

JOINT-STOCK COMPANY OTP BANK

Consolidated Financial Statements and
Independent Auditor's Report
for the Year Ended 31 December 2019

Joint-Stock Company OTP Bank

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INDEPENDENT AUDITOR'S REPORT

To the Shareholder of JOINT-STOCK COMPANY OTP BANK:

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of JOINT-STOCK COMPANY OTP BANK (the "Bank") and its subsidiary (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2019, and the consolidated statement of profit or loss and other comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2019, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs") and the preparation of the financial statements requirements of the Law of Ukraine "On accounting and financial reporting in Ukraine" ("Law on accounting and financial reporting").

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 Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the consolidated financial statements in Ukraine, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

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

Why the matter was determined to be a key audit matter	How the matter was addressed in the audit
Allowances for expected credit losses ("ECL") on loans to customers	Our audit procedures have included the following: Updating understanding of the Group's processes and control procedures for determination of a significant increase in credit risk and the event of default, assessment of the probability of default and measurement of expected credit losses on loans and advances to customers.

Why the matter was determined to be a key audit matter

Allowances for ECL represent management's best estimate of the 12-months ECL for stage 1 assets, or lifetime ECL for stage 2 or stage 3 assets at the reporting date. They are calculated on a collective basis for portfolios of loans of similar credit risk characteristics and on an individual basis for significant loans. The calculation of both collective and individual allowances for ECL is inherently judgmental. Collective ECL are calculated using statistical models, which approximate the impact of current and future economic and credit conditions on large portfolios of loans. The inputs to these models are subject to management judgment and model revisions are required. For individual assessment, judgment is required to estimate the expected future cash flows scenarios related to that loan. In addition, management's judgement is required to assess whether significant increase of credit risk ("SICR") has occurred since initial recognition.

Allowances for ECL is determined as a key audit matter due to significance of the loans balance that amounted to UAH 25,469,028 thousand as at 31 December 2019, and significant judgements used in calculations, as discussed in Note 3, Note 11 and Note 27.

How the matter was addressed in the audit

- For collective ECL allowances, the appropriateness of changes to the modeling policy and methodology used for material portfolios was independently assessed with involvement of credit risk and actuarial experts by reference to the accounting standards and market practices. We assessed the appropriateness of management's judgments in respect of calculation methodologies, segmentation, SICR identification, time period used for probability of default and recovery rates assessment, including macroeconomic adjustment, and valuation of collateral. We checked on sample basis completeness and accuracy of historical data used as inputs in collective models and checked forward-looking assumptions to external macroeconomic forecasts.
- For individual allowances, the appropriateness of changes to provisioning methodologies was independently assessed for a sample of loans across the whole portfolio selected on the risk basis. An independent assessment was performed in respect of the amount of ECL recognized based on the detailed loan and counterparty information in the credit file. We re-performed calculations within a sample of discounted cash flow models.
- We checked completeness and accuracy of the relevant notes to the consolidated financial statements.

Other Information

Management is responsible for the other information. The other information comprises the information included in the management report, and corporate governance report (but does not include the consolidated financial statements and our auditor's report thereon), which we obtained prior to the date of this auditor's report, and the issuers annual report, which also includes corporate governance report, which is expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the issuers annual report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

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

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

In preparing the consolidated financial statements, management is responsible for assessing the Group'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 Group or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

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

- Identify and assess the risks of material misstatement of the consolidated 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group'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 consolidated 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 Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated 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.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period, which constitute the key audit matters included herein. We describe these matters in our auditor's report, except for the cases when a law or regulation prohibits a public disclosure of a specific matter or, in extremely adverse circumstances, we determine that such an matter should not be addressed in our report, as negative consequences from such a disclosure may predictably outweigh its usefulness for interests of the public.

Report on Other Legal Requirements

We have been appointed as auditor of JOINT-STOCK COMPANY OTP BANK by Supervisory Board on 10 September 2019. In view of the previous renewals and reappointments, we conducted audit from 28 September 2018 to the date of this report.

We confirm that the audit opinion is consistent with the additional report to the Supervisory Board.

We confirm that the prohibited non-audited services referred to ISA or requirements of Article 6, paragraph 4 of Law of Ukraine «On Audit of Financial Statements and Audit Activities» were not provided and that the audit engagement partner and audit firm remains independent of the Group in conducting the audit.

Pursuant to the requirements of Article IV paragraph 11 of the Instruction on the procedure for preparation and publication of financial statements of Ukrainian banks approved by the Resolution of the Board of the National Bank of Ukraine No. 373 dated 24 October 2011 (with amendments) ("Instruction No. 373"), we report the following:

- In our opinion, based on the work undertaken in the course of our audit of the Group's consolidated financial statements, the Management report has been prepared in accordance with the requirements of the Article IV of the Instruction No. 373 and the information in the Management report is consistent with the consolidated financial statements.
- We are required to report if we have identified material misstatements in the Management report in light of our knowledge and understanding of the Group obtained during our audit of the Group's consolidated financial statements. We have nothing to report in this respect.

Basic information about audit firm

Name: LLC "Deloitte & Touche Ukrainian Services Company".

Address of registration and location of audit firm: 48, 50a Zhylianska Str., Kyiv, 01033, Ukraine

"LLC "Deloitte & Touche Ukrainian Services Company" was enrolled to Sections of "Audit Entities", "Audit Entities and Auditors That Have the Right to Conduct Statutory Audits of Financial Statements", and "Audit Entities and Auditors That Have the Right to Conduct Statutory Audits of Financial Statements of Public Interest Entities" of the Register of Auditors and Auditing Entities of the Audit Chamber of Ukraine under #1973."

LLC "Deloitte & Touche UHC"

Certified Auditor



Natalia Samoilova

Certificate of Banks' Auditor # 0202

Issued by the Audit Chamber of Ukraine on 24 December 2014

on the basis of Resolution of the Audit Chamber of Ukraine # 304/2

Registration Number in the Register of Auditors and Auditing Entities 102404

LLC "Deloitte & Touche Ukrainian Services Company"
48, 50a Zhylianska Str., Kyiv, 01033, Ukraine

26 March 2020

Joint-Stock Company OTP Bank

Consolidated Statement of Profit or Loss and Other Comprehensive Income for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

	Notes	2019	2018
Interest income	4, 24	5,253,438	4,133,371
Interest expense	4, 24	(1,635,423)	(1,226,343)
Net interest income before allowance for expected credit losses on interest bearing assets	4	3,618,015	2,907,028
Fee and commission income	6, 24	1,695,811	1,445,122
Fee and commission expense	6, 24	(392,952)	(297,109)
Net gain on foreign exchange and precious metals operations	24	176,917	152,056
Net gain on transactions with derivative financial instruments	24	164,169	164,224
Net gain on investments measured at fair value through other comprehensive income (FVTOCI)		43,502	5,570
Net loss on modification of financial assets		(12,884)	(20,320)
Impairment losses on interest bearing assets	5, 24	(145,694)	(393,928)
(Provision)/recovery of provision on other operations		(46,447)	4,344
Other income	24	165,598	97,632
Net non-interest profit		1,648,020	1,157,591
Operating profit		5,266,035	4,064,619
Operating expense	7, 24	(2,041,548)	(1,662,895)
Profit before income tax		3,224,487	2,401,724
Income tax expense	8	(557,610)	(427,414)
Net profit for the year		2,666,877	1,974,310
Other comprehensive (loss)/income			
Items that may be subsequently reclassified to profit or loss:			
Change in fair value of investments measured at fair value through other comprehensive income		(3,284)	65,465
Other comprehensive (loss)/income		(3,284)	65,465
Total comprehensive income for the year		2,663,593	2,039,775
Earnings per share			
Weighted average number of outstanding ordinary shares		499,238	499,238
Basic and diluted earnings per share, UAH		5,342	3,955

Authorized for issue by management of the Group and signed on its behalf by:

Tamas Hak-Kovacs,

Chairman of the Management Board

Natalia Diuba,

Chief Accountant

26 March 2020

26 March 2020

The accompanying notes on pages from 11 to 77 form an integral part of these consolidated financial statements.

Joint-Stock Company OTP Bank

Consolidated Statement of Financial Position
as at 31 December 2019
In Ukrainian Hryvnias and in thousands)

	Notes	31 December 2019	31 December 2018
ASSETS			
Cash and balances with the National Bank of Ukraine	9	3,139,593	2,320,458
Due from banks	10, 24	4,308,470	2,507,127
Loans to customers	11, 24	25,469,028	22,059,052
Investments measured at fair value through other comprehensive income	12	3,631,783	1,102,220
Investments measured at amortized cost	13	7,212,296	3,677,428
Property and equipment and intangible assets	14	570,535	478,898
Right-of-use assets	15	191,946	-
Current income tax assets		5,137	127,402
Deferred income tax assets	8	38,747	177,315
Investment property		28,152	39,381
Other assets	16, 24	233,118	267,857
TOTAL ASSETS		44,828,805	32,757,138
LIABILITIES			
Due to banks and other financial institutions	17, 24	567,801	441
Customer accounts	18, 24	35,094,301	26,855,632
Lease liabilities	19	174,425	-
Current income taxes payable		84,827	-
Other liabilities	20, 24	793,970	646,259
TOTAL LIABILITIES		36,715,324	27,502,332
EQUITY			
Share capital	21	6,186,023	6,186,023
Share premium	21	405,075	405,075
Other additional capital	21	1,236,294	1,236,294
Revaluation reserve for investments measured at fair value through other comprehensive income		71,001	67,683
Retained earnings/(Accumulated deficit)		215,088	(2,640,269)
TOTAL EQUITY		8,113,481	5,254,806
TOTAL LIABILITIES AND EQUITY		44,828,805	32,757,138

Authorized for issue by management of the Group and signed on its behalf by:

Tamas Hak-Kovacs,
Chairman of the Management Board

26 March 2020

Natalia Diuba,
Chief Accountant

26 March 2020

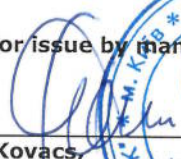
The accompanying notes on pages from 11 to 77 form an integral part of these consolidated financial statements.

Joint-Stock Company OTP Bank

Consolidated Statement of Changes in Equity
for the Year Ended 31 December 2019
In Ukrainian Hryvnias and in thousands

	Notes	Share capital	Share premium	Other additional capital	Revaluation reserve for investments measured at fair value through other comprehensive income	(Accumulated deficit)/ retained earnings	Total equity
1 January 2018		6,186,023	405,075	1,236,294	29,629	(4,614,579)	3,242,442
Change in fair value of investments measured at fair value through other comprehensive income		-	-	-	38,054	-	38,054
Net profit		-	-	-	-	1,974,310	1,974,310
1 January 2019		6,186,023	405,075	1,236,294	67,683	(2,640,269)	5,254,806
Change in fair value of investments measured at fair value through other comprehensive income		-	-	-	3,318	(3,526)	(208)
Gain on the bargain purchase of an entity	28	-	-	-	-	192,006	192,006
Net profit		-	-	-	-	2,666,877	2,666,877
31 December 2019		6,186,023	405,075	1,236,294	71,001	215,088	8,113,481

Authorized for issue by management of the Group and signed on its behalf by:


Tamas Hak-Kovacs,
Chairman of the Management Board

26 March 2020


Natalia Diuba,
Chief Accountant

26 March 2020

The accompanying notes on pages from 11 to 77 form an integral part of these consolidated financial statements.

Joint-Stock Company OTP Bank

Consolidated Statement of Cash Flows for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

	Notes	2019	2018
Cash flows from operating activities			
Interest received		4,843,858	4,067,586
Interest paid		(1,563,618)	(1,235,182)
Fee and commission received		1,695,811	1,445,122
Fee and commission paid		(392,952)	(297,109)
Net gain on foreign exchange and banking metals operations		236,591	227,450
Net gain on transactions with derivative financial instruments		167,162	166,613
Other income received		177,171	78,053
Operating expense paid		(1,775,680)	(1,507,226)
Cash flows from operating activities before movements in operating assets and liabilities		3,388,343	2,945,307
Changes in operating assets and liabilities			
Increase in due from banks		(483,132)	-
Increase in loans to customers		(4,077,017)	(5,442,089)
Increase in other assets		(68,134)	(33,918)
Increase in due to banks		187,026	4,139
Increase in customer accounts		10,126,857	1,386,129
Increase in other liabilities		160,849	40,557
Cash inflow/(outflow) from operating activities before income tax		9,234,792	(1,099,875)
Income taxes paid		(206,813)	-
Net cash inflow from operating activities		9,027,979	(1,099,875)
Cash flows from investing activities			
Purchase of property and equipment and intangible assets		(198,841)	(159,284)
Proceeds on sale of property and equipment, intangible assets, and investment property		11,964	4,891
Purchase of investments measured at fair value through other comprehensive income		(36,760,827)	(23,144,576)
Proceeds on sale and repayment of investments measured at fair value through other comprehensive income		34,291,919	22,766,422
Purchase of investments measured at amortized cost		(112,055,301)	(98,270,000)
Proceeds on repayment of investments measured at amortized cost		108,521,000	99,050,003
Net cash outflow from purchase of an entity		(60,151)	-
Net cash (outflow)/inflow from investing activities		(6,250,237)	247,456

Joint-Stock Company OTP Bank

Consolidated Statement of Cash Flows for the Year Ended 31 December 2019 (Continued) In Ukrainian Hryvnias and in thousands

	Notes	2019	2018
Cash flows from financing activities			
Proceeds on borrowings from international financial institutions		367,935	-
Repayment of lease liabilities		(154,803)	-
Net cash inflow from financing activities		213,132	-
Effect of changes in foreign exchange rates on cash and cash equivalents		(843,799)	(206,328)
Net increase/(decrease) in cash and cash equivalents		2,147,075	(1,058,747)
CASH AND CASH EQUIVALENTS, at the beginning of the year	9	4,827,585	5,886,332
CASH AND CASH EQUIVALENTS, at the end of the year	9	6,974,660	4,827,585

Authorized for issue by management of the Group and signed on its behalf by:

Tamas Hak-Kovacs,
Chairman of the Management Board

26 March 2020



Natalia Diuba,
Chief Accountant

26 March 2020

The accompanying notes on pages from 11 to 77 form an integral part of these consolidated financial statements.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

1. General information

JOINT STOCK COMPANY "OTP Bank" (the "Bank") is a bank with 100% foreign capital. On 1 June 2006, an agreement was signed on the sale of 100% shares in the Bank to Hungary-based Open Joint Stock Company "Central Savings and Commercial Bank" (hereinafter, "OTP Bank Plc." or the "Parent"). The permit of the Antimonopoly Committee of Ukraine was obtained on 15 August 2006. In accordance with Resolution of the Commission of the National Bank of Ukraine on Banking Supervision and Regulation # 266 dated 2 October 2006, OTP Bank Plc. also received the permission of the National Bank of Ukraine (the "NBU") on the purchase of 100% in the Bank's share capital.

On 7 November 2006, an entry was made to the State Register of Banks of Ukraine that recorded the revised Charter of Closed Joint Stock Company "OTP Bank" due to the change of the Bank's name from Joint Stock Commercial Bank "Raiffeisenbank Ukraine" to Closed Joint Stock Company "OTP Bank". This event followed the completed procedure on the purchase by OTP Bank Plc. of Joint Stock Commercial Bank "Raiffeisenbank Ukraine" that was founded on the basis of Incorporation and Activities Agreement of Joint Stock Commercial Bank "Raiffeisenbank Ukraine" dated 13 November 1997 and the Decision of the Bank's Constituent Meeting dated 28 November 1997.

Pursuant to the requirements of the Law of Ukraine "On Joint Stock Companies" # 514-VI dated 17 September 2008, as subsequently amended, and in accordance with the Decision of the General Shareholders' Meeting dated 23 April 2009 (Minutes of Meeting # 53), Closed Joint Stock Company "OTP Bank" changed its name to PUBLIC JOINT STOCK COMPANY "OTP Bank".

In accordance with the Decision of the General Shareholders' Meeting dated 5 April 2018 (Minutes of Meeting # 77), PUBLIC JOINT STOCK COMPANY "OTP Bank" changed the type of joint stock company of JSC "OTP Bank" from public to private and, correspondingly, amended its name to JOINT STOCK COMPANY "OTP Bank".

Registered address of the Bank and its location is at: 43 Zhylianska Str., Kyiv, 01033, Ukraine. The country of incorporation is Ukraine.

In its activities, the Bank is governed by the Laws of Ukraine "On Banks and Banking", "On Joint Stock Companies", "On Securities and Stock Market", "On Accounting and Financial Reporting in Ukraine", the Civil Code of Ukraine, the Commercial Code of Ukraine, other effective laws of Ukraine, as well as regulations issued by the NBU and other government authorities.

Participants (shareholders) of the Bank. As at 31 December 2019, the single shareholder of the Bank was represented by OTP Bank Plc., a legal entity duly incorporated under the laws of Hungary and located at: Nádor u. 16, Budapest, H-1051, Hungary.

The Parent, OTP Bank Plc., is a universal bank providing a full range of banking services to individuals and corporate clients. In Hungary, the OTP Group, one of the leading finance groups in the Hungarian banking market, comprises also large subsidiaries providing services in such spheres as insurance, real estate, factoring, leasing, and management of investment and pension funds.

OTP Bank Plc. was founded in 1949 as a state-owned savings bank. In late 1990, the bank was reorganized into a limited liability public company and renamed to National Savings and Commercial Bank. Upon privatization that commenced in 1995, the government share in the bank's equity reduced to one privileged ("golden") share. At present, most of the bank's shareholdings are owned by domestic and foreign investors, both private and institutional.

Corporate organization of the Bank. The Bank performs its activities through a regional network that consists of 88 non-accounting operational divisions (2018: 86 divisions) (with four of them having Regional Directorates registered by the NBU) and the Regional Directorate for Kyiv Region created within the structure of the Bank's Head Office. As at 31 December 2019, the number of the Bank's employees was 3,362 persons (2018: 3,437 persons).

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

1. General information (continued)

The Bank's licenses and permissions. Based on the License issued by the NBU # 191 dated 5 October 2011, the Bank provides a full range of banking services.

In accordance with the effective legislation and based on the respective licenses issued by the National Commission for Securities and Stock Market of Ukraine, the Bank may be involved in depositary activities as a securities custodian and professional trading in securities in stock market: brokerage, dealer, and underwriting activities. The Bank is not involved in any activities in the sphere of material production, trade, and insurance, other than acting as an insurance intermediary. The Bank is a full-fledged member of Individual Deposit Guarantee Fund.

The Bank's performance for the year ended 31 December 2019 is disclosed in the notes to these consolidated financial statements.

Structure of the Group of JOINT-STOCK COMPANY OTP Bank

The Bank is the Parent of the Group consisting of the following entities:

Name	Country of operations	Ownership interest/voting shares, %		Type of activities
		31 December 2019	31 December 2018	
JSC "OTP Bank" (Parent)	Ukraine			Banking
LLC "OTP Factoring Ukraine" (subsidiary)	Ukraine	100%	-	Collecting payments

LLC "OTP Factoring Ukraine" is the Bank's subsidiary. The Company operates on the basis of the Charter dated 1 February 2019. Principal activities of the Company presuppose rendering services on collecting payments and maintaining the bureau of credit histories.

The subsidiary's operating performance, as well as its assets and liabilities are included in these consolidated financial statements.

2. Operating environment

Since 2016, the Ukrainian economy has demonstrated signs of stabilization after years of political and economic tension. In 2019, the Ukrainian economy continued its recovery and achieved real GDP growth of around 3.6% (2018: 3.3%), modest annual inflation of 4.1% (2018: 9.8%), and stabilization of the national currency (appreciation of the national currency by around 5% to USD and 11% to EUR comparing to previous year averages).

Ukraine continues to limit its political and economic ties with Russia, given annexation of Crimea, an autonomous republic of Ukraine, and an armed conflict with separatists continued in certain parts of Luhanska and Donetska regions. As a result of this, the Ukrainian economy is refocusing on the European Union (the "EU") market by realizing potentials of established Deep and Comprehensive Free Trade Area with the EU.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

2. Operating environment (continued)

To further facilitate business activities in Ukraine, the NBU starting from 20 June 2019 has lifted the surrender requirement for foreign currency proceeds, cancelled all limits on repatriation of dividends since July 2019, and has gradually decreased its discount rate for the first time during the recent two years, from 18.0% in April 2019 to 11.0% in January 2020.

The degree of macroeconomic uncertainty in Ukraine in 2019 still remains high due to a significant amount of public debt scheduled for repayment in 2019-2020, which requires mobilizing substantial domestic and external financing in an increasingly challenging financing environment for emerging markets. At the same time, Ukraine has passed through the period of presidential and parliamentary elections. All newly elected authorities have demonstrated their commitment to introduce reforms in order to boost economic growth, while maintaining macro-fiscal stability and liberalizing economic environment. These changes have resulted in, inter alia, improved Fitch's rating of Ukraine's Long-Term Foreign- and Local-Currency Issuer Default Ratings from 'B-' to 'B', with a positive outlook.

Further economic growth depends, to a large extent, upon success of the Ukrainian government in realization of planned structural reforms and effective cooperation with the International Monetary Fund (the "IMF").

In addition to that, starting from early 2020 a new coronavirus disease (COVID-19) has begun rapidly spreading all over the world resulting in announcement of the pandemic status by the World Health Organization in March 2020. Responses put in place by many countries to contain the spread of COVID-19 are resulting in significant operational disruption for many companies and have significant impact on global financial markets. As the situation is rapidly evolving it may have a significant effect on business of many companies across a wide range of sectors, including, but not limited to such impacts as disruption of business operations as a result of interruption of production or closure of facilities, supply chain disruptions, quarantines of personnel, reduced demand and difficulties in raising financing. In addition, the Bank may face the increasingly broad effects of COVID-19 as a result of its negative impact on the global economy and major financial markets. The significance of the effect of COVID-19 on the Bank's business largely depends on the duration and the incidence of the pandemic effects on the world and Ukrainian economy.

3. Summary of significant accounting policies

Statement of compliance. These consolidated financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations issued by the International Financial Reporting Standards Interpretations Committee ("IFRS IC").

The consolidated financial statements are presented in Ukrainian Hryvnias and in thousands, unless otherwise indicated.

These consolidated financial statements have been prepared under the historical cost convention, except for the measurement at fair value of certain financial instruments.

In maintaining its accounting records, the Bank is governed by the Ukrainian legislation. These consolidated financial statements have been prepared from Ukrainian statutory accounting records maintained in accordance with the regulations of the NBU and have been adjusted to conform to IFRS. These adjustments to the consolidated financial statements include certain reclassifications to reflect the economic substance of underlying transactions, including reclassifications of certain assets and liabilities, income and expense to appropriate consolidated financial statements captions.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entity controlled by the Bank (its subsidiary) made up to 31 December each year. Control is achieved when the Bank:

- has the power over the investee;
- is exposed, or has rights, to variable return from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Bank reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Bank has less than a majority of the voting rights of an investee, it considers that it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally. The Bank considers all relevant facts and circumstances in assessing whether or not the Bank's voting rights in an investee are sufficient to give it power, including:

- the size of the Bank's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Bank, other vote holders or other parties;
- rights arising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Bank has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders' meetings.

Consolidation of a subsidiary begins when the Bank obtains control over the subsidiary and ceases when the Bank loses control of the subsidiary. Specifically, the results of subsidiaries acquired or disposed of during the year are included in the consolidated profit or loss account from the date the Bank gains control until the date when the Bank ceases to control the subsidiary.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring the accounting policies used into line with the Group's accounting policies.

All intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between the members of the Group are eliminated on consolidation.

Business combinations

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interest issued by the Group in exchange for control of the acquiree. Acquisition-related costs are recognised in profit or loss as incurred.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Group reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period (which cannot exceed one year from the acquisition date), or additional assets or liabilities are recognised, to reflect new information obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the amounts recognised as of that date.

Effects of business combinations of entities or businesses under common control are accounted for through equity.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Application of new Standards and amendments thereto

Impact on initial application of IFRS 16 "Leases"

In the current year, the Group has applied IFRS 16 "Leases" that is effective for annual periods that begin on or after 1 January 2019.

IFRS 16 introduces new or amended requirements with respect to lease accounting. It introduces significant changes to lessee accounting by removing the distinction between operating and finance lease and requiring the recognition of a right-of-use asset and a lease liability at commencement date for all leases, except for short-term leases and leases of low-value items. In contrast to lessee accounting, the requirements for lessor accounting have remained largely unchanged. The impact of adoption of IFRS 16 on the Group's separate financial statements is described below.

The date of initial application of IFRS 16 for the Group is 1 January 2019.

The Group has applied IFRS 16 retrospectively, with the recognized cumulative impact of the first application recognized at the date of initial application. Correspondingly, no restatement of comparable information was performed.

Impact of the new definition of a lease. The Group has made use of the practical expedient available on transition to IFRS 16 not to reassess whether a contract is or contains a lease. Accordingly, the definition of a lease in accordance with IAS 17 "Leases" and IFRIC 4 "Determining whether an Arrangement Contains a Lease" will continue to be applied to those leases entered or changed before 1 January 2019.

The Group applies the definition of a lease and related guidance set out in IFRS 16 to all lease contracts entered into or changed on or after 1 January 2019. In preparation for the first-time application of IFRS 16, the Group has carried out an implementation project. This project has shown that the new definition in IFRS 16 will not significantly change the scope of contracts meeting the definition of a lease for the Group.

Impact on lessee accounting

Operating leases: IFRS 16 changes how the Group accounts for leases previously classified as operating leases under IAS 17.

On initial application of IFRS 16, for all leases (except as noted below), the Group has:

- Recognized right-of-use assets and lease liabilities in the consolidated statement of financial position, initially measured at the present value of the future lease payments;
- Recognized depreciation of right-of-use assets and interest on lease liabilities in the consolidated statement of profit or loss and other comprehensive income;
- Separated the total amount of cash paid into a principal portion (presented within financing activities) and interest (presented within operating activities) in the consolidated statement of cash flows.

For short-term leases (lease term of 12 months or less) and leases of low-value assets (such as personal computers), the Group has opted to recognize a lease expense on a straight-line basis as permitted by IFRS 16. This expense is presented within operating expenses in profit or loss.

The Group has applied a single discount rate to a portfolio of leases with similar characteristics.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

3. Summary of significant accounting policies (continued)

Impact on Lessor Accounting

IFRS 16 does not change substantially how a lessor accounts for leases. Under IFRS 16, a lessor continues to classify leases as either finance leases or operating leases and account for those two types of leases differently.

However, IFRS 16 has changed and expanded the disclosures required, in particular regarding how a lessor manages the risks arising from its residual interest in leased assets.

Impact of initial application of IFRS 16 on the consolidated financial statements

As at 1 January 2019, the Group has recognized the right-of-use assets and lease liabilities in the amount of UAH 303,458 thousand.

As at 1 January 2019, the weighted average rate for discounting lease liabilities amounted to 18.37%.

The following table shows the operating lease commitments disclosed applying IAS 17 at 31 December 2018 discounted at the date of initial application and the lease liabilities recognized in the consolidated statement of financial position at the date of initial application.

	1 January 2019
Operating lease commitments at 31 December 2018	400,485
Present value of unpaid lease commitments	303,458
Short-term leases and leases of low-value assets	(10,007)
Effect of discounting	(87,020)
Lease liabilities as at 1 January 2019	303,458

Amendments to IFRS 9 "Financial Instruments" – Prepayment features with negative compensation

The Group has adopted the amendments to IFRS 9 for the first time in the current year. The amendments to IFRS 9 clarify that for the purpose of assessing whether a prepayment feature meets the 'solely payments of principal and interest' (SPPI) condition, the party exercising the option may pay or receive reasonable compensation for the prepayment irrespective of the reason for prepayment. In other words, financial assets with prepayment features with negative compensation do not automatically fail SPPI. The adoption of the amendment has not had any material impact on the Group's consolidated financial statements.

The application of the following amendments to Standards has not had any impact on the Group's financial position or performance and have not resulted in any changes in the Group's accounting policies and the amounts reported for the current or prior years:

- Amendments to IAS 28 "Investments in Associates and Joint Ventures" (issued on 12 October 2017 and effective for the annual periods beginning on or after 1 January 2019);
- Annual Improvements to IFRS Standards 2015–2017 Cycle – Amendments to IAS 12 "Income Taxes", IAS 23 "Borrowing Costs", IFRS 3 "Business Combinations", and IFRS 11 "Joint Arrangements" (issued on 12 December 2017 and effective for the annual periods beginning on or after 1 January 2019);
- Interpretation of IFRS IC 23 "Uncertainty over Income Tax Treatments" (issued on 7 June 2017 and effective for the annual periods beginning on or after 1 January 2019).

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Critical accounting judgments

Net interest income. Interest income and expense for all financial instruments, except for those classified as held for trading or those measured or designated as at fair value through profit or loss (FVTPL), are recognized in 'Net Interest Income' as 'Interest Income' and 'Interest Expense' in the consolidated statement of profit or loss and other comprehensive income using the effective interest rate method. Interest on financial instruments measured as at FVTPL is included within the fair value movement during the period.

The effective interest rate (EIR) is the rate that exactly discounts estimated future cash flows of the financial instrument through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. The future cash flows are estimated taking into account all the contractual terms of the instrument.

The calculation of the EIR includes all fees and points paid or received between parties to the contract that are incremental and directly attributable to the specific lending arrangement, transaction costs, and all other premiums or discounts. For financial assets at FVTPL, transaction costs are recognized in profit or loss at initial recognition.

The interest income/interest expense is calculated by applying the EIR to the gross carrying amount of non-credit impaired financial assets (i.e. at the amortized cost of the financial asset before adjusting for any expected credit loss allowance), or to the amortized cost of financial liabilities. For credit-impaired financial assets, the interest income is calculated by applying the EIR to the amortized cost of the credit-impaired financial assets (i.e. the gross carrying amount, less the allowance for expected credit losses (ECLs)). For financial assets purchased or originated credit-impaired (POCI), the EIR reflects the ECLs in determining the future cash flows expected to be received from the financial asset.

Fee and commission income/expense. Fee and commission income and expense include fees, other than those that are an integral part of EIR (see above). The fees included in this part of the Bank's separate statement of profit or loss and other comprehensive income include, among other things, fees charged for servicing a loan, non-utilization fees relating to loan commitments when it is unlikely that these will result in a specific lending arrangement and loan syndication fees.

Fee and commission expenses with regards to services are accounted for when the services are received.

Financial assets. All financial assets are recognized and derecognized on a trade date where the purchase or sale of a financial asset is under a contract whose terms require delivery of the financial asset within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at FVTPL. Transaction costs directly attributable to the acquisition of financial assets classified as at FVTPL are recognized immediately in profit or loss.

All recognized financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortized cost or fair value on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Specifically:

- Debt instruments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI), are subsequently measured at amortized cost;
- Debt instruments that are held within a business model whose objective is both to collect the contractual cash flows and to sell the debt instruments, and that have contractual cash flows that are SPPI, are subsequently measured at fair value through other comprehensive income ("FVTOCI");
- All other debt instruments (e.g., debt instruments managed on a fair value basis, or held for sale) and equity investments are subsequently measured at fair value through statement of profit and loss ("FVTPL").

Debt instruments at amortized cost or at FVTOCI. The Group assesses the classification and measurement of a financial asset based on the contractual cash flow characteristics of the asset and the Group's business model for managing the asset.

For an asset to be classified and measured at amortized cost or at FVTOCI, its contractual terms should give rise to cash flows that are solely payments of principal and interest on the principal outstanding (SPPI).

For the purpose of SPPI test, principal is the fair value of the financial asset at initial recognition. That principal amount may change over the life of the financial asset (e.g., if there are repayments of principal). Interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin. The SPPI assessment is made in the currency in which the financial asset is denominated.

Contractual cash flows that are SPPI are consistent with a basic lending arrangement. Contractual terms that introduce exposure to risks or volatility in the contractual cash flows that are unrelated to a basic lending arrangement, such as exposure to changes in equity prices or commodity prices, do not give rise to contractual cash flows that are SPPI. An originated or an acquired financial asset can be a basic lending arrangement irrespective of whether it is a loan in its legal form.

An assessment of business models for managing financial assets is performed at the date of initial application of IFRS 9 to determine the classification of a financial asset. The business model is applied retrospectively to all financial assets existing at the date of initial application of IFRS 9. The Group determines the business models at a level that reflects how groups of financial assets are managed together to achieve a particular business objective. The Group's business model does not depend on management's intentions for an individual instrument; therefore, the business model assessment is performed at a higher level of aggregation rather than on an instrument-by-instrument basis.

The Group has more than one business model for managing its financial instruments that reflect how the Group manages its financial assets in order to generate cash flows. The Group's business models determine whether cash flows will result from collecting contractual cash flows, selling financial assets, or both.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

The Group considers all relevant information available when making the business model assessment. However, this assessment is not performed based on scenarios that the Group does not reasonably expect to occur, such as so-called 'worst case' or 'stress case' scenarios. The Group takes into account all relevant evidence available, such as:

- How the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way in which those risks are managed; and
- How managers of the business are compensated (e.g., whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected).

At initial recognition of a financial asset, the Group determines whether newly recognized financial assets are part of an existing business model or whether they reflect the commencement of a new business model. The Group reassesses its business models each reporting period to determine whether the business models have changed since the preceding period. For the current reporting period, the Group has not identified a change in its business models.

When a debt instrument measured at FVTOCI is derecognized, the cumulative gain/loss previously recognized in OCI is reclassified from equity to profit or loss. In contrast, for an equity investment designated as measured at FVTOCI, the cumulative gain/loss previously recognized in OCI is not subsequently reclassified to profit or loss, but transferred within equity. Debt instruments that are subsequently measured at amortized cost or at FVTOCI are subject to impairment.

Financial assets at FVTPL. Financial assets at FVTPL are:

- Assets with contractual cash flows that are not SPPI; or/and
- Assets that are held in a business model, other than held to collect contractual cash flows or held to collect and sell; or
- Assets designated at FVTPL using the fair value option.

These assets are measured at fair value, with any gains/losses arising on re-measurement recognized in profit or loss.

Reclassifications. If the business model under which the Group holds financial assets changes, the financial assets affected are reclassified. The classification and measurement requirements related to the new category apply prospectively from the first day of the first reporting period following the change in business model that result in reclassifying the Group's financial assets. Changes in contractual cash flows are considered under the accounting policy on "Modification and De-recognition of Financial Assets" described below.

Impairment. The Group recognizes loss allowances for ECLs on the following financial instruments that are not measured at FVTPL:

- Cash and cash equivalents;
- Due from banks;
- Loans to customers;
- Investment securities;
- Other financial assets;
- Financial guarantee contracts issued and loan commitments.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

With the exception of POCI financial assets (which are considered separately below), ECLs are required to be measured through a loss allowance at an amount equal to:

- 12-month ECLs, i.e. lifetime ECLs that result from those default events on the financial instrument that are possible within 12 months after the reporting date (referred to as Stage 1); or
- Full lifetime ECLs, i.e. lifetime ECLs that result from all possible default events over the life of the financial instrument (referred to as Stage 2 and Stage 3).

A loss allowance for full lifetime ECLs is required for a financial instrument if the credit risk on that financial instrument has increased significantly since initial recognition. For all other financial instruments, ECLs are measured at an amount equal to the 12-month ECLs.

ECLs are a probability-weighted estimate of the present value of credit losses. These are measured as the present value of the difference between the cash flows due to the Group under the contract and the cash flows that the Group expects to receive arising from the weighting of multiple future economic scenarios, discounted at the asset's EIR.

- For undrawn loan commitments, the ECLs are the difference between the present value of the difference between the contractual cash flows that are due to the Group if the holder of the commitment draws down the loan and the cash flows that the Group expects to receive if the loan is drawn down; and
- For financial guarantee contracts, the ECLs are the difference between the expected payments to reimburse the holder of the guaranteed debt instrument less any amounts that the Group expects to receive from the holder, the debtor, or any other party.

The Group measures ECLs on an individual basis, or on a collective basis for portfolios of loans that share similar risk characteristics. The measurement of the loss allowance is based on the present value of the asset's expected cash flows using the asset's original EIR, regardless of whether it is measured on an individual basis or a collective basis.

Credit-impaired financial assets. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Credit-impaired financial assets are referred to as Stage 3 assets. Evidence of credit-impairment includes observable data about the following events:

- Significant financial difficulty of the borrower or issuer;
- A breach of contract such as a default or past due event;
- The lender of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession that the lender would not otherwise consider;
- The disappearance of an active market for a financial asset because of financial difficulties; or
- The purchase of a financial asset at a deep discount that reflects the incurred credit losses.

It may not be possible to identify a single discrete event instead; the combined effect of several events may have caused financial assets to become credit-impaired. The Group assesses whether debt instruments that are financial assets measured at amortized cost or FVTOCI are credit-impaired at each reporting date. To assess if sovereign debt instruments are credit impaired, the Group considers factors such as bond yields, credit ratings, and the ability of the borrower to raise funding.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

3. Summary of significant accounting policies (continued)

A loan is considered credit-impaired when a concession is granted to the borrower due to a deterioration in the borrower's financial condition, unless there is evidence that as a result of granting the concession the risk of not receiving the contractual cash flows has reduced significantly and there are no other indicators of impairment. For financial assets where concessions are contemplated but not granted, the asset is deemed credit impaired when there is observable evidence of credit-impairment, including meeting the definition of default. The definition of default (see below) includes unlikelihood to pay indicators and a backstop if amounts are overdue for 90 days or more.

Purchased or originated credit-impaired (POCI) financial assets. POCI financial assets are treated differently because the asset is credit-impaired at initial recognition. For these assets, the Bank recognizes all changes in lifetime ECLs since initial recognition as a loss allowance with any changes recognized in profit or loss. A favorable change for such assets creates an impairment gain.

Definition of default. Critical to the determination of ECLs is the definition of default. The definition of default is used in measuring the amount of ECLs and in the determination of whether the loss allowance is based on 12-month or lifetime ECLs, as default is a component of the probability of default (PD) which affects both the measurement of ECLs and the identification of a significant increase in credit risk.

The Group considers the following as constituting an event of default:

- The borrower is past due more than 90 days on any material credit obligation to the Group; or
- The borrower is unlikely to pay its credit obligations to the Group in full.

When assessing if the borrower is unlikely to pay its credit obligation, the Group takes into account both qualitative and quantitative indicators. The information assessed depends on the type of the asset, for example, in corporate lending, a qualitative indicator used is the breach of covenants, which is not relevant for retail lending. Quantitative indicators, such as overdue status and non-payment on another obligation of the same counterparty, are key inputs in this analysis. The Group uses a variety of sources of information to assess default, which are either developed internally or obtained from external sources.

Significant increase in credit risk. The Group monitors all financial assets, issued loan commitments, and financial guarantee contracts that are subject to the impairment requirements to assess whether there has been a significant increase in credit risk since initial recognition. If there has been a significant increase in credit risk, the Group will measure the loss allowance based on lifetime rather than 12-month ECLs.

In assessing whether the credit risk on a financial instrument has increased significantly since initial recognition, the Group compares the risk of a default occurring on the financial instrument at the reporting date based on the remaining maturity of the instrument with the risk of a default occurring that was anticipated for the remaining maturity at the current reporting date when the financial instrument was first recognized. In making this assessment, the Group considers both quantitative and qualitative information that is reasonable and supportable, including historical experience and forward-looking information that is available without undue cost or effort, based on the Group's historical experience and expert credit assessment including forward-looking information.

As a backstop when an asset becomes 30 days past due, the Group considers that a significant increase in credit risk has occurred and the asset is in Stage 2 of the impairment model, i.e. the loss allowance is measured as the lifetime ECLs.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Modification and de-recognition of financial assets. A modification of a financial asset occurs when the contractual terms governing the cash flows of a financial asset are renegotiated or otherwise modified between initial recognition and maturity of the financial asset. A modification affects the amount and/or timing of the contractual cash flows either immediately or at a future date. In addition, the introduction or adjustment of existing covenants of an existing loan would constitute a modification even if these new or adjusted covenants do not yet affect the cash flows immediately but may affect the cash flows depending on whether the covenant is or is not met (e.g., a change to the increase in the interest rate that arises when covenants are breached).

The Group renegotiates loans to customers in financial difficulty to maximize collection and minimize the risk of default. A loan forbearance is granted in cases where although the borrower made all reasonable efforts to pay under the original contractual terms, there is a high risk of default or default has already happened and the borrower is expected to be able to meet the revised terms. The revised terms in most of the cases include an extension of the maturity of the loan, changes to the timing of the cash flows of the loan (principal and interest repayment), reduction in the amount of cash flows due (principal and interest forgiveness), and amendments to covenants. The Group has an established forbearance policy, which applies for corporate and retail lending.

When a financial asset is modified, the Group assesses whether this modification results in de-recognition. In accordance with the Group's policy, a modification results in de-recognition when it gives rise to substantially different terms.

In the case where the financial asset is derecognized, the loss allowance for ECLs is re-measured at the date of de-recognition to determine the net carrying amount of the asset at that date. The difference between this revised carrying amount and the fair value of the new financial asset with the new terms will lead to a gain or loss on de-recognition. The new financial asset will have a loss allowance measured based on 12-month ECLs, except where the new loan is considered to be originated credit-impaired asset. This applies only in the case where the fair value of the new loan is recognized at a significant discount to its revised par amount because there remains a high risk of default, which has not been reduced by the modification.

The Group monitors credit risk of modified financial assets by evaluating qualitative and quantitative information, such as if the borrower is in past due status under the new terms.

When the contractual terms of a financial asset are modified and the modification does not result in de-recognition, the Group determines if the financial asset's credit risk has increased significantly since initial recognition.

For financial assets modified as part of the Group's forbearance policy, where modification did not result in de-recognition, the estimate of PD reflects the Bank's ability to collect the modified cash flows taking into account the Group's previous experience of similar forbearance action, as well as various behavioral indicators, including the borrower's payment performance against the modified contractual terms. If the credit risk remains significantly higher than what was expected at initial recognition, the loss allowance will continue to be measured at an amount equal to lifetime ECLs.

The loss allowance on forborne loans will generally only be measured based on 12-month ECLs when there is evidence of the borrower's improved repayment behavior following modification leading to a reversal of the previous significant increase in credit risk.

Where a modification does not lead to de-recognition, the Group calculates the modification gain/loss comparing the gross carrying amount before and after the modification (excluding the ECLs allowance). Then, the Group measures ECLs for the modified asset, where the expected cash flows arising from the modified financial asset are included in calculating the expected cash shortfalls from the original asset.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

The Group derecognizes a financial asset only when the contractual rights to the asset's cash flows expire (including expiry arising from a modification with substantially different terms), or when the financial asset and substantially all the risks and rewards of ownership of the asset are transferred to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognize the financial asset and also recognizes a collateralized borrowing for the proceeds received.

On de-recognition of a financial asset in its entirety, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain/loss that had been recognized in OCI and accumulated in equity is recognized in profit or loss, with the exception of equity investment designated as measured at FVTOCI, where the cumulative gain/loss previously recognized in OCI is not subsequently reclassified to profit or loss.

Write-off. Loans and debt securities are written off when the Group has no reasonable expectations of recovering the financial asset (either in its entirety or in a portion of it). This is the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. A write-off constitutes a de-recognition event. The Group may apply enforcement activities to financial assets written off. Recoveries resulting from the Bank's enforcement activities will result in impairment gains. Loans and debt securities written-off are still subject to enforcement activity. Amount of written-off loans and debt securities is disclosed in Note 5.

Presentation of allowance for ECLs in the consolidated statement of financial position. Loss allowances for ECLs are presented in the consolidated statement of financial position as follows:

- For financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- For debt instruments measured at FVTOCI: no loss allowance is recognized in the consolidated statement of financial position as the carrying amount is at fair value. However, the loss allowance is included as part of the revaluation amount in the investments revaluation reserve;
- For loan commitments and financial guarantee contracts: as a provision.

Financial liabilities. Financial liabilities are classified as either financial liabilities 'at FVTPL' or 'other financial liabilities'.

Other financial liabilities. Other financial liabilities, including deposits and borrowings, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortized cost using the effective interest rate method.

The effective interest rate method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. For details on EIR, see the "Net Interest Income" section above.

De-recognition of financial liabilities. The Group derecognizes financial liabilities when, and only when, the Group's obligations are discharged, cancelled, or have expired. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit or loss.

Financial guarantee contracts. A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Financial guarantee contracts issued by the Group are initially measured at their fair values and are subsequently measured at the higher of:

- The amount of the loss allowance determined in accordance with IFRS 9; and
- The amount initially recognized, less, where appropriate, cumulative amount of income recognized in accordance with the Group's revenue recognition policies.

Financial guarantee contracts are presented as provisions in the consolidated statement of financial position, and the re-measurement is presented in other revenue.

Going concern. These consolidated financial statements have been prepared assuming that the Group is a going concern and will continue operations for the foreseeable future. Management and shareholders are intending further develop the Group's operations in Ukraine. Management believes that the going concern assumption is appropriate for the Group's consolidated financial statements, considering its appropriate capital adequacy, the shareholders' intentions to support the Group, and the historical experience which evidences that current liabilities will be refinanced in the normal course of business.

Functional currency. Items included in the consolidated financial statements are measured using the currency that best reflects the economic substance of the underlying events and circumstances (the "functional currency"). The functional currency of these consolidated financial statements is Ukrainian Hryvnia ("UAH"). All amounts are rounded to the nearest UAH thousands, unless otherwise indicated.

Offsetting. Financial assets and financial liabilities are offset and the net amount reported in the consolidated statement of financial position only when there is a legally enforceable right to offset the recognized amounts, and there is an intention to settle on a net basis, or to realize the assets and settle the liability simultaneously. Income and expense are not offset in the consolidated statement of profit or loss and other comprehensive income unless required or permitted by any accounting Standard or Interpretation, and as specifically disclosed in the accounting policies of the Group. In accounting for the transfer of financial assets that do not result in de-recognition of such assets, the Group does not offset the assets transferred and the underlying liabilities.

Cash and cash equivalents. Cash and balances with the National Bank of Ukraine for the purposes of the consolidated statement of financial position include cash on hand and balances on correspondent and time deposit accounts with the NBU. For the purposes of the consolidated statement of cash flows, cash and cash equivalents include assets which may be converted to the respective cash amount within a short period of time, namely: cash on hand, unrestricted balances on correspondent accounts with the NBU, due from banks, and repurchase agreements with the original maturity within 90 days, except for guarantee deposits and other restricted balances. For the purposes of the consolidated statement of cash flows, the minimum reserve deposit required by the NBU is not included as a cash equivalent due to restrictions on its availability.

Repurchase and reverse repurchase agreements. Securities sold under repurchase agreements ("repos") are accounted for as collateralized financing transactions, and the securities sold continue to be carried in the consolidated statement of financial position, while the counterparty's liabilities are included in repayment amounts under the repurchase agreements within deposits and due from banks or current accounts and deposits from customers, as appropriate. The difference between selling and purchase back prices represents the interest expense and is recognized in profit or loss over the term of the purchase back agreement by using the effective interest rate method. Securities purchased under sale back agreements ("reverse repos") are accounted for as amounts receivable under the sale back agreements in due from banks or loans to customers, as appropriate. The difference between purchase and sale prices represents the interest income and is recognized in profit or loss over the term of the sale back agreement by using the effective interest rate method. In the event that assets purchased under reverse repurchase are sold to third parties, liabilities on the return of the securities are accounted for as liabilities and are measured at fair value.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Derivative financial instruments. In the normal course of business, the Group enters into various derivative financial instruments, including forwards and swaps to manage currency and liquidity risks and for trading purposes. Derivative financial instruments entered into by the Group are not designated as hedges and do not qualify for hedge accounting. Derivatives are initially recognized at fair value at the date a derivative contract is entered into and are subsequently re-measured to their fair value at each reporting date. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative.

Derivatives are included in other assets or other liabilities in the consolidated statement of financial position. Gains and losses resulting from these instruments are included in other income in the consolidated statement of profit or loss and other comprehensive income.

Taxation. Income tax expense represents the sum of the current and deferred tax expense.

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

Deferred income tax. Deferred income tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax assets are recognized to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized. Such assets are not recognized if the temporary difference arises from the initial recognition of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit.

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

Deferred tax is recognized in the consolidated statement of profit or loss and other comprehensive income, except when it relates to items related directly to equity, in which case the deferred tax is also recognized within equity.

Ukraine also has various other taxes which are assessed on the Group's activities. These taxes are included as a component of operating expenses in the consolidated statement of profit or loss and other comprehensive income.

Property and equipment and intangible assets. Property and equipment and intangible assets are carried at historical cost, less any accumulated depreciation or amortization and any recognized impairment losses.

Historical cost of property and equipment items consists of their original cost, including all expenditures directly attributable to the acquisition, delivery, installation, and commissioning of the assets.

All intangible assets of the Group have finite useful lives and include mainly software and licenses for the use of software products.

Depreciation and amortization are charged on the carrying value of property and equipment and intangible assets and are designed to write off assets over their estimated useful economic lives. They are calculated on a straight line basis.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

In 2019, the useful lives of property and equipment and intangible assets were reviewed, the useful lives of intangible assets were determined in accordance with the Provision on the Procedure of Accounting for Property and Equipment and Intangible Assets of JSC "OTP Bank".

An item of property and equipment and intangible assets is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset.

At each reporting date the Bank assesses whether there are any impairment indicators. Where carrying value exceeds this estimated recoverable amount, assets are written down to their recoverable amount.

Contingent assets. Contingent assets are not recognized in the consolidated statement of financial position, but are disclosed when an inflow of economic benefits is probable.

Contingent liabilities. Contingent liabilities are not recognized in the consolidated statement of financial position, but are disclosed unless the possibility of any outflow in settlement is remote.

Provisions for contingent liabilities. Provisions for contingent liabilities are recognized when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the obligation can be made. Provisions for contingent liabilities are measured in accordance with IAS 37 "Provisions, Contingent Liabilities, and Contingent Assets" and require estimates and judgments on behalf of management.

Equity instruments. An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Group are recognized at the proceeds received, net of direct issue costs.

Share capital and share premium. Contributions to share capital are recognized at cost. Share premium represents the excess of contributions over the nominal value of the shares issued. Gains and losses on sales of treasury stock are charged or credited to share premium.

Dividends on ordinary shares are recognized in equity as a reduction in the period in which they are declared.

Equity reserves. The reserves recorded in equity (other comprehensive income) in the Group's consolidated statement of financial position include a revaluation reserve which comprises changes in fair value of investments measured at FVTOCI.

Staff costs. Salary related costs, contributions to the state social funds, expense on annual paid vacations, payments of sick leaves, bonuses and non-cash benefits are accrued in the year when the respective services were provided by employees. In accordance with the requirements of the Ukrainian legislation, the Group makes contributions (payments) to the following state social funds: the State Pension Fund of Ukraine, social security, unemployment, and professional accident insurance funds.

Contributions paid to the state social funds are recognized as the Group's expense when incurred. Staff costs include amounts of provision for vacations and bonuses. The Group has no other obligations under post-retirement benefits or other significant compensated benefits requiring accrual.

Foreign currency transactions. The consolidated financial statements of the Group are presented in Ukrainian Hryvnias ("UAH"), the currency of the primary economic environment in which the Group operates (its functional currency). Monetary assets and liabilities denominated in currencies, other than the Group's functional currency (foreign currencies), are translated into UAH at the official exchange rates prevailing at the reporting date.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

3. Summary of significant accounting policies (continued)

The carrying amounts of assets and liabilities denominated in foreign currencies are carried in the consolidated statement of financial position at the official exchange rates prevailing at the dates of their origination and reassessed using the exchange rates at the reporting dates. Foreign currency denominated income and expense are recorded at the official exchange rates prevailing at the dates of their origination and not on settlement dates and, when a cash-basis method is applied, at the exchange rates on settlement dates. All gains and losses arising as a result of such translation are included in net gain/(loss) on foreign currency transactions.

Rates of exchange. The official exchange rates as at 31 December 2019 and 2018 used by the Group in the preparation of the consolidated financial statements were as follows:

	31 December 2019	31 December 2018
UAH/USD 1	23.686200	27.688264
UAH/EUR 1	26.422000	31.714138

Segment reporting. The Group defines the following operating segments of its activities: treasury segment, corporate business segment, medium and small business segment, retail business segment, and other transactions.

Adoption of new and revised IFRS

The Group has not applied the following new and revised IFRS that have been issued but are not yet effective:

Standards/Interpretations	Effective for the annual accounting periods beginning on or after
IFRS 17 "Insurance Contracts"	1 January 2023
Amendments to IFRS 10 and IAS 28 "Sale or Contribution of Assets between an Investor and its Associate or Joint Venture"	The effective date to be determined
Amendments to IFRS 3 "Definition of a business"	1 January 2020
Amendments to IAS 1 and IAS 8 "Definition of material"	1 January 2020
Amendments to References to the Conceptual Framework in IFRS Standards	1 January 2020
Annual Improvements to IFRSs (2010–2012 Cycle), Amendments to IAS 1 Classification of Liabilities as Current and Non-current	1 January 2022
Amendments to IFRS 9, IAS 39, and IFRS 7 "Interest Rate Benchmark Reform and its Effects on Financial Reporting"	1 January 2020

The new Standards listed in the table above are expected to have no significant impact on the Group's operations.

Areas of significant management judgment and sources of estimation uncertainty

The preparation of the consolidated financial statements in accordance with IFRS requires that management of the Group make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the reporting date, and the reported amount of income and expenses during the reporting period.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

3. Summary of significant accounting policies (continued)

Management evaluates its estimates and judgments on an ongoing basis. Management bases its estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

Significant assumptions

Business model assessment. Classification and measurement of financial assets depends on the results of the SPPI and the business model test. The Group determines the business model at a level that reflects how groups of financial assets are managed together to achieve a particular business objective. This assessment includes judgment reflecting all relevant evidence including how the performance of the assets is evaluated and their performance measured, the risks that affect the performance of the assets, and how these are managed and how the managers of the assets are compensated. The Group monitors financial assets measured at amortized cost or FVTOCI that are derecognized prior to their maturity to understand the reason for their disposal and whether the reasons are consistent with the objective of the business for which the asset was held. Monitoring is part of the Group's continuous assessment of whether the business model for which the remaining financial assets are held continues to be appropriate and if it is not appropriate whether there has been a change in business model and, so, a prospective change to the classification of those assets.

Significant increase in credit risk. ECLs are measured as an allowance equal to 12-month ECLs for Stage 1 assets, or lifetime ECLs assets for Stage 2 or Stage 3 assets. An asset moves to Stage 2 when its credit risk has increased significantly since initial recognition. IFRS 9 does not define what constitutes a significant increase in credit risk. In assessing whether the credit risk of an asset has significantly increased, the Group takes into account qualitative and quantitative reasonable and supportable forward looking information.

Establishing groups of assets with similar credit risk characteristics. When ECLs are measured on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics. The Group monitors the appropriateness of the credit risk characteristics on an ongoing basis to assess whether they continue to be similar. This is required in order to ensure that, should credit risk characteristics change, there is appropriate re-segmentation of the assets. This may result in new portfolios being created or assets moving to an existing portfolio that better reflects the similar credit risk characteristics of that group of assets. Re-segmentation of portfolios and movement between portfolios is more common when there is a significant increase in credit risk (or when that significant increase reverses) and so assets move from 12-month to lifetime ECLs, or vice versa, but it can also occur within portfolios that continue to be measured on the same basis of 12-month or lifetime ECLs, but the amount of ECL changes because the credit risk of the portfolios differs.

Models and assumptions used. The Group uses various models and assumptions in measuring fair value of financial assets, as well as in estimating ECLs. Judgment is applied in identifying the most appropriate model for each type of asset, as well as for determining the assumptions used in these models, including assumptions that relate to key drivers of credit risk.

Key sources of estimation uncertainty

The below are listed key estimations that the management have used in the process of applying the Group's accounting policies and that have the most significant effect on the amounts recognised in the consolidated financial statements.

Probability of default (PD). PD constitutes a key input in measuring ECLs. PD is an estimate of the likelihood of default over a given time horizon, the calculation of which includes historical data, assumptions, and expectations of future conditions.

Loss given default (LGD). LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, taking into account cash flows from collateral.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

3. Summary of significant accounting policies (continued)

Fair value of buildings and constructions obtained as collateral. The Group determines the cost of buildings and constructions (property) obtained as collateral under lending transactions at fair value. Since, as at 31 December 2019, there was no active real estate market for certain types of buildings and constructions available, and the existing property valuation standards and rules do not contain the procedure for measuring the market value of the property, in reality, when determining the value of the collateralized property, its assessed value is used which was arrived at mainly through the judgment of professional appraisers, and not from the analysis of market factors. Assessment of the fair value of property requires making judgments and using assumptions regarding comparability of property items and other factors. Considering the above, the allowance for loan impairment may be affected by the assessed property value applied. Accounting estimates related to the property appraisals in the absence of active market-based prices are considered to be a key source of uncertainty due to the fact that: (i) they are highly susceptible to change from period to period and (ii) a potential impact from recognition of such estimates may be material.

Estimation of a borrower's ability to repay the loan by using own funds. The Group assesses cash flows from business activities by analyzing the borrower's financial statements and assessing financial ratios (such as EBITDA, capital adequacy, etc.).

Fair value of the investments measured at FVTOCI. In measuring the fair value of investments, the Group uses market data to the extent they are available. In the absence of such data, the Group uses valuation models to determine the fair values of its financial instruments (see details in Note 25).

Lease period and the factor for discounting right-of-use assets and lease liabilities. The estimation of the lease period commonly involves material judgments on behalf of the Group on the ability to extend the lease, its potential cancellation by a lessee or a lessor, possible termination charges and other regulatory restrictions regarding the lease extension. The discount factor (or a lessee's incremental borrowing rate) is calculated on the basis of material judgments, since it is estimated as the interest rate that the lessee would agree to pay in order to borrow the funds for a similar period and by using similar collateral that are required to obtain the asset of the value similar to the right-of-use asset under similar economic conditions.

Initial recognition of related party transactions. In the course of normal business activities, the Group transacts with its related parties. IFRS 9 requires accounting for financial instruments at initial recognition at fair value. In view of absence of an active market for such transactions, to determine whether the transactions were performed at market or non-market prices, judgments are used. Such judgments are based on pricing for similar financial instruments and transactions therewith, including analysis of effective interest rates and parameters of the arrangements made.

Tax legislation. Due to the presence in the Ukrainian commercial legislation, and tax legislation in particular, of provisions allowing more than one interpretation, and also due to the practice developed in a generally unstable environment by the tax authorities of making arbitrary judgment of business activities, if a particular treatment based on management's judgment of the Group's business activities was to be challenged by the tax authorities, the Group may be assessed additional taxes, penalties, and interest. Tax records remain open to review by the tax authorities for three years.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

4. Net interest income before allowance for expected credit losses on interest-bearing assets

Net interest income, before allowance for expected credit losses on interest bearing assets, comprised:

	2019	2018
Interest income on financial assets measured at amortized cost:		
Interest income on financial assets:		
Interest income on loans to customers	4,444,283	3,566,556
Interest income on investments measured at amortized cost	433,937	366,983
Interest income on reverse repurchase agreements measured at amortized cost	58,705	-
Interest income on balances due from banks	82,828	79,483
Interest income on financial assets measured at FVTOCI:		
Interest income on investments measured at fair value through other comprehensive income	233,685	120,349
Total interest income	5,253,438	4,133,371
Interest expense		
Interest expense on financial liabilities measured at amortized cost:		
Interest expense on customer accounts	(1,578,175)	(1,220,828)
Interest expense on lease liabilities	(31,695)	(1,368)
Interest expense on due to banks and other financial institutions	(25,553)	(4,147)
Total interest expense	(1,635,423)	(1,226,343)
Net interest income before allowance for expected credit losses on interest-bearing assets	3,618,015	2,907,028

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

5. Allowance for expected credit losses

Movements in allowance for expected credit losses on interest-bearing assets were as follows:

	Due from banks	Loans to customers	Investments measured at fair value through other comprehensive income	Total
1 January 2018	157	6,536,485	28,105	6,564,747
Impairment losses on interest bearing assets	1,127	388,088	4,713	393,928
Effect of foreign exchange fluctuations	6	(77,976)	(1,154)	(79,124)
Write-off of assets	-	(317,502)	-	(317,502)
Effect of loan sales	-	(924,423)	-	(924,423)
Adjustment of interest income	-	67,490	-	67,490
31 December 2018	1,290	5,672,162	31,664	5,705,116
Impairment losses on interest bearing assets	(362)	128,916	17,140	145,694
Effect of foreign exchange fluctuations	(179)	(496,806)	(3,740)	(500,725)
Write-off of assets	-	(138,528)	-	(138,528)
Effect of loan sales	-	(818,668)	(9,374)	(828,042)
Adjustment of interest income	-	14,603	-	14,603
Other	-	(11,734)	-	(11,734)
31 December 2019	749	4,349,945	35,690	4,386,384

Loans to customers sold to factoring companies are disclosed in Note 11.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

6. Fee and commission income and expense

Fee and commission income and expense comprised:

	2019	2018
Fee and commission income		
Settlement and cash operations with clients	781,327	692,090
Plastic cards operations	316,824	247,217
Foreign currency transactions	298,433	290,357
Loans granted	122,283	83,561
Guarantees issued	80,170	61,844
Other income	96,774	70,053
Total fee and commission income	1,695,811	1,445,122
Fee and commission expense		
Plastic cards operations	(278,408)	(196,895)
Settlements	(58,554)	(53,930)
Agent fees	(31,564)	(31,773)
Other expense	(24,426)	(14,511)
Total fee and commission expense	(392,952)	(297,109)

7. Operating expense

Operating expense comprised:

	2019	2018
Staff costs	915,038	683,525
Depreciation and amortization	236,895	94,467
Salary related taxes and charges	167,119	123,028
Property and equipment maintenance	145,006	135,860
Contributions to Individual Deposit Guarantee Fund	97,642	81,215
Expense on customer acquisition	86,300	48,175
Costs of software use rights	70,686	80,239
Professional services	55,040	62,055
Advertising costs	49,986	48,835
Communication services	25,253	21,398
Write down of repossessed property to net realizable value	18,944	6,542
Security expenses	13,223	11,593
Operating leases	13,181	153,368
Taxes, other than income tax	13,013	10,017
Fines and penalties	7,993	123
Stationery	6,532	7,024
Business trips	6,238	4,802
Cash collection costs	5,208	6,146
Professional training	3,983	2,498
Other expenses	104,268	81,985
Total operating expense	2,041,548	1,662,895

Included in professional services for the year ended 31 December 2019 was remuneration to the auditor for the services, other than obligatory statutory audit services, in the amount of UAH 5,344 thousand.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

8. Income taxes

Temporary differences as at 31 December 2019 and 2018 were as follows:

	31 December 2019	31 December 2018
Deductible temporary differences:		
Allowance for expected credit losses	-	823,257
Provisions for liabilities	83,939	68,871
Property and equipment and intangible assets	78,832	74,504
Losses on sale of securities	50,108	9,536
Other temporary differences	2,380	8,916
Total deductible temporary differences	215,259	985,084
Net deferred income tax assets	38,747	177,315

The income tax rate applicable for the years ended 31 December 2019 and 2018 was 18%.

Reconciliation of income tax expense and accounting loss for the years ended 31 December 2019 and 2018 was as follows:

	2019	2018
Profit before income tax	3,224,487	2,401,724
Tax at the statutory tax rate	580,408	432,310
Tax effect of other permanent differences	(22,798)	(4,896)
Income tax expense	557,610	427,414
Current income tax expense	419,042	52,303
Deferred income tax expense	138,568	375,111
Income tax expense	557,610	427,414
	2019	2018
Deferred income tax assets		
At the beginning of the period	177,315	467,237
Impact on adoption of IFRS 9	-	84,576
Adjusted balance at the beginning of the period	177,315	551,813
Tax effect of changes in revaluation reserve for investments measured at fair value through other comprehensive income	-	613
Deferred income tax expense	(138,568)	(375,111)
At the end of the period	38,747	177,315

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

9. Cash and balances with the National Bank of Ukraine

	31 December 2019	31 December 2018
Balances with the National Bank of Ukraine	2,149,386	1,587,308
Cash	990,207	733,150
Total cash and balances with the National Bank of Ukraine	3,139,593	2,320,458

Cash and cash equivalents for the purposes of the consolidated statement of cash flows comprised the following:

	31 December 2019	31 December 2018
Cash and balances with the National Bank of Ukraine	3,139,593	2,320,458
Correspondent accounts with banks (Note 10):	3,069,562	2,489,606
In Ukraine	10,136	12,218
In OECD countries	2,904,430	2,415,257
In other countries	154,996	62,131
Loans under repo transactions	765,505	17,521
In Ukraine	765,505	17,521
Total cash and cash equivalents	6,974,660	4,827,585

10. Due from banks

Due from banks comprised:

	31 December 2019	31 December 2018
Correspondent accounts with banks	3,069,886	2,490,379
Loans under repo transactions	765,505	18,039
Loans to banks	473,828	-
Allowance for expected credit losses	(749)	(1,291)
Total due from banks	4,308,470	2,507,127

As at 31 December 2019 and 2018, the Group received securities that were used as a collateral under repo agreements in the amount of UAH 765,505 thousand and UAH 18,039 thousand, respectively.

As at 31 December 2019 and 2018, included in due from banks was accrued interest in the amount of UAH 2,066 thousand and UAH 1,487 thousand, respectively.

As at 31 December 2019, due from three banks for the total amount of UAH 2,469,941 thousand individually exceeded 10% of the Group's equity. As of 31 December 2018, due from three banks for the total amount of UAH 1,376,170 thousand individually exceeded 10% of the Group's equity.

As at 31 December 2019 and 2018, the maximum credit risk exposure on due from banks amounted to UAH 4,308,470 thousand and UAH 2,507,127 thousand, respectively.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

11. Loans to customers

Loans to customers comprised:

	31 December 2019	31 December 2018
Loans to legal entities and individual entrepreneurs	18,008,447	17,495,830
Consumer loans to individuals	8,172,464	6,106,219
Mortgage loans to individuals	2,395,346	3,359,928
Loans under repo agreements	696,130	184,113
Receivables under finance lease	542,564	583,837
Other loans to individuals	4,022	1,287
Loans to customers before allowance for expected credit losses	29,818,973	27,731,214
Less: Allowance for expected credit losses	(4,349,945)	(5,672,162)
Total loans to customers	25,469,028	22,059,052

As at 31 December 2019 and 2018, the Group received securities that were used as a collateral under repo agreements in the amount of UAH 696,130 thousand and UAH 184,113 thousand, respectively.

As at 31 December 2019 and 2018, included in loans to customers was interest accrued in the amount of UAH 1,098,339 thousand and 1,383,450 thousand, respectively.

Movements in allowance for expected credit losses are disclosed in Note 5.

Collateral and other instruments to mitigate credit risk. The amount and type of collateral required by the Group depend on its assessment of the credit risk exposure in respect of a specific counterparty. The Group has introduced basic acceptability principles for different types of collateral and assessment parameters. Main types of the collateral obtained include:

- For individual lending – residential property and other real estate, motor vehicles;
- For commercial lending – non-residential property, commercial property, other real estate assets, equipment, inventories and rights thereon, cash on deposit accounts.

The Group's management monitors the market value of collateral. If required, the Group re-assesses its value.

Revaluation of the collateral held by the Group, in the event its value differs significantly from the fair value, is performed by: a) determining the property's market value by independent certified appraisers or by the Group's employees possessing respective qualifications; b) adjusting the value of property groups against items with similar technical characteristics, designation, and operating conditions.

The Group does not hold any collateral which is allowed to sell or re-pledge in the event the collateral owner performs its obligations.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

11. Loans to customers (continued)

The table below summarizes the proportionate amounts of loans secured by collateral, rather than the fair value of the collateral itself:

	31 December 2019	31 December 2018
Guarantees	77,800	146,689
Secured loans:	17,484,800	16,077,621
Loans secured by other real estate	7,777,089	8,153,896
Loans secured by equipment, inventory, and rights thereon	6,112,782	4,818,033
Loans secured by residential properties	1,975,298	2,338,932
Loans secured by cash or guarantee deposits with the Bank	923,501	582,647
Loans secured by securities	696,130	184,113
Unsecured and uncollateralized loans	12,256,373	11,506,904
Loans to customers before allowance for expected credit losses	29,818,973	27,731,214
Less: Allowance for expected credit losses	(4,349,945)	(5,672,162)
Total loans to customers	25,469,028	22,059,052

The table below summarizes the proportionate amounts of impaired loans secured by collateral, rather than the fair value of the collateral itself:

	31 December 2019	31 December 2018
Secured loans:	3,296,407	4,070,781
Loans secured by other real estate	1,516,866	2,084,789
Loans secured by residential properties	1,338,455	1,605,742
Loans secured by equipment, inventory, and rights thereon	422,248	365,798
Loans secured by cash or guarantee deposits with the Bank	18,838	14,452
Unsecured and uncollateralized loans	2,113,166	3,191,602
Loans to customers before allowance for expected credit losses	5,409,573	7,262,383
Less: Allowance for expected credit losses	(3,855,878)	(5,212,157)
Total loans to customers	1,553,695	2,050,226

As at 31 December 2019 and 2018, almost all corporate loans (over 99% of loans to customers) were granted to the companies operating in Ukraine, which represents a significant geographical concentration in one region (Note 27).

As at 31 December 2019 and 2018, the Group granted loans to three groups of customers for the total amount of UAH 2,631,293 thousand and UAH 1,837,582 thousand, respectively, which individually exceeded 10% of the Group's equity.

As at 31 December 2019 and 2018, the maximum credit risk exposure on loans to customers amounted to UAH 25,469,028 thousand and UAH 22,059,052 thousand, respectively. As at 31 December 2019 and 2018, the maximum credit risk exposure on contingent lending commitments and undrawn credit lines amounted to UAH 9,374,069 thousand and UAH 5,437,308 thousand, respectively (Note 22). Credit quality of loans to customers is disclosed in Note 27.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019

In Ukrainian Hryvnias and in thousands

11. Loans to customers (continued)

As at 31 December 2019 and 2018, the maximum credit risk exposure on loans to customers registered in Crimea and Donetsk and Luhansk regions comprised the following:

	31 December 2019	31 December 2018
Loans to customers registered in Donetsk and Luhansk regions	493,469	674,076
Loans to customers registered in Crimea	-	86
Total loans to customers registered in Crimea and Donetsk and Luhansk regions, less allowance	493,469	674,162
Less: Allowance for expected credit losses on loans to customers registered in Donetsk and Luhansk regions	(493,321)	(414,275)
Less: Allowance for expected credit losses on loans to customers registered in Crimea	-	(56)
Total loans to customers registered in Crimea and Donetsk and Luhansk regions	148	259,831

As at 31 December 2019 and 2018, the maximum credit risk exposure on contingent lending commitments and undrawn credit lines granted by the Group to customers registered in Crimea and customers registered in Donetsk and Luhansk regions amounted to nil, UAH 1,074 thousand and UAH 334 thousand, UAH 19,462 thousand, respectively.

During 2019, the Group sold a portion of its loan portfolio the value of which, before allowance, amounted to UAH 989,150 thousand for UAH 170,482 thousand. As a result of the transaction, the allowances were written-off for the amount of UAH 818,668 thousand (Note 5). During the year ended 31 December 2018, the Group sold a portion of its loan portfolio the value of which, before allowance, amounted to UAH 1,046,959 thousand for UAH 122,536 thousand. As a result of the transaction, the allowances were written-off for the amount of UAH 924,423 thousand (Note 5).

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11. Loans to customers (continued)

As at 31 December 2019 and 2018, loans to customers included the finance lease receivables disclosed as follows:

	31 December 2019	
	Minimum lease payments	Present value of minimum lease payments
Receivables under finance leases		
Up to 1 year	109,949	53,284
From 1 to 2 years	400,845	348,018
From 2 to 3 years	54,936	43,850
From 3 to 4 years	30,223	22,491
From 4 to 5 years	58,066	53,213
Over 5 years	23,788	21,708
Total investments in finance leases	677,807	542,564
Unearned finance income on finance leases	(135,243)	-
Allowance for expected credit losses on finance leases	(83,220)	(83,220)
Net investments in finance leases	459,344	459,344
Current finance leases receivable		45,112
Non-current finance leases receivable		414,232
Net investments in finance leases		459,344

	31 December 2018	
	Minimum lease payments	Present value of minimum lease payments
Receivables under finance leases		
Up to 1 year	96,811	44,958
From 1 to 2 years	110,440	51,800
From 2 to 3 years	399,896	347,527
From 3 to 4 years	54,074	43,141
From 4 to 5 years	29,550	21,689
Over 5 years	81,642	74,722
Total investments in finance leases	772,413	583,837
Unearned finance income on finance leases	(188,576)	-
Allowance for expected credit losses on finance leases	(84,046)	(84,046)
Net investments in finance leases	499,791	499,791
Current finance leases receivable		38,486
Non-current finance leases receivable		461,305
Net investments in finance leases		499,791

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12. Investments measured at fair value through other comprehensive income

Investments measured at fair value through other comprehensive income comprised:

	31 December 2019	31 December 2018
Debt securities:		
- Government	3,647,425	1,133,150
- Corporate entities and banks	20,048	734
Debt securities measured at fair value through other comprehensive income	3,667,473	1,133,884
Allowance for expected credit losses	(35,690)	(31,664)
Total investments measured at fair value through other comprehensive income	3,631,783	1,102,220

As at 31 December 2019 and 2018, included in investments measured at fair value through other comprehensive income was accrued interest in the amount of UAH 99,972 thousand and UAH 14,808 thousand, respectively.

13. Investments measured at amortized cost

As at 31 December 2019 and 2018, investments measured at amortized cost included government debt securities in the amount of UAH 7,212,296 thousand and UAH 3,677,428 thousand, respectively.

As at 31 December 2019 and 2018, included in investments measured at amortized cost was accrued interest in the amount of UAH 12,314 thousand and UAH 7,440 thousand, respectively.

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14. Property and equipment and intangible assets

Property and equipment and intangible assets comprised the following:

	Buildings and other real estate	Furniture and equipment	Other non- current tangible assets	Vehicles	Construction in progress	Intangible assets	Total
Cost							
31 December 2017	133,565	324,400	110,059	15,961	32,721	469,219	1,085,925
Additions and internal transfers	75	71,571	16,956	11,716	8,631	67,424	176,373
Disposals	-	(9,815)	(6,556)	(1,372)	(5,174)	(13,841)	(36,758)
Impairment	(3,335)	-	-	-	-	-	(3,335)
31 December 2018	130,305	386,156	120,459	26,305	36,178	522,802	1,222,205
Additions and internal transfers	400	86,807	24,141	4,797	16,601	75,297	208,043
Additions as a result of acquisition of a subsidiary	327	2,835	34	2,162	-	5,191	10,549
Disposals	(664)	(12,262)	(2,056)	(1,743)	(8,794)	(4,312)	(29,831)
31 December 2019	130,368	463,536	142,578	31,521	43,985	598,978	1,410,966
Accumulated depreciation and amortization							
31 December 2017	21,048	238,592	95,222	8,692	-	317,225	680,779
Charges for the year	2,764	30,179	9,273	2,016	-	49,800	94,032
Eliminated on disposals	-	(9,735)	(6,556)	(1,372)	-	(13,841)	(31,504)
31 December 2018	23,812	259,036	97,939	9,336	-	353,184	743,307
Charges for the year	2,827	40,035	13,167	4,068	-	48,582	108,679
Additions as a result of acquisition of a subsidiary	239	2,075	33	1,922	-	4,589	8,858
Eliminated on disposals	(168)	(12,221)	(2,056)	(1,656)	-	(4,312)	(20,413)
31 December 2019	26,710	288,925	109,083	13,670	-	402,043	840,431
Net book value							
31 December 2019	103,658	174,611	33,495	17,851	43,985	196,935	570,535
31 December 2018	106,493	127,120	22,520	16,969	36,178	169,618	478,898

As at 31 December 2019 and 2018, included in property and equipment and intangible assets were fully depreciated property and equipment and amortized intangible assets in the amount of UAH 458,126 thousand and UAH 419,734 thousand, respectively.

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15. Right-of-use assets

Right-of-use assets comprised:

	Outlets and office premises	Apartments	Parking slots and storage facilities	Total
Cost				
1 January 2019	297,518	3,727	2,213	303,458
Additions and modifications	20,820	931	10	21,761
Additions as a result of acquisition of a subsidiary	3,006	-	-	3,006
Disposals	(28,445)	(1,554)	-	(29,999)
31 December 2019	292,899	3,104	2,223	298,226
Accumulated depreciation				
1 January 2019	-	-	-	-
Charges for the year	122,835	1,097	1,139	125,071
Additions as a result of acquisition of a subsidiary	2,918	-	-	2,918
Eliminated on disposals	(21,505)	(204)	-	(21,709)
31 December 2019	104,248	893	1,139	106,280
Net book value				
31 December 2019	188,651	2,211	1,084	191,946

During the year ended 31 December 2019, a portion of agreements under which right-of-use assets were derecognized amounted to 8%. New right-of-use assets under those agreements were not recognized.

During the year ended 31 December 2019, right-of-use assets had the following effect on the Group's financial performance:

	2019
Amounts recognized in profit or loss	
Depreciation of right-of-use assets	(127,989)
Operating expense on leases	(13,181)
Interest expense on leases	(31,736)
Gain on subleases of right-of-use assets	360
Total effect on financial performance	172,546

As at 31 December 2019, the average lease period of right-of-use assets was 25 months.

As at 31 December 2019, the Group had no lease contracts presupposing the purchase of assets at their nominal values.

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16. Other assets

Other assets comprised:

	31 December 2019	31 December 2018
Other financial assets before allowance for impairment	173,715	152,305
Less: Allowance for impairment	(20,516)	(12,248)
Total other financial assets	153,199	140,057
Other non-financial assets before allowance for impairment	80,845	130,936
Less: Allowance for impairment	(926)	(3,136)
Total other non-financial assets	79,919	127,800
Total other assets	233,118	267,857

17. Due to banks and other financial institutions

Due to banks and other financial institutions comprised:

	31 December 2019	31 December 2018
Borrowings from international financial institutions	378,133	315
Bank borrowings	189,542	-
Correspondent accounts of other banks	126	126
Total due to banks and other financial institutions	567,801	441

As at 31 December 2019 and 2018, included in due to banks and other financial institutions was accrued interest in the amount of UAH 13,689 thousand and UAH 1 thousand, respectively.

Borrowings from international financial institutions foresee certain financial and non-financial covenants. The management believes that the Group has complied with all covenants as at 31 December 2019 and during the year then ended.

The table below details changes in the Group's liabilities arising from financing activities, including both cash and non-cash changes. Liabilities arising from financing activities are those for which cash flows were, or future cash flows will be, classified in the Group's consolidated statement of cash flows as cash flows from financing activities.

	1 January 2019	Financing cash flows (i)	Other changes (ii)	31 December 2019
Borrowings from international financial institutions	315	367,935	9,883	378,133

- (i) The cash flows from borrowings from international financial institutions make up the net amount of proceeds from borrowings and repayments of borrowings in the consolidated statement of cash flows;
- (ii) Other changes include interest accruals and payments.

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18. Customer accounts

Customer accounts comprised:

	31 December 2019	31 December 2018
Current accounts and deposits repayable on demand	29,639,097	22,703,028
Term deposits	5,455,204	4,152,604
Total customer accounts	35,094,301	26,855,632

As at 31 December 2019 and 2018, included in customer accounts was interest accrued in the amount of UAH 81,999 thousand and UAH 61,180 thousand, respectively.

As at 31 December 2019 and 2018, customer accounts amounting to UAH 3,597,289 thousand (10.2%) and UAH 2,759,806 thousand (10.3%) were due to ten customers and twenty four customers, respectively, which represents a significant concentration.

As at 31 December 2019 and 2018, customer accounts amounting to UAH 1,180,806 thousand and UAH 710,622 thousand, respectively, were used as a collateral to secure for loans granted to customers, guarantees and letters of credit issued, and other transactions related to contingent obligations as follows:

	31 December 2019	31 December 2018
Loans to customers	1,017,094	628,939
Guarantees	163,712	81,683
Total customer accounts used as a collateral	1,180,806	710,622

19. Lease liabilities

Movements of lease liabilities in 2019 were as follows:

	2019
Initial recognition	303,458
Increase in lease liabilities	24,869
Interest accrued	31,695
Write-off of lease liabilities	(30,090)
Repayment of lease liabilities	(155,507)
Total lease liabilities as at 31 December 2019	174,425

Lease liabilities on the leases dependent on foreign exchange rate fluctuations at each reporting date are accounted for in relevant currencies. As at 31 December 2019, foreign currency denominated lease liabilities amounted to USD 2,863 thousand and EUR 32 thousand.

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19. Lease liabilities (continued)

The maturity profile of lease liabilities was as follows:

	31 December 2019
Lease liabilities	
Up to one year	91,363
More than one year, but less than two years	59,370
More than two years, but less than three years	17,000
More than three years, but less than four years	4,889
More than four years, but less than five years	1,803
Total lease liabilities	174,425

20. Other liabilities

Other liabilities comprised:

	31 December 2019	31 December 2018
Other financial liabilities		
Provision for unused vacations and bonuses	291,587	262,852
Transit and settlement accounts	252,470	175,544
Payables to other counterparties	44,960	28,412
Payables for property and equipment	7,485	13,342
Other	15,761	17,637
Total other financial liabilities	612,263	497,787
Other non-financial liabilities		
Allowance for losses on guarantees and other commitments	83,939	68,795
Deferred income	64,349	51,324
Payables on contributions to Individual Guarantee Deposit Fund	27,587	22,700
Taxes payable, other than income taxes	5,832	5,561
Other	-	92
Total other non-financial liabilities	181,707	148,472
Total other liabilities	793,970	646,259

21. Share capital, share premium, and other additional capital

As of 31 December 2019 and 2018, authorized and paid-in share capital consisted of 499,238 ordinary shares at par value of UAH 12,390.93 each.

All shares have been issued in a non-certificated form and are owned by one shareholder of the Group – OTP Bank Plc. – a legal entity under the laws of Hungary.

The Group has not issued any bearer and privileged shares.

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21. Share capital, share premium, and other additional capital (continued)

The Group's shareholders are entitled to:

- (i) Participate in the management of the Group in accordance with the procedures specified in the Group's Charter and internal regulations of the Group;
- (ii) Participate in distribution of the Group's profits and obtain its interest (dividends). The right to profits (dividends) is proportionate to the number of shares owned by respective shareholders at the beginning of dividends distribution;
- (iii) Receive complete and reliable information about the Group's activities;
- (iv) Use the shares held by them in accordance with the procedures determined by the effective legislation of Ukraine;
- (v) Purchase preemptively the shares additionally issued by the Group on a pro rata basis to the shareholder's interest in the Group's share capital in the event the Group conducts private placement of its shares;
- (vi) Propose on any issues included to the agenda of the Group's general shareholders' meetings;
- (vii) In the event of the Group's liquidation, receive a portion of the property value on a pro rata basis to their shareholdings.

The Group's distributable profits to shareholders are limited to the amount of its reserves as disclosed in its statutory accounts in accordance with the requirements to accounting and reporting of banking institutions in Ukraine. Non-distributable reserves are represented by a reserve fund which is created as required by the effective legislation and statutory regulations of the NBU in respect of general banking risks, including future losses and unforeseen risk contingencies. The Group's reserve is created upon the shareholders' decision in the amount envisaged by the law, provided the contributions amount to at least 5 percent of the Group's net profits. This reserve has been created in accordance with the Group's Charter.

As of 31 December 2019 and 2018, the share premium totaling to UAH 405,075 thousand represented an excess of contributions received over the nominal value of the shares issued.

In 2019 and 2018, all ordinary shares were ranked equally and carried one vote.

To comply with the requirements of the NBU, in 2009, the Group obtained a guarantee issued by the Parent. The guarantee was recognized by the Bank in the amount of UAH 1,632,338 thousand based on the guarantee agreement dated 23 December 2009 entered into with OTP Bank Plc.

In 2010, the guarantee agreement was canceled and OTP Bank Plc. paid the amount of USD 155,255 thousand to reimburse for it, which, as at 31 December 2019 and 2018, was accounted for in other additional capital in the amount of UAH 1,236,294 thousand.

During 2019 and 2018, the Group paid no dividends to its shareholder.

22. Contingencies and contractual commitments

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

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

The Group uses the same credit control and management policies in undertaking off-balance sheet commitments as it does for on-balance operations.

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22. Contingencies and contractual commitments (continued)

As of 31 December 2019 and 2018, the nominal or contractual amounts of contingent liabilities were as follows:

	31 December 2019	31 December 2018
Contingent liabilities and loan commitments		
Guarantees issued and similar commitments:	2,486,679	1,744,989
Guarantees issued	1,970,174	1,696,592
Import letters of credit	424,512	21,339
Avals	91,993	27,058
Irrevocable undrawn credit lines	6,971,329	3,761,114
Contingent liabilities and loan commitments before allowance for expected credit losses on guarantees and other liabilities	9,458,008	5,506,103
Less: Allowance for expected credit losses on guarantees and other liabilities	(83,939)	(68,795)
Total contingent liabilities and loan commitments	9,374,069	5,437,308

Legal proceedings. From time to time and in the normal course of business, customers and counterparties file claims to the Group. The Group's management believes that, as a result of legal proceedings, the Group will not incur significant losses.

Taxation. The Ukrainian economy is characterized by the increased tax burden and unexpectedness of the tax system. Banks act not only as taxpayers, but also perform functions of tax agents and intermediaries between taxpayers and the state, which increases tax risks.

Imperfect rule-making technique may lead to imposition of additional tax liabilities, fines, and penalties. The Group's management, based on its interpretation of the tax legislation, believes it has accrued all effective taxes.

As at 31 December 2019, the Group had no contingent obligations related to tax issues and no opened or pending legal cases in part of potential imposition of penalty sanctions.

23. Operating segments

Segment reporting format is based on the internal management accounting that reflects distribution of the Group's business by segments in accordance with management's responsibilities. Business segments are represented as independent business units that generate revenues and incur expenses, and operating performance of which is monitored by the Group's management on a regular basis.

Corporate business segment. Corporate business includes big corporations, government enterprises and institutions, ministries, local government authorities, transnational corporations, medium-size companies (with the annual turnover exceeding UAH 50 million), as well as finance industry companies: brokerage, insurance and leasing companies, credit unions, pension funds.

Medium and small business segment. Medium and small business segment covers medium-size companies (with the annual turnover of less than UAH 50 million), including professionals and individual entrepreneurs.

Retail business segment. Retail business segment covers private customers, including those using private banking services and the Group's employees.

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23. Operating segments (continued)

Treasury segment. Treasury segment includes relationships with international finance institutions, treasury and investment banking transactions trading in foreign currencies, and transactions with securities.

Other transactions. Other transactions are represented by all other transactions that are not attributable to business segments. "Other income" line is not allocated by segments and is allocated to the "other" segment. Interest expenses on lease liabilities are not allocated by segments and is reflected in segment "Other".

Methods. Methodology for calculating the operating segment profitability is based on transfer pricing methodology. Income and operating expense are calculated on an agreement-by-agreement basis or individual customer accounts, whereas administrative overheads are accounted for by cost centers and allocated by segments on a pro rata basis in accordance with the existing allocation methodology. Administrative overheads are allocated by using the following bases: number of employees, area of the space occupied (square meters), number of customers, agreements/accounts, and fixed interest determined with the help of expert appraisal. One of the key methodology principles contemplates that the total management results should be in line with the total financial performance of the Bank.

Net profit on foreign exchange operation is allocated to treasury as managing currency risk is performed by Treasury function.

One of the key criteria for assessment of the segment's profitability is profit before tax, the amount of which, within management reports, is monitored by the Group's management on a monthly basis.

Information about geographical areas. Information by geographical segments for 2019 and 2018 was not prepared, since, during the whole period of its existence, the Group operated solely within the territory of Ukraine.

Information about major customers. The Group has no significant concentrations of revenue generated from external customers.

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23. Operating segments (continued)

Information on profit/(loss), assets and liabilities of operating segments

	Year ended 31 December 2019					
	Corporate	SME	Retail	Treasury	Other	Total
Interest income on external customers	2,187,066	338,215	1,952,504	775,051	602	5,253,438
Interest expense on external customers	(953,668)	(137,519)	(486,947)	(25,553)	(31,736)	(1,635,423)
Intersegment interest margin on assets	(1,454,911)	(200,733)	(943,229)	(105,855)	-	(2,704,728)
Intersegment interest margin on liabilities	1,303,151	526,642	926,969	24,005	-	2,780,767
Marginal income on assets	732,155	137,482	1,009,275	669,196	602	2,548,710
Marginal income/(expense) on liabilities	349,483	389,123	440,022	(1,548)	(31,736)	1,145,344
Transformation results	-	-	-	(76,039)	-	(76,039)
Marginal income	1,081,638	526,605	1,449,297	591,609	(31,134)	3,618,015
Net fee and commission income	539,198	279,141	483,555	965	-	1,302,859
Trading result	-	-	-	384,588	-	384,588
Other income	-	-	-	-	165,598	165,598
GROSS INCOME	1,620,836	805,746	1,932,852	977,162	134,464	5,471,060
Allowance for expected credit losses, net loss on modification of financial assets	470,670	(364,074)	(270,488)	(10,940)	(30,193)	(205,025)
GROSS INCOME AFTER ALLOWANCE	2,091,506	441,672	1,662,364	966,222	104,271	5,266,035
Operating expense	(378,772)	(299,926)	(1,292,892)	(38,680)	(31,278)	(2,041,548)
PROFIT BEFORE TAX	1,712,734	141,746	369,472	927,542	72,993	3,224,487
Income tax expense	-	-	-	-	(557,610)	(557,610)
NET PROFIT/(LOSS)	1,712,734	141,746	369,472	927,542	(484,617)	2,666,877
Additions to property and equipment, intangible assets, and investment property	-	-	-	-	218,592	218,592
Depreciation and amortization	-	-	-	-	(236,895)	(236,895)
Impairment of property and equipment and investment property	-	-	-	-	(673)	(673)
ASSETS	15,705,688	2,181,304	7,582,035	15,152,551	4,207,227	44,828,805
LIABILITIES	14,651,301	6,169,747	14,273,253	567,801	1,053,222	36,715,324

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23. Operating segments (continued)

	Year ended 31 December 2018					
	Corporate	SME	Retail	Treasury	Other	Total
Interest income on external customers	2,049,753	161,223	1,355,580	566,815	-	4,133,371
Interest expense on external customers	(706,000)	(116,675)	(398,153)	(5,515)	-	(1,226,343)
Intersegment interest margin on assets	(1,329,679)	(116,048)	(640,182)	(570,040)	-	(2,655,949)
Intersegment interest margin on liabilities	1,108,975	434,031	759,810	4,731	-	2,307,547
Marginal income/(expense) on assets	720,074	45,175	715,398	(3,225)	-	1,477,422
Marginal income/(expense) on liabilities	402,975	317,356	361,657	(784)	-	1,081,204
Transformation results	-	-	-	348,402	-	348,402
Marginal income	1,123,049	362,531	1,077,055	344,393	-	2,907,028
Net fee and commission income	490,706	249,282	408,025	-	-	1,148,013
Trading result	-	-	-	321,850	-	321,850
Other income	-	-	-	-	97,632	97,632
GROSS INCOME	1,613,755	611,813	1,485,080	666,243	97,632	4,474,523
Allowance for expected credit losses, net loss on modification of financial assets	74,485	(70,813)	(401,176)	(5,515)	(6,885)	(409,904)
GROSS INCOME AFTER ALLOWANCE	1,688,240	541,000	1,083,904	660,728	90,747	4,064,619
Operating expense	(320,195)	(225,421)	(1,033,115)	(37,351)	(46,813)	(1,662,895)
PROFIT BEFORE TAX	1,368,045	315,579	50,789	623,377	43,934	2,401,724
Income tax expense	-	-	-	-	(427,414)	(427,414)
NET PROFIT/(LOSS)	1,368,045	315,579	50,789	623,377	(383,480)	1,974,310
Additions to property and equipment, intangible assets, and investment property	-	-	-	-	177,678	177,678
Depreciation and amortization	-	-	-	-	(94,467)	(94,467)
Impairment of property and equipment and investment property	-	-	-	-	(3,776)	(3,776)
ASSETS	15,301,804	945,260	5,812,066	7,288,224	3,409,784	32,757,138
LIABILITIES	10,968,238	5,091,275	10,796,119	5,013	641,687	27,502,332

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24. Related party transactions

In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely the legal form.

The Group had the following balances outstanding as at 31 December 2019 and 2018 with its related parties:

	31 December 2019		31 December 2018	
	Related party balances	Total category as per consolidated financial statements caption	Related party balances	Total category as per consolidated financial statements caption
Due from banks	1,073,699	4,308,470	696,170	2,507,127
- Parent	918,703		634,039	
- Entities under joint control or significant influence	154,996		62,131	
Loans to customers before allowance for expected credit losses	1,162,344	29,818,973	698,250	27,731,214
- Entities under joint control or significant influence	1,160,011		697,628	
- Key management personnel	2,333		622	
Allowance for expected credit losses on loans to customers	(7,573)	(4,349,945)	(4,503)	(5,672,162)
- Entities under joint control or significant influence	(7,516)		(4,500)	
- Key management personnel	(57)		(3)	
Other assets	87	233,118	663	267,857
- Parent	6		468	
- Entities under joint control or significant influence	81		195	
Due to banks and other financial institutions	108	567,801	126	441
- Parent	106		124	
- Entities under joint control or significant influence	2		2	
Customer accounts	331,013	35,094,301	217,138	26,855,632
- Entities under joint control or significant influence	290,850		184,340	
- Key management personnel	40,163		32,798	
Other liabilities	55,612	793,970	52,024	646,259
- Parent	7,489		2,720	
- Entities under joint control or significant influence	17,453		19,937	
- Key management personnel	30,670		29,367	
Irrevocable commitments on loans and undrawn credit lines	1,373	6,971,329	50,098	3,761,114
- Entities under joint control or significant influence	-		49,839	
- Key management personnel	1,373		259	

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24. Related party transactions (continued)

Included in the consolidated statement of profit or loss and other comprehensive income for the years ended 31 December 2019 and 2018 were the following amounts which arose due to the transactions with related parties:

	2019		2018	
	Related party transactions	Total category as per consolidated financial statements caption	Related party transactions	Total category as per consolidated financial statements caption
Interest income	143,218	5,253,438	109,678	4,133,371
- Parent	1,455		2,329	
- Entities under joint control or significant influence	141,613		107,237	
- Key management personnel	150		112	
Interest expense	(3,309)	(1,635,423)	(7,456)	(1,226,343)
- Entities under joint control or significant influence	(2,662)		(6,138)	
- Key management personnel	(647)		(1,318)	
Fee and commission income	4,167	1,695,811	3,849	1,445,122
- Parent	373		27	
- Entities under joint control or significant influence	3,794		3,822	
Fee and commission expense	(7,644)	(392,952)	(7,910)	(297,109)
- Parent	(7,569)		(7,862)	
- Entities under joint control or significant influence	(75)		(48)	
Net gain/(loss) on foreign exchange and precious metals operations	(348,124)	176,917	96,894	152,056
- Parent	(335,946)		84,364	
- Entities under joint control or significant influence	(12,178)		12,530	
Net gain on transactions with derivative financial instruments	70,692	164,169	119,093	164,224
- Parent	70,692		119,093	
Allowance for expected credit losses on interest-bearing assets	(3,032)	(145,694)	(192)	(393,928)
- Entities under joint control or significant influence	(3,015)		(327)	
- Key management personnel	(17)		135	
Other income	139	165,598	430	97,632
- Entities under joint control or significant influence	139		430	
Operating expense	(170,304)	(2,041,548)	(180,146)	(1,662,895)
- Parent	(8,995)		(10,156)	
- Entities under joint control or significant influence	(70,686)		(85,546)	
- Key management personnel	(90,623)		(84,444)	

During the years ended 31 December 2019 and 2018, remuneration to key management personnel comprised short-term benefits in the amount of UAH 90,623 thousand and UAH 84,444 thousand, respectively.

Financial instruments recognized as a result of transactions with related parties are initially recognized at fair value by using management judgments.

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25. Fair value of financial instruments

IFRS define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Fair value of the Group's financial assets and financial liabilities measured at fair value on a recurring basis

Some of the Group's financial assets and financial liabilities are measured at fair value at the end of each reporting period. The following table provides information about how the fair values of these financial assets and financial liabilities are determined (in particular, the valuation technique(s), and inputs used):

Financial assets/ financial liabilities	Fair value as at		Fair value hierarchy	Valuation technique(s) and key inputs
	31 December 2019	31 December 2018		
1) Derivative financial assets	454	2,183	Level 2	Discounted cash flows. Future cash flows are estimated based on forward exchange rates (from observable forward exchange rates at the end of the reporting period) and contractual forward rates discounted at a rate that reflects the credit risk of various counterparties
2) Investments measured at fair value through other comprehensive income	1,519,603	400,009	Level 1	Quoted bid prices in an active market
3) Investments measured at fair value through other comprehensive income	2,092,862	702,211	Level 2	Discounted cash flows. Future cash flows are estimated based on the inputs that are observable, either directly or indirectly, and the estimates use one or more observable quoted prices for orderly transactions in the markets that are not considered active

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25. Fair value of financial instruments (continued)

Financial assets/ financial liabilities	Fair value as at		Fair value hierarchy	Valuation technique(s) and key inputs
	31 December 2019	31 December 2018		
4) Investments measured at fair value through other comprehensive income	19,318	-	Level 3	The Group engages property appraisers to determine the fair value of buildings and land (being the most significant assets forming the fair value of the investment) by using the sales comparable approach, and for items for which there are no market analogs, the income approach is applied. In the sales comparable approach, the prices of market-based sales of comparable property and land plots in the immediate proximity are adjusted with reference to differences in main parameters (such as floor space of the property). The main parameter used in this valuation technique is the price per square meter of a property item or a land plot.
5) Derivative financial liabilities	3,447	4,572	Level 2	Discounted cash flows. Future cash flows are estimated based on forward exchange rates (from observable forward exchange rates at the end of the reporting period) and contractual forward rates discounted at a rate that reflects the credit risk of various counterparties

Securities are transferred between levels of fair value hierarchy when methods of their valuation change. Transfers from Level 1 occur when, as at the reporting date, there are no market quotations that were available as at the previous reporting date. In addition, if valuation as at the reporting date uses the present value of cash flows based on the observable market data, then such securities are included into Level 2 of the fair value hierarchy. In the event the information used differs from the observable market data, then such securities are included into Level 3 of the fair value hierarchy. Transfers from Levels 2 and 3 to Level 1 take place when, as at the reporting date, the securities have market prices in an active market, which were not available as at the previous reporting date.

As at 31 December 2019 and 2018, there were no transfers between the levels of fair value hierarchy.

Fair value of financial assets and financial liabilities that are not measured at fair value on a recurring basis (but fair value disclosures are required)

Management considers that the carrying amounts of financial assets and financial liabilities recognized in the consolidated financial statements approximately equals their fair values.

The fair values of foreign currency denominated loans to individuals cannot be measured reliably, since, due to the regulatory limitations introduced by the NBU, the market for those financial instruments during 2019 and 2018 was not available, and it is impracticable to obtain sufficient market data or apply any other valuation technique to such instruments. As at 31 December 2019 and 2018, the carrying amounts of such loans were UAH 56,763 thousand and UAH 88,158 thousand, respectively.

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26. Capital management

The Group's objectives in its capital management are to:

- 1) Comply with the requirements to the capital established by the NBU;
- 2) Be able to operate and develop in accordance with the Group's strategic plans;
- 3) Cover adverse consequences of varied risks assumed by the Group in the course of its operations;
- 4) Maintain a sufficient capital base at the level required to ensure the capital adequacy at the level of at least 8% under the Basel Accord.

The Group's policies in respect of the capital management include determining the effective level of its capital that ensure its long-term value for the shareholder, i.e. establishing objectives and rules of the Group's capital management in order to optimize the shareholders' requirements to their investments in meeting the following restrictions:

- Comply with the capital requirements established by supervisory authorities;
- The capital level that meets the requirements of investors and rating agencies in ensuring the Group's access to funds in global and domestic capital markets.

To determine an actual level of the capital considering its business risks, the Group consistently monitors the quality of its assets and off-balance liabilities, adjusts correspondingly their values by creating provisions for estimated (potential) losses from counterparties' obligations.

A quantitative capital assessment is complemented by qualitative, comprehensive discussions. The respective results are summarized in the form of goals regarding the required level of capital, including strategic objectives as to the ways of maintaining its sufficient level.

The capital structure of the Group consists of instruments and equity, comprising share capital, share capital in the process of registration, reserves, and other additional capital as disclosed in the consolidated statement of changes in equity.

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26. Capital management (continued)

The following table analyzes the Group's regulatory capital resources for capital adequacy purposes in accordance with the principles employed by the Basel Committee:

	31 December 2019	31 December 2018
Movements in Tier 1 capital		
As at the beginning of the year	5,254,806	3,242,442
Reserves disclosed	2,858,675	2,012,364
As at the end of the year	8,113,481	5,254,806
Composition of regulatory capital		
Tier 1 capital:		
Share capital	6,186,023	6,186,023
Share premium	405,075	405,075
Other additional capital	1,236,294	1,236,294
Reserves disclosed	286,089	(2,572,586)
Total qualifying Tier 1 capital	8,113,481	5,254,806
Total regulatory capital	8,113,481	5,254,806
Capital adequacy ratios:		
Tier 1 capital	20.9%	18.4%
Total capital	20.9%	18.4%

Quantitative measures established by regulation to ensure capital adequacy require that the Bank maintain minimum amounts and ratios of total (8%) and Tier 1 capital (4%) to risk weighted assets.

27. Risk management policies

Management of risks is fundamental to the Group's banking activities and is an essential element of the Group's operations. The main risks inherent to the Group's operations are those related to:

- Credit risk;
- Liquidity risk;
- Market risk.

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

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27. Risk management policies (continued)

Credit risk. The Group is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Credit risk management and monitoring is performed, within set limits of authority, by Risk Management Directorate, Credit Committees, and other collective decision-making committees, and the Group's management within their responsibilities.

Before any application is reviewed by Credit Committee, all recommendations on credit processes (borrower's limits approved, amendments made to loan agreements, etc.) are reviewed and approved by Risk Management Department. Daily risk management is performed by an appropriate department within Risk Management structure.

The Group structures levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to borrowers, products, and other segments. Limits on the structure of the loan portfolio are set by respective department within the Department of Integrated Risk Management and are approved by Assets and Liabilities Management Committee. Actual exposures against limits are monitored on a daily basis.

In the case of most loans in accordance with the internal regulations, the Group obtains collateral and corporate and personal guarantees. However, a significant portion of loans is represented by loans to individuals, where such facilities cannot always be obtained. Such risks are monitored on a continuous basis and subject to annual or more frequent reviews.

Credit risk on off-balance sheet financial instruments is defined as a probability of losses due to the inability of a counterparty to comply with contractual terms and conditions. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to a loss in the amount equal to the total unused commitments. However, the likely amount of the loss is less than the total unused commitments, since most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group applies the same credit policy to the contingent liabilities as it does to the off-balance sheet financial instruments, i.e. using limits to mitigate the risk and continuous monitoring.

The Group monitors the term to maturity on off-balance sheet contingencies because longer term commitments generally have a greater degree of credit risk than short-term commitments.

Significant increase in credit risk. Credit risk assessment is performed from the date of initial recognition till the date of de-recognition. The Group recognizes expected credit losses on financial assets as the first stage of impairment ("Stage 1") if, at the reporting date, the credit risk of financial assets has not increased significantly from their initial recognition. The Group recognizes expected credit losses on financial assets as the second stage of impairment ("Stage 2") if, at the reporting date, the credit risk of financial assets has increased significantly from their initial recognition.

The main factors that indicate that a significant increase in credit risk occurred are:

- Overdue payments for the period of over 30 calendar days;
- Restructuring;
- A substantial devaluation of the national currency against the exposure currency without relevant foreign currency denominated collateral;
- Deterioration of the financial asset's rating to the specified level/to the relevant level or, in comparison with the historical value, to the determined level;
- For mortgage loans, the ratio of debt to collateral exceeding 125%;
- Existing default indicators under other financial asset of the Retail Business borrower;
- As a result of the monitoring process with the use of the Early Warning system, financial assets of the Corporate Business borrower are assigned a worse risk status.

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27. Risk management policies (continued)

The Group recognizes expected credit losses on financial assets as the third stage of impairment ("Stage 3") if, at the reporting date, the financial assets have objective evidence of impairment. Stage 3 financial assets are the financial assets in respect of which there is objective evidence of expected loss or one or more events are observed that have a negative impact on the expected cash flows under such financial assets.

The main indicators that evidence for inclusion of financial assets to Stage 3 include:

- Significant financial difficulties of the counterparty/issuer;
- Breach of the contract terms, such as default or past due payment meeting the default definition;
- Provision by the Group of favorable terms to a borrower for economic reasons related to financial difficulties of the borrower that the Group would not otherwise consider;
- A high probability of a bankruptcy or other financial reorganization;
- The market becomes inactive for a financial asset as a result of financial difficulties;
- Acquisition or origination of a financial asset with significant discount which reflects incurred credit losses;
- As a result of the monitoring process with the use of the Early Warning system, business lines of the Corporate Business borrower is assigned the worst risk status.

The Group considers a comprehensive effect of several events that cannot be identified as a single event that has caused impairment.

Internal ratings. Financial assets are graded as follows: amounts due from banks are graded according to the current credit ratings issued by internationally reputable rating agencies, and, in their absence, according to the rating system internally developed by the Group; investments are graded in accordance with the current credit rating of Ukraine assigned by internationally regarded agencies; loans to customers are graded according to the rating system developed by the Group.

Credit risk of financial assets is assessed on an individual or portfolio basis. Financial assets for the purpose of calculating expected credit losses are divided into significant and insignificant. Significant assets include corporate clients whose amounts due, at the measurement date, exceed the equivalent of EUR 400 thousand. Loans that are treated as insignificant and possessing similar credit risk characteristics are assessed on a portfolio basis, and others – on an individual basis.

Incorporation of forward-looking information. The Group uses forward-looking information that is available without undue cost or effort in its assessment of significant increase of credit risk as well as in its measurement of ECLs. The Group involves experts of the OTP Group who use external and internal information to generate a 'base case' scenario of future forecast of relevant economic variables along with a representative range of other possible forecast scenarios. The external information used includes economic data and forecasts published by governmental bodies and monetary authorities. Factors that are taken into attention within this process include macroeconomic data, such as increase in GDP, export and investments.

The Group applies probabilities to the forecast scenarios identified. The base case scenario is the single most-likely outcome and consists of information used by the Group for strategic planning and budgeting. The Group uses external and internal information for building the 'base case' scenario of estimated economic variables together with a representative range of other forward-looking scenarios. External information applied includes economic data and forecasts published by government statistical bodies.

The Group uses probabilities for identified scenarios. The Group has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using a statistical analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses. The Group has not made changes in the estimation techniques or significant assumptions made during the reporting period.

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27. Risk management policies (continued)

Measurement of ECLs. The key inputs used for measuring ECLs are:

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

As explained above, these figures are generally derived from internally developed statistical models and other historical data and they are adjusted to reflect probability-weighted forward-looking information.

PD is an estimate of the likelihood of default over a given time horizon. It is estimated as at a point in time. The calculation is based on statistical rating models. These statistical models are based on market data (where available), as well as internal data comprising both quantitative and qualitative factors. The estimation is based on historical information and current conditions, adjusted to take into account estimates of future conditions that will impact PD.

LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, taking into account cash flows from any collateral. The LGD models for secured assets consider: collateral coverage, sale discounts, time to realization of collateral, cost of realization of collateral, and historical data about level and time of recovery. LGD models for unsecured assets consider time of recovery and recovery rates after default.

EAD is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, and expected drawdowns on committed facilities. The Group's modelling approach for EAD reflects expected changes in the balance outstanding over the lifetime of the loan exposure that are permitted by the current contractual terms, such as repayment in accordance with the contractual schedule, changes in utilization of undrawn commitments, and credit mitigation actions taken before default.

The Group measures ECLs considering the risk of default over the maximum contractual period (including extension options) over which the Group is exposed to credit risk and not a longer period, even if contact extension or renewal is common business practice.

The measurement of ECLs is based on probability weighted average credit loss. As a result, the measurement of the credit risk should be the same regardless of whether it is measured on an individual basis or a collective basis (although measurement on a collective basis is more practical for large portfolios of items).

For the purposes of assessing expected credit losses for loans to customers, other financial assets, due from banks that are subject to impairment requirements under IFRS 9, the Group allocates those financial assets into five risk levels, depending on the days past due and default indicators, in particular:

	Loans to customers	Financial accounts receivable	Due from banks
LEVEL 1	Not past due (DPD = 0)	Not past due (1–5 days)	Not past due (DPD = 0)
LEVEL 2	1–30 days past due	6–30 days past due	1–3 days past due
LEVEL 3	31–60 days past due	31–60 days past due	4–5 days past due
LEVEL 4	61–90 days past due	61–90 days past due	6–7 days past due
LEVEL 5 (default)	Default status	Default status	Default status

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27. Risk management policies (continued)

For the purposes of assessing expected credit losses for investments that are subject to impairment requirements under IFRS 9, the Group allocates those assets to four risk levels in accordance with the ratings assigned by international rating agencies (Fitch, Moody's, S&P). Level 1 corresponds to ratings from AAA to A-, Level 2 corresponds to ratings from BBB+ to B-, Level 3 corresponds to ratings from CCC+ to CCC-, and Level 4 (default) corresponds to rating CC.

An analysis of the Group's **credit risk exposure per class of financial asset, internal rating, and "stage"** is provided in the following tables. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For contingent and loan commitments, the amounts in the table represent the amounts committed.

As at 31 December 2019				
	Stage 1 12-months ECLs	Stage 2 Lifetime ECLs	Stage 3 Lifetime ECLs	Purchased or originated credit impaired financial instruments
Loans to customers				
LEVEL 1	22,153,216	1,677,887	1,676,130	469,868
LEVEL 2	268,524	169,735	27,638	41,894
LEVEL 3	-	96,779	31,808	17,708
LEVEL 4	-	43,259	8,983	10,525
LEVEL 5 (default)	-	-	2,807,261	317,758
Total	22,421,740	1,987,660	4,551,820	857,753
As at 31 December 2018				
	Stage 1 12-months ECLs	Stage 2 Lifetime ECLs	Stage 3 Lifetime ECLs	Purchased or originated credit impaired financial instruments
Loans to customers				
LEVEL 1	17,986,451	2,050,680	2,158,222	683,273
LEVEL 2	281,054	88,054	51,568	300,100
LEVEL 3	-	40,821	26,471	93,841
LEVEL 4	-	21,771	21,469	11,625
LEVEL 5 (default)	-	-	3,826,512	89,302
Total	18,267,505	2,201,326	6,084,242	1,178,141

Gross carrying value of due from banks as at 31 December 2019 and 2018 was at Stage 1 and Level 1. Gross carrying value of investments measured at FVTOCI and investments measured at amortized cost was at Stage 1 and Level 1.

The following tables analyze information on significant changes in gross carrying value of loans during the period, as well as movements in expected losses during the years ended 31 December 2019 and 2018 by classes of financial assets. Movements in expected credit losses by the items of guarantees issued and loan commitments, due from banks, investments measured at fair value through other comprehensive income, investments measured at amortized cost, and other financial assets are not material for the purpose of these consolidated financial statements. The effect of foreign exchange rate fluctuations on changes in gross carrying value and expected credit losses of financial instruments that are subject to impairment requirements under IFRS 9 in the tables below is not stated in separate lines, but included in items of respective changes.

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27. Risk management policies (continued)

Loans to customers – change in gross carrying value by Stages	Stage 1 12-months ECLs	Stage 2 Lifetime ECLs	Stage 3 Lifetime ECLs	Purchased or originated credit impaired loans
1 January 2019	18,267,505	2,201,326	6,084,242	1,178,141
New loans to customers or purchased loans	19,792,455	-	-	5,599
Changes due to acquisition of entity	-	-	-	216,000
Transfer from Stage 1, 12-month ECLs	(2,305,971)	1,538,219	576,404	-
Transfer from Stage 2, Lifetime ECLs	247,733	(560,086)	200,644	-
Transfer from Stage 3, Lifetime ECLs	12,898	65,675	(91,575)	-
Loans derecognized during the reporting period	(12,971,779)	(1,075,124)	(963,461)	(240,011)
Written off during the reporting period	-	-	(805,245)	(147,734)
Restructured loans	-	-	(12,884)	-
Effect of other changes	(621,101)	(182,350)	(436,305)	(154,242)
31 December 2019	22,421,740	1,987,660	4,551,820	857,753
Loans to customers – change in gross carrying value by Stages	Stage 1 12-months ECLs	Stage 2 Lifetime ECLs	Stage 3 Lifetime ECLs	Purchased or originated credit impaired loans
1 January 2018	13,226,359	1,488,662	7,419,856	1,446,625
New loans to customers or purchased loans	17,178,700	-	-	24,877
Transfer from Stage 1, 12-month ECLs	(2,031,817)	1,479,187	420,083	-
Transfer from Stage 2, Lifetime ECLs	170,625	(319,430)	56,201	-
Transfer from Stage 3, Lifetime ECLs	16,421	80,052	(115,184)	-
Loans derecognized during the reporting period	(9,932,653)	(398,872)	(498,412)	(100,837)
Written off during the reporting period	-	-	(1,210,992)	(30,933)
Restructured loans	(2,449)	(392)	(17,479)	-
Effect of other changes	(357,681)	(127,881)	30,169	(161,591)
31 December 2018	18,267,505	2,201,326	6,084,242	1,178,141

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27. Risk management policies (continued)

Loans to customers – change in expected credit losses by Stages	Stage 1 12-months ECLs	Stage 2 Lifetime ECLs	Stage 3 Lifetime ECLs	Purchased or originated credit impaired loans
1 January 2019	176,586	283,419	4,769,332	442,825
New loans to customers or purchased loans	449,200	-	-	2,522
Transfer from Stage 1, 12-month ECLs	(278,922)	198,875	249,984	-
Transfer from Stage 2, Lifetime ECLs	3,158	(82,474)	141,274	-
Transfer from Stage 3, Lifetime ECLs	261	25,456	(39,527)	-
Loans derecognized during the reporting period	(106,380)	(121,845)	(419,914)	(76,701)
Written off during the reporting period	-	-	(805,245)	(147,734)
Effect of changes in models or risk parameters	(12,519)	(40,748)	(363,424)	102,486
31 December 2019	231,384	262,683	3,532,480	323,398
Loans to customers – change in expected credit losses by Stages	Stage 1 12-months ECLs	Stage 2 Lifetime ECLs	Stage 3 Lifetime ECLs	Purchased or originated credit impaired loans
1 January 2018	217,742	283,551	5,631,632	403,560
New loans to customers or purchased loans	385,754	-	-	-
Transfer from Stage 1, 12-month ECLs	(256,448)	170,323	145,163	-
Transfer from Stage 2, Lifetime ECLs	1,977	(59,410)	27,394	-
Transfer from Stage 3, Lifetime ECLs	352	14,007	(27,271)	-
Loans derecognized during the reporting period	(147,199)	(94,533)	(167,177)	(32,784)
Written off during the reporting period	-	-	(1,210,992)	(30,933)
Effect of changes in models or risk parameters	(25,592)	(30,519)	370,583	102,982
31 December 2018	176,586	283,419	4,769,332	442,825

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27. Risk management policies (continued)

The table below analyzes the effect of modifications on financial assets measured at amortized cost or FVTOCI for the years ended 31 December 2019 and 2018.

	2019	2018
Amortized cost of financial assets before modification (Lifetime ECLs)	1,089,283	1,094,557
Modification result of financial assets (Lifetime ECLs)	(12,884)	(20,320)
Gross carrying value of modified financial assets, at the end of the reporting period, transferred to 12-month ECLs	120,822	137,405

Liquidity risk

Risk substance. Liquidity of the Group is defined as ability to meet its current financial liabilities on a timely basis and in full as they come due. This risk arises from inability to manage incidental cash outflows or changes in funding sources, as well as failure to fulfill its off-balance sheet obligations.

Objective of liquidity risk management. The objective of liquidity risk management is to ensure sufficient reliable funds to meet the Group's obligations in full and on a timely basis to customers, lenders, and other counterparties and to achieve the target rates of assets and profitability growth, which contemplates:

- Managing on a daily basis cash balances and nostro accounts in order to ensure timely settlements and payments, performance of the obligatory provision requirements, and compliance with the NBU's liquidity ratios at each reporting date;
- Ensuring funds for sustainable growth of business as envisaged by credit and investment policies of the Group;
- Creating a stock of liquid reserves against a possible liquidity crisis – abrupt outflow of customers' funds and/or a sudden closing of access to resource markets.

Liquidity risk management policies. Assets and Liabilities Management Committee which is delegated by the Group's management with functions to manage assets and liabilities determines the strategy for maintaining sufficient liquidity basing on the Parent's approaches and approves it in the form of liquidity risk management policies as a part of assets and liabilities management policies.

In order to manage liquidity, the Group sets up limits to the maximum volume of certain on-balance sheet items, monitors the amount of gaps between maturities of assets and liabilities as a measure of risk level to which the Group is exposed, diversifies external funding sources, plans funds to finance the Group's credit and investment policies.

A significant attention is given to concentrations in loan portfolio and deposits, as well as the liquidity level of existing assets. Assets and Liabilities Management Committee annually reviews its plan of anti-recessionary measures in the event of liquidity crisis.

Processes. Internal liquidity risk management processes, alongside with other risks, include:

- Identifying sources of risks and measuring their volumes, which is monthly performed by Assets and Liabilities Management Department on the basis of operating system data;
- Managing risk – a respective function is locally delegated to Assets and Liabilities Management Committee which regularly receives information on the risk volume to which the Group is exposed from the Assets and Liabilities Management Department of Treasury and complies with the respective limits. At the level of the OTP Group, risk management is performed by a respective committee of the Parent which receives information on the risk exposure on a monthly basis;

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27. Risk management policies (continued)

- 3) Monitoring the compliance with limits on the risk volume, which is daily performed by the Assets and Liabilities Management Department, with subsequent reporting to Assets and Liabilities Management Committee and the Parent;
- 4) Monitoring on a daily basis the compliance with regulatory requirements and internal limits;
- 5) Assessing the efficiency of strategic and operating liquidity management, which is the function of Assets and Liabilities Management Committee.

Methods. To manage an adequate level of liquidity, the Group performs a complex analysis of the following factors:

- Structure of the Group's assets and their distribution by maturity (a special attention is given to the volume of available high liquid assets);
- Volume, structure, and diversity of liabilities (firstly, the share of obligations is analyzed in liabilities, term and demand funds, due amounts to individuals and legal entities and other banks, stability of borrowing facilities, and dependence on expensive or unstable funds sources);
- Level of concentration of assets and liabilities (by counterparties, instruments, and remaining maturities);
- Analysis of cash flows by assets and liabilities type and by currencies;
- Performing stress testing for identification of the level of possible liquidity risk and compliance with the NBU ratios.

Liquidity is managed by national and foreign currencies. National currency liquidity management is de-centralized and is a full responsibility of a local Assets and Liabilities Management Committee. Foreign currency liquidity management is performed centrally on the level of the Parent using a method of the pool of funds.

Assets and Liabilities Management Committee consistently monitors its liquid position and employs a combined approach to liquidity management – in order to ensure timely fulfillment of the Group's obligations.

Liquidity management through assets is based on maintaining the adequate supply of high liquid assets, which allows meeting provision requirements, norms established by the NBU and which serves as a source for covering a temporary liquidity deficit. This approach is especially effective in the event of continued liquidity crisis and in other cases when the access to money markets is limited or missing. Liquidity management through liabilities is based on attracting interbank funding to cover temporary needs in liquidity.

Essential elements of liquidity management include analysis of credit and investment policies of the Bank and election of the most effective funding sources in accordance with the intended use of funds, as well as development of the emergency plan in case of liquidity crisis containing a clear description of crisis indicators, actions of employees responsible for anti-recessionary management, data flows and sources for replenishment of liquid funds.

In the event of liquidity crisis, a Plan of Anti-recessionary Measures determines key factors that might help in identifying the crisis at early stages and establishes clear procedures to regulate the information flows and actions of the staff engaged to manage the anti-crisis process.

Liquidity risk is managed by setting limits to volumes of operating liquidity or short-term gaps between maturities of assets and liabilities. The control of compliance with limits refers to matching the actual amounts of relevant open positions and restrictions imposed on them. In the event of failure to comply with the limit, origination reasons are analyzed, and a plan of measures is proposed with the aim of removing the deficiency or changing the existing system of limits.

Joint-Stock Company OTP Bank

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27. Risk management policies (continued)

The following tables present the analysis of liquidity risk between assets and liabilities based on the carrying values of financial assets and liabilities as presented in the separate statement of financial position. The tables were drawn on the basis of contractual maturity.

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	31 December 2019 Total
NON-DERIVATIVE FINANCIAL ASSETS:						
Cash and balances with the National Bank of Ukraine	3,139,593	-	-	-	-	3,139,593
Due from banks	4,308,470	-	-	-	-	4,308,470
Loans to customers	5,926,843	4,223,841	9,413,918	5,047,535	856,891	25,469,028
Investments measured at fair value through other comprehensive income	414,476	177,356	1,121,141	1,918,080	730	3,631,783
Investments measured at amortized cost	7,212,296	-	-	-	-	7,212,296
Other financial assets	152,745	-	-	-	-	152,745
Total non-derivative financial assets	21,154,423	4,401,197	10,535,059	6,965,615	857,621	43,913,915
Derivative financial assets	454	-	-	-	-	454
TOTAL FINANCIAL ASSETS	21,154,877	4,401,197	10,535,059	6,965,615	857,621	43,914,369
NON-DERIVATIVE FINANCIAL LIABILITIES						
Due to banks and other financial institutions	189,959	-	135,038	242,804	-	567,801
Customer accounts	33,945,684	361,920	763,971	22,726	-	35,094,301
Lease liabilities	14,612	14,317	62,434	83,062	-	174,425
Other financial liabilities	608,816	-	-	-	-	608,816
Guarantees issued and similar commitments	2,473,114	-	-	-	-	2,473,114
Irrevocable commitments on loans and undrawn credit lines	6,900,955	-	-	-	-	6,900,955
Total non-derivative financial liabilities	44,133,140	376,237	961,443	348,592	-	45,819,412
Derivative financial liabilities	3,447	-	-	-	-	3,447
TOTAL FINANCIAL LIABILITIES	44,136,587	376,237	961,443	348,592	-	45,822,859
Liquidity gap	(22,981,710)	4,024,960	9,573,616	6,617,023	857,621	
Cumulative liquidity gap	(22,981,710)	(18,956,750)	(9,383,134)	(2,766,111)	(1,908,490)	

Joint-Stock Company OTP Bank

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27. Risk management policies (continued)

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	31 December 2018 Total
NON-DERIVATIVE FINANCIAL ASSETS:						
Cash and balances with the National Bank of Ukraine	2,320,458	-	-	-	-	2,320,458
Due from banks	2,507,127	-	-	-	-	2,507,127
Loans to customers	3,348,928	4,653,265	7,261,042	5,462,228	1,333,589	22,059,052
Investments measured at fair value through other comprehensive income	115,148	441,768	527,135	17,435	734	1,102,220
Investments measured at amortized cost	3,677,428	-	-	-	-	3,677,428
Other financial assets	137,874	-	-	-	-	137,874
Total non-derivative financial assets	12,106,963	5,095,033	7,788,177	5,479,663	1,334,323	31,804,159
Derivative financial assets	2,183	-	-	-	-	2,183
TOTAL FINANCIAL ASSETS	12,109,146	5,095,033	7,788,177	5,479,663	1,334,323	31,806,342
NON-DERIVATIVE FINANCIAL LIABILITIES						
Due to banks and other financial institutions	126	-	-	315	-	441
Customer accounts	26,188,877	339,679	262,618	64,458	-	26,855,632
Other financial liabilities	493,215	-	-	-	-	493,215
Guarantees issued and similar commitments	1,733,895	-	-	-	-	1,733,895
Irrevocable commitments on loans and undrawn credit lines	3,703,413	-	-	-	-	3,703,413
Total non-derivative financial liabilities	32,119,526	339,679	262,618	64,773	-	32,786,596
Derivative financial liabilities	4,572	-	-	-	-	4,572
TOTAL FINANCIAL LIABILITIES	32,124,098	339,679	262,618	64,773	-	32,791,168
Liquidity gap	(20,014,952)	4,755,354	7,525,559	5,414,890	1,334,323	
Cumulative liquidity gap	(20,014,952)	(15,259,598)	(7,734,039)	(2,319,149)	(984,826)	

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Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

27. Risk management policies (continued)

Liquidity gap, which arose during the years ended 31 December 2019 and 2018 on assets and liabilities with maturities less than one year, is appropriately managed by the Group.

The major portion of interest-bearing liabilities is represented by both demand deposits of customers and short-term deposits that allow early termination, thus, they are included to the category requiring repayment up to one month. Based on a going concern assumption, effective maturity of core deposits is considered to be indefinite.

Deposits of customers are repayable on demand and when they are due. Commonly, demand deposits are more stable facilities, and they are not withdrawn within one month. The Group's liquidity risk management includes assessing major current accounts, i.e. the stable portion of deposits. As at 31 December 2019 and 2018, the stable portion of customers' deposits, calculated as the amount of customer accounts as at year end less standard deviation of deposits for the last three years, amounted to UAH 26,019,725 thousand and UAH 18,777,003 thousand, respectively.

Thus, as at 31 December 2019 and 2018, the excess of the Group's current liabilities over its current assets calculated with reference to the stable portion of customers' deposits as liabilities the actual maturities of which were treated as indefinite amounted to UAH 16,636,591 thousand and UAH 11,042,964 thousand, respectively.

A further analysis of the liquidity risk is presented in the following tables in accordance with IFRS 7 "Financial Instruments: Disclosures". The amounts disclosed in these tables do not correspond to the amounts recorded in the consolidated statement of financial position, as the presentation below includes a maturity analysis for financial liabilities that indicates the total remaining contractual payments (including interest payments), which are not recognized in the consolidated statement of financial position under the effective interest rate method.

The following tables have been prepared based on contractual maturities.

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	31 December 2019 Total
FINANCIAL LIABILITIES					
Due to banks and other financial institutions	189,981	-	177,531	295,195	662,707
Customer accounts	33,825,864	380,638	807,409	21,653	35,035,564
Lease liabilities	16,461	17,592	73,382	92,203	199,638
Other financial liabilities	608,816	-	-	-	608,816
Guarantees issued and similar commitments	2,473,114	-	-	-	2,473,114
Commitments on loans and unused credit lines	6,900,955	-	-	-	6,900,955
Non-derivative financial liabilities	44,015,191	398,230	1,058,322	409,051	45,880,794
Spot agreements	28,757	-	-	-	28,757
Forward contracts	74,587	-	86,306	-	160,893
Derivative financial liabilities	103,344	-	86,306	-	189,650
TOTAL FINANCIAL LIABILITIES	44,118,535	398,230	1,144,628	409,051	46,070,444

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27. Risk management policies (continued)

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	31 December 2018 Total
FINANCIAL LIABILITIES					
Due to banks and other financial institutions	126	-	-	315	441
Customer accounts	26,085,880	353,356	285,825	69,757	26,794,818
Other financial liabilities	493,215	-	-	-	493,215
Guarantees issued and similar commitments	1,733,895	-	-	-	1,733,895
Commitments on loans and unused credit lines	3,703,412	-	-	-	3,703,412
Non-derivative financial liabilities	32,016,528	353,356	285,825	70,072	32,725,781
Swap agreements	317,139	-	-	-	317,139
Forward contracts	359,322	-	-	-	359,322
Derivative financial liabilities	676,461	-	-	-	676,461
TOTAL FINANCIAL LIABILITIES	32,692,989	353,356	285,825	70,072	33,402,242

Market risk

Risk substance. The Group is exposed to market (price) risk as unexpected fluctuations in market prices may adversely affect its financial and real assets carried on the consolidated statement of financial position or recorded on off-balance accounts. However, in addition to the existing risk factors that are beyond management's direct control and level of their volatility, the necessary precondition of market risk is the existence of open position determining a sensitivity level of the financial institution to fluctuations of market indicators. Considering insignificant amounts of investments in securities with non-fixed returns and property and equipment, management is mainly focused on managing interest rate and foreign currency risks belonging to the group of market (price) risks.

Objective of market risk management. The objective of market risk management is to achieve the intended profitability level of the Group at acceptable risk for shareholders, i.e. mitigate losses from unexpected fluctuations in interest and foreign exchange rates.

Risk management policies. Market risks are managed at two levels: at the level of the OTP Group and locally.

Assets and Liabilities Management Committee which is delegated by the Group's Management Board with functions to manage assets and liabilities determines the strategy for managing market risk basing on the OTP Group's approaches and approves it in the form of interest rate and foreign currency risk management policies as a part of assets and liabilities management policies.

Risk management is defined as determining a tolerance level to a respective risk, i.e. the maximum permissible losses from fluctuations in market indicators, and establishing limits to the amount of the respective open positions the Group is exposed to.

Joint-Stock Company OTP Bank

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In Ukrainian Hryvnias and in thousands

27. Risk management policies (continued)

Management strategy is realized through coordinated management of the assets and liabilities structure and setting minimum/maximum interest rates for interest-bearing assets/liabilities.

Processes. Internal market risk management processes consist of the following:

- 1) Identifying risk sources and measuring their volumes, which is monthly performed by the Assets and Liabilities Management Department of Treasury independently from the units involved in market activities on the basis of operating system data;
- 2) Managing risk – the respective function is locally delegated to Assets and Liabilities Management Committee which regularly receives information on the risk volume to which the Group is exposed from the Assets and Liabilities Management Department of Treasury and complies with the respective limits. At the level of the OTP Group, risk management is performed by the respective committee of the Parent which receives information on the risk exposure on a quarterly basis;
- 3) Monitoring the compliance with limits on the risk volume, which is monthly performed by the Assets and Liabilities Management Department, with subsequent reporting to Assets and Liabilities Management Committee and the Parent;
- 4) Assessing the efficiency of strategic and operating liquidity management, which is the function of Assets and Liabilities Management Committee.

Interest rate risk. The Group treats interest rate risk as a risk of impact of the movements in market interest rates on the future cash flows or fair value of financial assets and liabilities.

The main objective of interest rate risk management is to decrease the impact of changes in interest rates on equity by limiting and reducing the amount of possible losses which the Group may incur on open positions from adverse changes in market conditions. Policies of interest rate risk management include describing basic criteria for management, managing, and monitoring interest rate risk in the Group.

Identifying risk sources is performed through the analysis of the existing structure of interest-bearing assets and liabilities. Analysis of interest gaps by remaining maturities (for fixed interest rate assets and liabilities) or by next interest rate change dates (for floating interest rate assets and liabilities or variable interest rate instruments) is convenient for determining positions that expose the Group to interest rate risk.

The Group assesses its interest rate risk based on the sensitivity analysis towards interest rate fluctuations and movements in economic value of equity as a result of even changes in the yield curve by specified interest points. Estimates include interest rate risk by all on-balance and off-balance positions of the Group for instruments with fixed and variable interest rates.

To obtain a quantitative estimation of changes in economic value of equity due to fluctuations in interest rates within a long-term period, a duration concept is applied.

The Parent centrally sets a limit to the volume of decrease in economic value of equity for subsidiary banks – not more than 20% of regulatory capital, and Assets and Liabilities Management Committee shall ensure minimum gaps between change dates of interest bearing assets and liabilities by changing parameters of certain large transactions and modifying the existing standards of banking products and pricing policies. The intended level of interest income is achieved through spread management.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

27. Risk management policies (continued)

Monitoring of weighted average nominal interest rates of interest-bearing financial instruments as at 31 December 2019 and 2018 was as follows:

	31 December 2019, %				
	UAH	USD	EUR	Other currencies	Interest rate
FINANCIAL ASSETS					
Due from banks	14.19	1.63	(0.5)	(0.17)	Fixed/ variable
Loans to customers	17.20	6.04	4.89	7.00	Fixed/ variable
Investments measured at fair value through other comprehensive income	15.98	5.55	4.6	-	Fixed
Investments measured at amortized cost	13.03	-	-	-	Fixed
FINANCIAL LIABILITIES					
Due to banks and other financial institutions	16.27	2.00	-	-	Fixed/variable
Customer accounts:					
Current accounts and deposits repayable on demand	7.61	0.13	0.01	-	Fixed/ variable
Term deposits	13.00	2.30	1.92	0.02	Fixed
Lease liabilities	17.3	9.6	2.6	-	Fixed
31 December 2018, %					
	UAH	USD	EUR	Other currencies	Interest rate
FINANCIAL ASSETS					
Due from banks	0.01	1.50	(0.27)	0.02	Fixed/ variable
Loans to customers	14.74	6.54	5.62	6.82	Fixed/ variable
Investments measured at fair value through other comprehensive income	18.43	5.65	4.04	-	Fixed
Investments measured at amortized cost	17.31	-	-	-	Fixed
FINANCIAL LIABILITIES					
Customer accounts:					
Current accounts and deposits repayable on demand	5.39	0.11	0.02	-	Fixed/ variable
Term deposits	13.11	1.58	1.43	0.01	Fixed

The following table presents the sensitivity to interest rate risk. Used percentage of interest rate multiplied by the value of financial assets and liabilities based, considering the tax rate, is the expected level of impact on profit/(loss) and equity.

Joint-Stock Company OTP Bank

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27. Risk management policies (continued)

The effect on profit or loss and equity was as follows:

	As at 31 December 2019		As at 31 December 2018	
	Interest rate +1	Interest rate -1	Interest rate +1	Interest rate -1
Impact on profit or loss before tax				
Sensitivity of financial assets	406,216	(406,216)	293,458	(293,458)
Sensitivity of financial liabilities	(358,365)	358,365	(268,556)	268,556
Net impact on profit or loss and equity				
	39,237	(39,237)	20,420	(20,420)

Foreign currency risk. Currency risk is defined as the risk that the value of the Group's assets, liabilities, or off-balance sheet items denominated in foreign currencies will be adversely affected by changes in foreign currency exchange rates.

Currency risk is managed by setting limits against which the estimated foreign currency risk is compared on a daily basis.

In accordance with the Group's asset and liability management policies, foreign currency risk impact is measured in two ways: on the one hand, as currency position in an individual currency and, on the other hand, as total open currency position.

Compliance with limits is monitored through comparing the actual amount of the respective open positions and the restrictions established for them. In the event of failure to comply with the limits, reasons of their origination are analyzed and a plan of measures is proposed to remove them or proposals to amend the existing system of limits.

Joint-Stock Company OTP Bank

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27. Risk management policies (continued)

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

	UAH	USD	EUR	Other currencies	Precious metals	31 December 2019 Total
FINANCIAL ASSETS						
Cash and balances with the National Bank of Ukraine	2,806,239	170,782	148,413	14,159	-	3,139,593
Due from banks	187,738	2,041,623	1,782,718	296,390	1	4,308,470
Loans to customers	17,785,206	5,654,529	2,002,517	26,776	-	25,469,028
Investments measured at fair value through other comprehensive income	2,276,902	1,157,393	197,488	-	-	3,631,783
Investments measured at amortized cost	7,212,296	-	-	-	-	7,212,296
Other financial assets	129,216	9,807	14,176	-	-	153,199
TOTAL FINANCIAL ASSETS	30,397,597	9,034,134	4,145,312	337,325	1	43,914,369
FINANCIAL LIABILITIES						
Due to banks and other financial institutions	378,153	189,648	-	-	-	567,801
Customer accounts	22,113,933	8,606,136	4,085,919	282,391	5,922	35,094,301
Lease liabilities	105,763	67,809	853	-	-	174,425
Other financial liabilities	542,378	21,646	40,460	7,779	-	612,263
TOTAL FINANCIAL LIABILITIES	23,140,227	8,885,239	4,127,232	290,170	5,922	36,448,790
CURRENCY POSITION	7,257,370	148,895	18,080	47,155	(5,921)	
Accounts payable on contracts with derivative financial instruments	(101,677)	(59,216)	-	(28,757)	-	(189,650)
Accounts receivable on contracts with derivative financial instruments	59,603	126,999	-	-	-	186,602
NET DERIVATIVE FINANCIAL INSTRUMENTS POSITION	(42,074)	67,783	-	(28,757)	-	
NET POSITION	7,215,296	216,678	18,080	18,398	(5,921)	

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Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 In Ukrainian Hryvnias and in thousands

27. Risk management policies (continued)

	UAH	USD	EUR	Other currencies	Precious metals	31 December 2018 Total
FINANCIAL ASSETS						
Cash and balances with the National Bank of Ukraine	2,068,915	135,695	103,621	12,227	-	2,320,458
Due from banks	18,699	1,083,318	1,217,083	188,025	2	2,507,127
Loans to customers	15,193,581	5,947,842	895,410	22,219	-	22,059,052
Investments measured at fair value through other comprehensive income	519,628	284,957	297,635	-	-	1,102,220
Investments measured at amortized cost	3,677,428	-	-	-	-	3,677,428
Other financial assets	120,038	11,231	8,788	-	-	140,057
TOTAL FINANCIAL ASSETS	21,598,289	7,463,043	2,522,537	222,471	2	31,806,342
FINANCIAL LIABILITIES						
Due to banks and other financial institutions	317	124	-	-	-	441
Customer accounts	16,833,556	6,956,168	2,850,173	211,884	3,851	26,855,632
Other financial liabilities	424,233	37,391	32,057	4,106	-	497,787
TOTAL FINANCIAL LIABILITIES	17,258,106	6,993,683	2,882,230	215,990	3,851	27,353,860
CURRENCY POSITION	4,340,183	469,360	(359,693)	6,481	(3,849)	
Accounts payable on contracts with derivative financial instruments	(30,773)	(693,200)	-	-	-	(723,973)
Accounts receivable on contracts with derivative financial instruments	329,607	27,688	364,713	-	-	722,008
NET DERIVATIVE FINANCIAL INSTRUMENTS POSITION	298,834	(665,512)	364,713	-	-	
NET POSITION	4,639,017	(196,152)	5,020	6,481	(3,849)	

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27. Risk management policies (continued)

Foreign currency risk sensitivity. The following table details sensitivity of the Group's financial performance and equity to 10% (31 December 2018: 10%) increase and decrease in USD and EUR official exchange rate against UAH. 10% (31 December 2018: 10%) is the sensitivity rate used by the Group when reporting foreign currency risk internally to key management personnel and represents management's assessment of the possible change in foreign currency exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjusts their translation at the end of the period for 10% (31 December 2018: 10%) change in foreign currency rates.

	31 December 2019		31 December 2018	
	UAH/USD	UAH/USD	UAH/USD	UAH/USD
	+10%	-10%	+10%	-10%
Impact on profit or loss and equity	17,768	(17,768)	(16,084)	16,084

	31 December 2019		31 December 2018	
	UAH/EUR	UAH/EUR	UAH/EUR	UAH/EUR
	+10%	-10%	+10%	-10%
Impact on profit or loss and equity	1,483	(1,483)	412	(412)

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

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

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

Geographical risk. The main requirement of the Parent presupposes complying with the limit levels established in the countries where counterparty banks are located. Estimation and management of the risk is performed in accordance with the Regulations on Country Risk Management. The document has been developed by the Group's employees according to the procedures of the Parent that aim primarily at using principles regarding the assigned ratings of respective countries.

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27. Risk management policies (continued)

Geographical belonging of corporate borrowers is established in accordance with the criteria of their registration. In accordance with the Group's corporate credit policies, its target customers are legal entities that are residents of Ukraine. Non-residents may be financed in exceptional cases if they belong to big Ukrainian groups of related companies. As at 31 December 2019 and 2018, the Group had no non-resident borrowers.

Concentration of assets and liabilities by regions is presented below:

	Ukraine	Non-OECD countries	OECD countries	31 December 2019 Total
FINANCIAL ASSETS				
Cash and balances with the National Bank of Ukraine	3,139,593	-	-	3,139,593
Due from banks	775,640	154,996	3,377,834	4,308,470
Loans to customers	25,464,701	3,580	747	25,469,028
Investments measured at fair value through other comprehensive income	3,631,783	-	-	3,631,783
Investments measured at amortized cost	7,212,296	-	-	7,212,296
Other financial assets	153,187	12	-	153,199
TOTAL FINANCIAL ASSETS	40,377,200	158,588	3,378,581	43,914,369
FINANCIAL LIABILITIES				
Due to banks and other financial institutions	189,851	2	377,948	567,801
Customer accounts	34,477,563	162,819	453,919	35,094,301
Lease liabilities	174,425	-	-	174,425
Other financial liabilities	605,083	7,103	77	612,263
TOTAL FINANCIAL LIABILITIES	35,446,922	169,924	831,944	36,448,790
NET POSITION	4,930,278	(11,336)	2,546,637	

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27. Risk management policies (continued)

	Ukraine	Non-OECD countries	OECD countries	31 December 2018 Total
FINANCIAL ASSETS				
Cash and balances with the National Bank of Ukraine	2,320,458	-	-	2,320,458
Due from banks	29,739	62,131	2,415,257	2,507,127
Loans to customers	22,057,498	891	663	22,059,052
Investments measured at fair value through other comprehensive income	1,102,220	-	-	1,102,220
Investments measured at amortized cost	3,677,428	-	-	3,677,428
Other financial assets	139,589	3	465	140,057
TOTAL FINANCIAL ASSETS	29,326,932	63,025	2,416,385	31,806,342
FINANCIAL LIABILITIES				
Due to banks and other financial institutions	315	2	124	441
Customer accounts	26,367,905	133,775	353,952	26,855,632
Other financial liabilities	496,583	-	1,204	497,787
TOTAL FINANCIAL LIABILITIES	26,864,803	133,777	355,280	27,353,860
NET POSITION	2,462,129	(70,752)	2,061,105	

28. Acquisition of a subsidiary

In January 2019, JSC "OTP Bank" acquired a 100% interest in the share capital of LLC "OTP Factoring Ukraine" from company that is a part of OTP Group for UAH 139,143 thousand. Principal activities of LLC "OTP Factoring Ukraine" presuppose rendering services on collecting payments.

The investment in LLC "OTP Factoring Ukraine" was performed based on the decision of the OTP Group to consolidate the work with non-performing debts at the level of banking institutions.

At the acquisition date, the gross contractual value of loans to customers amounted to UAH 2,016,807 thousand. The best estimate of the Group at the date of acquisition presupposes receiving cash flows in the amount of UAH 216,000 thousand.

Joint-Stock Company OTP Bank

Notes to the Consolidated Financial Statements for the Year Ended 31 December 2019 *In Ukrainian Hryvnias and in thousands*

28. Acquisition of a subsidiary (continued)

The fair values of the acquired assets and liabilities recognized at the acquisition date are presented below:

Assets

Cash and cash equivalents	78,992
Loans to customers	216,000
Investments measured at fair value through other comprehensive income	36,157
Property and equipment and intangible assets	1,691
Other assets	14,337

Total assets	347,177
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Liabilities

Current liabilities	16,028
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Total liabilities	16,028
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Net assets	331,149
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To determine the fair values, an income approach has been applied which transfers future cash flows into a discounted amount. The fair values are assessed based on the values expected by the current market in respect of such future amounts. The discount rate used to determine the fair values at the acquisition date amounted to 22.8%.

Net cash outflows on the subsidiary's acquisition are described below:

	2019
Payments in cash	139,143
Less: Acquired cash and cash equivalents	(78,992)
Total	60,151

The gain of JSC "OTP Bank" on the bargain purchase of LLC "OTP Factoring Ukraine" is described below:

	2019
Net assets	331,149
Consideration of cash and cash equivalents	(139,143)
Gain on bargain purchase	192,006

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28. Acquisition of a subsidiary (continued)

The gain on the bargain purchase arose as a result of revaluation of the investment's fair value in accordance with the requirements to the measurement period described in Note 3.

Included in interest income and profit for the year was the amount of UAH 160,874 thousand and UAH 130,121 thousand respectively, relating to the activities of LLC "OTP Factoring Ukraine".