

**TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC
AND ITS SUBSIDIARIES**

Consolidated Financial Statements

31 December 2016 and 2015

(With Independent Auditors' Report Thereon)

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Trade and Development Bank of Mongolia LLC
Corporate Information

**Registered office and
principal place of business**

Peace Avenue 19
Sukhbaatar district, 1st khoroo
Ulaanbaatar, 14210
Mongolia

Board of Directors

D.Erdenebileg (Chairman)
R.Koppa
Z.Shagdarsuren
T.Tsolmon
Ch.Enkhbold

Secretary of Bank

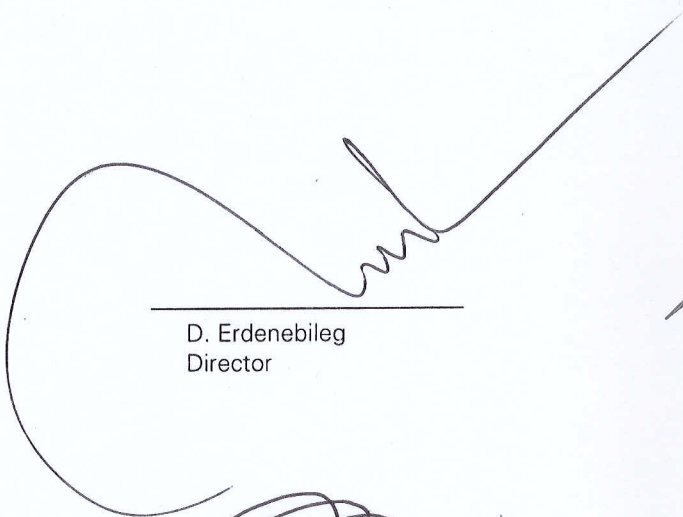
D. Davaajav

Independent auditors

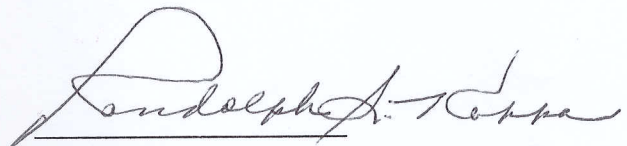
KPMG Samjong Accounting Corp.
Seoul, Korea

Statement by Directors and Executives

We, D. Erdenebileg, R. Koppa and O. Orkhon, being the directors and executives of Trade and Development Bank of Mongolia LLC (the "Bank"), and D. Yanjmaa, being the officer primarily responsible for the consolidated financial statements of the Bank and its subsidiaries (together the "Group"), do hereby state that, in our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2016 and 2015 and of its consolidated financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards as modified by Bank of Mongolia guidelines.



D. Erdenebileg
Director



R. Koppa
Director



O. Orkhon
Chief Executive Officer



D. Yanjmaa
Director of Financial Management and
Control Department

Ulaanbaatar, Mongolia

Date : 31 March 2017

KPMG Samjong Accounting Corp.

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Independent Auditors' Report

The Board of Directors and Shareholders
Trade and Development Bank of Mongolia LLC:

Opinion

We have audited the consolidated financial statements of Trade and Development Bank of Mongolia (the "Bank") and its subsidiaries (together the "Group"), which comprise the consolidated statements of financial position as at 31 December 2016 and 2015, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the years then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2016 and 2015, and of its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS) as modified by Bank of Mongolia ("BOM") guidelines.

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 Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Mongolia, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of Matters

We draw attention to Note 39 to the consolidated financial statements, which describes that in February 2017 the International Monetary Fund ("IMF") and the Government of Mongolia agreed a three year bailout programme which is subject to approval by the Mongolian Parliament and by the IMF's Executive Board. The full implications of this programme, and the related measures and impact on the Mongolian financial sector are as yet unclear. This creates a significant uncertainty the impact of which will only be realized with time. The financial impact resulting from this bailout programme on the Group's financial statements cannot be reasonably estimated at this time, therefore no adjustments for this matter were recorded to the Group's consolidated financial statements. Our opinion is not qualified in respect of this matter.

We draw attention to Note 42 to the consolidated financial statements. Mongolia's Parliament Standing Committee issued a report in relation to acquisition of 49 percent of common stock of Erdenet Mining Corporation LLC. (EMC), where the Group is alleged to improperly have extended loans to acquire companies. At this time there is uncertainty regarding the potential adverse impact to the Group. Our opinion is not qualified in respect of this matter.

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.

Allowance for loan losses

Refer to Note 7 to the consolidated financial statements.

| The key audit matter | How the matter was addressed in our audit |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Under IFRS as modified by BOM guidelines, the Group is required to determine the classification of loans and provisioning amount considering quantitative and qualitative factors. This allowance for loan losses was significant to our audit because the balance of MNT 153,566,637 thousand as of 31 December 2016, is material to the financial statements. In addition, the Group’s assessment process is complex and judgmental and is based on quantitative factors such as delinquency and qualitative factors such as a borrower’s financial and economic status.</p> | <p>Our audit procedures included, among others, performing credit file reviews on a sample basis to test appropriateness of the loan classification. We tested the accuracy of the delinquency information by testing relevant IT application controls and tested the Group’s assessment of the qualitative factors by challenging key assumptions applied by the Group and comparing the Group’s classification against our understanding of the relevant industries and business environment, and the requirements of the Bank of Mongolia’s Provisioning Guidelines.</p> |

Construction-in-progress

Refer to Note 10 to the consolidated financial statements.

| The key audit matter | How the matter was addressed in our audit |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>Construction in progress is significant to our audit because the balance of MNT 142,199,641 thousand as of 31 December 2016, is material to the financial statements and significantly increased from the prior year.</p> | <p>Our audit procedures included interviews with the Group’s management and the management of the Group’s contractor responsible for the construction in order to understand the status of the construction-in-progress, inspection of the construction contracts and payment evidence, and external confirmation of payments made in accordance with the construction contract.</p> |

Other Information

Management is responsible for the other information. The other information comprises the information included in the annual report but does not include the consolidated financial statements and our auditors' report thereon. The annual report is expected to be made available to us after the date of this auditors' report.

Our opinion on the consolidated financial statements does not cover the other information and we 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 when it becomes available 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.

When we read the 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 IFRS as modified by BOM guidelines 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.

Auditors' 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 auditors' 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.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements (continued)

- 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 auditors' 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 auditors' 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.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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 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 and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Other Matter

This report is made solely to the members of the Group, as a body, those in connection with the potential offering of US\$ notes by the Group, and for no other purpose. We do not assume responsibility to any other person for the content of this report.

The engagement partner on the audit resulting in this independent auditors' report is Jae-Beom Choi.

A handwritten signature in black ink that reads 'KPMG Samjong Accounting Corp.' The signature is enclosed in a thin black rectangular box.

KPMG Samjong Accounting Corp.
31 March 2017
Seoul, Korea

This report is effective as at 31 March 2017, the audit report date. Certain subsequent events or circumstances, which may occur between the audit report date and the time of reading this report, could have a material impact on the accompanying consolidated financial statements and notes thereto. Accordingly, the readers of the audit report should understand that the above audit report has not been updated to reflect the impact of such subsequent events or circumstances, if any.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Consolidated Statements of Financial Position

As at 31 December 2016 and 2015

| | Note | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------------------------------------------------------|-------------|-------------------------|-------------------------|
| Assets | | | |
| Cash and due from banks | 4 | 1,188,822,410 | 694,959,701 |
| Investment securities | 5 | 1,525,435,217 | 1,412,539,922 |
| Investment in associates and joint ventures | 6 | 59,490,789 | 46,763,866 |
| Loans and advances, net | 7 | 2,835,167,306 | 2,644,979,616 |
| Bills purchased under resale agreements | 8 | - | 99,799,000 |
| Subordinated loans | 9 | 4,000,000 | 4,000,000 |
| Property and equipment, net | 10 | 333,559,483 | 204,884,777 |
| Intangible assets, net | 11 | 5,048,116 | 1,449,739 |
| Investment property | 12 | 88,923,950 | 99,789,000 |
| Foreclosed real properties, net | 13 | 2,194,609 | 1,370,810 |
| Other assets | 14 | 602,543,026 | 333,547,874 |
| Total assets | | 6,645,184,906 | 5,544,084,305 |
| Liabilities and shareholders' equity | | | |
| Liabilities | | | |
| Deposits from customers | 15 | 2,415,529,106 | 2,209,953,463 |
| Deposits and placements by banks and other financial institutions | 16 | 143,207,671 | 112,754,972 |
| Bills sold under repurchase agreements | 17 | 129,960,388 | 99,799,000 |
| Borrowings | 18 | 1,392,176,891 | 1,012,394,089 |
| Current tax liabilities | | 1,524,308 | 4,385,983 |
| Debt securities issued | 19 | 1,569,366,930 | 1,175,921,345 |
| Subordinated debt securities issued | 20 | 24,895,300 | 29,939,700 |
| Other liabilities | 21 | 209,373,587 | 231,003,212 |
| Total liabilities | | 5,886,034,181 | 4,876,151,764 |
| Equity | | | |
| Share capital | 22 | 50,000,011 | 50,000,011 |
| Share premium | | 19,272,456 | 19,272,456 |
| Capital adjustments | 24 | (1,583,600) | - |
| Revaluation reserves | 10, 25 | 126,992,124 | 135,298,874 |
| Accumulated unrealised gain (loss) on available-for-sale financial assets | 25 | 30,219,254 | (23,831,129) |
| Accumulated unrealised gain on valuation of cash flow hedges | 25 | 14,905,402 | 39,938,362 |
| Retained earnings | | 516,572,740 | 445,209,993 |
| Total equity attributable to equity holders of the Group | | 756,378,387 | 665,888,567 |
| Non-controlling interests | | 2,772,338 | 2,043,974 |
| Total equity | | 759,150,725 | 667,932,541 |
| Total liabilities and equity | | 6,645,184,906 | 5,544,084,305 |

See accompanying notes to the consolidated financial statements.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Consolidated Statements of Comprehensive Income

For the years ended 31 December 2016 and 2015

| | Note | 2016 MNT'000 | 2015 MNT'000 |
|----------------------------------------------------------------------------|--------|--------------------------|---------------------------|
| Interest income | 26 | 593,217,355 | 532,856,753 |
| Interest expense | 27 | (400,832,691) | (358,520,676) |
| Net interest income | | <u>192,384,664</u> | <u>174,336,077</u> |
| Net fee and commission income | 28 | 30,618,600 | 29,419,494 |
| Other operating income (loss), net | 29 | 12,021,005 | (15,192,458) |
| Net non-interest income | | <u>42,639,605</u> | <u>14,227,036</u> |
| Operating income | | 235,024,269 | 188,563,113 |
| Operating expense | 30 | (92,650,037) | (91,417,672) |
| Share of profit of associates and joint ventures | 6 | 17,296,485 | 12,569,455 |
| Provision for impairment losses | 31 | (91,997,632) | (46,976,039) |
| Profit before tax | | 67,673,085 | 62,738,857 |
| Income tax expense | 33 | (212,876) | (1,263,569) |
| Net profit for the year | | <u>67,460,209</u> | <u>61,475,288</u> |
| Other comprehensive income for the year: | | | |
| Items that will never be reclassified to profit or loss | | | |
| Net change in revaluation reserves of property and equipment | 10, 25 | (7,317,887) | 7,943,000 |
| Items that are or may be reclassified to profit or loss | | | |
| Net unrealised change in fair value of available-for-sale financial assets | 25 | 54,050,383 | 3,656,568 |
| Net unrealised gain (loss) on valuation of cash flow hedges | 25 | (25,032,960) | 39,938,362 |
| Other comprehensive income | | <u>21,699,536</u> | <u>51,537,930</u> |
| Total comprehensive income for the year | | <u><u>89,159,745</u></u> | <u><u>113,013,218</u></u> |
| Profit attributable to: | | | |
| Equity holders of the Group | | 67,965,541 | 61,094,198 |
| Non-controlling interests | | (505,332) | 381,090 |
| Net profit for the year | | <u><u>67,460,209</u></u> | <u><u>61,475,288</u></u> |
| Total comprehensive income attributable to: | | | |
| Equity holders of the Group | | 89,665,077 | 112,632,128 |
| Non-controlling interests | | (505,332) | 381,090 |
| Total comprehensive income for the year | | <u><u>89,159,745</u></u> | <u><u>113,013,218</u></u> |

See accompanying notes to the consolidated financial statements.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Consolidated Statements of Changes in Equity

For the years ended 31 December 2016 and 2015

| | Attributable to equity holders of the Group | | | | | | | | (Unit : MNT'000) | | |
|----------------------------------------------------------------------------|---------------------------------------------|-------------------|-------------------|-----------------|----------------------|--------------------------------------------------------------------------|--------------------------------------------------------------|--------------------|--------------------|---------------------------|--------------------|
| | Note | Share capital | Share premium | Treasury shares | Revaluation reserves | Accumulated unrealised gain(loss) on available-for-sale financial assets | Accumulated unrealised gain on valuation of cash flow hedges | Retained earnings | Total | Non-controlling interests | Total equity |
| 1 January 2015 | | 16,525,280 | 19,272,456 | (2,620,626) | 153,645,983 | (27,487,697) | - | 395,019,832 | 554,355,228 | 1,662,884 | 556,018,112 |
| Total comprehensive income | | | | | | | | | | | |
| Net profit for the year | | - | - | - | - | - | - | 61,094,198 | 61,094,198 | 381,090 | 61,475,288 |
| Other comprehensive income | | | | | | | | | | | |
| Net unrealised change in fair value of available-for-sale financial assets | 25 | - | - | - | - | 3,656,568 | - | - | 3,656,568 | - | 3,656,568 |
| Net change in revaluation reserves of property and equipment | 10, 25 | - | - | - | (18,347,109) | - | - | 26,290,109 | 7,943,000 | - | 7,943,000 |
| Net unrealised gain on valuation of cash flow hedges | 25 | - | - | - | - | - | 39,938,362 | - | 39,938,362 | - | 39,938,362 |
| Total other comprehensive income | | - | - | - | (18,347,109) | 3,656,568 | 39,938,362 | 26,290,109 | 51,537,930 | - | 51,537,930 |
| Transactions with shareholders | | | | | | | | | | | |
| Capitalisation of retained earning | | 33,474,731 | - | - | - | - | - | (33,474,731) | - | - | - |
| Dividend withholding tax | | - | - | - | - | - | - | (3,719,415) | (3,719,415) | - | (3,719,415) |
| Disposition of treasury shares | | - | - | 2,620,626 | - | - | - | - | 2,620,626 | - | 2,620,626 |
| 31 December 2015 | | <u>50,000,011</u> | <u>19,272,456</u> | <u>-</u> | <u>135,298,874</u> | <u>(23,831,129)</u> | <u>39,938,362</u> | <u>445,209,993</u> | <u>665,888,567</u> | <u>2,043,974</u> | <u>667,932,541</u> |

See accompanying notes to the consolidated financial statements.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Consolidated Statements of Changes in Equity, Continued

For the years ended 31 December 2016 and 2015

| | Note | Attributable to equity holders of the Group | | | | | | | (Unit : MNT'000) | | |
|----------------------------------------------------------------------------|--------|---------------------------------------------|-------------------|--------------------|----------------------|--------------------------------------------------------------------------|--------------------------------------------------------------|--------------------|--------------------|---------------------------|--------------------|
| | | Share capital | Share premium | Capital adjustment | Revaluation reserves | Accumulated unrealised gain(loss) on available-for-sale financial assets | Accumulated unrealised gain on valuation of cash flow hedges | Retained earnings | Total | Non-controlling interests | Total equity |
| 1 January 2016 | | 50,000,011 | 19,272,456 | - | 135,298,874 | (23,831,129) | 39,938,362 | 445,209,993 | 665,888,567 | 2,043,974 | 667,932,541 |
| Total comprehensive income | | | | | | | | | | | |
| Net profit for the year | | - | - | - | - | - | - | 67,965,541 | 67,965,541 | (505,332) | 67,460,209 |
| Other comprehensive income | | | | | | | | | | | |
| Net unrealised change in fair value of available-for-sale financial assets | 25 | - | - | - | - | 54,050,383 | - | - | 54,050,383 | - | 54,050,383 |
| Net change in revaluation reserves of property and equipment | 10, 25 | - | - | - | (8,306,750) | - | - | 988,863 | (7,317,887) | - | (7,317,887) |
| Net unrealised loss on valuation of cash flow hedges | 25 | - | - | - | - | - | (25,032,960) | - | (25,032,960) | - | (25,032,960) |
| Total other comprehensive income | | - | - | - | (8,306,750) | 54,050,383 | (25,032,960) | 988,863 | 20,115,936 | - | 21,699,536 |
| Transactions with shareholders | | | | | | | | | | | |
| Change due to business combination | | - | - | - | - | - | - | 586,060 | 586,060 | 2,814,643 | 3,400,703 |
| Subsidiary's acquisition of treasury shares | 24 | - | - | (1,583,600) | - | - | - | - | (1,583,600) | - | (1,583,600) |
| Other changes | | - | - | - | - | - | - | 1,822,283 | 1,822,283 | (1,580,947) | 241,336 |
| 31 December 2016 | | <u>50,000,011</u> | <u>19,272,456</u> | <u>(1,583,600)</u> | <u>126,992,124</u> | <u>30,219,254</u> | <u>14,905,402</u> | <u>516,572,740</u> | <u>756,378,387</u> | <u>2,772,338</u> | <u>759,150,725</u> |

See accompanying notes to the consolidated financial statements.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Consolidated Statements of Cash Flows

For the years ended 31 December 2016 and 2015

| | Note | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------------------------------------------------------------------|-------------|-------------------------|-------------------------|
| Cash flows from operating activities: | | | |
| Net profit for the year | | 67,460,209 | 61,475,288 |
| Adjustments for: | | | |
| Depreciation and amortisation | 10, 11, 30 | 12,310,763 | 11,379,427 |
| Share of profit of associates and joint ventures | 6 | (17,296,485) | (12,569,456) |
| Gain on disposition of securities | 29 | (21,827,163) | (411,065) |
| Gain on disposition of investment in associates and joint ventures | 29 | (8,907,904) | - |
| Net interest income | 26, 27 | (192,384,664) | (174,336,077) |
| Income tax expense | 33 | 212,876 | 1,263,569 |
| Loss on disposition of property and equipment | 29 | 9,348 | 1,777,788 |
| Loss on disposition of investment property | 29 | 1,252,400 | - |
| Property and equipment written off | 30 | 9,380 | 10,376,532 |
| Investment property written off | 30 | 1,151,774 | - |
| Provision for impairment losses | 31 | 91,997,632 | 46,976,039 |
| Valuation loss (gain) on investment property | 12, 29 | 7,792,650 | (4,654,281) |
| Impairment losses of goodwill | 11, 30 | - | 2,803,205 |
| Personnel expense | 30 | 404,458 | - |
| Operating profit before changes in operating assets and liabilities: | | <u>(57,814,726)</u> | <u>(55,919,031)</u> |
| Decrease (Increase) in balances with BOM | 4, 35 | (746,435) | 24,245,240 |
| Decrease (Increase) in loans and advances | | (343,124,012) | 84,864,873 |
| Decrease (Increase) in bills purchased under resale agreement | 8 | 99,799,000 | (99,799,000) |
| Decrease (Increase) in other assets(*) | 14 | (194,115,525) | 52,800,779 |
| Increase (Decrease) in deposits from customers | 15 | 205,575,643 | (323,653,538) |
| Increase (Decrease) in deposits and placements by banks and other financial institutions | 16 | 30,452,699 | (7,252,364) |
| Decrease in other liabilities(*) | 21 | (42,727,799) | (43,326,037) |
| Increase in current tax | | - | 5,676,348 |
| Interest received | | 548,122,973 | 497,315,781 |
| Interest paid | | (379,865,380) | (363,342,585) |
| Income taxes paid | | (3,074,551) | (958,332) |
| Net cash flows used in operating activities | | <u>(137,518,113)</u> | <u>(229,347,866)</u> |
| Cash flows from investing activities: | | | |
| Purchase of investment securities | 5 | (373,254,578) | (1,291,419,591) |
| Disposal of investment securities | 5 | 344,557,792 | 791,847,245 |
| Purchase of investment in associates and joint ventures | 6 | (292,383) | (19,664,333) |
| Disposal of investment in associates and joint ventures | 6 | 13,769,849 | - |
| Proceeds from disposal of Investment properties | 12 | 161,600 | - |
| Purchase of property and equipment | 10 | (146,672,015) | (9,501,274) |
| Proceeds from disposal of property and equipment | 10 | 420,866 | 26,591,946 |
| Purchase of intangible assets | 11 | (5,436,596) | (680,125) |
| Proceeds from disposal of foreclosed real properties | 13 | 618,077 | - |
| Net cash flows used in investing activities | | <u>(166,127,388)</u> | <u>(502,826,132)</u> |

See accompanying notes to the consolidated financial statements.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES
Consolidated Statements of Cash Flows, Continued
For the years ended 31 December 2016 and 2015

| | Note | 2016 MNT'000 | 2015 MNT'000 |
|-------------------------------------------------------------|-------------|-------------------------|-------------------------|
| Cash flows from financing activities: | | | |
| Net proceeds from bills sold under repurchase agreements | 17 | 30,161,388 | 99,799,000 |
| Proceeds from borrowings | 18 | 1,040,459,826 | 826,022,999 |
| Repayments of borrowings | 18 | (660,677,024) | (920,957,874) |
| Proceeds from debt securities issued | 19 | 482,023,478 | 962,349,391 |
| Repayments of debt securities issued | 19 | (88,577,893) | (527,782,891) |
| Repayment of from subordinated debt securities issued | 20 | (5,044,400) | (45,411,869) |
| Sales of treasury shares | 23 | - | 2,620,626 |
| Subsidiary's acquisition of treasury shares | 24 | (1,583,600) | - |
| Net cash flows provided by financing activities | | <u>796,761,775</u> | <u>396,639,382</u> |
| Net Increase (decrease) in cash and cash equivalents | | 493,116,274 | (335,534,616) |
| Cash and cash equivalents at beginning of year | | <u>398,172,183</u> | <u>733,706,799</u> |
| Cash and cash equivalents at end of year | 35 | <u>891,288,457</u> | <u>398,172,183</u> |

(*) Represents fluctuation of other assets and other liabilities other than changes in accrued interest receivables and accrued interest payables, respectively.

See accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

1 Organisation and business

Trade and Development Bank of Mongolia LLC (the "Bank"), the controlling company, and its subsidiaries included in consolidation (together the "Group") are summarised as follows:

Controlling company

The Bank is a Mongolian domiciled limited liability company, incorporated in accordance with the Company Law of Mongolia. The Bank was given special permission to conduct banking activities by Decree No.3/149 issued by the President of the Bank of Mongolia ("BOM") on 29 May 1993 in accordance with the Banking Law of Mongolia, and License No.8 was renewed by BOM on 27 February 2002.

Pursuant to the aforementioned resolutions, license and charter, the Bank conducts banking activities such as cash savings, lending, handling and settlements of cash transfers, foreign currency transactions and other banking activities through its 23 branches and 28 settlement centers.

Subsidiaries included in consolidation

(i) *TDB Capital LLC*

The Group established TDB Capital LLC ("TDBC"), a wholly owned subsidiary, on 14 August 2008. TDBC is a Mongolian domiciled limited liability company incorporated in accordance with the Company Law of Mongolia and may be engaged in financial services activities within the parameters set forth in the Company Law, Civil Law and Law of Security Market of Mongolia and other relevant laws and regulations and those activities include, but are not limited to, brokerage and underwriting services to various customers.

(ii) *National News Corporation LLC*

National News Corporation LLC ("NNC", formerly TDB Media LLC) was established in 2011. The Group has been cooperating with Bloomberg L.P. to broadcast international financial news through NNC, which is a media company licensed by the Mongolia Telecommunication Regulatory Commission to operate Bloomberg TV Mongolia in Ulaanbaatar since 2011. On 19 November 2013, the Group obtained control of TDB Media LLC ("TDBM"). In March 2016, TDBM merged with NNC by newly issuing 340,400 ordinary shares. Following the business combination, TDBM changed its name to NNC and the Group's ownership interest in NNC decreased from 84.4% to 69.8%. After the business combination, NNC acquired 10,000 treasury shares from UB City Bank and the Group's ownership interest increased from 69.8% to 75.9%.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

1 Organisation and business (continued)

Condensed financial statements of subsidiaries as at 31 December 2016 and 2015, and for the years ended 31 December 2016 and 2015 were as follows:

| Subsidiaries | 2016 MNT'000 | | 2015 MNT'000 | |
|--------------|-----------------|-----------|-----------------|-----------|
| | Asset | Liability | Asset | Liability |
| TDBC | 39,188,526 | 6,095,058 | 32,208,496 | 44,162 |
| NNC | 19,870,788 | 7,911,428 | 14,397,058 | 1,732,424 |

| Subsidiaries | 2016 MNT'000 | | 2015 MNT'000 | |
|--------------|-------------------|-------------|-------------------|------------|
| | Operating revenue | Net income | Operating revenue | Net Income |
| TDBC | 1,403,632 | 618,589 | 1,825,636 | 945,101 |
| NNC | 4,114,361 | (2,766,693) | 3,727,957 | 819,426 |

Associates and joint ventures

(i) Mongol General Leasing LLC

Mongol General Leasing LLC ("MGLL") is a joint venture among the Bank, TDB Capital LLC and MG Leasing Corporation of Japan and sole shareholder of TDB Leasing LLC. MGLL is formed to be a commercial company pursuing for-profit business objectives within the scope of the Shareholder's Agreement entered into by the shareholders on 11 June 2013 and to be guided by the Civil Code of Mongolia, the company law of Mongolia and other related laws and regulations of Mongolia.

Scope of activities that the company conducts as permitted by the Applicable Law are providing financial leasing and providing business consultancy service.

(ii) MIK Holding JSC

Mongolian Mortgage Corporation HFC LLC was founded in 2008 under the category of "Special Purpose Company A". MIK Holding JSC is the parent company of Mongolian Mortgage Corporation HFC LLC.

The main purpose of the company is to issue Mortgage Backed Securities in domestic and international markets, develop primary and secondary markets for mortgages, provide the Mongolian population with housing and further create a long-term financing system aimed at building modern cities.

(iii) JCDecaux LLC

JCDecaux LLC is principally engaged in the business of outdoor advertising. JCDecaux LLC is a limited liability company, incorporated and domiciled in Mongolia on 28 April 2014 as a joint venture between JCDecaux Asia Pte. Ltd., and NNC. Outdoor advertising services mainly comes from sales of advertising spaces on street furniture equipment. JCDecaux LLC is the exclusive operator of bus shelters, taxi shelters and city information panels in Ulaanbaatar which cover all major roads of the city. In addition, the company maintains daily inspection of its media.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

1 Organisation and business (continued)

The Group's subsidiaries, associates and joint ventures as of 31 December 2016 and 2015 were as follows:

| Parent | Name | Classification | Group's Ownership (%) | | Location | Reporting date | Industry |
|----------|---------------------------------|----------------|-----------------------|--------|----------|----------------|------------|
| | | | 2016 | 2015 | | | |
| The Bank | TDB Capital LLC | Subsidiary | 100.00 | 100.00 | Mongolia | 31 December | Finance |
| | NNC(*1) | Subsidiary | 75.89 | 84.36 | Mongolia | 31 December | Media |
| | MGLL(*2) | Joint venture | 55.00 | 55.00 | Mongolia | 31 December | Finance |
| | MIK Holding JSC(*3) | Associate | 31.27 | 33.18 | Mongolia | 31 December | Mortgage |
| | JCDecaux LLC(*4) | Associate | 49.00 | 49.00 | Mongolia | 31 December | Marketing |
| | Times Media Corporation LLC(*5) | Subsidiary | 100.00 | 100.00 | Mongolia | 31 December | Media |
| | NNC UB Omnimedia LLC(*5) | Subsidiary | 51.00 | - | Mongolia | 31 December | Media |
| | ZGMMedeelel LLC(*5) | Subsidiary | 100.00 | - | Mongolia | 31 December | Publishing |
| | Grand Step LLC(*6) | - | - | 70.00 | Mongolia | 31 December | Publishing |

(*1) The Group acquired 10% and TDB Capital LLC acquired 74.36% equity interest of TDB Media LLC, respectively. In March 2016, TDB Media LLC merged with NNC LLC. The Group acquired 9% and TDB Capital LLC acquired 66.89% equity interest of NNC LLC, respectively as at 31 December 2016.

(*2) The Group acquired 10% and TDB Capital LLC acquired 45% equity interest.

(*3) In 2016, as a result of non-proportionate capital reduction, the Group's ownership interest in MIK Holding JSC decreased to 22.95% and TDB Capital LLC acquired 8.32% equity interest.

(*4) NNC acquired 49% equity interest in JCDecaux LLC.

(*5) Times Media Corporation LLC, NNC UB Omnimedia LLC and ZGMMedeelel LLC are subsidiaries of NNC LLC.

(*6) The Group disposed all shares of Grand Step LLC during the year ended 31 December 2016.

2 Basis of preparation

Statement of compliance

The accompanying financial statements are consolidated financial statements that have been prepared in accordance with International Financial Reporting Standards ("IFRS") as modified by the BOM guidelines.

The major items modified by the BOM guidelines that are not in compliance with IFRS include the following, and the details are included in the corresponding notes:

- Allowance for loan loss reserves, receivables, letters of credit, unused credit commitments, unfunded syndicated and foreclosed properties
- Accounting for deferred tax

The consolidated financial statements were authorised for issue by the Board of Directors on 31 March 2017.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

2 Basis of preparation (continued)

Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except for the following:

- Derivative financial instruments that are measured at fair value
- Available-for-sale financial assets that are measured at fair value
- Certain property and equipment that are measured at fair value subsequent to acquisition
- Investment property that is measured at fair value
- Precious metal that is measured at fair value

Functional and presentation currency

These consolidated financial statements are presented in Mongolian Togrog ("MNT"), rounded to the nearest thousand. MNT is the Group's functional currency.

Use of estimates and judgments

The preparation of the consolidated financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Significant areas of estimation uncertainty and critical judgments of the Group in applying accounting policies that have the most significant effect on the amounts recognised in the consolidated financial statements are allowance for loan losses, valuation of financial instruments, and valuation of property and equipment and investment property.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

2 Basis of preparation (continued)

Changes in accounting policies

Except for the following new standards and amendments to existing standards, the Group applies its accounting policies consistently which were used for preparing its annual consolidated financial statements as at and for the year ended 31 December 2015. The following changes in accounting policies are reflected in the Group's consolidated financial statements as at and for the year ending 31 December 2016.

i) Amendments to IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets

The amendments clarify that a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. These amendments are effective for annual periods beginning on or after 1 January 2016.

The Group applied the amendments retrospectively and the amendments did not impact the consolidated financial statements.

ii) Amendments to IFRS 11 Joint Arrangements

The amendments require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business must apply the relevant IFRS 3 principles for business combinations accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation while joint control is retained. These amendments are effective for annual periods beginning on or after 1 January 2016.

The Group applied the amendments retrospectively and the amendments did not impact the consolidated financial statements.

(iii) Amendments to Bank of Mongolia's Provisioning Guidelines

The amendments require that classification for loan is determined based on both quantitative and qualitative factors. Depending on the assessment of quantitative and qualitative factor, the Group is required to determine the provisioning ratio within a range for each loan classification while under the previous guidelines a fixed provisioning ratio was assigned to each loan classification. The amendments also clarify the provisioning ratio to be applied for off-balance sheet, and provide updated provisioning ratio to be applied for repossessed assets. These amendments are effective for annual periods beginning on or after 20 December 2016.

The Group applied the amendments prospectively for the year ended 31 December 2016 as required by the BOM Provisioning Guidelines.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies

The accounting policies set out below have been consistently applied by the Group and are consistent with those used in previous years other than new accounting policies adopted by the Group in the current year.(see note 2)

Basis of consolidation

(i) *Subsidiaries*

Subsidiaries are investees controlled by the Group. The Group controls an investee when it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) *Loss of control*

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, and any related non-controlling interests and other components of equity. Any resulting gain or loss is recognised in profit or loss. Any interest retained in the former subsidiary is measured at fair value when control is lost.

(iii) *Intra-group transactions eliminated on consolidation*

Intra-group balances, transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Intra-group losses are recognised as expense if intra-group losses indicate an impairment that requires recognition in the consolidated financial statements.

(iv) *Non-controlling interests*

Non-controlling interests in a subsidiary are accounted for separately from the parent's ownership interests in a subsidiary. Each component of net profit or loss and other comprehensive income is attributed to the owners of the parent and non-controlling interests holders, even when the allocation reduces the non-controlling interests balance below zero.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)

Business combination

(i) Business combination

A business combination is accounted for by applying the acquisition method, unless it is a combination involving entities or businesses under common control.

Each identifiable asset and liability is measured at its acquisition-date fair value.

As at the acquisition date, non-controlling interests in the acquiree are measured as the non-controlling interests' proportionate share of the acquiree's identifiable net assets.

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 the assets transferred by the acquirer, the liabilities incurred by the acquirer to former owners of the acquiree and the equity interests issued by the acquirer.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

(ii) Goodwill

The Group measures goodwill at the acquisition date as:

- the fair value of the consideration transferred; plus
- the recognised amount of any non-controlling interests in the acquiree; plus
- if the business combination is achieved in stages, the fair value of the pre-existing equity interest in the acquiree; less
- the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed.

When the excess is negative, bargain purchase gain is recognised immediately in profit or loss.

When the Group additionally acquires non-controlling interest, the Group does not recognise goodwill since the transaction is regarded as equity transaction.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)

Investment in associates and joint ventures

Associates are entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity.

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

The investment in an associate and a joint venture is initially recognised at cost, and the carrying amount is increased or decreased to recognise the Group's share of the profit or loss and changes in equity of the associate and the joint venture after the date of acquisition. Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Intra-group losses are recognised as expense if intra-group losses indicate an impairment that requires recognition in the consolidated financial statements.

If an associate or a joint venture uses accounting policies different from those of the Group for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements in applying the equity method.

When the Group's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest, including any long-term investments, is reduced to nil and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has to make payments on behalf of the investee for further losses.

Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies are translated to the functional currency at the exchange rate at the reporting date. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated to the functional currency at the exchange rate when the fair value was determined. Foreign currency differences are generally recognised in profit or loss. Non-monetary items that are measured based on historical cost in a foreign currency are not translated.

However, foreign currency differences arising from the translation of available-for-sale equity investment (except on impairment, in which case foreign currency differences that have been recognised in OCI are reclassified to profit or loss), are recognised in OCI.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)

Financial instruments

(i) Classification

Financial assets and financial liabilities held for trading include debt securities, equity securities and securities acquired and held by the Group for short-term trading purposes. Changes in fair value are recognised in profit or loss.

Derivatives recorded at fair value through profit or loss include certain derivative contracts that are not designated as effective hedging instruments. All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as trading assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as trading liabilities.

Financial assets or financial liabilities at fair value through profit or loss include those financial assets and financial liabilities designated at initial recognition because 1) such designation eliminates or significantly reduces an accounting mismatch; 2) respective financial assets and financial liabilities are part of a group of financial assets, liabilities or both and their performance is evaluated on a fair value basis in accordance with a documented risk management or investment strategy; or 3) the embedded derivative does not meet the separation criteria. Financial assets and financial liabilities at fair value through profit or loss are recorded at fair value and changes in fair value are recorded in the current operations.

Originated loans and receivables are loans and receivables created by the Group providing money to a debtor other than those created with the intention of short-term trading. Originated loans and receivables comprise loans and advances to customers and are reported net of an allowances to reflect the estimated recoverable amounts. The allowance is estimated in accordance with the Regulations on Asset Classification and Provisioning, jointly approved by the President of BOM and the Ministry of Finance.(BOM Provisioning Guidelines)

Held-to-maturity assets are non-derivative assets with fixed or determinable payments and fixed maturity that the Group has the intent and ability to hold to maturity, and are not designated at fair value through profit or loss or as available-for-sale. This includes certain investment securities held by the Group.

Available-for-sale assets are non-derivative assets that are designated as available-for-sale or are not classified as another category of financial assets.

(ii) Initial recognition

A financial asset or financial liability is measured initially at fair value plus transaction costs that are directly attributable to its acquisition or issue if the financial assets are not subsequently accounted for at fair value through profit or loss. For financial assets at FVTPL, directly attributable transaction costs are recognised in profit or loss as incurred.

3 Significant accounting policies (continued)

Financial instruments (continued)

(iii) Subsequent measurement

Subsequent to initial recognition, all financial assets and liabilities held for trading, derivatives recorded at fair value through profit or loss, financial assets and liabilities at fair value through profit or loss and available-for-sale assets are measured at fair value, except that any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is carried at cost, including transaction costs, less impairment losses. Gains and losses arising from changes in the fair value of trading instruments and available-for-sale assets are recognised in profit or loss and directly in equity, respectively.

All non-trading financial liabilities, originated loans and receivables, and held-to-maturity assets are measured at amortised cost less impairment losses where applicable. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Derecognition of financial assets and liabilities

(i) Financial assets

The Group derecognises a financial assets when the contractual rights to the cash flows from the financial asset expire, or the Group has either transferred the contractual right to receive the cash flows from that asset, or has assumed an obligation to pay those cash flows to one or more recipients, subject to certain criteria, or if it transfers substantially all the risks and rewards of ownership.

The Group enters into transactions in which it transfers previously recognised financial assets but retains substantially all the associated risks and rewards of those assets. In transactions in which substantially all the risks and rewards of ownership of a financial asset are neither retained nor transferred, the Group derecognises the transferred asset if control over that asset (i.e. the practical ability to sell the transferred asset) is relinquished. The rights and obligations retained in the transfer are recognised separately as assets and liabilities, as appropriate. If control over the asset is retained, the Group continues to recognise the asset to the extent of its continuing involvement, which is determined by the extent to which it remains exposed to changes in the value of the financial asset transferred.

The derecognition criteria are also applied to the transfer of part of an asset, rather than the asset as a whole, or to a group of similar financial assets in their entirety, when applicable. If transferring a part of an asset, such part must be a specifically identified cash flow, a fully proportionate share of the asset, or a fully proportionate share of a specifically-identified cash flow.

3 Significant accounting policies (continued)

Derecognition of financial assets and liabilities (continued)

(ii) *Financial liabilities*

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. If an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of the existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the consolidated statements of comprehensive income.

Cash flow hedges

When a derivative is designated as the hedging instrument in a hedge of the variability in cash flows attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction that could affect profit or loss, the effective portion of changes in the fair value of the derivative is recognised in other comprehensive income. Any ineffective portion of changes in the fair value of the derivative is recognised immediately in profit or loss. If the hedging derivative expires or is sold, terminated, or exercised, or the hedge no longer meets the criteria for cash flow hedge, or the hedge designation is revoked, then hedge accounting is discontinued prospectively. In a discontinued hedge of a forecast transaction, the cumulative amount recognised in other comprehensive income from the year when the hedge was effective is reclassified from equity to profit or loss as a reclassification adjustment when the forecast transaction occurs and affects profit or loss. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is reclassified immediately to profit or loss as a reclassification adjustment.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand and unrestricted due from banks and other financial institutions with original maturities of less than three months, which are subject to insignificant risk of changes in fair value, and are used by the Group in the management of short-term commitments.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)**Property and equipment****(i) *Recognition and subsequent measurement***

The initial cost of an item of property and equipment comprises its purchase price, including import duties, non-refundable purchase taxes and any directly attributable costs of bringing the asset to its working condition and location for its intended use. After recognition as an asset, property and equipment whose fair value can be measured reliably are carried at a revalued amount, being its fair value at the date of revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Expenditure incurred after property and equipment has been put into operation, such as repairs and maintenance and overhaul costs, are normally charged to income in the year in which the costs are incurred. In situations where it can be clearly demonstrated that the expenditure has resulted in an increase in the future economic benefits expected to be obtained from the use of an item of property and equipment beyond its originally assessed standard of performance, the expenditure is capitalised as an additional cost of property and equipment.

The Group revalues its property and equipment to ensure that the fair value of revalued assets does not differ materially from its carrying amount. Surpluses arising from revaluation are dealt with in the revaluation reserve in equity. Any deficit arising is offset against the revaluation reserve to the extent of a previous increase for the same asset. In all other cases, a decrease in carrying amount is charged to profit or loss as impairment.

(ii) *Depreciation*

Depreciation is charged to profit or loss on a straight-line basis over the estimated useful life of each item of property and equipment. The estimated useful lives of property and equipment are as follows:

| | |
|---------------------------------------|-----------|
| ● Buildings | 40 years |
| ● Office equipment and motor vehicles | 10 years |
| ● Computers | 3-5 years |

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted, if appropriate. The change is accounted for as changes in accounting estimates.

Construction-in-progress

Construction-in-progress represents the cost of construction of new buildings and premises, which have not been fully completed or installed. No depreciation is provided for construction-in-progress during the period of construction.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)

Intangible assets

(i) *Acquired intangible assets*

Intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and any impairment losses.

(ii) *Amortisation*

Amortisation is charged to the consolidated statements of comprehensive income on a straight-line basis over the estimated useful lives of intangible assets unless such lives are indefinite. The estimated useful lives of intangible assets are as follows:

- | | |
|------------|----------|
| ● Software | 3 years |
| ● Patent | 10 years |

Amortisation methods and amortisation periods are reviewed at each reporting date and adjusted, if appropriate. The change is accounted for as changes in accounting estimates.

Investment property

Property held for the purpose of earning rentals or benefiting from capital appreciation is classified as investment property. Investment property is measured initially at its cost. Transaction costs are included in the initial measurement. Subsequently, investment property is measured at fair value and changes in fair value are recognised in profit or loss.

Due to the commencement of owner-occupation or of development with a view to sell, the deemed cost of investment property carried at fair value transferred to owner-occupied property or inventories is the investment property's fair value at the date of change in use.

If an owner-occupied property becomes an investment property that will be carried at fair value due to the cease of owner-occupation, the Group shall revalue it at the fair value at the date of change in use, and reclassify it to investment property.

Foreclosed real properties

Properties acquired through foreclosure are initially recognised at fair value, recorded as foreclosed properties. The allowance is subsequently estimated in accordance with the Regulations on Asset Classification and Provisioning, jointly approved by the President of BOM and Ministry of Finance. Such a model classifies the Group's foreclosed properties based on time characteristics and makes allowances at the rates of 0%, 25%, 50%, 75% and 100% for credit classification categories of performing, in arrears, substandard, doubtful and loss, respectively

3 Significant accounting policies (continued)

Impairment

The carrying amounts of the Group's assets are reviewed at each reporting date to determine whether there is any indication of impairment. If such an indication exists, the asset's recoverable amount is estimated.

(i) *Loans and receivables*

Loans and receivables are presented net of allowances for uncollectability. Allowances are made against the carrying amount of loans and receivables that are identified as being potentially impaired, based on regular reviews of outstanding balances, to reduce these loans and receivables to their recoverable amount in accordance with BOM Provisioning Guidelines. Increases in the allowance account are recognised in profit or loss. When a loan is known to be uncollectible, all the necessary legal procedures have been completed and the final loss has been determined, the loan is written off directly.

In accordance with the BOM Provisioning Guidelines revised on 9 December 2016, the Group is required to determine the quality of receivables based on their time factor and qualitative characteristics in classifying them and determining provisions. Such a model classifies the Group's allowances for receivable losses at the rates of 0.5%, 1% to 5%, 5% to 25%, 15% to 50% and 50% to 100%, based on credit classification categories of performing, in arrears, substandard, doubtful and loss, respectively. Previously 1%, 5%, 25%, 50% and 100% were applied, respectively. The Group does not recognise allowance for the deposit collateralised loans and overnight loans.

Qualitative characteristics taken into consideration for determining credit classification include completeness of loan file, financial indicators of the borrower, value of the collateral and previous rescheduling of the loan, etc.

In accordance with the BOM Provisioning Guidelines revised on 9 December 2016, the bank is required to determine the quality of off-balance assets and contingent liabilities based on obligor's qualitative characteristics in classifying them and determining provisions. BOM Provisioning Guidelines had set the model of provisioning rate depending on the remaining period to maturity. Such a model classifies the Bank's allowances for off-balance assets and contingent liabilities losses at the rates of 0%, 5%, 25%, 50% and 100% in case of remaining period less than 1 year, based on credit classification categories of performing, in arrears, substandard, doubtful and loss, respectively. While in case of remaining period more than 1 year, it classifies the Bank's allowances for off-balance assets and contingent liabilities losses at the rates of 0%, 1%, 15%, 35% and 75%, based on credit classification categories of performing, in arrears, substandard, doubtful and loss, respectively.

When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

3 Significant accounting policies (continued)**Impairment (continued)*****(ii) Available-for-sale financial assets***

When a decline in the fair value of an available-for-sale financial asset has been recognised in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment even though the financial asset has not been derecognised. Impairment losses recognised in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss is recognised in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. When a decline in the fair value of an available-for-sale financial asset has been recognised in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment even though the financial asset has not been derecognised. Impairment losses recognised in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss is recognised in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

(iii) Held-to-maturity financial assets

An impairment loss in respect of held-to-maturity financial assets measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate and is recognised in profit or loss. Interest on the impaired asset continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

(iv) Assets other than financial instruments

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group estimates the recoverable amount of the respective asset. The recoverable amount is the higher of the asset's or cash generating unit's fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment is recognised as loss of current operation in the consolidated statements of comprehensive income.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised. All reversals of impairment are recognised as profit in the consolidated statements of comprehensive income.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)**Repurchase agreements**

The Group enters into purchase (sale) of investments under agreements to resell (repurchase) substantially identical investments at a certain date in the future at a fixed price. Investments purchased subject to commitments to resell them at future dates are not recognised on the consolidated statements of financial position. The amounts paid are recognised in loans to either banks or customers. The receivables are shown as collateralised by the underlying security. Investments sold under repurchase agreements continue to be recognised in the consolidated statement of financial position and are measured in accordance with the accounting policy for either assets held for trading or available-for-sale as appropriate. The proceeds from the sale of the investments are reported as liabilities to either banks or customers. The difference between the sale and repurchase considerations is treated as interest income or expense and is accrued over the period of the agreement using the effective interest method.

Share capital**(i) Ordinary shares**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of ordinary shares and share options are recognised as a deduction from equity, net of taxes.

(ii) Treasury shares

When share capital recognised as equity is repurchased, the amount of the consideration paid, which includes directly attributable costs, is net of any tax effects, and is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognised as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to / from retained earnings.

(iii) Non-controlling interests

Non-controlling interests, which represent the equity in a subsidiary not attributable, directly or indirectly, to a parent's ownership interests, consist of the amount of those non-controlling interests at the date of the original combination calculated in accordance with IFRS 3, 'Business Combinations' and the non-controlling interests share of changes in equity since the date of the combination.

Provisions

A provision is recognised in the consolidated statements of financial position when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. All operating segments' operating results are regularly reviewed by the Group's chief operating decision maker ("CODM") to make decisions about resources to be allocated to the segment and assess its performance and for which discrete financial information is available.

3 Significant accounting policies (continued)

Revenue

(i) Interest income

Interest income and expense is recognised in the consolidated statements of comprehensive income as it accrues, taking into account the effective yield of the asset or liability. Interest income and expense include the amortisation of any discount or premium or other differences between the carrying amount of an interest bearing instrument and its amount at maturity calculated on an effective interest rate basis except that the Group does not amortise loan originating costs and fees on an effective interest rate basis but rather recognises them in profit or loss as incurred.

(ii) Fee and commission income

Fee and commission income is charged to customers for the financial services provided. Fee and commission income is recognised when the corresponding service is provided.

(iii) Rental income

Rental income from leased property is recognised in the consolidated statements of comprehensive income on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

(iv) Dividends

Dividend income is recognised when the right to receive dividends is established.

Operating lease payments

Payments made under operating leases are recognised in the consolidated statements of comprehensive income on a straight-line basis over the term of the lease. Lease incentives received are recognised in the consolidated statements of comprehensive income as a deduction to the total rental expenses over the term of the lease.

Income tax

Income tax expense is comprised of current tax only.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using the tax rates enacted or substantially enacted at the reporting date and any adjustment to tax payable in respect of previous years.

The Ministry of Finance issued a regulation on deferred tax differences in May 2010. However, the Taxation Office of Mongolia has not implemented the regulation yet and deferred tax issues have not been incorporated in the Tax Methodology yet due to unfamiliarity of the deferred tax accounting among companies, including commercial banks, as well as the tax authorities. Substantial implementation efforts such as issuance of calculation methodologies, training and discussions with practitioners are required for smooth adoption. BOM is planning to issue guidelines for commercial banks on the accounting for deferred tax assets and liabilities and recognises that current accounting practices for deferred taxes by commercial banks do not comply with IFRS.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)

Income tax (continued)

The Government of Mongolia continues to reform the business and commercial infrastructure in its transition to a market economy. As a result the laws and regulations affecting businesses continue to change rapidly. These changes are sometimes characterized by poor drafting, varying interpretations and inconsistent application by the tax authorities. In particular, taxes are subject to review and investigation by a number of authorities who are enabled by law to impose fines and penalties. While the Group believes it has provided adequately for all tax liabilities based on its understanding of the tax legislation and status at the period-end, the above facts may create tax risks for the Group which are not possible to quantify at this stage.

Employee benefits

The Group does not provide severance benefits to its employees except for providing the employer's portion in accordance with statutory social insurance payments to the State Social Insurance Scheme. Contributions made by the Group are recognised as an expense in the consolidated statements of comprehensive income as incurred.

New standards and interpretations not yet adopted

The following new standards, interpretations and amendments to existing standards have been published and are effective for annual periods beginning after January 1, 2017, and the Group has not early adopted them.

(i) *IFRS 9 Financial Instruments*

IFRS 9, published in December 2015, replaces the existing guidance in IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, a new expected credit loss model for calculating impairment on financial assets, and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IFRS 9. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early adoption permitted.

The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 9.

(ii) *IFRS 15 Revenue from Contracts with Customers*

IFRS 15, published in January 2016, establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18, Revenue, IAS 11, Construction Contracts and IFRIC 13, Customer Loyalty Programmes. IFRS 15 is effective for annual reporting periods beginning on or after January 1, 2018, with early adoption permitted.

The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 15.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

3 Significant accounting policies (continued)

New standards and interpretations not yet adopted (continued)

(iii) IFRS 16 Leases

IFRS 16, published in January 2016, supersedes IAS 17. IFRS 16 eliminates the classification of leases as either operating or finance leases for a lessee. Instead, all leases are treated in a similar way to finance leases under IAS 17. For those leases previously classified as operating leases, the most significant effect of the new requirements will be an increase in lease assets and financial liabilities and a change to the nature of expenses. IFRS 16 does not require a lessee to recognise assets and liabilities for short-term leases and leases of low-value assets. IFRS 16 is effective for annual periods beginning on or after January 1, 2019, with early adoption permitted.

The Group is assessing the potential impact on its consolidated financial statements resulting from the application of IFRS 16.

(iv) Revised Accounting Guidelines by Bank of Mongolia and Ministry of Finance

Bank of Mongolia and Ministry of Finance announced revised accounting guidelines for Mongolian Banks (the "Revised Accounting Guidelines") on 6 February 2015. The Revised Accounting Guidelines include more detailed and specific accounting treatments of assets, liabilities, equity, revenue and expense, and off-balance sheet items relating to banks. It includes accounting treatments for various types of financial instruments, option to estimate the loan loss impairment based on IAS 39 and related accounting treatment. In addition, it requires banks to apply deferred tax accounting for corporate income tax. The Revised Accounting Guidelines are prospectively effective for annual reporting periods beginning on or after 1 January 2017.

The Group is assessing the potential impact on its consolidated financial statements resulting from the Revised Accounting Guidelines.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

4 Cash and due from banks

| | 2016 MNT'000 | 2015 MNT'000 |
|---------------------------------------------------------------------|-------------------------------|-------------------------------|
| Cash on hand | 73,377,054 | 62,391,611 |
| Deposits and placements with banks and other financial institutions | 658,425,089 | 287,224,533 |
| Balances with BOM(*) | 457,020,267 | 345,343,557 |
| | <u>1,188,822,410</u> | <u>694,959,701</u> |

(*) At 31 December 2016 and 2015, BOM requires that a minimum 12% of average customer deposits for two weeks must be maintained with BOM. In relation to the daily requirement, the Group also should maintain no less than 50% of the required reserve amount at the end of each day. At 31 December 2016 and 2015, the required reserve amount was MNT 297,533,953 thousand and MNT 296,787,518 thousand, respectively.

5 Investment securities

| | 2016 MNT'000 | 2015 MNT'000 |
|-------------------------------------------------|-------------------------------|-------------------------------|
| Available-for-sale investment securities | | |
| Unquoted equity securities, at cost(*1) | 443,430 | 443,430 |
| Repossessed assets, at cost(*2) | 92,257,890 | - |
| Equity securities, at fair value(*3) | 103,732,318 | 94,006,770 |
| Government bonds(*4) | 55,462,606 | 9,336,383 |
| Bank of Mongolia Treasury bills(*5) | 99,891,902 | 194,649,861 |
| Residential mortgage-backed securities(*6) | 57,919,000 | 51,814,600 |
| Promissory notes(*7) | - | 74,193,728 |
| | <u>409,707,146</u> | <u>424,444,772</u> |
| Held-to-maturity investment securities | | |
| Government bonds | 992,594,073 | 988,095,150 |
| Development Bank of Mongolia bonds(*8) | 123,133,998 | - |
| | <u>1,115,728,071</u> | <u>988,095,150</u> |
| | <u>1,525,435,217</u> | <u>1,412,539,922</u> |

(*1) Unquoted equity securities represent investments made in unlisted private companies and are recorded at cost as there is no quoted market price in active markets and their fair value cannot be reliably measured.

(*2) The Group acquired the shares of the Mongolian National Rare Earth Corp LLC ("MNREC") based on a separate agreement between the Group and MNREC's shareholder where MNREC shares are transferred to the Group if MNREC does not repay the loan. The Group acquired 100% equity interest in MNREC as at 26 December 2016 and classified as available-for-sale investment securities in accordance with BOM guidelines. Repossessed assets are recorded at cost as the fair value cannot be reliably measured.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

5 Investment securities (continued)

- (*3) The Group disposed 1,266,799 shares of Turquoise Hill Resources Ltd ("TRQ") and all shares of Mongolian Mining Corporation during the year ended 31 December 2016. Unrealised gain of MNT 38,872,036 thousand arising from changes in the fair value of equity securities was recognised directly in equity as other comprehensive income for the year ended 31 December 2016 respectively.
- (*4) Unrealised gain (loss) of MNT 2,325,918 thousand and MNT (442,003) thousand arising from changes in the fair value of such investment were recognised directly in equity as other comprehensive income for the years ended 31 December 2016 and 2015.
- (*5) Bank of Mongolia treasury bills have short maturities from one week to three weeks. The carrying amount approximates fair value.
- (*6) Residential mortgage-backed securities represent senior and junior notes issued by MIK active SPC (one to nine) ("MIK SPCs"), which bear interest of 10.5% based on 8% mortgage loans transferred to MIK SPCs by Mongolian banks. The carrying amount approximates fair value.
- (*7) Promissory notes were fully redeemed during the year ended 31 December 2016.
- (*8) The Group acquired Development Bank of Mongolia bonds ("DBM Bond") during the year ended 31 December 2016 whose maturities are from 21 December 2018 to 14 March 2022.

6 Investment in associates and joint ventures

| | 2016 | 2015 |
|-----------------------------------------|-------------------|-------------------|
| | MNT'000 | MNT'000 |
| Investment in MIK Holding JSC(*1) | 52,912,775 | 43,438,826 |
| Investment in MG Leasing LLC(*2) | 3,562,516 | 871,839 |
| Investment in JCDecaux Mongolia LLC(*3) | 3,015,498 | 2,453,201 |
| | <u>59,490,789</u> | <u>46,763,866</u> |

- (*1) MIK Holding LLC ("MIK") decreased paid in capital in 2016, carrying amount decreased by MNT 3,206,429 thousand. The Group's ownership interest in MIK decreased to approximately 31.27% due to non-proportionate capital decrease. MNT 1,655,516 thousand decreased by receiving dividend in 2016. In applying the equity method, the Group used the financial information of MIK as at 31 December 2016. The Group recognised its share of gain of MIK of MNT 14,335,894 thousand and MNT 9,206,541 thousand in 2016 and 2015, respectively.
- (*2) In 2013, the Group entered into a MNT 1,773,610 thousand investment acquiring 55% equity interest in MG Leasing LLC ("MGLL") which is a joint venture established by the Group and MGL corporation. However, as decisions about relevant activities require the unanimous consent of the parties sharing control, the Group does not deem MGLL as a subsidiary but as a joint venture. In applying the equity method, the Group used the financial information of MGLL as at 31 December 2016. The Group recognised its share of gain (loss) of MGLL of MNT 2,690,677 thousand and MNT (823,728) thousand in 2016 and 2015, respectively.
- (*3) In 2014, the Group entered into a MNT 1,316,003 thousand investment acquiring 49% equity interest in JCDecaux Mongolia LLC ("JCD"). As decisions about relevant activities requires the unanimous consent of the parties sharing control, the Group deems JCD as a joint venture. JCD increased paid in capital in June 2016, the Group entered into a MNT 292,383 thousand investment. The Group's ownership interest in JCD is not changed due to proportionate capital contribution. In applying the equity method, the Group used the financial information of JCD as at 31 December 2015, and recognised its share of gain of JCD of MNT 269,914 thousand and MNT 148,271 thousand in 2016 and 2015, respectively.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

6 Investment in associates and joint ventures (continued)

Condensed financial statements of associates as at 31 December 2016 and 2015, and for the years ended 31 December 2016 and 2015 were as follows:

| Investees | 2016 MNT'000 | | 2015 MNT'000 | |
|-----------|-----------------|---------------|-----------------|---------------|
| | Asset | Liability | Asset | Liability |
| MIK | 2,322,484,358 | 2,187,354,486 | 2,167,353,263 | 2,053,908,760 |
| MGLL | 79,795,265 | 73,317,964 | 44,533,672 | 42,948,511 |
| JCD | 6,622,820 | 468,741 | 5,237,585 | 231,054 |

| Investees | 2016 MNT'000 | | 2015 MNT'000 | |
|-----------|----------------------|---------------|----------------------|---------------|
| | Operating revenue | Net income | Operating revenue | Net income |
| MIK | 192,685,281 | 50,737,893 | 125,520,407 | 30,374,884 |
| MGLL | 6,768,049 | 2,268,114 | 3,417,093 | (1,649,657) |
| JCD | 2,072,096 | 560,361 | 1,448,209 | 296,503 |

7 Loans and advances

| | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------------------|----------------------|----------------------|
| Loans and advances to customers | 2,953,228,405 | 2,713,765,929 |
| Loans to executives, directors and staff | 35,505,538 | 29,354,297 |
| | 2,988,733,943 | 2,743,120,226 |
| Allowance for loan losses | (153,566,637) | (98,140,610) |
| | <u>2,835,167,306</u> | <u>2,644,979,616</u> |

Movements in the allowance for loan losses for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|-----------------------------|--------------------|-------------------|
| At 1 January | 98,140,610 | 58,742,342 |
| Provision for the year, net | 91,794,836 | 44,573,901 |
| Written off | (36,368,809) | (5,175,633) |
| At 31 December | <u>153,566,637</u> | <u>98,140,610</u> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

7 Loans and advances (continued)

In addition, the Group transferred its mortgage loans to MIK SPCs with carrying amounts of MNT 61,073,170 thousand and MNT 234,396,500 thousand during 2016 and 2015, respectively. These transactions qualified for derecognition.

The Group transferred pool of mortgage loans with carrying amounts of MNT 613,153 thousand to Mongolian Mortgage Corporation HFC LLC during 2016. But the loans do not qualify for derecognition criteria for financial assets since significant risks and rewards were not transferred to Mongolian Mortgage Corporation HFC LLC. Accordingly, the Group did not derecognise in the financial statements but accounted for these transactions as collateralised financing for which the balance at 31 December 2016 amounted to MNT 504,930 thousand. (Note 18)

The Group entered into Troubled Asset Recovery Program ("TARP") agreement with Bank of Mongolia in June 2016. TARP is intended to assist two borrowers in designated economic sectors who do not expect to be able to fully repay the principal and interest of its loans in the medium term. Under this agreement, BOM purchased debt securities issued by the Group and the Group granted certain loans. In addition, the Group should apply specific asset classification and provisioning ratio for the relevant borrowers as determined by BOM, which is higher than BOM Provisioning Guidelines disclosed in the Group's annual consolidated financial statements as at and for the year ended 31 December 2016.

BOM obligated the Group to amend certain mining loan repayment schedules breached as those loans were issued to finance strategically important projects by end of first quarter of 2017 considering the economic situation of the mining industry. Additionally, BOM obligated Group to more closely monitor the construction industry loans without downgrading the classification and report the result at the end of every month, specifically reviewing loan repayment, business operation and financial indicators including sales.

8 Bills purchased under resale agreements

| <u>Contract party</u> | <u>Sold date</u> | <u>Maturity</u> | <u>Interest rate</u> | <u>2016 MNT'000</u> | <u>2015 MNT'000</u> |
|------------------------------|------------------|-----------------|----------------------|-------------------------|-------------------------|
| Development Bank of Mongolia | 16 Oct 2015 | 14 Apr 2016 | 6.1% | - | 99,799,000 |

9 Subordinated loans

| | <u>2016 MNT'000</u> | <u>2015 MNT'000</u> |
|--------------|-------------------------|-------------------------|
| UB City Bank | 4,000,000 | 4,000,000 |

The loan to UB City Bank bears a fixed interest of 8% per annum and is to be repaid in full on 25 September 2017.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

10 Property and equipment

Property and equipment as at 31 December 2016 and 2015 were as follows:

31 December 2016
(In MNT'000)

| | Buildings | Office equipment and motor vehicles | Computers and others | Construction- in-progress(*1) | Total |
|---------------------------------|--------------|-------------------------------------------|-------------------------|----------------------------------|--------------|
| At cost/revaluation | | | | | |
| At cost | 45,524,298 | 13,137,013 | 20,184,676 | 6,258,473 | 85,104,460 |
| At revaluation | 134,378,958 | 919,916 | - | - | 135,298,874 |
| At 1 January 2016 | 179,903,256 | 14,056,929 | 20,184,676 | 6,258,473 | 220,403,334 |
| Additions | 3,783,471 | 1,169,320 | 4,535,493 | 137,183,731 | 146,672,015 |
| Disposals | (736,446) | (413,526) | (121,958) | - | (1,271,930) |
| Write-offs | - | (88,582) | (768,549) | - | (857,131) |
| Reclassification(*2) | 2,574,949 | - | - | (1,242,563) | 1,332,386 |
| Revaluation surplus | (11,356,448) | (78,360) | - | - | (11,434,808) |
| At 31 December 2016 | 174,168,782 | 14,645,781 | 23,829,662 | 142,199,641 | 354,843,866 |
| Measured at: | | | | | |
| Cost | 51,146,272 | 13,804,225 | 23,829,662 | 142,199,641 | 230,979,800 |
| Revaluation | 123,022,510 | 841,556 | - | - | 123,864,066 |
| | 174,168,782 | 14,645,781 | 23,829,662 | 142,199,641 | 354,843,866 |
| Accumulated depreciation | | | | | |
| At 1 January 2016 | 305,392 | 3,778,341 | 11,434,824 | - | 15,518,557 |
| Charge for the year | 4,717,407 | 1,260,513 | 4,494,624 | - | 10,472,544 |
| Disposals | (528,158) | (106,207) | (96,670) | - | (731,035) |
| Write-offs | - | (80,544) | (767,081) | - | (847,625) |
| Revaluation surplus | (3,128,058) | - | - | - | (3,128,058) |
| At 31 December 2016 | 1,366,583 | 4,852,103 | 15,065,697 | - | 21,284,383 |
| Carrying amounts | | | | | |
| At 31 December 2016 | 172,802,199 | 9,793,678 | 8,763,965 | 142,199,641 | 333,559,483 |

(*1) Construction-in-progress account mainly consists of costs for construction of the Group's new office building and branch buildings. The Group made a contract to build its new corporate head office with Riverstone Property LLC and paid MNT 136,973,200 thousand in June 2016. Riverstone Property LLC is currently in the process of appointing sub-contractors and the actual construction work is planned to be commenced in 2017 and to be completed in 2019.

(*2) Portion of the Group's office building was reclassified from investment property. Building reclassified from investment property is MNT 1,332,386 thousand.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

10 Property and equipment (continued)
31 December 2015
(In MNT'000)

| | Buildings | Office equipment and motor vehicles | Computers and others | Construction- in-progress | Total |
|---------------------------------|--------------|-------------------------------------------|-------------------------|------------------------------|--------------|
| At cost/revaluation | | | | | |
| At cost | 121,641,188 | 11,122,186 | 19,206,522 | 4,572,154 | 156,542,050 |
| At revaluation | 153,645,983 | - | - | - | 153,645,983 |
| At 1 January 2015 | 275,287,171 | 11,122,186 | 19,206,522 | 4,572,154 | 310,188,033 |
| Additions | 2,925,186 | 2,760,692 | 2,129,077 | 1,686,319 | 9,501,274 |
| Disposals | (11,382,083) | (720,827) | (1,069,865) | - | (13,172,775) |
| Write-offs | (1,497,734) | (25,038) | (81,058) | - | (1,603,830) |
| Reclassification(* 1) | (61,460,406) | - | - | - | (61,460,406) |
| Revaluation surplus | (23,968,878) | 919,916 | - | - | (23,048,962) |
| At 31 December 2015 | 179,903,256 | 14,056,929 | 20,184,676 | 6,258,473 | 220,403,334 |
| Measured at: | | | | | |
| Cost | 50,226,151 | 13,137,013 | 20,184,676 | 6,258,473 | 89,806,313 |
| Revaluation | 129,677,105 | 919,916 | - | - | 130,597,021 |
| | 179,903,256 | 14,056,929 | 20,184,676 | 6,258,473 | 220,403,334 |
| Accumulated depreciation | | | | | |
| At 1 January 2015 | 610,285 | 3,258,548 | 8,276,932 | - | 12,145,765 |
| Charge for the year | 5,107,018 | 1,075,920 | 4,226,842 | - | 10,409,780 |
| Disposals | (157,638) | (556,127) | (1,068,851) | - | (1,782,616) |
| Write-offs | (224,330) | - | (99) | - | (224,429) |
| Reclassification(* 1) | (328,090) | - | - | - | (328,090) |
| Revaluation surplus | (4,701,853) | - | - | - | (4,701,853) |
| At 31 December 2015 | 305,392 | 3,778,341 | 11,434,824 | - | 15,518,557 |
| Carrying amounts | | | | | |
| At 31 December 2015 | 179,597,864 | 10,278,588 | 8,749,852 | 6,258,473 | 204,884,777 |

(* 1) Portion of the Group's office building is reclassified to investment property. Building reclassified to investment property is MNT 61,132,316 thousand.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

10 Property and equipment (continued)

Details of the latest valuation of buildings appraised by an independent professional valuation company are as follows:

| <u>Date of valuation</u> | <u>Description of property</u> | <u>Basis of valuation</u> |
|--------------------------|--------------------------------|---------------------------|
| 31 October 2008 | Buildings | Market value |
| 31 December 2011 | Buildings | Market value |
| 30 June 2014 | Buildings | Market value |
| 31 December 2014 | Buildings | Market value |
| 31 December 2015 | Buildings | Market value |
| 31 December 2016 | Buildings | Market value |

The following table shows the valuation technique used in measuring the fair value of buildings, as well as the significant unobservable inputs used.

| <u>Valuation technique</u> | <u>Significant unobservable inputs</u> | <u>Inter-relationship between key unobservable inputs and fair value measurement</u> |
|----------------------------|-----------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------|
| Market price approach | Average selling price for proxy (unit: MNT'000 per m ²); buildings: 300 ~ 7,500 apartments: 1,573 ~ 2,648 | The estimated fair value would increase (decrease) if: Expected market price for proxy land ownership, buildings and apartments was higher (lower). |

11 Intangible assets and goodwill

| | <u>2016 MNT'000</u> | <u>2015 MNT'000</u> |
|-------------------------------------------|-------------------------|-------------------------|
| Cost | | |
| At 1 January | 8,949,905 | 8,269,780 |
| Additions | | |
| Software | 4,634,105 | 680,125 |
| Patent | 802,491 | - |
| At 31 December | <u>14,386,501</u> | <u>8,949,905</u> |
| Amortisation and impairment losses | | |
| At 1 January | 7,500,166 | 3,727,314 |
| Amortisation charge for the year(*1) | 1,838,219 | 969,647 |
| Impairment loss(*2) | - | 2,803,205 |
| At 31 December | <u>9,338,385</u> | <u>7,500,166</u> |
| Carrying amounts | | |
| At 31 December | <u><u>5,048,116</u></u> | <u><u>1,449,739</u></u> |

(*1) Amortisation is charged for software and patent.

(*2) Impairment loss is charged for goodwill only.(Note 30)

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

12 Investment property

| | 2016 MNT'000 | 2015 MNT'000 |
|----------------------|-------------------------------|-------------------------------|
| At 1 January | 99,789,000 | 33,689,000 |
| Disposals | (588,240) | - |
| Write-offs | (1,151,774) | - |
| Reclassification(*) | (1,332,386) | 61,132,316 |
| Change in fair value | (7,792,650) | 4,967,684 |
| At 31 December | <u>88,923,950</u> | <u>99,789,000</u> |

(*) Portion of the Group's office building was reclassified to property and equipment and reclassified from property and equipment during 2016 and 2015, respectively.

The fair value of investment property was appraised by an independent professional valuation company. The independent appraiser provides the fair value of the Group's investment property portfolio every year.

The fair value hierarchy for investment property has been categorised as level 3 based on the inputs used in the valuation techniques.

There was no transfer to or from level 3 of investment property during 2016 and 2015.

The following table shows the valuation technique used in measuring the fair value of investment property, as well as the significant unobservable inputs used.

| Valuation technique | Significant unobservable inputs | Inter-relationship between key unobservable inputs and fair value measurement |
|----------------------------|-----------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------|
| Market price approach | Average selling price for proxy (unit: MNT'000 per m ²); Buildings: 5,500 ~ 7,500 | The estimated fair value would increase (decrease) if: Expected market price for proxy buildings was higher (lower). |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

13 Foreclosed real properties

| | 2016 MNT'000 | 2015 MNT'000 |
|-----------------------|-------------------------------|-------------------------------|
| Industrial buildings | 10,960,459 | 10,983,950 |
| Apartments and houses | 1,069,616 | 425,920 |
| Less: Allowances | (9,835,466) | (10,039,060) |
| | <u>2,194,609</u> | <u>1,370,810</u> |

During 2016 and 2015, an allowance of MNT 504,653 thousand and MNT 135,000 thousand were written back upon recovery from foreclosed real properties, respectively, and foreclosed real properties were not written off against impairment losses.

14 Other assets

| | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------------------|-------------------------------|-------------------------------|
| Precious metals | 31,334 | 23,678 |
| Accrued interest receivables | 141,186,879 | 99,680,366 |
| Prepayment | 23,378,378 | 19,028,986 |
| Inventory supplies | 1,954,431 | 1,498,486 |
| Spot trading receivables | 9,146,782 | 104,719,018 |
| Derivative assets for trading | 70,898,721 | 34,642,718 |
| Hedging instruments(*1)(*2)(*3) | 288,075,402 | 66,333,362 |
| Domestic exchange settlement receivables | 13,974,953 | 3,781,011 |
| Other receivables, net(*4) | 53,896,146 | 3,840,249 |
| | <u>602,543,026</u> | <u>333,547,874</u> |

(*1) Changes in deferred gains recognised at initial recognition of hedging instruments were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|-------------------|-------------------------------|-------------------------------|
| Beginning balance | 79,843,677 | - |
| Deferral | - | 91,459,139 |
| Amortisation(*) | (30,099,198) | (11,615,462) |
| Ending balance | <u>49,744,479</u> | <u>79,843,677</u> |

(*) Amortisation of deferred gains were recognised as other comprehensive income for the year ended 31December 2016, in connection with cash flow hedge, as the effective portion of changes in fair value of the derivative.

(*2) The Group applied cash flow hedges amount at USD 500,000 thousand by using derivatives (FX swaps) to hedge the foreign currency risks arising from its issuance of notes denominated in USD from 15 May 2015.

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31 December 2016 and 2015

14 Other assets (continued)

(*3) Changes in other comprehensive income recognised as effective portion of cash flow hedge for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|---------------------|-------------------------------|-------------------------------|
| Beginning balance | 39,938,362 | - |
| Increase | 221,742,040 | 66,333,362 |
| Reclassification(*) | (246,775,000) | (26,395,000) |
| Ending balance | <u>14,905,402</u> | <u>39,938,362</u> |

(*) Valuation gain which were reclassified to profit or loss for the years ended 31 December 2016 and 2015. The recognised amount of the ineffective portion of the gain or loss on the hedging instruments is nil. The Group expects that the period when derivative contracts designated as a cash flow hedge are exposed to cash flow volatility risk as at 31 December 2016, will be up until 29 April 2020.

(*4) Other receivables are presented net of impairment losses amounting to MNT 443,131 thousand and MNT 36,741 thousand as at 31 December 2016 and 31 December 2015, respectively.

15 Deposits from customers

| | 2016 MNT'000 | 2015 MNT'000 |
|------------------|-------------------------------|-------------------------------|
| Current accounts | 857,112,725 | 705,643,603 |
| Savings deposits | 272,206,435 | 293,612,096 |
| Time deposits | 1,181,790,112 | 1,173,232,888 |
| Other deposits | 104,419,834 | 37,464,876 |
| | <u>2,415,529,106</u> | <u>2,209,953,463</u> |

Current accounts and other deposits generally bear no interest. However, for depositors maintaining current account balances above the prescribed limit, interest is provided at rates of approximately 1.97% and 3.35% (2015: 1.51% and 3.18%) per annum for foreign and local currency accounts, respectively.

Foreign and local currency savings deposits bear interest at a rate of approximately 1.95% and 6.42% (2015: 1.95% and 6.59%), respectively.

Foreign and local currency time deposits bear interest at a rate of approximately 6.69% and 14.71% (2015: 6.50% and 13.78%), respectively.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

16 Deposits and placements by banks and other financial institutions

| | 2016 MNT'000 | 2015 MNT'000 |
|--------------------------------------|-------------------------------|-------------------------------|
| Current accounts deposits: | | |
| Foreign currency deposits | 46,329,176 | 11,812,893 |
| Local currency deposits | 985,892 | 815,763 |
| Foreign currency cheques for selling | 8,307 | 3,689 |
| Deposits from banks | 95,884,296 | 100,122,627 |
| | <u>143,207,671</u> | <u>112,754,972</u> |

17 Bills sold under repurchase agreements

| Contract party | Sold date | Maturity | Interest rate | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------|------------------|-----------------|----------------------|-------------------------------|-------------------------------|
| Bank of Mongolia | 16 Oct 2015 | 14 Apr 2016 | 5.0% | - | 99,799,000 |
| Development Bank of Mongolia | 8 Feb 2016 | 21 Sep 2018 | 7.5% | 64,960,388 | - |
| Development Bank of Mongolia | 8 Feb 2016 | 6 Oct 2021 | 7.5% | 15,000,000 | - |
| Development Bank of Mongolia | 25 Feb 2016 | 23 Nov 2021 | 7.5% | 20,000,000 | - |
| Development Bank of Mongolia | 3 Mar 2016 | 29 Nov 2021 | 7.5% | 20,000,000 | - |
| Development Bank of Mongolia | 23 Mar 2016 | 14 Dec 2021 | 7.5% | 10,000,000 | - |
| | | | | <u>129,960,388</u> | <u>99,799,000</u> |

The Group entered into repurchase agreement with Development Bank of Mongolia ("DBM"), the agreement where the Group sold DBM investment securities under repurchase agreement at an aggregate amount of MNT 129,960,388 thousand.

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31 December 2016 and 2015

18 Borrowings

| | 2016 MNT'000 | 2015 MNT'000 |
|-----------------------------------------------|-------------------------------|-------------------------------|
| Kreditanstalt fuer Wiederaufbau | 6,007,564 | 6,212,256 |
| World Bank | 1,158,663 | 1,541,910 |
| Asian Development Bank | 4,200,842 | 1,217,820 |
| International Development Association | 1,189,341 | 977,505 |
| Export-Import Bank of Korea | 1,665,936 | 14,155,757 |
| Export-Import Bank of Republic of China | 4,537,157 | 4,739,314 |
| Japan International Cooperation Agency | 26,997,352 | 24,122,817 |
| Atlantic Forfaitierungs AG | 13,697,560 | 7,789,578 |
| SME Fund, Ministry of Industry | 9,605,783 | 39,798,757 |
| Commerzbank AG | 103,966,539 | 62,009,771 |
| ING Bank | 1,866,397 | 6,640,160 |
| Baoshang Bank | 35,796,000 | - |
| Sumitomo Mitsui Banking Corporation | 61,483,128 | 45,077,031 |
| Netherlands Development Finance Company | 12,447,650 | 16,633,167 |
| Bank of Mongolia | 1,081,325 | 45,946,900 |
| Development bank of Mongolia | 293,811,162 | 168,211,079 |
| Mortgage Financing Programme by BOM | 217,607,766 | 132,030,609 |
| MG Leasing Corporation | 12,352,880 | 9,831,718 |
| Russian Agricultural Bank | - | 23,951,760 |
| TDB Syndicated Facility | 57,482,926 | 78,693,375 |
| Cargill TSF Asia Pte.Ltd | 60,164,529 | 49,546,647 |
| Cargill Financial Services International, Inc | 252,189,389 | 170,232,486 |
| Bank of Tokyo-Mitsubishi UFJ | 46,006,219 | 5,821,172 |
| China Trade Solutions | - | 648,208 |
| Exim Bank of Russia | 944,196 | 6,960,142 |
| Erste Group Bank | 5,866,636 | 9,980,723 |
| Banca Popolare Di Sondrio | 55,189,158 | 13,447,660 |
| Banco Popular Espanol | 28,106,741 | 757,543 |
| UBI Banca | 212,398 | 141,693 |
| OPEC Fund for International Development | 61,637,113 | 49,174,766 |
| Japan Bank of International Cooperation | 4,249,666 | 5,541,940 |
| Industrial and Commercial Bank of China | 1,727,515 | 10,058,476 |
| Agricultural Bank of China | 835,336 | 461,312 |
| Mongolian Mortgage Corporation HFC LLC | 504,930 | - |
| Natixis Bank | 1,003,229 | - |
| Chailease International Financial Services | 5,713,521 | - |
| Other | 870,344 | 40,037 |
| | <u>1,392,176,891</u> | <u>1,012,394,089</u> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)

Kreditanstalt fuer Wiederaufbau ("KfW")

- (a) In 1997, the Group entered into Financing Agreement with KfW through Bank of Mongolia, under which the Group can borrow equivalent up to EUR 4,345,981 from KfW via BOM, in EUR and MNT as a Programme-Executing Agency for mainly providing financing to various small and medium enterprises customers at preferential interest rates. The outstanding KfW loan amounted to EUR 1,522,389 (MNT 3,967,025 thousand) and EUR 2,456,461 (MNT 5,361,717 thousand) at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 1.25% per annum. Principal repayment is on a semi-annual basis, and the repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers
- (b) Under the Financing Agreement as described in (a) above, the outstanding MNT loan amounted to MNT 2,040,539 thousand and MNT 850,539 thousand at 31 December 2016 and 2015, respectively. The MNT loan bears interest at a rate equal to the BOM's Policy rate. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

World Bank

- (a) In 2006, the Group entered into the TDB Subsidiary Loan Agreement with World Bank, under which the Group can borrow up to USD 4,000,000 from the World Bank via the Ministry of Finance to finance the Second Private Sector Development Project through the provision of sub-loans. The outstanding World Bank USD loan amounted to USD 180,000 (MNT 448,115 thousand) and USD 320,000 (MNT 638,713 thousand) at 31 December 2016 and 2015, respectively. The loan bears interest at six-month London Inter-Bank Offering Rate ("LIBOR") USD rate plus a margin of 1% per annum. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.
- (b) Under the TDB Subsidiary Loan Agreement as described in (a) above, the Group can also borrow amounts in various currencies including in MNT up to Special Drawing Rights (SDR) 6,250,000 from the World Bank via the Ministry of Finance to finance specific investment projects through the provision of sub-loans. The outstanding World Bank MNT loan amounted to MNT 300,000 thousand and MNT 534,000 thousand at 31 December 2016 and 2015, respectively. The loan bears interest at a rate equal to the average rate for MNT demand deposits published by BOM for the preceding twelve months. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.
- (c) In 2006, the Group obtained a USD loan in the amount of USD 300,000 from the World Bank under the World Bank Training Assistance Programme loan via the Ministry of Finance for the purpose of financing the Group's implementation of institutional development programme, including staff training in the areas of credit analysis and risk assessment and risk-based internal auditing. The outstanding World Bank loan under this programme amounted to USD 164,909 (MNT 410,548 thousand) and USD 184,970 (MNT 369,197 thousand) at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 2% per annum. The loan is repayable semi-annually until final repayment due in May 2025.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)

Asian Development Bank ("ADB")

- (a) In 1999, the Group obtained a USD loan in the amount of USD 134,164 from ADB via BOM to upgrade the Group's accounting information systems. The outstanding loan amounted to USD 67,082 (MNT 167,002 thousand) and USD 71,554 (MNT 142,820 thousand) at 31 December 2016 and 2015, respectively. The loan matures in 2031 and bears interest at a fixed rate of 1% per annum and is repayable in 30 annual installments which commenced in 2002.
- (b) In 2011, the Group entered into a Finance Agreement with ADB, under which the Group can borrow up to USD 11,000,000 from ADB via the Ministry of Finance to provide loans exclusively to customers who need to finance the cost of goods, works, and consulting services required to carry out Value Chain Development ("VCD") subprojects related to the development of agriculture and rural areas. The sub-loan matures in June 2018 and bears interest at a fixed rate of up to 12% per annum. The Group can also borrow in MNT. The outstanding MNT loan amounted to MNT 675,000 thousand and MNT 1,075,000 thousand at 31 December 2016 and 2015, respectively. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.
- (c) In 2016, an On-Lending Agreement for additional financing was made between Trade and Development Bank and Ministry of Finance ("MOF"). Under this agreement the Group can borrow up to USD 41,187,500 from ADB via the MOF to finance agricultural and rural development projects. The sub-loan matures in January 2024 and bears interest at a fixed rate of MNT 8% and USD 7% per annum. The outstanding MNT loan amounted to MNT 3,358,840 thousand at 31 December 2016.

International Development Association ("IDA")

In 1998, the Group obtained a USD loan in the amount of USD 600,000 from IDA to finance the Twinning Agreement with Norwegian Banking Resources Ltd. ("NBR"), under which NBR had transferred operational knowhow and technical skills to the Group. The outstanding IDA loan amounted to USD 477,737 (MNT 1,189,341 thousand) and USD 489,737 (MNT 977,505 thousand) at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 1% per annum. Principal repayments commenced in August 2007 with the final repayment due in February 2037.

Export-Import Bank of Korea ("KEXIM")

In 2004, the Group entered into the Comprehensive Interbank Export Credit Agreement with KEXIM under which the Group can borrow up to USD 2,000,000 for relending purposes to finance customers who purchase goods from Korean exporters. Effective from July 2012, the maximum amount of facility increased to USD 30,000,000 but it decreased to USD 20,000,000 in July 2016. The outstanding borrowings under this line of credit agreement amounted to USD 669,177 (MNT 1,665,936 thousand) and USD 7,092,134 (MNT 14,155,757 thousand) at 31 December 2016 and 2015, respectively. The interest of this particular loan varies with each drawdown, which is determined by KEXIM. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Export-Import Bank of Republic of China ("TEXIM")

In 2004, the Group entered into a Relending facility with TEXIM under which the Group could borrow up to USD 5,000,000 for relending purposes to finance customers who purchase machinery and other manufactured goods produced in Taiwan. The outstanding borrowings under agreement amounted to USD 1,822,495 (MNT 4,537,157 thousand) and USD 2,374,430 (MNT 4,739,314 thousand) at 31 December 2016 and 2015, respectively. The loan bears interest at six-month LIBOR USD rate plus a margin of 1.25% per annum. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

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31 December 2016 and 2015

18 Borrowings (continued)

Japan International Cooperation Agency ("JICA")

- (a) In 2006, the Group entered into a Loan Financing Agreement with JICA, under which the Group can borrow USD or MNT loans up to the amount equivalent to JPY 2,981,000,000 from JICA via the Ministry of Finance which was channeled to various borrowers for the purpose of Small and Medium-Scaled Enterprises ("SME") Development and Environmental Protection. The outstanding USD loan amounted to USD 83,500 (MNT 207,876 thousand) and USD 155,500 (MNT 310,375 thousand) at 31 December 2016 and 2015, respectively. The loan bears interest at six-month LIBOR USD rate plus a margin of 1% per annum. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.
- (b) Under the Loan Financing Agreement as described in (a) above, the outstanding MNT loan amounted to MNT 1,951,120 thousand and MNT 2,343,580 thousand at 31 December 2016 and 2015, respectively. The MNT loan bears interest at a rate equal to the average rate for MNT demand deposits published by BOM for the preceding twelve months. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.
- (c) In 2011, the Group entered into another Loan Financing Agreement with JICA, under which the Group can borrow USD or MNT loans up to the amount equivalent to JPY 5,000,000,000 from JICA via the Ministry of Finance which was channeled to various borrowers for the second phase of developing SME Development and Environmental Protection purposes. The outstanding loans amounted to USD 1,076,500 (MNT 2,679,979 thousand) and MNT 22,158,377 thousand at 31 December 2016, and USD 1,238,500 (MNT 2,472,021 thousand) and MNT 18,996,841 thousand at 31 December 2015. The loan bears interest at a rate equal to the average rate for MNT demand deposits published by BOM for the preceding twelve months. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

Atlantic Forfaitierungs AG ("AF")

In 2009, the Group entered into a Facility Agreement with AF for the purpose of relending to customers participating in a plantation support fund. The outstanding USD loans amounted to USD 5,502,067 (MNT 13,697,560 thousand) and USD 3,902,633 (MNT 7,789,578 thousand) at 31 December 2016 and 2015, respectively. The interest rate of this particular loan varies with each drawdown which is determined by AF. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)

SME Fund, Ministry of Food, Agriculture and Light Industry

(a) In 2009, the Group entered into a credit facility loan agreement with the Ministry of Food, Agriculture and Light Industry for the purpose of SME development. The Ministry of Food, Agriculture and Light Industry budgeted MNT 30,000,000 thousand for this facility which is available to all Mongolian commercial banks with no specific set amount allocated to individual banks. In 2010 and 2011, the Group renewed this facility agreement, and the aggregate budget increased to MNT 60,000,000 thousand and MNT 150,000,000 thousand, respectively. The loan bears interest at a fixed rate of 1.2% per annum with varying repayment dates depending on the draw date. In February 2016, the Group renewed this facility agreement with the Ministry of Food, Agriculture and Light Industry for the purpose of supporting SME development and increasing working place. The outstanding borrowings amounted to MNT 1,619,017 thousand and MNT 6,994,652 thousand at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 7.0% per annum. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

In 2013, the Group signed a new facility agreement with the Ministry of Food, Agriculture and Light Industry within the above mentioned credit program. This credit facility expires in December 2017 and bears interest at a fixed rate of 1.8% per annum depending on the finances of Development Bank of Mongolia. The outstanding borrowings under this credit facility amounted to MNT 1,548,930 thousand and MNT 2,908,808 thousand at 31 December 2016 and 2015, respectively.

(b) In October 2011, the Group signed a second credit facility agreement with the Ministry of Food, Agriculture and Light Industry for the purpose of Wool and Cashmere sector development. The Ministry of Food, Agriculture and Light Industry budgeted MNT 150,000,000 thousand for this facility. The loan bears interest at a fixed rate of 0.6% per annum with varying repayment dates depending on the draw date. The outstanding borrowings under this credit facility amounted to MNT 3,186,100 thousand and MNT 25,670,596 thousand at 31 December 2016 and 2015, respectively. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

(c) In August 2014, the Group entered into a loan agreement with the Ministry of Food, Agriculture and Light Industry for the purpose of SME development within the encouraging export and substituting import program (888 Project). Projects with amount is less than MNT 2,000,000 thousand were implemented by SME Fund, Ministry of Industry and financed by Development bank of Mongolia. The outstanding borrowings amounted to MNT 3,251,736 thousand and MNT 4,224,700 thousand at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 3.0% per annum. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

Commerzbank AG

In 2011, the Group entered into an Uncommitted Bilateral Trade Finance Facility Master Agreement with Commerzbank AG for the purpose of relending to customers to finance import and export transactions. The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. Under this facility agreement, the Group has outstanding loans of USD 34,209,760 (MNT 85,166,223 thousand) and EUR 7,214,824 (MNT 18,800,316 thousand) at 31 December 2016, and USD 27,640,512 (MNT 55,169,909 thousand) and EUR 3,133,670 (MNT 6,839,862 thousand) at 31 December 2015. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)

ING Bank

In 2011, the Group obtained a trade finance line with ING Bank under which the Group can borrow up to EUR 15,000,000 for relending purposes or confirmations of letter of credit(LC). The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. Under this trade finance facility, the Group has outstanding loans of EUR 716,250 (MNT 1,866,397 thousand) at 31 December 2016 and USD 1,538,576 (MNT 3,070,966 thousand) and EUR 1,635,220 (MNT 3,569,194 thousand) at 31 December 2015. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Baoshang Bank

The Group entered into various facility agreements with Baoshang Bank, under which the Baoshang Bank loans were extended to other borrowers.

In August 2016, the Group entered into a Master Agreement on General Conditions of CNY Interbank loan under which the Group can borrow CNY funding from Baoshang bank from time to time.

The outstanding of Baoshang Bank loan amounted to CNY 100,000,000 (MNT 35,796,000 thousand) at 31 December 2016.

Sumitomo Mitsui Banking Corporation ("SMBC")

In March 2012, the Group entered into a Refinancing Letter of Credit Facilities Agreement with SMBC under which the Group can borrow up to USD 55,000,000 for further relending to customers. The maturity dates and interest for the facilities vary in accordance with the tenor of each advance, up to 12 and 18 months. The outstanding loan amounted to USD 18,654,494 (MNT 46,440,923 thousand), EUR 174,982 (MNT 455,966 thousand) and JPY 688,354,815 (MNT 14,586,239 thousand) at 31 December 2016 and USD 8,590,079 (MNT 17,145,627 thousand), EUR 12,316 (MNT 26,882 thousand) and JPY 1,683,023,031 (MNT 27,904,522 thousand) at 31 December 2015. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Netherlands Development Finance Company ("FMO")

In June 2012, the Group entered into a Senior Term Facility Agreement with FMO under which the Group can borrow up to USD 10,000,000 which shall be used for relending purposes for small and medium entities. The outstanding loan amounted to USD 5,000,000 (MNT 12,447,650 thousand) and USD 8,333,333 (MNT 16,633,167 thousand) at 31 December 2016 and 2015, respectively. The Group has an option to pay interest at a fixed or floating interest rate. The facility is repayable semi-annually until final repayment due in April 2018.

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31 December 2016 and 2015

18 Borrowings (continued)**Bank of Mongolia**

Since 2012, the Group has continued to act as a participant bank within the relending agreement with the Bank of Mongolia Midterm Sub-programme named "To stabilise price of basic commodities and products" consists of four sub programs: i) price stability of staple food; ii) fuel retail price stability; iii) reducing the cost of imported consumption goods; and iv) promoting the construction sector and achieving stability of housing prices. In 2014, the Group signed a new credit facility agreement with the Bank of Mongolia for the purpose of Cashmere Industry support. This credit facility agreement bears interest at a fixed rate of 6.0% to 9.5% per annum with varying repayment dates depending on the draw date. Within the above sub programs total of over 51 borrowers have successfully taken out loans at flexible conditions that were provided by the programme. From all these programme, the outstanding loan amounted to MNT 1,081,325 thousand and MNT 45,946,900 thousand at 31 December 2016 and 2015, respectively. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

Development Bank of Mongolia

- (a) In July 2014, the Group entered into a credit facility loan agreement with the Development Bank of Mongolia for the purpose of supporting raw leather purchase and commodity manufacturing. This credit facility bears interest at a fixed rate of 5.0% per annum with varying repayment dates depending on the draw date. Within this program, 9 sub borrowers were financed successfully in 2014 and 2015. The outstanding borrowings under this credit facility amounted to MNT 2,874,994 thousand and MNT 3,650,250 thousand at 31 December 2016 and 2015, respectively. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.
- (b) In July 2014, the Group entered into a loan agreement with the Development Bank of Mongolia for the purpose of larger project support within the encouraging export and substituting import program (888 Project). Projects with amount of more than MNT 2,000,000 thousand were implemented and financed by Development Bank of Mongolia. The outstanding borrowings amounted to MNT 56,573,000 thousand and MNT 60,523,800 thousand at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 5.0% per annum. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.
- (c) In June 2015, the Group entered into a trilateral credit facility agreement with Development Bank of Mongolia and SME Fund, Ministry of Industry for the purpose of encouraging export and substituting import, creating working place. This program were implemented by SME Fund, Ministry of Industry and financed by Development Bank of Mongolia. This credit facility agreement expires on 5 March 2019 and bears interest at a fixed rate of 6.0% per annum with varying repayment dates depending on the draw date. The outstanding borrowings amounted to MNT 13,331,652 thousand and 9,500,066 thousand at 31 December 2016 and 2015, respectively.
- (d) In Jun 2015, the Group signed a new credit facility agreement with the Development Bank of Mongolia for the purpose of supporting manufacturers and processors of cashmere. Development Bank of Mongolia budgeted MNT 100,000,000 thousand for this facility. This credit facility bears interest at a fixed rate of 6.0% per annum with varying repayment dates depending on the draw date. The outstanding borrowings under this credit facility amounted to MNT 12,600,000 thousand and MNT 6,000,000 thousand at 31 December 2016 and 2015, respectively.
- (e) In September 2015, the Group signed a new credit facility agreement with the Development Bank of Mongolia for the purpose of encouraging export and substituting import within the target of industrialisation supporting. Development Bank of Mongolia budgeted MNT 300,000,000 thousand for this facility. This credit facility bears interest at a fixed rate of 6.0% per annum with varying repayment dates depending on the draw date. The outstanding borrowings under this credit facility amounted to MNT 11,745,000 thousand, MNT 2,000,000 thousand at 31 December 2016 and 2015, respectively.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)

Development Bank of Mongolia (continued)

- (f) In September and December 2015, the Group signed new credit facility agreements with the Development Bank of Mongolia for the purpose of financing ASEM(Asia-Europe Meeting) Villa project and hotel, building for ASEM. Development Bank of Mongolia budgeted MNT 275,000,000 thousand for above facilities. The loan bears interest at a fixed rate of 4.5% per annum with varying repayment dates depending on the draw date. The outstanding borrowings under this credit facilities amounted to MNT 182,836,816 thousand and 86,536,963 thousand at 31 December 2016 and 2015, respectively.
- (g) In April 2016, the Group signed new credit facility agreements with the Development Bank of Mongolia for the purpose of financing "Meat" program. Development bank of Mongolia budgeted MNT 25 billion for above facility. The loan bears interest at a fixed rate of 9.5% per annum with varying repayment dates depending on the draw date. The outstanding borrowings amounted to MNT 11,681,400 thousand at 31 December 2016.
- (h) In April 2016, the Group signed new credit facility agreements with the Development Bank of Mongolia for the purpose of financing "Agriculture production stabilizing" program. Development bank of Mongolia budgeted MNT 25 billion for above facility. The loan bears interest at a fixed rate of 9.0% per annum with varying repayment dates depending on the draw date. The outstanding borrowings amounted to MNT 2,168,300 thousand at 31 December 2016.

Mortgage Financing Programme by BOM

In 2013, the Group entered into credit facility loan agreement titled "Mortgage financing from Bank of Mongolia provided to banks" with Bank of Mongolia. The intended purpose is to support the middle class and support the long-term sustainable economic growth by increasing the savings of the middle class. The outstanding Bank of Mongolia loan amounted to MNT 217,607,766 thousand and MNT 132,030,609 thousand at 31 December 2016 and 2015, respectively. The loan bears interest at a fixed rate of 4.00% per annum with varying repayment dates depending on the draw date.

MG Leasing Corporation

In September 2013, the Group entered into a USD 1,000,000 Facility Agreement with MG Leasing Corporation under which the Group utilise the facility to on-lend the proceeds to Mongolian knitting companies which are purchasing machines from Shima Seiki MFG Ltd. and the loan was fully repaid in September 2015. In December 2015, the Group entered into a Term Loan Agreement for the facility of USD 5,000,000. The outstanding loan amounted to USD 4,961,932 (MNT 12,352,880 thousand) and USD 4,925,760 (MNT 9,831,718 thousand) at 31 December 2016 and 2015, respectively. The interest of this particular loan varies with each drawdown which is determined by MG Leasing Corporation. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Russian Agricultural Bank ("RHB")

RHB approved a trade finance limit in 2009, for the purpose of relending to the customer. In January 2014 and October 2015, the Group entered into Loan Agreement of USD 9,000,000 and USD 12,000,000 with maturities of January 2015 and April 2016, respectively. The outstanding loan amounted to USD 12,000,000 (MNT 23,951,760 thousand) at 31 December 2015. The loan has been fully repaid and there were no outstanding loan at 31 December 2016.

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31 December 2016 and 2015

18 Borrowings (continued)**TDB Syndicated Facility**

In September 2013, the Group entered into A/B Syndicated Term Facility Agreement with Netherlands Development Finance Company ("FMO"). The syndicated term facility of USD 82,000,000 comprised of development tranche ('A' loan) of USD 35,000,000 arranged by FMO and joined by International Investment Bank and of commercial tranche ('B' loan) of USD 47,000,000 arranged by ING Bank N.V. and TDB Capital LLC. The 'B' loan participations were received from AKA Ausfuhrkredit, Bank of Tokyo-Mitsubishi UFJ, Ltd., VTB Moscow, Commerzbank, Atlantic Forfaitierungs, MG Leasing Corporation and Chailease Group. The proceeds of the Facility will be used to finance general funding requirements of the Group including on-lending to its customers. The principal is payable in accordance with the facility agreement and the interest is repayable semi-annually until final repayment due in September 2018. The rate of interests on each loan is the percentage rate per annum, which is the aggregate of the applicable margin and LIBOR. The outstanding loan amounted to USD 23,089,871 (MNT 57,482,926 thousand) and USD 39,425,933 (MNT 78,693,375 thousand) at 31 December 2016 and 2015, respectively

Cargill TSF Asia Pte. Ltd

Since May 2014, the Group entered into a trade related loan agreement under which the Group financed import of goods amounted to USD 24,167,023 (MNT 60,164,529 thousand) and to USD 24,823,218 (MNT 49,546,647 thousand) at 31 December 2016 and 2015, respectively. The interest of this particular loan varies with each drawdown which is determined by Cargill TSF Asia Pte. Ltd. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

Cargill Financial Services International, Inc

In December 2014, May 2015 and November 2015 the Group entered into a Trade related Loan Agreement under which the Group for financing of import of goods for the total amount of USD 25,000,000, USD 8,800,000 and 51,500,000 with tenor of 2 years, respectively. The outstanding loan amounted to USD 101,300,000 (MNT 252,189,389 thousand) and USD 85,287,671 (MNT 170,232,486 thousand) at 31 December 2016 and 2015, respectively. The interest of this particular loan varies with each drawdown which is determined by Cargill Financial Services International, Inc.

Bank of Tokyo-Mitsubishi UFJ

In March 2014, the Group obtained USD 25,000,000 trade finance facility for LC confirmation and LC refinancing for its customers business. The outstanding loan amounted to USD 17,316,743 (MNT 43,110,552 thousand) and JPY 136,652,500 (MNT 2,895,667 thousand) as at 31 December 2016 and USD 2,916,448 (MNT 5,821,172 thousand) at 31 December 2015, respectively. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

China Trade Solutions

The Group entered into a Short-Term Trade Finance Facilities Agreement with China Trade Solutions. The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. The outstanding loan amounted to USD 324,757 (MNT 648,208 thousand) at 31 December 2015 and it was fully repaid as of the end of 2016.

Exim Bank of Russia ("Rosexim Bank")

In September 2015, the Group entered into Interbank Loan Agreement with Rosexim Bank for the purpose of relending to the customer. The outstanding loan amounted to USD 379,267 (MNT 944,196 thousand) and USD 3,487,080 (MNT 6,960,142 thousand) at 31 December 2016 and 2015, respectively.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)**Erste Group Bank**

The Group entered into "Master Forfaiting Agreement" for total amount of EUR 5 million with Erste Group Bank in February 2015 which enabled us to provide import financing to our customers engaged with 13 countries of East Europe. Under this facility agreement, the Group has outstanding loans of EUR 1,900,119 (MNT 4,951,311 thousand) and USD 367,670 (MNT 915,325 thousand) at 31 December 2016 and EUR 4,572,650 (MNT 9,980,723 thousand) at 31 December 2015, respectively. The interest of this particular loan varies with each drawdown which is determined by Erste Group Bank. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Banca Popolare Di Sondrio

Since October 2015, Banca Popolare Di Sondrio, Italy has been offering post import financing on Italy and non-Italy deals. The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. The Group has outstanding loans of USD 20,697,683 (MNT 51,527,502 thousand) and EUR 1,405,200 (MNT 3,661,656 thousand) at 31 December 2016 and USD 6,573,272 (MNT 13,120,119 thousand) and EUR 150,062 (MNT 327,541 thousand) at 31 December 2015. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Banco Popular Espanol

Banco Popular Espanol has been cooperating trade related deals related to Spanish beneficiaries on case by case basis since September 2015. The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. The Group has outstanding loans of EUR 1,512,622 (MNT 3,941,575 thousand) and of USD 9,706,718 (MNT 24,165,166 thousand) at 31 December 2016 and EUR 347,067 (MNT 757,543 thousand) at 31 December 2015. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

UBI Banca

Since November 2015, UBI Banca, Italy has been offering post import financing to Italy originated imports from TDBM. The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. The Group has outstanding loans of USD 43,993 (MNT 109,522 thousand) and EUR 39,480 (MNT 102,876 thousand) at 31 December 2016 and USD 43,562 (MNT 86,948 thousand) and EUR 25,081 (MNT 54,745 thousand) at 31 December 2015. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

OPEC Fund for International Development ("OFID")

In August 2015, the Group entered into a Trade Finance Term Loan Agreement with The OFID under which the Group borrowed USD 25,000,000 which shall be used for supporting local corporates and SMEs for their foreign trade finance requirements. The outstanding loan amounted to USD 24,758,534 (MNT 61,637,113 thousand) and USD 24,636,903 (MNT 49,174,766 thousand) at 31 December 2016 and 2015, respectively. The interest of the facility is repayable semi-annually until final repayment due in October 2018 and the principal is repayable at the maturity of the facility.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

18 Borrowings (continued)

Japan Bank of International Cooperation (“JBIC”)

In 2013, the Group entered into On-lending agreement with Ministry of Finance based on the Export Credit Line Agreement made between Japan Bank of International Cooperation and Mongolian Government in 2013, for the purpose of financing the equipment, machineries, goods and services produced by Japanese exporters. The Group can obtain JPY and USD loans up to the total financing amount of JPY 8,000,000 thousand. The outstanding loan amounted to JPY 200,550,552 (MNT 4,249,666 thousand) and JPY 334,254,552 (5,541,940 thousand) at 31 December 2016 and 2015, respectively. The loan matures in May 2018 and bears base interest at a rate of 3.35%.

Industrial and Commercial Bank of China (“ICBC”)

In 2010, the Group entered into a Relending facility agreement with ICBC for relending purposes to finance its customers. The outstanding loan under the agreement amounted to CNY 4,826,000 (MNT 1,727,515 thousand) at 31 December 2016 and USD 245,454 (MNT 489,921 thousand) and CNY 31,113,205 (MNT 9,568,555 thousand) at 31 December 2015. The amount and currency of each drawdown, applicable interest rate, disbursement date and repayment date shall be agreed with ICBC on a case by case basis. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Agricultural Bank of China

In 2011, the Group entered into an Import Financing Agreement which enables the Group to finance its customers for import goods. The outstanding loan amounted to CNY 2,333,600 (MNT 835,336 thousand) and CNY 1,500,000 (MNT 461,310 thousand) at 31 December 2016 and 2015, respectively. The repayment dates for this loan vary in accordance with the tenor of loans granted to the various borrowers.

Mongolian Mortgage Corporation HFC LLC

In March and June 2016, the Group transferred pool of mortgage loans with carrying amounts of MNT 367,314 thousand and MNT 245,839 thousand to Mongolian Mortgage Corporation HFC LLC, respectively. The loans were transferred on a recourse basis and do not qualify for derecognition criteria for financial assets since significant risks and rewards were not transferred to Mongolian Mortgage Corporation HFC LLC. Accordingly, the Group accounted for these transactions as collateralised financing for which the balance at 31 December 2016 amounted to MNT 504,930 thousand.

Natixis Bank

Since November 2016, the Natixis bank, Singapore has been offering post import financing for import transactions. The amount and currency of each drawdown, the applicable interest rate, disbursement date, repayment date and certain other terms and conditions of each drawdown shall be agreed upon by the Group and the customer on a case by case basis. The outstanding loan amounted to EUR 385,000 (MNT 1,003,229 thousand) at 31 December 2016. The repayment dates for this loan vary in accordance to the tenor of loans granted to the various borrowers.

Chailease International Financial Services

In January 2016, the Group entered into bilateral loan agreement with Chailease International Financial Services for the amount of USD 2,500,000. The loan has a 2 year tenor and will be repaid in 4 installments of 5%, 12.5%, 12.5% and 70% on semi-annual basis. The outstanding loan amounted to USD 2,295,020 (MNT 5,713,521 thousand) at 31 December 2016.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

19 Debt securities issued

| | 2016 MNT'000 | 2015 MNT'000 |
|-------------------------------------------|-------------------------------|-------------------------------|
| Debt securities issued, at amortised cost | 1,569,366,930 | 1,175,921,345 |

On 21 January 2014, the Group issued CNY 700,000,000 senior notes due on 21 January 2017 at a price of 99.367% under its USD 700,000,000 Euro Medium Term Note ("EMTN") Programme which was launched on 13 October 2012. These bonds bear interest at 10.0% per annum payable semi-annually.

On 19 May 2015, the Group issued USD 500,000,000 guaranteed notes (unconditionally and irrevocably guaranteed by the government of Mongolia) due on 19 May 2020 at a price of 100% under its USD 500,000,000 Global Medium Term Note ("GMTN") Programme which was launched on 28 April 2015. These bonds bear interest at 9.375% per annum payable semi-annually.

On 28 June 2016, the Group issued MNT 160,000,000,000 notes due on 28 June 2021 at a price of 100% under Troubled Asset Refinance Program ("TARP") by Central bank of Mongolia.

During 2016 and 2015, the respective debt securities accreted by MNT 11,947,629 thousand and MNT 7,840,740 thousand, respectively, using the effective interest method.

The Group is also obligated to bear withholding tax in addition to the interest expenses paid to certain investors on its senior notes in accordance with the relative double tax treaty between Mongolia and related countries, and these additional cash outflows effectively increase actual interest rates for the notes.

20 Subordinated debt securities issued

| | 2016 MNT'000 | 2015 MNT'000 |
|--------------------------------------|-------------------------------|-------------------------------|
| Subordinated debt, at amortised cost | 24,895,300 | 29,939,700 |

On 24 May 2011 and 27 June 2012, the Group issued USD 5,000,000 and USD 10,000,000 subordinated notes due on 25 May 2016 and 6 June 2017 at face value, both of which are payable semi-annually, respectively.

The Group is also obligated to bear withholding tax in addition to the interest expenses paid to certain investors on its subordinated notes in accordance with the double tax treaty between Mongolia and related country, and these additional cash outflows effectively increase actual interest rates for the notes. The above liabilities will, in the event of the winding-up of the Group, be subordinated to the claims of depositors and all other creditors of the issuer.

During 2016 and 2015, the respective debt securities accreted by nil and MNT 76,671 thousand, respectively, using the effective interest method.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

21 Other liabilities

| | 2016 MNT'000 | 2015 MNT'000 |
|---------------------------------------|-------------------------------|-------------------------------|
| Accrued interest payables | 94,075,114 | 73,107,803 |
| Delay on clearing settlement | 23,241,786 | 5,990,901 |
| Spot trading payables | 9,173,670 | 104,718,936 |
| Derivative liabilities for trading | 47,289,538 | 27,904,044 |
| Finance lease payable | 5,723,739 | 2,642,334 |
| Domestic exchange obligation payables | 8,347,828 | 3,540,888 |
| Others | 21,521,912 | 13,098,306 |
| | <u>209,373,587</u> | <u>231,003,212</u> |

22 Share capital

| | Number of ordinary shares | | 2016 MNT'000 | 2015 MNT'000 |
|------------------------|----------------------------------|------------------|-------------------------------|-------------------------------|
| | 2016 | 2015 | | |
| At 1 January | 3,305,056 | 3,305,056 | 50,000,011 | 16,525,280 |
| Issued during the year | <u>-</u> | <u>-</u> | <u>-</u> | <u>33,474,731</u> |
| At 31 December | <u>3,305,056</u> | <u>3,305,056</u> | <u>50,000,011</u> | <u>50,000,011</u> |

At 31 December 2016 and 2015, 3,305,056 shares were issued and outstanding out of a total 4,000,000 authorised shares. The Group increased its share capital from MNT 16,525,280 thousand to MNT 50,000,011 thousand by capitalisation of retained earnings during the year ended 31 December 2015. As at 31 December 2016 and 2015, all issued shares were fully paid and have a par value of MNT 15,128. In connection with the capitalisation of retained earnings, the Group paid dividend withholding tax on behalf of the Group's shareholders, which shall be payable on distributions to shareholders. Such tax is recognised directly in equity as part of the distribution to shareholders. Dividend withholding tax directly recognised in equity for the year ended 31 December 2015 amounted to MNT 3,719,415 thousand.

23 Treasury shares

| | 2016 MNT'000 | 2015 MNT'000 |
|-------------------------|-------------------------------|-------------------------------|
| At 1 January | - | 2,620,626 |
| Sale of treasury shares | <u>-</u> | <u>(2,620,626)</u> |
| At 31 December | <u>-</u> | <u>-</u> |

The outstanding treasury shares were 126,015 shares, representing approximately 3.81% of the total issued and outstanding ordinary shares as at 31 December 2014. The Group disposed of all treasury shares to United Banking Corporation during the year ended 31 December 2015.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

24 Capital adjustments

During 2016, NNC LLC acquired 10,000 treasury shares with carrying amounts of MNT 1,583,600 from UB City Bank, representing 8.04% of the total ordinary shares as at December 2016.

25 Accumulated other comprehensive income

| | 2016 MNT'000 | | | |
|------------------------------------------------------------|------------------------------------------------------------------------------------|----------------------------------------------------------------|---------------------------------|--------------------|
| | Net change in fair value of available-for-sale financial assets | Net change in valuation of cash flow hedges | Revaluation reserves | Total |
| Beginning balance | (23,831,129) | 39,938,362 | 135,298,874 | 151,406,107 |
| Changes in fair value | 41,197,955 | - | (7,317,887) | 33,880,068 |
| Net unrealised gain on valuation of cash flow hedges | - | (25,032,960) | - | (25,032,960) |
| Changes due to disposal and write-offs | 12,852,428 | - | (988,863) | 11,863,565 |
| Ending balance | <u>30,219,254</u> | <u>14,905,402</u> | <u>126,992,124</u> | <u>172,116,780</u> |
| | 2015 MNT'000 | | | |
| | Net change in fair value of available-for-sale financial assets | Net change in valuation of cash flow hedges | Revaluation reserves | Total |
| Beginning balance | (27,487,697) | - | 153,645,983 | 126,158,286 |
| Changes in fair value | (15,794,880) | - | 7,943,000 | (7,851,880) |
| Net unrealised gain on valuation of cash flow hedges | - | 39,938,362 | - | 39,938,362 |
| Changes due to disposal and write-offs | 19,451,448 | - | (26,290,109) | (6,838,661) |
| Ending balance | <u>(23,831,129)</u> | <u>39,938,362</u> | <u>135,298,874</u> | <u>151,406,107</u> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

26 Interest income

| | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------------------------------------------------|-------------------------------|-------------------------------|
| Loans and advances | 371,947,581 | 340,982,730 |
| Investment securities | 196,953,296 | 166,998,538 |
| Deposits and placements with banks and other financial institutions | 18,496,759 | 20,769,389 |
| Bills purchased under resale agreements | 5,494,386 | 3,781,652 |
| Subordinated loans | 325,333 | 324,444 |
| | <u>593,217,355</u> | <u>532,856,753</u> |

27 Interest expense

| | 2016 MNT'000 | 2015 MNT'000 |
|----------------------------------------|-------------------------------|-------------------------------|
| Deposits | 160,758,871 | 156,722,952 |
| Borrowings | 79,979,835 | 66,412,474 |
| Bills sold under repurchase agreements | 13,955,270 | 3,181,170 |
| Debt securities issued | 143,606,860 | 126,082,205 |
| Subordinated debt securities issued | 2,531,855 | 6,121,875 |
| | <u>400,832,691</u> | <u>358,520,676</u> |

28 Net fee and commission income

| | 2016 MNT'000 | 2015 MNT'000 |
|--------------------------------------|-------------------------------|-------------------------------|
| Fee and commission income | | |
| Wire transfer | 5,717,728 | 5,259,369 |
| Card service | 13,565,508 | 11,618,027 |
| Loan related service | 14,620,895 | 15,088,605 |
| Others | 4,752,873 | 3,199,376 |
| Total fee and commission income | <u>38,657,004</u> | <u>35,165,377</u> |
| Fee and commission expenses | | |
| Card service expense | 5,072,975 | 4,313,008 |
| Others | 2,965,429 | 1,432,875 |
| Total fee and commission expenses | <u>8,038,404</u> | <u>5,745,883</u> |
| Net fee and commission income | <u><u>30,618,600</u></u> | <u><u>29,419,494</u></u> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

29 Other operating income (loss), net

| | 2016 MNT'000 | 2015 MNT'000 |
|--------------------------------------------------------------------|-------------------------------|-------------------------------|
| | <hr/> | <hr/> |
| Foreign exchange loss, net | (15,653,147) | (24,936,845) |
| Precious metal trading gain, net | 1,598,180 | 272,783 |
| Gain on disposition of securities, net | 21,827,163 | 411,065 |
| Gain on disposition of investment in associates and joint ventures | 8,907,904 | - |
| Valuation gain (loss) on investment property | (7,792,650) | 4,654,281 |
| Loss on disposition of property and equipment, net | (9,348) | (1,777,788) |
| Loss on disposition of investment property | (1,252,400) | - |
| Others | 4,395,303 | 6,184,046 |
| | <hr/> | <hr/> |
| | 12,021,005 | (15,192,458) |
| | <hr/> | <hr/> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

30 Operating expenses

| | 2016 | 2015 |
|-------------------------------------------------------|-------------------|-------------------|
| | MNT'000 | MNT'000 |
| Personnel expense | 32,355,970 | 30,008,387 |
| Depreciation on property and equipment (note 10) | 10,472,544 | 10,409,780 |
| Amortisation of intangible assets (note 11) | 1,838,219 | 969,647 |
| Advertising and public relations | 7,955,187 | 8,065,456 |
| Rental expenses | 4,882,541 | 4,555,035 |
| Professional fees | 10,051,702 | 3,036,016 |
| Technical assistance and foreign bank remittance fees | 1,148,260 | 1,619,185 |
| Write-off of property and equipment | 9,380 | 10,376,532 |
| Write-off of investment property | 1,151,774 | - |
| Insurance | 6,339,408 | 5,601,473 |
| Business travel expenses | 1,393,627 | 1,649,807 |
| Cash handling | 491,057 | 438,994 |
| Stationary and supplies | 1,046,893 | 831,859 |
| Communication | 1,201,448 | 3,295,209 |
| Training expenses | 275,808 | 133,034 |
| Utilities | 884,237 | 772,310 |
| Repairs and maintenance | 427,957 | 866,483 |
| Security | 249,835 | 213,858 |
| Meals and entertainment | 965,919 | 579,921 |
| Transportation | 306,142 | 354,224 |
| IT maintenance | 1,770,654 | 1,397,618 |
| Goodwill impairment(*1) | - | 2,803,205 |
| Others(*2) | 7,431,475 | 3,439,639 |
| | <u>92,650,037</u> | <u>91,417,672</u> |

(*1) The Group impaired the goodwill, which was previously recognised in connection with the acquisition of TDB Media LLC in 2013, to nil for the year ended 31 December 2015.

(*2) Others includes costs incurred for loan collections, cleaning and other miscellaneous administrative expenses.

31 Provision for impairment losses

| | 2016 | 2015 |
|------------------------------------------------------------------------------------|---------------------|---------------------|
| | MNT'000 | MNT'000 |
| Provision for impairment losses for loans | (91,794,836) | (44,573,901) |
| Provision for impairment losses for other assets and foreclosed real properties | (202,796) | (2,402,138) |
| | <u>(91,997,632)</u> | <u>(46,976,039)</u> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

32 Leases

The Group leases some of its branch offices under various lease agreements. Minimum lease commitments that the Group will pay under the non-cancelable operating lease agreements with initial terms of one year or more at 31 December 2016 and 2015 were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|---------------|-------------------------------|-------------------------------|
| Within a year | 3,260,901 | 3,013,141 |
| 1 – 5 years | 4,589,308 | 2,638,080 |
| | <u>7,850,209</u> | <u>5,651,221</u> |

33 Income tax expense

Recognised in the consolidated statements of comprehensive income:

| | 2016 MNT'000 | 2015 MNT'000 |
|-----------------------------------|-------------------------------|-------------------------------|
| Income tax expense – current year | 212,876 | 1,263,569 |

Reconciliation of effective tax expense:

| | 2016 MNT'000 | 2015 MNT'000 |
|-------------------------------------------------------|-------------------------------|-------------------------------|
| Profit before tax | 67,673,085 | 62,738,857 |
| Tax at statutory income tax rate (*1) | 16,468,271 | 15,234,714 |
| Tax effect of non-deductible expense | 8,478,009 | 13,892,534 |
| Tax effect of non-taxable income | (24,929,456) | (27,797,848) |
| Tax effect of income taxable on special tax rate (*2) | 136,247 | 663,378 |
| Effect of tax rates in subsidiaries | (36,678) | (738,851) |
| Other | 96,483 | 9,642 |
| | <u>212,876</u> | <u>1,263,569</u> |

(*1) Pursuant to Mongolian Tax Laws, the Group is required to pay Government Income Tax at the rate of 10% of the portion of taxable profit up to MNT 3 billion and 25% of the portion of taxable profits in excess of MNT 3 billion.

(*2) According to Mongolian Tax Laws, the Group is required to pay the special tax for certain type of taxable income.

34 Dividends

There were no dividends declared for the years ended 31 December 2016 and 2015.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

35 Cash and cash equivalents

Cash and cash equivalents in the consolidated statements of cash flows include cash on hand and unrestricted due from banks and other financial institutions with original maturities of less than three months. Cash and cash equivalents reported in the consolidated statements of cash flows for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|-------------------------------------|-------------------------------|-------------------------------|
| Cash and due from banks (note 5) | 1,188,822,410 | 694,959,701 |
| Balances with BOM restricted in use | (297,533,953) | (296,787,518) |
| Cash and cash equivalents | <u>891,288,457</u> | <u>398,172,183</u> |

Details of significant non-cash activities for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|---------------------------------------------------------------|-------------------------------|-------------------------------|
| Investment properties transferred to property and equipment | 1,332,386 | - |
| Investment properties transferred from property and equipment | - | 61,132,316 |
| Valuation gain on available-for-sale financial assets | 54,050,383 | 3,656,568 |
| Revaluation of property and equipment | (7,317,887) | 7,943,000 |
| Valuation gain (loss) on cash flow hedges | (25,032,960) | 39,938,362 |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

36 Segment reporting

Segment information is presented in respect of the Group's business segments. The primary format, operating segments, is based on the Group's management and internal reporting structure.

Operating segments pay to and receive interest from the Treasury on an arm's length basis to reflect the allocation of capital and funding costs.

Segment capital expenditure is the total cost incurred during the period to acquire property and equipment and intangible assets other than goodwill.

Operating segments

The Group comprises the following main operating segments:

- *Corporate Banking* Includes loans, deposits and other transactions and balances with corporate customers. The Group classifies its customer as Corporate Banking customer, where the loan amount is greater than MNT 3,000,000 thousand, or the borrower's sales amount is greater than MNT 6,000,000 thousand.
- *Small and Medium-sized Enterprise ("SME") Banking* Includes loans, deposits and other transactions and balances with SME customers. The Group classifies its customer as SME Banking customer, where the loan amount is between MNT 350,000 thousand and MNT 3,000,000 thousand, or the borrower's sales amount is between MNT 1,500,000 thousand to MNT 6,000,000 thousand.
- *Retail Banking* Includes loans, deposits and other transactions and balances with retail customers and card customers. The Group classifies its customer as Retail Banking customer, where the loan amount is less than MNT 350,000 thousand, and the borrower's sales amount is less than MNT 1,500,000 thousand.
- *Investment and International Banking* Includes the Group's trading, corporate finance, borrowing from foreign financial institutions and bond issuance in the international capital market.
- *Treasury* Undertakes the Group's funding and centralised risk management activities through borrowings, issues of debt securities, use of derivatives for risk management purposes and investing in assets such as short-term placements and corporate and government debt securities. Operation is the Group's funds management activities.
- *Others* Includes Headquarter operations and central shared services operation that manages the Group's premises and certain corporate costs.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

36 Segment reporting (continued)

(In MNT'000)

| As at and for the year ended 31 December 2016 | Corporate Banking | SME Banking | Retail Banking | Investment and International Banking | Treasury | Others | Total |
|----------------------------------------------------------|------------------------------|------------------------|---------------------------|-----------------------------------------------------|----------------------|---------------------|----------------------|
| Segment results | | | | | | | |
| External revenue | | | | | | | |
| Net interest income (expenses) | 288,769,011 | 16,003,139 | (48,489,425) | (197,813,173) | 134,015,463 | (100,351) | 192,384,664 |
| Net fee and commission income | 8,809,563 | 156,656 | 20,080,641 | 246,751 | 752,647 | 572,342 | 30,618,600 |
| Other operating income (loss), net | - | 28 | 6,568,014 | 2,541,530 | 9,259,921 | (6,348,488) | 12,021,005 |
| Intersegment revenue (expenses) | <u>(190,407,980)</u> | <u>(3,709,253)</u> | <u>111,133,003</u> | <u>205,424,542</u> | <u>(122,402,115)</u> | <u>(38,197)</u> | <u>-</u> |
| Total segment revenue (expenses) | <u>107,170,594</u> | <u>12,450,570</u> | <u>89,292,233</u> | <u>10,399,650</u> | <u>21,625,916</u> | <u>(5,914,694)</u> | <u>235,024,269</u> |
| Operating expenses | (1,030,426) | (59) | (32,792,390) | (5,832,779) | (2,895,301) | (50,099,082) | (92,650,037) |
| Share of profit of associates and joint venture | | | | | | 17,296,485 | 17,296,485 |
| Reversal of (provision for) impairment losses | <u>(82,736,618)</u> | <u>(3,428,822)</u> | <u>(5,553,953)</u> | <u>-</u> | <u>(287,274)</u> | <u>9,035</u> | <u>(91,997,632)</u> |
| Profit (loss) before tax | <u>23,403,550</u> | <u>9,021,689</u> | <u>50,945,890</u> | <u>4,566,871</u> | <u>18,443,341</u> | <u>(38,708,256)</u> | 67,673,085 |
| Income tax expense | | | | | | | (212,876) |
| Net profit for the year | | | | | | | <u>67,460,209</u> |
| Non-controlling interests | | | | | | | <u>505,332</u> |
| Segment assets | <u>2,319,752,370</u> | <u>92,531,517</u> | <u>566,119,424</u> | <u>-</u> | <u>3,069,522,050</u> | <u>597,259,545</u> | <u>6,645,184,906</u> |
| Segment liabilities | <u>86,132,136</u> | <u>58,995</u> | <u>2,223,315,735</u> | <u>2,346,004,571</u> | <u>1,213,756,686</u> | <u>16,766,058</u> | <u>5,886,034,181</u> |
| Depreciation and amortisation | (4,482) | - | (3,130,419) | (5,576) | (9,669) | (9,160,617) | (12,310,763) |
| Capital expenditures | 220 | - | 4,774,835 | 127 | 5,017 | 147,328,412 | 152,108,611 |

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

36 Segment reporting (continued)

(In MNT'000)

| As at and for the year ended 31 December 2015 | Corporate Banking | SME Banking | Retail Banking | Investment and International Banking | Treasury | Others | Total |
|--------------------------------------------------|----------------------|--------------------|----------------------|--------------------------------------------|----------------------|---------------------|----------------------|
| Segment results | | | | | | | |
| External revenue | | | | | | | |
| Net interest income (expenses) | 249,508,278 | 17,413,822 | (23,806,089) | (157,995,079) | 119,683,147 | (30,468,002) | 174,336,077 |
| Net fee and commission income | 10,618,841 | 200,909 | 16,821,128 | 236,755 | 120,889 | 1,420,972 | 29,419,494 |
| Other operating income (loss), net | 420,000 | - | 3,236,722 | 61,039 | (27,469,339) | 8,559,120 | (15,192,458) |
| Intersegment revenue (expenses) | <u>(160,617,051)</u> | <u>(5,081,158)</u> | <u>82,223,497</u> | <u>164,933,852</u> | <u>(98,703,267)</u> | <u>17,244,127</u> | <u>-</u> |
| Total segment revenue (expenses) | <u>99,930,068</u> | <u>12,533,573</u> | <u>78,475,258</u> | <u>7,236,567</u> | <u>(6,368,570)</u> | <u>(3,243,783)</u> | <u>188,563,113</u> |
| Operating expenses | (1,108,930) | - | (31,344,784) | (2,257,491) | (4,859,630) | (51,846,837) | (91,417,672) |
| Share of profit of associates and joint venture | - | - | - | - | - | 12,569,455 | 12,569,455 |
| Reversal of (provision for) impairment losses | <u>(42,835,397)</u> | <u>457,390</u> | <u>(4,597,317)</u> | <u>-</u> | <u>-</u> | <u>(715)</u> | <u>(46,976,039)</u> |
| Profit (loss) before tax | <u>55,985,741</u> | <u>12,990,963</u> | <u>42,533,157</u> | <u>4,979,076</u> | <u>(11,228,200)</u> | <u>(42,521,880)</u> | <u>62,738,857</u> |
| Income tax expense | | | | | | | <u>(1,263,569)</u> |
| Net profit for the year | | | | | | | <u>61,475,288</u> |
| Non-controlling interests | | | | | | | <u>(381,090)</u> |
| Segment assets | <u>2,139,782,228</u> | <u>115,501,330</u> | <u>484,758,282</u> | <u>-</u> | <u>2,422,259,063</u> | <u>381,783,402</u> | <u>5,544,084,305</u> |
| Segment liabilities | <u>18,053,850</u> | <u>-</u> | <u>1,676,582,526</u> | <u>1,859,640,398</u> | <u>1,302,255,130</u> | <u>19,619,860</u> | <u>4,876,151,764</u> |
| Depreciation and amortisation | (8,195) | - | (2,558,440) | (5,658) | (10,462) | (8,796,672) | (11,379,427) |
| Capital expenditures | - | - | 3,047,189 | 29,874 | 10,114 | 7,094,222 | 10,181,399 |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

37 Significant transactions and balances with related parties

The following entities are considered as related parties of the Group:

- *UB City Bank and its subsidiary* The Group's chairman is a member of the board of directors of UB City Bank.
- *MIK Holding JSC and its subsidiaries("MIK")* The Group holds approximately 31.27% equity interest in MIK as at 31 December 2016. (note 6)
- *Mongolian General Leasing LLC and its subsidiary ("MGLL")* The Group holds 55% equity interest in Mongolian General Leasing LLC as at 31 December 2016. (note 6)
- *JCDecaux LLC* The Group holds 49% equity interest in JCDecaux LLC as at 31 December 2016. (note 6)
- *Valiant Art LLC* Certain key management of the Group and his immediate relative own Valiant Art LLC as at 31 December 2016.

The Group's executive officers and their immediate relatives are also considered as the Group's related parties.

Significant transactions and balances with related parties as at and for the years ended 31 December 2016 and 2015 were as follows:

| | 2016 MNT'000 | 2015 MNT'000 |
|---------------------------------------------------------------------|-------------------------------|-------------------------------|
| UB City Bank and its subsidiary: | | |
| <i>For the year ended 31 December</i> | | |
| Interest income | 8,245,657 | 7,629,444 |
| Interest expense | (1,275,662) | (4,484,327) |
| Net fee and commission income | (16) | (12) |
| <i>As at 31 December</i> | | |
| Deposits and placements with banks and other financial institutions | 124,349,000 | 99,799,000 |
| Deposits and placements by banks and other financial institutions | 12,696,603 | 9,680,503 |
| Loans and advances | 12,696,580 | 11,676,483 |
| Subordinated loans (note 9) | 4,000,000 | 4,000,000 |
| Accrued interest income | 102,182 | 13,671 |
| Accrued interest expense | 18,784 | 4,244 |
| Current account | 1,572,658 | 974,072 |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

37 Significant transactions and balances with related parties (continued)

| | 2016 MNT'000 | 2015 MNT'000 |
|----------------------------------------------------------------------|-------------------------------|-------------------------------|
| MIK: | | |
| <i>For the year ended 31 December</i> | | |
| Interest income | 6,301,629 | 4,776,022 |
| Interest expense | (4,566,995) | (1,286,789) |
| <i>As at 31 December</i> | | |
| Investment securities (note 5) | 57,919,000 | 51,814,600 |
| Deposits and placements by banks and other financial institutions | 31,610,000 | 31,720,000 |
| Accrued interest income | 794,143 | 632,980 |
| Accrued interest expense | 760,716 | 148,682 |
| MGLL: | | |
| <i>For the year ended 31 December</i> | | |
| Net fee and commission income | 310,000 | 360,000 |
| Interest income | 147,705 | 203,846 |
| Interest expense | (92,461) | (140,919) |
| Operating expense | (153) | - |
| <i>As at 31 December</i> | | |
| Other assets | - | 90,000 |
| Deposit placements by banks and other financial institutions | 5,505,292 | 3,966,494 |
| Loans and advances | 237,754 | 16,463,281 |
| Accrued interest income | 1,234 | 83,054 |
| Receivables | 1,634,160 | - |
| Other liabilities | 654 | 1,424 |
| Accrued interest expense | - | 253 |
| Lease payables | 5,742,678 | 2,577,072 |
| JCDecaux LLC: | | |
| <i>For the year ended 31 December</i> | | |
| Operating expenses | (10,071) | (69,150) |
| Valiant Art LLC: | | |
| <i>For the year ended 31 December</i> | | |
| Interest income | 255,283 | 326,074 |
| <i>As at 31 December</i> | | |
| Loans and advances | 1,968,240 | 1,963,267 |
| Accrued interest income | - | 4,738 |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

37 Significant transactions and balances with related parties (continued)

| | 2016 | 2015 |
|----------------------------------------------|----------------|----------------|
| | MNT'000 | MNT'000 |
| | <hr/> | <hr/> |
| Executive officers: | | |
| <i>For the year ended 31 December</i> | | |
| Interest income | 644,200 | 655,728 |
| <i>As at 31 December</i> | | |
| Loans and advances | 7,526,693 | 7,961,039 |
| Accrued interest income | 38,256 | 31,559 |

The loans to executive officers are included in loans and advances of the Group. Interest rates charged on mortgage loans and other loans extended to executive officers are less than would be charged in an arm's length transaction. The mortgages granted are secured by the properties of the respective borrowers.

Total remuneration and employees benefit paid to the executive officers and directors for the years ended 31 December 2016 and 2015 amounted to MNT 6,612,414 thousand and MNT 5,339,872 thousand, respectively.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

38 Categories of financial instruments

The carrying amounts of the categories of financial assets and financial liabilities as at 31 December 2016 and 2015 were summarised as follows:

(In MNT'000)

| As at 31 December 2016 | Trading | Held-to-maturity investments | Loans and receivables | Available-for-sale financial assets | Financial liabilities measured at amortised cost | Derivative held for hedging | Total |
|-------------------------------------------------------------------|-------------------|-------------------------------------|------------------------------|--------------------------------------------|---------------------------------------------------------|------------------------------------|----------------------|
| Financial assets | | | | | | | |
| Cash and due from banks | - | - | 1,188,822,410 | - | - | - | 1,188,822,410 |
| Investment securities | - | 1,115,728,071 | - | 409,707,146 | - | - | 1,525,435,217 |
| Loans and advances | - | - | 2,835,167,306 | - | - | - | 2,835,167,306 |
| Subordinated loans | - | - | 4,000,000 | - | - | - | 4,000,000 |
| Derivative assets | 70,898,721 | - | - | - | - | 288,075,402 | 358,974,123 |
| Spot trading receivables | - | - | 9,146,782 | - | - | - | 9,146,782 |
| Other assets(*1) | - | - | 209,057,978 | - | - | - | 209,057,978 |
| | <u>70,898,721</u> | <u>1,115,728,071</u> | <u>4,246,194,476</u> | <u>409,707,146</u> | <u>-</u> | <u>288,075,402</u> | <u>6,130,603,816</u> |
| Financial liabilities | | | | | | | |
| Deposits from customers | - | - | - | - | 2,415,529,106 | - | 2,415,529,106 |
| Deposits and placements by banks and other financial institutions | - | - | - | - | 143,207,671 | - | 143,207,671 |
| Bills sold under repurchase agreements | - | - | - | - | 129,960,388 | - | 129,960,388 |
| Borrowings | - | - | - | - | 1,392,176,891 | - | 1,392,176,891 |
| Debt securities issued | - | - | - | - | 1,569,366,930 | - | 1,569,366,930 |
| Subordinated debt securities issued | - | - | - | - | 24,895,300 | - | 24,895,300 |
| Derivative liabilities | 47,289,538 | - | - | - | - | - | 47,289,538 |
| Spot trading payables | - | - | - | - | 9,173,670 | - | 9,173,670 |
| Other liabilities(*2) | - | - | - | - | 152,906,967 | - | 152,906,967 |
| | <u>47,289,538</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>5,837,216,923</u> | <u>-</u> | <u>5,884,506,461</u> |

(*1) Prepayments, precious metal, inventory supplies, derivative assets and spot receivables were excluded.

(*2) Unearned income, derivative liabilities and spot payables were excluded.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES
Notes to the Consolidated Financial Statements
31 December 2016 and 2015

38 Categories of financial instruments (continued)

(In MNT'000)

As at 31 December 2015

| | Trading | Held-to-maturity investments | Loans and receivables | Available-for-sale financial assets | Financial liabilities measured at amortised cost | Derivative held for hedging | Total |
|-------------------------------------------------------------------|-------------------|-------------------------------------|------------------------------|--------------------------------------------|---------------------------------------------------------|------------------------------------|----------------------|
| Financial assets | | | | | | | |
| Cash and due from banks | - | - | 694,959,701 | - | - | - | 694,959,701 |
| Investment securities | - | 988,095,150 | - | 424,444,772 | - | - | 1,412,539,922 |
| Loans and advances | - | - | 2,644,979,616 | - | - | - | 2,644,979,616 |
| Reverse repurchase agreements | - | - | - | 99,799,000 | - | - | 99,799,000 |
| Subordinated loans | - | - | 4,000,000 | - | - | - | 4,000,000 |
| Derivative assets | 34,642,718 | - | - | - | - | 66,333,362 | 100,976,080 |
| Spot trading receivables | - | - | 104,719,018 | - | - | - | 104,719,018 |
| Other assets(*1) | - | - | 107,301,626 | - | - | - | 107,301,626 |
| | 34,642,718 | 988,095,150 | 3,555,959,961 | 524,243,772 | - | 66,333,362 | 5,169,274,963 |
| Financial liabilities | | | | | | | |
| Deposits from customers | - | - | - | - | 2,209,953,463 | - | 2,209,953,463 |
| Deposits and placements by banks and other financial institutions | - | - | - | - | 112,754,972 | - | 112,754,972 |
| Bills sold under repurchase agreements | - | - | - | - | 99,799,000 | - | 99,799,000 |
| Borrowings | - | - | - | - | 1,012,394,089 | - | 1,012,394,089 |
| Debt securities issued | - | - | - | - | 1,175,921,345 | - | 1,175,921,345 |
| Subordinated debt securities issued | - | - | - | - | 29,939,700 | - | 29,939,700 |
| Derivative liabilities | 27,904,044 | - | - | - | - | - | 27,904,044 |
| Spot trading payables | - | - | - | - | 104,718,936 | - | 104,718,936 |
| Other liabilities(*2) | - | - | - | - | 97,837,860 | - | 97,837,860 |
| | 27,904,044 | - | - | - | 4,843,319,365 | - | 4,871,223,409 |

(*1) Prepayments, precious metal, inventory supplies, derivative assets and spot receivables were excluded.

(*2) Unearned income, derivative liabilities and spot payables were excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

38 Categories of financial instruments (continued)

Net gains (losses) by financial instruments categories for the years ended 31 December 2016 and 2015 were as follows:

(In MNT'000)

For the year ended 31 December 2016

| | Interest income | Interest expenses | Fee and commission income | Other operating income | Provision for impairment loss | Net gains (losses) | Other compre- hensive income |
|--------------------------------------------------|----------------------------|------------------------------|------------------------------------------|---------------------------------------|----------------------------------------------|-----------------------------------|-------------------------------------------------|
| Held-to-maturity investments | 163,215,917 | - | - | - | - | 163,215,917 | - |
| Loans and receivables | 396,264,059 | - | 14,620,895 | - | (92,201,226) | 318,683,728 | - |
| Available-for-sale financial assets | 33,737,379 | - | - | 21,827,163 | - | 55,564,542 | 54,050,383 |
| Derivatives and spot trading | - | - | - | (15,653,147) | - | (15,653,147) | (25,032,960) |
| Financial liabilities measured at amortised cost | - | (400,832,691) | - | - | - | (400,832,691) | - |
| | <u>593,217,355</u> | <u>(400,832,691)</u> | <u>14,620,895</u> | <u>6,174,016</u> | <u>(92,201,226)</u> | <u>120,978,349</u> | <u>29,017,423</u> |

For the year ended 31 December 2015

| | Interest income | Interest expenses | Fee and commission income | Other operating income | Provision for impairment loss | Net gains (losses) | Other compre- hensive income |
|--------------------------------------------------|----------------------------|------------------------------|------------------------------------------|---------------------------------------|----------------------------------------------|-----------------------------------|-------------------------------------------------|
| Held-to-maturity investments | 105,083,652 | - | - | - | - | 105,083,652 | - |
| Loans and receivables | 365,858,215 | - | 15,088,605 | - | (44,593,884) | 336,352,936 | - |
| Available-for-sale financial assets | 61,914,886 | - | - | 411,065 | - | 62,325,951 | 3,656,568 |
| Derivatives and spot trading | - | - | - | (24,936,845) | - | (24,936,845) | 39,938,362 |
| Financial liabilities measured at amortised cost | - | (358,520,676) | - | - | - | (358,520,676) | - |
| | <u>532,856,753</u> | <u>(358,520,676)</u> | <u>15,088,605</u> | <u>(24,525,780)</u> | <u>(44,593,884)</u> | <u>120,305,018</u> | <u>43,594,930</u> |

39 Financial risk management

(a) Introduction and overview

The Group has exposure to the following risks arising from financial instruments:

- Credit risks
- Liquidity risks
- Market risks

This note provides information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established the Asset and Liability Committee ("ALCO") and Credit Committee, which are responsible for developing and monitoring the Group's risk management policies in their specified areas.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Group's Representative Governing Board ("RGB") is responsible for monitoring compliance with the Group's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Group. The RGB is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the RGB.

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31 December 2016 and 2015

39 Financial risk management (continued)

(b) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's loans and advances and investment securities.

Management of credit risk

The Board of Directors has delegated responsibility for the management of credit risk to its Credit Committee. Each branch is required to implement the Group's credit policies and procedures, with credit approval authorities delegated from the Group's Credit Committee. Each branch is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios, including those subject to central approval.

Regular audits of branches and credit processes are undertaken by Internal Audit.

An analysis of the net amounts of loans and investment securities with respective allowances at the reporting date was shown below. Classification of related loans to Troubled Asset Recovery Program("TARP") and BOM waiver applied specific asset classification and provisioning ratio.(note 7)

| <i>(In MNT'000)</i> | Loans and advances | | Investment securities | |
|----------------------------------------|---------------------------|----------------------|------------------------------|----------------------|
| | 2016 | 2015 | 2016 | 2015 |
| Carrying amount | <u>2,835,167,306</u> | <u>2,644,979,616</u> | <u>1,329,001,579</u> | <u>1,412,539,922</u> |
| Performing | 2,495,898,306 | 2,343,211,617 | 1,329,001,579 | 1,412,539,922 |
| In arrears(*) | 269,964,291 | 225,843,900 | - | - |
| Non-performing loans: | | | | |
| a) Substandard | 101,288,684 | 83,290,704 | - | - |
| b) Doubtful | 105,022,665 | 76,841,944 | - | - |
| c) Loss | 16,559,997 | 13,932,061 | - | - |
| Gross amount | 2,988,733,943 | 2,743,120,226 | - | - |
| Allowance | <u>(153,566,637)</u> | <u>(98,140,610)</u> | - | - |
| Net carrying amount | <u>2,835,167,306</u> | <u>2,644,979,616</u> | <u>1,329,001,579</u> | <u>1,412,539,922</u> |
| Letters of credit and guarantees | 639,918,016 | 393,897,555 | - | - |
| Loan and credit card commitments | 172,678,391 | 160,542,611 | - | - |
| Unfunded Syndicated risk participation | <u>111,791,240</u> | <u>134,518,272</u> | - | - |
| | <u>924,387,647</u> | <u>688,958,438</u> | - | - |

(*) Loans included in this classification are those for which contractual interest or principal payments are past due, but the Group believes that impairment is not appropriate based on the level of security/collateral available and/or the stage of collection of amounts owed to the Group.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(b) Credit risk (continued)

Impaired loans and securities

Impaired loans and securities are loans and securities for which objective evidence demonstrates that a loss event has occurred after the initial recognition of the assets and that the loss event has an impact on the future cash flows of the assets that can be estimated reliably.

Set out below is an analysis of the gross and net (after allowances for loan losses) amounts of delinquent or individually impaired assets by classifications.

| | 2016 MNT'000 | | | 2015 MNT'000 | | |
|-------------|--------------------|--------------------|-----------------------------|--------------------|--------------------|-----------------------------|
| | Gross | Net | Fair value of collateral(*) | Gross | Net | Fair value of collateral(*) |
| In arrears | 269,964,291 | 223,146,289 | 197,553,676 | 225,843,900 | 214,551,704 | 192,555,800 |
| Substandard | 101,288,684 | 75,966,513 | 75,803,959 | 83,290,704 | 62,468,028 | 61,564,992 |
| Doubtful | 105,022,665 | 52,511,332 | 49,853,563 | 76,841,944 | 38,420,972 | 37,967,140 |
| Loss | 16,559,997 | - | - | 13,932,061 | - | - |
| | <u>492,835,637</u> | <u>351,624,134</u> | <u>323,211,198</u> | <u>399,908,609</u> | <u>315,440,704</u> | <u>292,087,932</u> |

(*) The fair value of collateral represents the mitigation of credit risk due to collateral by each item. The fair value of collateral does not include mitigation of credit risk by other types of credit enhancement such as floating charge, guarantee from the third party and other tangible assets.

The Group holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Collateral generally is not held over loans and advances to banks except when securities are held as part of reverse repurchase and securities borrowing activities. Collateral usually is not held against investment securities, and no such collateral was held at 31 December 2016 or 2015.

The ultimate collectability of the loans is subject to a number of factors, including the successful performance of the debtors under various restructuring plans in place or in process of negotiation and their ability to perform on loan and debt obligations given the status of the Mongolian economy and the potential continuation of adverse trends or other unfavorable developments. Consequently, it is reasonably possible that adjustments could be made to the reserves for impaired loans and to the carrying amount of investments in the near term in amounts that may be material to the Group's consolidated financial statements.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(b) Credit risk (continued)

The Group monitors concentration of credit risk by sector. An analysis of concentration of credit risk at the reporting date is shown below:

| | 2016 MNT'000 | 2015 MNT'000 |
|--------------------------------|-------------------------------|-------------------------------|
| Agriculture | 15,714,040 | 14,999,422 |
| Mining and quarrying | 240,828,986 | 357,352,881 |
| Manufacturing | 274,246,131 | 254,559,053 |
| Petrol import and trade | 91,124,769 | 114,907,340 |
| Trading | 494,210,051 | 432,642,345 |
| Construction | 456,448,086 | 531,639,949 |
| Electricity and thermal energy | 67,796,130 | 6,214,824 |
| Hotel, restaurant and tourism | 221,693,441 | 179,258,186 |
| Financial services(*) | 341,952,173 | 166,778,566 |
| Transportation | 42,641,764 | 62,462,802 |
| Health | 19,419,045 | 21,004,416 |
| Education | 22,357,776 | 3,152,349 |
| Mortgage | 343,081,723 | 249,235,635 |
| Payment card | 82,231,423 | 96,837,809 |
| Saving collateralised | 22,195,922 | 20,802,803 |
| Others | 99,225,846 | 133,131,236 |
| Total | <u>2,835,167,306</u> | <u>2,644,979,616</u> |

(*) The Group classified the holding company that only owns shares of companies in other industries as financial services in accordance with the Group's sector codification.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)**(b) Credit risk (continued)**

As stipulated in the Banking Law of Mongolia, the total value of loans, loan equivalent assets and guarantees provided to one person or group of related persons shall not exceed 20% of the total equity of the Group. The maximum value of loans, loan equivalent assets and guarantees provided to a shareholder, the chairman, a member of the Representative Governing Board, an executive director or a Group officer or any related person thereof shall not exceed 5% of the capital of the Group, and the total amount shall not exceed 20% of the capital of the Group respectively. The criteria for concentration of loan as at 31 December 2016 are as follows:

| Description | Suitable ratios | 31 December 2016 | Violation |
|----------------------------------------------------------|-----------------|---------------------|-----------|
| The loan and guarantee given to one borrower | <Eq 20% | 17.77% | None |
| The loan and guarantee given to the single related party | <Eq 5% | 3.83% | None |
| Total loans and guarantees given to the related parties | <Eq 20% | 6.88% | None |

(c) Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations from its financial liabilities. The Group's approach for managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The Group is exposed to frequent calls on its available cash resources from current deposits, maturing deposits and loan drawdowns. The Group's ALCO sets limits on the minimum proportion of maturing funds available to cover such cash outflows and on the minimum level of interbank and other borrowing facilities that should be in place to cover withdrawals at unexpected levels of demand.

Exposure to liquidity risk

The key measure used by the Group for managing liquidity risk is the ratio of liquid assets to total liabilities, which is in line with the liquidity ratio described in Banking Law of Mongolia.

For this purpose the Group maintained a liquidity ratio; calculated as a ratio of a the Group's liquid assets, including cash on hand, deposits and placements with banks and other financial institutions, balances with BOM and investment securities to the Group's liquid liabilities; including deposit from customers, deposits and placements from the Groups and other financial institutions, loans from foreign financial institutions, taxation and debt securities issued.

Details of the reported ratio at the reporting date were as follows:

| | 2016 | 2015 |
|-------------------|------|------|
| As at 31 December | 47% | 44% |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)
(c) Liquidity risk (continued)

The following table provides an analysis of the financial assets and liabilities of the Group into relevant maturity groupings based on the remaining periods to repayment:

(In MNT'000)

| As at 31 December 2016 | Less than three months | Three to six months | Six months to one year | One to five years | Over five years | Total |
|---------------------------------------------------------------------------|-----------------------------------|--------------------------------|-----------------------------------|------------------------------|----------------------------|----------------------|
| Financial assets | | | | | | |
| Cash on hand | 73,377,054 | - | - | - | - | 73,377,054 |
| Deposits and placements with banks and other financial institutions | 658,425,089 | - | - | - | - | 658,425,089 |
| Balances with BOM | 457,020,267 | - | - | - | - | 457,020,267 |
| Investment securities | 149,865,167 | 4,983,718 | - | 626,802,724 | 743,783,608 | 1,525,435,217 |
| Loans and advances | 287,951,793 | 274,414,437 | 699,422,143 | 1,278,905,541 | 294,473,392 | 2,835,167,306 |
| Subordinated loans | - | - | 4,000,000 | - | - | 4,000,000 |
| Other assets(*1) | 175,320,673 | 50,932 | - | 378,965,005 | 22,842,273 | 577,178,883 |
| | <u>1,801,960,043</u> | <u>279,449,087</u> | <u>703,422,143</u> | <u>2,284,673,270</u> | <u>1,061,099,273</u> | <u>6,130,603,816</u> |
| Financial liabilities | | | | | | |
| Deposits from customers | 1,668,217,430 | 268,733,902 | 412,507,220 | 66,070,554 | - | 2,415,529,106 |
| Deposits and placements by banks and other financial Institutions | 61,302,134 | 49,790,600 | 32,114,937 | - | - | 143,207,671 |
| Bills sold under repurchase agreements | - | - | - | 129,960,388 | - | 129,960,388 |
| Borrowings | 178,806,622 | 232,209,355 | 263,150,348 | 483,591,267 | 234,419,299 | 1,392,176,891 |
| Debt securities issued | 206,531,928 | - | - | 1,362,835,002 | - | 1,569,366,930 |
| Subordinated debt securities issued | - | 24,895,300 | - | - | - | 24,895,300 |
| Other liabilities(*2) | 111,856,687 | 12,953,087 | 24,169,339 | 60,369,433 | 21,629 | 209,370,175 |
| Issued financial guarantee contracts | 639,918,016 | - | - | - | - | 639,918,016 |
| Unrecognised loan commitments | 172,678,391 | - | - | - | - | 172,678,391 |
| Unfunded Syndicated risk participation | 111,791,240 | - | - | - | - | 111,791,240 |
| | <u>3,151,102,448</u> | <u>588,582,244</u> | <u>731,941,844</u> | <u>2,102,826,644</u> | <u>234,440,928</u> | <u>6,808,894,108</u> |
| Net financial assets/(liabilities) | <u>(1,349,142,405)</u> | <u>(309,133,157)</u> | <u>(28,519,701)</u> | <u>181,846,626</u> | <u>826,658,345</u> | <u>(678,290,292)</u> |

(*1) Prepayments, precious metal and inventory supplies were excluded.

(*2) Unearned income was excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)
(c) Liquidity risk (continued)
(In MNT'000)

| As at 31 December 2015 | Less than three months | Three to six months | Six months to one year | One to five years | Over five years | Total |
|---------------------------------------------------------------------------|---------------------------|------------------------|---------------------------|----------------------|----------------------|----------------------|
| Financial assets | | | | | | |
| Cash on hand | 62,391,611 | - | - | - | - | 62,391,611 |
| Deposits and placements with banks and other financial institutions | 287,224,533 | - | - | - | - | 287,224,533 |
| Balances with BOM | 345,343,557 | - | - | - | - | 345,343,557 |
| Investment securities | 194,649,861 | 4,516,389 | 74,918,525 | 253,000,000 | 885,455,147 | 1,412,539,922 |
| Loans and advances | 545,091,337 | 296,818,327 | 666,009,123 | 903,391,505 | 233,669,324 | 2,644,979,616 |
| Reverse repurchase agreements | - | 99,799,000 | - | - | - | 99,799,000 |
| Subordinated loans | - | - | - | 4,000,000 | - | 4,000,000 |
| Other assets(*1) | 180,597,612 | 1,739,475 | 1,931,908 | 101,928,853 | 26,798,876 | 312,996,724 |
| | <u>1,615,298,511</u> | <u>402,873,191</u> | <u>742,859,556</u> | <u>1,262,320,358</u> | <u>1,145,923,347</u> | <u>5,169,274,963</u> |
| Financial liabilities | | | | | | |
| Deposits from customers | 1,776,286,299 | 156,730,456 | 210,551,733 | 66,384,975 | - | 2,209,953,463 |
| Deposits and placements by banks and other financial institutions | 21,580,545 | 43,969,500 | 47,204,927 | - | - | 112,754,972 |
| Bills sold under repurchase agreements | - | 99,799,000 | - | - | - | 99,799,000 |
| Borrowings | 63,158,931 | 155,508,698 | 279,239,586 | 350,482,505 | 164,004,369 | 1,012,394,089 |
| Debt securities issued | - | - | - | 1,175,921,345 | - | 1,175,921,345 |
| Subordinated debt securities issued | - | 19,959,800 | - | 9,979,900 | - | 29,939,700 |
| Other liabilities(*2) | 157,077,765 | 8,338,833 | 12,024,586 | 52,988,451 | 31,206 | 230,460,841 |
| Issued financial guarantee contracts | 393,897,555 | - | - | - | - | 393,897,555 |
| Unrecognised loan commitments | 160,542,611 | - | - | - | - | 160,542,611 |
| Unfunded Syndicated risk participation | 134,518,272 | - | - | - | - | 134,518,272 |
| | <u>2,707,061,978</u> | <u>484,306,287</u> | <u>549,020,832</u> | <u>1,655,757,176</u> | <u>164,035,575</u> | <u>5,560,181,848</u> |
| Net financial assets/(liabilities) | <u>(1,091,763,467)</u> | <u>(81,433,096)</u> | <u>193,838,724</u> | <u>(393,436,818)</u> | <u>981,887,772</u> | <u>(390,906,885)</u> |

(*1) Prepayments, precious metal and inventory supplies were excluded.

(*2) Unearned income was excluded.

39 Financial risk management (continued)

(d) Market risks

Market risk is the risk that changes in market prices, such as interest rate and foreign exchange rates will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

On 19 February 2017, the International Monetary Fund (IMF) announced an initial agreement with the Government of Mongolia for a three-year bailout programme including external financing of USD 5.5 billion. The bailout programme is conditional on various measures which the Government should put in place to improve the economy and the financial sector in the long term. These measures are expected to include tax rate increases as well as steps to reduce non-performing loans. At the date of approval of these financial statements, final signing of the agreement by the Government and the IMF is pending, and the full implications of the programme and measures for the Mongolian financial sector and for the Group specifically are as yet unclear. This creates significant uncertainty in market, regulatory, credit and other risks and the Group's future exposure to such risks, the implications of which will only be realised with time. The financial impact resulting from this bailout programme on the Group's financial statements cannot be reasonably estimated at this time, therefore no adjustments for this matter were recorded to the Group's financial statements.

Management of market risks

The Group is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest rate risk is measured by the extent to which changes in market interest rates impact margins and net income. To the extent the term structure of interest bearing assets differs from that of liabilities, net of interest income will increase or decrease as a result of movements in interest rates.

Interest rate risk is managed by increasing or decreasing positions within limits specified by the Group's management. These limits restrict the potential effect of movements in interest rates on interest margin and on the value of interest sensitive assets and liabilities.

Overall authority for market risk is vested with the ALCO.

Exposure to interest rate risks

The principal risk to which the Group's financial assets and liabilities are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands. A summary of the Group's interest rate gap position on its financial assets and liabilities are as follows:

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(d) Market risks (continued)

As at 31 December 2016

(In MNT'000)

| | Effective interest rate | Total | Non-interest sensitive | Less than three months | Three to six months | Six months to one year | One to five years | Over five years |
|---------------------------------------------------------------------|--------------------------------|----------------------|-------------------------------|-------------------------------|----------------------------|-------------------------------|--------------------------|------------------------|
| Financial assets | | | | | | | | |
| Cash on hand | - | 73,377,054 | 73,377,054 | - | - | - | - | - |
| Deposits and placements with banks and other financial institutions | 2.88% | 658,425,089 | 372,256,639 | 286,168,450 | - | - | - | - |
| Balances with BOM | | 457,020,267 | 457,020,267 | - | - | - | - | - |
| Investment securities | 14.62% | 1,525,435,217 | 104,175,747 | 45,689,420 | 4,983,718 | - | 626,802,724 | 743,783,608 |
| Loans and advances | 12.68% | 2,835,167,306 | - | 287,951,793 | 274,414,437 | 699,422,143 | 1,278,905,541 | 294,473,392 |
| Subordinated loan | 8.00% | 4,000,000 | - | - | - | 4,000,000 | - | - |
| Other assets(*1) | - | 577,178,883 | 577,178,883 | - | - | - | - | - |
| | | <u>6,130,603,816</u> | <u>1,584,008,590</u> | <u>619,809,663</u> | <u>279,398,155</u> | <u>703,422,143</u> | <u>1,905,708,265</u> | <u>1,038,257,000</u> |
| Financial liabilities | | | | | | | | |
| Deposits from customers | 6.37% | 2,415,529,106 | - | 1,668,217,430 | 268,733,902 | 412,507,220 | 66,070,554 | - |
| Deposits and placements with banks and other financial institutions | 6.70% | 143,207,671 | 45,344,034 | 15,958,100 | 49,790,600 | 32,114,937 | - | - |
| Borrowing | 5.86% | 1,392,176,891 | - | 178,806,621 | 232,209,355 | 263,150,348 | 483,591,267 | 234,419,300 |
| Bills sold under repurchase agreements | 7.50% | 129,960,388 | - | - | - | - | 129,960,388 | - |
| Debt securities issued | 9.54% | 1,569,366,930 | - | 206,531,928 | - | - | 1,362,835,002 | - |
| Subordinated debt securities issued | 8.26% | 24,895,300 | - | - | 24,895,300 | - | - | - |
| Other liabilities(*2) | - | 209,370,175 | 209,370,175 | - | - | - | - | - |
| | | <u>5,884,506,461</u> | <u>254,714,209</u> | <u>2,069,514,079</u> | <u>575,629,157</u> | <u>707,772,505</u> | <u>2,042,457,211</u> | <u>234,419,300</u> |
| Net financial assets/(liabilities) | | <u>246,097,355</u> | <u>1,329,294,381</u> | <u>(1,449,704,416)</u> | <u>(296,231,002)</u> | <u>(4,350,362)</u> | <u>(136,748,946)</u> | <u>803,837,700</u> |

(*1) Prepayments, precious metal and inventory supplies were excluded.

(*2) Unearned income was excluded.

TRADE AND DEVELOPMENT BANK OF MONGOLIA LLC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(d) Market risks (continued)

As at 31 December 2015

(In MNT'000)

| | Effective interest rate | Total | Non-interest sensitive | Less than three months | Three to six months | Six months to one year | One to five years | Over five years |
|---------------------------------------------------------------------|--------------------------------|----------------------|-------------------------------|-------------------------------|----------------------------|-------------------------------|--------------------------|------------------------|
| Financial assets | | | | | | | | |
| Cash on hand | | 62,391,611 | 62,391,611 | - | - | - | - | - |
| Deposits and placements with banks and other financial institutions | 5.5% | 287,224,533 | 97,602,110 | 189,622,423 | - | - | - | - |
| Balances with BOM | | 345,343,557 | 345,343,557 | - | - | - | - | - |
| Investment securities | 14.9% | 1,412,539,922 | 94,450,200 | 194,649,861 | 4,516,389 | 74,918,525 | 253,000,000 | 791,004,947 |
| Loans and advances | 13.6% | 2,644,979,616 | - | 545,091,337 | 296,818,327 | 666,009,123 | 903,391,505 | 233,669,324 |
| Reverse repurchase agreements | 6.1% | 99,799,000 | - | - | 99,799,000 | - | - | - |
| Subordinated loan | 8.0% | 4,000,000 | - | - | - | - | 4,000,000 | - |
| Other assets(*1) | | 312,996,724 | 312,996,724 | - | - | - | - | - |
| | | <u>5,169,274,963</u> | <u>912,784,202</u> | <u>929,363,621</u> | <u>401,133,716</u> | <u>740,927,648</u> | <u>1,160,391,505</u> | <u>1,024,674,271</u> |
| Financial liabilities | | | | | | | | |
| Deposits from customers | 6.8% | 2,209,953,463 | - | 1,776,286,299 | 156,730,456 | 210,551,733 | 66,384,975 | - |
| Deposits and placements with banks and other financial institutions | 5.3% | 112,754,972 | 11,874,249 | 9,706,296 | 43,969,500 | 47,204,927 | - | - |
| Borrowing | 5.2% | 1,012,394,089 | - | 63,158,932 | 155,508,698 | 279,239,585 | 350,482,505 | 164,004,369 |
| Bills sold under repurchase agreements | 5.0% | 99,799,000 | - | - | 99,799,000 | - | - | - |
| Debt securities issued | 9.8% | 1,175,921,345 | - | - | - | - | 1,175,921,345 | - |
| Subordinated debt securities issued | 8.7% | 29,939,700 | - | - | 19,959,800 | - | 9,979,900 | - |
| Other liabilities(*2) | | 230,460,841 | 230,460,841 | - | - | - | - | - |
| | | <u>4,871,223,410</u> | <u>242,335,090</u> | <u>1,849,151,527</u> | <u>475,967,454</u> | <u>536,996,245</u> | <u>1,602,768,725</u> | <u>164,004,369</u> |
| Net financial assets/(liabilities) | | <u>298,051,553</u> | <u>670,449,112</u> | <u>(919,787,906)</u> | <u>(74,833,738)</u> | <u>203,931,403</u> | <u>(442,377,220)</u> | <u>860,669,902</u> |

(*1) Prepayments, precious metal and inventory supplies were excluded.

(*2) Unearned income was excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(d) Market risks (continued)

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various standard and non-standard interest rate scenarios. An analysis of the Group's sensitivity to a 100 basis point (bp) increase or decrease in interest rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position) for net financial assets/(liabilities) less than one year is as follows:

| | 100 bp parallel increase MNT'000 | 100 bp parallel decrease MNT'000 |
|------------------------------------------------------------|-------------------------------------------------|-------------------------------------------------|
| | <hr/> | <hr/> |
| <i>Sensitivity of projected net interest income</i> | | |
| 2016 | | |
| At 31 December | <u>(14,547,233)</u> | <u>14,547,233</u> |
| 2015 | | |
| At 31 December | <u>(8,006,027)</u> | <u>8,006,027</u> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)
(d) Market risks (continued)
Exposure to foreign exchange rate risks

The Group is exposed to effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Group's management sets limits on the level of exposure by currencies (primarily USD) and in total. These limits also comply with the minimum requirements set by BOM.

(In MNT'000)

| | MNT denominated | 2016 Foreign currencies | Total | MNT denominated | 2015 Foreign currencies | Total |
|--------------------------------------------------------------------------|----------------------|-------------------------------|----------------------|----------------------|-------------------------------|----------------------|
| Financial assets | | | | | | |
| Cash on hand | 30,437,277 | 42,939,777 | 73,377,054 | 30,086,238 | 32,305,373 | 62,391,611 |
| Deposits and placements with banks and other financial instruments | 124,355,972 | 534,069,117 | 658,425,089 | 99,799,722 | 187,424,812 | 287,224,534 |
| Balances and deposits with the BOM | 133,806,175 | 323,214,092 | 457,020,267 | 138,049,193 | 207,294,364 | 345,343,557 |
| Investment securities | 1,421,604,807 | 103,830,410 | 1,525,435,217 | 1,325,346,534 | 87,193,388 | 1,412,539,922 |
| Loan and advances | 1,672,127,290 | 1,163,040,016 | 2,835,167,306 | 1,323,279,054 | 1,321,700,562 | 2,644,979,616 |
| Bills purchased under resale agreements | - | - | - | - | 99,799,000 | 99,799,000 |
| Subordinated loans | 4,000,000 | - | 4,000,000 | 4,000,000 | - | 4,000,000 |
| Other assets (*1) | 441,921,676 | 135,257,207 | 577,178,883 | 64,926,104 | 248,995,703 | 313,921,807 |
| | <u>3,828,253,197</u> | <u>2,302,350,619</u> | <u>6,130,603,816</u> | <u>2,985,486,845</u> | <u>2,184,713,202</u> | <u>5,170,200,047</u> |
| Financial liabilities | | | | | | |
| Deposits from customers | 1,007,248,638 | 1,408,280,468 | 2,415,529,106 | 1,084,139,596 | 1,125,813,868 | 2,209,953,464 |
| Deposits and placement by bank and other financial institutions | 1,010,892 | 142,196,779 | 143,207,671 | 840,763 | 111,914,209 | 112,754,972 |
| Bills sold under repurchase agreements | 129,960,388 | - | 129,960,388 | - | 99,799,000 | 99,799,000 |
| Borrowings | 553,094,842 | 839,082,049 | 1,392,176,891 | 409,821,669 | 602,572,420 | 1,012,394,089 |
| Debt securities issued | 160,000,000 | 1,409,366,930 | 1,569,366,930 | - | 1,175,921,345 | 1,175,921,345 |
| Subordinated debt | - | 24,895,300 | 24,895,300 | - | 29,939,700 | 29,939,700 |
| Other liabilities (*2) | 107,180,360 | 102,189,815 | 209,370,175 | 137,106,798 | 93,354,043 | 230,460,841 |
| | <u>1,958,495,120</u> | <u>3,926,011,341</u> | <u>5,884,506,461</u> | <u>1,631,908,826</u> | <u>3,239,314,585</u> | <u>4,871,223,411</u> |
| Off-balance foreign currency exposure, net | | <u>1,585,454,291</u> | | | <u>1,187,650,650</u> | |
| Net foreign currency exposure | | <u>(38,206,431)</u> | | | <u>133,049,267</u> | |

(*1) Prepayments, precious metal and inventory supplies were excluded.

(*2) Unearned income was excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(d) Market risks (continued)

Exposure to foreign exchange rate risks (continued)

A ten percent strengthening or weakening of the MNT against the USD at 31 December 2016 and 2015 would have increased (decreased) comprehensive income by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant.

| | Ten percent Strengthening MNT'000 | Ten percent Weakening MNT'000 |
|----------------|--------------------------------------------------|----------------------------------------------|
| | <hr/> | <hr/> |
| 2016 | | |
| At 31 December | 3,820,643 | (3,820,643) |
| | <hr/> | <hr/> |
| 2015 | | |
| At 31 December | (13,304,927) | 13,304,927 |
| | <hr/> | <hr/> |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

39 Financial risk management (continued)

(e) Capital Management

BOM sets and monitors capital requirements for the Group as a whole.

The Bank of Mongolia requires the Group to maintain a minimum capital adequacy ratio of 14.0% at 31 December 2016 and 2015, complied on the basis of total capital and total assets as adjusted for their risk ("CAR"), and a minimum of 9.0% at 31 December 2016 and 2015, complied on the basis of total tier 1 capital and total assets as adjusted for their risk ("TCAR").

Various limits are applied to elements of the capital base. The qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying term subordinated borrowings capital may not exceed 50 percent of tier 1 capital.

Risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

The Group's policy is to maintain a strong capital base so as to maintain investors, creditors and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Group recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Group has complied with all externally imposed capital requirements throughout the period. There have been no material changes in the Group's management of capital during the year.

On 1 April 2015, the Governor of the Bank of Mongolia announced Order A-58, which requires the Group to increase its share capital to MNT 50 billion by 31 December 2015 and not to pay dividends by 31 December 2017.

The suitable ratios of the Group's capital adequacy as at 31 December 2016 and 2015, respectively, were as following:

| | 2016 MNT'000 | 2015 MNT'000 |
|------------------------------------------------------------------------------------------|-------------------------------|-------------------------------|
| Tier 1 capital | 559,892,249 | 490,113,103 |
| Tier 2 capital | 173,983,557 | 173,222,689 |
| Total Tier 1 and Tier 2 capital | 733,875,806 | 663,335,792 |
| Risk weighted assets | 5,019,707,306 | 3,980,409,511 |
| Capital ratios | | |
| Total regulatory capital expressed as a percentage of total risk-weighted assets ("CAR") | 14.62% | 16.67% |
| Total tier 1 capital expressed as a percentage of risk-weighted assets ("TCAR") | 11.15% | 12.31% |

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

40 Fair values of financial assets and liabilities

Determination of fair value and fair value hierarchy

The Group follows the following hierarchy for determining and disclosing the fair value of financial instruments based on the level of significant inputs used in measurement.

Level 1: Fair value is based on quoted prices in active markets for identical assets or liabilities

Level 2: The inputs used for fair value measurement are market observable inputs, either directly or indirectly.

Level 3: Valuation techniques are used to estimate fair value of which significant inputs are not based on observable market data.

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

The Group determines fair values for those financial instruments which are not carried at fair value in the consolidated financial statements as follows:

(i) *Financial assets and liabilities for which fair value approximates carrying amount*

For financial assets and financial liabilities that are liquid or having short term maturity of less than one year, it is assumed that the carrying amounts approximate to their respective fair value. This assumption is also applicable to demand deposits, time deposits and variable rate financial instruments, which is principally due to the fact that the current market rates offered for similar deposit products do not differ significantly from market rates at inception.

(ii) *Fixed rate financial instruments*

The fair value of fixed rate financial assets and liabilities carried at amortised cost basis are estimated by comparing market interest rates when they were first recognised with the current market rates offered for the similar financial instruments available in Mongolia. For quoted debt issued, the fair values are measured based on quoted market prices and in case where observable market inputs are not available, a discounted cash flow model is employed.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

40 Fair values of financial assets and liabilities (continued)

(In MNT'000)

| | Note | 2016 | | 2015 | |
|---------------------------------------------------------------------|------|----------------------|----------------------|----------------------|----------------------|
| | | Carrying amount | Fair value | Carrying amount | Fair value |
| Financial assets | | | | | |
| Cash on hand | 5 | 73,377,054 | 73,377,054 | 62,391,612 | 62,391,612 |
| Deposits and placements with banks and other financial institutions | 5 | 1,115,445,356 | 1,115,445,356 | 632,568,089 | 632,568,089 |
| Investment securities | 6 | 1,525,435,217 | 1,401,861,397 | 1,412,539,922 | 1,447,532,256 |
| Loans and advances to customers | 8 | 2,835,167,306 | 2,872,860,132 | 2,644,979,617 | 2,672,755,808 |
| Bills purchased under repurchase agreements | 9 | - | - | 99,799,000 | 99,799,000 |
| Subordinated loans | 10 | 4,000,000 | 4,000,000 | 4,000,000 | 4,000,000 |
| Other assets(* 1) | 15 | 577,178,883 | 577,178,883 | 312,996,724 | 312,996,724 |
| | | <u>6,130,603,816</u> | <u>6,044,722,822</u> | <u>5,169,274,964</u> | <u>5,232,043,489</u> |
| Financial liabilities | | | | | |
| Deposits from customers | 16 | 2,415,529,106 | 2,413,087,367 | 2,209,953,464 | 2,208,001,687 |
| Deposits and placements by banks and other financial institutions | 17 | 143,207,671 | 143,207,671 | 112,754,972 | 112,754,972 |
| Bills sold under repurchase agreements | 18 | 129,960,388 | 129,960,388 | 99,799,000 | 99,799,000 |
| Borrowings | 19 | 1,392,176,891 | 1,392,176,891 | 1,012,394,089 | 1,012,394,089 |
| Debt securities issued | 20 | 1,569,366,930 | 1,372,738,626 | 1,175,921,345 | 1,151,884,991 |
| Subordinated debt securities issued | 21 | 24,895,300 | 24,461,061 | 29,939,700 | 29,501,465 |
| Other liabilities(*2) | 22 | 209,370,175 | 209,370,175 | 230,460,841 | 230,460,841 |
| | | <u>5,884,506,461</u> | <u>5,685,002,179</u> | <u>4,871,223,411</u> | <u>4,844,797,045</u> |

(*1) Prepayments, precious metal and inventory supplies were excluded.

(*2) Unearned income was excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

40 Fair values of financial assets and liabilities (continued)

The fair value hierarchy of financial instruments which are measured at fair value in the consolidated statement of financial position as at 31 December 2016 and 2015 were as follows:

(In MNT'000)

| | 2016(*2) | | | Total |
|---------------------------------|--------------------|--------------------|--------------------|--------------------|
| | Level 1 | Level 2 | Level 3(*3) | |
| Investment securities (AFS)(*1) | 103,732,318 | 213,273,508 | - | 317,005,826 |
| Derivative assets | - | 70,898,721 | 288,075,402 | 358,974,123 |
| | <u>103,732,318</u> | <u>284,172,229</u> | <u>288,075,402</u> | <u>675,979,949</u> |
| Derivative liabilities | - | 47,289,538 | - | 47,289,538 |

(*1) As at 31 December 2016, repossessed assets and unquoted equity securities at cost amounting to MNT 92,257,890 thousand and MNT 443,430 thousand, respectively, were excluded.

(*2) The fair value of level 2 financial instruments were measured by valuation technique using market observable interest rate and foreign currency exchange rate, etc.
There was no transfer between level 1 and level 2 for the year ended 31 December 2016.

(*3) The fair value of level 3 financial instrument was measured by discounted cash flow method using market unobservable forward exchange rate. USD to MNT forward exchange rate is 3,373.18 as at 31 December 2016.

A ten percent strengthening or weakening of input unobservable in markets as at 31 December 2016 would have increased or decreased other comprehensive income by MNT 82,467,530 thousand.

Total gains or losses for the period recognised in the profit or loss and other comprehensive income related to financial instruments in level 3 were MNT 273,170,000 thousand and MNT 14,905,402 thousand for the year ended 31 December 2016.

There was no transfer between level 3 and other levels for the year ended 31 December 2016.

(In MNT'000)

| | 2015(*2) | | | Total |
|---------------------------------|-------------------|--------------------|--------------------|--------------------|
| | Level 1 | Level 2 | Level 3(*3) | |
| Investment securities (AFS)(*1) | 94,006,770 | 329,994,572 | - | 424,001,342 |
| Derivative assets | - | 34,642,718 | 66,333,362 | 100,976,080 |
| | <u>94,006,770</u> | <u>364,637,290</u> | <u>66,333,362</u> | <u>524,977,422</u> |
| Derivative liabilities | - | 27,904,044 | - | 27,904,044 |

(*1) As at 31 December 2015, unquoted equity securities at cost amounting to MNT 443,430 were excluded.

(*2) There was no transfer between level 1 and level 2 for the year ended 31 December 2015.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

40 Fair values of financial assets and liabilities (continued)

(*3) The fair value of level 3 financial instrument was measured by discounted cash flow method using market unobservable forward exchange rate. USD to MNT forward exchange rate is 2,549.04 as at 31 December 2015.

A ten percent strengthening or weakening of input unobservable in markets as at 31 December 2015 would have increased or decreased other comprehensive income by MNT 61,572,401 thousand.

Total gains or losses for the period recognised in the profit or loss and other comprehensive income related to financial instruments in level 3 were MNT 26,395,000 thousand and MNT 39,938,362 thousand for the year ended 31 December 2015.

There was no transfer between level 3 and other levels for the year ended 31 December 2015.

The fair value of level 2 financial instruments were measured by valuation technique using market observable interest rate and foreign currency exchange rate, etc.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

40 Fair values of financial assets and liabilities (continued)

The fair value hierarchy of financial instruments which are not measured at fair value in the consolidated statement of financial position as at 31 December 2016 and 2015 were as follows:

(In MNT'000)

| | 2016 | | | Total |
|------------------------------------------------------------------------|-------------------|----------------------|----------------------|----------------------|
| | Level 1 | Level 2 | Level 3 | |
| Cash on hand | 73,377,054 | - | - | 73,377,054 |
| Deposits and placements with banks and other financial institutions | - | - | 1,115,445,356 | 1,115,445,356 |
| Investment securities (HTM) | - | 1,084,855,571 | - | 1,084,855,571 |
| Loans and advances | - | - | 2,872,860,132 | 2,872,860,132 |
| Subordinated loans | - | - | 4,000,000 | 4,000,000 |
| Spot receivables | 9,146,782 | - | - | 9,146,782 |
| Other assets(*1) | - | - | 209,057,978 | 209,057,978 |
| | <u>82,523,836</u> | <u>1,084,855,571</u> | <u>4,201,363,466</u> | <u>5,368,742,873</u> |
| Deposits from customers | - | - | 2,413,087,367 | 2,413,087,367 |
| Deposits and placements by banks and other financial institutions | - | - | 143,207,671 | 143,207,671 |
| Bills sold under repurchase agreements | - | - | 129,960,388 | 129,960,388 |
| Borrowings | - | - | 1,392,176,891 | 1,392,176,891 |
| Debt securities issued | - | 1,372,738,626 | - | 1,372,738,626 |
| Subordinated debt securities issued | - | 24,461,061 | - | 24,461,061 |
| Spot payables | 9,173,670 | - | - | 9,173,670 |
| Other liabilities(*2) | - | - | 152,906,967 | 152,906,967 |
| | <u>9,173,670</u> | <u>1,397,199,687</u> | <u>4,231,339,284</u> | <u>5,637,712,641</u> |

(*1) Prepayments, precious metal, inventory supplies, derivative assets and spot receivables were excluded.

(*2) Unearned income, derivative liabilities and spot payables were excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

40 Fair values of financial assets and liabilities (continued)

(In MNT'000)

| | 2015 | | | |
|------------------------------------------------------------------------|--------------------|----------------------|----------------------|----------------------|
| | Level 1 | Level 2 | Level 3 | Total |
| Cash on hand | 62,391,612 | - | - | 62,391,612 |
| Deposits and placements with banks and other financial institutions | - | - | 632,568,089 | 632,568,089 |
| Investment securities (HTM) | - | 1,023,530,914 | - | 1,023,530,914 |
| Loans and advances | - | - | 2,672,755,808 | 2,672,755,808 |
| Bills purchased under resale agreements | - | - | 99,799,000 | 99,799,000 |
| Subordinated loans | - | - | 4,000,000 | 4,000,000 |
| Spot receivables | 104,719,018 | - | - | 104,719,018 |
| Other assets(*1) | - | - | 60,467,724 | 60,467,724 |
| | <u>167,110,630</u> | <u>1,023,530,914</u> | <u>3,469,590,621</u> | <u>4,660,232,165</u> |
| Deposits from customers | - | - | 2,208,001,687 | 2,208,001,687 |
| Deposits and placements by banks and other financial institutions | - | - | 112,754,972 | 112,754,972 |
| Bills sold under repurchase agreements | - | - | 99,799,000 | 99,799,000 |
| Borrowings | - | - | 1,012,394,089 | 1,012,394,089 |
| Debt securities issued | - | 1,151,884,991 | - | 1,151,884,991 |
| Subordinated debt securities issued | - | 29,501,465 | - | 29,501,465 |
| Spot payables | 104,718,936 | - | - | 104,718,936 |
| Other liabilities(*2) | - | - | 50,968,312 | 50,968,312 |
| | <u>104,718,936</u> | <u>1,181,386,456</u> | <u>3,483,918,060</u> | <u>4,770,023,452</u> |

(*1) Prepayments, precious metal, inventory supplies, derivative assets and spot receivables were excluded.

(*2) Unearned income, derivative liabilities and spot payables were excluded.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

41 Offsetting financial assets and liabilities

Details of financial assets and financial liabilities subject to offsetting, enforceable master netting agreements and similar agreements as at 31 December 2016 and 2015 are as follows:

(In MNT'000)

| | 2016 | | | | | |
|-----------------------------------------------|---------------------------------------------------|-----------------------------------------------------------------|----------------------------------------------------------------|------------------------------------------------------------------|-----------------------------|-------------------|
| | Financial assets and liabilities recognised | Offsetting financial assets and liabilities recognised | Financial assets and liabilities recognised after offset | Amount not offsetting in the statements of financial position | | Total |
| | | | | Financial instruments | Cash collateral received | |
| Financial assets | | | | | | |
| Derivative assets(*1) | - | - | - | 9,146,782 | - | - |
| Receivable spot exchange(*1) | 9,146,782 | - | 9,146,782 | - | - | - |
| | <u>9,146,782</u> | <u>-</u> | <u>9,146,782</u> | <u>9,146,782</u> | <u>-</u> | <u>-</u> |
| Financial liabilities | | | | | | |
| Derivative liabilities(*1) | 20,657,925 | - | 20,657,925 | 9,146,782 | - | 20,684,813 |
| Payable spot exchange(*1) | 9,173,670 | - | 9,173,670 | - | - | - |
| Bills sold under repurchase agreements(*2) | 129,960,388 | - | 129,960,388 | 129,960,388 | - | - |
| | <u>159,791,983</u> | <u>-</u> | <u>159,791,983</u> | <u>139,107,170</u> | <u>-</u> | <u>20,684,813</u> |

(*1) The Group has certain derivative transactions subject to the ISDA (International Derivatives Swaps and Dealers Association) agreement. According to the ISDA agreement, when credit events (e.g. default) of counterparties occur, all derivative agreements are terminated and set off.

(*2) Resale and repurchase agreement, securities borrowing and lending agreement are also similar to ISDA agreement with respect to enforceable netting agreements.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

41 Offsetting financial assets and liabilities (continued)

(In MNT'000)

2015

| | Financial assets and liabilities recognised | Offsetting financial assets and liabilities recognised | Financial assets and liabilities recognised after offset | Amount not offsetting in the statements of financial position | | Total |
|-------------------------------------------------|---------------------------------------------------|-----------------------------------------------------------------|----------------------------------------------------------------|------------------------------------------------------------------|-----------------------------|------------------|
| | | | | Financial instruments | Cash collateral received | |
| Financial assets | | | | | | |
| Derivative assets(*1) | 45,893 | - | 45,893 | | | |
| Receivable spot exchange(*1) | 3,994,152 | - | 3,994,152 | 3,994,152 | - | 45,893 |
| Bills purchased under resale agreements (*2) | 99,799,000 | - | 99,799,000 | 99,799,000 | - | - |
| | <u>103,839,045</u> | <u>-</u> | <u>103,839,045</u> | <u>103,793,152</u> | <u>-</u> | <u>45,893</u> |
| Financial liabilities | | | | | | |
| Derivative liabilities(*1) | 7,965,038 | - | 7,965,038 | | | |
| Payable spot exchange(*1) | 3,994,428 | - | 3,994,428 | 3,994,152 | - | 7,965,314 |
| Bills sold under repurchase agreements(*2) | 99,799,000 | - | 99,799,000 | 99,799,000 | - | - |
| | <u>111,758,466</u> | <u>-</u> | <u>111,758,466</u> | <u>103,793,152</u> | <u>-</u> | <u>7,965,314</u> |

(*1) The Group has certain derivative transactions subject to the ISDA (International Derivatives Swaps and Dealers Association) agreement. According to the ISDA agreement, when credit events (e.g. default) of counterparties occur, all derivative agreements are terminated and set off.

(*2) Resale and repurchase agreement, securities borrowing and lending agreement are also similar to ISDA agreement with respect to enforceable netting agreements.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

42 Commitment and contingent liabilities**Financial guarantees and letters of credit**

At any time the Group has outstanding commitments to extend credit, these commitments take the form of undrawn portions of approved loans, credit card limits and overdraft facilities.

The Group provides financial guarantees and letters of credit to guarantee the performance of customers third parties. These agreements have fixed limits and generally extend for a period of less than one year. The Group also provides guarantees by acting as settlement agent in securities borrowing and lending transactions. The contractual amounts of commitments and contingent liabilities are set out in the following table by category.

The amounts reflected in the table for guarantees and letters of credit represent the maximum exposure to credit risk would be recognised at the reporting date if counterparties failed completely to perform as contracted.

| As at 31 December | 2016 MNT'000 | 2015 MNT'000 |
|----------------------------------------|-------------------------------|-------------------------------|
| Letters of credit and guarantees | 639,918,016 | 393,897,555 |
| Loan and credit card commitments | 172,678,391 | 160,542,611 |
| Unfunded Syndicated risk participation | 111,791,240 | 134,518,272 |

A significant portion of the contingent liabilities and commitments will expire without being advanced in whole or in part. Accordingly, the amounts do not represent expected future cash flows.

EMC Matter

In January 2017, a working group (WG) formed by Legal Standing Committee of Parliament of Mongolia issued an investigation report on the Mongolian Copper Corporation's acquisition of 49% stake in Erdenet Mining Corporation (EMC) (the "Deal"), where the Group provided financing to Mongolian Copper Corporation LLC (MCC).

The WG's report alleged that the Group might have financed the Deal indirectly through the loans originated to United Energy System LLC (UES) and Kanetic LLC (KNK) in addition to the above mentioned loans to MCC were able to acquire 49% of EMC Shares, together with funding from other companies' such as QSC LLC and Riverstone Properties LLC. The report alleged that the Group's loan extended to the companies involved in the Deal exceeded the limits on the exposure to single party and related parties per the Banking Law of Mongolia. Furthermore, the report alleged that the fund provided to the Deal might have been originally provided by Government of Mongolia (GoM) to the Group. Based on this allegation, the report claims that the Group breached the limits on the exposure to single related party and related parties per the Banking Law of Mongolia.

Based on the report, Mongolia Parliament announced resolution in February 2017 that GoM shall take 49% share from MCC and payment to be made shall deduct the alleged funding from GoM to the Group and GoM shall implement required actions on those who breached Mongolian laws and regulations.

Bank of Mongolia (BoM) investigated all relevant documents and other documents furnished to State Legal Entities Registration Office (SLERO). The Group also submitted monthly related party loan reports to BoM. BoM did not formally communicate with the Group regarding any findings from their investigation.

Notes to the Consolidated Financial Statements

31 December 2016 and 2015

42 Commitment and contingent liabilities (continued)

EMC Matter (Continued)

As of the end of 2016 total exposure to the Group was as below:

- KNK paid fully its loan back in August 2016 and there is no outstanding balance.
- UES's loan is performing normal and has outstanding balance of USD 21,522,755.61
- MCC's loan is performing normal and has outstanding balance of USD 55,969,719.59

The Group believed that loans to those entities were extended within legal and regulatory framework of Mongolia and the Group did not breach single and related party loan exposure in terms of loans extended to above mentioned entities, based on the documents furnished to SLERO and to the Group by MCC, KNK and UES.

Even in case of the EMC's 49 percent share is taken by the GoM from MCC above loans will be paid before their maturity and at this time it is uncertain any adverse effect and material loss may cause to the Group.

43 Interests in unconsolidated structured entities

Nature of risk associated with interests in unconsolidated structured entities as at 31 December 2016 was as follows:

| Type | Nature and purpose | Financing | Total Assets |
|------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------|---------------------|---------------------|
| | To generate: | | |
| Securitisation vehicles for loans and advances | <ul style="list-style-type: none"> ▪ funding for the Group's lending activities. ▪ fees for loan servicing. | Issue of RMBS notes | 2,150,867,102 |
| | These vehicles are financed through the issue of notes to investors. | | |

Exposure to risk relating to interests in unconsolidated structured entities as at 31 December 2016 was as follows:

| | Securitisation vehicles for loans and advances |
|-----------------------|-------------------------------------------------------|
| Asset: | |
| Investment securities | 57,919,000 |