matters as set forth in the Note, the existence of a material uncertainty which may cast significant doubt about the Bank's ability to continue as a going concern.

Baku, Republic of Azerbaijan
April 10, 2013

“AZER-TURK BANK” OJSC

STATEMENT OF FINANCIAL POSITION
As at 31 DECEMBER 2012
(In Azerbaijani Manats)

In Azerbaijani Manats	Note	31 December 2012	31 December 2011
ASSETS			
Cash and balances with the CBAR	6	7,415,434	3,708,766
Due from banks and other financial institutions	7	14,882,989	17,064,028
Loans and advances to Customers	8	49,106,380	36,706,580
Available for sale investments	9	11,965,538	5,701,341
Non-current assets held for sale	10	350,178	-
Property, equipment	11	712,236	722,686
Intangible assets	11	63,623	66,213
Other assets	12	37,587	52,193
TOTAL ASSETS		**84,533,965**	**64,021,807**
LIABILITIES			
Due to banks and other financial institutions	13	43,791,693	20,745,469
Customer accounts	14	26,073,289	29,913,115
Current tax liability	16	263,032	37,655
Deferred tax liability	16	169,575	72,993
Other liabilities	15	269,690	246,364
TOTAL LIABILITIES		**70,567,279**	**51,015,596**
EQUITY			
Share Capital	17	12,242,908	11,624,080
Retained earnings		1,723,778	1,351,626
Available for sale reserve		-	30,505
TOTAL EQUITY		**13,966,686**	**13,006,211**
TOTAL EQUITY AND LIABILITIES		**84,533,965**	**64,021,807**

On behalf of the Board of Directors:

Chief of Board of Directors

April 10, 2013
Baku, Azerbaijan

Chief Accountant

April 10, 2013
Baku, Azerbaijan

Notes on pages 7-58 form an integral part of these financial statements

"AZER-TURK BANK" OJSC

STATEMENT OF COMPREHENSIVE INCOME
As at 31 December 2012
(in Azerbaijani Manats)

In Azerbaijani Manats	Note	2012	2011
Interest Income	18	7,663,305	6,755,681
Interest Expense	18	(2,603,788)	(2,090,140)
Net interest income before provision for impairment loses on interest bearing assets		**5,059,517**	**4,665,541**
Allowances for impairement loses on interest bearing assets	19	(303,218)	(726,806)
Net interest income		**4,756,299**	**3,938,735**
Net gain on foreign exchange operations	20	454,764	314,983
Fee and commission income	21	1,463,336	1,293,146
Fee and commission expense	21	(400,497)	(285,117)
Other income	22	16,042	8,568
Administrative and other operating expenses	23	(4,279,137)	(3,791,686)
Profit before income tax		**2,010,807**	**1,478,629**
Income tax expense	16	(548,497)	(218,885)
NET PROFIT FOR THE YEAR		**1,462,310**	**1,259,744**
Available for sale securities' gains		(38,131)	38,131
Income tax recorded directly in equity		7,626	(7,626)
Other comprehensive income for the year		**(30,505)**	**30,505**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**1,431,805**	**1,290,249**
Earnings per share			
Basic and diluted (AZN)		**0.119**	**0.110**

On behalf of the Board of Directors:

Chief of Board of Directors

April 10, 2012
Baku, Azerbaijan

Chief Accountant

April 10, 2012
Baku, Azerbaijan

Notes on pages 7-58 form an integral part of these financial statements

"AZER-TURK BANK" OJSC

STATEMENT OF CHANGES IN EQUITY
As at 31 December 2012
(in Azerbaijani Manats)

In Azerbaijani Manats	**Share Capital**	**Retained Earnings**	**Available for sale reserve**	**Total Equity**
Balance at 31 December 2010	**10,990,520**	**1,215,446**	**-**	**12,205,966**
Issue of ordinary shares (Note #)	633,560	(633,560)	-	**-**
Total comprehensive income for the year	-	1,259,744	30,505	**1,290,249**
Dividends declared on ordinary shares	-	(490,004)	-	**(490,004)**
Balance at 31 December 2011	**11,624,080**	**1,351,626**	**30,505**	**13,006,211**
Issue of ordinary shares (Note#)	618,828	(618,828)	-	**-**
Total comprehensive income for the year	-	1,462,310	(30,505)	**1,431,805**
Dividends declared on ordinary shares	-	(471,330)	-	**(471,330)**
Balance at 31 December 2012	**12,242,908**	**1,723,778**	**-**	**13,966,686**

On behalf of the Board of Directors:

Chief of Board of Directors

April 10, 2013
Baku, Azerbaijan

Chief Accountant

April 10, 2013
Baku, Azerbaijan

Notes on pages 7-58 form an integral part of these financial statements

AZER-TURK BANK OJSC

STATEMENT OF CASH FLOWS
As at 31 December 2012
(in Azerbaijani Manats)

In Azerbaijani Manats	**Note**	**31 december 2012**	**31 december 2011**
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income tax		**2,010,807**	**1,478,629**
Adjustments for non-cash items:			
Provision/ impairment losses on interest bearing assets	19	294,504	726,806
Foreign exchange translation loss	20	(454,764)	39,116
Amortization and depreciation expense	11	178,986	165,930
Loss from disposal of property and equipment	11	3,718	7,643
Dividend income	22	(6,000)	(5,483)
Change in interest accruals, net	7,8,13,14	(6,822)	(160,215)
Cash flows from operating activites before changes in operating assets and liabilities:		**2,020,429**	**2,252,426**
Changes in operating assets and liabilities			
(Increase)/decrease in operating assets:			
Mandatory reserves with CBAR	6	(90,480)	(689,689)
Due from banks	7	(5,194,697)	488,368
Loans to customers	8	(12,401,622)	(7,848,884)
Other assets	12	(335,538)	(166,463)
Increase/(decrease) in operating liabilities:			
Due to banks and other financial institutions	13	22,999,421	7,115,810
Customer accounts	14	(3,789,180)	(3,734,729)
Other liabilities	15	23,548	23,524
Cash inflow/(outflow) from operating activites before taxation:		**3,231,881**	**(2,559,637)**
Income tax paid	16	(218,912)	(61,313)
Net cash inflow/(outflow) from operating activities		**3,012,969**	**(2,620,950)**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property equipment and intangible assets	11	(169,664)	(87,525)
Proceeds from sale of available-for-sale investments	9	62,231,021	10,650,710
Payments for available-for-sale investments	9	(68,512,309)	(1,669,440)
Dividends received	16	6,000	5,483
Net cash inflow/(outflow) from investing activities:		**(6,444,952)**	**8,899,228**
CASH FLOWS FROM FINANCING ACTIVITIES			
Dividends paid	17	(471,330)	(465,792)
Net cash inflow from financing activities		**(471,330)**	**(465,792)**
Effect of changes in foreign exch. rate on cash and cash eq.	20	8,434	(882)
NET INCREASE/(DECREASE) IN CASH AND CASH EQV.		**(3,894,879)**	**5,811,604**
CASH AND CASH EQUIVALENTS, beginning of the year	6	**13,023,033**	**7,211,429**
CASH AND CASH EQUIVALENTS, end of the year	6	**9,128,154**	**13,023,033**

On behalf of the Board of Directors:

Chief of Board of Directors
April 10, 2013
Baku, Azerbaijan

Chief Accountant
April 10, 2013
Baku, Azerbaijan

Notes on pages 7-58 form an integral part of these financial statements

1. INTRODUCTION

"Azer-Turk Bank" OJSC (the "Bank") was incorporated in the Republic of Azerbaijan as a closed joint stock company in May 1995 and was granted its full banking license by the Central Bank of the Azerbaijan Republic (the "CBAR") on 30 June 1995. In April 2005 the Bank was registered as open joint stock company in compliance with the regulations of the Republic of Azerbaijan. The Bank's ultimate controlling party is "T.C. Ziraat Bankasi", A.S. – the Republic of Turkey and "Aqrarkredit" Closed Joint Stock Non-Banking Credit Organization - the Republic of Azerbaijan.

Principal activity. The principal activities of the Bank are the commercial banking operations within the Republic of Azerbaijan.

Registered address and place of business . The registered address of the Bank is 5, I. Safarli Street, Baku, the Republic of Azerbaijan AZ1005.

The majority of the Bank's assets and liabilities are located within the Republic of Azerbaijan.

The Bank has the following branches:

- Central Branch, located at 5, I. Safarli Street, Baku, Azerbaijan operating under banking permit No234/4 dated July 19, 2010.
- Baku Branch, located at 140 S. Vurgun Street, Baku, Azerbaijan operating under banking permit No234/1 dated June 16, 2006.
- Ganja Branch, located at 68 M. A. Abbaszade Street, Ganja, Azerbaijan, operating under banking permit No 234/2 dated October 31, 2007.
- Nakhchivan Branch located at 37 H. Aliyev Ave, Nakhchivan, Azerbaijan, operating under banking permit No 234/3 dated October 1, 2009.

2. OPERATING ENVIRONMENT OF THE BANK

The Central Bank of the Republic of Azerbaijan pursued its financial stability policy in 2012 in the environment of fragile growth in the world economy, elevated global risks and volatility in the global financial and commodity markets. Growth dynamics of the country economy continued over the year stemming mainly from the non-oil sector and macroeconomic stability was maintained amid global uncertainties.

In order to maintain financial sustainability of the banking system the Central Bank has taken measures on reinforcing risk managament potential in banks, improving the supervisory-regulatory system and raising the capitalization level of banks. At the same time, deepening of financial intermediation of the banking system was on the spotlight.

The tax, currency and customs legislation within the Republic of Azerbaijan is subject to varying interpretations, and changes, which can occur frequently. Furthermore, the need for further developments in the bankruptcy laws, the absence of formalised procedures for the registration and enforcement of collateral, and other legal and fiscal impediments contribute to the difficulties experienced by banks currently operating in the Republic of Azerbaijan. The future economic direction of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

Going Concern

According to the Board decision of Central Bank of Azerbaijan Republic dated July 25, 2012, the total Share Capital of the Banks should be increased to AZN 50,000,000.

The new minimum of Share Capital comes to force on January 01, 2014.

As at December 31, 2012, the Bank's Share Capital amounts to AZN 13,966,686 which constitutes only 28% of the new minimum level.

In order to meet the Central Bank's criteria on the Share Capital the Bank should increase its Share Capital by 72% until January 01, 2014.

The Bank's management is intended to increase the Shareholder's Capital by means of issuing new shares to meet the Central Bank's criteria of AZN 50,000,000. The decision on the shareholders' participation portions on new Share Capital will be decided in the Annual General Meeting of Shareholders on May of 2013.

If the Bank fails to meet the criteria of increasing the shareholders' capital it will face an issue of going concern. The Financial Statements stated above have not been adjusted for uncertainities rised as a result of these issues.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Preparation. These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") under the historical cost convention, except for the revaluation of premises and equipment, investment properties, available-for-sale financial assets and held-for-trading financial assets. The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Functional and presentation currency: These Financial Statements are presented in Azerbaijani Manats, which is the Bank's functional currency.

Foreign Currency. Transactions in foreign currencies are translated into the respective functional currencies of the operations at the spot exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange of CBAR rate at that date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on translation are recognised in profit or loss. The exchange rates at the reporting date used by the Bank in the preparation of these financial statements are as follows:

	2012		**2011**	
	Year-end rate	Average rate	Year-end rate	Average rate
USD	0.7850	0.7856	0.7979	0.8026
EUR	1.0377	1.0106	1.0560	1.0646
GBP	1.2694	1.2458	1.2377	1.2413
TRY	0.4387	0.4370	0.5139	0.5332
RUR	0.0258	0.0254	0.0263	0.0264

Interest income and expense. Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses. The calculation of the effective interest rate includes all transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability. Interest income and expense presented in the statement of comprehensive income include interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis and interest income on available-for-sale investments.

Commission income and expense. Fees and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate. Other fees and commission income, including account servicing fees, investment management fees, sales commission are recognized as the related services are performed. When a loan commitment is not expected to result in the drawdown of a loan, the related loan commitment fees are recognized on a straight-line basis over the commitment period. Other fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

Financial Assets and liabilities.

Recognition and initial measurement. The Bank recognizes financial assets and liabilities in its statement of financial position when it becomes a party to the contractual obligations of the instrument. Regular way purchases and sales of financial assets and liabilities are recognized using settlement date accounting. Financial assets and financial liabilities are initially measured at fair value.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit and loss accounts.

Classification. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition. Financial assets are classified into the following specified categories:

Financial assets at fair value through profit or loss Financial assets classified as held for trading are included in the category "financial assets at fair value through profit or loss". Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Gains or losses on financial assets held for trading are recognized in the profit and loss accounts.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity dates that the Bank has the positive intent and ability to hold to maturity. Held-to-maturity investments are measured at amortized cost using the effective interest method less any impairment.

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for sale financial assets are measured at fair value with gains or losses being recognized in other comprehensive income until the investment is derecognized or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is reclassified to profit and loss accounts. However, interest calculated using the effective interest method is recognized in profit and loss accounts.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortized cost using the effective interest method. Gains and losses are recognized in profit and loss accounts when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Derecognition. The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred), and consideration received is recognised in profit or loss.

In transactions in which the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The Bank derecognizes financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit and loss accounts.

Reclassification of financial assets. If a non-derivative financial asset classified as held for trading is no longer held for the purpose of selling in the near term, it may be reclassified out of the fair value through profit or loss category in one of the following cases:

- A financial asset that would have met the definition of loans and receivables above may be reclassified to loans and receivables category if the Bank has the intention and ability to hold it for the foreseeable future or until maturity;
- Other financial assets may be reclassified to available for sale or held-to-maturity categories only in rare circumstances.

A financial asset classified as available-for-sale that would have met the definition of loans and receivables may be reclassified to loans and receivables category of the Bank has the intention and ability to hold it for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value on the date of reclassification. Any gain or loss already recognized in profit and loss accounts is not reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortized cost, as applicable.

Offsetting. Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank has a legal right to set off the recognised amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted under IFRSs.

Amortized cost measurement. The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

Fair value measurement. Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date. When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis. If a market for a financial instrument is not active, then the Bank establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in profit or loss on an appropriate basis over the life of the instrument.

Identification and measurement of impairment. At each reporting date the Bank assesses whether there is objective evidence that financial assets carried at amortised cost are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset or group of assets, and that the loss event has an impact on the future cash flows of the asset or group of assets that can be estimated reliably.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

The Bank considers evidence of impairment for loans and advances and investment securities measured at amortised costs at both a specific asset and collective level. All individually significant loans and advances and investment securities measured at amortised cost are assessed for specific impairment. All individually significant loans and advances and investment securities measured at amortised cost found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances and investment securities measured at amortised cost that are not individually significant are collectively assessed for impairment by grouping together loans and advances and investment securities measured at amortised cost with similar risk characteristics.

In assessing collective impairment the Bank uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and advances. Interest on impaired assets is not recognised. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Loans and advances are written off against the allowance for impairment losses when deemed uncollectible. Loans and advances are written off after management has exercised all possibilities available to collect amounts due to the Bank and after the Bank has sold all available collateral. Subsequent recoveries of amounts previously written off are reflected as an offset to the charge for impairment of financial assets in profit and loss accounts in the period of recovery.

For available-for-sale financial investments, the Bank assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in profit and loss accounts – is reclassified from other comprehensive income to profit or loss. Impairment losses on equity investments are not reversed through profit or loss; increases in their fair value after impairment are recognized in other comprehensive income.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in profit and loss accounts.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit and loss accounts, the impairment loss is reversed through profit and loss accounts.

Cash and cash equivalents include cash on hand, unrestricted balances on correspondent and time deposit accounts with the CBRA and advances to banks in countries included in the Organization for Economic Co-operation and Development (“OECD”) with original maturities up to 90 days. For purposes of determining cash flows, the minimum reserve deposits required by the CBRA are not included as a cash equivalent due to restrictions on its availability.

Due from banks In the normal course of business, the Bank maintains advances or deposits for various periods of time with other banks. Due from banks are initially recognized at a fair value. Due from banks with affixed maturity term are subsequently measured at amortized cost using the effective interest method and are carried net of any allowance for impairment losses. Those that do not have fixed maturities are carried at amortized cost based on expected maturities. Amounts due from credit institutions are carried net of any allowancefor impairment losses.

Due to banks and other credit institutions. Amounts due to banks are recorded when money or other assets are advanced to the Bank by counterparty banks. The non-derivative liability is carried at amortized cost. If the Bank purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from early retirement of debt.

Loans to customers are non-derivative assets with fixed or determinable payments that are not quoted in an active market. Loans granted by the Bank are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method. Where the fair value of consideration given does not equal the fair value of the loan, for example where the loan is issued at lower than market rates, the difference between the fair value of consideration given and the fair value of the loan is recognized as a loss on initial recognition of the loan and included in the statement of comprehensive income according to nature of these losses. Subsequently, loans are carried at amortized cost using the effective interest method. Loans to customers are carried net of any allowance for impairment losses.

Repurchase and reverse repurchase agreements. Sale and repurchase agreements (“repos”) are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the statement of financial position and, in case the transferee has the right by contract or custom to sell or replete them, reclassified as securities pledged under sale and repurchase agreements. The corresponding liability is presented within amounts due to credit institutions or customers. Securities purchased under agreements to resell (“reverse repo”) are recorded as amounts due from credit institutions or loans to customers as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

Renegotiated loans. Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan’s original or current effective interest rate.

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Debt securities in issue include promissory notes, bonds, certificates of deposit and debentures issued by the Bank. Debt securities are stated at amortized cost. If the Bank purchases its own debt securities in issue, they are removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains arising from retirement of debt.

Financial guarantee contracts. A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument. Financial guarantee contracts issued by the Bank are initially measured at their fair values which are normally evidenced by the amount of fees received. This amount is amortized on a straight line basis over the life of the commitment and included in other liabilities. If not designated as at FVTPL, they are subsequently measured at the higher of:

- the best estimate of expenditure required to settle the commitment at the end of each reporting period.; and
- The amount initially recognized less, where appropriate, cumulative amortization recognized in accordance with the revenue recognition policies.

Amounts payable under guarantee contracts are included under other liabilities.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred. In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Property, equipment and intangible assets are carried at historical cost less accumulated depreciation and amortization and any recognised impairment loss. Depreciation on assets under construction and those not placed in service commences from the date the assets are ready for their intended use. Depreciation and amortization are charged on the carrying value of property, equipment and intangible assets and is designed to write off assets over their useful economic lives. The estimated useful lives, residual values and depreciation/amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate accounted for on a prospective basis at the following annual rates:

	2012	**2011**
Furniture and fixtures	17.5%	12.5%
Computer and equipment	30%	20%
Vehicles	1.5%	12.5%
Other fixed assets	12%	10%
Intangible assets	12%	10%

Expenses related to repairs and renewals are charged when incurred and included in operating expenses unless they qualify for capitalisation.

Intangible assets with finite useful lives that are acquired separately are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with indefinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

At the end of each reporting period, the Bank reviews the carrying amounts of its property, equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Bank estimates the recoverable amount of the cash-generating unit to which the asset belongs.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset(or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in whichcase the reversal of the impairment loss is treated as are valuation increase.

An item of property, equipment and intangible assets is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss rising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit and loss.

Taxation. Income tax expense represents the sum of the tax currently payable and deferred tax expense.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank's current tax expense is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax base used in the computation of taxable profit. Deferred tax liability is recognised for all taxable temporary differences. Deferred tax asset is recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realised. Deferred tax is charged or credited in the statement of comprehensive income, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Deferred income tax assets and deferred income tax liability are offset and reported net on the statement of financial position if:

- The Bank has a legally enforceable right to set off current income tax assets against current income tax liability; and
- Deferred income tax assets and the deferred income tax liability relate to income taxes levied by the same taxation authority on the same taxable entity.

The Republic of Azerbaijan also has various other taxes, which are assessed on the Bank's activities. These taxes are included as a component of operating expenses in the statement of comprehensive income.

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made. The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (where the effect of the time value of money is material). When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognized as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Retirement and other benefit obligations In accordance with the requirements of the legislation of the Republic of Azerbaijan state pension system provides for the calculation of current payments by the employer as a percentage of current total payments to staff. This expense is charged in the period the related salaries are earned. Upon retirement all retirement benefit payments are made by pension funds selected by employees. The Bank does not have any pension arrangements separate from the State pension system of the Republic of Azerbaijan. In addition, the Bank has no post-retirement benefits or other significant compensated benefits requiring accrual.

Contingencies. Contingent liabilities are not recognized in the statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognized in the statement of financial position but disclosed when an inflow of economic benefits is probable.

Share capital. Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognized as a deduction from equity, net of any tax effects. Dividends on ordinary shares are recognized in equity as a reduction in the period in which they are declared. Dividends that are declared after the reporting date are treated as a subsequent event under International Accounting Standard 10 "Events after the Reporting Date" ("IAS 10") and disclosed accordingly.

Segment reporting. Operating segments are identified on the basis of internal reports about components of the Bank that are regularly reviewed by the chief operating decision maker in order to allocate resources to the segment and to assess its performance. The Bank's segmental reporting is based on the following operating segments: Retail banking (Principally handling individual customers' deposits, and providing consumer loans, overdrafts, credit cards facilities and funds transfer facilities) and Corporate banking (Principally handling loans and other credit facilities and deposit and current accounts for corporate and institutional customers). The Bank measures information about reportable segments in accordance with IFRS.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Information about reportable operating segment meets any one of the following quantitative thresholds:

- Its reported revenue, from both external customers and intersegment sales or transfers, is 10 percent or more of the revenue, internal and external, of all operating segments; or

- The absolute measure of its reported profit or loss is 10 per cent or more of the greater, in absolute amount, of (i) the combined reported profit of all operating segments that did not report a loss and (ii) the combined reported loss of all operating segments that reported a loss; or

- Its assets are 10 per cent or more of the combined assets of all operating segments. If the total external revenue reported by operating segments constitutes less than 75 per cent of the entity's revenue, additional operating segments are identified as reportable segments (even if they do not meet the quantitative thresholds set out above) until at least 75 per cent of the Bank's revenue is included in reportable segments.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES

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

Impairment losses on loans and advances. The Bank regularly reviews its loan portfolios to assess impairment. In determining whether an impairment loss should be recorded in the statement of comprehensive income the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS IN APPLYING ACCOUNTING POLICIES (Continued)

Investments carried at carrying value. Management could not reliably estimate the fair value of the Bank's investments in equity. These investments are carried at total cost of AZN 455,400 (2010: AZN 455,100). The investee companies have not published their recent financial information about its operations, their shares are not quoted and recent trade prices are not publicly accessible. The market for these assets is not liquid, but the management believes potentially interested buyers could be other resident commercial banks and equity investment companies at a price close to their carrying value.

Loans and advances to customers. Management have assessed the nature of the agreement with the Azerbaijan Mortgage Fund, and in particular whether the Bank is acting as an agent of the fund, or as a principal with the borrower under this program. Having considered the risks and rewards related to the loans issued under this program, management have concluded that the Bank is acting as principal and accordingly the accounting in these financial statements follows this judgment. Had an alternative conclusion been reached, the gross amounts of loans to customers and due to the Fund, of AZN 809,867 as at 31 December 2012 (2011: 875,851 AZN), would have been excluded from the financial statements.

Useful lives of property, equipment and intangible assets. The Bank reviews the estimated useful lives of property, equipment and intangible assets at the end of each annual reporting period. After the financial year, the directors determined that the useful lives of certain items of equipment should be revised, due to long usage of these items. As a result of the review, the estimated useful lives of classes were changed accordingly starting from January 01, 2011.

Change of comparative figures

In 2012 the Bank's management discovered errors in the financial statements for the year ended 31 December 2011. In accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors" the correction of the errors was done retrospectively. Certain reclassifications have been made to the financial statements as at 31 December 2011 and for the year then ended to conform to the presentation as at 31 December 2012 and for the year then ended:

In Azerbaijani Manats	**Balance sheet line as per previous report**	**Reclassified amount**	**Balance sheet line as per current report**	**Description of Adjustments**
Loans to Customers	36,875,075	(168,495)	36,706,580	Reclassification of deferred loan origination fees to the Loans to Customers Accounts from Other Liabilities accounts
Investment securities available-for-sale	5,653,872	47,469	5,701,340	Reclassification of coupon discounts receivable from Other assets to Investment securities availabe-for-sale accounts
Other assets	252,291	(47,469)	52,193	Reclassification of coupon discounts receivable from Other assets to Investment securities availabe-for-sale accounts
		(152,629)		Reclassification of deferred loan origination fees to the Due to Baks accounts from Other Assets accounts
Due to Banks and other Financial Institutions	20,898,098	(152,629)	20,745,468	Reclassification of deferred loan origination fees to the Due to Baks accounts from Other Assets accounts
Other liabilities	414,859	(168,495)	246,364	Reclassification of deferred loan origination fees to the Loans to Customers Accounts from Other Liabilities accounts

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

These consolidated financial statements have been prepared on a going concern basis and in accordance with International Financial Reporting Standards ("IFRS"), being Standards and Interpretations issued by the International Accounting Standards Board ("IASB"), in force at 31 December 2012. The consolidated financial statements have been prepared under the historical cost convention, unless mentioned otherwise in the accounting policies below (eg certain financial instruments that are measured at fair value). Historical cost is generally based on the fair value of the consideration given in exchange for assets.

The consolidated financial statements comprise an income statement, a statement of comprehensive income, a statement of financial position, a statement of changes in equity, a statement of cash flows, and notes. Income and expenses, excluding the components of other comprehensive income, are recognised in the income statement. Other comprehensive income is recognised in the statement of comprehensive income and comprises items of income and expense (including reclassification adjustments) that are not recognised in the income statement, as required or permitted by IFRS. Reclassification adjustments are amounts reclassified to profit or loss in the income statement in the current period that were recognised in other comprehensive income in the current or previous periods. Transactions with the owners of the Group in their capacity as owners are recognised in the statement of changes in equity.

For the preparation of these consolidated financial statements, the following amended pronouncements are mandatory for the first time for the financial year beginning 1 January 2012 (the list does not include information about new pronouncements that affect first-time adopters of IFRS or not-for-profit and public sector entities since they are not relevant to IFRS Statements Limited).

Amendments to IAS 1 Presentation of Items of Other Comprehensive Income (issued in June 2011) - These amendments improve the presentation of the components of other comprehensive income, mainly the Group will be required to group items presented in OCI based on whether or not they will be reclassified to profit or loss subsequently. They are effective for annual periods beginning on or after 1 July 2012.

Amendment to IAS 1 Presentation of Financial Statements (Annual Improvements to IFRSs 2009–2011 Cycle, issued in May 2012) - The amendment clarifies that additional comparative information is not necessary for periods beyond the minimum required by IAS 1, however if voluntarily presented, it should be in accordance with IFRS, without triggering a requirement to provide a complete set of financial statements. It also clarifies that, in the case of changes in accounting policies retrospectively or a retrospective restatement or reclassification which has a material effect on the information in the statement of financial position at the beginning of the preceding period, the Group should present the statement of financial position at the end of the current period and the beginning and end of the preceding period. However, other than disclosure of certain specified information, related notes will not be required to accompany the opening statement of financial position as at the beginning of the preceding period. The amendment is effective for annual periods beginning on or after 1 January 2013.

Amendment to IAS 16 Property, Plant and Equipment (Annual Improvements to IFRSs 2009–2011 Cycle, issued in May 2012) - The amendment clarifies that items such as spare parts, stand-by equipment and servicing equipment should be recognised as PPE when they meet the definition in IAS 16 and as inventory otherwise. It is effective for annual periods beginning on or after 1 January 2013.

Revised IAS 19 Employee Benefits (issued in June 2011) - The key amendments include elimination of the 'corridor approach', modification of accounting for termination benefits and improvement of the recognition and disclosure requirements for defined benefit plans. The amendments are effective for annual periods beginning on or after 1 January 2013. The Group will not be able to continue using the 'corridor approach' for recognising actuarial gains and losses. The effect of this is yet to be quantified.

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTREPRETATIONS (Continued)

Revised IAS 27 Separate Financial Statements (issued in May 2011) – The revised and re-titled Standard now only deals with the requirements for separate financial statements, which have been carried over largely unchanged from IAS 27 Consolidated and Separate Financial Statements. The Standard mainly requires that when an entity prepares separate financial statements, investments in subsidiaries, associates, and jointly controlled entities are accounted for either at cost, or in accordance with IFRS 9 Financial Instruments / IAS 39 Financial Instruments: Recognition and Measurement. It also deals with the recognition of dividends, certain group reorganisations and includes a number of disclosure requirements. It is effective for annual periods beginning on or after 1 January 2013.

Revised IAS 28 Investments in Associates and Joint Ventures (issued in May 2011) – The revised and re-titled Standard prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. It defines 'significant influence', provides guidance on how the equity method of accounting is to be applied (including exemptions from applying the equity method in some cases) and prescribes how investments in associates and joint ventures should be tested for impairment. It is effective for annual periods beginning on or after 1 January 2013.

Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities (issued in December 2011) – The amendments address inconsistencies in current practice when applying the offsetting criteria in IAS 32, mainly by clarifying the meaning of 'currently has a legally enforceable right of set-off' and that some gross settlement systems may be considered equivalent to net settlement. They are effective for annual periods beginning on or after 1 January 2014.

Amendment to IAS 32 Financial instruments: Presentation (Annual Improvements to IFRSs 2009–2011 Cycle issued in May 2012) - The amendment clarifies that income tax relating to distributions to holders of an equity instrument and to transaction costs of an equity transaction should be accounted for in accordance with IAS 12. It is effective for annual periods beginning on or after 1 January 2013.

Amendments to IFRS 7 Disclosures - Offsetting Financial Assets and Financial Liabilities (issued in December 2011) - The amendments allow investors to bridge differences in the offsetting reporting requirements of IFRS and US GAAP and introduce new disclosures that provide better information on how companies mitigate credit risk, including on related collateral pledged or received. They are effective for annual periods beginning on or after 1 January 2013.

IFRS 9 Financial Instruments (issued in November 2009 and amended in October 2010) **-** This standard introduces new requirements for the classification and measurement of financial assets and financial liabilities and for derecognition.

- IFRS 9 requires all recognised financial assets that are within the scope of IAS 39 Financial Instruments: Recognition and Measurement to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods.

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTREPRETATIONS (Continued)

- The most significant effect of IFRS 9 regarding the classification and measurement of financial liabilities relates to the accounting for changes in fair value of a financial liability (designated as at fair value through profit or loss) attributable to changes in the credit risk of that liability. Specifically, under IFRS 9, for financial liabilities that are designated as at fair value through profit or loss, the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is recognised in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Currently, under IAS 39, the entire amount of the change in the fair value of the financial liability designated as at fair value through profit or loss is recognised in profit or loss.

- The derecognition provisions are carried over almost unchanged from IAS 39.

IFRS 9 is effective for annual periods beginning on or after 1 January 2015. The Directors anticipate that IFRS 9 will be adopted in the Group's consolidated financial statements when it becomes mandatory and that the application of the new Standard might have a significant impact on amounts reported in respect of the Groups' financial assets and financial liabilities. However, it is not practicable to provide a reasonable estimate of that effect until a detailed review has been completed.

IFRS 10 Consolidated Financial Statements (issued in May 2011) – The new Standard replaces all of the guidance on control and consolidation in IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation— Special Purpose Entities. The core principle that a consolidated entity presents a parent and its subsidiaries as if they are a single economic entity remains unchanged, as do the mechanics of consolidation. IFRS 10 introduces a single consolidation model that identifies control as the basis for consolidation for all types of entities, where control is based on whether an investor has power over the investee, exposure/rights to variable returns from its involvement with the investee and the ability to use its power over the investee to affect the amount of the returns. The new standard also includes guidance on participating and protective rights and on agent/principal relationships. It is effective for annual periods beginning on or after 1 January 2013.

IFRS 11 "Joint Arrangements" will be effective for annual periods beginning on or after 1 January 2013 with retrospective application required. The new standard supersedes IAS 31 "Interests in Joint Ventures". The main change introduced by IFRS 11 is that all joint arrangements are classified either as joint operations, which are consolidated on a proportionate basis, or as joint ventures, for which the equity method is applied. The type of arrangement is determined based on the rights and obligations of the parties to the arrangement arising from joint arrangement's structure, legal form, contractual arrangement and other facts and circumstances. When the adoption of IFRS 11 results in a change in the accounting model, the change is accounted for retrospectively from the beginning of the earliest period presented. Under the new standard all parties to a joint arrangement are within the scope of IFRS 11 even if all parties do not participate in the joint control. Early adoption of IFRS 11 is permitted provided the entity also early-adopts IFRS 10, IFRS 12 and IAS 28 (2011).

IFRS 12 Disclosure of Interests in Other Entities (issued in May 2011) – The new Standard combines, enhances and replaces the disclosure requirements for subsidiaries, joint arrangements, associates and unconsolidated structured entities. It requires extensive disclosure of information that enables users of financial statements to evaluate the nature of, and risks associated with, interests in other entities and the effects of those interests on the Group's financial position, financial performance and cash flows. IFRS 12 is effective for annual periods beginning on or after 1 January 2013.

5. ADOPTION OF NEW OR REVISED STANDARDS AND INTREPRETATIONS (Continued)

IFRS 13 Fair Value Measurement (issued in May 2011) – The new Standard defines fair value, sets out a single framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies when other IFRSs require or permit fair value measurements. It does not introduce any new requirements to measure an asset or a liability at fair value, change what is measured at fair value in IFRS or address how to present changes in fair value. The new requirements are effective for annual periods beginning on or after 1 January 2013.

IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine (issued in October 2011) **-** The interpretation provides guidance on the accounting for waste removal (stripping) costs in the production phase of a mine. Such stripping costs should be recognised as an asset if they generate a benefit of improved access to an identifiable component of the ore body, it is probable that the benefits will flow to the entity and the costs can be measured reliably. Capitalised stripping costs are amortised over the useful life of the identified component. On transition, existing production stripping costs must be written off to retained earnings, unless they can be attributed to an identifiable component of an ore body. IFRIC 20 is effective for annual periods beginning on or after 1 January 2013.

6. CASH AND CASH EQUIVALENTS

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Cash in hand	2,749,945	2,303,850
-Cash balances with the CBAR (other than mandatory reserve deposits)	3,722,496	556,615
-Mandatory reserves	942,993	848,301
Total cash and cash equivalents	**7,415,434**	**3,708,766**

The balances with the Central Bank of Azerbaijan represent the obligatory minimum reserve deposits with the CBA. The Bank is required to maintain the reserve balance at the CBAR at all times provided that average daily balance for 30 days period will be eventually higher than required mandatory reserve. These accounts do not bear any interest.

Cash and cash equivalents for the purposes of the statement of cash flows comprise:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Cash in hand	2,749,945	2,303,850
Cash balances with the CBAR	4,665,489	1,404,916
Due from banks in OECD countries	2,655,713	10,162,568
Less: Mandatory reserves	(942,993)	(848,301)
Total cash and cash equivalents	**9,128,154**	**13,023,033**

7. DUE FROM OTHER BANKS AND FINANCIAL INSTITUTIONS

(In Azerbaijani Manats)	**31 December 2012**	**31 December 2011**
Correspondent accounts with other banks	5,953,476	14,347,310
Loans to banks	3,055,580	2,566,250
Term deposits with other banks	5,873,933	170,131
Less: Allowance for impairment losses	-	(19,663)
Total due from other banks and financial institutions	**14,882,989**	**17,064,028**

Accrued interest included in due from banks at the year ended 31 December 2012 is AZN 17,940 (31 December 2011: AZN 12,831). As at 31 December 2011, maximum credit risk exposure of due from banks amounted to AZN 14,882,989 (31 December 2011: AZN 17,064,028).

On dates between December 20 and December 28, 2012 the bank issued three loans totalling USD 3,200,000 (equivalent AZN 3,017,400) to Turanbank OJSC, and received two deposits totalling AZN 2,076,000 from the same bank.

On dates between December 19 and December 28, 2012 the bank issued two loans totalling USD 4,250,000 (equivalent AZN 4,094,350) to Bank of Azerbaijan OJSC, and received two deposits totalling AZN 4,250,000 from the same bank.

On 21 December, 2012, the bank issued a loan amounting USD 500,000 (equivalent AZN 518,850) to Amrahbank OJSC and received a deposit of AZN 517,750 from the same bank.

Because the Management has not found any objective proof for the impairment of Due from Other Banks and Financial Institutions the allowance for impairment has not been calculated for the years ending 31 December 2012 and 31 December 2011.

8. LOANS AND ADVANCES TO CUSTOMERS

In Azerbaijani Manats	31 December 2012	31 December 2011
Corporate loans	26,167,371	19,276,082
Loans to individuals – consumer loans	21,659,257	16,916,519
Loans to individuals – entrepreneurship loans	3,368,042	2,213,665
Loans to individuals – mortgage loans	812,225	877,632
Less: Provision for loan impairment	(2,900,515)	(2,577,318)
Total loans and advances to customers	**49,106,380**	**36,706,580**

Breakdown of loan portfolio per type of collateral excluding loan origination fees as at 31 December 2012 is as follows:

In Azerbaijani Manats	Corporate loans	Loans to individuals – consumer loans	Loans to individuals – entrepreneurship loans	Loans to individuals – mortgage loans	Total
Unsecured loans	340,649	15,813,751	21,928	72,504	**16,248,832**
Loans collateralized by:					
Real estate	11,748,756	3,446,209	3,287,538	739,721	**19,222,224**
Vehicle and equipment	1,055,417	485,265	58,576	-	**1,599,258**
Cash deposits	7,174,904	674,082	-	-	**7,848,986**
Jewellery	-	1,180,886	-	-	**1,180,886**
Securities	5,847,645	59,064	-	-	**5,906,709**
Gross amount of loans	**26,167,371**	**21,659,257**	**3,368,042**	**812,225**	**52,006,895**
Less: Provision for loan impairment	(1,864,727)	(714,305)	(321,483)	-	**(2,900,515)**
Total loans and advances to customers	**24,302,644**	**20,944,952**	**3,046,559**	**812,225**	**49,106,380**

8. LOANS AND ADVANCES TO CUSTOMERS (Continued)

Breakdown of loan portfolio per type of collateral excluding loan origination fees as at 31 December 2011 is as follows:

In Azerbaijani Manats	**Corporate loans**	**Loans to individuals – consumer loans**	**Loans to individuals – entrepreneurship loans**	**Loans to individuals – mortgage loans**	**Total**
Unsecured loans	1,054,775	11,777,505	-	-	12,832,280
Loans collateralized by:					
Real estate	11,736,528	3,348,065	2,190,888	877,632	18,153,113
Vehicle and equipment	1,634,495	69,254	22,777	-	1,726,526
Cash deposits	1,219,208	336,223	-	-	1,555,431
Jewellery	-	1,385,472	-	-	1,385,472
Securities	3,631,076	-	-	-	3,631,076
Gross amount of loans excluding LOF	**19,276,082**	**16,916,519**	**2,213,665**	**877,632**	**39,283,898**
Less: Provision for loan impairment	(1,374,105)	(930,270)	(255,423)	(17,520)	(2,577,318)
Total loans and advances to customers	**17,901,977**	**15,986,249**	**1,958,241**	**860,112**	**36,706,580**

8. LOANS AND ADVANCES TO CUSTOMERS (Continued)

The analysis by credit quality of loans outstanding at 31 December 2012 is as follows:

In Azerbaijani Manats	**Corporate loans**	**Loans to individuals – consumer loans**	**Loans to individuals – entrepreneurship loans**	**Loans to individuals – mortgage loans**	**Total**
Neither overdue nor impaired loans	18,844,258	20,203,999	2,738,770	812,225	**42,599,252**
Overdue but not impaired loans					
Less than 30 days overdue	1,253,672	652,668	373,902	-	**2,280,242**
30 to 90 days overdue	4,788,669	171,152	-	-	**4,959,821**
90 to 180 days overdue	-	9,291	25,908	-	**35,199**
180 to 360 days overdue	-	4,446	-	-	**4,446**
Total overdue but not impaired loans	**6,042,341**	**837,557**	**399,810**	**-**	**7,279,708**
Individually impaired loans					
Less than 30 days overdue	-	2,887	-	-	**2,887**
30 to 90 days overdue	-	11,051	-	-	**11,051**
90 to 180 days overdue	-	30,154	-	-	**30,154**
180 to 360 days overdue	419,831	140,514	22,285	-	**582,630**
Over 360 days overdue	860,941	433,095	207,177	-	**1,501,213**
Total individually impaired loans	**1,280,772**	**617,701**	**229,462**	**-**	**2,127,935**
Gross carrying value of loans	**26,167,371**	**21,659,257**	**3,368,042**	**812,225**	**52,006,895**
Less: Provision for loan impairment	(1,864,727)	(714,305)	(321,483)	-	**(2,900,515)**
Total loans to customers	**24,302,644**	**20,944,952**	**3,046,559**	**812,225**	**49,106,380**

8. LOANS AND ADVANCES TO CUSTOMERS (Continued)

The analysis by credit quality of loans outstanding at 31 December 2011 is as follows:

In Azerbaijani Manats	Corporate loans	Loans to individuals – consumer loans	Loans to individuals – entrepreneurship loans	Loans to individuals – mortgage loans	Total
Neither overdue nor impaired loans	**18,033,007**	**15,480,503**	**1,863,148**	**877,632**	**36,254,290**
Overdue but not impaired loans					
Less than 30 days overdue	-	326,782	93,858	-	**420,640**
30 to 90 days overdue	193,527	336,326	-	-	**529,853**
90 to 180 days overdue	24,828	94,479	34,218	-	**153,525**
Total overdue but not impaired loans	**218,355**	**757,587**	**128,076**	**-**	**1,104,018**
Individually impaired loans					
90 to 180 days overdue	88,649	131,901	-	-	**220,550**
180 to 360 days overdue	433,111	134,743	82,805	-	**650,659**
Over 360 days overdue	502,960	411,785	139,636	-	**1,054,381**
Total individually impaired loans	**1,024,720**	**678,429**	**222,441**	**-**	**1,925,590**
Gross carrying value of loans	**19,276,082**	**16,916,519**	**2,213,665**	**877,632**	**39,283,898**
Less: Provision for loan impairment	(1,374,105)	(930,270)	(255,423)	(17,520)	**(2,577,318)**
Total loans to customers	**17,901,977**	**15,986,249**	**1,958,242**	**860,112**	**36,706,580**

The primary factors that the Bank considers in determining the loan as impaired is its overdue status and reliability of related collateral, if any. As a result, the Bank presents above an ageing analysis of loans that are individually determined to be impaired.

Current and not impaired, but renegotiated loans represent the carrying amount of loans that would otherwise be past due or impaired whose terms have been renegotiated. Past due but not impaired loans represent collateralised loans where the fair value of collateral covers the overdue interest and principal repayments and overdue period would not be more than 90 days. The amount reported as past due but not impaired is the whole balance of such loans, not only the individual instalments that are past due.

Disclosure of the fair value of collaterals in respect of loans past due but not impaired and in respect of loans individually determined to be impaired at 31 December 2012 and 31 December 2011 was considered impracticable by the management of the Bank.

8. LOANS AND ADVANCES TO CUSTOMERS (Continued)

Economic sector risk concentrations within the loans to customer's portfolio are as follows:

In Azerbaijani Manats	31 December 2012		31 December 2011	
	Amount	**%**	**Amount**	**%**
Individuals	22,471,375	43%	17,794,151	45%
Trade and service	10,443,676	20%	9,046,202	23%
Construction	1,731,100	3%	2,293,025	6%
Agriculture	8,424,173	16%	5,889,979	15%
Manufacturing	7,967,816	15%	3,912,943	10%
Other	968,755	2%	347,598	1%
Total loans to customers, gross	**52,006,895**	**100%**	**39,283,898**	**100%**

As at 31 December 2012 and 31 December 2011, the Bank had no single borrower whose loan balances exceeded 10% of total loans to customers.

Credit concentration risk

As at 31 December 2012 and 31 December 2011 the Bank had 10,630 and 8,293 borrowers, respectively; the largest single borrower represented 9.6% of the total loan portfolio as at 31 December 2012 and 4.5% of the total loan portfolio as at 31 December 2011. The next largest borrower represents another of 4.6% the Bank's loan portfolio as at 31 December 2012 and 3.3% of the Bank's loan portfolio as at 31 December 2011.

As at 31 December 2012 the credit concentration of the Bank was as follows:

In Azerbaijani Manats	31 December 2012		
	Number of borrowers	**Total debt**	**% of total**
More than 100,000	100	26,278,408	51%
From 50,001 to 100,000	60	2,187,482	4%
From 10,001 to 50,000	555	7,131,680	14%
From 3,001 to 10,000	2,563	7,810,742	15%
From 1,001 to 3,000	5,145	6,848,164	13%
1,000 or less	2,180	1,750,419	3%
Total loans to customers, gross	**10,603**	**52,006,895**	**100%**

8. LOANS AND ADVANCES TO CUSTOMERS (Continued)

As at 31 December 2011 the credit concentration of the Bank was as follows:

In Azerbaijani Manats		**31 December 2012**	
	Number of borrowers	**Total debt**	**% of total**
More than 100,000	61	17,769,540	45%
From 50,001 to 100,000	28	2,080,618	5%
From 10,001 to 50,000	308	6,356,807	16%
From 3,001 to 10,000	1,128	5,086,057	13%
From 1,001 to 3,000	3,493	6,213,428	16%
1,000 or less	3,275	1,777,448	5%
Total loans to customers, gross	**8,293**	**39,283,898**	**100%**

As at 31 December 2012, the amount of loans to customers those were individually determined to be impaired was AZN 2,127,935 (31 December 2011: AZN 1,933,835). The fair value of collateral obtained against those loans are vehicles and equipment – AZN 85,000 and real estate – AZN 4,786,555 totalling to AZN 4,871,555 (31 December 2011: AZN 5,106,643).

9. AVAILABLE-FOR-SALE INVESTMENTS

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Debt securities	11,510,138	5,246,241
Equity securities	455,400	455,100
Total available-for-sale investments	**11,965,538**	**5,701,341**

Debt Security

In Azerbaijani Manats	**Nominal interest rate**	**31 December 2012**	**Nominal interest rate**	**31 December 2011**
Coupon bonds of the Ministry of Finance of the Republic of Azerbaijan	2.97%-5.12%	7,555,457	3%-5%	5,246,241
Debt securities of the Azerbaijan Mortgage Fund	-	-	-	-
CBAR short term notes	1.28%-2.15%	3,004,681	-	-
Unibank CB	9%	450,000	-	-
Bank of Baku OJSC	11%	500,000	-	-
Total debt security		**11,510,138**		**5,246,241**

Equity Security

In Azerbaijani Manats	**Notes**	**Ownership interest %**	**31December 2012**	**Ownership interest %**	**31December 2011**
Milli Kart Processing centre		2.40%	120,000	2.40%	120,000
Bashak Inam Insurance company		5.83%	350,000	5.83%	350,000
Baku Stock Exchange		5.00%	60,000	5.00%	60,000
Less: Provision for impairment	**18**		(74,600)		(74,900)
Total equity security			**455,400**		**455,100**

9. AVAILABLE-FOR-SALE INVESTMENTS (Continued)

Management could not reliably estimate the fair value of the Bank's investments in shares of the above investees. These investments are carried at total cost of AZN 455,400 (31 December 2011: AZN 455,100). These investee companies have not published their recent financial information about its operations, their shares are not quoted and recent trade prices are not publicly accessible. The market for these assets is not liquid, but the management of the Bank believes potentially interested buyers could be other resident commercial banks and equity investment companies at a price close to their carrying value.

9. NON-CURRENT ASSETS HELD FOR SALE

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Received pledged assets on Loans to Customers	350,178	-
Total non-current assets held for sale	**350,178**	**-**

Non-current assets held for sale represent the assets transferred to the Bank's accounts which were pledged for the Loans to Customers accounts for the impaired loans. The Bank has obtained legal ownership over these assets based on the court decision. Based on Central Bank's regulations these assets have to be declared for sale and must be sold during the next three years from the date of transfer to the Bank's balance.

10. PREMISES, EQUIPMENT AND INTANGIBLE ASSETS

In Azerbaijani Manats	**Furniture and Fixtures**	**Computer and Equipment**	**Vehicles**	**Other fixed assets**	**Intangible assets**	**Total**
Net book value as at 31 December 2010	**440,588**	**256,228**	**43,921**	**52,593**	**83,269**	**876,599**
Additions	8,419	53,515	17,700	7,891	-	**87,525**
Disposals/Sales	(1,883)	-	-	(210)	(8,863)	**(10,956)**
Depreciation charge for the year	(65,944)	(74,380)	(10,248)	(5,804)	(9,554)	**(165,930)**
Eliminated on disposals	259	-	-	40	1,362	**1,661**
Net book value as at 31 December 2011	**381,439**	**235,363**	**51,373**	**54,510**	**66,214**	**788,899**
Cost at 31 December 2011	732,631	627,316	213,676	74,424	102,722	**1,750,769**
Accumulated Depreciation	(351,192)	(391,953)	(162,303)	(19,914)	(36,508)	**(961,870)**
Net book value as at 31 December 2011	**381,439**	**235,363**	**51,373**	**54,510**	**66,214**	**788,899**
Additions	19,313	58,409	83,000	2,878	6,064	**169,664**
Disposals/Sales	(1,172)	(5,025)	-	(529)	-	**(6,726)**
Depreciation charge for the year	(66,856)	(80,781)	(16,256)	(6,438)	(8,655)	**(178,986)**
Eliminated on disposals	653	2,224	-	131	-	**3,008**
Net book value as at 31 December 2012	**333,377**	**210,190**	**118,117**	**50,552**	**63,623**	**775,859**
Cost at 31 December 2012	750,772	680,700	296,676	76,773	108,786	**1,913,707**
Accumulated Depreciation	(417,395)	(470,510)	(178,559)	(26,221)	(45,163)	**(1,137,848)**
Net book value as at 31 December 2012	**333,377**	**210,190**	**118,117**	**50,552**	**63,623**	**775,859**

As at 31 December 2012 and 31 December 2011, included in property, equipment and intangible asset were fully depreciated assets of AZN AZN 19,820 and AZN 196,489, respectively.

As at 31 December 2012 included in property, equipment and intangible assets there were neither any assets with restrictions on title, nor any assets that were pledged as security for liabilities.

All tangible fixed assets were insured both in 2012 and 2011 years. Net book value of insured assets as at 31 December 2012 and 31 December 2011 was AZN 712,236 and AZN 693,622 respectively. Total insurance payments during 2012 and 2011 years were AZN 11,658 and AZN 6,669, correspondingly.

11. OTHER ASSETS

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Other financial assets:		
Settlements on money transfers	4,322	2,138
Plastic cards settlements	30,802	43,294
Total other financial assets	**35,124**	**45,432**
Other non-financial assets:		
Prepayments to suppliers for goods and services	2,463	6,761
Total other assets	**37,587**	**52,193**

12. DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Loans from banks and financial institutions	12,010,907	8,763,780
Term deposits of banks and other financial institutions	29,444,820	11,925,143
Correspondent accounts of other banks	42,266	56,546
Blocked accounts on Letters of Credit	1,037,700	-
Blocked accounts on Letters of Guarantee	1,256,000	
Total due to banks and other financial institutions	**43,791,693**	**20,745,469**

Accrued interest included in due to banks and other financial institutions is in the amount of AZN 243,314 and AZN 87,913 as at 31 December 2012 and 31 December 2011, respectively.

As at 31 December 2012, term deposits of banks and other financial institutions include AZN 5,000,000 from a “ASB Bank” OJSC with an interest rate of 9% per annum and maturity in December 2013. Remaining resident banks and other financial institutions hold AZN 16,744,320 (in EUR, AZN and USD) term deposits with interest rates 0%-10%.and maturities between January and December 2013. Additionally term deposits include AZN 8,738,200 (both in EUR and USD) from nonresident banks with interest rates 3.33%-6.67% and maturities between January and December of 2013.

As at 31 December 2012, loans from banks and financial institutions include AZN 2,968,930 (in EUR, AZN, USD) loans from non-resident banks with interest rates (6.93%-7.47%) and maturity between October 2014 and July 2017, AZN 8,299,014 from resident banks and financial institutions with interest rates 0%-2% and maturities between August 2013 and April 2017 and AZN 808,597 from Azerbaijan Mortgage Fund with interest rates 1%-2% and maturity in May 2037.

As at 31 December 2012 due to banks accounts amounted to AZN 2,293,700 were held as security against letter of credits, guarantees issued and other transaction related contingent obligations.

13. CUSTOMER ACCOUNTS

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Current and settlement account	11,211,269	11,180,387
Time deposits	14,862,020	18,732,728
Total customer accounts	**26,073,289**	**29,913,115**

Accrued interest included in customer accounts is in the amount of AZN 493,683 and AZN 431,726 as at 31 December 2012 and 31 December 2011, respectively.

As at 31 December 2012 and 31 December 2011, customer accounts amounted to AZN 9,281 and AZN 7,087,413, respectively, were held as security against letter of credits, guarantees issued and other transaction related contingent obligations.

As at 31 December 2012, the Bank had one customer had a total balance of AZN of AZN 3,178,445 or 12.19% total customer accounts (31 December 2011, one customer amounted to AZN 5,995,347or 20.04% of total customer accounts).

Economic sector concentrations within customer accounts are as follows:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Analysis by sector:		
Individuals	18,250,520	15,863,212
Trade and Services	6,181,513	9,562,699
Manufacturing	230,650	2,270,820
Energy and Chemicals	55,214	-
Insurance	-	27,297
State and public organizations	1,240,205	1,299,751
Construction	42,279	540,747
Agriculture	1,570	69,635
Transportation and communication	8,847	46,999
Other	62,491	231,955
Total Customer Accounts	**26,073,289**	**29,913,115**

14. OTHER LIABILITIES

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Other financial liabilities:		
Settlements on money transfer	22,487	67,278
Unused vacation and other payables to employees	27,966	85,187
Accrued expenses	108,012	68,036
Dividends payable	83,009	-
Taxes payable	92	-
Total financial liabilities	**241,566**	**220,501**
Other non-financial liabilities:		
Deferred income on guarantees and other commitments	28,124	25,863
Total other liabilities	**269,690**	**246,364**

15. INCOME TAXES

The Bank measures and records its current income tax payable and its tax bases related to assets and liabilities in accordance with the statutory tax regulations of the Republic of Azerbaijan where the Bank operates, which differ from IFRS.

The Bank is subject to certain permanent tax differences due to non-tax deductibility of certain expenses and certain income being treated as non-taxable for tax purposes.

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Temporary differences as at 31 December 2012 and 31 December 2011 relate mostly to different methods timing of income and expense recognition as well as to temporary differences generated by taxation bases' differences for certain assets.

On 28 October 2008, a Law on "Stimulation of increase of capitalisation of banks, insurance and reinsurance companies" was adopted. According to the Law, part of the profit of banks, insurance and reinsurance companies directed to increase their share capital is not subject to profit tax for three years beginning from 1 January 2009. The current reporting year is the last year for exercising the aforementioned tax holiday and the law is not expected to be extended for the future periods.

As a result of this law, if the subject matter of the taxable temporary differences is realized within the period of these holidays no tax liabilities should be accrued; otherwise it should be accrued using the current profit tax rate.

16. INCOME TAXES (Continued)

Tax legislation of the Republic of Azerbaijan in particular may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result the Bank may be assessed additional taxes, penalties and interest which could be material for these financial statements.

Temporary differences as at 31 December 2012 and 31 December 2011 comprise:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
(Taxable) / Deductible temporary differences:		
Available for sale investments	(5,600)	-
Due from Banks	(49,076)	-
Loans and advances to customers	(572,477)	-
Property and equipment	(145,459)	13,496
Intangible assets	51	-
Other assets	(103,438)	(404,021)
Other liabilities	28,124	25,559
Total (taxable) / deductible temporary differences	**(847,875)**	**(364,966)**
Statutory tax rate	20%	20%
Net deferred tax (liability) / asset	**(169,575)**	**(72,993)**

Relationships between tax expenses and accounting profit for the years ended 31 December 2012 and 31 December 2011 are explained as follows:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Profit before income tax	2,010,808	1,478,629
Theoretical tax charge at the statutory tax rate (20%)	(402,162)	(295,726)
Profit tax amount to be capitalized	-	123,766
Non-deductible expenses	(146,335)	(46,925)
Income tax expense	**(548,497)**	**(218,885)**
Current income tax expense	(444,289)	(123,766)
Change in the deferred tax	(104,208)	(95,119)
Income tax expense	**(548,497)**	**(218,885)**

16. INCOME TAXES (Continued)

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Deferred income tax (liabilities)/asset		
Beginning of the year	**(72,993)**	**29,752**
Change in the deferred income tax for the period charged to profit and loss accounts	(104,208)	(95,119)
Change in the deferred income tax for the period charged to equity	7,626	(7,626)
End of the year	**(169,575)**	**(72,993)**

16. SHARE CAPITAL

As of 31 December 2012, authorized, issued and paid-in share capital consisted of ordinary 12,242,908 shares with par value of AZN 1 each (31 December 2011: 11,624,080 ordinary shares with par value of AZN 1 each).

During 2012, the Bank increased its authorized share capital and issued an additional 618,828 ordinary shares (2011: 633,560) with a nominal value of AZN 1 per share, as a result of transfer of AZN 618,828 (2011: AZN: 633,560) from retained earnings to share capital. This emission has been performed to benefit from the enacted law on tax holidays. All issued shares were acquired by existing shareholders in proportion of their existing interest.

General meeting of Shareholders declared dividends of AZN 471,330 (2011: AZN 490,004) according to Bank’s 2011 financial year results, which was paid AZN 471,330 (2011: AZN 465,792) due to undervalued profit tax of 2009 paid by Bank and charged to shareholders’ received dividends respective to their shareholding percentages. As at 31 December 2012 and 31 December 2011, the Bank’s authorized and issued ordinary shares comprised the following number of shares per AZN 1 each:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Shareholder		
“T.C. Ziraat Bankasi” A.S. (the Republic of Turkey)	5,631,738	5,347,077
“Aqrarkredit” Closed Joint Stock Non-Banking Credit Organization (the Republic of Azerbaijan)	5,631,738	5,347,077
“Ziraat Bank International” A.G. (the Federal Republic of Germany)	489,716	464,963
“Turanbank” OJSC (the Republic of Azerbaijan)	489,716	464,963
Total ordinary shares	**12,242,908**	**11,624,080**

17. NET INTEREST INCOME

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Interest income on financial assets at amortised cost:		
Interest income on unimpaired assets	6,896,828	6,179,108
Interest income on impaired assets	353,219	344,970
	7,250,047	**6,524,078**
Interest income on available-for-sale investments	413,258	231,603
Total interest income	**7,663,305**	**6,755,681**
Interest income on financial assets at amortized cost:		
Interest income on loans to customers	7,002,556	6,096,514
Interest income on due from banks	247,491	427,564
	7,250,047	**6,524,078**
Interest income on available-for-sale investments	413,258	231,603
	7,663,305	**6,755,681**
Interest expense comprise of:		
Interest expense on customer accounts	(1,599,156)	(1,703,481)
Interest expense on due to banks and other financial institutions	(1,004,632)	(386,659)
Total interest expense	**(2,603,788)**	**(2,090,140)**
Net interest income before provision for impairment losses on interest bearing assets	**5,059,517**	**4,665,541**

18. ALLOWANCE FOR IMPAIRMENT LOSSES, OTHER PROVISIONS

In Azerbaijani Manats	**Loans to Customers (Note 8)**	**Available-for-sale investments (Note 9)**	**Guarantees and other commitment (Note 25)**	**Due from banks (Note 7)**	**Total**
31 December 2010	**(1,743,325)**	**(74,900)**	**(91,264)**	**(35,586)**	**(1,945,075)**
(Charge) / recovery of provision for impairment	(833,993)	-	91,264	15,907	(726,822)
31 December 2011	**(2,577,318)**	**(74,900)**	**-**	**(19,679)**	**(2,671,897)**
(Charge) / recovery of provision for impairment	(323,197)	300	-	19,679	(303,218)
31 December 2012	**(2,900,515)**	**(74,600)**	**-**	**-**	**(2,975,115)**

19. NET GAIN ON FOREIGN EXCHANGE OPERATIONS

Net gain on foreign exchange operations comprises:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Dealing, net	460,130	354,099
Translation differences, net	(5,366)	(39,116)
Total net gain on foreign exchange operations	**454,764**	**314,983**

20. FEE AND COMMISSION INCOME AND EXPENSE

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Fee and commission income		
Settlements	552,252	412,767
Plastic cards operations	330,911	282,484
Cash operations	299,252	257,917
Fees from documentary operations	178,714	156,066
Foreign exchange operations	99,197	137,348
Other	3,010	46,564
Total fee and commission income	**1,463,336**	**1,293,146**
Fee and commission expense		
Plastic cards operations	(234,166)	(164,399)
Settlements	(89,305)	(76,121)
Securities operations	(36,074)	(1,826)
Fees from documentary operations	(2,450)	(1,993)
Cash operations	-	(3,138)
Other	(38,502)	(37,640)
Total fee and commission expense	**(400,497)**	**(285,117)**
Net fee and commission income	**1,062,839**	**1,008,029**

21. OTHER INCOME

Other income comprises:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Dividends received from Baku Stock Exchange	6,000	5,483
Other income	10,042	3,085
Other Income	**16,042**	**8,568**

22. ADMINISTRATIVE AND OTHER OPERATING EXPENSES

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Staff costs	(2,049,575)	(1,775,454)
Rent expenses	(678,550)	(666,587)
Contributions to SPF	(399,019)	(337,852)
Communications	(226,289)	(192,037)
Security expenses	(183,681)	(187,887)
Depreciation and amortization (See Note 11)	(196,480)	(165,930)
Penalties and Fines	(112,913)	-
Professional and legal services	(95,301)	(54,885)
Payments to Azerbaijan Deposit Insurance Fund	(72,160)	(66,356)
Office repair and supplies	(41,171)	(58,276)
Representation expenses	(38,352)	-
Taxes other than income tax	(32,876)	(13,091)
Advertising costs	(32,627)	(23,128)
Repair and maintenance	(29,324)	(76,574)
Utilities expenses	(26,632)	(9,771)
Membership fees	(12,600)	(22,548)
Business trip expenses	(12,120)	(39,549)
Insurance expenses	(11,658)	-
Transportation expenses	(11,516)	-
Training costs	(3,468)	(3,658)
Other expenses	(12,825)	(98,103)
Total Operational and Administrative Expenses	**(4,279,137)**	**(3,791,686)**

23. EARNINGS PER SHARE

The earnings and weighted average number of ordinary shares used in calculation of basic and diluted earnings per share are as follows:

In Azerbaijani Manats, except the number of shares	**31 December 2012**	**31 December 2011**
Net profit for the year	1,462,310	1,259,744
Weighted average number of ordinary shares in issue (in thousands of units)	12,242,908	11,360,097
Earnings/(loss) per ordinary share – basic and diluted (in AZN per share)	**0.119**	**0.110**

24. COMMITMENTS AND CONTINGENCIES

In the normal course of business, the Bank is a party to financial instruments with off-balance sheet risk in order to meet the needs of its customers. These instruments, involving varying degrees of credit risk, are not reflected in the statement of financial position.

The Bank's maximum exposure to credit loss under contingent liabilities and commitments to extend credit, in the event of non-performance by the other party where all counterclaims, collateral or security prove valueless, is represented by the contractual amounts of those instruments.

The Bank uses the same credit control and management policies in undertaking off-balance sheet commitments as it does for on-balance operations. As at 31 December 2012 and 31 December 2011, the nominal or contract amounts of operating lease and credit related commitments were as following:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Operating lease commitments		
Less than 1 year	35,325	422,640
Less than 1 year but not later than 5 years	2,634,837	1,667,560
More than 5 years	-	821,280
Total operating lease commitments	**2,670,162**	**2,911,480**

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Credit commitments		
Guarantees issued	4,484,991	3,220,411
Commitments on loans and unused credit lines	5,915,657	6,778,823
Letters of Credit	1,037,700	11,158,613
Total credit commitments	**11,438,348**	**21,157,847**

Accrued income on fee and commissions on guarantees issued is included in other liabilities Note15.

Maturities of whole amount of unused credit lines as at 31 December 2012 (5,915,657 AZN) and 31 December 2011 (6,778,823 AZN) are considered as on demand and less than one month.

Credit related commitments are denominated in below currencies as follows:

In Azerbaijani Manats	**31 December 2012**	**31 December 2011**
Credit commitments		
US Dollars	3,874,145	10,317,431
Euros	1,246,278	4,071,200
Azerbaijani Manats	6,317,925	6,769,216
Total credit commitments	**11,438,348**	**21,157,847**

25. COMMITMENTS AND CONTINGENCIES (Continued)

Legal proceedings

From time to time and in the normal course of business, claims against the Bank might be received from customers and counterparties. Management is of the opinion that no material un-accrued losses will beincurred and accordingly no provision has been made in these financial statements.

Taxation

Provisions of tax legislation of the Republic of Azerbaijan are sometimes inconsistent and may have more than one interpretation, which allows the tax authorities to take decisions based on their own arbitrary interpretation of these provisions. In practice, the tax authorities often interpret the tax legislation not in favour of the taxpayers, who have to resort to court proceeding to defend their position against the tax authorities. It should be noted that the tax authorities can use the clarifications issued by the judicial bodies that have introduced the concept of “unjustified tax benefit”, “primary commercial goal of transaction” and the criteria of “commercial purpose (substance) of transaction”.

Such uncertainty could, in particular, be attributed to tax treatment of financial instruments/derivatives and determination of market price of transactions for transfer pricing purposes. It could also lead to temporary taxable differences occurred due to loan impairment provisions and income tax liabilities being treated by the tax authorities as understatement of the tax base. The management of the Bank is confident that applicable taxes have all been accrued and, consequently, creation of respective provisions is not required.

Generally, taxpayers are subject to tax audits with respect to three calendar years preceding the year of the audit. However, completed audits do not exclude the possibility of subsequent additional tax audits performed by upper-level tax inspectorates reviewing the results of tax audits of their subordinate tax inspectorates. Also according to the clarification of the Constitutional Court of the Republic of Azerbaijan, the statute of limitation for tax liabilities may be extended beyond the three year term set forth in the tax legislation, if a court determines that the taxpayers have obstructed or hindered a tax inspection.

25. TRANSACTIONS WITH RELATED PARTIES

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

Shareholders, key management personnel and their relatives are main categories of related parties that Bank reports on. Details of transactions between the Bank and aforementioned related parties are disclosed below:

As at 31 December 2012/for the year then ended	Shareholders	Key Management personnel	Other (including relatives)	Total related party balances/ transactions	Total per category in financial statements
Statement of financial position					
Due from banks	3,088,688	-	-	3,088,688	14,882,989
Loans to customers, net	-	183,206	17,742	200,948	49,106,380
Due to Banks	2,080,688			2,080,688	43,791,693
Customer Accounts	-	80,002	-	80,002	26,073,289
Statement of Comprehensive income					
Interest Income	3,222	17,740	1,104	22,066	7,663,305
Interest Expense	(3,243)	(6,869)	(4,896)	(15,008)	(2,603,788)
Fee and commission income	1,439	11,869	1,115	14,423	1,463,336
Fee and commission expense	(7,000)	-	-	(7,000)	(400,497)
Operating expenses	-	(700,019)	-	(700,019)	(4,279,137)

As at 31 December 2011/for the year then ended	Shareholders	Key Management personnel	Other (including relatives)	Total related party balances/ transactions	Total per category in financial statements
Statement of financial position					
Due from banks	36,169	-	-	36,169	17,064,028
Loans to customers, net	-	120,938	-	120,938	36,875,075
Due to Banks	26,696	-	-	26,696	20,745,469
Customer Accounts	-	7,328	-	7,328	29,913,115
Statement of Comprehensive income					
Interest Income	-	8,647	160	8,807	6,755,681
Interest Expense	-	(1,663)	(653)	(2,316)	(2,090,140)
Fee and commission income	1,984	4,904	-	6,888	1,293,146
Fee and commission expense	(2,093)	-	-	(2,093)	(285,117)
Operating expenses	-	(469,507)	-	(469,507)	(3,791,686)

26. CAPITAL MANAGEMENT

The Bank's objectives when managing capital are to comply with the capital requirements set by the CBAR, to safeguard the Bank's ability to continue as a going concern and to maintain a sufficient capital base to achieve a capital adequacy ratio of at least 12%. Compliance with capital adequacy ratios set by the CBAR is monitored monthly with reports outlining their calculation reviewed and signed by the Bank's Chairman of Management Board, Chief Accountant, Chief of Internal Audit Department and the Chairman of Supervisory Board. Other objectives of capital management are evaluated annually.

Under the current capital requirements set by the CBAR banks have to: (a) hold the minimum level of share capital of AZN 10,000,000 (2010: AZN 10,000,000); (b) maintain a ratio of regulatory capital to risk weighted assets ("statutory capital ratio") at or above a prescribed minimum of 12% (2011: 12%) and (c) maintain a ratio of tier-1 capital to the risk-weighted assets (the "Tier-1 capital ratio") at or above the prescribed minimum of 6% (2011: 6%).

As at 31 December 2012 statutory capital ratio and Tier 1 capital ratio calculated per the requirements of CBAR was 18.42% and 20.80% respectively. (as at 31 December 2011 the same ratios were 21.21% and 23.59% respectively).

The Central Bank of the Republic of Azerbaijan has constanly increased qualitative and quantitative capital requirements within the framework of the strategy aimed at further strenghtening of financial stability and sustainability of the banking sector, development of the corporative governance system and protection of interests of depositors and investors built upon best practices. Currently, banks are capitalized up to a new qualitative level which led to eventual high effectiveness of the banking sector and improved financial sustainability indicators.

On July 25, 2012 CBA Management Board took a decision to increase the threshold of aggregate capital of operational banks, as well as authorized capital for newly launched banks up to AZN 50 mln. A new norm on the minimum amount of aggregate capital shall take effect from January 1, 2014. Application of new capital requirements shall result in strenghtened capital position of Azerbaijani banks along with high capital quality and effectiveness of financial intermediation, the sustainable banking system and further enhanced and further enhanced financial stabilit.

27. SEGMENT ANALYSIS

The Bank is organized on the basis of two main business segments:

• Retail banking – representing private banking services, private customer current accounts, savings, deposits, investment savings products, custody, credit and debit cards, consumer loans and mortgages;

• Corporate banking – representing direct debit facilities, current accounts, deposits, overdrafts, loan and other credit facilities, foreign currency and derivative products.

There are no other material items of income or expense between the business segments. Internal charges and transfer pricing adjustments have been reflected in the performance of each business.

Revenue sharing agreements are used to allocate external customer revenues to a business segment on a reasonable basis.

28. SEGMENT ANALYSIS (Continued)

Segment information for the year ended 31 December 2012:

In Azerbaijani Manats	**Retail Banking**	**Corporate Banking**	**Other Segments**	**Total**
Interest Income	4,502,388	3,160,917	-	7,663,305
Interest Expense	(697,338)	(1,906,450)	-	(2,603,788)
Provision for impairment losses on interest bearing assets	(257,284)	(27,980)	(17,954)	(303,218)
Net gain on foreign exchange operations	247,352	207,412	-	454,764
Fee and commission income	458,541	517,637	487,158	1,463,336
Fee and commission expense	(275,118)	(125,379)	-	(400,497)
Other income	-	-	16,042	16,042
Operating expenses	(2,436,846)	(1,353,719)	(488,572)	(4,279,137)
Profit before income tax	**1,541,695**	**472,438**	**(3,326)**	**2,010,807**
Segment assets	**21,074,287**	**62,296,054**	**1,163,624**	**84,533,965**
Segment liabilities	**18,250,520**	**51,614,462**	**702,297**	**70,567,279**
Other segment items:				
Depreciation and amortization charge on property, equipment and intangible assets (See Note 11)	-	-	196,480	196,480
Loans to Customers	21,074,287	28,032,093	-	49,106,380
Property, equipment and intangible assets	-	-	712,236	712,236
Customer accounts	18,250,520	7,822,769	-	26,073,289

28. SEGMENT ANALYSIS (Continued)

Segment information for the year ended 31 December 2011 is included in below table:

In Azerbaijani Manats	**Retail Banking**	**Corporate Banking**	**Other Segments**	**Total**
Interest Income	2,909,130	3,501,581	344,970	6,755,681
Interest Expense	(1,407,939)	(682,201)	-	(2,090,140)
Provision for impairment losses on interest bearing assets	(90,050)	(636,656)	(100)	(726,806)
Net gain on foreign exchange operations	-	-	314,983	314,983
Fee and commission income	838,847	160,872	293,427	1,293,146
Fee and commission expense	(168,125)	(86,253)	(30,739)	(285,117)
Other income	-	5,483	3,085	8,568
Operating expenses	(2,116,964)	(1,654,899)	(19,823)	(3,791,686)
Profit before income tax	**(35,101)**	**607,927**	**905,803**	**1,478,629**
Segment assets	**17,316,691**	**39,003,879**	**7,701,237**	**64,021,807**
Segment liabilities	**15,327,956**	**34,730,407**	**957,233**	**51,015,596**
Other segment items:				
Depreciation and amortization charge on property, equipment and intangible assets (See Note 11)	-	-	(165,930)	(165,930)
Loans to Customers	19,921,081	19,362,817	(2,577,318)	36,706,580
Property, equipment and intangible assets	-	-	788,899	788,899
Customer accounts	15,863,212	13,817,948	231,955	29,913,115

28. FAIR VALUE OF FINANCIAL INSTRUMENTS

Estimated fair value disclosures of financial instruments are made in accordance with the requirements of the IAS 32 “Financial Instruments: Disclosure and Presentation” and IAS 39 “Financial Instruments: Recognition and Measurement”. Fair value is defined as the amount at which the instrument could be exchanged in a current transaction between knowledgeable willing parties in an arm’s length transaction, other than in forced or liquidation sale. The estimates presented herein are not necessarily indicative of the amounts the Bank could realize in a market exchange from the sale of its full holdings of a particular instrument.

Management of the Bank has assessed that except where otherwise stated, fair values of assets and liabilities not currently carried at fair value do not differ materially from carrying values of corresponding assets and liabilities in the statement of financial position.

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments carried at fair value by valuation technique:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;

- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);

- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

31 December 2012	Level 1	Level 2	Level 3	Total
Available-for-sale investment:				
Coupon bonds of the Ministry of Finance of the Republic of Azerbaijan	-	7,555,457	-	**7,555,457**
CBAR short term notes	-	3,004,681	-	**3,004,681**
Unibank CB	-	450,000	-	**450,000**
Bank of Baku OJSC	-	500,000	-	**500,000**
Bashak Inam Insurance Company	-	-	350,000	**350,000**
Baku Stock Exchange	-	-	60,000	**60,000**
Milli Kart Processing Centre	-	-	45,400	**45,400**
Total Available-for-sale Investments	**-**	**11,510,138**	**455,400**	**11,965,538**

29. FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

31 December 2011	Level 1	Level 2	Level 3	Total
Available-for-sale investment:				
Coupon bonds of the Ministry of Finance of the Republic of Azerbaijan	-	5,246,241	-	**5,246,241**
Bashak Inam Insurance Company	-	-	350,000	**350,000**
Baku Stock Exchange	-	-	60,000	**60,000**
Milli Kart Processing Centre	-	-	45,100	**45,100**
Total Available-for-sale Investments	**-**	**5,246,241**	**455,100**	**5,701,341**

A reconciliation of movements in Level 3 of the fair value hierarchy by class of instruments for the year ended 31 December 2012 is as follows:

	Equity investments available for sale
	Corporate shares
Fair value at 1 January 2012	**-**
Transfers into level 3	**455,400**
Fair value at 31 December 2011	**455,400**

The methods and assumptions applied in determining fair values

The estimated fair values of financial instruments have been determined by the Bank, using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Republic of Azerbaijan continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and, therefore, not represent fair values of financial instruments. The management of the Bank has used all available market information in estimating the fair value of financial instruments.

30. FINANCIAL RISK MANAGEMENT

The risk management function within the Bank is carried out in respect of financial risks (credit, market, geographical, currency, liquidity and interest rate), operational risks and legal risks. The primary objectives of the financial risk management function are to establish risk limits, and then ensure that exposure to risks stays within these limits. The operational and legal risk management functions are intended to ensure proper functioning of internal policies and procedures to minimize operational and legal risks.

The Bank recognizes that it is essential to have efficient and effective risk management processes in place. To enable this, the Bank has established a risk management framework, whose main purpose is to protect the Bank from risk and allow it to achieve its performance objectives. Through the risk management framework, the Bank manages the risks the following risks:

30. FINANCIAL RISK MANAGEMENT (Continued)

Credit risk

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

According to the Credit Policy of the Bank, which was approved by the Supervisory Board, there are certain limits set for the loan portfolio in order to ensure its diversification and minimisation of possible credit risks. These limits are, as follows:

i. Limits for business portfolio and consumer loans portfolio;
ii. Limits by sectors of economy;
iii. Regional limits;
iv. Concentration limits; and
v. Limits by collateral type.

Besides there are certain limits introduced and regularly monitored by the CBAR, which are also mandatory to comply with for all financial institutions of the Republic of Azerbaijan. According to the CBAR the exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on and off balance sheet exposures and daily delivery risk limits in relation to trading items such as forward foreign exchange contracts. Actual exposures against limits are monitored daily. The following sub-limits are applied by the Bank:

1. The maximum loan amount for one borrower or related borrowers' group is, as follows:
   i. 20 percent of the Bank's total equity if the market value of the collateral is at least equal to150 percent of the value of the loan; and
   ii. 7 percent of the Bank's total equity if the market value of the collateral is more than 150percent of the value of the loan;
   iii. The value of the all loans should not exceed the 8 times of the Bank's total equity;
2. The total maximum amount of the Bank's loans to related parties must not exceed:
   i. 20 percent of the Bank's total equity;
   ii. 10 percent of the Bank's equity per legal person; or
   iii. 3 percent of the Bank's equity per individual.

These ratios are calculated based on balances derived from statutory financial statements.
The limits besides those defined by the CBRA are developed and revised by the Risk Management Department on a quarterly basis. In case of material change of the market environment, the limits may also be reviewed. A proposal for limits change is provided firstly to the Credit Committee and next to the Management Board for approval.

The Lending Operations and Reporting department controls maintenance of all limits on a regular basis and some of them (maximum exposure to a single borrower or group of related borrowers, maximum exposure to related parties) are controlled before new loan issue.

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

30. FINANCIAL RISK MANAGEMENT (Continued)

Loan approval procedure and delegations
The loan approval process is conducted in accordance with the procedures described in Lending Policy of the Bank. The delegation of authorities for the loan granting approval process has been defined within the limits approved by Supervisory Board of the Bank for each level of decisionmakingauthority.

Delegation of authorities for credit granting approval
The Supervisory Board reviews and approves all secured loans with amounts over 1,000,000 AZN.

The Credit Commission reviews and approves secured loans with amounts from AZN 500,000 to AZN 1,000,000 for corporate loans, amouts to AZN 1,000,000 for interbank loans.

The Credit Committee reviews and approves secured loans with amounts to AZN 500,000 and interbank loans with amounts to AZN 500,000.

The Credit Commission of customer services structure reviews and approves secured credits with amounts up to AZN 50,000.

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

Monitoring is implemented on a periodic basis during the whole duration of a loan and also depends on the rating granted for the borrower. As the interest payments under the majority of the loans are made on a monthly basis, it gives the Bank additional indicators of the borrower's financial condition. In the case of overdue payments, an extraordinary monitoring is performed by the Credit Committee, which executes all types of loans' monitoring for the purpose of ensuring the security of the Bank's assets and minimising possible credit risks and losses, and the results of it are formulated in a special monitoring report presented for consideration to the Credit Committee of the Bank. A majority of the loans are secured by guarantees and various forms of collateral (real estate, property and equipment, goods in turnover, etc).

The appraisal of the collaterals valued above the 5% of Bank's Capital is performed by a professional valuation firm.

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

Maximum Exposure
The Bank's maximum exposure to on statement of financial position credit risk is generally reflected in the carrying amounts of financial assets on the statement of financial position. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

The maximum credit risk for off-balance items, mainly letters of credit and guarantees, represents the gross amount of the commitment. The Bank's maximum exposure to off-balance credit risk is disclosed in Note 25 "Contingencies and Commitments".

30. FINANCIAL RISK MANAGEMENT (Continued)

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

The following table presents the maximum exposure to credit risk of financial assets and contingent liabilities. For financial assets the maximum exposure equals to a carrying value of those assets prior to any offset or collateral. For financial guarantees and other contingent liabilities the maximum exposure to credit risk is the maximum amount the Bank would have to pay if the guarantee was called on or in the case of commitments, if the loan amount was called on.

31 December 2012	Maximum exposure	Offset (cash deposit)	Net exposure after offset	Collateral pledged	Net exposure after offset and collateral
Due from banks	14,882,989	-	14,882,989	-	14,882,989
Available-for-sale investments	11,965,538	-	11,965,538	-	11,965,538
Loans to Customers	49,106,380	7,848,986	41,257,394	27,909,077	13,348,317
Other financial assets	35,124	-	35,124	-	35,124

31 December 2011	Maximum exposure	Offset (cash deposit)	Net exposure after offset	Collateral pledged	Net exposure after offset and collateral
Due from banks	17,064,028	-	17,064,028	-	17,064,028
Available-for-sale investments	5,701,341	-	5,701,341	-	5,701,341
Loans to Customers	36,706,580	1,562,102	35,144,478	25,002,971	10,141,507
Other financial assets	45,432	-	45,432	-	45,432

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

Financial assets are graded according to the current credit rating they have been issued by a "Fitch Ratings" global rating agency. The highest possible rating is A+. Investment grade financial assets have ratings from A+ to B-. Financial assets which have ratings lower than B- are classed as speculative grade.

30. FINANCIAL RISK MANAGEMENT (Continued)

The following table details the credit ratings of financial assets held by the Bank:

31 December 2012	A+	A	BB+	BBB-	B-	Not rated	Total
Due from banks	284,336	2,304,394	-	87,706	-	12,206,553	14,882,989
Available-for-sale investments	-	-	-	11,510,138	-	455,400	11,965,538
Loans to Customers	-	-	-	-	-	49,106,380	49,106,380
Other financial assets	-	-	-	-	-	35,124	35,124

31 December 2011	A+	A	BB+	BBB-	B-	Not rated	Total
Due from banks	1,066,611	-	-	2,597,370	6,533,931	6,866,116	17,064,028
Available-for-sale investments	-	-	-	5,246,241	-	455,100	5,701,341
Loans to Customers	-	-	-	-	-	36,706,580	36,706,580
Other financial assets	-	-	-	-	-	45,432	45,432

Geographical concentration

The Management exercises control over the risk in the legislation and regulatory arena and assesses its influence on the Bank's activity. This approach allows the Bank to minimize potential losses from the investment climate fluctuations in the Republic of Azerbaijan. The Bank's Management Board sets up country limits, which mainly applies to banks of the Commonwealth of Independent States and Baltic countries.

The geographical concentration of assets and liabilities is set out below:

31 December 2012	The Republic of Azerbaijan	Other non-OECD countries	OECD Countries	Total
Financial Assets				
Cash and balances with the CBAR	7,415,434	-	-	**7,415,434**
Due from banks	12,206,553	20,723	2,655,713	**14,882,989**
Loans to customers	42,608,299	43,095	6,454,986	**49,106,380**
Available-for-sale investments	11,965,538	-	-	**11,965,538**
Other financial assets	35,124	-	-	**35,124**
Total Financial Assets	**74,230,948**	**63,818**	**9,110,699**	**83,405,465**
Financial Liabilities				
Due to banks	32,240,686	2,767,392	8,783,615	**43,791,693**
Customer Accounts	19,858,249	598,632	5,616,408	**26,073,289**
Other financial liabilities	241,565	-	-	**241,565**
Total Financial Liabilities	**52,340,500**	**3,366,024**	**14,400,023**	**70,106,547**
Net Position	**21,890,448**	**(3,302,206)**	**(5,289,324)**	**13,298,918**

30. FINANCIAL RISK MANAGEMENT (Continued)

31 December 2011	The Republic of Azerbaijan	Other non-OECD countries	OECD Countries	Total
Financial Assets				
Cash and balances with the CBAR	3,708,766	-	-	**3,708,766**
Due from banks	6,866,115	35,345	10,162,568	**17,064,028**
Loans to customers	34,727,518	1,971,671	7,391	**36,706,580**
Available-for-sale investments	5,701,341	-	-	**5,701,341**
Other financial assets	45,432	-	-	**45,432**
Total Financial Assets	**51,049,172**	**2,007,016**	**10,169,959**	**63,226,147**
Financial Liabilities				
Due to banks	13,892,139	2,622,230	4,231,100	**20,745,469**
Customer Accounts	22,991,064	700,308	6,221,743	**29,913,115**
Other financial liabilities	220,501	-	-	**220,501**
Total Financial Liabilities	**37,103,704**	**3,322,538**	**10,452,843**	**50,879,085**
Net Position	**13,945,468**	**(1,315,522)**	**(282,884)**	**12,347,062**

Liquidity risk

Liquidity risk is defined as the risk when the maturity of assets and liabilities does not match. The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs, guarantees and from margin and other calls on cash settled derivative instruments. Liquidity risk is managed by the Assets and Liabilities Committee ("ALCO") of the Bank.

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

The daily liquidity position is monitored and regular liquidity stress testing under a variety of scenarios covering both normal and more severe market conditions is performed by the Treasury Department and Finance Department. The Treasury Department and Finance Department responsibilities include:

- compliance with requirements of the CBRA for minimum liquidity ratio (the percentage correlation between assets and liabilities shall not be below 30%);
- cash flow forecasting and reporting on it to ALCO and Management Board if necessary;
- monitoring of largest depositors as a factor of risk of liquidity concentration;
- active involvement into domestic and international markets for obtaining mid and short-terms borrowings in case of necessity; and
- monitoring of possible cash movements due to credit activity of the Bank.

A further analysis of the liquidity and interest rate risks is presented in the following tables in accordance with IFRS 7.

30. FINANCIAL RISK MANAGEMENT (Continued)

The amounts disclosed in below tables do not correspond to the amounts recorded on the statement of financial position as the presentation below includes a maturity analysis for financial liabilities that indicates the total remaining contractual payments (including interest payments), which are not recognized in the statement of financial position under the effective interest rate method.

The maturity analysis of financial liabilities at 31 December 2012 is as follows:

31 December 2012	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Total
Financial Liabilities						
Due to banks	9,477,589	4,699,138	16,742,377	14,735,142	806,211	46,460,457
Customer Accounts	15,094,950	3,733,011	6,658,196	1,124,200	-	26,610,357
Other financial liabilities	241,565	-	-	-	-	241,565
Total Financial Liabilities	**24,814,104**	**8,432,149**	**23,400,573**	**15,859,342**	**806,211**	**73,312,379**

The maturity analysis of financial liabilities at 31 December 2011 is as follows:

31 December 2011	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Total
Financial Liabilities						
Due to banks	5,184,954	3,552,368	5,502,781	6,812,384	1,626,393	22,678,880
Customer Accounts	12,775,868	6,071,530	10,594,150	1,150,446	-	30,591,994
Other financial liabilities	212,936	3,039	4,526	-	-	220,501
Total Financial Liabilities	**18,173,758**	**9,626,937**	**16,101,457**	**7,962,830**	**1,626,393**	**53,491,375**

Customer accounts are classified in the above analysis based on contractual maturities. However, in accordance with Azerbaijani Civil Code, individuals have a right to withdraw their deposits prior to maturity if they forfeit their right to accrued interest.

Market Risk

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

Interest rate risk

The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates in the form of both fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce or create losses in the event that unexpected movements arise. The Bank's Assets and Liabilities Management Committee sets limits on the level of mismatch of interest rate re-pricing that may be undertaken, which is monitored regularly. The majority of the Bank's assets and liabilities are priced on a fixed rate basis. Where the Bank has entered into fixed rate contracts these are generally fixed on a short term basis normally at three month intervals.

30. FINANCIAL RISK MANAGEMENT (Continued)

In practice, the Bank has the ability to make immediate changes to rates on most interest bearing assets in response to changes in the interest rate environment.

The Bank retains its right to revise interest rates for the majority of interest bearing liabilities and re-price in line with changes in the CBRA refinancing rate. Management does not consider the Bank to have significant exposure as a result of taking long term deposits at fixed interest rates.

Assuming that the financial assets and liabilities as of 31 December 2012 and 31 December 2011 were to remain until maturity or settlement without any action by the Bank to alter the resulting interest rate risk exposure, an immediate increase of 1% in market interest rates across all maturities and currencies with variable interest would increase the profit for the following year by approximately AZN 76,653 and AZN 82,795, respectively.

An analysis of the Bank's weighted average interest rates on interest bearing assets and liabilities by reference to the next interest rate re-fixing date as at 31 December 2012 is presented below:

31 December 2012	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Maturity undefined	Weighted average rates
Financial Assets							
Due from banks	5.00%	7.31%	7.00%	16.00%	-	-	**7.39%**
Loans to customers	22.60%	22.47%	22.50%	22.28%	21.44%	24.63%	**22.74%**
Available-for-sale investments	1.72%	-	5.12%	11.25%	-	-	**5.05%**
Weighted average interest rates on Financial Assets	**9.77%**	**9.93%**	**11.54%**	**16.51%**	**7.15%**	**8.21%**	**11.73%**
Financial Liabilities							
Due to banks	4.39%	5.97%	5.50%	5.11%	1.80%	-	**7.95%**
Customer Accounts	7.19%	6.16%	8.51%	9.81%	-	-	**7.95%**
Weighted average interest rate on Financial Liabilities	5.79%	6.07%	7.01%	7.46%	0.90%	-	**7.95%**

30. FINANCIAL RISK MANAGEMENT (Continued)

An analysis of the Bank's weighted average interest rates on interest bearing assets and liabilities by reference to the next interest rate re-fixing date as at 31 December 2011 is presented below:

31 December 2011	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Maturity undefined	Weighted average rates
Financial Assets							
Due from banks	-	9.42%	7.30%	-	-	-	**8.36%**
Loans to customers	21.46%	18.56%	18.20%	16.93%	5.84%	31.70%	**17.72%**
Available-for-sale investments	-	3.00%	-	5.00%	-	-	**4.35%**
Weighted average interest rates on Financial Assets	**21.46%**	**8.51%**	**17.13%**	**15.27%**	**5.84%**	**31.70%**	**15.62%**
Financial Liabilities							
Due to banks	3.88%	7.36%	6.83%	4.67%	1.83%	-	**5.68%**
Customer Accounts	6.17%	6.84%	8.02%	10.06%	-	-	**7.55%**
Weighted average interest rate on Financial Liabilities	**5.51%**	**7.03%**	**7.63%**	**15.27%**	**5.84%**	**31.70%**	**15.62%**

The tables below summarise the Bank's exposure to interest rate risks as at 31 December 2012 and 31 December 2011. Included in the tables are both interest-bearing part and non-interest bearing part of financial assets and liabilities at carrying amount, categorised by the earlier of contractual re-pricing or maturity dates:

30. FINANCIAL RISK MANAGEMENT (Continued)

31 December 2012	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Maturity undefined	Total for 2012
Financial Assets							
Due from banks	2,234,994	4,339,187	2,224,782	130,550	-	-	**8,929,513**
Loans to customers	4,656,278	7,339,610	22,538,958	11,851,115	776,199	1,944,220	**49,106,380**
Available-for-sale investments	3,069,841	-	7,940,297	500,000	-	-	**11,510,138**
Total interest bearing financial assets	**9,961,113**	**11,678,797**	**32,704,037**	**12,481,665**	**776,199**	**1,944,220**	**69,546,031**
Cash and balances with CBAR	7,415,434	-	-	-	-	-	**7,415,434**
Due from banks	5,953,476	-	-	-	-	-	**-**
Available-for-sale investments	-	-	-	-	-	455,400	**455,400**
Other financial assets	35,124	-	-	-	-	-	**35,124**
Total Financial Assets	**23,365,147**	**11,678,797**	**32,704,037**	**12,481,665**	**776,199**	**2,399,620**	**83,405,465**
Financial Liabilities							
Due to banks	8,995,831	5,907,700	13,276,086	13,264,286	806,211	-	**42,250,114**
Customer Accounts	3,486,930	3,703,066	6,601,035	1,072,888	-	-	**14,863,919**
Total interest bearing financial liabilities	**12,482,761**	**9,610,766**	**19,877,121**	**14,337,174**	**806,211**	**-**	**57,114,033**
Due to banks	285,579	-	1,256,000	-	-	-	**1,541,579**
Customer Accounts	11,209,370	-	-	-	-	-	**11,209,370**
Other financial liabilities	241,565	-	-	-	-	-	**241,565**
Total Financial Liabilities	**24,219,275**	**9,610,766**	**21,133,121**	**14,337,174**	**806,211**	**-**	**70,106,547**
Liquidity gap	**(854,128)**	**2,068,031**	**11,570,916**	**(1,855,509)**	**(30,012)**	**2,399,620**	**13,298,918**

30. FINANCIAL RISK MANAGEMENT (Continued)

31 December 2011	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	Maturity undefined	Total for 2011
Financial Assets							
Due from banks	-	1,283,500	1,264,014	-	-	-	**2,547,514**
Loans to customers	90,669	959,400	11,566,050	21,747,778	852,164	1,490,519	**36,706,580**
Available-for-sale investments	-	1,726,214	-	3,520,027	-	-	**5,246,241**
Total interest bearing financial assets	**90,669**	**3,969,114**	**12,830,064**	**25,267,805**	**852,164**	**1,490,519**	**44,500,335**
Cash and balances with CBAR	3,708,766	-	-	-	-	-	**3,708,766**
Due from banks	14,516,514	-	-	-	-	-	**14,516,514**
Available-for-sale investments	-	-	-	-	-	455,100	**455,100**
Other financial assets	45,432	-	-	-	-	-	**45,432**
Total Financial Assets	**18,361,381**	**3,969,114**	**12,830,064**	**25,267,805**	**852,164**	**1,945,619**	**63,226,147**
Financial Liabilities							
Due to banks	954,619	3,420,653	5,073,163	6,424,275	870,452	-	**16,743,162**
Customer Accounts	2,349,084	5,899,535	10,301,045	1,049,084	-	-	**19,598,748**
Total interest bearing financial liabilities	**3,303,703**	**9,320,188**	**15,374,208**	**7,473,359**	**870,452**	**-**	**36,341,910**
Due to banks	4,002,307	-	-	-	-	-	**4,002,307**
Customer Accounts	10,314,367	-	-	-	-	-	**10,314,367**
Other financial liabilities	220,501	-	-	-	-	-	**220,501**
Total Financial Liabilities	**17,840,878**	**9,320,188**	**15,374,208**	**7,473,359**	**870,452**	**-**	**50,879,085**
Liquidity gap	**520,503**	**(5,351,074)**	**(2,544,144)**	**17,794,446**	**(18,288)**	**1,945,619**	**12,347,062**

Currency risk

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

The Bank's exposure to foreign currency exchange rate risk is presented in the table below:

30. FINANCIAL RISK MANAGEMENT (Continued)

31 December 2012	AZN	USD	EURO	Other currency	Total
Cash and balances with CBAR	5,779,735	1,480,581	155,118	-	**7,415,434**
Due from banks	1,131,047	6,006,477	7,693,575	51,890	**14,882,989**
Loans to customers	35,882,016	11,902,208	1,322,156	-	**49,106,380**
Available-for-sale investments	11,965,538	-	-	-	**11,965,538**
Other financial assets	35,124	-	-	-	**35,124**
Total Financial Assets	**54,793,460**	**19,389,266**	**9,170,849**	**51,890**	**83,405,465**
Due to banks	29,781,597	6,729,051	7,281,045	-	**43,791,693**
Customer Accounts	11,576,921	12,591,976	1,869,306	35,086	**26,073,289**
Other financial liabilities	241,565	-	-	-	**241,565**
Total Financial Liabilities	**41,600,083**	**19,321,027**	**9,150,351**	**35,086**	**70,106,547**
Liquidity gap	**13,193,377**	**68,239**	**20,498**	**16,804**	**13,298,918**

31 December 2011	AZN	USD	EURO	Other currency	Total
Cash and balances with CBAR	2,319,104	1,327,512	62,150	-	**3,708,766**
Due from banks	600,546	11,285,502	5,129,337	48,643	**17,064,028**
Loans to customers	18,341,990	17,105,446	1,259,144	-	**36,706,580**
Available-for-sale investments	5,701,341	-	-	-	**5,701,341**
Other financial assets	45,432	-	-	-	**45,432**
Total Financial Assets	**27,008,413**	**29,718,460**	**6,450,631**	**48,643**	**63,226,147**
Due to banks	5,252,588	9,335,504	6,157,377	-	**20,745,469**
Customer Accounts	9,958,672	19,610,964	314,463	29,016	**29,913,115**
Other financial liabilities	120,910	91,416	8,058	117	**220,501**
Total Financial Liabilities	**15,332,170**	**29,037,884**	**6,479,898**	**29,133**	**50,879,085**
Liquidity gap	**11,676,243**	**680,576**	**(29,267)**	**19,510**	**12,347,062**

The following table details the Bank's sensitivity to a 10% increase and decrease in the USD and EUR against the AZN. 10% is the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for a 10% change in foreign currency rates. The sensitivity analysis includes external loans as well as loans to foreign operations within the Bank where the denomination of the loan is in a currency other than the currency of the lender or the borrower.

30. FINANCIAL RISK MANAGEMENT (Continued)

In Azerbaijani Manats	**31 December 2012** **Impact on profit or loss**	**31 December 2011** **Impact on profit or loss**
US Dollars strengthening by 10%	(6,824)	(85,051)
US Dollars weakening by 10%	6,824	85,051
Euro strengthening by 10%	(2,050)	(1,543)
Euro weakening by 10%	2,050	1,543
TOTAL	-	-

Price risks

Price risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market prices whether those changes are caused by factors specific to the individual security or its issuer or factors affecting all securities traded in the market. The Bank is exposed to price risks of its products which are subject to general and specific market fluctuations.

Limitations of sensitivity analysis

The above tables demonstrate the effect of a change in a key assumption while other assumptions remain unchanged. In reality, there is a correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear, and larger or smaller impacts should not be interpolated or extrapolated from these results.

The sensitivity analysis does not take into consideration that the Bank's assets and liabilities are actively managed. Additionally, the financial position of the Bank may vary at the time that any actual market movement occurs. For example, the Bank's financial risk management strategy aims to manage the exposure to market fluctuations. As investment markets move past various trigger levels, management actions could include selling investments, changing investment portfolio allocation and taking other protective action. Consequently, the actual impact of a change in the assumptions may not have any impact on the liabilities, whereas assets are held at market value on the statement of financial position. In these circumstances, the different measurement bases for liabilities and assets may lead to volatility in shareholder equity.

Other limitations in the above sensitivity analyses include the use of hypothetical market movements to demonstrate potential risk that only represent the Bank's view of possible near-term market changes that cannot be predicted with any certainty; and the assumption that all interest rates move in an identical fashion.

31. EVENTS AFTER THE REPORTING DATE

No significant events have been registered during the period after the reporting date.