XACBANK LLC

Financial Statements together with Independent Auditor's Report for the year ended 31 December 2016

XACBANK LLC

FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2016

CONTENTS **PAGE**

XACBANK LLC

CORPORATE INFORMATION

REGISTERED ADDRESS:	XacBank Building Prime Minister Amar's Street, Post Branch # 46, P.O Box 721, Ulaanbaatar 14200 Mongolia
BOARD OF DIRECTORS:	Mr. Ganbold Chuluun Mr. Boldoo Magvan Ms. Tselmuun Nyamtaishir Mr. Richard Ranken Mr. Michael Madden Mr. James Stent Mr. Ulambayar Bayansan (appointed on 1 July 2015) Mr. Yoshiaki Matsuoka (appointed on 9 December 2015) Ms. Julian Healy (appointed on 19 February 2016) Mr. Yves Jacquot (appointed on 12 February 2016) Mr. Mathew Welch (appointed on 10 October 2016)
CORPORATE SECRETARY:	Ms. Ashidmaa Dashnyam
AUDITORS	Deloitte Onch Audit LLC

XACBANK LLC

STATEMENT BY EXECUTIVES

We, Bold Magvan being Chief Executive Officer of XacBank LLC ("the Bank") and Erdenebayar Ganzorig being Chief Financial Officer primarily responsible for the financial statements of the Bank, do hereby state that, in our opinion, the accompanying financial statements set out on pages 1 to 98 present fairly, in all material respects the financial position of the Bank as at 31 December 2016 and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

BOLDOO MAGVAN	ERDENEBAYAR GANZORIG
(Chief Executive Officer)	(Chief Financial Officer)

Ulaanbaatar
Date: 29 March 2017

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INDEPENDENT AUDITOR'S REPORT

To the Shareholder of XacBank LLC

Report on the Audit of the Financial Statements

Opinion

We have audited the accompanying financial statements of XacBank LLC (the "Bank"), which comprise the statement of financial position as at 31 December 2016, the statement of comprehensive income, the statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2016, and their financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for Opinion

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

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

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

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Deloitte.

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

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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

Other matter

This report is made solely to the shareholder of the Bank, as requested and for no other purpose. We do not assume responsibility towards, or accept liability to, any other person for the contents of this report.

The engagement partner on the audit resulting in this independent auditor's report is Norjinbat Shagdarsuren.

DELOITTE ONCH AUDIT LLC

Norjinbat Shagdarsuren
Director, CPA
Deloitte Onch Audit LLC
29 March 2017

XACBANK LLC

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	2016 MNT'000	2015 MNT'000
Interest and similar income	4	260,906,917	277,576,731
Interest and similar expenses	5	(170,362,720)	(145,238,943)
Net interest income		**90,544,197**	**132,337,788**
Fees and commission income	6	10,435,265	8,539,383
Fees and commission expenses	6	(1,742,748)	(1,517,964)
Net fees and commission income	6	**8,692,517**	**7,021,419**
Net trading loss	7	(17,046,410)	(27,599,340)
Other operating income (loss) – net	8	28,229,589	(11,012,179)
Total operating income		**110,419,893**	**100,747,688**
Credit and other losses	9	(31,141,931)	(21,709,543)
Net operating income		**79,277,962**	**79,038,145**
Operating expenses	10	(56,677,699)	(54,668,708)
Amortisation of deferred grants	30	604,327	397,110
Profit before tax		**23,204,590**	**24,766,547**
Income tax expense	11	(1,751,137)	(2,282,097)
Profit for the year		**21,453,453**	**22,484,450**
Other comprehensive income			
Items that may be reclassified subsequently to profit or loss			
fair value gains of available for sale securities		1,255,916	–
Total comprehensive income, (net of tax) attributable to equity holder of the Bank		**22,709,369**	**22,484,450**
Earnings per share (MNT):			
Basic earnings per share	12	1,054.03	1,104.69
Diluted earnings per share	12	1,054.03	1,104.69

The accompanying notes form an integral part of the financial statements

XACBANK LLC

STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2016

	Note	2016 MNT'000	2015 MNT'000
ASSETS			
Cash and balances with BoM	**13**	326,779,876	183,893,271
Due from banks	**14**	158,627,068	99,107,298
Reverse repurchase agreements	**15**	-	9,981,555
Derivative financial instruments	**16**	125,019,231	2,307,271
Financial investments – available-for-sale	**17**	28,117,332	19,639,167
Financial investments – held-to-maturity	**17**	355,119,924	373,542,234
Loans and advances to customers	**18**	1,157,201,583	1,171,289,306
Other assets	**19**	29,270,431	9,954,513
Properties held for sale	**20**	24,039,038	19,229,982
Property and equipment	**21**	36,619,582	34,796,900
Intangible assets	**22**	10,298,683	8,991,025
Investment property	**23**	4,860,809	-
Deferred tax asset	**24**	1,326,486	3,412,101
TOTAL ASSETS		**2,257,280,043**	**1,936,144,623**
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks	**25**	750,413	20,660,868
Repurchase agreements	**26**	-	100,299,411
Due to customers	**27**	985,503,687	886,255,648
Derivative financial instruments	**16**	928,603	6,669,429
Borrowed funds	**28**	936,093,995	643,220,219
Subordinated loans	**29**	123,443,085	104,216,742
Deferred grants	**30**	1,279,902	1,454,737
Other liabilities	**31**	30,243,515	16,256,639
Income tax payable		2,272	785,728
TOTAL LIABILITIES		**2,078,245,472**	**1,779,819,421**
EQUITY			
Ordinary shares	**32**	55,342,753	55,342,753
Other reserves	**33**	10,531,368	10,531,368
Available for sale reserve		1,255,916	-
Regulatory reserve		8,144,440	-
Retained profits		103,760,094	90,451,081
TOTAL EQUITY		**179,034,571**	**156,325,202**
TOTAL LIABILITIES AND EQUITY		**2,257,280,043**	**1,936,144,623**

The accompanying notes form an integral part of the financial statements.

XACBANK LLC

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2016

	Ordinary shares MNT'000	Share premium MNT'000	Other reserves MNT'000	Retained earnings MNT'000	Available for sale reserve MNT'000	Regulatory Reserve MNT'000	Total equity MNT'000
At January 2015	20,353,656	34,989,097	10,531,368	67,966,631	-	-	133,840,752
Total comprehensive income	-	-	-	22,484,450	-	-	22,484,450
Transfer	34,989,097	(34,989,097)	-	-	-	-	-
At 31 December 2015	**55,342,753**	**-**	**10,531,368**	**90,451,081**	**-**	**-**	**156,325,202**
Total comprehensive income	-	-	-	21,453,453	1,255,916	-	22,709,369
Transfer to regulatory reserve	-	-	-	(8,144,440)	-	8,144,440	-
At 31 December 2016	**55,342,753**	**-**	**10,531,368**	**103,760,094**	**1,255,916**	**8,144,440**	**179,034,571**

The regulatory reserve is set up in compliance with Bank of Mongolia requirement and is distributable to Shareholder of the Bank subject to consultation with them.

The accompanying notes form an integral part of the financial statements.

XACBANK LLC

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016

	Note	2016 MNT'000	2015 MNT'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit before tax		23,204,590	24,766,547
Adjustments for:-			
Loss on disposal of property and equipment	**8**	439	44,075
Gain on disposal of properties held for sale	**8**	(742,952)	(100,653)
Unrealised foreign exchange loss/(gain)	**8**	(26,975,522)	12,375,283
Credit loss for loans and advances to customers	**9**	24,351,510	20,581,344
Impairment for other assets	**9**	429,422	329,498
Impairment (reversal)/loss on properties held for sale	**9**	(108,638)	859,359
Impairment loss on financial investments	**9**	516,445	-
Impairment loss/(reversal) on foreclosed properties	**9**	5,953,192	(60,658)
Depreciation of property and equipment	**10**	5,095,793	4,852,543
Amortisation of intangible assets	**10**	1,633,170	1,705,752
Property and equipment written off	**10**	115,614	15,197
Intangible asset written off	**10**	1,936	2,370
Utilisation of deferred grants	**30**	(604,327)	(397,110)
Dividend income	**8**	(50,802)	-
Operating profit before working capital changes		**32,819,870**	**64,973,547**
Changes in operating asss:-			
Statutory deposits with BoM		(21,789,907)	(9,735,118)
Due from banks		10,260,528	15,749,977
Reverse repurchase agreements		9,981,555	142,817,569
Loans and advances to customers		(22,448,178)	19,739,599
Properties held for sale		(8,818,275)	(9,261,131)
Derivative financial instruments		(122,711,960)	(838,184)
Other assets		(25,252,418)	(3,608,922)
Changes in operating liabilities:-			
Due to banks		(20,292,157)	(14,522,295)
Repurchase agreements		(100,299,411)	(79,464,265)
Due to customers		40,821,792	78,270,270
Derivative financial instruments		138,448,923	10,253,443
Other liabilities		10,734,989	(5,817,792)
Cash used in operations		**(78,544,649)**	**208,556,698**
Income tax paid		(867,618)	(2,988,371)
Net cash flows used in operating activities		**(79,412,267)**	**205,568,327**

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2016 (CONT'D)

	Note	2016 MNT'000	2015 MNT'000
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of financial investments		(90,470,294)	(206,857,820)
Proceeds from financial investments		123,840,400	45,000,000
Proceeds on disposal of property and equipment		195,869	559,938
Purchase of property and equipment	**21**	(7,299,388)	(9,008,488)
Purchase of intangible assets	**22**	(2,873,773)	(2,291,472)
Dividends received from financial investments		50,802	-
Net cash flows generated from (used in) investing activities		**23,443,616**	**(172,597,842)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Drawdown of borrowed funds		528,343,758	257,753,773
Repayment of borrowed funds		(372,587,406)	(340,615,012)
Repayment of subordinated loans		(6,941,657)	-
Dividends paid	**34**	(39)	-
Deferred grants received	**30**	429,492	229,316
Net cash flows generated from/(used in) financing activities		**149,244,148**	**(82,631,923)**
Effect of exchange rate changes on cash and cash equivalents		98,219,406	12,680,708
Net increase (decrease) in cash and cash equivalents		93,275,497	(49,661,438)
Cash and cash equivalents brought forward		255,846,765	292,827,495
Cash and cash equivalents carried forward	**35**	**447,341,668**	**255,846,765**
Operational cash flows from interest			
Interest paid		149,020,527	143,558,980
Interest received		237,455,127	272,122,735

The accompanying notes form an integral part of the financial statements.

1. Corporate Information

XacBank LLC is principally engaged in the business of providing banking and financial services pursuant to License No. 24 issued by the Bank of Mongolia ("BoM"). There have been no significant changes in the nature of the Bank's activities during the year.

The Bank is a limited liability company, incorporated and domiciled in Mongolia. The Bank's registered address and the principal place of business is at XacBank Building, Prime Minister Amar's Street, Sukhbaatar District, Ulaanbaatar, Mongolia.

The holding company of the Bank is TenGer Financial Group LLC, ("TFG" or the "Company") which is incorporated in Mongolia. The shareholders of the holding company are:

- Mongolyn Alt (MAK) Corporation LLC
- International Finance Corporation (IFC)
- ORIX Corporation
- European Bank for Reconstruction and Development (EBRD)
- National Bank of Canada (NBC)
- Ronoc Partners S.A.R.L.
- Mongolia Financial Services
- Triodos Fair Share Fund
- Open Society Forum
- UB Rotary Club
- Boldoo Magvan
- Ganbold Chuluun

The financial statements of the Bank were authorised for issue by the Board of Directors in accordance with a resolution of the Directors on 29 March 2017.

2.1 Basis of preparation

The financial statements of the Bank have been prepared on a historical cost basis, except for derivative financial instruments and available-for-sale financial investments which have been measured at fair value. The financial statements are presented in Mongolian Togrog, which is denoted by the symbol MNT, and all values are rounded to the nearest thousands, except when otherwise indicated.

Statement of compliance

The financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

2.1 Basis of preparation (Contd.)

Presentation of financial statements

The Bank presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the statement of financial position date (current) and more than 12 months after the statement of financial position date (non–current) is presented in Note 38.

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expense is not offset in the statement of comprehensive income unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Bank.

Going concern

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on a going concern basis.

2.2 Significant accounting judgments, estimates and assumptions

In the process of applying the Bank's accounting policies, management has exercised judgment and estimates in determining the amounts recognised in the financial statements. The most significant uses of judgment and estimates are as follows:

Impairment losses on loans and advances

The Bank reviews its individually significant loans and advances at each statement of financial position date to assess whether an impairment loss should be recorded in the statement of comprehensive income. In particular, management judgment is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

2.2 Significant accounting judgments, estimates and assumptions (Contd.)

Loans and advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as levels of arrears, credit utilisation, loan to collateral ratios, etc.), and judgments to the effect of concentrations of risks and economic data.

The impairment loss on loans and advances is recorded under ‘Credit and other losses - net’ and disclosed in more detail in Notes 9 and 18.

Sale of mortgage loans sold to “MIK Holding” JSC (“MIK”)

The Bank has sold mortgage loan portfolios to MIK and its subsidiaries in exchange for bonds issued by MIK SPC and derecognized the loans as it is considered that the transactions meet the derecognition criteria as envisaged in IAS39:AG 39 on the basis that the Bank has transferred substantially all the risks and rewards, in conjunction with the recognition of the “Residual Mortgage Backed Securities (“RMBS”). Although there is a mandatory buy back by the Bank if the default rate of the mortgage loans purchased reaches 20%, any such buy back would be at fair value. Management judgment is required to determine that substantially all the risks and rewards have been transferred.

Deferred tax assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that taxable profit will be available against which can be utilised. Judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies (Note 24).

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions. The fair value of financial instruments as well as its fair hierarchy are described in more detail in Note 36.

Tax legislation

Mongolian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management’s interpretation of such legislation as applied to the transactions and activity of the Bank may be challenged by tax authorities.

2.2 Significant accounting judgments, estimates and assumptions (Contd.)

Tax legislation (Contd.)

Mongolian tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged by tax authorities. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for five calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Mongolian transfer pricing legislation provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of all controllable transactions, including those related to domestic transfer pricing. In case of deviation of transaction terms from market terms, the tax authorities have the right to adjust taxable items and to impose additional taxes, fines and interest penalties. Given the brief nature of the current Mongolian transfer pricing rules, the impact of any such challenge cannot be reliably estimated. However, it may be significant to the financial position and/or the overall operations of the entity.

Mongolian tax legislation does not provide definitive guidance in certain areas, specifically in areas such as VAT, withholding tax, corporate income tax, personal income tax and other areas. From time to time, the Bank adopts interpretations of such uncertain areas that reduce the overall tax rate of the Bank.

As noted above, such tax positions may come under heightened scrutiny as a result of recent developments in administrative and court practices. The impact of any challenge by the tax authorities cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the entity. Management performs regular re-assessment of tax risks and its position may change in the future as a result of the change in conditions that cannot be anticipated with sufficient certainty at present.

2.3 Application of new and amendments to International Financial Reporting Standards (IFRSs)

Amendments to IFRSs and new Interpretations that are mandatorily effective for the current year

In the current year, the Bank has applied a number of amendments to IFRSs issued by the International Accounting Standards Board ('IASB') that are mandatorily effective for an accounting periods that begins on or after 1 January 2016.

Effective Date	New Standards or amendments
1 January 2016	• Amendments to IFRS 11 *Accounting for Acquisitions of Interests in Joint Operations* • Amendments to lAS 16 and lAS 38 *Clarification of Acceptable Methods of Depreciation and Amortisation* • Amendments to IAS 1 *Disclosure Initiative* • Amendments to IAS 27 *Equity Method in Separate Financial Statements* • Amendments to IFRS 10, IFRS 12 and IAS 28 *Investment Entities: Applying the Consolidation Exception* • Annual Improvements to *IFRSs 2012-2014 Cycle – Various Standards*

The adoption of the above amendments to standards did not result in significant changes to the accounting policies and did not have any effect on the financial statements of the Bank.

2.3 Application of new and amendments to International Financial Reporting Standards (IFRSs)

Amendments to IFRSs and new Interpretations that are mandatorily effective for the current year (Contd.)

The Bank has not applied the following new and amendments to IFRSs that have been issued but are not yet effective.

The Standards' amendments and Interpretations that are issued, but not yet effective, up to the date of issuance of the Bank's financial statements are disclosed below. The Bank intends to adopt these standards, if applicable, when they become effective.

Effective Date	New Standards or amendments
1 January 2017	• Amendments to IAS 7 *Disclosure Initiative* • Amendments to IAS 12 *Recognition of Deferred tax assets for unrealised losses*
1 January 2018	• IFRS 9 *Financial Instruments* • IFRS 15 *Revenue from Contracts with Customer* • Amendments to IFRS 2 *Classification and Measurement of Share-based Payment Transactions* • IFRIC 22 *Foreign Currency Transactions and Advance Consideration* • Amendments to IAS 40 *Transfers of Investment Property* • Amendments to IFRS 4 *Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts* • Clarification to IFRS 15 *Revenue from Contracts with Customers*
1 January 2017 or 1 January 2018*	• Annual Improvements to IFRS standards 2014-2016 Cycle
1 January 2019	• IFRS 16 *Leases*
To be determined	• Amendments to IFRS 10 and IAS 28 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*

* The amendments to IFRS 1 and IAS 28 are effective for annual periods beginning on or after 1 January 2018, and IFRS 12 for annual periods beginning on or after 1 January 2017.

2.3 Application of new and amendments to International Financial Reporting Standards (IFRSs)

Amendments to IFRSs and new Interpretations that are mandatorily effective for the current year (Contd.)

None of the above new standards and amendments to Standards and interpretation is expected to have a significant effect on the financial statements of the Bank except the following set out below:

IFRS 9 Financial Instruments

Based on the Bank's financial instruments and risk management policies as at December 31, 2016, application of IFRS 9 in the future may have a material impact on the classification and measurement of the Bank's financial assets. The Bank's available-for-sale financial assets, including those currently stated at cost less impairment, will either be measured as fair value through profit or loss or be designated as FVTOCI. In addition, the expected credit loss model may result in early provision of credit losses which are not yet incurred in relation to the Bank's financial assets measured at amortized cost. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 9 until the Bank performs a detailed review.

IFRS 15 ***Revenue from Contracts with Customers***

IFRS 15, deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity’s contracts with customers. An entity recognises revenue when (or as) a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15. However, it is not practicable to provide a reasonable estimate of the effect of IFRS 15 until the Bank performs a detailed review.

2.4 Summary of significant accounting policies

Foreign currency translation

The financial statements of the Bank are presented in Mongolian Togrogs (MNT), which is the Bank's functional and presentation currency. Transactions in foreign currencies are initially recorded at the functional currency rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange at the statement of financial position date. All differences arising on non–trading activities are taken to 'Other operating income/(loss) - net' in the statement of comprehensive income. Non–monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non–monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Financial instruments – initial recognition and subsequent measurement

(i) Date of recognition

All financial assets and liabilities are initially recognised on the trade date, i.e., the date that the Bank becomes a party to the contractual provisions of the instrument. This includes "regular way trades": purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

(ii) Derivatives recorded at fair value through profit or loss

The Bank uses derivatives such as currency forwards and swaps to manage its exposure to market risks. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liabilities when their fair value is negative. Changes in the fair value of derivatives are included in 'Other operating income /(loss) - net'.

2.4 Summary of significant accounting policies (Contd.)

Financial instruments – initial recognition and subsequent measurement (Contd.)

(ii) Derivatives recorded at fair value through profit or loss (Contd.)

Derivatives embedded in other financial instruments are treated as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract, and the host contract is not itself held-for-trading or designated at fair value through profit or loss. The embedded derivatives separated from the host are carried at fair value in the trading portfolio with changes in fair value recognised in the statement of comprehensive income.

(iii) Financial assets or financial liabilities held-for-trading

Financial assets or financial liabilities held–for–trading are recorded in the statement of financial position at fair value. Changes in fair value are recognised in ‘Net trading loss'. Interest and dividend income or expense are recorded in ‘Net trading loss’ according to the terms of the contract, or when the right to the payment has been established.

Included in this classification are debt securities, equities and securities that have been acquired principally for the purpose of selling or repurchasing in the near term.

(iv) Financial assets and financial liabilities designed at fair value through profit or loss

Financial assets and financial liabilities classified in this category are those that have been designated by management on initial recognition. Management may only designate an instrument at fair value through profit or loss upon initial recognition when the following criteria are met, and designation is determined on an instrument by instrument basis:

- The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis.

- The assets and liabilities are part of a group of financial assets, financial liabilities or both which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.
- The financial instrument contains one or more embedded derivatives which significantly modify the cash flows that otherwise would be required by the contract.

2.4 Summary of significant accounting policies (Contd.)

Financial instruments – initial recognition and subsequent measurement (Contd.)

(iv) Financial assets and financial liabilities designed at fair value through profit or loss (Contd.)

Financial assets and financial liabilities at fair value through profit or loss are recorded in the statement of financial position at fair value. Changes in fair value are recorded in 'Other operating income'. Interest earned or incurred is accrued in 'Interest and similar income' or 'Interest similar expense', respectively, using the Effective interest rate (EIR), while dividend income is recorded in 'Other operating income/(loss) - net' when the right to the payment has been established.

The Bank has no financial assets or liabilities designated at fair value through profit or loss as at 31 December 2016 and 2015.

(v) Available-for-sale financial investments

Available-for-sale financial investments include equity and debt securities. Equity investments classified as available-for-sale financial investments are those which are neither classified as held-for-trading nor designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

The Bank has not designated any loans or receivables as available-for-sale financial investments. After initial measurement, available-for-sale financial investments are subsequently measured at fair value.

Unrealised gains and losses are recognised directly in equity (other comprehensive income) in the 'Available-for-sale reserve'. When the investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the income statement in 'Other operating income/(loss) - net'. Where the Bank holds more than one investment in the same security they are deemed to be disposed of on a first-in first-out basis. Interest earned whilst holding available-for-sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available-for-sale financial investments are recognised in the income statement as 'Other operating income/(loss) - net' when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the statement of comprehensive income and removed from the 'Available-for-sale reserve'.

2.4 Summary of significant accounting policies (Contd.)

Financial instruments – initial recognition and subsequent measurement (Contd.)

(vi) Held-to-maturity financial investments

Held-to-maturity financial investments are non-derivative financial assets with fixed or determinable payments and fixed maturities, which the Bank has the intention and ability to hold to maturity. After initial measurement, held-to-maturity financial investments are subsequently measured at amortised cost using the EIR, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR. The amortisation is included in 'Interest and similar income' in the comprehensive income statement. The losses arising from impairment of such investments are recognised in the statement of comprehensive income.

If the Bank were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available-for-sale. Furthermore, the Bank would be prohibited from classifying any financial asset as held-to-maturity financial investments during the following two years.

(vii) Loans and advances

This includes 'Due from banks' and 'Loans and advances to customers' which are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- Those that the Bank intends to sell immediately or in the near term and those that the Bank upon initial recognition designates as at fair value through profit or loss.
- Those that the Bank, upon initial recognition, designates as available-for-sale financial investments.
- Those for which the Bank may not recover substantially all of its initial investment, other than because of credit deterioration.

After initial measurement, amounts 'Due from banks' and 'Loans and advances to customers' are subsequently measured at amortised cost using the EIR, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortisation is included in 'Interest and similar income' in the income statement. The losses arising from impairment are recognised in the ‘credit and other losses - net’ in the statement of comprehensive income.

2.4 Summary of significant accounting policies (Contd.)

Financial instruments – initial recognition and subsequent measurement (Contd.)

(vii) Loans and advances (Contd.)

The Bank may enter into certain lending commitments where the loan, on drawdown, is expected to be classified as held-for-trading because the intent is to sell the loans in the short term. These commitments to lend are recorded as derivatives and measured at fair value through profit or loss.

Where the loan, on drawdown, is expected to be retained by the Bank, and not sold in the short term, the commitment is recorded only when the commitment is an onerous contract and it is likely to give rise to a loss (for example, due to a counterparty credit event).

(viii) Borrowed funds and subordinated loans

Borrowed funds and subordinated loans are contractual obligations to local and foreign financial institutions.

After initial measurement, borrowed funds and subordinated loans are subsequently measured at amortised cost using the EIR. The amortised cost of borrowed funds and subordinated loans is calculated using EIR by taking into account any transaction costs related to the transaction.

An analysis of the Bank's borrowed funds and subordinated loans is disclosed in Note 28 and Note 29, respectively.

(ix) Due to banks

This includes deposits from other banks and financial institutions in foreign currency and local currency accounts and time deposits placed by local and foreign commercial banks and BoM (Note 25).

After initial measurement, borrowings are subsequently measured at amortised cost using the EIR.

(x) Due to customers

This includes current, savings and time deposits from customers (Note 27).

After initial measurement, due to customers are subsequently measured at amortised cost using the EIR.

2.4 Summary of significant accounting policies (Contd.)

Financial instruments – initial recognition and subsequent measurement (Contd.)

(xi) Reclassification of financial assets

For a financial asset reclassified out of the 'Available-for-sale financial investments' category, any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the EIR. Any difference between the new amortised cost and the expected cash flows is also amortised over the remaining life of the asset using the EIR. If the asset is subsequently determined to be impaired then the amount recorded in equity is recycled to the statement of comprehensive income.

The Bank may reclassify a non-derivative trading asset out of the 'Held-for-trading' category and into the ‘Loans and receivables’ if it meets the definition of loans and receivables and the Bank has the intention and ability to hold the financial asset for the foreseeable future or until maturity. If a financial asset is reclassified, and if the Bank subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the EIR from the date of the change in estimate.

Reclassification is at the election of management, and is determined on an instrument by instrument basis. The Bank does not reclassify any financial instrument into the fair value through profit or loss category after initial recognition.

Derecognition of financial assets and financial liabilities

(i) Financial assets

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

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

2.4 Summary of significant accounting policies (Contd.)

Derecognition of financial assets and financial liabilities (Contd.)

(i) Financial assets (Contd.)

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank's continuing involvement in the asset. In that case, the Bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the bank could be required to repay.

The Bank derecognised certain mortgage loans in 2016 and 2015 (Note 18).

(ii) Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expired. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in statement of comprehensive income.

2.4 Summary of significant accounting policies (Contd.)

Repurchase and reverse repurchase agreements

Securities sold under agreements to repurchase at a specified future date are not derecognised from the statement of financial position as the Bank retains substantially all the risks and rewards of ownership. The corresponding cash received is recognised in the statement of financial position as an asset with a corresponding obligation to return it, including accrued interest, as a liability within ‘repurchase agreements', reflecting the transaction's economic substance as a loan to the Bank. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of agreement using the EIR.

Conversely, securities purchased under agreements to resell at a specified future date are not recognised in the statement of financial position. The consideration paid, including accrued interest, is recorded in the statement of financial position, within 'Reverse repurchase agreements', reflecting the transaction's economic substance as a loan by the Bank. The difference between the purchase and resale prices is recorded in 'Interest and similar income' and is accrued over the life of the agreement using the EIR.

If securities purchased under agreement to resell are subsequently sold to third parties, the obligation to return the securities is recorded as a short sale within 'Financial liabilities held-for-trading' and measured at fair value with any gains or losses included in 'Net trading income'.

Determination of fair value

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

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

2.4 Summary of significant accounting policies (Contd.)

Determination of fair value (Contd.)

Certain financial instruments are recorded at fair value using valuation techniques in which current market transactions or observable market data are not available. Their fair value is determined using a valuation model that has been tested against prices or inputs to actual market transactions and using the Bank's best estimate of the most appropriate model assumptions. Models are adjusted to reflect the spread for bid and ask prices to reflect costs to close out positions, credit and debit valuation adjustments, liquidity spread and limitations in the models. Also, profit or loss calculated when such financial instruments are first recorded ('Day 1' profit or loss) is deferred and recognised only when the inputs become observable or on derecognition of the instrument.

An analysis of fair values of financial instruments and further details as to how they are measured are provided in Note 36.

Impairment of financial assets

The Bank assesses at each statement of financial position date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

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

(i) Financial assets carried at amortised cost

For financial assets carried at amortised cost (such as amounts due from banks, loans and advances to customers as well as held-to-maturity investments), the Bank first assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

2.4 Summary of significant accounting policies (Contd.)

Impairment of financial assets (Contd.)

(i) Financial assets carried at amortised cost (Contd.)

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of comprehensive income. Interest income continues to be accrued 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 as part of 'Interest and similar income'. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the 'Credit and other losses' in the statement of comprehensive income.

The present value of the estimated future cash flows is discounted at the financial asset's original EIR. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current EIR. If the Bank has reclassified trading assets to loans and advances, the discount rate for measuring any impairment loss is the new EIR determined at the reclassification date. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank's internal credit grading system, that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

The Bank adopted the basic approach where the impairment allowances are computed on an average of historical loss experience of each risk grouping over the outstanding balance. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

2.4 Summary of significant accounting policies (Contd.)

Impairment of financial assets (Contd.)

(i) Financial assets carried at amortised cost (Contd.)

Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(ii) Available-for-sale financial investments

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

In the case of debt instruments classified as available-for-sale, the Bank assesses individually whether there is objective evidence of impairment based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of comprehensive income. 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 as part of 'Interest and similar income'. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognised in the statement of comprehensive income, the impairment loss is reversed through the statement of comprehensive income.

In the case of equity investments classified as available-for-sale, objective evidence would also 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 recognised in the statement of comprehensive income, is removed from equity and recognised in the statement of comprehensive income. Impairment losses on equity investments are not reversed through the income statement; increases in the fair value after impairment are recognised in other comprehensive income.

2.4 Summary of significant accounting policies (Contd.)

Impairment of financial assets (Contd.)

(iii) 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 any impairment is measured using the original EIR as calculated before the modification of terms and the loan is no longer considered past due. Management continually 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 EIR.

Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, therefore, the related assets and liabilities are presented gross in statement of financial position.

‘Day 1’ profit or loss

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

2.4 Summary of significant accounting policies (Contd.)

Leasing

The determination of whether an arrangement is a lease, or it contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Bank as a lessee

Leases which do not transfer to the Bank substantially all the risks and benefits incidental to ownership of the leased items are operating leases. Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight line basis over the lease term.

Bank as a lessor

Leases where the Bank does not transfer substantially all the risk and benefits of ownership of the asset are classified as operating leases. Initial direct costs incurred in negotiating operating leases are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income.

Amounts due from lessees under finance leases are recognised as receivables at the amount of the Bank's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect the constant periodic rate of return on the Bank's net investment outstanding in respect of the leases.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

(i) Interest and similar income and expenses

For all financial instruments measured at amortised cost, interest bearing financial assets classified as available-for-sale and financial instruments designated at fair value through profit or loss, interest income or expense is recorded using the EIR.

2.4 Summary of significant accounting policies (Contd.)

Recognition of income and expenses (Contd.)

(i) Interest and similar income and expenses (Contd.)

The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded as 'Other operating income/(loss) - net'. However, for a reclassified financial asset for which the Bank subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the EIR from the date of the change in estimate.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(ii) Fees and commission income

The Bank earns fees and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

Fee income earned from services that are provided over a certain period of time

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the EIR on the loan (ie. as interest income recorded under “Interest and similar income’). When it is unlikely that a loan will be drawn down, the loan commitment fees are recognised over the commitment period on a straight line basis.

2.4 Summary of significant accounting policies (Contd.)

Recognition of income and expenses (Contd.)

(ii) Fees and commission income (Contd.)

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses, are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

(iii) Net trading income

Results arising from trading activities include all gains and losses from changes in fair value and related interest income or expense and dividends for financial assets and financial liabilities 'held-for-trading'.

Cash and cash equivalents

Cash and cash equivalents as referred to in the cash flow statement comprises cash on hand, non-restricted current accounts with BoM and amounts due from banks on demand or with an original maturity of three months or less.

Property and equipment

All items of property and equipment are initially recorded at cost. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of any replaced part is derecognised. All other repairs and maintenance are charged to the statement of comprehensive income during the financial period in which they are incurred.

Subsequent to recognition, property and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses.

2.4 Summary of significant accounting policies (Contd.)

Property and equipment (Contd.)

Depreciation of other property and equipment is provided for on a straight-line basis to write off the cost of each asset to its residual value over the estimated useful life at the following annual rates:

Premises	40 years
Office furniture	10 years
Computer equipment and others	5 years
Vehicles	10 years
Leasehold improvements	Lower of lease term or useful lives

The residual values, useful life and depreciation method are reviewed at each financial year-end to ensure that the amount, method and period of depreciation are consistent with previous estimates and the expected pattern of consumption of the future economic benefits embodied in the items of property and equipment.

An item of property and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. The difference between the net disposal proceeds, if any and the net carrying amount is recognised in statement of comprehensive income.

Intangible assets

The Bank's other intangible assets include the value of computer software and licenses, software under development and patents and rights.

An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Bank.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

2.4 Summary of significant accounting policies (Contd.)

Intangible assets (Contd.)

The amortisation expense on intangible assets with finite lives is recognised in the statement of comprehensive income in the expense category consistent with the function of the intangible asset.

Amortisation is calculated using the straight–line method to write down the cost of intangible assets to their residual values over their estimated useful lives as follows:

Computer software (core banking software)	2 - 10 years
Patents and rights	3 – 60 years

Impairment of non–financial assets

The Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Bank estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash–generating unit's (CGU) fair value less costs to sell and its value in use. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre–tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded subsidiaries or other available fair value indicators.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Bank estimates the asset's or CGU's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of comprehensive income.

2.4 Summary of significant accounting policies (Contd.)

Financial guarantees

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the financial statements (within ‘Other liabilities’) at fair value, being the premium received. Subsequent to initial recognition, the Bank’s liability under each guarantee is measured at the higher of the amount initially recognised less, when appropriate, cumulative amortisation recognised in the statement of comprehensive income, and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is recorded in the statement of comprehensive income. The premium received is recognised in the statement of comprehensive income in ‘Fees and commission income’ on a straight line basis over the life of the guarantee.

Employee benefits

(i) Short term benefits

Wages, salaries and other salary related expenses are recognised as an expense in the year in which the associated services are rendered by employees of the Bank. Short term accumulating compensated absences such as paid annual leave are recognised when services are rendered by employees that increase their entitlement to future compensated absences, and short term non-accumulating compensated absences such as sick leave are recognised when absences occur.

(ii) Defined contribution plans

As required by law, companies in Mongolia make contributions to the government pension scheme, Social and Health Fund. Such contributions are recognised as an expense in profit or loss as incurred. The Bank also contributes to a defined contribution pension plan. The contribution paid is recorded as an expense under "Pension fund expense" in proportion to the services rendered by the employees to the Bank.

Provisions

Provisions are recognised when the Bank has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to any provision is presented in the statement of comprehensive income net of any reimbursement.

2.4 Summary of significant accounting policies (Contd.)

Taxes

(i) Current tax

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the statement of financial position date.

(ii) Deferred tax

Deferred tax is provided on temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognised for all taxable temporary differences, except:

- Where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

- Where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

- In respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each statement of financial position date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

2.4 Summary of significant accounting policies (Contd.)

Taxes (Contd.)

(ii) Deferred tax (Contd.)

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the statement of financial position date.

Current tax and deferred tax relating to items recognised directly in equity are also recognised in equity and not in the statement of comprehensive income.

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

Dividends on ordinary shares

Dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the Bank’s shareholder. Interim dividends are deducted from equity when they are declared and no longer at the discretion of the Bank.

Dividends for the year that are approved after the statement of financial position date are disclosed as an event after the statement of financial position date.

Equity reserves

The reserves recorded in equity on the Bank's statement of financial position include:

'Other reserves' which represent appropriations of retained earnings based on the decision of the Bank’s Board of Directors. The purpose of this account is not specified at present.

'Regulatory reserve' is set up in compliance with the BoM requirement and is distributable to the Shareholder of the Bank subject to consultation with BoM.

Government grants

Government grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate. When the grant relates to an asset, it is recognised as deferred income and released to income in equal amounts over the expected useful life of the related asset.

2.4 Summary of significant accounting policies (Contd.)

Government grants (Contd.)

When the Bank receives non-monetary grants, the asset and the grant are recorded gross at nominal amounts and released to the statement of comprehensive over the expected useful life and pattern of consumption of the benefit of the underlying asset by equal annual installments. When loans or similar assistance are provided by governments or related institutions with an interest rate below the current applicable market rate, the effect of this favourable interest is regarded as additional government grants.

Precious metals

Coins and cultural valuables are stated at the lower of cost and net realisable value.

Repossessed assets

The Bank's policy is to determine whether a repossessed asset is best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset category. Assets that are determined better to be sold are immediately transferred to 'Properties held for sale'. Repossessed assets where the Bank is yet to determine its use are retained under this account.

Repossessed assets are initially recognised at the lower of their fair values less costs to sell and the amortised cost of the related outstanding loans on the date of the repossession, and the related loans and advances together with the related impairment allowances are derecognised from the balance sheet. Subsequently, repossessed assets are measured at the lower of their cost and fair value less costs to sell and are included in 'Other assets'.

Properties held for sale

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

Segment reporting

The Bank's segment reporting is based on the following operating segments: retail banking, business banking, mortgage banking and treasury.

2.4 Summary of significant accounting policies (Contd.)

Earnings per share

Basic earnings per share is calculated by dividing the net profit for the year attributable to ordinary equity holders of the Bank by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share is calculated by dividing the net profit attributable to ordinary equity holders of the Bank (after adjusting for interest on the convertible preference shares and interest on the convertible bond, in each case net of tax, if any) by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

Transactions with related parties

For the purposes of these financial statements, a party is considered to be related to the Bank if:

- the party has the ability, directly or indirectly through one or more intermediaries, to control the Bank or exercise significant influence over the Bank in making financial and operating policy decisions, or has joint control over the Bank;
- the Bank and the party are subject to common control;
- the party is a member of key management personnel of the Bank or the Bank's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;
- the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or
- the party is a post-employment benefit plan which is for the benefit of employees of the Bank or of any entity that is a related party of the Bank.

Close family members of an individual are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the entity.

All material transactions and balances with the related parties are disclosed in the relevant notes to financial statements and the details are presented in Note 39.

3. SEGMENT INFORMATION

For management purposes, the Bank is organised into three operating segments based on products and services as follows:

Retail banking	-	Individual customer's current accounts, savings, credit and debit cards, micro business loans, consumer loans, financial leasing, eco loans, as well as payment and remittances.
Business banking	-	Commercial banking activities for SME and corporate customers including direct debit facilities, current accounts, deposits, overdrafts, loan, trade finance and other credit facilities as well as international remittances.
Treasury	-	Cash management, BoM securities, interbank loan and deposit, and financial instruments trading.

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss which in certain respects is measured differently from operating profit or loss in the financial statements. Income taxes are managed on a Bank wide basis and are not allocated to operating segments.

Interest income is reported net as management primarily relies on net interest revenue as a performance measure, not the gross income and expense.

Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Bank's total revenue in 2016 nor 2015.

GEOGRAPHICAL INFORMATION

All the Bank's activities were carried out in Mongolia during the years ended 31 December 2016 and 2015. Therefore, no geographical analysis is presented.

3. SEGMENT INFORMATION (Contd.)

The following table presents income and profit and certain asset and liability information related to the Bank's operating segments for 2016.

	Retail Banking	Business Banking	Treasury	Total
	2016 MNT'000	2016 MNT'000	2016 MNT'000	2016 MNT'000
Income				
Third party	58,206,810	51,402,792	810,291	110,419,893
Inter–segment	(1,061,053)	(3,943,651)	5,004,704	-
Total operating income	**57,145,757**	**47,459,141**	**5,814,995**	**110,419,893**
Credit and other losses	(12,150,074)	(18,991,857)	-	(31,141,931)
Net operating income	**44,995,683**	**28,467,284**	**5,814,995**	**79,277,962**
Results				
Net interest income/(expense)	52,130,865	50,318,369	(11,905,037)	90,544,197
Net fees and commission income	6,496,020	2,196,497	-	8,692,517
Net trading loss	-	-	(17,046,410)	(17,046,410)
Depreciation of property and equipment	(3,892,221)	(1,196,396)	(7,176)	(5,095,793)
Amortisation of intangible assets	(1,014,737)	(618,433)	-	(1,633,170)
Other operating expenses	(34,389,303)	(14,443,486)	(1,115,947)	(49,948,736)
Amortisation of deferred grants	-	604,327	-	604,327
Net other operating income	(420,075)	(1,112,074)	29,761,738	28,229,589
Credit and other losses	(12,150,074)	(18,991,857)	-	(31,141,931)
Inter segment	(1,061,053)	(3,943,651)	5,004,704	-
Segment profit for the year before tax	**5,699,422**	**12,813,296**	**4,691,872**	**23,204,590**
Income tax expense				(1,751,137)
Segment profit for the year after tax				**21,453,453**
Assets				
Capital expenditures:				
Property and equipment	5,611,106	1,688,282	-	7,299,388
Other intangible assets	1,614,784	1,327,980	-	2,942,764
	7,225,890	**3,016,262**	**-**	**10,242,152**
Total segment assets	**999,474,041**	**686,517,873**	**571,288,129**	**2,257,280,043**
Total segment liabilities	**909,376,202**	**616,014,924**	**552,854,346**	**2,078,245,472**

3. SEGMENT INFORMATION (Contd.)

The following table presents income and profit and certain asset and liability information related to the Bank's operating segments for 2015.

	Retail Banking 2015 MNT'000	Business Banking 2015 MNT'000	Treasury 2015 MNT'000	Total 2015 MNT'000
Income				
Third party	91,477,395	58,378,187	(49,107,894)	100,747,688
Inter–segment	(25,351,363)	(26,762,812)	52,114,175	-
Total operating income	**66,126,032**	**31,615,375**	**3,006,281**	**100,747,688**
Credit and other losses	(16,657,220)	(5,052,323)	-	(21,709,543)
Net operating income	**49,468,812**	**26,563,052**	**3,006,281**	**79,038,145**
Results				
Net interest income/(expense)	86,707,367	56,467,693	(10,837,272)	132,337,788
Net fees and commission income	4,367,350	2,654,069	-	7,021,419
Net trading loss	-	-	(27,599,340)	(27,599,340)
Depreciation of property and equipment	(3,790,702)	(1,055,923)	(5,918)	(4,852,543)
Amortisation of intangible assets	(1,148,736)	(557,016)	-	(1,705,752)
Other operating expenses	(35,647,393)	(11,384,502)	(1,078,518)	(48,110,413)
Amortisation of deferred grants	-	397,110	-	397,110
Net other operating income	402,679	(743,576)	(10,671,282)	(11,012,179)
Credit and other losses	(16,657,220)	(5,052,323)	-	(21,709,543)
Inter segment	(25,351,363)	(26,762,812)	52,114,175	-
Segment Profit before tax	**8,881,982**	**13,962,720**	**1,921,845**	**24,766,547**
Income tax expense				(2,282,097)
Segment Profit after tax				**22,484,450**
Assets				
Capital expenditures:				
Property and equipment	6,808,812	2,199,676	-	9,008,488
Other intangible assets	1,361,406	930,066	-	2,291,472
	8,170,218	**3,129,742**	**-**	**11,299,960**
Total segment assets	**903,174,694**	**578,398,679**	**454,571,250**	**1,936,144,623**
Total segment liabilities	**809,869,166**	**517,061,663**	**452,888,592**	**1,779,819,421**

4. INTEREST AND SIMILAR INCOME

	2016 MNT'000	2015 MNT'000
Loans and advances to customers	204,459,053	232,039,736
Financial investments – held-to-maturity	38,815,411	33,348,376
Cash and balances with BoM	9,231,171	8,892,544
Due from banks	5,626,504	843,650
Financial investments – Available-for-sale	2,554,171	1,975,069
Reverse repurchase agreements	220,607	477,356
	260,906,917	**277,576,731**

5. INTEREST AND SIMILAR EXPENSES

	2016 MNT'000	2015 MNT'000
Due to customers	98,008,831	82,477,531
Borrowed funds	60,469,954	51,560,312
Subordinated loans	9,123,940	7,986,925
Due to banks	1,961,469	2,561,074
Repurchase agreements	264,741	349,657
Other interest expenses	533,785	303,444
	170,362,720	**145,238,943**

6. FEES AND COMMISSION INCOME

	2016 MNT'000	2015 MNT'000
Fees and commission income		
Remittance and other service fees	4,737,233	3,685,650
Card related fees and commissions	3,615,952	3,000,635
Account service fees and commissions	1,351,474	1,081,908
Credit related fees and commissions	730,606	771,190
	10,435,265	**8,539,383**
Fees and commission expenses		
Card transaction charges	1,135,895	965,878
Bank service charges	606,853	552,086
	1,742,748	**1,517,964**
Net fees and commission income	**8,692,517**	**7,021,419**

7. NET TRADING LOSS

	2016 MNT'000	2015 MNT'000
Foreign exchange	(17,046,410)	(27,599,340)
	(17,046,410)	**(27,599,340)**

Foreign exchange income includes gains and losses from spot and forward contracts and other currency derivatives.

8. OTHER OPERATING INCOME/(LOSS) – NET

	2016 MNT'000	2015 MNT'000
Unrealised foreign exchange gain/ (loss)*	26,975,522	(12,375,283)
Rental income	162,491	103,430
Gain on disposal of properties held for sale and others (Note 19 and Note 20)	742,952	100,653
Loss on disposal of property and equipment	(439)	(44,075)
Dividend income	50,802	43,322
Others	298,261	1,159,774
	28,229,589	**(11,012,179)**

*Unrealised foreign exchange gain / (loss) include the Day 1 gain from long term swaps of MNT 38,558 million (2015: Nil) due to favourable terms offered by BoM.

9. CREDIT AND OTHER LOSSES - NET

	2016 MNT'000	2015 MNT'000
Loans and advances to customers (Note 18)		
Small and medium sized enterprises (SME) loans	11,662,754	8,653,368
Micro business loans	8,786,281	5,093,520
Mortgage loans	6,280,143	2,654,593
Consumer loans	(764,952)	2,414,369
Finance leases	(284,470)	521,174
Others	(1,328,246)	1,244,320
	24,351,510	**20,581,344**
Impairment loss on other assets (Note 19)	429,422	329,498
Impairment loss on financial investments	516,445	-
Impairment loss/(reversal) on foreclosed properties (Note 19)	5,953,192	(60,658)
Impairment (reversal)/loss on properties held for sale (Note 20)	(108,638)	859,359
	31,141,931	**21,709,543**

10. OPERATING EXPENSES

	2016 MNT'000	2015 MNT'000
Personnel expenses*	26,228,496	25,770,404
Depreciation of property and equipment (Note 21)	5,095,793	4,852,543
Rental of premises	4,632,374	5,074,000
Professional fees	4,030,659	2,839,131
Deposit insuranse expense	2,340,728	2,127,560
Armored guard and security	1,985,705	1,974,230
Advertising	1,678,018	2,384,168
Amortisation of intangible assets (Note 22)	1,633,170	1,705,752
Other operating expenses	1,439,245	1,309,615
Travelling expenses	1,207,075	662,856
Communications	1,201,729	1,226,774
Entertainment	1,151,529	874,936
Utilities	823,645	703,417
Stationary	753,921	849,402
Transportation	642,103	711,478
Repairs and maintenance	551,101	639,145
Membership and audit expenses	470,648	351,882
Insurance	470,597	357,183
Loan collection expenses	182,661	193,960
Property and equipment written-off	115,614	15,197
Donations	30,039	18,744
Penalty	10,913	23,961
Intangible asset written-off	1,936	2,370
	56,677,699	**54,668,708**

*** Personnel expenses**		
Salaries, wages and bonus	23,003,416	22,434,676
Contribution to social and health fund	2,522,671	2,563,383
Contribution to defined contribution pension plan	561,425	587,827
Staff training	140,984	184,518
	26,228,496	**25,770,404**

11. INCOME TAX EXPENSE

The components of income tax expense for the years ended 31 December 2016 and 2015 are:

	2016 MNT'000	2015 MNT'000
Current tax:		
Current income tax	84,162	3,372,783
Deferred tax		
Relating to origination and reversal of temporary differences (Note 24)	1,666,975	(1,090,686)
	1,751,137	**2,282,097**

The Bank provides for income taxes on the basis of its income for financial reporting purposes, adjusted for items which are not assessable or deductible for income tax purposes. The income tax rate for profits of the Bank is 10% (2015: 10%) for the first MNT 3 billion (2015: MNT 3 billion) of taxable income, and 25% (2015: 25%) on the excess of taxable income over MNT 3 billion (2015: MNT 3 billion). Interest income on government bonds is not subject to income tax.

A reconciliation of income tax expense applicable to profit before tax at the statutory income tax rate to income tax expense at the effective income tax rate of the Bank for the years ended 31 December 2016 and 2015 is as follows:

	2016 MNT'000	2015 MNT'000
Profit before taxation	23,204,590	24,766,547
Tax at statutory tax rate of 25% (2015: 25%)	5,801,148	6,191,637
Effect of income tax subject to lower tax rate	(450,000)	(450,000)
Effect of income not subject to tax	(6,909,571)	(6,335,089)
Effect of expenses not deductible for tax purposes	3,309,560	2,875,549
Tax expense for the year	**1,751,137**	**2,282,097**

The effective income tax rate for 2016 is 7.55% (2015: 9.21%).

12. EARNINGS PER SHARE

The following table shows the income and share data used in the basic and diluted earnings per share calculations:

	2016 MNT'000	2015 MNT'000
Profit for the year attributable to the equity holder of the Bank	21,453,453	22,484,450

	2016	2015
Weighted average number of ordinary shares for basic and diluted earnings per share	20,353,656	20,353,656

Earnings per share

	2016 MNT	2015 MNT
Equity holder of the Bank for the year:		
Basic earnings per share	1,054.03	1,104.69
Diluted earnings per share	1,054.03	1,104.69

There have been no transactions involving ordinary shares or potential ordinary shares between the reporting date and the date of the completion of these financial statements which would require the restatement of earnings per share.

13. CASH AND BALANCES WITH BANK OF MONGOLIA (BoM)

	2016 MNT'000	2015 MNT'000
Current accounts with BoM	280,863,167	150,955,629
Cash on hand	45,916,709	32,937,642
	326,779,876	**183,893,271**

Current accounts with BoM are maintained in accordance with BoM's regulations. The balances maintained with BoM are determined at not less than 12.0% (2015: 12.0 %) of customer deposits based on average balance of two (2) weeks. As at 31 December 2016, the average reserve required by BoM for that period of 2 weeks was MNT 111,685.65 million (2015: MNT 88,365.43 million) for local currency and MNT 30,407.64 million (2015: MNT 31,937.96 million) for foreign currency maintained in current accounts with BoM.

14. DUE FROM BANKS

	2016 MNT'000	2015 MNT'000
Placements with other banks and financial institutions	**158,627,068**	**99,107,298**

Due from banks represent local and foreign currency current accounts and deposits maintained with foreign and local financial institutions.

15. REVERSE REPURCHASE AGREEMENTS

	2016 MNT'000	2015 MNT'000
Reverse repurchase agreements	**-**	**9,981,555**

The Bank purchased securities with an agreement to sell back at specific future date. Reverse repurchase agreement all matured before 31 December 2016.

16. DERIVATIVE FINANCIAL INSTRUMENTS

The table below shows the fair value of derivative financial instruments recorded as assets or liabilities together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are indicative of neither the market risk nor the credit risk.

	Assets 2016 MNT'000	Liabilities 2016 MNT'000	Notional amount 2016 MNT'000
Derivatives held for trading			
Currency forwards	-	-	-
Currency swaps	125,019,231	928,603	559,080,805
	125,019,231	**928,603**	**559,080,805**

	2015 MNT'000	2015 MNT'000	2015 MNT'000
Derivatives held for trading			
Currency forwards	-	18,941	(18,941)
Currency swaps	2,307,271	6,650,488	372,963,120
	2,307,271	**6,669,429**	**372,944,179**

16. DERIVATIVE FINANCIAL INSTRUMENTS (Contd.)

At their inception, derivatives often involve only a mutual exchange of promises with little or no transfer of consideration. However, these instruments frequently involve a high degree sof leverage and are very volatile. A relatively small movement in the value of the asset, rate or index underlying a derivative contract may have a significant impact on the profit or loss of the Bank.

The Bank's exposure under derivative contracts is closely monitored as part of the overall management of its market risk (see also Note 40.4).

Forward contracts

Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

Swaps

Swaps are contractual agreements between two parties to exchange streams of payments over time, based on specified notional amounts, in relation to movements in a specified underlying index such as an interest rate, foreign currency rate or equity index.

In a currency swap, the Bank pays a specified amount in one currency and receives a specified amount in another currency. Currency swaps are mostly gross-settled.

Fair values

Disclosures concerning the fair value of derivatives are provided in Note 36.

17. FINANCIAL INVESTMENTS

	2016 MNT'000	2015 MNT'000
Available-for-sale:		
Junior RMBS, at fair value (a)	22,837,304	18,778,377
Unquoted fund, at fair value	3,124,459	-
	25,961,763	**18,778,377**
Equity investments		
Unquoted equities, at cost (c)	250,597	860,790
Quoted equities, at fair value (b)	1,904,972	-
	28,117,332	**19,639,167**
Held-to-maturity:		
Government treasury bills, at amortised cost (d)	254,901,094	222,924,880
BoM treasury bills, at amortised cost (d)	69,941,289	109,790,430
Government bonds, at amortised cost (e)	30,277,541	35,277,314
Government promissory notes, at amortised cost	-	5,549,610
	355,119,924	**373,542,234**

(a) The Bank sold mortgage loan portfolio to MIK and its subsidiaries in exchange for RMBS issued by MIK SPC. The sale of mortgage loan portfolios is part of a broader scheme administered by MIK whereby 9 of the largest banks in Mongolia, including the Bank, have sold parts of their mortgage loan portfolio under a Government program. The loans have been purchased by MIK-SPCs on a non-recourse basis. The risk profile of the issued bond by MIK is different from the risk profile of the derecognized loan by the Bank as the risk profile of the bond issued is backed by collective or commingled pool of loans from various banks.

The bonds are split between the senior tranche and the junior tranche ("Junior RMBS"); the senior tranche comprises 90% of the bond and carries an interest rate of 4.5%, while the junior tranche consists of 10% of the bond and carries an interest rate of 10.5%. The principal of the junior tranche has a minimum holding period of 3 years and will only be redeemed subsequent to the full redemption of the senior tranche and payments on the junior tranche are subordinate to payments on the senior tranche. The Senior tranche was subsequently sold to BoM in order to repay its borrowing (See Note 18).

(b) In late December 2015, MIK initiated a successful IPO placement of its shares on Mongolian Stock Exchange and the shares were listed on 4 January 2016. As at 31 December 2016, the Bank holds the number of 210,621 shares (1.20% of total shares), which are valued at the market price as at that date of MNT 9,090 per share. The amount of the investment increased by MNT 1,674 million due to revaluation.

17. FINANCIAL INVESTMENTS (Contd.)

(c) Unquoted equities represent investment made in unquoted companies. Investments in unquoted shares are recorded at cost as the fair value cannot be measured reliably. The variability in the range of reasonable fair value estimates derived from valuation techniques is expected to be significant. There is no market for these investments and the Bank does not intend to dispose of these investments in the foreseeable future.

(d) BoM treasury bills ("BoM bills") and Government treasury bills are interest bearing short-term bills issued at a discount.

(e) The Government bonds are interest bearing long term bills issued at a discount.

18. LOANS AND ADVANCES TO CUSTOMERS

	2016 MNT'000	2015 MNT'000
SME loans	570,094,457	566,126,191
Micro business loans	216,315,568	238,871,320
Mortgage loans	200,691,580	190,033,597
Consumer loans	124,541,795	100,934,278
Finance leases	10,393,299	18,967,740
Others	103,505,653	102,243,058
	1,225,542,352	**1,217,176,184**
Accrued interest receivables	22,505,769	22,284,398
Gross loans and advances	1,248,048,121	1,239,460,582
Less: Allowance for impairment losses	(90,846,538)	(68,171,276)
Net loans and advances to customers	**1,157,201,583**	**1,171,289,306**

Transferred financial assets that are derecognised in their entirety

The Bank sold the rights to 100% of the cash flows arising on a portfolio of fixed rate mortgage loans to a wholly owned special purpose company of MMC in exchange for RMBS. The Bank derecognised the loan portfolio and recognised the Senior RMBS and Junior RMBS received as financial assets. The Bank continues to service these loans and earns 2.5% servicer fee from MIK. The carrying amount of the transferred loan portfolio during the year was MNT 40,817 million (2015: MNT 117,086 million). The Senior and Junior RMBS received in exchange amounted to MNT 36,735 million (2015: MNT 105,378 million) and MNT 4,082 million (2015: MNT 11,708 million) respectively. The Senior tranche was subsequently sold to BoM in order to repay its borrowing (See Note 17).

18. LOANS AND ADVANCES TO CUSTOMERS (Contd.)

Impairment allowance for loans and advances to customers

A reconciliation of the allowance for impairment losses for loans and advances to customers by type is as follows:

	SME MNT'000	Mortgage MNT'000	Micro Business MNT'000	Consumer MNT'000	Finance Lease MNT'000	Others MNT'000	Total MNT'000
At 31 December 2016							
At 1 January 2016	49,139,509	4,183,266	7,701,065	4,105,963	929,210	2,112,263	68,171,276
Charge for the year (Note 9)	39,746,493	8,152,191	12,538,748	1,581,557	181,279	389,694	62,589,962
Recoveries (Note 9)	(28,083,739)	(1,872,048)	(3,752,467)	(2,346,509)	(465,749)	(1,717,940)	(38,238,452)
Amounts written off	(30,136)	(235,719)	(220,199)	(848,219)	(302,917)	(39,058)	(1,676,248)
At 31 December 2016	60,772,127	10,227,690	16,267,147	2,492,792	341,823	744,959	90,846,538
Individual impairment	24,721,040	195,548	-	-	-	-	24,916,588
Collective impairment	36,051,087	10,032,142	16,267,147	2,492,792	341,823	744,959	65,929,950
	60,772,127	**10,227,690**	**16,267,147**	**2,492,792**	**341,823**	**744,959**	**90,846,538**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**56,328,426**	**281,241**	**-**	**-**	**-**	**-**	**56,609,667**

18. LOANS AND ADVANCES TO CUSTOMERS (Contd.)

Impairment allowance for loans and advances to customers (contd.)

A reconciliation of the allowance for impairment losses for loans and advances to customers by type is as follows (Contd.):

	SME MNT'000	Mortgage MNT'000	Micro Business MNT'000	Consumer MNT'000	Finance Lease MNT'000	Others MNT'000	Total MNT'000
At 31 December 2015							
At 1 January 2015	40,614,312	1,544,721	2,751,157	1,836,263	505,572	869,223	48,121,248
Charge for the year (Note 9)	32,300,072	3,171,942	6,222,174	3,077,165	687,461	2,025,115	47,483,929
Recoveries (Note 9)	(23,646,704)	(517,349)	(1,128,654)	(662,796)	(166,287)	(780,795)	(26,902,585)
Amounts written off	(128,171)	(16,048)	(143,612)	(144,669)	(97,536)	(1,280)	(531,316)
At 31 December 2015	49,139,509	4,183,266	7,701,065	4,105,963	929,210	2,112,263	68,171,276
Individual impairment	19,313,763	-	-	-	-	-	19,313,763
Collective impairment	29,825,746	4,183,266	7,701,065	4,105,963	929,210	2,112,263	48,857,513
	49,139,509	**4,183,266**	**7,701,065**	**4,105,963**	**929,210**	**2,112,263**	**68,171,276**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**35,371,230**	**-**	**-**	**-**	**-**	**-**	**35,371,230**

18. LOANS AND ADVANCES TO CUSTOMERS (Contd.)

The fair value of the collateral that the Bank holds relating to loans individually determined to be impaired at 31 December 2016 amounts to MNT 72,772 million (2015: MNT 32,200 million). These values are estimated by management based on the latest available information. For a more detailed description, see 'Collateral and other credit enhancement' under Note 40.2.

19. OTHER ASSETS

	2016 MNT'000	2015 MNT'000
Other assets	5,239,934	2,647,339
Less: Allowance for impairment losses	(870,711)	(453,421)
	4,369,223	**2,193,918**
Foreclosed properties		
At beginning of the year	3,732,958	1,271,234
Add: Possession	52,366,027	12,529,732
Less: Sold during the year	(2,274,490)	(105,813)
Less: Transfer to investment in private fund	(752,796)	-
Less: Repayment by borrower	(63,471)	(4,020)
Less: Reclassification to properties held for sale and others	(26,793,947)	(9,958,175)
	26,214,281	**3,732,958**
Less: Allowances for impairment losses	(6,398,228)	(445,036)
At end of the year	**19,816,053**	**3,287,922**
Prepaid expenses	2,400,378	2,040,626
Consumables and other office supplies	1,290,981	1,348,919
Deposits	1,299,357	988,689
Precious metals	94,439	94,439
	5,085,155	**4,472,673**
Total other assets	**29,270,431**	**9,954,513**
Impairment allowance for other assets		
At beginning of the year	453,421	139,084
Charge for the year (Note 9)	429,422	329,498
Written off	(12,132)	(15,161)
At end of the year	**870,711**	**453,421**

19. OTHER ASSETS (Contd.)

	2016 MNT'000	2015 MNT'000
Impairment allowance for foreclosed properties		
At beginning of the year	445,036	505,694
Charge for the year (Note 9)	8,599,109	1,165,276
Reversal (Note 9)	(2,645,917)	(1,225,934)
At end of the year	**6,398,228**	**445,036**

Proceeds from the sale of foreclosed properties amounted to MNT 2,446 million (2015: MNT 130 million) and the gain amounted to MNT 48 million (2015: MNT 8 million).

20. PROPERTIES HELD FOR SALE

The Bank has sold or is in the process of selling certain properties and repossessed assets as follows:

	2016 MNT'000	2015 MNT'000
At beginning of the year	20,089,341	10,727,557
Add: Possession	26,767,847	10,388,520
Less: Sold during the year	(7,211,759)	(1,026,736)
Less: Transfer to investment in private fund	(2,910,138)	-
Less: Transfer to investment property (Note 23)	(4,976,156)	-
Less: Reclassification to foreclosed properties and others	(7,720,097)	-
	24,039,038	**20,089,341**
Less: Allowances for impairment losses	-	(859,359)
At end of the year	**24,039,038**	**19,229,982**

Proceeds from the sale of buildings during the year were MNT 7,935 million (2015: MNT 1,178 million). The gain from the sale of those buildings amounted to MNT 695 million (2015: MNT 93 million) and is recorded as part of 'Other operating income/(loss) - net' (Note 8).

	2016 MNT'000	2015 MNT'000
At beginning of the year	859,359	-
Charge (reversal) for the year (Note 9)	(108,638)	859,359
Impairment reclassified to PPE and others	(750,721)	-
At end of the year	-	**859,359**

21. PROPERTY AND EQUIPMENT

At 31 December 2016	Leasehold improvements	Premises	Vehicles	Office furniture	Computer equipment and others	Land held for future development	Construct-ion in progress	Total
	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000
At cost								
At 1 January 2016	**3,229,390**	**16,147,889**	**3,727,684**	**4,891,270**	**20,117,453**	**2,091,896**	**3,683,499**	**53,889,081**
Additions	941,381	1,969,536	-	33,932	629,605	-	3,724,934	7,299,388
Write-off	-	-	-	(133,114)	(1,041,112)	-	-	(1,174,226)
Disposals	-	-	(542,875)	(134,832)	(355,883)	-	-	(1,033,590)
Reclassification	-	1,086,328	440,000	1,103,085	3,949,047	-	(6,578,460)	-
Reclassification to intangible assets	-	-	-	-	-	-	(68,991)	(68,991)
At 31 December 2016	**4,170,771**	**19,203,753**	**3,624,809**	**5,760,341**	**23,299,110**	**2,091,896**	**760,982**	**58,911,662**
Accumulated depreciation								
At 1 January 2016	**1,564,016**	**2,358,297**	**1,462,526**	**1,631,837**	**12,075,505**	**-**	**-**	**19,092,181**
Charge for the year	643,115	446,244	377,238	493,635	3,135,561	-	-	5,095,793
Write-off	-	-	-	(93,385)	(965,227)	-	-	(1,058,612)
Disposals	-	-	(392,450)	(97,349)	(347,483)	-	-	(837,282)
At 31 December 2016	**2,207,131**	**2,804,541**	**1,447,314**	**1,934,738**	**13,898,356**	**-**	**-**	**22,292,080**
Net carrying amount at 31 December 2016	**1,963,640**	**16,399,212**	**2,177,495**	**3,825,603**	**9,400,754**	**2,091,896**	**760,982**	**36,619,582**

21. PROPERTY AND EQUIPMENT (CONTD.)

	Leasehold improvements	Premises	Vehicles	Office furniture	Computer equipment and others	Land held for future development	Construct-ion in progress	Total
At 31 December 2015	**MNT'000**	**MNT'000**	**MNT'000**	**MNT'000**	**MNT'000**	**MNT'000**	**MNT'000**	**MNT'000**
At cost								
At 1 January 2015	**2,128,104**	**14,873,625**	**3,788,964**	**3,744,024**	**19,279,823**	**2,210,792**	**1,090,535**	**47,115,867**
Additions	1,188,991	749,526	126,288	57,042	320,729	-	6,565,912	9,008,488
Write-off	-	-	-	(52,984)	(319,182)	-	-	(372,166)
Disposals	-	(397,410)	(383,507)	(244,072)	(744,584)	-	-	(1,769,573)
Reclassification	(87,705)	922,148	195,939	1,387,260	1,580,667	(118,896)	(3,972,948)	(93,535)
At 31 December 2015	**3,229,390**	**16,147,889**	**3,727,684**	**4,891,270**	**20,117,453**	**2,091,896**	**3,683,499**	**53,889,081**
Accumulated depreciation								
At 1 January 2015	**1,063,352**	**2,034,782**	**1,373,594**	**1,411,659**	**9,990,829**	**-**	**-**	**15,874,216**
Charge for the year	588,369	387,603	379,003	386,777	3,110,791	-	-	4,852,543
Write-off	-	-	-	(46,412)	(310,557)	-	-	(356,969)
Disposals	-	(44,262)	(290,071)	(115,669)	(715,558)	-	-	(1,165,560)
Reclassification	(87,705)	(19,826)	-	(4,518)	-	-	-	(112,049)
At 31 December 2015	**1,564,016**	**2,358,297**	**1,462,526**	**1,631,837**	**12,075,505**	**-**	**-**	**19,092,181**
Net carrying amount at 31 December 2015	**1,665,374**	**13,789,592**	**2,265,158**	**3,259,433**	**8,041,948**	**2,091,896**	**3,683,499**	**34,796,900**

22. INTANGIBLE ASSETS

	Patents and rights MNT'000	Computer software MNT'000	Software under development MNT'000	Total MNT'000
At 31 December 2016				
At cost				
At 1 January 2016	4,303,256	8,518,140	427,468	13,248,864
Additions*	73,999	184,968	2,683,797	2,942,764
Write-off	(93)	(19,418)	-	(19,511)
Reclassification	1,027,230	1,028,775	(2,060,805)	(4,800)
At 31 December 2016	5,404,392	9,712,465	1,050,460	16,167,317
Accumulated amortisation				
At 1 January 2016	1,461,800	2,796,039	-	4,257,839
Charge for the year	587,016	1,046,154	-	1,633,170
Write-off	(93)	(17,482)	-	(17,575)
Reclassification	(4,800)	-	-	(4,800)
At 31 December 2016	2,043,923	3,824,711	-	5,868,634
Net carrying amount	**3,360,469**	**5,887,754**	**1,050,460**	**10,298,683**
At 31 December 2015				
At cost				
At 1 January 2015	3,450,593	6,886,493	722,406	11,059,492
Additions	82,282	34,042	2,175,148	2,291,472
Write-off	(101,262)	(838)	-	(102,100)
Reclassification	871,643	1,598,443	(2,470,086)	-
At 31 December 2015	4,303,256	8,518,140	427,468	13,248,864
Accumulated amortisation				
At 1 January 2015	898,290	1,753,527	-	2,651,817
Charge for the year	662,709	1,043,043	-	1,705,752
Write-off	(99,199)	(531)	-	(99,730)
Reclassification	-	-	-	-
At 31 December 2015	1,461,800	2,796,039	-	4,257,839
Net carrying amount	**2,841,456**	**5,722,101**	**427,468**	**8,991,025**

* Addition includes transfer from property and equipment amounting to MNT 68,991 thousand.

23. INVESTMENT PROPERTY

	2016 MNT'000	2015 MNT'000
Beginning of the year	-	-
Transfer from properties held for sale (Note 20)	4,860,809	-
Disposals		-
End of the year	**4,860,809**	**-**

24. DEFERRED TAX ASSET

	2016 MNT'000	2015 MNT'000
At 1 January	3,412,101	2,321,415
Recognised in statement of profit or loss (note 11)	(1,666,975)	1,090,686
Recognised in other comprehensive income	(418,640)	-
At 31 December	**1,326,486**	**3,412,101**

	Deferred tax liability MNT'000	Deferred tax asset MNT'000	Net deferred asset/(liability) MNT'000
As at 31 December 2016			
Property and equipment			
-accelerated tax depreciation	731,210	-	(731,210)
Loans and advances to customers			
-deferral of loan origination fees	-	1,289,783	1,289,783
Derivative financial instruments			
-swap revaluation	2,035,636	-	(2,035,636)
Other liabilities	-	506,731	506,731
Available for sale reserve	418,640	-	(418,640)
Tax loss	-	2,715,458	2,715,458
	3,185,486	**4,511,972**	**1,326,486**
As at 31 December 2015			
Property and equipment			
-accelerated tax depreciation	489,954	-	(489,954)
Loans and advances to customers			
-deferral of loan origination fees	-	829,295	829,295
Derivative financial instruments			
-swap revaluation	-	3,024,209	3,024,209
Other liabilities	-	48,551	48,551
	489,954	**3,902,055**	**3,412,101**

24. DEFERRED TAX ASSET (Contd.)

	2016 MNT'000	2015 MNT'000
Unused tax losses for which no deferred tax assets have been recognised	**1,765,805**	**-**

The unrecognised tax credit will expire in 2018.

25. DUE TO BANKS

	2016 MNT'000	2015 MNT'000
Deposits from other banks and financial institutions	**750,413**	**20,660,868**

26. REPURCHASE AGREEMENTS

	2016 MNT'000	2015 MNT'000
Repurchase agreements	-	**100,299,411**

The Bank sold BoM bills with an agreement to repurchase them in the future. The repurchase agreements all matured before 31 December 2016.

27. DUE TO CUSTOMERS

	2016 MNT'000	2015 MNT'000
Government deposits		
- Current accounts	6,995,461	2,694,059
- Demand deposits	364,905	765,635
- Time deposits	557,022	7,177,258
Private sector deposits		
- Current accounts	96,454,589	94,487,744
- Demand deposits	31,006,392	17,623,668
- Time deposits	65,069,217	140,300,903
Individual deposits		
- Current accounts	17,702,303	12,292,747
- Demand deposits	128,992,658	89,394,012
- Time deposits	638,361,140	521,519,622
	985,503,687	**886,255,648**

Included in 'Due to customers' were deposits of MNT 3,189 million (2015: MNT 5,530 million) held as collateral for irrevocable commitments under financial guarantees provided by the Bank as at 31 December 2016 and 2015 respectively.

28. BORROWED FUNDS

	2016 MNT'000	2015 MNT'000
Borrowed funds from foreign financial institutions		
International Finance Corporation ("IFC")	111,821,876	-
Cargill Financial Services International	94,051,794	-
Asian Development Bank ("ADB")	53,178,454	59,520,898
European Bank for Reconstruction and Development ("EBRD")	39,626,976	55,253,859
Microfinance Enhancement Facility S.A SICAV -SIF (Cyrano pool) ("MEF")	38,228,861	30,464,029
Global Climate Partnership Fund S.A., SICAV-SIF ("GCPF")	37,291,187	29,839,658
Women Entrepreneurs Debt Fund LP	36,986,149	-
Netherlands Development Finance Company ("FMO")	30,114,659	36,544,881
Bank Im Bistum Essen EG ("BiB")	28,854,174	17,067,608
BlueOrchard Microfinance Fund	24,976,985	-
SwedFund	24,620,719	-
Finnish Fund For Industrial Cooperation Ltd	24,611,248	-
International Investment Bank ("IIB")	24,590,753	-
Development Bank of Austria ("OeEB")	21,836,752	26,063,562
Societe De Promotion Et De Participation Pour La Cooperation Economique S.A ("PROPARCO")	21,510,166	25,799,876
SIFEM AG	19,740,005	-
Cargill TSF Asia Pte Ltd	17,349,815	-
Guevoura Fund	14,213,854	11,368,153
Calvert Social Investment Foundation, Inc	12,787,782	10,237,833
Microfinance Initiative for Asia ("MIFA")	12,489,963	-
Developing World Markets ("DWM")	12,485,988	-
Deutsche Investitions- Und Entwicklungsgesellschaft MBH ("DEG")	12,462,109	19,932,028
VDK Spaarbank	10,213,910	8,173,103
CaixaBank	10,001,695	-
Triodos Sicav II - Triodos Microfinance Fund	6,482,033	12,436,055
Triodos Custody B.V.- Triodos Fair Share Fund	6,482,033	12,435,522
Kreditanstalt fuer Wiederanfbau ("KfW")	4,784,377	3,711,661
KIVA	440,562	463,508
OPEC Fund for International Development ("OFID")	-	39,751,395
Micro, Small and Medium Enterprises Bonds SA	-	19,539,246
Credit Suisse Microfinance Fund Management Company/ responsAbility Global Microfinance Fund ("CSMFMC/ RGMF")	-	10,100,629
KCD Mikrofinanzfonds	-	6,051,811

28. BORROWED FUNDS (Contd.)

	2016 MNT'000	2015 MNT'000
Borrowed funds from foreign financial institutions		
Oikocredit, Ecumenical Development Co-operative Society U.A ("Oikocredit")	-	5,728,920
responsAbility SICAV(Lux) MikroFinanz-Fonds	-	4,040,252
responsAbility SICAV (Lux) Microfinance Leaders Fund	-	2,020,126
Dual Return Fund SICAV	-	1,995
Capital Gestion-Microfinance	-	1,552
Total borrowed funds from foreign financial institutions	**752,234,879**	**446,548,160**
Borrowed funds from government organisations		
SME Development Fund	68,504,433	83,936,386
Bank of Mongolia	1,252,105	86,449,141
Government of Mongolia	87,994,529	-
Ministry of Finance/ Japan Bank for International Cooperation	16,443,985	14,823,751
Ministry of Finance	4,109,480	7,161,213
Asian Development Bank	1,259,720	1,485,663
Educational Loan Fund	1,000,000	-
Rural Poverty Reduction Program	2,002,073	1,459,840
UB City and SME development fund	1,279,559	1,285,212
Employment Generation Support Fund	13,232	24,998
Micro Finance Development Fund	-	379
	183,859,116	**196,626,583**
Borrowed funds from other company		
Oyu Tolgoi LLC	-	45,476
Total borrowed funds	**936,093,995**	**643,220,219**

28. BORROWED FUNDS (Contd.)

All borrowed funds from government organisations are related to the Government of Mongolia.

The Bank has not prepaid any debt during the year ended 31 December 2016 (As at 31 December 2015: Nil). The Bank did not have any defaults on principal or interest payments with regard to all liabilities as at 31 December 2016. (As at 31 December 2015: Nil).

Most of the borrowing agreements require compliance with certain debt covenants, which can be grouped in the following categories:

- capital related ratios (such as risk weighted capital adequacy ratio, solvency ratio, ratio between tier 1 capital and total capital)
- financial risks related ratios (such as maturity mismatches, currency mismatches, aggregate foreign currency open position, single currency foreign exchange risk ratio, negative liquidity gap ratio, aggregate interest rate risk ratio and interest rate risk ratio);
- credit related ratios (such as portfolio at risk, open loan exposure ratio, write off ratio, single largest borrowers to the equity ratio, related party lending ratio and aggregate large exposures ratio);
- other ratios (deposits to loans ratio, interest coverage ratio, shareholding in single entity, fixed assets to total assets, fixed assets plus equity investments ratio, overhead ratio etc.).

In case of non-compliance to covenants, i.e., in the event of default and such event of default is subsisting, the borrowing becomes immediately payable on demand. For this reason, quarterly monitoring of debt covenants is carried out by relevant departments and officers (Finance and Accounting Division, including Chief Finance Officer, Integrated Risk Management Division, Treasury, Credit Administration Division etc.). In case of anticipated or noted non-compliance with certain covenants, appropriate action is taken by management, such as requesting waiver on breached covenants or negotiating new agreement to change the limits (ratios).

As of 31 December 2016, the Bank has complied with debt covenants on all borrowings.

	2016 MNT'000	2015 MNT'000
Borrowed funds from financial institution and others		
Maturity less than 1 year	462,974,238	309,253,369
Maturity 1-5 years	462,325,188	317,251,128
Maturity more than 5 years	10,794,569	16,715,722
Total borrowed funds	**936,093,995**	**643,220,219**

29. SUBORDINATED LOANS

	2016 MNT'000	2015 MNT'000
International Finance Corporation	112,853,126	90,050,609
KfW, Frankfurt am Main	10,589,959	8,151,183
Incofin Impulse Microfinance Investment Fund	-	6,014,950
	123,443,085	**104,216,742**

Subordinated convertible loan from International Finance Corporation (IFC)

(i) On 19 August 2010, the Bank received subordinated convertible debt of USD 5,000,000 from IFC, which is due for repayment on 15 December 2018. According to the agreement, conversion option can be exercised only if the existing shareholders of the Bank's parent Company TenGer Financial Group LLC make a decision on the increase in share capital of TenGer Financial Group LLC and some of these shareholders decide not to use their pre-emptive rights. In such situation, IFC is entitled to purchase remaining shares of TenGer at the same price offered to shareholders. IFC is entitled to make decision on whether shares are to be purchased for cash consideration or through requesting the Bank to repay the outstanding balance of subordinated debt.

The new shares to be acquired by IFC under the conversion option shall be common shares with full voting powers, shall rank pari passu to all other shares of TenGer Financial Group LLC and shall not exceed 20% of the aggregate share capital of TenGer Financial Group LLC.

The Bank cannot repay the subordinated convertible loan prior to the maturity date, except in the case of revocation of its banking license, insolvency, liquidation or restructuring and with the prior approval of BoM.

The loan carries a variable interest rate of 6-month LIBOR USD plus a margin of 6.5 % per annum. The EIR as of 31 December 2016 is 7.799% (2015: 7.247%) per annum. The debt ranks subordinated to all other senior creditors in case of liquidation.

(ii) In June 2012, the Bank entered into a Subordinated Loan Agreement in the amount of USD 40,000,000 with IFC Capitalization Fund. The Bank obtained the loan in 2 tranches: USD 9,000,000 in December 2012 at a fixed rate of 8.955% per annum, USD 31,000,000 in 2014 at a variable interest rate of 6-month LIBOR USD plus a margin of 7.40%. The EIR for USD 31,000,000 as of 31 December 2016 is 8.663% (2015: 7.925%). The loan is due for repayment in December 2020.

29. SUBORDINATED LOANS (Contd.)

Subordinated convertible loans from KfW, Frankfurt am Main ("KfW")

The Bank received USD 2,747,230 equivalent of EUR 1,800,000 under a 10-year subordinated convertible loan from KfW. The subordinated convertible loan has a maximum interest rate to be capped at 9% per annum. The EIR at the reporting date is 6.750% (2015: 6.175%) per annum.

The subordinated convertible loan can be fully repaid by cash on 20 July 2017 or it can be converted into equity shares of the Bank's parent company TenGer Financial Group LLC. A conversion option can be exercised only if TenGer Financial Group LLC's shareholders approve issue of additional share capital and some of the existing shareholders of TenGer Financial Group LLC decide not to use their pre-emptive rights. In such case, TenGer Financial Group LLC has the obligation to offer the remaining shares to KfW at the same price as to the existing shareholders. The price of new shares to be issued shall be fixed by the Shareholders Meeting of TenGer Financial Group LLC that authorises the capital increase. In such circumstances, KfW can exercise conversion option either through purchase of shares for cash consideration or through requesting the Bank to repay the outstanding balance of subordinated debt, which would enable KfW to use returned funds to purchase shares of TenGer Financial Group LLC. The amount of consideration to be paid by KfW for acquisition of shares of TenGer Financial Group LLC is the same under both options.

The new shares to be acquired by KfW under the conversion option shall be common shares with full voting powers, shall rank pari passu to all other shares of TenGer Financial Group LLC and shall not exceed 20% of the aggregate shall capital of TenGer Financial Group LLC.

The Bank cannot repay the subordinated convertible loan prior to the maturity date, except in the case of revocation of its banking license, its insolvency, liquidation or restructuring and with the prior approval of BoM. The debt ranks after all other creditors in case of liquidation.

Subordinated loan from Incofin Impulse Microfinance Investment Fund

The subordinated loan was repaid by cash in full amount on the 84th month after the first disbursement date, which was December 2016. The loan bears interest at a rate of 9.25% (2015: 9.25%) per annum.

30. DEFERRED GRANTS

	2016 MNT'000	2015 MNT'000
Micro Energy Credit Corporation (“MEC”)	904,987	870,966
Clean Air Fund	210,402	359,880
Foundation EKO	66,898	145,628
The Small Enterprise Education and Promotion Network (“SEEP”)	89,362	71,646
Women’s World Banking (“WWB”)	4,287	3,437
Consultative Group to Assist the Poorest (“CGAP”)	3,966	3,180
International Finance Corporation ("IFC")	-	-
	1,279,902	**1,454,737**

Movements in deferred grants are presented as follows:

	2016 MNT'000	2015 MNT'000
Balance at beginning of year	1,454,737	1,622,531
Received during the year	429,492	229,316
Amortisation recognised in statement of comprehensive income	(604,327)	(397,110)
Balance at end of year	**1,279,902**	**1,454,737**

31. OTHER LIABILITIES

	2016 MNT'000	2015 MNT'000
Payables	26,873,704	15,522,127
Delay on clearing settlement	3,369,811	734,473
Dividends payable (Note 34)	-	39
	30,243,515	**16,256,639**

32. ORDINARY SHARES

	Number of shares of MNT 2,719.06 each 2016	Number of shares of MNT 2,719.06 each 2015	Amount 2016 MNT'000	Amount 2015 MNT'000
At 1 January and 31 December	20,353,656	20,353,656	55,342,753	55,342,753

As at 31 December 2016 the Bank has 20,353,656 issued shares (2015: 20,353,656) at a par value of MNT 2,719.06 (2015: MNT 2,719.06).

The Bank has one class of shares and each share carries one voting right. The dividend proposed by the board of directors is subject to approval by the shareholder in the annual general meeting, except in the case of an interim dividend. In the event of liquidation, the equity shareholder is eligible to receive the remaining assets of the Bank after distribution of all preferential amounts.

33. OTHER RESERVES

There is no movement in other reserves during the year. At the date of this report, no policy is formalised by the Board as to the purpose of these reserves.

34. DIVIDENDS

	2016 MNT'000	2015 MNT'000
Dividends payable at 1 January	39	39
Dividends declared during the year	-	-
Dividends paid during the year	(39)	-
Dividends payable at 31 December (Note 31)	**-**	**39**

35. CASH AND CASH EQUIVALENTS

		2016 MNT'000	2015 MNT'000
Cash and balances with BoM	13	326,779,876	183,893,271
Due from banks	14	158,627,068	99,107,298
BoM treasury bills	17	69,941,289	109,790,430
Government treasury bills	17	254,901,094	222,924,880
		810,249,327	**615,715,879**
Less: Minimum reserve with BoM not available to finance the Bank's day to day operations (Note 13)		(142,093,290)	(120,303,383)
Less: Placement with other banks with original maturities of more than three months		(50,368,989)	(60,629,517)
Less: BoM Bills with original maturities of more than 3 months		-	-
Less: Government treasury bills with original maturities of more than 3 months		(170,445,380)	(178,936,214)
Total cash and cash equivalents		**447,341,668**	**255,846,765**

NON CASH TRANSACTIONS

During the year, the Bank sold 8% mortgage loans with a carrying amount of MNT 40,817 million (2015: MNT 117,086 million) to MIK for which it received RMBS amounting to MNT 36,735 million (2015: MNT 105,378 million) senior tranche and MNT 4,082 million (2015: MNT 11,708 million) junior tranche (see also note 18).

During the year the Bank repaid 4% funding due to BoM by selling the senior tranche RMBS notes amounting to MNT 36,735 million (2015: MNT 105,378 million) (see also note 17).

36. FAIR VALUE OF FINANCIAL INSTRUMENTS

Determination of fair value and fair value hierarchy

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

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

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

	Level 1 MNT'000	Level 2 MNT'000	Level 3 MNT'000	Total MNT'000
At 31 December 2016				
Financial assets				
Derivative financial instruments				
Currency swaps	-	125,019,231	-	125,019,231
Forward foreign exchange contracts	-	-	-	-
	-	**125,019,231**	**-**	**125,019,231**
Financial investments available-for-sale				
Junior RMBS, at the fair value	-		22,837,304	22,837,304
Unquoted fund, at the fair value			3,124,459	3,124,459
Quoted equities	1,904,972	-	-	1,904,972
	1,904,972	**-**	**25,961,763**	**27,866,735**
Financial liabilities				
Derivative financial instruments				
Currency swaps	-	928,603	-	928,603
Forward foreign exchange contracts	-	-	-	-
	-	**928,603**	**-**	**928,603**
At 31 December 2015				
Financial assets				
Currency swaps	-	2,307,271	-	2,307,271
Forward foreign exchange contracts	-	-	-	-
	-	**2,307,271**	**-**	**2,307,271**
Financial investments available-for-sale				
Junior RMBS, at the fair value	-	-	18,778,377	18,778,377
	-	**-**	**18,778,377**	**18,778,377**
Financial liabilities				
Currency swaps	-	6,650,488	-	6,650,488
Forward foreign exchange contracts	-	18,941	-	18,941
	-	**6,669,429**	**-**	**6,669,429**

36. FAIR VALUE OF FINANCIAL INSTRUMENTS (Contd.)

Financial assets and liabilities which are not measured at fair value but whose fair values are disclosed in the fair value table

The fair value of these financial assets and liabilities are categorised under level 2 where the Bank determined the fair value based on valuation technique (eg. discounted cash flow model) using market observable inputs.

Transfers between level 1 and 2

There were no transfers between level 1 to level 2 of the fair value hierarchy for the financial assets and liabilities which are recorded at fair value.

Fair value of financial assets and liabilities not carried at fair value

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements:

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or having short term maturity (less than one year), it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits, time deposits and variable rate financial instruments.

36. FAIR VALUE OF FINANCIAL INSTRUMENTS (Contd.)

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates offered for similar financial instruments available in Mongolia.

Set out below is a comparison, by class, of the carrying amounts and fair values of the Bank's financial instruments that are not carried at fair value in the financial statements. This table does not include the fair values of non-financial assets and non-financial liabilities.

As at 31 December 2016	Note	Carrying amount MNT'000	Fair value MNT'000
Financial assets			
Cash and balances with BoM	13	326,779,876	326,779,876
Due from banks	14	158,627,068	158,627,068
Reverse repurchase agreements	15	-	-
Financial investments - held-to-maturity	17	355,119,924	355,119,924
Loans and advances to customers	18	1,157,201,583	1,154,925,751
Other assets	19	5,462,032	5,462,032
		2,003,190,483	**2,000,914,651**
Financial liabilities			
Due to banks	25	750,413	750,413
Repurchase agreements	26	-	-
Due to customers	27	985,503,687	985,503,687
Borrowed funds	28	936,093,995	935,815,861
Subordinated loans	29	123,443,085	124,996,747
Other liabilities	31	22,132,908	22,132,908
		2,067,924,088	**2,069,199,616**

36. FAIR VALUE OF FINANCIAL INSTRUMENTS (Contd.)

As at 31 December 2015	Note	Carrying amount MNT'000	Fair value MNT'000
Financial assets			
Cash and balances with BoM	13	183,893,271	183,893,271
Due from banks	14	99,107,298	99,107,298
Reverse repurchase agreements	15	9,981,555	9,981,555
Financial investments - held-to-maturity	17	373,542,234	373,542,234
Loans and advances to customers	18	1,171,289,306	1,177,931,328
Other assets	19	3,105,331	3,105,331
		1,840,918,995	**1,847,561,017**
Financial liabilities			
Due to banks	25	20,660,868	20,660,868
Repurchase agreements	26	100,299,411	100,299,411
Due to customers	27	886,255,648	886,255,648
Borrowed funds	28	643,220,219	645,137,245
Subordinated loans	29	104,216,742	106,721,907
Other liabilities	31	8,795,536	8,795,536
		1,763,448,424	**1,767,870,615**

37 . CONTINGENT LIABILITIES AND COMMITMENTS

To meet the financial needs of customers, the Bank enters into various irrevocable commitments and contingent liabilities. Even though these obligations may not be recognised on the statement of financial position, they do contain credit risk and are therefore part of the overall risk of the Bank.

	2016 MNT'000	2015 MNT'000
Contingent liabilities		
Letters of credit	18,252,843	3,304,052
Financial guarantees	13,208,125	16,238,682
Performance and tender guarantees	9,726,851	8,150,455
	41,187,819	27,693,189
Commitments		
Undrawn commitments to lend	34,226,912	25,767,574
Total	**75,414,731**	**53,460,763**

37. CONTINGENT LIABILITIES AND COMMITMENTS (Contd.)

Contingent liabilities

Letters of credit and guarantees (including standby letters of credit) commit the Bank to make payments on behalf of customers in the event of a specific act, generally related to the import or export of goods. Guarantees and standby letters of credit carry the same risk as loans even though they are of a contingent nature. No material losses are anticipated as a result of these transactions.

Undrawn commitments to lend

Commitments to extend credit represent contractual commitments to make loans and revolving credits. Commitments have fixed expiry dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements.

The potential credit loss is less than the total unused commitments since commitments to extend credit are contingent upon customers maintaining specific standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

Other commitments

	2016 MNT'000	2015 MNT'000
Approved and contracted for:		
Property and equipment	956,317	1,507,432
Intangible assets	917,354	115,567
Consumables and other inventories	12,346	26,849
Consulting services	2,250	151,694
	1,888,267	**1,801,542**

Operating lease commitments - Bank as lessee

The Bank as lessee has entered into operating leases of various buildings under cancellable operating lease agreements. The Bank is required to give a month's notice for the termination of those agreements. The leases have no renewal option, purchase option or escalation clauses included in the agreements. There are no restrictions placed upon the Bank by entering these leases.

37. CONTINGENT LIABILITIES AND COMMITMENTS (Contd.)

Operating lease commitments – Bank as lessor

The Bank acts as lessor of various buildings under cancellable operating lease agreements. The lessee is required to give a month's notice for the termination of those agreements. The leases have no renewal option, purchase option or escalation clauses included in the agreements. There are no restrictions placed upon the lessee by entering into these leases.

Legal claims

Litigation is a common occurrence in the Banking industry due to the nature of the business. The Bank has an established protocol for dealing with such legal claims. Once professional advice has been obtained and the amount of damages reasonably estimated, the Bank makes adjustments to account for any adverse effects which the claim may have on its financial standing.

38. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled. See Note 40.3 Liquidity risk and funding management for the Banks contractual undiscounted repayment obligations.

At 31 December 2016	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
Financial assets			
Cash and balances with BoM	326,779,876	-	326,779,876
Due from banks	158,627,068	-	158,627,068
Derivative financial instruments	32,012,473	93,006,758	125,019,231
Financial investments -			
- held-for-trading	-	-	-
- available-for-sale	-	28,117,332	28,117,332
- held-to-maturity	355,117,924	2,000	355,119,924
Loans and advances to customers	426,090,378	731,111,205	1,157,201,583
Other assets	4,613,391	848,641	5,462,032
	1,303,241,110	**853,085,936**	**2,156,327,046**
Non financial assets			
Property and equipment	-	36,619,582	36,619,582
Intangible assets	100,125	10,198,558	10,298,683
Investment property	-	4,860,809	4,860,809
Other assets	23,713,960	94,439	23,808,399
Properties held for sale	24,039,038	-	24,039,038
Deferred tax assets	-	1,326,486	1,326,486
	47,853,123	**53,099,874**	**100,952,997**
Total	**1,351,094,233**	**906,185,810**	**2,257,280,043**

38. MATURITY ANALYSIS OF ASSETS AND LIABILITIES (Contd.)

At 31 December 2016	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
Financial liabilities			
Due to banks	750,413	-	750,413
Repurchase agreements	-	-	-
Due to customers	736,778,366	248,725,321	985,503,687
Derivative financial instruments	928,603	-	928,603
Borrowed funds	462,974,238	473,119,757	936,093,995
Subordinated loans	10,589,959	112,853,126	123,443,085
Other liabilities	5,525,528	16,607,380	22,132,908
	1,217,547,107	**851,305,584**	**2,068,852,691**
Non financial liabilities			
Deferred grants	1,279,902	-	1,279,902
Other liabilities	5,048,427	3,062,180	8,110,607
Income tax payable	2,272	-	2,272
	6,330,601	**3,062,180**	**9,392,781**
Total	**1,223,877,708**	**854,367,764**	**2,078,245,472**
Net Position	**127,216,525**	**51,818,046**	**179,034,571**

At 31 December 2015	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
Financial assets			
Cash and balances with BoM	183,893,271	-	183,893,271
Due from banks	99,107,298	-	99,107,298
Reverse repurchase agreements	9,981,555	-	9,981,555
Derivative financial instruments	285,647	2,021,624	2,307,271
Financial investments -			
- held-for-trading	-	-	-
- available-for-sale	1,475,777	18,163,390	19,639,167
- held-to-maturity	343,299,311	30,242,923	373,542,234
Loans and advances to customers	518,996,394	652,292,912	1,171,289,306
Other assets	2,554,477	550,854	3,105,331
	1,159,593,730	**703,271,703**	**1,862,865,433**

38. MATURITY ANALYSIS OF ASSETS AND LIABILITIES (Contd.)

At 31 December 2015	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
Non financial assets			
Property and equipment	-	34,796,900	34,796,900
Intangible assets	39,575	8,951,450	8,991,025
Other assets	6,754,743	94,439	6,849,182
Properties held for sale	19,229,982	-	19,229,982
Deferred tax assets	-	3,412,101	3,412,101
	26,024,300	**47,254,890**	**73,279,190**
Total	**1,185,618,030**	**750,526,593**	**1,936,144,623**

At 31 December 2015	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
Financial liabilities			
Due to banks	20,660,868	-	20,660,868
Repurchase agreements	100,299,411	-	100,299,411
Due to customers	669,060,347	217,195,301	886,255,648
Derivative financial instruments	5,216,110	1,453,319	6,669,429
Borrowed funds	309,253,369	333,966,850	643,220,219
Subordinated loans	6,014,950	98,201,792	104,216,742
Other liabilities	3,498,847	5,296,689	8,795,536
	1,114,003,902	**656,113,951**	**1,770,117,853**
Non financial liabilities			
Deferred grants	1,454,737	-	1,454,737
Other liabilities	2,786,759	4,674,344	7,461,103
Income tax payable	785,728	-	785,728
	5,027,224	**4,674,344**	**9,701,568**
Total	**1,119,031,126**	**660,788,295**	**1,779,819,421**
Net Position	**66,586,904**	**89,738,298**	**156,325,202**

39. RELATED PARTY DISCLOSURES

The Bank is controlled by TenGer Financial Group LLC. TenGer Financial Group LLC is owned by the shareholders detailed in Note 1.

A number of banking transactions are entered into with related parties in the normal course of business. These include loans, deposits and foreign currency transactions. These transactions were carried out on commercial terms and at market rates.

As at 31 December 2016 and 2015, the Bank had the following balances and transactions with related parties.

	2016 MNT'000	**2015 MNT'000**
a) Loans and advances to related companies:		
Holding company	8,710,432	8,773,138
Fellow subsidiaries	3,403,813	2,997,182
	12,114,245	11,770,320
Members of the Board of Directors and key management personnel of the Bank	2,196,269	1,653,946
	14,310,514	**13,424,266**

The loans and advances to related parties are secured, bear interest rates from 6.5% to 24.0% (2015: 6.5% to 27.6%) per annum and are repayable within one to 20 years. The interest income received from such loans during the financial year amounted to MNT 1,946.7 million (2015: MNT 1,673.9 million).

	2016 MNT'000	**2015 MNT'000**
b) Deposits from related companies:		
Holding company	25,085	81,434
Fellow subsidiaries	9,755,932	7,289,376
Shareholders of holding company	35,191	1,692,262
	9,816,208	**9,063,072**
Members of the Board of Directors and key management personnel of the Bank	1,741,576	1,500,727
	11,557,784	**10,563,799**

The deposits from the above related parties bear interest rates from 0% to 15.2% (2015: 0% to 16.1%) per annum. The interest expenses paid to the above depositors during the financial year amounted to MNT 477.5 million (2015: MNT 974.5 million).

39. RELATED PARTY DISCLOSURES (Contd.)

	2016 MNT'000	2015 MNT'000
c) Loans from shareholders of TenGer Financial Group LLC:		
European Bank for Reconstruction and Development	39,626,976	55,253,859
International Finance Corporation ("IFC")	111,821,876	-
Triodos Fair Share Fund	6,482,033	12,435,522
	157,930,885	**67,689,381**

The loans from the above shareholders of TenGer Financial Group LLC bear interest rates from 2.95% to 15.46% (2015: 2.95% to 15.46%) per annum. The interest expenses paid on such loans during the financial year amounted to MNT 8,230.8 million (2015: MNT 5,937.6 million).

	2016 MNT'000	2015 MNT'000
d) Subordinated loan from shareholder of TenGer Financial Group LLC:		
International Finance Corporation ("IFC")	**112,853,126**	**90,050,609**

The subordinated loan from the above shareholder of TenGer Financial Group LLC bears interest rates of 7.25% to 8.96% (2015: 6.94% to 8.96%) per annum. The interest expenses paid on such subordinated loan during the financial year amounted to MNT 8,164.2 million (2015: MNT 7,126.0 million).

	2016 MNT'000	2015 MNT'000
e) Finance lease from related companies		
Fellow subsidiary	65,922	-
	65,922	**-**

The finance lease from the above related parties bears interest rate 18% (2015: 0%) per annum. The interest expenses paid on the above finance lease during the financial year amounted to MNT 13.1 million (2015: Nil).

39. RELATED PARTY DISCLOSURES (Contd.)

	2016 MNT'000	2015 MNT'000
f) Security fees paid to related company:		
Fellow subsidiary	1,779,785	1,967,647
	1,779,785	**1,967,647**

	2016 MNT'000	2015 MNT'000
g) Commission income from related companies:		
Holding company	891	621
Fellow subsidiaries	5,130	4,468
Shareholders of holding company	119	509
	6,140	**5,598**
Members of the Board of Directors and key management personnel of the Bank	2,462	4,924
	8,602	**10,522**
h) Contract fee paid to related companies:		
Holding company	-	-
Fellow subsidiaries	798,940	370,238
	798,940	**370,238**
i) Rental income from related companies:		
Fellow subsidiaries	58,320	63,785
	58,320	**63,785**
j) Insurance brokerage income from related companies:		
Fellow subsidiaries	283,885	320,132
	283,885	**320,132**
k) Claims income from related companies:		
Fellow subsidiaries	5,669	26,029
	5,669	**26,029**

39. RELATED PARTY DISCLOSURES (Contd.)

	2016 MNT'000	2015 MNT'000
l) Compensation of key management personnel:		
Short-term employee benefits	4,628	1,928
Salaries	2,629,083	2,838,738
Contribution to social and health fund	284,332	307,051
	2,918,043	**3,147,717**

Terms and conditions of transactions with related parties

The above mentioned transactions and outstanding balances arose in the ordinary course of business. The interest charged to and by related parties are at normal commercial rates. Outstanding balances except for loans and advances to related parties at the year-end are unsecured. There have been no guarantees provided or received for any related party receivables or payables. For the years ended 31 December 2016 and 2015, the Bank has not made any impairment allowance relating to amounts owed by related parties.

40. RISK MANAGEMENT

40.1 Introduction

Risk is inherent in the Bank's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. The main risk inherent in the Bank's day to day operation involves credit risk, liquidity risk, market risk and operational risk. Such risk could either result in a direct loss in earnings and capital or may result in constraints on the Bank's ability to meet its objectives.

The Bank has a clearly defined risk management framework which is not designed to eliminate the risk but to optimise the risk and return trade off. The risk management framework in place is to ensure that:

(i) Individuals who manage the risks clearly understand the requirement and measurement system;
(ii) The Bank's risk exposure is within the limits established by the Board of Directors ("BOD");
(iii) The risk measured is in line with the business strategy as approved by the BOD;
(iv) The capital allocation is consistent with the risk of exposures; and
(v) The Bank's performance objectives are aligned with the risk tolerance.

Risk management structure

The BOD is responsible for the overall risk management approach and for approving the risk strategies and principles. However, there are separate independent bodies responsible for managing and monitoring risks.

Board Risk Management Committee (BRMC) and Bank Risk Management Committee (RMC)

The RMC sets the comprehensive risk management policies and tolerances. RMC is responsible for anticipating and managing new and ongoing financial risk across business departments and maintaining appropriate limits on risk taking, adequate systems and standards for measuring financial risk and performance, comprehensive risk reporting and management review process. The BRMC is responsible ensuring independent risk management oversight function of the Bank.

Risk Management Division (RMD)

The RMD has direct accountability for identifying, measuring, monitoring, and managing the daily financial positions and market risk. It is also primarily responsible for the credit portfolio risk, liquidity risk and operational risk of the Bank.

40. RISK MANAGEMENT (Contd.)

40.1 Introduction (Contd.)

Internal audit

Risk management processes throughout the Bank are audited regularly by the internal audit function, that examines both the adequacy of the procedures and the Bank's compliance with the procedures. Internal audit discusses the results of all assessments with management, and reports its findings and recommendations to the Board Audit Committee.

Risk measurement and reporting system

The Bank's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Bank also runs worse case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition, the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Board of Directors, BRMC, RMC, and the head of each business division. The report includes aggregate credit exposure, credit metric forecasts, hold limit exceptions, VaR, liquidity ratios and risk profile changes. On a monthly basis detailed reporting of industry and customer risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a quarterly basis. The Supervisory Board receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Bank.

For all levels throughout the Bank, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

A monthly briefing is given to the Executive Committee and all other relevant members of the Bank on the utilisation of market limits, analysis of VaR and liquidity, plus any other risk developments.

40. RISK MANAGEMENT (Contd.)

40.1 Introduction (Contd.)

Risk mitigation

As part of its overall risk management, the Bank uses VaR and basis sensitivity analysis to manage exposures resulting from changes in interest rates, foreign currencies, credit risks, and exposures arising from forecast transactions. The Bank actively uses collateral to reduce its credit risks.

Excessive risk concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly. At the individual basis, BoM sets the standards of a limitation as follows:

(i) The maximum amount of the overall credit exposures issued and other credit-equivalent assets to the individual and his/her related persons shall not exceed 20% of the capital of the Bank.

(ii) The maximum amount of the credit exposures issued and other credit-equivalent assets shall not exceed 5% of the capital for one related person to the bank, and the aggregation of overall lending to the related persons shall not exceed 20% of the capital of the Bank.

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk

The Bank is exposed to credit risk which is the risk that the Bank's customers, clients or counterparties will be unable or unwilling to pay interest, repay capital, or otherwise fulfill their contractual obligations under loan agreements, other credit facilities, or in respect of other financial instruments.

The Bank's RMC, through the Credit Management Division ("CMD") promotes diversification of the loan portfolio of the Bank's lending activities. The CMD structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, and to industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review. Credit limit to any single borrower and portfolio limits by loan products are approved by the Board of Directors and reviewed periodically by the CMD.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral and corporate and personal guarantees.

Credit-related commitments risks

The Bank makes available to its customers guarantees which may require that the Bank makes payments on their behalf. Such payments are collected from customers based on the terms of the letter of guarantee. They expose the Bank to similar risks to loans and these are mitigated by the same control processes and policies.

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans.

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)

Maximum exposure to credit risk without taking account of any collateral and other credit enhancements

The table below shows the maximum exposure to credit risk for the components of the statement of financial position. The maximum exposure is shown gross, before the effect of mitigation through the use of collateral agreements.

	Notes	Gross maximum exposure 2016 MNT'000	Gross maximum exposure 2015 MNT'000
Cash and balances with BoM (excluding cash on hand)	13	280,863,167	150,955,629
Due from banks	14	158,627,068	99,107,298
Reverse repurchase agreements	15	-	9,981,555
Derivative financial instruments	16	125,019,231	2,307,271
Financial investments - available for sale		22,837,304	18,778,377
Financial investments – held-to-maturity	17	355,119,924	373,542,234
Loans and advances to customers	18	1,248,048,121	1,239,460,582
Other assets	19	5,462,032	3,105,331
Total		**2,195,976,847**	**1,897,238,277**
Contingent liabilities	37	41,187,819	27,693,189
Commitments	37	34,226,912	25,767,574
Total		**75,414,731**	**53,460,763**
Total credit risk exposure		**2,271,391,578**	**1,950,699,040**

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)

Risk concentrations by industry

The table below show the analysis per industry sector and economic purpose of the Bank's loans and advances to customers (Note 18) in gross amounts, before taking into account the fair value of the loan collateral held or other credit enhancements.

	2016 Gross maximum exposure		2015 Gross maximum exposure	
	MNT'000	%	MNT'000	%
Trading	277,248,431	22.21	297,764,750	24.02
Production	194,057,350	15.55	227,271,619	18.34
Mortgage	188,579,944	15.11	177,307,450	14.31
Services	145,617,752	11.67	148,466,128	11.98
Consumption	128,535,477	10.30	112,569,112	9.08
Deposit backed	107,859,289	8.64	100,426,394	8.10
Construction	94,207,840	7.55	63,909,196	5.16
Other	31,750,627	2.54	44,472,092	3.59
Agricultural	39,305,251	3.15	30,358,547	2.45
Loans to staff	19,384,458	1.56	21,331,556	1.72
Mining	19,617,664	1.57	14,285,039	1.15
Loans to key management	1,884,038	0.15	1,298,699	0.10
Total	**1,248,048,121**	**100**	**1,239,460,582**	**100**

Collateral and other credit enhancements

The amount and type of collateral required depends on the assessment of the credit risk of the borrower or counterparty and the type of loan granted. The Bank follows the collateral guidelines set by the Credit Management Committee in determining the type and value of collateral to be obtained.

The main types of collateral obtained are as follows:

(i) For small business, consumer, agricultural, SME and employee loans - cash, guarantees, securities and real estate properties, chattels, inventory, etc.
(ii) For mortgage loans - mortgages on residential properties and vehicles.
(iii) For wholesale loans - cash, equities and real estate properties.
(iv) For deposit backed loans - cash deposit.

The Bank performs physical inspection of the collateral and regularly monitors the market value of collateral, requests additional collateral in accordance with underlying agreement, and monitors the market value of collateral obtained during its review of adequacy of the allowance for impairment losses.

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)

Credit quality per class of financial assets

The credit quality of loans and advances to customers is managed by the Bank using internal credit grading.

The following table shows the description of Credit Risk Grading System of the Bank:

Credit Rating	Grade Description
A	Excellent
B	Good
C	Satisfactory
D	Substandard

The Bank's 4-Grade Risk Rating is used in order to categorise exposures according to the risk profile. The 4-Grade Risk Rating is modeled using parametric approaches (logit model) that quantify the probability of default in determining the risk grade. Both qualitative and quantitative historical experience are taken into account by the Bank’s risk management department for the assumptions used. The risk grading system is used for determining impairment allowances against specific credit exposures. The current risk grading framework consists of four grades which are applied in an uniform matter.

It is the Bank’s policy to maintain accurate and consistent risk grades across the credit portfolio. This facilitates the management of the applicable risks and the comparison of credit exposures across all lines of loan products. The grading system is supported by a variety of financial and statistical analytics, combined with processed portfolio and market information to provide the main inputs for the measurement of counterparty risk. All risk grades are tailored to the various loans exposures and are derived in accordance with the Bank’s grading policy across all risk groupings reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation.

The Bank does not rate the unquoted financial investments.

The table below shows that credit quality by class of asset for all financial assets exposed to credit risk, based on the Bank’s internal credit rating system. The amounts presented are gross of impairment allowances.

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)
Credit quality per class of financial assets (Contd.)

		Neither past due nor impaired					Past due or individually impaired	
At 31 December 2016	**Note**	**Excellent MNT'000**	**Good MNT'000**	**Satisfactory MNT'000**	**Substandard MNT'000**	**Not rated MNT'000**	**MNT'000**	**Total MNT'000**
Cash and balances with BoM	13	326,779,876	-	-	-	-	-	326,779,876
Due from banks	14	1,130,444	151,167,666	3,659,078	-	2,669,880	-	158,627,068
Derivative financial instruments	16	125,019,231	-	-	-	-	-	125,019,231
Financial investments								
-available-for-sale	17	-	-	-	-	28,117,332	-	28,117,332
-held to maturity	17	355,119,924	-	-	-	-	-	355,119,924
Loans and advances to customers								
SME loans	18	44,316,901	43,685,817	335,639,341	19,673,643	-	135,979,587	579,295,289
Mortgage loans	18	48,619,224	9,257,691	123,994,306	5,001,550	-	15,216,005	202,088,776
Micro business loans	18	43,563,204	18,841,529	124,108,172	689,959	-	32,167,035	219,369,899
Consumer loans	18	9,787,118	71,372,223	37,058,330	1,348,450	-	6,269,715	125,835,836
Finance leases	18	4,381,383	1,600,423	3,451,896	24,076	-	1,075,343	10,533,121
Other	18	107,800,586	50,833	520,079	8,510	-	2,545,192	110,925,200
		258,468,416	144,808,516	624,772,124	26,746,188	-	193,252,877	1,248,048,121
Other assets	19	5,462,032	-	-	-	-	-	5,462,032
Total		**1,071,979,923**	**295,976,182**	**628,431,202**	**26,746,188**	**30,787,212**	**193,252,877**	**2,247,173,584**

40. RISK MANAGEMENT (Contd.)

40.2 Credit quality per class of financial assets (Contd.)

At 31 December 2015	Note	Neither past due nor impaired					Past due or individually impaired	Total
		Excellent MNT'000	Good MNT'000	Satisfactory MNT'000	Substandard MNT'000	Not rated MNT'000	MNT'000	MNT'000
Cash and balances with BoM	13	183,893,271	-	-	-	-	-	183,893,271
Due from banks	14	77,716,441	20,245,765	1,145,092	-	-	-	99,107,298
Reverse repurchase agreements	15	9,981,555	-	-	-	-	-	9,981,555
Derivative financial instruments	16	2,307,271	-	-	-	-	-	2,307,271
Financial investments								
-available-for-sale	17	-	-	-	-	19,639,167	-	19,639,167
-held to maturity	17	373,542,234	-	-	-	-	-	373,542,234
Loans and advances to customers								
SME loans	18	15,024,227	56,610,361	358,045,050	16,511,801	24,136	130,673,925	576,889,500
Mortgage loans	18	43,981,266	12,248,313	115,453,569	11,638,097	135,741	7,888,805	191,345,791
Micro business loans	18	17,793,505	19,061,024	184,708,043	6,325,927	-	14,227,572	242,116,071
Consumer loans	18	13,104,950	33,197,492	43,213,658	5,161,358	10,641	7,356,501	102,044,600
Finance leases	18	6,816,760	3,208,319	6,809,784	597,659	-	1,786,339	19,218,861
Other	18	104,207,988	301,352	685,236	40,065	54,073	2,557,045	107,845,759
		200,928,696	124,626,861	708,915,340	40,274,907	224,591	164,490,187	1,239,460,582
Other assets	19	3,104,099	-	-	-	-	1,232	3,105,331
Total		**851,473,567**	**144,872,626**	**710,060,432**	**40,274,907**	**19,863,758**	**164,491,419**	**1,931,036,709**

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)

Past due loans and advances to customers include those that are only past due by a few days. An analysis of past due loans, by age, is provided below. The majority of the past due loans are not considered to be impaired.

Aging analysis of past due but not impaired loans by class of financial assets

	Less than 30 days MNT'000	31 to 60 days MNT'000	61 to 90 days MNT'000	More than 90 days MNT'000	Total MNT'000
As at 31 December 2016					
Loan and advances to customers					
SME loans	25,281,196	2,656,065	20,095,361	31,618,539	79,651,161
Mortgage loans	2,032,279	1,845,416	1,103,162	9,953,907	14,934,764
Micro business loans	3,573,860	3,500,743	2,522,491	22,569,941	32,167,035
Consumer loans	791,103	566,161	242,753	4,669,698	6,269,715
Finance leases	84,124	48,706	29,961	912,552	1,075,343
Other	116,056	193,590	10,639	2,224,907	2,545,192
	31,878,618	**8,810,681**	**24,004,367**	**71,949,544**	**136,643,210**

	Less than 30 days MNT'000	31 to 60 days MNT'000	61 to 90 days MNT'000	More than 90 days MNT'000	Total MNT'000
As at 31 December 2015					
Loan and advances to customers					
SME loans	57,546,416	9,110,303	10,743,910	17,902,066	95,302,695
Mortgage loans	855,844	674,264	975,551	5,383,146	7,888,805
Micro business loans	2,221,455	1,098,747	1,153,470	9,753,899	14,227,571
Consumer loans	1,165,875	808,573	513,657	4,868,396	7,356,501
Finance leases	311,906	182,977	129,875	1,161,582	1,786,340
Other	56,309	22,193	343,625	2,134,918	2,557,045
	62,157,805	**11,897,057**	**13,860,088**	**41,204,007**	**129,118,957**

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)

Aging analysis of past due but not impaired loans by class of financial assets (Contd.)

Of the total aggregate amount of gross past due but not impaired loans and advances to customers, the fair value of collateral that the Bank held as at 31 December 2016 was MNT 247,975 million (2015: MNT 226,141 million). Please refer Note 18 for more detailed information with respect to allowance for impairment losses on loans and advances to customers.

Carrying amount per class of financial assets whose terms have been renegotiated

The table below shows the carrying amount for renegotiated financial assets, by class.

	2016 MNT'000	2015 MNT'000
Loans and advances to customers:		
SME loans	24,832,590	2,719,588
Micro business loans	2,854,057	47,859
Mortgage loans	788,730	1,891
Finance leases	112,193	-
Customer loan		36,610
Other	-	-
	28,587,570	**2,808,948**

Impairment assessment

The main considerations for the loan impairment assessment include whether any payments of principal or interest are overdue by more than 90 days or there are any known difficulties in the cash flows of counterparties, credit rating downgrades, or infringement of the original terms of the contract. The Bank addresses impairment assessment in two areas: individually assessed allowances and collectively assessed allowances.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected dividend payout should bankruptcy ensue, the availability of the other financial support and the realisable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

40. RISK MANAGEMENT (Contd.)

40.2 Credit risk (Contd.)

Collectively assessed allowances

Allowances are assessed collectively for losses on loans and advances that are not individually significant and for individually significant loans and advances where there is not yet objective evidence of individual impairment. Allowances are evaluated quarterly with each portfolio receiving a separate review by the management.

The collective assessment takes account of impairment that is likely to be present in the portfolio even though there is not yet objective evidence of impairment in an individual assessment. Impairment losses are estimated by taking into consideration of the following information: historical losses on the portfolio, current economic conditions, the approximate delay between the time a loss is likely to have been incurred and the time it will be identified as requiring an individually assessed impairment allowance, and expected receipts and recoveries once impaired.

Local management is responsible for deciding the length of this period which can extend for as long as one year. The impairment allowance is then reviewed by credit management to ensure alignment with the Bank's overall policy.

40.3 Liquidity risk

The Bank is exposed to liquidity risks that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. The Bank sets limits on the minimum funding composition that should be in place to cover withdrawals at unexpected levels of demand. It is the Bank's policy to maintain a prudent mix of borrowed and core deposit base. In addition, the Bank maintains a statutory deposit with BoM equal to 12% (2015: 12%) of customer deposits.

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Bank’s financial liabilities based on contractual undiscounted repayment obligations. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank’s deposit retention history.

40. RISK MANAGEMENT (Contd.)

40.3 Liquidity risk (Contd.)

Analysis of non-derivative financial liabilities by remaining contractual maturities (Contd.)

Financial liabilities	On demand MNT'000	Less than 3 months MNT'000	3 to 6 months MNT'000	6 months to 1 year MNT'000	1 to 5 years MNT'000	Over 5 years MNT'000	Total undiscounted financial liabilities MNT'000
At 31 December 2016							
Due to banks	753,668	-	-	-	-	-	753,668
Repurchase agreement	-	-	-	-	-	-	-
Due to customers	283,306,374	150,127,015	138,638,220	196,445,304	127,941,688	263,409,541	1,159,868,142
Borrowed funds	4,902,840	61,711,024	183,183,952	261,645,219	514,167,227	11,343,055	1,036,953,317
Subordinated loans	843,716	1,687,432	2,531,147	15,459,898	139,900,351	-	160,422,544
Other liabilities	-	4,650,279	6,800	868,450	12,780,330	3,827,049	22,132,908
Total	**289,806,598**	**218,175,750**	**324,360,119**	**474,418,871**	**794,789,596**	**278,579,645**	**2,380,130,579**

40. RISK MANAGEMENT (Contd.)

40.3 Liquidity risk (Contd.)

Analysis of non-derivative financial liabilities by remaining contractual maturities (Contd.)

Financial liabilities	On demand MNT'000	Less than 3 months MNT'000	3 to 6 months MNT'000	6 months to 1 year MNT'000	1 to 5 years MNT'000	Over 5 years MNT'000	Total undiscounted financial liabilities MNT'000
At 31 December 2015							
Due to banks	1,063,962	336,847	18,644,850	1,637,802	-	-	21,683,461
Repurchase agreement	101,554,699	-	-	-	-	-	101,554,699
Due to customers	218,645,217	117,120,629	141,924,815	222,470,685	112,347,052	229,159,871	1,041,668,269
Borrowed funds	3,823,259	28,468,431	49,996,257	261,026,928	341,604,007	17,227,848	702,146,730
Subordinated loans	671,714	1,343,427	2,015,141	10,045,232	125,797,902	-	139,873,416
Other liabilities	-	2,303,785	332,042	863,019	273,789	5,022,901	8,795,536
Total	**325,758,851**	**149,573,119**	**212,913,105**	**496,043,666**	**580,022,750**	**251,410,620**	**2,015,722,111**

40. RISK MANAGEMENT (Contd.)

40.3 Liquidity risk (Contd.)

Analysis of financial liabilities by remaining contractual maturities (Contd.)

The table below shows the contractual expiry by maturity of the Bank's contingent liabilities and commitments.

	On demand MNT'000	Less than 3 months MNT'000	3 to 6 Months MNT'000	6 months to 1 year MNT'000	1 to 5 years MNT'000	Over 5 years MNT'000	Total undiscounted financial liabilities MNT'000
At 31 December 2016							
Contingent liabilities (Note 37)	4,898,943	6,374,101	10,470,013	8,668,244	10,776,518	-	41,187,819
Commitments (Note 37)	7,032,817	1,155,310	4,318,470	15,572,164	6,148,151	-	34,226,912
Total	**11,931,760**	**7,529,411**	**14,788,483**	**24,240,408**	**16,924,669**	**-**	**75,414,731**
At 31 December 2015							
Contingent liabilities (Note 37)	6,109,245	3,119,357	5,212,033	5,263,965	3,996,629	3,991,960	27,693,189
Commitments (Note 37)	578,166	1,884,561	1,954,819	7,156,450	14,193,578	-	25,767,574
Total	**6,687,411**	**5,003,918**	**7,166,852**	**12,420,415**	**18,190,207**	**3,991,960**	**53,460,763**

40. RISK MANAGEMENT (Contd.)

40.4 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates or foreign exchange rates. The Bank manages and monitors this risk element using VaR and sensitivity analyses. Except for the concentrations within foreign currencies, the Bank has no significant concentration of market risk.

Interest rate risk

Interest rate risk arises when there is a mismatch between positions, which are subject to interest rate adjustment within a specified period. The Bank's lending, funding and investment activities give rise to interest rate risk. The immediate impact of variation in interest rate is on Bank's net interest income, while a long term impact is on the Bank's net worth since the economic value of the Bank's assets, liabilities and off-balance sheet exposures will be affected. The management has established limits on the interest rate gaps for stipulated periods. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained with the established limits.

The following table demonstrates the sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Bank's statement of comprehensive income. The sensitivity of the statement of comprehensive income is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate financial assets and financial liabilities held at 31 December 2016 and 31 December 2015.

Currency	**Change in basis points**	**Sensitivity of net interest income MNT'000**
At 31 December 2016		
USD	+120	(6,683,975)
MNT	+120	204,486
USD	-120	6,683,975
MNT	-120	(204,486)
At 31 December 2015		
USD	+120	(2,936,884)
MNT	+120	(46,378)
USD	-120	2,936,884
MNT	-120	46,378

40. RISK MANAGEMENT (Contd.)

40.4 Market risk (Contd.)

Currency risk

Currency risk is the possibility of financial loss to the Bank arising from adverse movements in foreign exchange rates. The Bank's management sets limits on the level of exposure by currencies, which are monitored on a frequent basis. Apart from using foreign exchange exposure mismatch, the Bank has applied Value-at-Risk ("VaR") simulation model to manage and measure foreign exchange risk since March 2007. VaR is a method used in measuring financial risk by estimating the potential negative change in the market value of a portfolio at a given confidence level and over specified time horizon.

Objectives and limitations of the VaR Methodology

The VaR model is designed to measure market risk in a normal market environment. The model assumes that any changes occurring in the risk factors affecting the normal market environment will follow a normal distribution. The Bank uses Variance/Covariance model to assess possible changes in foreign currency portfolio based on historical data from the past one day. The VaR methodology employed by the Bank uses a one-day period, using 99% confidence level, of the potential loss that is not expected to be exceeded if the current market risk positions were to be held unchanged for one day, and are determined by observing market data movements over a 250-day period. The use of a 99% confidence level means that, within one day horizon, losses exceeding the VaR figure should occur, on average, not more than once every hundred days.

The use of VaR has limitations because it is based on historical correlations and volatilities in market prices and assumes that future price movements will follow a statistical distribution. Due to the fact that VaR relies heavily on historical data to provide information and may not clearly predict the future changes and modifications of the risk factors, the probability of large market moves may be underestimated if changes in risk factors fail to align with the normal distribution assumption. VaR may also be under or over-estimated due to the assumptions placed on risk factors and the relationship between such factors for specific instruments. Even though positions may change throughout the day, the VaR only represents the risk of the portfolios at the close of each business day, and it does not account for any losses that may occur beyond the 99% confidence level.

VaR is an integral part of the Bank's market risk management since March 2007. VaR limits and exposures are reviewed regularly against the limits set by management. The estimated potential one-day losses on its foreign currency denominated financial instruments, as calculated in the VAR model, are the following:

	Variance/ Covariance MNT’000		**Variance/ Covariance MNT’000**
2016 – 31st December	59,928	2015 – 31st December	29,648
2016 - Average Daily	75,703	2015 - Average Daily	53,821
2016 – Highest	277,278	2015 - Highest	293,116
2016 – Lowest	16,508	2015 - Lowest	8,053

40. RISK MANAGEMENT (Contd.)
40.4 Market risk (Contd.)

Currency risk (Contd.)

The table below summarises the Bank's exposure to foreign exchange risk as 31 December, 2016. Included in the table are the Bank's financial assets and liabilities at carrying amounts, categorised by currencies.

Financial assets and financial liabilities	**MNT MNT'000**	**USD MNT'000**	**Euro MNT'000**	**Other MNT'000**	**Total MNT'000**
As at 31 December 2016					
Assets					
Cash and balances with BoM	115,994,154	203,471,420	1,365,545	5,948,757	326,779,876
Due from banks	322	149,141,742	4,255,730	5,229,274	158,627,068
Reverse repurchase agreements	-	-	-	-	-
Derivative financial instruments*	89,928,202	648,790,510	-	-	738,718,712
Financial investments					
-available-for-sale	28,117,332	-	-	-	28,117,332
-held-to-maturity	266,524,798	88,595,126	-	-	355,119,924
Loans and advances to customers	1,043,416,847	113,606,499	173,862	4,375	1,157,201,583
Other assets	4,490,555	954,782	3,721	12,974	5,462,032
	1,548,472,210	**1,204,560,079**	**5,798,858**	**11,195,380**	**2,770,026,527**
Liabilities					
Due to banks	46,631	703,232	550	-	750,413
Repurchase agreements	-	-	-	-	-
Due to customers	754,487,277	217,573,493	5,818,633	7,624,284	985,503,687
Derivative financial instruments*	524,918,380	89,709,704	-	-	614,628,084
Borrowed funds	192,318,659	743,775,336	-	-	936,093,995
Subordinated loans	-	123,443,085	-	-	123,443,085
Other liabilities	10,227,480	11,847,991	404	57,033	22,132,908
	1,481,998,427	1,187,052,841	5,819,587	7,681,317	2,682,552,172
Net position	**66,473,783**	**17,507,238**	**(20,729)**	**3,514,063**	**87,474,355**

** The figure is shown at gross amount to reflect the actual currency position*

40. RISK MANAGEMENT (Contd.)

40.4 Market risk (Contd.)

Currency risk (Contd.)

The table below summarizes the Bank's exposure to foreign exchange risk as 31 December, 2015. Included in the table are the Bank's financial assets and liabilities at carrying amounts, categorized by currencies (Contd.).

Financial assets and financial liabilities	MNT MNT'000	USD MNT'000	Euro MNT'000	Other MNT'000	Total MNT'000
As at 31 December 2015					
Assets					
Cash and balances with BoM	125,794,619	50,955,125	2,520,935	4,622,592	183,893,271
Due from banks	8,003,636	85,784,175	1,182,058	4,137,429	99,107,298
Reverse repurchase agreements	9,981,555	-	-	-	9,981,555
Derivative financial instruments*	19,940,786	394,561,979	-	-	414,502,765
Financial investments					-
-available-for-sale	19,639,167	-	-	-	19,639,167
-held-to-maturity	302,525,949	71,016,285	-	-	373,542,234
Loans and advances to customers	976,643,967	194,413,943	129,939	101,457	1,171,289,306
Other assets	2,560,566	534,161	3,242	7,362	3,105,331
	1,465,090,245	**797,265,668**	**3,836,174**	**8,868,840**	**2,275,060,927**
Liabilities					
Due to banks	10,222,264	10,438,604	-	-	20,660,868
Repurchase agreements	100,299,411	-	-	-	100,299,411
Due to customers	648,998,095	228,142,663	3,773,267	5,341,623	886,255,648
Derivative financial instruments*	397,247,123	19,959,800	-	1,658,000	418,864,923
Borrowed funds	226,185,931	417,034,288	-	-	643,220,219
Subordinated loans	-	104,216,742	-	-	104,216,742
Other liabilities	8,560,015	128,175	-	107,346	8,795,536
	1,391,512,839	779,920,272	3,773,267	7,106,969	2,182,313,347
Net position	**73,577,406**	**17,345,396**	**62,907**	**1,761,871**	**92,747,580**

** The figure is shown as gross amount to reflect the actual currency position*

40. RISK MANAGEMENT (Contd.)

40.4 Market risk (Contd.)

Prepayment risk

Prepayment risk is the risk that the Bank will incur a financial loss because its customers and counterparties repay or request repayment earlier or later than expected.

The Bank uses the simplified approach to project the impact of varying levels of prepayment on its net interest income.

If 20% of repayable financial instruments were prepaid at the beginning of the year, with all other variables held constant, the profit before tax for the year would be reduced by MNT 9,239 million (2015: MNT 14,400 million).

Operational risk

Operational risk is the risk of loss arising from systems failure, human errors, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, and lead to financial loss. The Bank cannot expect to eliminate all operational risk, but through a dual control framework, segregation of duties between front-office and back office functions, controlled access to systems, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit, the Bank seeks to manage operational risk.

41. CAPITAL ADEQUACY

The Bank actively manages its capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by BoM. During the past year, the Bank complied in full with all its externally imposed capital requirements.

Capital management

The primary objectives of the Bank's capital management are to ensure that the Bank complies with externally imposed capital requirements and that the Bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholder's value.

The Bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to the shareholder, return capital to the shareholder or issue new equity or equity related securities.

Regulatory capital

BoM requires commercial banks to maintain a minimum core capital adequacy ratio of 9% (2015: 9%) and risk weighted capital ratio of at least 14% (2015: 14%) compiled on the basis of total capital and total assets as adjusted for their intrinsic risk characteristics. The capital adequacy ratios of the Bank as at 31st December were as follows:

	2016	**2015**
Core capital ratio	12.73%	13.72%
Risk weighted capital ratio	19.19%	20.57%

	2016 MNT'000	**2015 MNT'000**
Tier I capital		
Ordinary shares	55,342,753	55,342,753
Share premium	-	-
Other reserves	10,531,368	10,531,368
Retained profits	103,760,094	90,451,081
Total Tier I Capital	169,634,215	156,325,202
Tier II capital		
Subordinated loans	84,817,108	78,162,601
Other	1,255,916	-
Total capital /capital base	**255,707,239**	**234,487,803**

41. CAPITAL ADEQUACY (Contd.)

Regulatory capital (Contd.)

The breakdown of risk weighted assets into the various categories of risk weights as at 31st December was as follows:

	2016		2015	
	Risk		**Risk**	
	Assets	**Weighted**	**Assets**	**Weighted**
%	**MNT'000**	**MNT'000**	**MNT'000**	**MNT'000**
0	784,237,755	-	718,900,019	-
20	79,018,911	15,803,782	30,015,577	6,003,115
50	211,441,179	105,720,590	173,749,847	86,874,924
70	294,049,642	205,834,749	271,607,169	190,125,018
100	907,340,470	907,340,470	688,099,603	688,099,603
120	57,969,019	69,562,823	107,869,226	129,443,071
150	-	-	8,308,835	12,463,253
Adjustments:				
Operational risk ratio		23,881,130		22,239,030
Foreign exchange risk ratio		4,448,672		4,435,838
Total	**2,334,056,976**	**1,332,592,216**	**1,998,550,276**	**1,139,683,852**

42. MONGOLIAN TRANSLATION

These financial statements are also prepared in Mongolian language. In the event of discrepancies or contradictions between the English version and the Mongolian version, the English version will prevail.

43. EVENTS AFTER THE REPORTING PERIOD

There have been no significant events after the reporting period requiring disclosure in the financial statements.