Best Corporate Governance
2014, 2015, 2016, 2017 and 2018
AFGHANISTAN

Bank of the Year
2012, 2013, 2014, 2015, 2016 and 2017
AFGHANISTAN

AIB
بانك بين المللى افغانستان
Afghanistan International Bank

Your Partner for Growth

Annual Report 2017

Our Vision

We aspire to remain the most reputable financial institution and bank of choice in Afghanistan.

Our Mission

Our mission is to foster economic development in Afghanistan, to be a catalyst for growth, and ultimately contribute to the prosperity of the country and its people.

We strive to adhere to international best practices in corporate governance, financial and risk management (including anti-money laundering and 'know your customer'), customer service, operations, information technology, and internal controls. A major factor in our success is dedication to staff development and training within a culture of integrity and professionalism.

Our Future

Through our financial performance and the specific investments we have made in our people and infrastructure, AIB has become a positive emblem for achievement and transformation, despite its challenging environment.

In our second decade of operation, we remain committed to enabling a better future for Afghanistan and we are proud to play a role in shaping the opportunities that lie ahead.

Contents

From inception in 2004, Afghanistan International Bank's major objective has been to assist in developing the Afghan economy and to conduct business in accordance with international standards of governance and integrity. The many awards received from authoritative industry bodies is independent endorsement of AIB's success in achieving its goals, notably being named *The Banker* magazine's 'Bank of the Year, Afghanistan' for six consecutive years from 2012 to 2017.

AIB is now well-established as an industry leader, and widely acknowledged to be the nation's most respected and trusted financial institution. Its growth as an enduring institution combines international expertise with intimate local knowledge and a deep-rooted understanding of customer needs.

Despite the political, security, and economic conditions that existed in Afghanistan during the year, I am pleased to report that the Bank's financial performance in 2017 was highly successful, with all major financial targets being achieved.

Unfortunately, we do not see significant improvements in the overall situation in Afghanistan going into 2018. Hence, the Bank will continue to maintain a conservative position for the foreseeable future.

AIB's success continues to be driven by its reputation for integrity, good governance, and attention to customer needs. Our position as the most respected financial institution and the bank of choice in Afghanistan has become stronger over time.

In 2017, the Board and management continued to pursue the strategic agenda developed over the past several years. Following is a summary of the progress the Bank has made during 2017 against these objectives:

Achieve world-class standards in anti-money laundering and financial crime compliance

In 2017, with the assistance of an external consultant, management continued to improve implementation of policies and procedures involving these compliance functions. Staff training continued during the year, as well as monitoring to ensure procedures were followed. The Compliance Committee was also established.

The full Board received quarterly reports on key indicators regarding this programme. The project team will continue into 2018 as there is more work to be done. As one can imagine, implementing world-class procedures in AML and FCC affects AIB's staff and our customers. In 2018 management will bolster the Compliance Department's capabilities to act as a second line of defence for this important function.

Complete the new head office building in June 2017

Unfortunately, due to a number of circumstances beyond the Bank's control, the head office building was delayed beyond the June target date.

However, staff will begin to move into the new building in March 2018. This will be a major milestone in the Bank's development as this building will reflect the important position AIB holds in the banking system in Afghanistan.

Focus on organisation and human resource development

This initiative continued to be a key long-term priority, with the objective of developing the capabilities and competencies of senior Afghan staff to replace expatriate management over the next three to five years, and to generally build staff competencies across the Bank. To this end, several senior Afghan staff have been promoted to executive positions with increased responsibilities. We continued to overhaul personnel administration, job descriptions, and job grading, and to put in place a comprehensive succession planning programme. All senior management had staff training and development objectives in their annual goal statement.

Position for the future in underserved markets and product offerings: Shariah banking, small business banking, and electronic banking

This initiative is intended to position AIB in the small business and consumer segments in the long term. There has been uplift in business as a result of actions taken by management over the past year, and we expect to see increased business especially in Afghani currency deposits and Shariah loans. A lending programme for small businesses met with moderate success, mainly due to reluctance of businesses to borrow. This initiative is basically an investment in the future.

Maintain existing correspondent banking relationships and develop new relationships for US dollar clearing

AIB continued its correspondent banking relationship with Standard Chartered Bank during the year. At this point, we see no threat to that relationship; however, management has stepped up the search for another correspondent bank. This is not easy due to Afghanistan's poor risk profile among international banks. Management has begun to open direct accounts with banks in major trading partner countries to serve customers' payment needs in those countries.

Maintain financial stability and satisfactory returns

AIB had a successful financial 2017 and our forecast for the next three years shows slightly higher profitability, mainly stemming from our very strong fee-based business (49 percent of AIB's revenues are from fees and foreign exchange activities).

During 2017, the Board had several changes in its composition and membership:

- Veronica John resigned from her director position on 31 December due to ill-health. We were particularly saddened to learn of her death in January 2018. Ms John made an invaluable contribution to AIB over 14 years. The shareholders, Board, and management offer our heartfelt condolences to her family, and record our appreciation for her tenure as a director.
- Salman Shoaib resigned from the Board during 2017. Mr. Shoaib served on the Board for five years from 2012 and was chair of the Investment Committee. I thank him sincerely for his contribution to the Board and the Bank.
- Samuel Sidiqi and Hugo Minderhoud joined the Board as directors in late 2017. Messrs Sidiqi and Minderhoud bring extensive governance and banking experience to the Board.
- The Investment Committee was folded into the Planning and Strategy Committee to streamline meetings and the Board structure.
- The Audit Committee will be joined by Mr. Minderhoud to strengthen its oversight role.

As a result, the Board will have six members and five committees going into 2018: Risk, Remuneration, Nominating, Planning and Strategy, and Audit. The activities of these committees are highlighted in another section of this report.

The Board met 12 times in 2017: four in-person meetings and eight conference calls. In particular, the Board focused on the strategic agenda mentioned above, as well as closely monitoring the security situation in the country.

The Board and senior management undertook a three-year strategic planning exercise during 2017. A three-year time horizon was chosen due to the political, security, and economic uncertainties in the country. A longer horizon involved too much guesswork under the circumstances. Key points in the plan are:

- Afghanistan will continue to get by over the next three years, although the overall situation in the country will not provide much economic growth. However, this provides an opportunity for AIB to consolidate its position as the leading bank by addressing selective market opportunities and continuing to strengthen internal capabilities:
  - Take market share in lending from weak competitors
  - Invest in segments that have potential future growth, for example, small and mid-sized companies
  - Build external and internal capabilities for improving service to customers and strengthening systems, processes, and people skills
- Internally, investment in staff training is a key area of focus over the three years.
- Building the Audit Department's capability to become the third line of defence for management and the Board is another priority for management, in line with international best practice.
- Finally, the plan calls for achieving 15 percent return on equity.

The final terms and conditions for the Internal Finance Corporation (IFC) to purchase a 7.5 percent stake in the Bank from existing shareholders was completed in late 2017, and shares were exchanged between the shareholders in November. The IFC will invest another 7.5 percent through the issuance of new shares. This second investment will take place within the next two years.

Other highlights of 2017 include:

- For the sixth consecutive year The Banker magazine voted AIB 'Best Bank in Afghanistan'. We are proud of this honour, which reflects the professionalism of the Bank.
- For the fifth consecutive year, AIB was recipient of the prestigious 'Best Corporate Governance – Afghanistan' award from the London-based Capital Finance International organisation.
- For the third year, AIB took a stand at the SWIFT International Banking Operations Seminar (SIBOS) held in Toronto, Canada. Two of the Bank's Afghan staff attended the conference, in addition to our CEO, Mr. Barned. At the conference, several international banks expressed interest in working with AIB in a variety of ways.

As I noted earlier, it is unclear whether conditions in Afghanistan will improve in 2018. Each year I find myself stating the same cautious words about the political, security, and economic conditions in Afghanistan. However, that is the reality of the situation. 2018 appears to be no different.

In closing, I would like to again thank the staff of the Bank as well as my fellow Board members and shareholders for their support and dedication to the institution.

Ronald Stride
Chairman

At a time when the combined balance sheet of the overall banking system is shrinking, I am pleased to be able to advise that AIB expanded in a number of areas during 2017.

60.93bn
Assets increased by 4.7 percent

2.27bn
Revenue increased by 13 percent

Assets increased by 4.7 percent to AFN 60.93 billion (2016: AFN 58.19 billion), bringing compound annual asset growth since 2010 to 15.18 percent. The increase was led by a 4.0 percent rise in deposits to AFN 56.26 (AFN 54.08 billion). Commercial lending was subdued throughout the year.

Revenue increased by 13 percent to AFN 2.27 billion (AFN 2.02 billion). Non-interest income accounted for 49 percent of total revenue, the growth being led by the 37 percent increase in outward international transfers to AFN 3.03 billion from AFN 2.22 billion in 2016.

The volume of outward transfers grew to 31,500 transactions, while AIB also received 37,500 inward transfers totalling AFN 2.37 billion. Together, these transactions underline the value of strong correspondent partnerships and sound regulatory compliance.

Active management of the Bank's bond portfolio also contributed to growth, generating revenue of AFN 0.36 billion. Total revenue was also assisted by the liquidation of real estate collateral for just under AFN 0.32 billion, even though loan recovery was negatively affected by the arduous and very lengthy process for foreclosure and obtaining vacant possession.

Operating expenses increased by 20 percent, as was anticipated when preparing the budget, driven by: additions to executive management and engagement of new staff in expectation of opening the new head office branch; increased costs relating to compliance and professional advisors (44 percent); and a rise in security costs (28 percent).

With both revenues and expenses being in line with budget, the Bank was able to achieve a 14 percent increase in pre-tax profit to AFN 0.646 billion (AFN 0.567 billion). Net profit showed a reduction of 31 percent to AFN 0.358 billion (AFN 0.519) following a one-off income tax provision based on the assessment order for the financial years 2012, 2013, and 2014. Included is one major business expense related to a Department of Justice action in the USA (see note 14.1), not allowed as a deductible expense by the tax department of the Ministry of Finance. The Bank considers this ruling arbitrary in nature and has filed an appeal which is still pending.

Subject to approval at the annual general meeting, the final dividend will be AFN 0.42 billion (interim: AFN 0.412 billion), bringing total distribution to shareholders to AFN 0.832 billion for the year. This equates to dividend per share of AFN 27.73.

Total equity after payment of the interim dividend decreased by 2.0 percent from AFN 3.90 billion to AFN 3.84 billion. Our capital adequacy ratio of 15.42 percent and 65.92 percent liquidity ratio are very satisfactory by domestic and international standards.

Business initiatives

Despite a quiet year for generating new loans in corporate and institutional banking, we were able to participate in a number of development projects by providing performance guarantees and other related support to international construction companies. These totalled AFN 3.74 billion, relating to 14 projects including roads, railways, and telecommunications.

Our Business and Community Banking units, which are responsible for the small and middle market segment as well as development finance, signed a $25 million memorandum of understanding with the Afghanistan Industrial Association to support local production and manufacturing companies, using conventional and Islamic structures. I am pleased to be able to mention here that with excellent collaboration between the Bank's lending units and our Shariah banking unit, we are experiencing a significant increase in requests for Shariah-compliant loans.

To assist our customers with their international trade transactions, we have Standard Chartered Bank as our major international clearing bank, as well as correspondent banking relationships with State Commercial Bank of Turkmenistan and Asaka Bank in Uzbekistan. The latter support bilateral trade with two major trading partners, and we are also working towards a correspondent relationship with a British bank and a Russian bank.

Having experienced slow loan growth through much of the year, in the last quarter AIB developed a product to promote borrowing among medium-sized manufacturing companies where previously the cost and collateral requirements made access to loans challenging.

AIB introduced loans of AFN 7 million to AFN 35 million at 7.5 percent annual interest, designed to promote local products and encourage manufacturers to expand and create more jobs. The facility is available only in Afghani currency as a term loan of up to three years, payable in monthly instalments. These loans are guaranteed by the Afghan Credit Guarantee Foundation (ACGF), established with funding from the German government and USAID and subsequently from the World Bank, to facilitate access to finance for Afghan small and medium enterprises. ACGF's participation allows AIB to reduce both its interest rate and collateral requirement.

As I indicated earlier, AIB's loan portfolio did not expand in 2017. AIB believes that one reason for this is that Da Afghanistan Bank, the central bank, is over-regulating the banking sector. A typical example is the focus on collateral as the primary requirement for loan approval. AIB believes that collateral requirements should be a decision for the Bank's Board and management – for example, enabling loans to exporters who have no need to own real estate and are therefore unable to provide collateral.

Although our commercial lending departments were relatively quiet, Consumer Banking implemented a series of initiatives designed to enhance customer care and add to the ease and simplicity of doing business with AIB.

Extended opening hours – from 8am to 8pm – now apply at four branches, one in Kabul and three in provinces (Mazar, Herat, and Kandahar). We also plan to open a 'smart' branch in Kabul where all cash activities will be handled by interactive teller machines (ITMs) – the modern version of the traditional ATM. Fast-deposit and pay-in counters have also been established in large branches and all ATMs are now equipped with anti-skimming protection. Added functionalities include inter-account transfers and cash deposits.

One centralised portal has been established for customer feedback, and all customer-facing employees were trained by an outsourced company in how best to facilitate customer needs. A new quality control team is now responsible for customer service improvement.

Electronic banking advances included e-commerce activation, enabling MasterCard acceptance on customers' websites. Consumer loan applications and card modifications are now available online.

We also launched a new Islamic credit card and introduced in-house printing and personalisation of all cards (chip and magstripe), speeding production and the turnaround time for delivery to customers. A new agreement with the World Food Programme enables direct payment to beneficiary families through a pre-paid card.

As in previous years, AIB undertook a thorough review and upgrade of crucial business operations, adopting the 'three lines of defence' approach based on best-practice policies and procedures for anti-money laundering, compliance, and internal audit. We have furthered strengthened our resources and capabilities in these areas, largely based on the 2015 guidelines for corporate governance stipulated by the Basel Committee on Banking Supervision.

The guidelines state that a risk governance framework should include well-defined organisational responsibilities for risk management, typically referred to as the three lines of defence:

- The business line
- A risk management function and a compliance function independent from the first line
- An internal audit function independent from the first and second lines

In conjunction with an internationally recognised expert – formerly global head of financial crime compliance for correspondent banking with a major international bank – we also focused closely on updating and improving data quality for 'know your customer' requirements and financial crime compliance. An anti-bribery and corruption policy was also developed and approved by the Board.

Further activities under the broad heading of rigorous compliance included installing new and more sophisticated software for transaction monitoring and comprehensive screening. This interfaces with our core banking system, analysing all daily entries and comparing them with certain benchmarks to check for irregularities.

Enhancements to corporate governance include a management information system for the Board of Supervisors and correspondent banks, generating detailed reports so that our improvements can be monitored quarterly, while the launch of an 18-month programme for financial crime compliance will enhance our capabilities even further. Together with risk tolerance measures for financial crime compliance, the Board carefully monitors and checks that the Bank conforms with requirements in every way.

Overall, these activities have helped achieve our goal of a high level of compliance implementation and control, especially in terms of the demanding requirements that are now imposed by our correspondent banks.

The Bank also participated in a number of domestic and international exhibitions and seminars. Domestically, we presented lending products to the top 70 Afghan traders and exporters, at the invitation of USAID to the US embassy, and also participated in a round table with HE Eklil Hakimi, Afghanistan's Minister of Finance, again presenting AIB lending products and services to traders and entrepreneurs. Wider community involvement extended to sponsoring conferences such as Business Expo, Youth to Business Forum, and the Afghanistan Industrial Festival.

Internationally, AIB was again represented at SIBOS, the annual conference, exhibition, and networking event organised by SWIFT for the financial industry. Held in Toronto, the event was an excellent opportunity to refresh existing relationships and establish new ones.

We also represented Afghanistan at the International Chamber of Commerce's Trade Finance Conference in London on a panel discussion of 'Access to Finance in Frontier Markets'.

We also participated in Afghanistan's 98th Independence Day celebrations in Dubai.

A first for AIB was coverage in *The Economist* magazine, which carried an article on AIB subtitled 'The value of a good reputation in a troubled country'. We continue to seek international media coverage, not only for AIB but to improve the image of Afghanistan.

Community

In keeping with AIB's commitment to good corporate citizenship, we continued to support projects that have a beneficial impact on the communities where we operate. We again contributed to Women for Afghan Women, a New York-based grassroots organisation concerned with human rights and women's rights in Afghanistan; to the American University of Afghanistan; and to Save the Children, Shamsa Children Village Orphanage, and Amiri Medical Complex.

Closer to home, the Bank has taken many wide-ranging steps to support its female employees, aiming to play a positive role in developing their careers and ambitions. For female staff, AIB has arranged:

- Work requirements to ensure that women are able to attend university at the same time as having a job
- Transport to and from homes, offices, and universities
- A comprehensive childcare system in all offices, freeing mothers to advance their careers

In closing, I take this opportunity to express sincere thanks to our shareholders and Board for their continued confidence and support; to our loyal customers for their patronage; and to our management. To our employees, I offer special thanks for their dedication and hard work throughout 2017 in what was a very challenging environment.

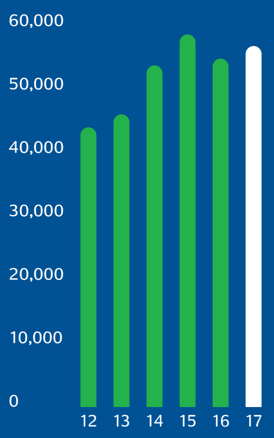
Anthony Barned
Chief Executive Officer

Record pre-tax profit was the leading highlight of 2017's results.

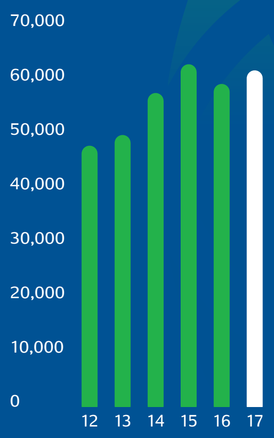
646mn
Net profit before tax

2.27bn
Revenue

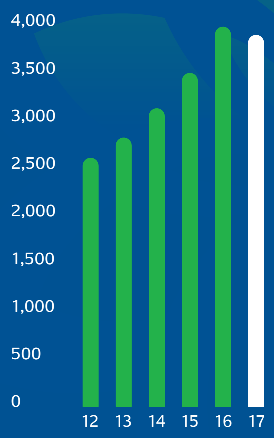
Deposits
(AFN millions)



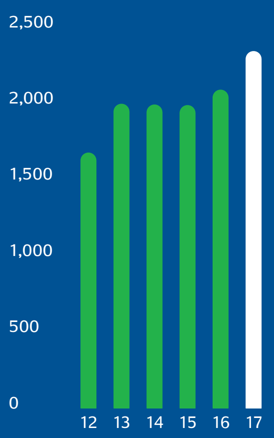
Total assets
(AFN millions)



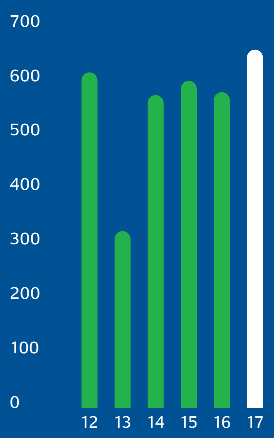
Capital growth
(AFN millions)



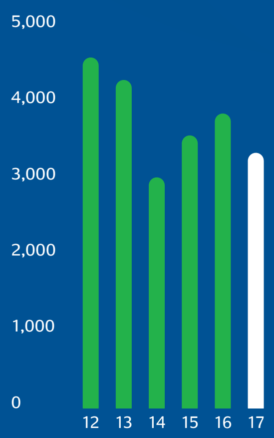
Revenues
(AFN millions)



Net profit before tax
(AFN millions)



Advances
(AFN millions)



Afghanistan's economic growth reflected a slightly upward trend during 2017.

However, due to the security situation and political instability, economic activity was still sluggish.

Gross domestic product (GDP) grew 3.60 percent, compared to an average of 11.12 percent between 2003 and 2016, reaching an all-time high of 28.60 percent in 2003 and a record low of 2.10 percent in 2016. Strong growth in the agricultural and industrial sectors was responsible for most of the 2017 improvement.

The inflation rate was 3.08 percent in December 2017, averaging 4.62 percent over 2016 and 2017. Inflation reached a record low of 0.70 percent in January 2016, and an all-time high of 7.37 percent in July. Per capita income in 2017 was estimated at $663.

Exports in Afghanistan improved to $596 million in 2017 from $571.50 million in 2016.

Exports averaged $486.66 million from 2008-09 until 2017, reaching an all-time high of $596 million in 2017. However, due to presidential elections, exports recorded a low of $376-388 million in 2013-2014. Exports account for around 20 percent of GDP, mainly carpets and rugs (45 percent); dried fruits (31 percent); and medicinal plants (12 percent). Core export partners are Pakistan (48 percent of total) and India (19 percent). Exports to India significantly increased in 2017, as well as to Russia (9 percent). Other export markets include Iran, Iraq, and Turkey.

Imports decreased to $6,534 million in 2017 from $7,723 million in 2016. Imports averaged $6,422 million from 2008-09 until 2017, reaching an all-time high of $9,069 million in 2013 and a record low of $3,020 million in 2008-09.

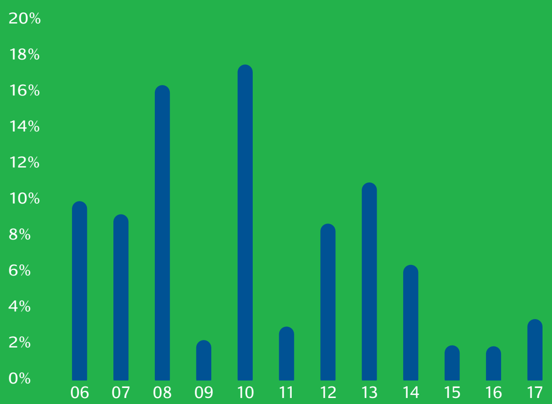
596mn

Exports in Afghanistan improved to $596 million in 2017 from $571.50 million in 2016

3.60

Gross domestic product (GDP) grew 3.60 percent

Afghanistan GDP annual growth rate (% pa)



Afghanistan inflation rate 2016-2017

Source: Central Statistics Organisation of Afghanistan.

Main imports are: petroleum (33 percent of total), machinery and equipment (15 percent), food items (14 percent), and base metals and related articles (9 percent). The main import partners are Pakistan (14 percent of total), Russia (13 percent), Uzbekistan (11 percent), Iran (9.1 percent), and China (9 percent). Others include Malaysia, China, Indonesia, Turkmenistan, Japan, Kazakhstan, and Middle Eastern countries.

Banks' lending to the private sector has continued to decline over the past three years. Total banking sector loans dropped slightly in 2017 to $582 million, compared to $613 million in 2016 and $747 million in 2015. Banking sector lending is not projected to rise much faster as banks tighten credit standards in the face of a deteriorating economy. Meanwhile, banks' total deposits decreased to $3.762 billion from $3.82 billion the previous year.

The Afghani currency depreciated slightly by 1.49 percent against the US dollar in the first half of 2017. Foreign exchange reserves increased in September 2016, from AFN 477,665 million ($6.851 billion) to AFN 512,160 million ($7.345 billion), before dropping in December 2016 to AFN 500,916 million ($7.185 billion) – equivalent to 13 months of imports. Overall reserves increased between March and December 2017, largely due to the decline in imports, resulting from weakening demand and slightly higher exports in 2017.

Afghanistan was removed from the grey list by the Financial Action Task Force (FATF) in 2017. FATF welcomed Afghanistan's significant progress in improving its AML/CFT regime and noted that it has established the legal and regulatory framework to meet the commitments in its action plan regarding the strategic deficiencies that FATF had identified in June, 2012. Afghanistan is therefore no longer subject to FATF monitoring.

Economic development and the livelihood of Afghans will improve due to the Central Asia-South Asia power project (CASA 1000), the TAPI gas pipeline, the Salma Dam becoming operational, and construction of other small dams. The possible inclusion of Afghanistan in the Chinese-Pakistan Economic Corridor (CPEC) and Asian Development Bank (ADB) grants in the energy sector will further help GDP. ADB and the World Bank provide long-term support for national development projects, in health, women's empowerment, transport, energy, natural resources, and economic management.

ADB collective lending to Afghanistan totals almost $1 billion and approved grants amount to $3.3 billion. The country also secured its financial commitment from international donor communities for the next five years, with $3.5 billion per year pledged at the Brussels Conference 2016. The Government also received the same level of annual assistance from Tokyo Conference ($3.9 billion per year).

Dependence on transit through neighbouring countries has been a historical challenge for Afghanistan, but with the establishment of the new Lapis Lazuli Corridor accord, the country has acquired a direct link to transport goods to Europe by road, rail, and sea. Goods will be transported through Turkmenistan, across the Caspian Sea to Azerbaijan, then Georgia, and across the Black Sea and through Turkey to the Mediterranean and Europe.

Similarly, The Sino-Afghan Special Railway Transportation connects Afghanistan to China's 'One Belt, One Road' trade corridor that links Uzbekistan, Kazakhstan. China has always shown interest in investment in the region and in fostering commercial ties with Afghanistan, especially in constructing railways, dams, roads, and housing; carrying out electricity projects; and importing Afghan hygiene products to the main Chinese markets.

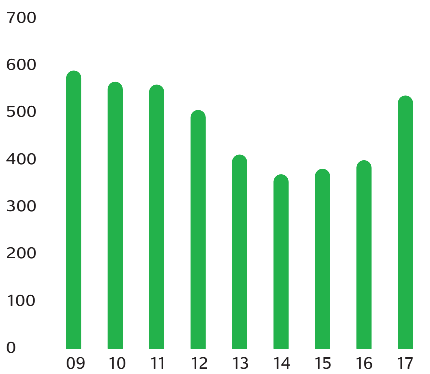
In addition, the Chabahar seaport is opening a gateway for trade with India and Afghanistan. The Afghan government received $2,064 million from donors in 2016-17, against total commitment of $2,894 million.

Along with the continuing deterioration of the security situation, the country is facing a humanitarian crisis. More than 296,000 Afghans returned from Pakistan and Iran in 2017; 202,000 were internally displaced by conflicts, and another 44,000 by natural disasters. The return of refugees from neighbouring countries will place further pressure on the economy over the next two years.

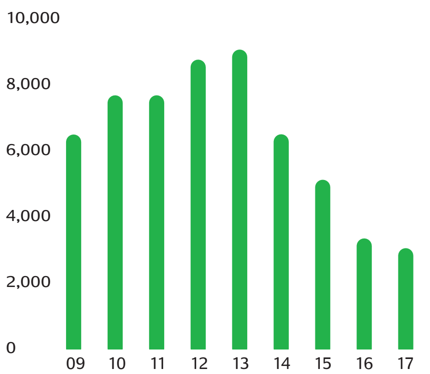
The 3.6 percent GDP growth in 2017 is projected to fall to 3.4 percent in 2018 and 3.1 percent in 2019. However, the US administration's new strategy for Afghanistan is expected to improve the security situation, economic growth, and political stability.

Sources: World Bank database, Da Afghanistan Bank, Asian Development Bank, Central Statistics Organisation of Afghanistan, IMF.

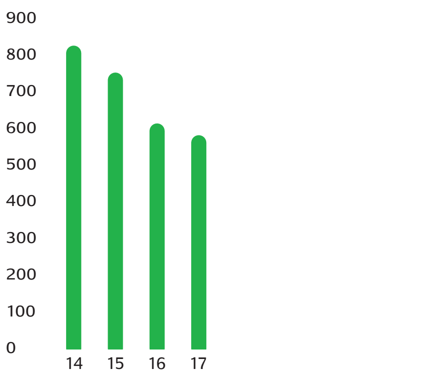
Afghanistan exports 2009-2017
(USD millions)



Afghanistan imports 2009-2017
(USD millions)



Banks' lending to private sector
(USD millions)



Source: Da Afghanistan Bank

Ronald Stride
Independent Director, Chair of the Board of Supervisors, Chair of the Strategy and Planning Committee, Member of the Remuneration Committee, the Nominating Committee, and the Risk Committee

Mr Stride spent most of his career with Booz Allen & Hamilton, the management consulting firm, where he was a senior vice-president and managing partner for Asia. He also served on the firm's Board of Directors in the USA. Mr Stride has been a member of AIB's Board since November 2009. He is currently a member of several business boards as well as chairing a large Singapore-based charity – Food from the Heart. He was formerly president of the American Association of Singapore, a position he held for five years. Mr Stride received his BA from Providence College in the USA.

Hamidullah A. Mohib
Shareholder-appointed Member of the Board of Supervisors, Member of the Remuneration Committee, the Nominating Committee, the Risk Committee, and the Audit Committee

Mr Mohib has been a member of the board since 2005. He is an executive director at Mohib Holdings, responsible for strategic planning and treasury operations for the group's various activities in Central Asia and the Middle East. Mr Mohib was educated at King's University College at the University of Western Ontario.

Hugo Minderhoud
Independent Director, Member of the Audit Committee

Mr Minderhoud joined the board in December 2017. He is based in Tashkent, Uzbekistan where he is senior advisor to Ipak Yuli Bank Uzbekistan. He has worked in various capacities in Central Asia and the former Soviet Union since 1994, at first with ABN AMRO Bank, Netherlands; and since 2006 as independent financial advisor and board member of various banks and companies in the region.

He holds a law degree from Leiden University in The Netherlands.

Veronica John

Independent Director, Chair of the Remuneration Committee and the Nominating Committee, Member of the Strategy and Planning Committee

Ms John had been a member of the AIB Board since 2004. She resigned in 2017 due to ill-health, and sadly died early in 2018.

She had more than 30 years' experience in international finance, especially in emerging markets in Asia and the CIS, specialising in private equity funds, diversified fund of funds management, and investment banking. She was a senior managing director at Diamond Dragon Advisors, a private equity general partner advisory and fund placement business. She was also chief executive of IDFC Capital, an emerging markets private equity fund of funds business, and was a member of the Asian Development Bank team that founded AIB. Ms John graduated with a BA from Elmira College and an MBA from George Washington University.

Samuel Sidiqi

Independent Director, Member of the Remuneration Committee, Nominating Committee, and the Strategy and Planning Committee

Mr Sidiqi joined the Board in 2017. He is currently the Chief Executive Officer of NREC, a Middle East-focused real estate developer listed on the Kuwait Stock Exchange. He previously worked with Agility Logistics in Europe, America, Asia, and the Middle East, and began his career at Bain & Company where he advised Fortune 500 clients on strategy. Mr Sidiqi has an MBA from the Wharton School and an MA from the Lauder Institute, both of the University of Pennsylvania. He has bachelor's degrees in economics and political science from MIT and was a Fulbright Fellow.

Aditya Srivastava

Independent Director, Chair of the Risk Committee, and Member of the Strategy and Planning Committee

Mr Srivastava has been a Board member since August 2012. He is chief commercial officer of Wasl Asset Management Group, a Government of Dubai-owned corporation with interests in property, hospitality, and leisure. Before joining Wasl in 2008, he had a 20-year career in banking, the last 10 years with Société Générale where he was GCC head of project finance and corporate relationships. Mr Srivastava holds a master's degree in economics from the Delhi School of Economics and is a member of the Institute of Chartered Accountants in England and Wales.

Lutfullah Rahmat

Shareholder-appointed Member of the Board of Supervisors, Member of the Strategy and Planning Committee, the Nominating Committee, and the Risk Committee

Mr Rahmat is past-chairman of AIB and has been a member of the Board since the Bank's inception in 2004. He is also managing director of the Rahmat Group, the Karachi-based company that has Star Textile Mills Ltd as its principal member; president of Rahmat Fruit Processing Corporation; and a partner in the sole agents for Samsung Electronics and Appliances in Afghanistan. He graduated with a BCom from Bombay University.

As a matter of principle and good business practice, AIB has conducted its banking business in an ethical, prudent, and professional manner, according to international standards of governance.

Philosophy of governance

AIB endeavours to enhance shareholder value; protect the interests of all stakeholders including shareholders, customers, employees, regulators, and the public at large; and ensure compliance with international best practices for financial institutions. The Bank complies with all legal and regulatory requirements of Afghanistan – but also formulates and adheres to strong corporate governance practices beyond what is mandated by regulators. In fact, 'international' in our name reflects the standard of performance we strive to achieve.

The adoption and implementation of corporate governance is the direct responsibility of the Board of Supervisors. In this role, the Board ensures that the management of the Bank is meeting the requirements and obligations of good governance.

Shareholders

The Bank has three shareholders, each with an ownership percentage as shown in the table below. The shareholders operate under a policy of non-interference in management decisions and the Bank's operations. The positive reputation and widespread business interests and relationships of the Bank's shareholders in Afghanistan have contributed significantly to the success of the institution. Each shareholder has the right to appoint one individual to the Board of Supervisors.

Shareholder	Beneficial shareholder	Type of company	Incorporated	Board members	Ownership %
International Finance Corporation (IFC)	Not applicable	Global development institution	Washington, District of Columbia	No one appointed	7.50
Horizon Associates	Mohammed Abrahim Mohib	Holding Company	Delaware, USA	Lutfullah Rahmat	46.25
Wilton Holdings	Lutfullah Rahmat, Izzatullah Rahmat, Nasrullah Rahmat	Holding Company	Cayman Islands	Hamidullah A. Mohib	46.25

Board of Supervisors

The major purpose of the Board of Supervisors is to formulate the overall strategic and financial objectives of the Bank; to monitor these objectives and ensure they are met by management; and to ensure that the risks associated with operating a financial institution in Afghanistan are managed and mitigated as far as possible. Ensuring the upholding of good corporate governance is key to the Bank achieving its goals, and the Board ensures that best practices are maintained.

The Board is composed of the Chairman, shareholder-appointed directors, and independent directors. The Chairman is an independent director, which complies with Central Bank regulations.

Independent Board members are in the majority, in line with regulations and international governance standards. According to the Articles of Association, each shareholder has the right to appoint one shareholder-designated director. The shareholders have agreed to a Board of Supervisors consisting of seven individuals. There are currently seven Board members: five independent and two shareholder-appointed. This reduced to six with the resignation of one independent director on 31 December 2017. It is the intention of the shareholders and the Board to fill this vacancy at the annual general meeting of shareholders to be held in March 2018. Brief biographical profiles of the seven current directors are included in this annual report.

The Chairman is a non-executive director and is responsible for leadership of the Board and ensuring its effectiveness. Shareholder-nominated directors are appointed by the respective shareholders of the Bank and represent the interests of these shareholders. There are currently two shareholder-appointed directors.

Finally, the independent directors are expected to bring impartial judgement to the Board through their expertise in the financial world, as well as governance experience through having served on other boards. Independent directors and directors who are shareholder representatives are elected/appointed for terms of four years, but must stand for reappointment each year.

The Board has five committees: Remuneration; Nominating; Risk; Planning and Strategy; and Audit. Each committee has a Chairman and a formal charter to guide its activities.

The Board of Supervisors meets monthly: four times in person and the balance by conference call. The Committees of the Board meet four times a year in person and in conjunction with Board meetings, with occasional conference calls. Board committee meetings are attended by the Chief Executive Officer. Minutes of committee meetings are circulated to all Board members for their information. The role of these committees is explained in more detail in the following subsections.

In 2017, the Board met 12 times. During each meeting the Board monitored the financial performance of the Bank as well as the status of non-performing loans and operational risks. Each quarter, the Board reviewed the anti-money laundering/ compliance dashboard to ensure the Bank's adherence to the policies and procedures established for this function by outside experts. The Bank has invested significant resources into compliance, resulting in very satisfactory implementation of these policies and procedures, although more needs to be done.

In addition to routine matters conducted during the year, the Board and shareholders approved the purchase of 15 percent of the Bank by the Internal Finance Corporation (IFC). This acquisition reflects the sound position of AIB in Afghanistan and the Bank's commitment to help develop the economy of Afghanistan. We are proud that the IFC has chosen AIB as the commercial bank to invest in.

Another major achievement in 2017 was the completion of the Bank's second strategic plan. The first plan was formulated in 2012 to cover a period of five years. The new plan spans three years through 2020, and is focused on external market development and internal capability-building.

The Board and shareholders were planning to have the Bank's new headquarters building completed in 2016, but unfortunately, due to delays, the head office will now be occupied in the first quarter of 2018. We are excited about finally having our own headquarters building.

Planning and Strategy Committee

The committee is responsible for AIB's strategic plan and annual business plan and budget. It also monitors management's performance quarterly against plans. At its July meeting, the Board decided to merge the Planning and Investment Committees, as there was significant overlap in committee memberships and this action was deemed to more efficient in managing the affairs of the Bank.

In 2017, the committee met four times in person. Specific accomplishments during the year were:

- Developing a three-year strategic plan to cover the years 2018 to 2020
- Developing the business plan and budget for 2018
- Instituting planning by business unit/segment
  - Developing plans for each business unit: corporate and institutional, business banking, community banking, and consumer banking.
  - Developing profit and loss statements and balance sheets for each business unit
  - Establishing a method for monitoring each unit's plans
- Monitoring the investment portfolio, which yielded 2.63 percent (about $5 million) in interest income in 2017
- Approving a plan to realise additional major contract guarantee business
- Approving model branch cost/benefit analysis to include staffing and organisation, physical layout, cost structure, service standards, and performance measures
- Approving a revised organisation structure for the Bank

As a part of its ongoing responsibilities, the committee monitored progress of the 2017 business plan and budget each quarter. As the political, security, and economic conditions in Afghanistan are not likely to improve in 2018, the committee has taken a conservative approach to planning the Bank's activities and finances.

Risk Committee

The Board's committee to provide comprehensive oversight and best practices in risk governance and risk management.

The principal role of the committee is to review the Bank's risk exposure under different products. This encompasses foreign exchange positions, assets and liabilities, capital adequacy, credit and market risk, and sovereign risk. The committee also reviews performance of the classified and non-performing loan portfolio, and, most importantly, reviews and submits to the Board of Supervisors all the Bank's policies associated with risk management. Finally, the committee identifies unacceptable risk conditions to the full Board for consideration and action.

The Board and the shareholders of AIB place high priority on implementing, maintaining, and developing the highest standards in anti-money laundering (AML) and counter-terrorism financing (CTF). During the year, AIB completed a financial crime compliance/AML project with the assistance of a reputed external firm to ensure 'know your customer', AML, and CTF processes are best in class. The committee introduced a measure to ensure the early detection of borrowers who appear to be having problems in their business. The committee also oversaw other key initiatives during the year, including an external consultant completing a credit risk review of the Bank's loan portfolio, with recommendations currently being implemented, as well as refinements to the Bank's business continuity plan. A new chief risk officer has been appointed to further strengthen the risk function.

The committee was pleased to note that the external consultancy that conducted an IT penetration audit had commended AIB's IT architecture, and provided assurance that the Bank would be able to withstand an external attack on its systems.

Due to uncertainties in the economic outlook for Afghanistan, the Risk Committee adopted a conservative approach for the Bank's risk profile. This approach will continue in 2018 to ensure that the balance between risk and return is maintained.

Audit Committee

The Audit Committee is responsible for overseeing financial reporting; compliance with risk management policies and procedures; internal controls; ethical behaviour; and management and functioning of the internal audit department. Consistent with previous years, in 2017 the committee assessed and approved the annual internal audit plan, including budget and resources, and regularly monitored progress of the plan. The committee also reviews the Bank's annual budget and business plan, and recommends to the Board of Supervisors the payment of dividends. The committee regularly monitors and assesses the role and effectiveness of the internal audit function.

The committee receives quarterly reports from major operational segments of the Bank, reviewed at every quarterly committee meeting. The reports include the key performance indicators of different segments and issues related to operational and financial controls.

The committee discussed control environment issues reported by the Internal Audit Department, their root causes and management responses, and remediation activities. Significant audit issues were also brought to the committee's attention.

The committee is responsible for relationships with the external auditors, and meets them on completion of the annual audit and quarterly reviews. On the committee's recommendation, the Board of Supervisors approves the annual financial statements and three quarterly-reviewed condensed financial information. These meetings enable committee members to discuss matters relating to the external auditors' remit and issues arising from the audit.

During 2017, the committee regularly focused on the controls and issues related to anti-money laundering and countering financing of terrorism.

The committee currently has four members, all qualified and experienced in audit, accounting, or banking. Under Afghanistan banking regulations, the Board of Supervisors may appoint members to the Audit Committee who are not members of the Board of Supervisors.

Any individual who is proposed to join the committee is subject to the same fit and proper requirements as members of the Board of Supervisors. The committee currently has two non-board members.

Remuneration Committee

The Remuneration Committee has five major responsibilities:

- Establish compensation policies for the Bank's senior management to include base salary, fringe benefits, and bonus scheme.
- Establish performance goals for each member of senior management and monitor performance against these goals.
- Establish and review development and succession plans for senior management.
- Recommend to the full Board for final decision on matters relating to senior management compensation and bonus actions.
- Review and approve the Bank's human resource policies.

The committee has four members, three of whom are independent directors including the Chairperson, Veronica John. In 2017, the committee met four times in person in conjunction with Board meetings. Major undertakings by the committee during the year included:

- Reviewed action plan and timeline to upgrade all human resource functions: organisation of HR department, succession planning, skills gap analysis, career planning, job grading, performance management, training needs analysis, and employee on-boarding method.
- Approved revised senior management compensation policy.
- Reviewed, approved and monitored senior management goal statements.
- Reviewed and approved 2016 bonus and salary actions for senior management.
- Approved revised HR policy manual.
- Reviewed and approved amended staff compensation scheme covering pay scales, job grades, and the like.
- Approved succession and transition plan for CEO and key managers, and introduced corporate titles along with a revised organisation chart.
- Reviewed staff mortgage scheme.

Many of the agenda items tabled by the committee were directed towards installing a more professional HR function in the Bank and having comprehensive and transparent HR policies.

A challenge for AIB is the ability to deploy world-class human resource leadership and knowledge in a country lacking the depth of management skills necessary to achieve the Bank's objectives in this regard. This challenge has been further exasperated by regulations limiting the use of foreign management in the HR function.

Nominating Committee

The Nominating Committee works as a preparatory committee for the Board of Supervisors with respect to nomination and appointment of candidates to the Board of Supervisors, the Management Board, and other key senior managers as determined by the committee.

The committee is composed of five members of the Board of Supervisors, including the Chairman of the Board; two members representing employees; and two members representing shareholders. A majority of the members are independent. At least one-third of the Independent Directors of the Board are committee members.

In 2017, the committee met four times in person, in conjunction with Board meetings, and held a number of conference calls to interview Board candidates. The committee's major activities for 2017 were:

- Interviewing candidates to fill two Board positions. In all, five candidates were shortlisted and two were nominated for approval to the full Board, and subsequently to the shareholders and the Central Bank.
- The committee also reviewed and approved candidates to fill key management positions: Head of Banking, Head of Internal Audit, and Chief Risk Officer.
- The committee also developed a checklist for evaluating Board candidates.
- The committee nominated Mr. Hugo Minderhoud, a new director, to be a member of the Audit Committee.
- The committee also submitted existing Board members for re-appointment at the Annual General Meeting of shareholders.

Committee members spent considerable time and effort in 2017 due to the substantial number of positions to fill on the Board and in senior management.

Committee meetings and attendance records

Key: ⊙ Attended ○ Absent ⦸ was not a member during this period

Board	24 Jan 2017	21 Feb 2017	11 Mar 2017	18 Apr 2017	23 May 2017	20 June 2017	8 July 2017	22 Aug 2017	23 Sept 2017	16 Oct 2017	21 Nov 2017	9 Dec 2017
Ronald Stride, Chairman	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Veronica John	⊙	⊙	⊙	⊙	⊙	○	⊙	⊙	⊙	○	⊙	⊙
Hamidullah A. Mohib	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	○	⊙	⊙
Lutfullah Rahmat	⊙	⊙	⊙	○	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Salman Shoaib	⊙	○	⊙	⊙	○	⦸	⦸	⦸	⦸	⦸	⦸	⦸
Aditya Srivastava	⊙	⊙	⊙	⊙	⊙	⊙	⊙	○	⊙	⊙	⊙	⊙
Samuel Sidiqi	⦸	⦸	⦸	⦸	⦸	⦸	⦸	⦸	⊙	⊙	⊙	⊙
Hugo Minderhoud	⦸	⦸	⦸	⦸	⦸	⦸	⦸	⦸	⦸	⦸	⦸	○

Planning & Strategy/ Planning, Strategy & Investment (from 23 Sept 2017)	10 Mar 2017	7 July 2017	22 Sept 2017	8 Dec 2017
Ronald Stride, Chairman	⊙	⊙	⊙	⊙
Veronica John	⊙	⊙	⊙	⊙
Lutfullah Rahmat	⊙	⊙	⊙	⊙
Aditya Srivastava	⊙	⊙	⊙	⊙
Samuel Sidiqi	⦸	⦸	⦸	⊙

Risk Committee	10 Mar 2017	7 July 2017	22 Sept 2017	8 Dec 2017
Ronald Stride, Chairman	⊙	⊙	⊙	⊙
Hamidullah A. Mohib	⊙	⊙	⊙	⊙
Lutfullah Rahmat	⊙	⊙	⊙	⊙
Aditya Srivastava	⊙	⊙	⊙	⊙

Investment Committee (disbanded from 23 Sept 2017)	10 Mar 2017
Ronald Stride, Chairman	⊙
Salman Shoaib	⊙
Aditya Srivastava	⊙

Remuneration Committee	10 Mar 2017	7 July 2017	22 Sept 2017	8 Dec 2017
Ronald Stride, Chairman	⊙	⊙	⊙	⊙
Veronica John	⊙	⊙	⊙	⊙
Hamidullah A. Mohib	⊙	⊙	○	⊙
Salman Shoaib	⊙	⦸	⦸	⦸
Samuel Sidiqi	⦸	⦸	⦸	⊙

Nominating Committee	24 Jan 2017	6 Feb 2017	8 Feb 2017	9 Feb 2017	11 Mar 2017	22 Sept 2017	8 Dec 2017
Ronald Stride, Chairman	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Veronica John	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Hamidullah A. Mohib	⊙	⊙	⊙	⊙	⊙	○	⊙
Lutfullah Rahmat	⊙	⊙	⊙	⊙	⊙	⊙	○
Salman Shoaib	○	⊙	⊙	⊙	⊙	⦸	⦸
Samuel Sidiqi	⦸	⦸	⦸	⦸	⦸	⦸	⊙

Audit Committee	6 May 2017	12 Aug 2017	14 Nov 2017	28 Feb 2017	5 July 2017	21 Sept 2017	7 Dec 2017
Said Arab Khan, Chairman	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Marion Day	○	⊙	○	⊙	○	⊙	○
Hamidullah A. Mohib	⊙	○	⊙	⊙	⊙	⊙	⊙
Hugo Minderhoud	⦸	⦸	⦸	⦸	⦸	⦸	○

Management Profiles

Anthony Barned
Chief Executive Officer,
Chairman of Management Board

Mr. Barned assumed the position in April 2016, having worked with the Bank in an advisory role and chairing the Audit Committee for the previous seven years. He brings more than 40 years of international commercial banking experience, with the Barclays group and Bank of Ceylon and as a consultant with Booz Allen & Hamilton. He is an Associate of the Chartered Institute of Bankers, London.

Lalit Kumar Jha
Chief Finance Officer,
Member of Management Board

Mr. Jha holds a bachelor's degree in commerce and is a qualified chartered accountant with more than 20 years' experience, mainly in the banking sector. He has been CFO at AIB since 2010, having previously been senior vice-president at Dresdner Bank, New Delhi, and head of accounts and taxation at Bank of Tokyo Mitsubishi UFJ, New Delhi.

Asadullah Fayzi
Chief Operating Officer,
Member of Management Board

Mr. Fayzi holds the dual positions of CIO and COO, having joined AIB at its inception in 2004 as head of IT, and having previously been IT manager for Afghanistan Reconstruction Company. He was appointed to his current position during 2012. He holds an MSc in telecommunications from Istanbul Technical University, Turkey.

Omer Omery
Head of Retail Banking,
Member of Management Board

Mr. Omery has more than a decade of banking experience with AIB, from managing a regional branch to electronic banking, marketing, and retail banking. He also spent three years in a managerial position with the United Nations. He holds an MBA from the University of Liverpool, England.

Wissam Jarkassi
Chief Risk Officer

Mr. Jarkassi joined AIB in July, 2017. He holds a bachelor's degree in accounting, a master's in banking and capital markets, and is a certified financial risk manager. He has more than 16 years' banking experience in different areas, mainly credit. He was previously a senior consultant at Solution & More, the financial services specialist, and before that headed risk management at Banque Misr Liban in Lebanon.

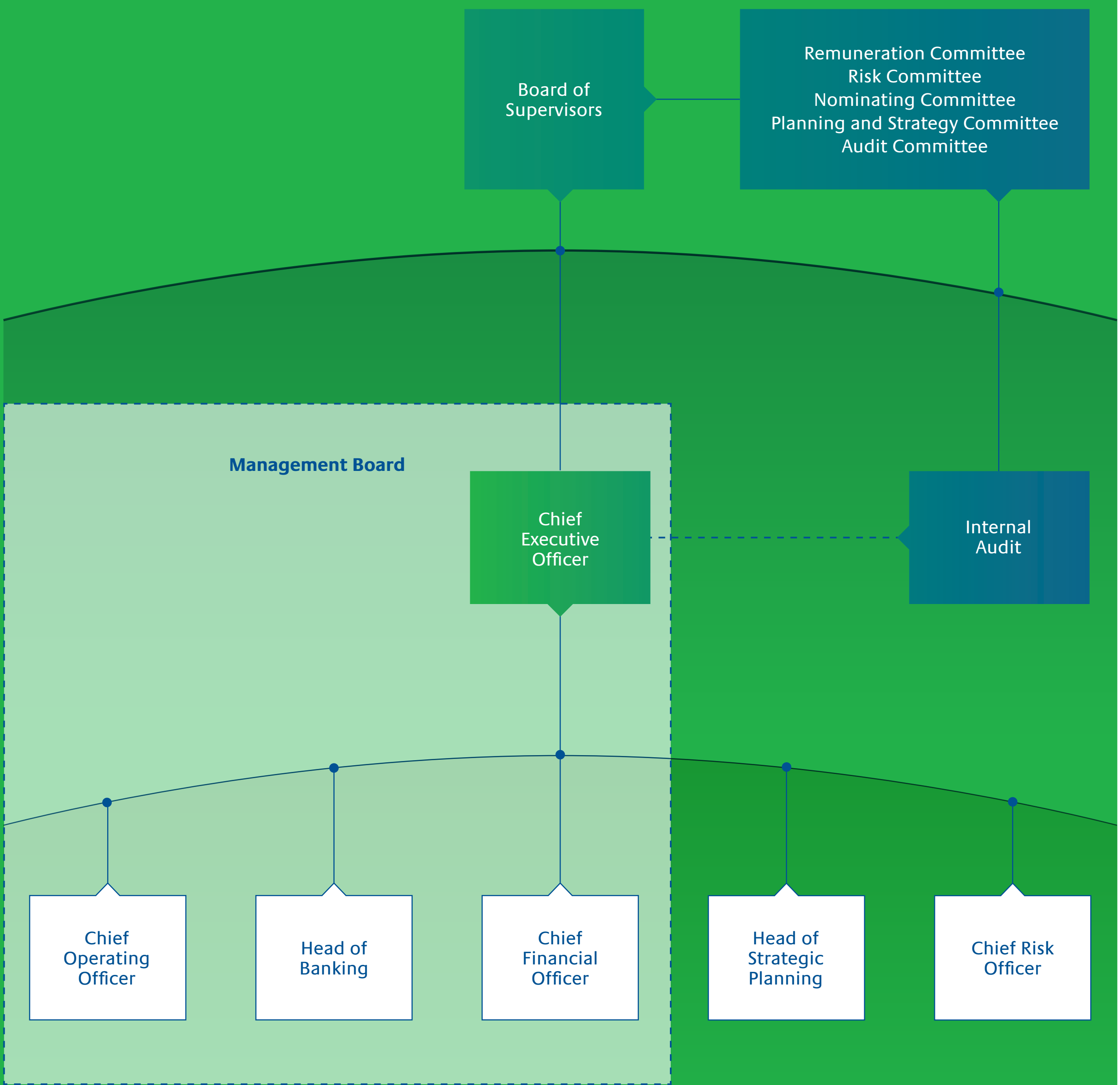
Mohammad Taofiq Mir
Head of Strategic Planning

Mr. Mir began his banking career in 2006 with AIB. He managed electronic banking channels and was head of retail banking before becoming head of strategic planning in 2014. He also leads the Bank's programme to enhance anti-money laundering processes. Mr Mir holds a BSc in electrical engineering from Delft University of Technology, Netherlands.

Bishwajit Mazumder
Head of Internal Audit

Mr. Mazumder is a qualified chartered accountant, certified internal auditor, and certified information systems auditor. He also holds a law degree from India and is a USA-certified fraud examiner. He has more than 30 years' experience in banking in various institutions in different geographies and cultures, including more than a decade of heading internal audit.

Organisation



AIB's history has been distinguished by consistent improvement in performance metrics, successive awards recognising its achievements, and establishing a well-earned reputation for sound governance and business integrity.

CFI.co 'Best Corporate Governance' award

AIB wins the CFI.co *'Best Corporate Governance, Afghanistan'* award for the fifth consecutive year

Best Large Tax-Payer Award

Afghanistan's Ministry of Finance recognises large tax-payers with awards for their contribution to raising the level of tax compliance and developing economic activities

The Banker magazine

AIB wins Banker magazine's *'Bank of the Year, Afghanistan'* award for the sixth consecutive year

Bibi Khadija Award

Honorary award presented by the Afghanistan Women Chamber of Commerce and Industry in recognition of AIB's work in supporting women's development

2004

AIB signs a Management Services and Technical Assistance Agreement with ING Institutional and Government Advisory Services BV, the independent advisory unit of Netherlands-headquartered ING Wholesale Banking. This agreement expired in September 2007, ING having fulfilled its mandate.

Asian Development Bank's Board of Directors approves a US$2.6 million equity investment in AIB.

ADB enters into an agreement with three other investors to form the shareholders group, each owning 25 percent equity.

2005

Opening of first branch outside Kabul.

2006

Khalilullah Sediq joins as Chief Executive Officer.

2007

AIB shows annual profit for the first time.

2008

Appointed bankers to the American forces in Afghanistan.

2010

AIB pays first dividend to shareholders, with total distribution of $10 million.

2011

Deposits exceed $500 million.

Site of 4,550 m² purchased for development of new head office, a 12-storey property with total built area of roughly 15,500 m².

2012

Deposits exceed $800 million.

AIB acquires Standard Chartered Bank's business in Afghanistan.

The Banker magazine designates AIB as 'Bank of the Year' in Afghanistan.

2013

The Banker magazine again designates AIB as 'Bank of the Year' in Afghanistan.

2014

After being nominated by the World Bank, AIB wins 'Best Corporate Governance, Afghanistan' in the 2014 CFI.co awards.

The Banker magazine designates AIB as 'Bank of the Year' in Afghanistan for the third consecutive year.

The Bank begins building its 15,500 m² 12-storey head office.

2015

Khalilullah Sediq retires as CEO to become Governor of Da Afghanistan Bank (Afghanistan's central bank).

AIB wins the CFI.co 'Best Corporate Governance, Afghanistan' award and *The Banker* magazine designates AIB as 'Bank of the Year' in Afghanistan for the fourth year running.

Construction of the Bank's new Head Office reaches the ninth floor.

The Bank exhibits for the first time at SIBOS, the annual conference, exhibition and networking event organised by SWIFT for the financial industry.

2016

AIB wins the CFI.co 'Best Corporate Governance, Afghanistan' award for the second consecutive year and *The Banker* magazine designates AIB as 'Bank of the Year' in Afghanistan for the fifth year running.

Construction of the Bank's new Head Office is completed and fit-out begins.

The Bank exhibits at SIBOS for the second time.

2017

AIB wins the CFI.co 'Best Corporate Governance, Afghanistan' award for the fourth consecutive year and *The Banker* magazine designates AIB as 'Bank of the Year' in Afghanistan for the sixth year running.

Construction of the Bank's new Head Office nears completion with occupancy expected in the first quarter of 2018.

The Bank exhibits at SIBOS for the third time.

AIB Branch Network

Herat branches: 2

Herat Main Branch
Herat Darb-e-Khosk Branch

Herat ATMs: 7

Balkh branches: 4

Mazar-e-Sharif Main Branch
Mazar-e-Sharif Kefayat Branch
Mazar-e-Sharif Sinafar Branch
Hairatan Branch

Mazar-e-Sharif ATMs: 4

Kunduz branches: 1

Kunduz Branch

Baghlan branches: 1

Pol-e-Khumri Branch

Parwan branches: 1

Bagram Branch

Parwan ATMs: 1

Nangarhar branches: 1

Jalalabad Branch

Nangarhar ATMs: 2

Khost branches: 1

Khost City Branch

Kabul branches: 21

Shahr-e-Naw (Head Office)
Shahr-e-Naw Ansari Square Branch
Microrayan Branch
Sarai Shahzada Branch
Mirwais Maidan Branch
Khair Khana Branch
Kolola Pushta Branch
Taimani Branch
Kart-e-Naw Branch
Khair Khana Second Branch
Park ha-e-Sanati Branch
Jad-e-Maiwand Branch
Green Village
Pule Bagh-e-Omomi Branch
Dasht-e-Barchi Branch
Kart-e-Se Branch
Wazir Akbar Khan Branch
UNOCA Branch
Baraki Branch
AUAF Branch
US Embassy Branch

Kabul Cash Outlets: 2

ISAF HQ
KAIA

Kabul ATMs: 58

Kandahar branches: 2

Kandahar Main Branch
Kandahar Ayno Mina

Kandahar ATMs: 5

Helmand branches: 1

Lashkargah Branch

Helmand ATMs: 1

Nimroz branches: 1

Nimroz City Branch

Financial Statements

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INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF AFGHANISTAN INTERNATIONAL BANK

Opinion

We have audited the accompanying financial statements of Afghanistan International Bank (the Bank), which comprise the statement of financial position as at 31 December 2017, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies.

In our opinion, the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with the accounting framework as stated in note 2 to the financial statements.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank in accordance with the ethical requirements that are relevant to our audit of the financial statements in Afghanistan, 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.

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

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the accounting framework as stated in note 2 to the financial statements and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

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 financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by 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 Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We are responsible for the direction, supervision and performance of the 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.

Ernst & Young Ford Rhodes Sidat Hyder

Ernst & Young Ford Rhodes Sidat Hyder
Chartered Accountants

Date: 10 March 2018
Kabul, Afghanistan
Engagement Partner: Shabbir Yunus

Statement of Financial Position

As at 31 December 2017

	Note	31 December 2017 AFN '000'	31 December 2016 AFN '000'
ASSETS			
Cash and balances with Da Afghanistan Bank	5	**13,765,061**	10,452,572
Balances with other banks	6	**10,174,148**	6,606,085
Placements – net	7	**13,439,256**	19,313,157
Investments – net	8	**15,966,565**	14,382,579
Loan and advances to customers – net	9	**3,369,970**	3,729,388
Receivables from financial institutions	10	**587,534**	522,484
Operating fixed assets	11	**2,546,205**	1,625,342
Intangible assets	12	**445,918**	527,457
Deferred tax assets	13	**73,603**	21,440
Other assets	14	**568,956**	1,007,100
Total assets		**60,937,216**	58,187,604
LIABILITIES			
Customers' deposits	15	**56,261,420**	54,077,642
Deposits from bank	16	**500,000**	–
Deferred income		**18,989**	15,824
Other liabilities	17	**311,873**	193,068
Total liabilities		**57,092,282**	54,286,534
EQUITY			
Share capital	18	**1,465,071**	1,465,071
Capital reserves	19	**236,497**	218,600
Retained earnings		**2,139,818**	2,211,835
Surplus on revaluation of available for sale investments – net		**3,548**	5,564
Total equity		**3,844,934**	3,901,070
Total equity and liabilities		**60,937,216**	58,187,604

Contingencies and commitments	20		

Chief Executive Officer

Chief Financial Officer

Chairman

The annexed notes 1 to 35 form an integral part of these financial statements.

Statement of Comprehensive Income

For the year ended 31 December 2017

	Note	31 December 2017 AFN '000'	31 December 2016 AFN '000'
Interest income	21	1,141,357	1,071,271
Interest expense	22	(60,009)	(13,346)
Net interest income		1,081,348	1,057,925
Fee and commission income	23	940,467	788,349
Fee and commission expense	24	(16,601)	(31,492)
Net fee and commission income		923,866	756,857
Income from dealing in foreign currencies		172,609	144,023
		2,177,823	1,958,805
Other income	25	55,964	55,717
Gain (loss)/on sale of securities		36,472	(477)
Reversal/(provision) on placements		52,444	(65,222)
Provision on investments		(64,366)	(1,788)
Provision against loan losses	9.4	48,091	(79,818)
General provision on:			
Guarantees	17.2	(65,310)	–
Other assets	14.2	(5,747)	–
Commercial letter of credit	17.2	(2,928)	–
General and administrative expenses	26	(1,586,985)	(1,299,302)
PROFIT BEFORE INCOME TAX		645,458	567,915
Taxation	27	(287,513)	(48,843)
PROFIT FOR THE YEAR		357,945	519,072
OTHER COMPREHENSIVE INCOME			
Items that may be classified to profit and loss subsequently			
Net changes in fair value of available for sale financial instruments		(15,382)	36,554
Related tax		13,366	(7,215)
Other comprehensive income/(loss), net of tax		(2,016)	29,339
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		355,929	548,411
Earnings per share	30	11.93	17.30

Chief Executive Officer

Chief Financial Officer

Chairman

The annexed notes 1 to 35 form an integral part of these financial statements.

Statement of Cash Flows

For the year ended 31 December 2017

	Note	31 December 2017 AFN '000'	31 December 2016 AFN '000'
CASH FLOWS FROM OPERATING ACTIVITIES			
Profit for the year		357,945	519,072
Adjustments for:			
Provision against loans and advances	9.4	(48,091)	79,818
Depreciation	11.2	57,319	50,651
Amortization	12.1	99,236	99,056
Reversal/(provision) on placements	7.3	(52,444)	65,222
Provision on investments		64,366	1,788
General provision on:			
Guarantees	17.2	65,310	–
Other assets	14.2	5,747	–
Commercial letters of credit	17.2	2,928	–
Net interest income		(1,081,348)	(1,057,925)
Income tax expense	27	287,513	48,843
		(241,519)	(193,475)
Changes in operating assets and liabilities			
Receivable from financial institutions		(65,050)	(350,004)
Required reserve maintained with DAB		(1,378,903)	244,839
Cash margin held with other banks		(48,143)	8,962
Loans and advances to customers – net		407,509	(351,353)
Other assets		287,837	(309,771)
Deferred income		(3,165)	(11,286)
Customers' deposits		2,183,778	(3,919,884)
Deposits from banks		500,000	–
Other liabilities		50,567	(14,497)
		1,693,011	(4,896,468)
Interest received		1,167,371	998,190
Interest paid		(60,009)	(13,346)
Income tax paid		(435,318)	(221,219)
Net cash (used in)/from operating activities		2,365,055	(4,132,843)
CASH FLOWS FROM INVESTING ACTIVITIES			
Capital work-in-progress		(941,868)	(586,110)
Acquisition of operating fixed assets		(36,314)	(42,568)
Acquisition of intangible assets		(17,697)	(53,565)
Placements (with maturity more than three months)		7,801,384	(3,746,107)
Investments		(1,649,623)	(815,904)
Net cash used in investing activities		5,155,882	(5,244,254)
CASH FLOWS FROM FINANCING ACTIVITIES			
Dividend paid	18	(412,605)	(335,100)
Net cash used in financing activities		(412,605)	(335,100)
Net increase/(decrease) in cash and cash equivalents		7,108,872	(9,712,197)
Cash and cash equivalents at 01 January		18,458,976	28,171,173
Cash and cash equivalents at 31 December	29	25,567,848	18,458,976

Chief Executive Officer

Chief Financial Officer

Chairman

The annexed notes 1 to 35 form an integral part of these financial statements.

Statement of Changes in Equity

For the year ended 31 December 2017

	Share capital AFN '000	Surplus on available for sale on investments AFN '000	Capital reserve AFN '000	Retained earnings AFN '000	Total AFN '000
Balance as at 31 December 2015	1,465,071	(23,296)	192,646	2,053,817	3,688,238
Balance as at 31 December 2015	1,465,071	(23,296)	192,646	2,053,817	3,688,238
Balance as at 01 January 2016	1,465,071	(23,296)	192,646	2,053,817	3,688,238
Profit for the year	–	–	–	519,072	519,072
Other comprehensive income, net of tax:					
Fair value reserve (available-for-sale financial assets):					
Net change in fair value	–	36,553	–	–	36,553
Related tax on available for sale financial assets	–	(7,311)	–	–	(7,311)
Reclassification adjustments relating to available for sale investments disposed off during the year – net	–	(477)	–	–	(477)
Related tax on loss on disposal of available for sale					
investments during the year	–	95	–	–	95
Total comprehensive income					
Transferred to capital reserve	–	–	25,954	(25,954)	–
Transactions with owners of the bank					
Dividend paid	–	–	–	(335,100)	(335,100)
Balance as at 31 December 2016	1,465,071	5,564	218,600	2,211,835	3,901,070
Total comprehensive income					
Profit for the year	–	–	–	357,945	357,945
Other comprehensive income, net of tax:					
Fair value reserve (available-for-sale financial assets):					
Net change in fair value	–	(15,382)	–	–	(15,382)
Related Tax on available for sale financial assets	–	3,076	–	–	3,076
Reclassification adjustments relating to available for sale investments disposed off during the year – net	–	12,862	–	–	12,862
Related tax on loss on disposal of available for sale					
Investments during the year	–	(2,572)	–	–	(2,572)
Total comprehensive income					
Transferred to capital reserve	–	–	17,897	(17,897)	–
Transactions with owners of the bank					
Dividend paid	–	–	–	(412,065)	(412,065)
	–	(2,016)	17,816	(72,017)	(56,136)
Balance as at 31 December 2017	1,465,071	3,548	236,497	2,139,818	3,844,934

Chief Executive Officer

Chief Financial Officer

Chairman

The annexed notes 1 to 35 form an integral part of these financial statements.

1. STATUS AND NATURE OF BUSINESS

Afghanistan International Bank (the Bank) was registered with Afghan Investment Support Agency (AISA) on 27 December 2003 and received formal commercial banking license on 22 March 2004 from Da Afghanistan Bank (DAB), the central bank of Afghanistan, to operate nationwide. The Bank obtained Islamic banking license from DAB via letter no. 1863/1890 dated 21 July 2014.

The Bank initially was incorporated as a limited liability company and domiciled in Afghanistan, however on the basis that the Bank's capital is divided into shares, the status of the Bank changed from limited liability to Corporation under the Corporations and Limited Liability Companies Law, effective from 4 May 2016. The principal business place of the Bank is at AIB head office, Shahr-e-now, Haji Yaqoob Square, Shahabuddin Watt, Kabul, Afghanistan.

The Bank has been operating as one of the leading commercial banking service providers in Afghanistan. The Bank has 37 branches and 2 cash outlets (2016: 35 branches and 4 cash outlets) in operation.

2. BASIS OF PREPARATION AND MEASUREMENT

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standard Board and the Law of Banking in Afghanistan. Whenever the requirement of the Law of Banking in Afghanistan differs with the requirements of the IFRS, the requirement of the Law of Banking in Afghanistan takes precedence.

These financial statements have been prepared under the historical cost convention except that certain investments are stated at fair value.

These financial statements comprise statement of financial position, statement of comprehensive income as a single statement, statement of changes in equity, statement of cash flows and the accompanying notes.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 4.18.

3. NEW STANDARDS, AMENDMENTS TO APPROVED ACCOUNTING STANDARDS AND NEW INTERPRETATIONS

The accounting policies adopted in preparing the financial statements are consistent with those followed in the preparation of the Bank's annual financial statements for the year ended 31 December 2016, except for the adoption of new standards and interpretations described below, starting from 01 January 2017.

The Bank has adopted the following accounting standards, amendments and interpretations of IFRSs which became effective during the current year:

Standard or Interpretation

IAS 7 Financial Instruments: Disclosures – Disclosure Initiative – (Amendment)

IAS 12 Income Taxes – Recognition of Deferred Tax Assets for Unrealized losses (Amendments)

Annual Improvements to IFRSs 2014-2016 Cycle

IFRS 12 Disclosure of Interests in Other Entities – Clarification of the scope of the disclosure requirements in IFRS 12

The adoption of the above amendments, improvements to accounting standards and interpretations did not have any effect on the financial statements.

Standards, amendments and improvements to approved accounting standards that are not yet effective

The following revised standards, amendments and improvements would be effective from the dates mentioned below against the respective standard or interpretation:

Standard or Interpretation	Effective date (annual periods beginning on or after)
IFRS 2: Share-based Payments – Classification and Measurement of Share-based Payments Transactions (Amendments)	01 January 2018
IFRS 10 Consolidated Financial Statements and IAS 28 Investment in Associates and Joint Ventures – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendment)	01 January 2019
IFRS 4 Insurance Contracts: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts – (Amendments)	01 January 2018
IAS 40 Investment Property: Transfers of Investment Property (Amendments)	01 January 2018
IFRS 9 – Financial Instruments: Classification and Measurement	01 January 2018
IFRS 9 – Prepayment Features with Negative Compensation (Amendments)	01 January 2018
IFRS 15 – Revenue from Contracts with Customers	01 January 2018
IFRS 16 – Leases	01 January 2019
IFRS 17 – Insurance Contracts	01 January 2021
IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration FRS 16 – Leases 01 January 2019	01 January 2018
IFRIC 23 Uncertainty over Income Tax Treatments	01 January 2019

The Bank expects that the adoption of the above amendments and interpretation of the standards will not materially affect the Bank's financial statements in the period of initial application except for IFRS 9- "Financial Instruments".

IFRS 9 includes three parts on accounting of financial instruments: recognition and measurement, impairment and hedge accounting. IFRS 9 is mandatorily effective for annual periods beginning on or after 01 January 2018, with early adoption permitted. Except for hedge accounting, the standard is applied retrospectively, but provision of comparative information is not mandatory. Requirements in respect of hedge accounting are mainly applied prospectively, with several limited exclusions.

The Bank plans to apply the new standard from the required effective date and will not recalculate comparative information. Currently, the Bank is in the process of performing a detailed assessment of the impact of IFRS 9 and therefore it has not been presented in these financial statements.

In addition to the above standards and amendments, improvements to various accounting standards have also been issued by the IASB in December 2016. Such improvements are generally effective for accounting periods beginning on or after 01 January 2018 and 01 January 2019. The Bank expects that such improvements to the standards will not have any impact on the Bank's financial statements in the period of initial application.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all the periods presented in these financial statements.

4.1 Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise balances with less than three months maturity including cash in hand and at ATM, unrestricted balances with the DAB, balances with banks and placements.

4.2 Financial instruments

Financial assets and liabilities are recognized when the Bank becomes a party to the contractual provisions of the instrument, and derecognized when the Bank loses control of the contractual rights that comprise the financial assets, and in case of financial liabilities when the obligation specified in the contract is discharged, cancelled or expired. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

These are subsequently measured at fair value, amortized cost or cost, as the case may be. Any gain or loss on de-recognition of financial assets and financial liabilities is included in income for the year.

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

When a sales or transfer of held to maturity securities represents a material contradiction with the Bank's stated intent to hold those securities to maturity or when a pattern of such sales has occurred, any remaining held to maturity securities are reclassified to available for sale. The reclassification is recorded in the reporting period in which the sale or transfer occurs and accounted for as a transfer.

4.3 Financial assets

The Bank classifies its financial assets in four categories: at fair value through profit or loss, loans and receivables, held to maturity and available for sale investments. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

a) Financial assets at fair value through profit or loss

Financial assets are classified at fair value through profit or loss when the financial asset is either held-for-trading or it is designated as at fair value through profit or loss.

A financial asset is classified as held-for-trading if it is acquired principally for the purpose of selling in the short term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives (if any) are also categorized as held for trading unless they are designated as hedges.

Financial assets are designated at fair value through profit or loss at inception when:

- Doing so significantly reduces measurement inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortized cost for such as loans and advances to customers or banks and debt securities in issue;
- Certain investments, such as equity investments, that are managed and evaluated on a fair value basis in accordance with a documented risk management or investment strategy and reported to key management personnel on that basis are designated at fair value through profit or loss;
- Financial instruments, such as debt securities held, containing one or more embedded derivatives significantly modify that cash flows, are designated at fair value through profit or loss; and
- Financial assets at fair value through profit or loss are stated at fair value, with any gains or losses arising on re-measurement recognized in profit or loss.

b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (a) those that the entity intends to sell immediately or in short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the entity upon recognition designates as available for sale; or (c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

Loans and receivables are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortized cost using the effective interest method.

Cash and balances with DAB, balances with other banks, placements, and receivable from financial institutions, loans and advances to customers and security deposits and other receivables are classified under this category.

c) Held-to-maturity (HTM) financial assets

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. If the Bank were to sell other than an insignificant amount of held-to-maturity financial assets before its maturity, the entire category would be reclassified as available for sale.

Held-to-maturity investments are carried at amortized cost using the effective interest method, less any impairment losses (see 4.4(a)).

Capital notes with DAB and certain investment bonds are classified under this category.

d) Available-for-sale (AFS) financial assets

Available-for-sale financial assets are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Available-for-sale financial assets (AFS) are non-derivatives that are either designated as AFS or are not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss.

Regular-way purchases and sales of financial assets at fair value through profit or loss, held-to-maturity and available for sale are recognized on trade-date i.e. the date on which the Bank commits to purchase or sell the asset.

Financial assets are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the statement of comprehensive income. Financial assets are de-recognised when the rights to receive cash flow from the financial asset have expired or where the Bank has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets carried at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortized cost using the effective interest rate method.

Gains or losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are presented in the statement of comprehensive income as a part of other income in the period in which they arise. Gains and losses arising from changes in fair value of available-for-sale financial assets are recognized directly in other comprehensive income, until the financial asset is derecognized or impaired.

The fair value of AFS monetary financial assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate prevailing at the end of the reporting period. The foreign exchange gains and losses that are recognized in profit or loss are determined based on the amortized cost of the monetary asset. Other foreign exchange gains and losses are recognized in other comprehensive income.

4.4 Impairment of financial assets

a) Assets carried at amortized cost except for loans and advances to customers

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

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

4.4 Impairment of financial assets continued

a) Assets carried at amortized cost except for loans and advances to customers continued

The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower (for example, equity ratio, net income percentage of sales);
- Breach of loan covenants or conditions
- Initiation of bankruptcy proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral; and
- Downgrading below investment grade level.

The amount of loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in the income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as and improvement in the debtor's credit rating), the previously recognized impairment loss is reversed by adjusting the allowance account. The amount of reversal is recognized in the statement of comprehensive income in impairment charge for credit losses.

b) Loans and advances to customers

These are stated net of general provision on loans and advances considered 'Standard' and specific provision for non-performing loans and advances, if any. The outstanding principal of the advances is classified in accordance with the Asset Classification and Provisioning Regulation issued by DAB.

i) Standard: These are loans and advances, which are paying in a current manner or at most past due for the period of 1-30 days, fully secured and are supported by sound net worth, profitability, liquidity and cash flow of the obligor. Standard assets are sufficiently secured with respect to the repayment of both the principal amount and interest. An overdraft would be regarded as Standard if monthly interest payments and other charges are past due for 1-30 days, and there was regular activity on the account with no sign of a hard core of debt developing. A standard provision is maintained in the books of account @1% (31 December 2016: 3%) of value of such loans and advances.

ii) **Watch:** These are loans and advances which are adequately protected, but are potentially weak. Such an asset constitutes an unwarranted credit risk, but not to the point of requiring a classification of Substandard. The credit risk may be minor, and in most instances, bank management can correct the noted deficiencies with increased attention. Further, all loans and advances which are past due by 31 to 60 days for principal or interest payments are classified as Watch. A provision is maintained in the books of account @ not less than 5% of value of such loans and advances.

iii) **Substandard:** These are loans and advances which show clear manifestations of credit weaknesses that jeopardize the liquidation of the debt. Substandard loans and advances include loans to borrowers whose cash flows are not sufficient to meet currently maturing debts, loans to borrowers which are significantly undercapitalized, and loans to borrowers lacking sufficient working capital to meet their operating needs.

Further, all loans and advances which are past due by 61 to 120 days for principal or interest payments are also classified as Substandard. A provision is maintained in the books of account not less than 25% of value of such loans and advances.

iv) **Doubtful:** These are loans and advances which display all the weaknesses inherent in loans and advances classified as Substandard but with the added characteristics that they are not well secured and the weaknesses make collection or liquidation in full, on the basis of currently available information, highly questionable and improbable. The possibility of loss is extremely high, but because of certain mitigating circumstances, which may work to the advantage and strengthening of the facility, its classification as an estimated loss is postponed until its more defined status is ascertained. Further all loans and advances which are past due by 121 to 480 days for principal or interest payments are also classified as Doubtful. A provision is maintained in the books of account not less than 50% of value of such loans and advances.

v) **Loss:** These are loans and advances which are considered uncollectible and of such little value that their continuation as recoverable facilities is not defensible. This classification does not imply that the facility has absolutely no recoverable value, but rather it is not practical or desirable to defer making full provisions for the facility even though partial recover in future may not be entirely ruled out. Loans and advances classified as Loss include those to bankrupt companies and insolvent firms with negative working capital and cash flow or those to judgment debtors with no means or foreclosable collateral to settle the debts. Further, all loans and advances which are past due over 481 days for principal and interest payments are classified as Loss. This category of loans shall be retained in Bank's balance sheet for the period of 6 month for recovery purposes and 100% loan loss provisioning should be made. After 6 months, they shall be immediately written off with the provisioning made.

c) Assets classified as available for sale

The Bank assesses at each statement of financial position date whether there is objective evidence that a financial asset or a group of financial assets is impaired. In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on those financial assets previously recognized in the statement of comprehensive income is removed from equity and recognized in the statement of comprehensive income. Impairment losses recognized in the statement of comprehensive income on equity instruments are not reversed through the statement of comprehensive income. 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 was recognized in the statement of comprehensive income, the impairment loss is reversed through the statement of comprehensive income, related to an event occurring after the impairment loss was recognized.

4.5 Financial liabilities

The Bank classifies its financial liabilities in the following categories.

a) Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss are financial liabilities held for trading. A financial liability is classified in this category if incurred principally for the purpose of trading or payment in the short term. Derivatives (if any) are also categorized as held for trading unless they are designated as hedges.

b) Other financial liabilities measured at amortized cost

These are non-derivatives financial liabilities with fixed or determinable payments that are not quoted in an active market. These are recognized initially at fair value, net of transaction costs incurred and are subsequently stated at amortized cost; any differences between the proceeds (net of transaction costs) and the redemption value is recognized in the income statement.

4.6 Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximizes the use of relevant observable inputs and minimize the use of unobservable all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognized in profit and loss in an appropriate basis over the life of the instrument but no later than when valuation is wholly supported by observable market data or transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at a bid price and liabilities and short position at an ask price.

Portfolio of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Bank on the basis of the net exposure to either market risk or credit risk or measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for a particular risk exposure. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The Bank recognizes transfer between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

4.7 Operating fixed assets

These are stated at historical cost less accumulated depreciation and impairment, if any, except for land and capital work in progress which is stated at cost less impairment, if any. Historical cost includes expenditure that is directly attributable to the acquisition of the asset.

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

Depreciation is calculated using the straight-line method to allocate the depreciable amount of the assets over their estimated useful life as follows:

	Useful life
Leasehold improvements	3 to 10 years
Computers	3 to 5 years
Office equipment	3 to 5 years
Furniture and fittings	3 to 10 years
ATMs	5 years
Vehicles	5 years

Depreciation is charged on additions during the year from the month they become available for their intended use while no depreciation is charged in the month of disposal of assets. The residual values, useful lives and depreciation method are reviewed and adjusted, if appropriate, at each statement of financial position date.

Gains and losses on disposal of property and equipment are determined by comparing proceeds with the carrying amount. These are included in other income in the statement of comprehensive income.

4.8 Intangible assets

Intangible assets are capitalized only to the extent that the future economic benefits can be derived by the Bank having useful life of more than one year. Intangible assets are stated at cost less accumulated amortization. Amortization is charged to income applying the straight line method.

i) Computer software

Acquired computer software is capitalized on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortized over their estimated useful life of 3 to 10 years.

ii) License fee

Acquired trademarks and licenses are initially recognized at historical cost and subsequently recognized at cost less accumulated amortization. Amortization is calculated using the straight-line method to allocate the cost of the licenses over their estimated useful life.

iii) Core deposits

Core deposits are recognized as a result of acquisition of Standard Chartered Branch Afghanistan. Amortization is calculated using the straight-line method over the estimated useful life of core deposits.

The useful lives of intangibles are reviewed and adjusted, if appropriate, at each statement of financial position date.

4.9 Impairment of non-financial assets

Non-financial assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Non-financial assets that are subject to depreciation/amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss or reversal of impairment loss is recognized in the statement of comprehensive income. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date. Reversal of the impairment losses is restricted to the original cost of the assets.

4.10 Taxation

Current

The current income tax charge is calculated in accordance with Income Tax Law, 2009. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation and establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred

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

4.11 Revenue recognition

a) Interest income and expenses for all interest-bearing financial instruments, except for those classified as held for trading or designated at fair value through profit or loss, are recognized within `interest income' and `interest expense' in the statement of comprehensive income using the effective interest rate method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONTINUED

4.11 Revenue recognition continued

b) Due but unpaid interest income is accrued on overdue advances for periods up to 90 days in compliance with the Banking regulations issued by DAB. After 90 days, overdue advances are classified as non-performing and further accrual of unpaid interest income ceases.

c) Gains and losses on disposal of property and equipment are recognized in the period in which disposal is made.

d) Fees and commission income and expense are recognized on an accrual basis when the service has been provided/received. Deferred income is amortized over the period of underlying guarantees.

e) Fee and commission income that are integral part of the effective interest rate on financial assets and liability are included in the measurement of effective interest rate. Other fee and commission expenses related mainly to the transactions are services fee, which are expensed as the services are received

4.12 Foreign currency transactions and translation

a) Functional and presentation currency

Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the entity operates (the functional currency), which is Afghani (AFN). All amounts have been rounded to the nearest thousands, except when otherwise indicated.

b) Transactions and balances

Foreign currency transactions are translated into functional currency using the exchange rate prevailing at the date of the transaction. Foreign currency assets and liabilities are translated using the exchange rate at the balance sheet date. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of assets and liabilities denominated in foreign currencies are recognized in income currently.

The exchange rate for following currencies against AFN were:

	1 USD	1 Euro	1 AED
As at 31 December 2016	69.72	83.27	18.89
As at 31 December 2015	66.82	70.01	18.19

4.13 Provisions

Provisions are recognized when there are present, legal or constructive obligations as a result of past events; it is probable that an out flow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate of the amounts can be made. Provision for guarantee claims and other off balance sheet obligations is recognized when intimated and reasonable certainty exists to settle the obligations.

4.14 Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount is reported in the financial statements when there is a legally enforceable right to offset the recognized amounts and the Bank intends to settle either on a net basis or realize the assets and settle the liabilities simultaneously.

4.15 Dividend Distribution

Final dividend distributions to the Bank's shareholders are recognized as a liability in the financial statements in the period in which the dividends are approved by the Bank's shareholders at the Annual General Meeting while interim dividends are recognized in the period in which the dividends are declared by the Board of Supervisors.

4.16 Earnings per share

The Bank presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss that is attributable to shareholders of the Bank by the weighted-average number of shares outstanding during the year.

4.17 Employee benefits

Defined contribution plan

Obligations for contributions to defined contribution plans are expensed as the related service is provided and recognised as personnel expenses (salaries and benefits) in profit or loss. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

4.18 USE OF CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The resulting accounting estimates and judgments will, by definition, rarely equal the related actual results.

During the year, DAB has revised Asset Classification and Provisioning Regulation which were effective from 01 October 2017. These regulations required banks to maintain certain general provisions in the financial statements. Accordingly, general provision created against other assets and off-balance sheet obligations amounted to AFN 74,080 thousands at the year end. However, the above general provisions have been reversed subsequent to year end, due to further revision in the above regulations which was approved by the Supreme Council of DAB on 06 January 2018, and effective from 01 January 2018.

The material estimates, assumptions and judgments used to measure and classify the carrying amounts of assets and liabilities are outlined below:

a) Provision for loan losses

The Bank reviews loans to customer balances quarterly for possible impairment and records the provision for possible loan losses as per the Bank's policy and in accordance with DAB regulations. The Bank maintains a general provision of 1% (31 December 2016: 3%) against outstanding loan and advances to customers as at the year end.

b) Provision of income taxes

The Bank recognizes tax liability in accordance with the provisions of Income Tax Law 2009. The final tax liability is dependent on assessment by Ministry of Finance, Government of Islamic Republic of Afghanistan.

c) General provision on investments and placements

The management also maintains a provision of 1% on collective balance of investments (excluding those with DAB and investments in money market fund) and placements (excluding placements having with original maturity of 1 month) to cover the counter party risk.

d) General provision on off-balance sheet items

As per Asset Classification and Provisioning Regulation, the management maintains a provision of 1% on secured portion and 5% on unsecured portion of off-balance sheet items.

e) Useful life of property and equipment and intangible assets

The Bank reviews the useful life, depreciation method and residual value of property and equipment and intangible assets at each statement of financial position date. Any change in estimates may affect the carrying amounts of the respective items of property and equipment and intangible assets with a corresponding effect on the depreciation/amortization charge.

f) Held-to-maturity investments

The Bank follows the IAS 39 guidance on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held to maturity. This classification requires significant judgment. In making this judgment, the Bank evaluates its intention and ability to hold such investments to maturity.

5. CASH AND BALANCES WITH DA AFGHANISTAN BANK (DAB)

	Note	2017 AFN '000	2016 AFN '000
Cash in hand		1,759,928	1,357,027
Cash in hand – Islamic banking division		118,804	76,114
Cash at Automated Teller Machines (ATMs)		605,922	545,278
		2,484,654	1,978,419
Balances with Da Afghanistan Bank:			
Local currency:			
- Deposit facility accounts	5.1	2,490,242	1,050,902
- Required reserve accounts	5.2	649,217	4,185,981
- Current accounts		687,403	300,329
		3,826,862	5,537,212
Foreign currency:			
- Required reserve accounts	5.2	4,915,567	–
- Current accounts		2,537,978	2,936,941
		11,280,407	8,474,153
		13,765,061	10,452,572

5.1 This represents interest bearing account carrying interest @ 0.10% (31 December 2016: 0.80%) per annum.

5.2 Required reserve account is being maintained with DAB which is denominated in respective currencies to meet minimum reserve requirement in accordance with Article 3 "Required Reserves Regulation" of the Banking Regulations issued by DAB. Theses balances are interest free.

6. BALANCES WITH OTHER BANKS

	Note	2017 AFN '000	2016 AFN '000
Outside Afghanistan:			
With Standard Chartered Bank			
- in nostro accounts		3,025,559	2,375,329
- others		3,563,784	2,146,777
	6.1	6,589,343	4,522,106
With Commerzbank, Germany:			
- in nostro accounts	6.2	66,916	143,282
- in cash margin held	6.3	45,260	93,403
		112,176	236,685
With other banks	6.4	3,472,629	1,847,294
		10,174,148	6,606,085

6.1 These represent balances with Standard Chartered Bank, Singapore which carries interest @ 0.2% to 0.3% p.a. (2016: 0.2% to 0.3% p.a.) and are available on demand.

6.2 This represents interest bearing nostro accounts and carries interest @ LIBOR – 0.25% (31 December 2016: LIBOR – 0.25%).

6.3 It carries interest @ LIBOR – 0.25% (31 December 2016: LIBOR – 0.25%), held with Commerzbank, Germany against letters of credit issued on behalf of the Bank.

6.4 This includes balances maintained with investment managers and other banks. These are non-interest bearing and available on demand.

7. PLACEMENTS – NET

	Note	2017 AFN '000	2016 AFN '000
Placements with banks	7.1	13,551,521	19,477,866
		13,551,521	19,477,866
General provision held	7.2 & 7.3	(112,265)	(164,709)
		13,439,256	19,313,157

7.1 These represent overnight and fixed term placements with financial institutions outside Afghanistan up to a maximum period of one year (2016: one year) in USD carrying interest at rates ranging from 0.75% p.a. 2.10% p.a. (31 December 2016: 0.40% p.a. to 1.75% p.a.).

7.2 General provision of 1% (31 December 2016: 1%) maintained on placements with original maturity of more than 30 days is provided based on DAB requirement to cover the counter party and market risk.

7.3 Movement in provision during the year

	2017 AFN '000	2016 AFN '000
Balance at 01 January 2017	164,709	99,487
Reversal/(provision) made during the year	(52,444)	65,222
Balance at 31 December 2017	112,265	164,709

8. INVESTMENTS – NET

	Note	2017 AFN '000	2016 AFN '000
Available for sale investments:			
- Investment bonds	8.1	4,586,137	4,351,290
- Investment in money market fund		–	679,702
		4,586,137	5,030,993
Held-to-maturity investments:			
- Capital notes with DAB	8.2	3,533,535	1,520,054
- Investment bonds	8.3	7,972,479	7,892,752
		11,506,014	9,412,806
		16,092,151	14,443,799
General provision held	8.4	(125,586)	(61,220)
		15,966,565	14,382,579

8.1 These represent investments in bonds having maturity ranging from January 2018 to April 2025 and carrying coupon interest rates ranging from 1% to 9.38% (31 December 2016: 1% to 11.63%) per annum. These investments are managed by Julius Baer and Emirates NBD on behalf of the Bank.

8.2 These represent investments in capital notes issued by DAB up to a maximum period of one year (31 December 2016: one year) carrying yield at rates ranging from 0.40% to 4.2% p.a. (31 December 2016: 3.53% to 6.68% p.a.) receivable on maturity of respective notes.

8.3 These represent investments in bonds from various financial institutions and sovereign corporates carrying coupon interest rates ranging from 1.30% to 7.75% (2016: 1.50% to 7.75%). These investments have maturity ranging from January 2018 to October 2022. These investments are classified as "Held-to-maturity" because of the Bank's ability and intention to hold these investments up to maturity. These investments are managed by Julius Baer and Emirates NBD on behalf of the Bank.

8.4 General provision of 1% (31 December 2016: 0.5%) on collective investments (excluding capital notes with DAB and Investment in money market fund) is provided to cover the market and counter party risk.

9. LOANS AND ADVANCES TO CUSTOMERS – NET

	Note	2017 AFN '000	2016 AFN '000
Overdrafts	9.1	2,751,975	3,489,206
Term loans	9.2	654,135	343,016
Consumer loans	9.3	49,489	44,226
		3,455,599	3,876,448
Provision against loans and advances	9.4	(85,629)	(147,060)
		3,369,970	3,729,388
Particulars of loans and advances – (gross)			
Short term (for up to one year)		2,760,106	3,101,287
Non-current (for over one year)		695,493	775,161
		3,455,599	3,876,448

9. LOANS AND ADVANCES TO CUSTOMERS – NET CONTINUED

9.1 These represent balances due from customers at various interest rates ranging from 10% to 15% p.a. (31 December 2016: 11% to 15% p.a.) and are secured against mortgage of properties, personal guarantees, lien on equipment, pledge of stocks and/or assignment of receivables of the borrowers. The overdrafts are repayable on demand. These include loans and advances to customers amounting to AFN 427,567 thousands (31 December 2016: AFN 440,702 thousands) which are partially backed by Deutsche Investitions- und Entwicklungsgesellschaft mbh (ACGF) guarantees to the extent defined in agreement with ACGF.

9.2 Term loans carry interest at various rates ranging from 11% to 18% p.a. (31 December 2016: 11% to 18% p.a.) and are secured against mortgage of properties, personal guarantees, lien on equipment, pledge of stocks and/or assignment of receivables of the borrowers. These include loans and advances to customers amounting to AFN 125,738 thousands (31 December 2016: AFN 137,594 thousands) which are partially backed by DEG guarantee to the extent defined in the agreement with DEG.

Term loans include Small Business loans amounting to AFN 32,819 thousands (31 December 2016: AFN 17,320 thousands) carrying interest rate ranging from 13% to 18% p.a. (31 December 2016: 13% to 18% p.a.). These loans are secured against deposit of original title deed, negative lien letter, corporate guarantee by a registered company and hypothecation of movable fixed assets as collateral after registration from DAB.

9.3 These represent consumer loans due from individual payroll account holders, employees of corporate customers having payroll account with the Bank carries interest ranging from 15% to 22% (31 December 2016: 15% to 18%) and credit card carries interest up to @ 36% (31 December 2016: 36%) on annual basis outstanding balances. General provision of 1% (31 December 2016: 3%) has been maintained on these balances.

9.4 Provision against loans and advances

		2017			2016		
	Note	Specific AFN '000	General AFN '000	Total AFN '000	Specific AFN '000	General AFN '000	Total AFN '000
Opening		37,304	109,756	147,060	140,982	41,623	182,605
Charge for the year		34,650	–	34,650	38,939	77,022	115,961
Reversal of provision		(1,331)	(81,741)	(82,741)	(28,198)	(7,945)	(36,143)
		33,319	(81,410)	(48,091)	10,741	69,077	79,818
Write off against provision	9.4.1	(17,656)	–	(17,656)	(111,055)	–	(111,055)
Exchange rate difference		(446)	4,762	4,316	(3,364)	(944)	(4,308)
Closing		52,521	33,108	85,629	37,304	109,756	147,060

9.4.1 These represent 'loss' category loans balances overdue by more than 360 days which have been written off in accordance with the requirements of policy of the Bank.

In terms of paragraph 3.3.1(g) of part C of the DAB Regulations, the write-off does not affect the Bank's rights to recover the debt due from customers and does not eliminate the borrowers' responsibility to repay the loan.

9.5 Classification of loans and advances

		2017			
Classification	Note	*Provisioning rates AFN '000	Amount outstanding AFN '000	Provision required AFN '000	Provision held AFN '000
Standard	4 (a)	1%	3,310,708	33,107	33,107
Watch-list	9.6	5%	16,770	839	254
Substandard		25%	41,724	10,431	10,431
Doubtful	9.6 & 9.7	50%	86,397	43,199	41,837
Loss	9.8	100%	8	8	8
Write-offs			(8)	(8)	(8)
			–	–	–
Loans and advances and provision held 31 December 2017			3,455,599	87,576	85,629

	2016			
Classification	*Provisioning rates AFN '000	Amount outstanding AFN '000	Provision required AFN '000	Provision held AFN '000
Standard	1%	3,677,294	36,773	109,588
Watch-list	5%	117,344	5,317	5,317
Substandard	25%	2,301	564	564
Doubtful	50%	79,509	24,507	31,591
Loss	100%	22	22	22
Write-offs		(22)	(22)	(22)
Loans and advances and provision held 31 December 2016		3,876,448	67,161	147,060

* Provisioning rates are as per DAB regulation except for in case of standard loans and advances which are provided by bank as per bank's policy.

9.6 The Bank has taken provision on outstanding amount of four (31 December 2016: three) parties included in Watch and Doubtful category after deducting amount covered by ACGF guarantees.

9.7 As per the DAB Regulation, Article three (part-B) (3.2.1), loan loss provision has been immediately charged off against the reserve for losses. The amount of these loans are AFN 8 thousands (31 December 2016: AFN 22 thousands).

9.8 Classification of regular, overdue but not impaired and impaired loans and advances to customers in terms of product and overdue time period along with details of loans and advances to customers which are renegotiated during the year, has been disclosed in note 31.2.6.

9.9 The Bank has filed suits for the recovery of loans and advances principal due against the defaulted borrowers amounting to AFN 683,168 thousands (31 December 2016: AFN 756,630 thousands) as at the year end. These suits are pending decisions at various courts. The Bank's management is of the view that the aforementioned suits will be decided in its favor due to sound legal footings.

10. RECEIVABLE FROM FINANCIAL INSTITUTIONS

This represents non-interest bearing receivable balance due from CSC Bank SAL (CSC). The Bank has entered into an agreement with CSC whereby credit card/debit card holders of various financial institutions can use ATM machines of the Bank and the amount withdrawn including bank charges will be paid by CSC to the Bank.

11. OPERATING FIXED ASSETS

	Note	2017 AFN '000	2016 AFN '000
Capital work in progress	11.1	2,264,025	1,362,167
Property and equipment	11.2	282,180	263,175
		2,546,205	1,625,342

11.1 Capital work in progress

	Note	2017 AFN '000	2016 AFN '000
Advances to suppliers and contractors		766,118	281,757
Advances to related party	11.1.2	1,497,907	1,080,410
	11.1.1	2,264,025	1,362,167

11.1.1 Movement in capital work-in-progress

	2017 AFN '000	2016 AFN '000
Opening	1,362,167	799,377
Additions during the year	941,868	586,110
Transferred to property and equipment	(40,010)	(23,320)
Closing	2,264,025	1,362,167

11.1.2 This represents to date payments made against the construction of head office building to Mohib Advance Design Construction Company (MADCC), related party of the Bank.

11.2 Property and equipment

	Land AFN '000	Leasehold improvements AFN '000	Computers AFN '000	Office equipment AFN '000	Furniture & fittings AFN '000	ATMs AFN '000	Vehicles AFN '000	Total AFN '000
Cost								
Balance at 1 January 2016	177,568	69,304	90,823	131,985	16,835	95,290	80,003	661,808
Transfers from CWIP	–	4,448	–	1,881	325	13,258	3,407	23,319
Additions	–	923	13,089	19,118	597	8,635	206	42,568
Balance at 31 December 2016	177,568	74,675	103,912	152,984	17,757	117,183	83,616	727,695
Balance at 1 January 2017	177,568	74,675	103,912	152,984	17,757	117,183	83,616	727,695
Transfers from CWIP	–	6,638	–	8,494	1,380	10,452	13,046	40,010
Additions	–	497	11,839	13,622	67	9,300	989	36,314
Balance at 31 December 2017	177,568	81,810	115,751	175,100	19,204	136,935	97,651	804,019
Depreciation								
Balance at 1 January 2016	–	66,656	68,686	120,018	15,279	71,883	71,346	413,868
Charge for the year	–	3,682	8,141	21,537	788	10,748	5,756	50,652
Balance at 31 December 2016	–	70,338	76,827	141,555	16,067	82,631	77,102	464,520
Balance at 1 January 2017	–	70,338	76,827	141,555	16,067	82,631	77,102	464,520
Charge for the year	–	5,109	10,266	23,455	988	10,908	6,593	57,319
Balance at 31 December 2017	–	75,447	87,093	165,010	17,055	93,539	83,695	521,839
Carrying amounts								
Balance at 1 January 2016	177,568	2,648	22,137	11,967	1,556	23,407	8,657	247,940
Balance at 31 December 2016	177,568	4,337	27,085	11,429	1,690	34,552	6,514	263,175
Balance at 31 December 2017	177,568	6,363	28,658	10,090	2,149	43,396	13,956	282,180
Useful life		3 to 10 years	3 to 5 years	3 to 5 years	3 to 10 years	5 years	5 years	

12. INTANGIBLE ASSETS

	Note	2017 AFN '000	2016 AFN '000
Computer software, licenses and core deposits	12.1	445,918	527,457

12.1 Computer software, licenses and core deposits

	Computer software AFN '000	License fee AFN '000	Core deposits AFN '000	Total AFN '000
Cost				
Balance at 1 January 2016	283,447	43,897	542,677	870,021
Additions	24,942	28,623	–	53,565
Balance at 31 December 2016	308,389	72,520	542,677	923,586
Balance at 1 January 2017	308,389	72,520	542,677	923,586
Additions	17,197	–	–	17,197
Balance at 31 December 2017	326,086	72,520	542,677	941,283
Amortization				
Balance at 1 January 2016	140,310	37,617	119,146	297,073
Charge for the year	52,274	10,604	36,178	99,056
Balance at 31 December 2016	192,584	48,221	155,324	396,129
Balance at 1 January 2017	192,584	48,221	155,324	396,129
Charge for the year	53,018	8,487	37,731	99,236
Balance at 31 December 2017	245,602	56,708	193,055	495,365
Carrying amounts				
Balance at 1 January 2016	143,137	6,280	423,531	572,948
Balance at 31 December 2016	115,805	24,299	387,353	527,457
Balance at 31 December 2017	80,484	15,812	349,622	445,918
Useful life	3 to 10 years	3 to 10 years	15 years	

13. DEFERRED TAX ASSETS

	2017 AFN '000	2016 AFN '000
Deferred tax (assets)/liabilities arising in respect of:		
Provision on investments, placements and other assets	48,720	45,186
Provision on guarantees and commercial letter of credits	13,648	–
Deficit on revaluation of investments	(887)	(1,391)
Accelerated tax depreciation and amortization	12,122	(22,355)
	73,603	21,440

13.1 Movement in temporary differences during the year

	Balance as at 01 January 2016 AFN '000	Recognized in profit or loss AFN '000	Recognized in equity AFN '000	Balance as at 31 December 2016 AFN '000	Recognized in profit or loss AFN '000	Recognized in equity AFN '000	Balance as at 31 December 2017 AFN '000
Deferred tax assets arising in respect of:							
Provision on investments and placements	31,784	13,402	–	45,186	3,534	–	42,802
Provision on guarantees and commercial letter of credits	–	–	–	–	13,648	–	
Revaluation reserve on investments	5,824	–	(7,215)	(1,391)	–	(504)	(887)
	37,608	–	(7,215)	43,795	(2,888)	(7,215)	34,196
Deferred tax liabilities arising in respect of:							
Accelerated tax depreciation and amortization	(16,967)	(5,388)	–	(22,355)	34,477	–	12,122
	(16,967)	(5,388)	–	(22,355)	(5,388)	–	12,122
	20,641	8,014	(7,215)	21,440	51,659	504	73,603

14. OTHER ASSETS

	Note	2017 AFN '000	2016 AFN '000
Advances to employees		60,756	15,734
Security deposits		10,029	8,859
Prepayments		59,144	88,525
Interest receivable		295,513	321,525
Advance income tax – net		63,191	181,739
Other receivable and advances		86,070	56,516
Receivable from DoJ	14.1	250,605	250,605
Less: Balance written off		(250,605)	(250,605)
		–	–
		574,703	1,007,100
General provision held	14.1.1	(5,747)	–
		575,907	1,007,100

14.1 Receivable from DoJ

This represents receivables from the United States Government department, Department of Justice (the "DoJ"). The DoJ seized an amount of AFN 565,701,000 (equivalent to USD 10,100,000) from the Bank's account with Standard Chartered's branch in New York. Pursuant to Title 18, U.S. Code Section 981(k), the United States sought to reach the customer's Afghan-based accounts by seizing funds from the Bank's correspondent account in the United States. The United States has not alleged any wrongdoing against the Bank. In September 2013, the United States returned to the Bank approximately US$ 5.7 million, plus accrued interest, of the seized funds. The United States then moved to strike AIB's claim as to the remaining monies. In September 2015, that motion was denied as to all but USD 147,939, leaving approximately USD 4.1 million at issue. AIB has had some discussions with the U.S. government regarding settlement of the funds, but the U.S. government has advised that it is unable to engage in further discussions given the pendency of customer's competing claim to the same money. The U.S. government has moved to strike customer's claim, and, if the motion is granted, the Bank intends to pursue settlement discussions with the U.S. government. However, on prudent basis, the Bank has made provision of AFN 250,605 thousands in its books of account.

14.1.1 General provision of 1% (31 December 2016); Nil) on other assets in maintained as per Asset Classification and Provisioning Regulations issued by DAB.

15. CUSTOMERS' DEPOSITS

	Note	2017 AFN '000	2016 AFN '000
Current deposits		53,505,342	51,180,050
Saving deposits	15.1	203,752	151,699
Term deposits	15.2	697,200	1,091,490
Islamic deposits	15.3	640,199	364,619
Cash margin held against bank guarantees and letters of credit		1,214,927	1,289,784
		56,261,420	54,077,642

15.1 Saving deposits carry interest @ 3% p.a. (31 December 2016: 3% p.a.).

15.2 Term deposits carry 0.75% to 7.05% interest rates per annum (31 December 2016: 0.25% to 0.75% interest rates per annum).

15.3 Current and saving Islamic deposits stand at AFN 62,070 thousands (31 December 2016: AFN 81,065 thousands) and AFN 578,129 thousands (31 December 2016: AFN 283,554 thousands) respectively.

16. DEPOSITS FROM BANK

Represents term deposit of AFN 500,000 thousands (31 December 2016: Nil) by Bank Millie Afghan that carries interest @ 7.05% per annum and maturing on 05 April 2018.

17. OTHER LIABILITIES

	Note	2017 AFN '000	2016 AFN '000
Accruals and other payables		40,888	53,899
Amounts pending transfers to customers' accounts	17.1	88,461	5,882
Provision for bonus to employees		16,176	15,238
Retention money payable		61,815	67,467
Provision on:			
Guarantees	17.2	65,310	–
Commercial letter of credits	17.2	2,928	–
Others		36,295	29,756
		311,873	193,068

17.1 This represents amounts received on behalf of the customers, however not credited in the respective customers' accounts due to incomplete identification data.

17.2 Represents 1% provision on secured portion and 5% on unsecured portion as required under Assets Classification and Provisioning Regulation issued by DAB

18. SHARE CAPITAL

		2017	2016
Authorized 30,000,000 (2016: 30,000,000) ordinary shares of USD 1 each	USD '000'	30,000	30,000
	AFN '000'	1,465,071	1,465,071
Issued, subscribed and paid-up – 30,000,000 (31 December 2016: 30,000,000) ordinary shares of USD 1 each fully paid in cash	AFN	1,465,071	1,465,071

18.1 Pursuant to letter no.918/703 dated 17 May 2010 issued by Da Afghanistan Bank (DAB), the Bank complies with the minimum paid-up capital requirement for commercial banks in Afghanistan amounting to AFN 1,000,000 thousands (equivalent to US $ 20,000 thousands).

18.2 Issued, subscribed and paid up capital comprises 46.25% holding by Horizon Associates LLC and 46.25% holding by Wilton Holding Limited and 7.5% by International Finance Corporation. (31 December 2016: 50% holding by Horizon Associates LLC and 50% holding by Wilton Holding Limited).

During the year IFC purchased 7.5% shareholding in the bank from the two shareholders (i.e. Horizon Associates LLC and Wilton Holdings Limited) in equal proportions.

18.3 During the year the Bank has paid an Interim dividend of AFN 11.17 per share amounting to AFN 335.10 million.

19. CAPITAL RESERVES

'Article 93 "Reserve Capital" of Corporations and Limited Liability Companies Law of Afghanistan, requires that Bank should transfer 5% of its profit to Capital Reserve to compensate for future possible losses to the extent such capital reserves reaches up to 25% of the Bank's capital. The Bank's capital reserves as at 31 December 2017 stood at AFN 236,497 thousands (31 December 2016: AFN 218,600 thousands).

20. CONTINGENCIES AND COMMITMENTS

20.1 Contingencies

	Note	2017 AFN '000	2016 AFN '000
Guarantees	20.1.1	6,463,038	3,404,690

20.1.1 These represent bid bonds and performance based guarantees issued by the Bank.

20.1.2 The Bank has filed suits for the recovery of loans and advances (principle due) against the defaulted borrowers that are pending for decisions at various courts. The management is confident that these cases will be decided in Bank's favor due to sound legal footings.

20.2 Commitments

	2017 AFN '000	2016 AFN '000
(a) Undrawn loan and overdraft facilities	1,265,872	848,222
(b) Commercial letters of credit	134,575	149,945
	1,400,447	998,167

21. INTEREST INCOME

	2017 AFN '000	2016 AFN '000
Interest income on:		
Balances with DAB and other banks	20,838	13,776
Placements	275,778	221,658
Investments	397,749	392,848
Investments classified as 'available for sale'	119,252	278,497
Investments classified as 'held to maturity'	278,497	114,351
Loans and advances to customers	446,992	442,989
	1,141,357	1,071,271

22. INTEREST EXPENSE

	2017 AFN '000	2016 AFN '000
Interest expense on:		
Customers' deposits	33,354	13,346
Deposits from bank	26,655	
	60,009	13,346

23. FEE AND COMMISSION INCOME

	2017 AFN '000	2016 AFN '000
Fee and commission income on:		
Loans and advances to customers	32,561	34,074
Trade finance products	41,810	9,670
Cash withdrawals/Cash transfers	539,551	448,070
Customers' account service charges	144,152	114,843
Income from ATMs	73,822	57,068
Income from guarantee arrangements	39,168	74,297
Payroll services	44,921	41,403
Others	24,482	8,924
	940,467	788,349

24. FEE AND COMMISSION EXPENSE

	2017 AFN '000	2016 AFN '000
Guarantee/letter of credit commission	9,532	11,046
Bank charges	7,069	20,446
	16,601	31,492

25. OTHER INCOME

	2017 AFN '000	2016 AFN '000
Loans and advances recovered previously written off	55,664	54,490
Others	300	1,227
	55,964	55,717

26. GENERAL AND ADMINISTRATIVE EXPENSES

	Note	2017 AFN '000	2016 AFN '000
Salaries and benefits		544,573	378,388
Rental, rates and taxes		95,200	98,019
Electricity, generator and fuel		48,215	32,961
Repairs and maintenance		76,325	65,551
Security cost		108,167	84,869
Depreciation	11.2	57,319	50,651
Amortization	12.1	99,236	99,056
Directors fee and their meeting expenses		32,935	20,103
Travelling and accommodation		43,765	39,223
Communication, swift and internet		50,207	53,461
Stationary and printing		42,917	30,385
Legal and professional charges		97,142	78,203
Investment management fee to investment advisors		28,261	24,532
Auditors' remuneration	26.1	12,690	4,823
Marketing and promotion		33,477	38,493
Money service providers charges		1,873	858
Insurance		137,276	135,492
Subscriptions and memberships		8,732	8,676
Other charges		56,127	47,609
Taxes and penalties		768	1,062
Corporate social responsibility		3,898	4,779
Others		7,882	3,979
		1,586,985	1,299,302

26.1 Auditor's remuneration

	2017 AFN '000	2016 AFN '000
Audit fee	6,552	5,518
Other professional services	6,138	3,173
	12,690	8,691

27. TAXATION

	2017 AFN '000	2016 AFN '000
Current		
For the year	65,455	56,857
Prior periods	273,716	–
Deferred		
For the year	(51,658)	(8,014)
	287,513	48,843

27.1 Relationship between tax expense and accounting profit

	2017 AFN '000	2016 AFN '000
Accounting profit for the year	645,458	567,915
Applicable tax @ 20%	129,092	113,583
Deductible expenses	(123,570)	11,887
Non-deductible expenses	59,933	–
Effect of deferred tax charge for the year	(51,658)	(8,014)
Adjustment in respect of current income tax of prior years	273,716	(67,019)
Others	–	(1,594)
	287,513	48,843

28. RELATED PARTY TRANSACTIONS

The Bank has a related party relationship with its shareholders, their related entities, directors and key management personnel. The Bank had transactions with following related parties at mutually agreed terms during the year:

	Directors and other key management personnel (and close family members)		Shareholders and its associated companies	
Nature of transactions	2017 AFN '000	2016 AFN '000	2017 AFN '000	2016 AFN '000
a) Loans and advances to related parties				
Loans outstanding at the beginning of the year	–	–	177,559	213,750
Loans issued during the year	–	–	232,266	410,379
Loans repayments during the year	–	–	(255,031)	(454,565)
Exchange gain	–	–	721	7,995
Loans outstanding at the end of the year	–	–	155,515	177,559
Interest income earned	–	–	24,759	36,710

During the year, an amount of AFN 417,459 thousands (31 December 2016: 409,170 thousands) was paid to MADCC (related party) on account of contract awarded on arms length basis for the construction of head office building.

Provision on outstanding balances of loans and advances to related parties amounts to AFN 3,174 thousands (31 December 2016: AFN 5,327 thousands).

The facilities provided to related parties carries mark-up at interest rates 10% p.a. (31 December 2016: 10% p.a.) payable on monthly basis and are secured against mortgage of residential property and personal guarantees of directors and representative of shareholders of the Bank.

	Directors and other key management personnel (and close family members)		Shareholders and its associated companies	
Nature of transactions	2017 AFN '000	2016 AFN '000	2017 AFN '000	2016 AFN '000
b) Deposits from related parties				
Deposits at the beginning of the year	57,402	87,051	107,434	154,206
Deposits received during the year	290,454	411,590	1,499,544	1,509,946
Deposits repaid during the year	(299,629)	(439,765)	(1,509,173)	(1,553,423)
Exchange rate difference	1,040	(1,474)	6,305	(3,295)
Deposits at the end of the year	49,267	57,402	104,110	107,434
Interest expense of deposits	–	–	–	–

These represent current account of related parties, which carry Nil interest rate (31 December 2016: Nil).

		Directors and other key management personnel (and close family members)		Shareholders and its associated companies	
Nature of transactions	Note	2017 AFN '000	2016 AFN '000	2017 AFN '000	2016 AFN '000
c) Other related party transactions					
Fee and commission income		–	–	13,203	5,256
Directors' fee		22,922	14,351	–	–
Fee and commission expense		–	–	–	–
Rental expenses		–	–	136,197	7,892
Other expenses		10,851	8,780	–	–
Capital work-in-progress	28.1	–	–	589,509	409,170
Guarantees issued by the Bank		–	–	333	333
Commercial letters of credit issued including accepted bills and export bills purchased		–	–	84,423	84,423

28.1 This represents the payment made against the construction of new head office building to Mohib Advance Design Construction Company (MADCC), related party of the Bank.

	2017 AFN '000	2016 AFN '000
d) Key Management compensation		
Salaries and other short-term benefits	99,596	63,012
	99,596	63,012

Key Management personnel of the Bank include the Chief Executive Officer, Chief Financial Officer, Chief Operating Officer and Head of Banking.

29. CASH AND CASH EQUIVALENTS

	2017 AFN '000	2016 AFN '000
Cash in hand and at ATM	2,484,654	1,978,419
Balances with DAB (other than minimum reserve requirement)	5,715,623	4,288,172
Balances with other banks	10,128,888	6,512,681
Placements (with maturity less than three months)	7,238,68	5,679,704
	25,567,847	18,458,976

30. EARNINGS PER SHARE – BASIC AND DILUTED

	2017	2016
Profit after taxation (AFN '000)	357,945	519,072
Weighted average number of ordinary shares (number in thousand)	30,000	30,000
Earnings per share – Basic and diluted (AFN per share)	11.93	17.30

30.1 There is no dilutive effect on basic earnings per share of the Bank.

31. FINANCIAL RISK MANAGEMENT

31.1 Financial assets and liabilities

31 December 2017	Loans and receivables AFN '000	Held-to-maturity AFN '000	Available-for-sale AFN '000	Other financial liabilities AFN '000	Total AFN '000
Financial assets					
Cash and balances with					
Da Afghanistan Bank	13,765,061	–	–	–	13,765,061
Balances with other banks	10,174,148	–	–	–	10,174,148
Placements – net	13,439,256	–	–	–	13,439,256
Investments – net	–	11,426,289	4,540,276	–	15,966,565
Loans and advances to customers – net	3,369,970	–	–	–	3,369,970
Receivables from financial institutions	587,534	–	–	–	587,534
Other assets	–	–	–	447,844	447,844
	41,335,969	11,426,289	4,540,276	447,844	57,750,378
Financial liabilities					
Customers' deposits	–	697,200	–	55,564,220	56,261,420
Deposits from banks	–	–	–	500,000	500,000
Other liabilities	–	–	–	191,164	191,164
	–	–	–	56,255,384	56,952,584

31 December 2016	Loans and receivables AFN '000	Held-to-maturity AFN '000	Available-for-sale AFN '000	Other financial liabilities AFN '000	Total AFN '000
Financial assets					
Cash and balances with					
Da Afghanistan Bank	10,452,572	–	–	–	10,452,572
Balances with other banks	6,606,085	–	–	–	6,606,085
Placements – net	19,313,157	–	–	–	19,313,157
Investments – net	–	9,373,343	5,009,236	–	14,382,578
Loans and advances to customers – net	3,729,388	–	–	–	3,729,388
Receivables from financial institutions	522,484	–	–	–	522,484
Other assets	–	–	729,467	729,467	
	40,623,686	9,373,343	5,009,236	729,467	55,735,732
Financial liabilities					
Customers' deposits	–	1,091,490	–	54,077,642	54,077,642
Other liabilities	–	–	–	148,074	148,074
	–	–	–	54,225,716	54,225,716

31. FINANCIAL RISK MANAGEMENT CONTINUED

31.2 Financial risk factors

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business and the operational risks are an inevitable consequence of being in business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimize potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyze these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up to date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out by a Risk Management Department (RMD) under policies approved by the Management Board. RMD identifies, evaluates and manages financial risks in close co-operation with the Bank's operating units. The Management Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk and use of non-derivative financial instruments. The internal audit is responsible for the independent review of risk management and control environment. The most important types of risk are credit risk, liquidity risk, market risk and other operational risk. Market risk includes currency risk, interest rate and other price risk.

31.2.1 Credit Risk

The Bank takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Credit risk is the most important risk for the Bank's business; management therefore carefully manages its exposure to credit risk. Credit exposures arise principally in lending activities that lead to loans and advances, balances with banks and receivable from financial institution, participation purchased and placements with other banks. Credit risk also arises in off-balance sheet financial instruments, such as Bank's contingencies and commitments. The credit risk management and control are centralized in credit risk management team of Bank and reported to the management team and head of each business unit regularly. Balances with DAB are not exposed to credit risk.

31.2.2 Credit risk measurement

a) Loans and advances

In measuring credit risk of loans and advances to customers and to banks at a counterparty level, the Bank reflects three components (i) the 'probability of default' by the client or counterparty on its contractual obligations; (ii) current exposures to the counterparty and its likely future development, from which the Bank derive the 'exposure at default'; and (iii) the likely recovery ratio on the defaulted obligations (the 'loss given default').

These credit risk measurements, which reflect expected loss are embedded in the Bank's daily operational management. The operational measurements can be contrasted with impairment allowances required under IAS 39, which are based on losses that have been incurred at the date of statement of financial position.

i) Overdue balances on loans to customers are segmented into four categories as described in note 4.4(b). The percentage of provision created on such overdue balances are as per guidelines issued by DAB and reflects the range of default probabilities defined for each category. This means that, in principle, exposures migrate between classes as the assessment of their probability of default changes.

ii) Exposure at default is based on the amounts, the Bank expects to be owed at the time of default. For example, for a loan this is the face value. For a commitment, the Bank includes any amount already drawn plus the further amount that may have been drawn by the time of default, should it occur.

iii) Loss given default or loss severity represents the Bank's expectation of the extent of loss on a claim should default occur. It is expressed as percentage loss per unit of exposure and typically varies by type of counterparty, type and seniority of claim and availability of collateral or other credit mitigation.

b) Other than loans and advances

Other than loans and advances includes balances with other banks and financial institutions and placements with other banks, investments in bonds and held with DAB, participation purchased and other assets. Judgments and instructions from the Bank's treasury are being used by the Bank's management in placing funds with other banks and are viewed as a way to gain better credit quality mapping and maintain a readily available source to meet the funding requirements at the same time when required.

Further, the Bank has banking relationships with financial institutions which have good international reputation and strong financial standing and therefore, probability of default by such financial institutions is low.

31.2.3 Risk limit control and mitigation policies

The Bank manages, limits and controls concentrations of credit risk wherever they are identified – in particular, to individual counterparties and groups, industries and countries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product and industry sector are approved quarterly by the Management Board.

The exposure to any one borrower is further restricted by sub-limits covering on- and off-balance sheet exposures. Actual exposures against limits are monitored daily.

Exposure to credit risk is also managed through analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations at the time of loan appraisal for initial and subsequent loans.

Some other specific control and mitigation measures are outlined below.

a) Collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advances, which is common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties
- Charges over business assets such as premises, inventory and accounts receivable

In addition, in order to minimize the credit loss, the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

b) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions – are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

Commitments to extend credit represent unused portions of authorizations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

31.2.4 Maximum exposure to credit risk before collateral held or other credit enhancements

	Maximum exposure	
	2017 AFN '000	2016 AFN '000
Credit risk exposures relating to on-balance sheet items are as follows:		
Balances with other banks	10,174,148	6,606,085
Placements – net	13,439,256	19,313,157
Investments – net (excluding capital notes with DAB)	12,433,030	12,862,525
Loans and advances to customers – net	3,369,970	3,729,388
Receivables from other financial institutions	587,534	522,484
Other assets	447,844	736,836
	40,451,783	43,770,475

	Maximum exposure	
	2017 AFN '000	2016 AFN '000
Credit risk exposures relating to off-balance sheet items are as follows:		
Guarantees	6,463,038	3,404,690
Undrawn loan and overdraft facilities	1,265,872	1,894,331
Commercial letters of credit	134,575	149,945
	7,863,485	4,402,857

The above table represents credit risk exposure to the Bank at 31 December 2017 and 31 December 2016, taking account of any collateral held or other enhancements attached. For on-balance-sheet assets the exposure set out above is based on net carrying amounts as reported in the statement of financial position.

The percentage of the maximum credit exposure in balances with other banks, placements, investments and loans and advances are as follows (in percentage of the total credit exposure):

	2017 AFN '000	2016 AFN '000
Balances with other banks	25.15%	15.09%
Placements – net	33.22%	44.12%
Investments – net (excluding capital notes with DAB)	30.74%	29.39%
Loans and advances to customers – net	8.33%	8.52%

31.2.5 Credit quality of financial assets

The credit qualities of Bank's financial assets have been assessed below by the reference to external credit ratings of counter parties determined by various international credit rating agencies. The counterparties for which external credit ratings were not available, and have been assessed by reference to internal credit ratings determined based on their historical information for any defaults in meeting obligations.

Balances with other banks/FIs	Credit rating	Credit rating agency	2017 AFN '000	2016 AFN '000
Counter parties with external credit ratings:				
Standard Chartered Bank	Aa2	Moody's	6,589,343	4,522,106
Commerzbank Germany	Baa1	Moody's	112,176	236,685
Emirates NBD	Baa1	Moody's	399,620	661,632
AkBank, Turkey	Baa3	Moody's	12,958	1,956
State commercial bank of Turkmenistan	N.A	N.A	1,647,969	669,552
IDFC Bank	BBB-	Fitch	1,380	474
Julius Baer	A2	Moody's	1,160,916	513,653
Aktif Bank	B2	Moody's	13,871	–
Asaka Bank	BBB-	Eurasia	235,634	–
Yes Bank, India	Baa3	Moody's	281	27

Placements	Credit rating	Credit rating agency	2017 AFN '000	2016 AFN '000
Abu Dhabi Commercial bank	A1	Moody's	348,600	1,002,300
Al Hilal Bank	A1	Moody's	1,394,400	–
Al Khalij Commercial Bank	A3	Moody's	348,600	–
Bank of Baroda Dubai	Baa3	Moody's	697,200	668,200
CIMB Malaysia	A3	Moody's	697,200	1,002,300
Commercial Bank International	A	Fitch	697,200	1,002,300
Commercial Bank of Dubai	Baa1	Moody's	697,200	–
Dubai Islamic Bank	A2	Moody's	697,200	668,200
IDBI DXB	Ba2	Moody's	697,200	–
IDFC Bank	Aa3	Moody's	697,200	–
Julius Baer	Aa2	Moody's	1,351,871	1,336,400
National bank of Oman	Baa3	Moody's	697,200	–
Qatar Islamic Bank	A1	Moody's	697,200	1,002,300
Qatar National Bank	Aa3	Moody's	1,045,800	1,002,300
Union National Bank	A1	Moody's	697,200	668,200
Yes Bank India	Baa3	Moody's	697,200	668,200
CSC Bank SAL	Ba2	Moody's	416,350	–
Emirates NBD	Baa1	Moody's	864,448	704,508

31. FINANCIAL RISK MANAGEMENT CONTINUED

31.2 Financial risk factors continued

31.2.5 Credit quality of financial assets continued

	2017 AFN '000	2016 AFN '000
Receivables from financial institutions		
Counter parties	587,534	522,484
Loans and advances – net		
Counter parties	3,369,970	3,729,388
Other assets		
Counter parties	568,956	736,836

Investments

Investments held carries various credit rating and ranges from B1& BBB+ to A & AAA,. These investments are managed by investment managers Emirates NBD and Julius Baer under investment criteria defined by the Bank.

31.2.6 Loans and advances – net

	Note	2017 AFN '000	2016 AFN '000
Loans and advances are summarized as follows:			
Neither past due nor impaired		3,310,708	3,676,076
Past due but not impaired		–	167
Impaired		144,891	200,205
Gross		3,455,599	3,876,448
Less: Allowance for impairment			
General		(33,108)	(109,756)
Specific		(52,521)	(37,304)
	9.4	(85,629)	(147,060)
		3,369,970	3,729,388

a) Loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the DAB regulations.

	Commercial loans		SME loans	Consumer loans	
	Overdraft AFN '000	Term loans AFN '000	Term loans AFN '000	Term loans AFN '000	Total AFN '000
31 December 2017					
Regular loans	2,694,235	528,384	41,215	46,874	3,310,708
31 December 2016					
Regular loans	3,415,649	161,630	80,606	18,191	3,676,076
(b) Loans and advances past due but not impaired					
31 December 2017					
Past due up to 30 days	–	–	–	–	–
Fair value of collateral	–	–	–	–	–
31 December 2016					
Past due up to 30 days	–	167	–	–	167
Fair value of collateral	–	10,308	–	–	10,308

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated by reference to market price or indexes of similar assets.

c) Loans and advances individually impaired

The individually impaired loans and advances to customers before taking into consideration the cash flows from collateral held is AFN 141,640 thousands (31 December 2016: AFN 189,865 thousands).

	Commercial loans		
	Overdraft AFN '000	Term loans AFN '000	Total AFN '000
31 December 2017			
Watch	16,770	–	16,770
Substandard	–	41,724	41,724
Doubtful	–	86,397	86,397
Loss	–	–	–
Total	16,770	128,121	144,891
Fair value of collateral	31,993	433,101	465,094
31 December 2016			
Watch	117,344	–	117,344
Substandard	–	2,301	2,301
Doubtful	–	79,509	79,509
Loss	–	–	–
Total	117,344	81,810	199,154
Fair value of collateral	253,448	568,277	821,725

d) Loans and advances restructured/rescheduled

Restructuring activities include extended payment arrangements and deferral of payments. Restructuring policies and practices are based on indicators or criteria which, in the judgment of management, indicate that payment will most likely continue. These policies are kept under continuous review. Renegotiated loans that would otherwise be past due or impaired at 31 December 2017 were AFN nil (31 December 2016: Nil).

	2017		2016	
Commercial loans and advances:	Loan amount at the time of rescheduling AFN '000	At year-end AFN '000	Loan amount at the time of rescheduling AFN '000	At year-end AFN '000
- Term loans	–	–	–	–
- Overdraft	55,776	51,909	3,144,475	409,948
Total	55,776	51,909	3,144,475	409,948

31.2.7 Concentration of risk of financial assets with credit risk exposure

a) Geographical sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by geographical region as of 31 December 2017. For this table, the Bank has allocated exposures to regions based on the country of domicile of our counterparties.

	Afghanistan AFN '000	Lebanon AFN '000	Singapore AFN '000	Germany AFN '000	Mexico AFN '000	Turkey AFN '000	Switzerland AFN '000	UAE AFN '000	India AFN '000	Qatar AFN '000	Korea AFN '000	Slovenia AFN '000	England AFN '000	Pakistan AFN '000	USA AFN '000	*Others AFN '000	Total AFN '000
2017																	
On balance sheet:																	
Balances with other banks	–	–	3,563,784	112,176	–	26,829	1,160,916	399,620	1,661	–	–	–	57,495	–	2,968,064	1,883,603	10,174,148
Placements – net	–	416,350	–	–	–	–	1,351,871	6,093,448	1,394,400	2,788,800	–	–	–	–	–	1,394,387	13,439,269
Investments – net (excluding capital notes)	–	–	–	–	400,241	388,376	–	1,308,467	–	1,222,350	1,333,919	301,420	–	407,894	–	7,263,757	12,433,031
Loans and advances to customers – net	3,369,970	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	3,369,970
Receivable from financial institutions	–	587,534	–	–	–	–	–	–	–	–	–	–	–	–	–	–	587,534
Other assets	447,844	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	447,844
	3,817,814	1,003,884	3,563,784	112,176	400,241	415,205	2,512,787	7,715,418	1,396,061	3,903,874	1,333,919	301,420	57,495	407,894	2,968,064	10,541,747	40,451,783
Off balance sheet:																	
Contingencies and commitments	7,863,485	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	7,863,485
	11,681,299	1,003,884	3,563,784	112,176	404,241	419,205	2,512,787	7,715,418	1,396,061	3,903,874	1,333,919	301,420	57,495	407,894	2,968,064	10,541,747	48,315,268
2016																	
On balance sheet:																	
Balances with other banks	–	–	2,146,777	236,685	–	1,956	513,653	661,632	501	–	–	–	60,593	–	2,314,736	669,552	6,606,085
Placements – net	–	–	–	–	–	–	1,336,400	8,221,758	2,004,600	–	–	–	–	–	–	8,018,400	19,581,158
Investments – net (excluding capital notes)	–	14,289	33,701	–	545,070	515,174	–	2,540,902	–	1,245,652	715,030	697,968	64,551	545,599	228,434	5,716,154	12,862,524
Loans and advances to customers – net	3,729,388	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	3,729,388
Receivable from financial institutions	–	522,484	–	–	–	–	–	–	–	–	–	–	–	–	–	–	522,484
Other assets	736,836	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	736,836
	4,466,224	536,773	2,180,478	236,685	545,070	517,130	1,850,053	11,424,292	2,005,101	1,245,652	715,030	697,968	125,144	545,599	2,543,170	14,404,106	44,038,475
Off balance sheet:																	
Contingencies and commitments	4,402,857	–	–	–	–	–	–	–	–	–	–	–	–	–	–	–	4,402,857
	8,869,081	536,773	2,180,478	236,685	545,070	517,130	1,850,053	11,424,292	2,005,101	1,245,652	715,030	697,968	125,144	545,599	2,543,170	14,404,106	48,441,332

31. FINANCIAL RISK MANAGEMENT CONTINUED

31.2 Financial risk factors continued

31.2.7 Concentration of risk of financial assets with credit risk exposure continued

b) Industry sectors

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by the industry sectors of counterparties.

	Government/ Public sector AFN '000	Manu-facturing AFN '000	Agriculture AFN '000	Construction AFN '000	Telecommu-nication AFN '000	Banks and financial institutions AFN '000	Traders AFN '000	Fuel suppliers AFN '000	Others AFN '000	Total AFN '000
2017										
On balance sheet:										
Balances with other banks	–	–	–	–	–	10,174,148	–	–	–	10,174,148
Placements – net	–	–	–	–	–	13,439,256	–	–	–	13,439,256
Investments – net (excluding capital notes)	12,397,030	–	–	–	–	36,001	–	–	–	12,433,031
Loans and advances to customers – net	–	505,873	–	78,384	–	–	1,739,513	943,347	102,853	3,369,970
Receivable from financial institutions	–	–	–	–	–	587,534	–	–	–	587,534
Other assets	–	–	–	–	–	–	–	–	447,844	447,844
	12,397,030	504,873	–	78,384	–	24,236,939	1,739,513	943,347	550,697	40,451,783
Off balance sheet:										
Contingencies and commitments	–	85	–	886,110	379,762	–	333,340	1,292,608	4,971,580	7,863,485
Total	12,397,030	505,958	–	964,494	379,762	24,236,939	2,072,853	2,235,955	5,522,277	48,315,268
2016										
On balance sheet:										
Balances with other banks	–	–	–	–	–	6,606,085	–	–	–	6,606,085
Placements – net	–	–	–	–	–	19,313,157	–	–	–	19,313,157
Investments – net (excluding capital notes)	10,145,337	100,158	–	–	166,175	2,037,660	–	–	413,198	12,862,528
Loans and advances to customers – net	–	463,767	49,175	134,340	–	–	1,318,370	938,826	824,910	3,729,388
Receivable from financial institutions	–	–	–	–	–	522,484	–	–	–	522,484
Other assets	–	–	–	–	–	–	–	–	736,836	736,836
	10,145,337	563,925	49,175	134,340	166,175	28,479,386	1,318,370	938,826	1,974,944	43,770,478
Off balance sheet:										
Contingencies and commitments	–	74	–	614,847	71,902	–	401,233	225,246	3,089,555	4,402,857
Total	10,145,337	563,999	49,175	749,187	238,077	28,479,386	1,719,603	1,164,072	5,064,499	48,173,335

31.3 Market risk

The Bank takes on exposure to market risks, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads and foreign exchange.

31.3.1 Foreign exchange risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Management committee sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily. The table below summarizes the Bank's exposure to foreign currency exchange rate risk at 31 December 2017 and 31 December 2016. Included in the table are the Bank's financial instruments at carrying amounts, categorized by currency.

	AED	USD	EURO	GBP	INR		Total
	Converted to AFN '000					AFN '000	AFN '000
As at 31 December 2017							
Assets							
Cash and balances with Da Afghanistan Bank	–	7,567,866	342,489	–	–	5,854,706	13,765,061
Balances with other banks	44,426	9,331,226	681,131	57,495	1,661	58,210	10,174,148
Placements – net	–	13,022,906	416,350	–	–	–	13,439,256
Investments – net	–	12,433,030	–	–	–	3,533,535	15,966,565
Loans and advances to customers – net	–	2,210,797	–	–	–	1,159,173	3,369,970
Receivables from financial institutions	–	505,555	67,425	–	–	14,554	587,534
Other assets	–	308,805	14,265	–	–	245,886	568,956
Total financial assets	44,426	45,380,184	1,521,660	57,495	1,661	10,866,064	57,871,491
Liabilities							
Customers' deposits	–	46,540,670	1,386,887	51,778	–	8,782,085	56,761,420
Deposits from bank	–	–	–	–	–	500,000	500,000
Other liabilities	–	208,052	2,401	–	–	101,420	311,873
Total financial liabilities	–	46,748,721	1,389,288	51,778	–	8,883,506	57,073,293
On-balance sheet financial position – net	44,426	(1,368,537)	132,372	5,717	1,661	1,982,559	798,197
As at 31 December 2016							
Total financial assets	90,938	45,277,296	1,575,119	62,991	500	9,006,520	56,013,365
Total financial liabilities	–	45,265,022	1,580,939	82,939	–	7,341,810	54,270,710
On-balance sheet financial position – net	90,938	(88,076)	(5,820)	(19,948)	500	1,765,060	1,742,655

If the functional currency, at the year end date, strengthens/weakens by 10% against the USD with all other variables held constant, the impact on profit or loss for the period would have been AFN 136,854 thousands higher/lower (31 December 2016: AFN 88,076 thousands higher/lower) respectively mainly as a result of exchange gains/losses on translation of foreign exchange denominated receivables and payables.

If the functional currency, at the year end date, strengthens/weakens by 10% against the EURO with all other variables held constant, the impact on profit or loss for the period would be AFN 13,237 thousands lower/higher (31 December 2016: AFN 582 thousands lower/higher) respectively mainly as a result of exchange gains/losses on translation of foreign exchange denominated receivables and payables.

If the functional currency, at the year end date, strengthens/weakens by 10% against the AED with all other variables held constant, the impact on profit or loss for the period would be AFN 4,443 thousands higher/lower (2016: AFN 9,094 thousands higher/lower) respectively mainly as a result of exchange gains/losses on translation of foreign exchange denominated receivables and payables.

If the functional currency, at the year end date, strengthens/weakens by 10% against the GBP with all other variables held constant, the impact on profit or loss for the period would be AFN 572 thousands higher/lower (2016: AFN 1,995 thousands higher/lower) respectively mainly as a result of exchange gains/losses on translation of foreign exchange denominated receivables and payables.

If the functional currency, at the year end date, strengthens/weakens by 10% against the INR with all other variables held constant, the impact on profit or loss for the period would be AFN 166 thousands higher/lower (2016: AFN 50 thousands higher/lower) respectively mainly as a result of exchange gains/losses on translation of foreign exchange denominated receivables and payables.

31.3.2 Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce losses in the event that unexpected movements arise. Bank's investments, loans and advances are primarily linked to EONIA, LIBOR and US Prime.

The table below summarizes the Bank's exposure to interest rate risks. It includes the Bank's financial instruments at carrying amount, categorized by the earlier of contractual reprising or maturity dates.

	Interest bearing							
	Up to 1 month AFN '000	1 to 3 months AFN '000	3 to 12 months AFN '000	1 to 5 years AFN '000	Over 5 years AFN '000	Total interest bearing AFN '000	Non-interest bearing AFN '000	Total AFN '000
As at 31 December 2017								
Assets								
Cash and balances with Da Afghanistan Bank	2,490,242	–	–	–	–	2,490,242	11,274,819	13,765,061
Balances with other banks	6,701,519	–	–	–	–	6,701,519	3,472,629	10,174,148
Placements – net	4,656,519	2,507,937	5,577,600	697,200	–	13,439,256	–	13,439,269
Investments – net	219,489	219,658	1,121,028	13,675,930	730,460	15,966,565	–	15,966,565
Loans and advances to customers – net	2,953,959	68,721	205,693	141,597	–	3,369,970	–	3,369,970
Receivables from financial institutions	–	–	–	–	–	–	587,534	587,534
Other assets	–	–	–	–	–	–	447,844	447,844
Total financial assets	17,021,728	2,796,316	6,904,321	14,514,727	730,460	41,967,552	15,782,826	5,750,378
Liabilities								
Customers' deposits	510,738	37,353	37,353	455,707	–	1,041,151	55,220,269	56,761,420
Deposits from bank	–	–	500,000	–	–	500,000	–	500,000
Other liabilities	–	–	–	–	–	–	191,164	191,164
Total financial liabilities	510,738	37,353	537,353	455,707	–	1,541,151	55,411,433	56,952,584
Total interest reprising gap	16,510,990	2,758,963	6,366,968	14,059,020	730,460	40,426,401	(39,628,606)	797,794
As at 31 December 2016								
Total financial assets	12,831,055	4,712,164	16,732,275	10,310,126	223,164	44,808,783	10,934,317	55,743,100
Total financial liabilities	516,319	33,410	386,074	668,200	–	1,604,003	52,621,713	54,225,716
Total interest reprising gap	12,314,736	4,678,754	16,346,201	9,641,926	223,164	43,204,780	(41,687,396)	1,517,384

If the interest increase/(decrease) by 100 bps, the impact on profit or loss for the year would have been AFN 432,048 thousands (31 December 2016: AFN 396,401 thousands) lower/higher respectively.

31. FINANCIAL RISK MANAGEMENT CONTINUED

31.4 Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

31.4.1 Liquidity risk management process

The Bank's liquidity management process, includes:

- Day-to-day funding, managed by monitoring future cash flows to ensure that requirements can be met. This includes replenishment of funds as they mature or are borrowed by customers;
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- Monitoring balance sheet liquidity ratios against internal and regulatory requirements; and
- Managing the concentration and profile of debt maturities.

Monitoring and reporting take the form of cash flow measurement and projections for the next day, week and month respectively, as these are key periods for liquidity management. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets.

Bank Treasury also monitors unmatched medium-term assets, the level and type of undrawn lending commitments, the usage of overdraft facilities and the impact of contingent liabilities such as standby letters of credit and guarantees.

31.4.2 Funding approach

Sources of liquidity are regularly reviewed by the Asset Liability Committee (ALCO) to maintain a wide diversification by currency, geography, provider, product and term.

Liquidity Ratios

Advance to deposit ratios

	2017	2016
Year-end	6.09%	6.90%
Maximum	6.90%	6.37%
Minimum	5.57%	5.14%
Average	6.31%	5.92%

31.4.3 Non-derivative financial liabilities and assets held for managing liquidity risk

The table below presents the cash flows payable by the Bank under non-derivative financial liabilities and assets held to manage liquidity risk by remaining contractual maturities at the date of the statement of financial position. The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Bank manages the inherent liquidity risk based on expected undiscounted cash inflows.

	Up to 1 month AFN '000	1 to 3 months AFN '000	3 to 12 months AFN '000	1 to 5 years AFN '000	Over 5 years AFN '000	Total AFN '000
As at 31 December 2017						
Liabilities						
Customers' deposits	55,731,007	37,353	537,353	455,707	–	56,261,420
Deposits from bank	–	500,000	–	–	–	500,000
Other liabilities	191,164	–	–	–	–	191,164
Total financial liabilities (contractual maturity dates)	55,922,171	37,353	537,353	455,707	–	56,952,584
Total financial assets (contractual maturity dates)	32,804,554	2,796,316	6,904,321	14,514,727	730,460	57,750,378
As at 31 December 2016						
Liabilities						
Customers' deposits	52,989,958	33,410	386,074	668,200	–	54,077,642
Other liabilities	193,068	–	–	–	–	193,068
Total financial liabilities (contractual maturity dates)	53,183,026	33,410	386,074	668,200	–	54,270,710
Total financial assets (contractual maturity dates)	23,765,371	4,712,164	16,732,275	10,310,126	223,164	55,743,100

Assets available to meet all of the liabilities and to cover outstanding loans commitment include cash and balances with Da Afghanistan Bank, balances with other banks and receivable from financial institutions, placements, loans and advances to customers and security deposits and other receivables.

31.4.4 Off-balance sheet items

The dates of the contractual amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers and other facilities are summarized in the table below.

	Not later than 1 year AFN '000	1 to 5 years AFN '000	Over 5 years AFN '000	Total AFN '000
As at 31 December 2017				
Guarantees	2,321,104	4,141,935	–	6,463,038
Undrawn loans and overdraft facilities	850,618	415,254	–	1,265,872
Commercial letters of credit	134,575	–	–	134,575
Total	3,306,297	4,557,188	–	7,863,485
As at 31 December 2016				
Guarantees	2,147,457	1,257,233	–	3,404,690
Undrawn loans and overdraft facilities	848,222	252,880	–	1,101,102
Commercial letters of credit	149,945	–	–	149,945
Total	3,145,624	1,510,113	–	4,655,737

31.5 Fair value of financial assets and financial liabilities

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

a) Financial instruments measured at fair value using a valuation technique

The table below analyses financial instruments carried at fair value, by valuation method. The various fair value levels have been defined as follows:

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

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

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	Level 1 AFN '000	Level 2 AFN '000	Level 3 AFN '000
Investments in bonds – available for sale investments	–	4,586,137	–
As at 31 December 2017	–	4,586,137	–
As at 31 December 2016	–	5,030,993	–

Valuation technique and key inputs used for investments in bonds were quoted market bid price in active market.

There were no transfers made among various levels of fair value hierarchy during the year.

b) Financial instruments not measured at fair value

The table below summarizes the carrying amounts and fair values of those financial assets and liabilities which are presented on the Bank's statement of financial position at value other than fair value.

	Carrying Value		Fair Value	
	2017 AFN '000	2016 AFN '000	2017 AFN '000	2016 AFN '000
Financial assets				
Cash and balances with Da Afghanistan Bank	13,765,061	10,452,572	13,765,061	10,452,572
Balances with other banks	10,174,148	6,606,085	10,174,148	6,606,085
Placements – net	13,439,256	19,313,157	13,439,256	19,313,157
Investments – net	15,963,017	14,377,016	15,966,565	14,382,580
Loans and advances to customers – net	3,369,970	3,729,388	3,369,970	3,729,388
Receivables from financial institutions	587,534	522,484	587,534	522,484
Advance to staff, Security deposits and other receivables – net	447,844	736,836	447,844	736,836
Financial liabilities				
Customers' deposits	56,761,420	54,077,642	56,761,420	54,077,642
Deposits from bank	500,000	–	500,000	–
Other liabilities	311,873	193,068	311,873	193,068
Off-balance sheet financial instruments				
Bank's guarantees	6,463,038	3,404,690	6,463,038	3,404,690
Bank's commitments	1,400,447	998,167	1,400,447	998,167

The carrying values of these financial assets and liabilities approximates their fair values as at the date of statement of financial position.

i) Investments:

These include investment bonds classified as held-to-maturity which are measured at amortized cost. The fair value of these investments is equal to the carrying amount.

ii) Loans and advances, other assets and other financial liabilities

Fair value of loans and advances, security deposits and other receivables and all the financial liabilities cannot be calculated with sufficient reliability due to absence of current and active market for such assets and reliable data regarding market rates for similar instruments, so its carrying amount is its fair value. The provision for loans and advances has been calculated in accordance with the Bank's policy and regulations issued by DAB.

iii) Off-balance sheet financial instruments

The fair value of the off-balance sheet financial instruments is equal to the carrying amounts.

31.6 The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of balance sheets, are:

i) to comply with the capital requirements set by the DAB;

ii) to safeguard the Bank's ability to continue as a going concern so that it can continue to be self-sustainable; and

iii) to maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored regularly by the Bank's management. DAB requires each bank to maintain its Tier 1 Capital ratio and Regulatory Capital ratio to be at least 6% and 12% respectively. The Bank is maintaining this ratio well above the required level.

The table below summarizes the composition of the regulatory capital and ratio of the Bank:

	2017 AFN '000	2016 AFN '000
Tier 1 (Core) Capital:		
Total equity capital	3,844,934	3,901,072
Less: Intangible assets	445,918	527,457
Net deferred tax assets	73,603	21,440
Profit for the year	357,945	519,072
	2,967,468	2,833,103
Tier 2 (Supplementary) Capital:		
General reserves as per DAB's regulation, but restricted to 1.25% of total risk-weighted exposure	213,611	109,756
Profit for the year	357,945	519,072
Revaluation reserve on bonds (45%)	1,597	–
	571,556	628,828
Tier 2 (Supplementary) Capital (restricted 100% of Tier (Core) Capital)	571,556	628,828
Regulatory Capital = Tier 1 + Tier 2	3,539,024	3,461,931

31. FINANCIAL RISK MANAGEMENT CONTINUED

Risk-weight categories

	2017 AFN '000	2016 AFN '000
0% risk weight:		
Cash in Afghani and fully-convertible foreign currencies	2,484,654	1,978,419
Direct claims on DAB	14,813,942	9,994,207
Direct claims on other Governments	1,613,406	773,442
Others	–	578,314
Total	18,912,002	13,324,382
0% risk-weight total (above total x 0%)	–	–
20% risk weight:		
Balances with other banks	24,313,203	26,441,726
	586,124	–
20% risk-weight total (above total x 20%)	4,979,865	5,288,345
100% risk weight:		
All other assets	17,037,862	18,757,185
Less: Intangible assets	(445,918)	(527,457)
Less: Deferred tax assets	(73,603)	(21,440)
All other assets – net	16,518,341	18,208,288
100% risk-weight total (above total x 100%)	16,518,341	18,208,288

Credit conversion factor

	2017 AFN '000	2016 AFN '000
0% risk weight:		
Undrawn loan and overdraft facilities	1,265,872	848,222
Guarantees	1,175,619	3,391,190
0% credit conversion factor total (risk-weighted total x 0%)	–	–
0% risk-weight total (above total x 0%)	–	–
20% risk weight:		
Commercial letters of credit	134,575	149,945
Guarantees	3,847,157	–
20% credit conversion factor total (risk-weighted total x 20%)	26,915	29,989
20% risk-weight total (above total x 20%)	5,383	5,998
100% risk weight:		
Guarantees	1,440,262	13,500
100% credit conversion factor total (risk-weighted total x 100%)	1,440,262	13,500
100% risk-weight total (above total x 100%)	1,440,262	13,500
Total risk-weighted assets	22,943,852	23,516,131
Tier 1 Capital Ratio		
(Tier 1 capital as % of total risk-weighted assets)	12.93%	12.05%
Regulatory Capital Ratio		
(Regulatory capital as % of total risk-weighted assets)	15.42%	14.72%

32. ISLAMIC BANKING

The Bank started Islamic banking operations in November 2015 with the following Islamic deposit products.

Qardul Hasana Current Account

This account is profit-free account specifically designed to meet the requirements of the Bank's customers. Account holders will have easy access to their account at any time to meet their personal or business expenses.

Mudarabah Savings Account

This account is designed specifically to meet the requirements of customers who authorize the Bank to invest their cash deposits. Customers can deposit or withdraw money at any time they wish, and can earn profits on their savings.

Mudarabah Term Investment Deposit

These funds are accepted with different investment periods. The Bank manages and invests the funds aiming at realizing the best profit for the mutual interest of the parties.

Below are the figures relating to Islamic banking as at 31 December 2017

	2017 AFN '000	2016 AFN '000
Assets		
Cash and balances with banks	290,887	202,158
Loans and advances	42,279	–
Other assets	10,600	–
Receivable – head Office	299,600	148,445
	643,366	350,603
Liabilities		
Payable to head Office	–	–
Deposit – current	94,520	81,065
Deposit – saving	495,818	246,962
Deposit – term Deposit	49,861	36,592
Others	12,419	–
	652,618	364,619
Accumulated losses	(9,252)	(14,017)
	643,366	350,602
General and administrative expenses net off	(13,197)	(14,017)

33. GENERAL

33.1 Corresponding figures have been reclassified/re-arranged wherever necessary to facilitate comparison in the presentation in the current year. However, there are no material reclassification/re-arrangement to report.

33.2 The figures in these financial statements have been rounded off to the nearest in thousands in AFN.

34. DATE OF AUTHORIZATION FOR ISSUE

These financial statements were authorized for issue by the Board of Supervisors of the Bank on 10 March 2018.

Chief Executive Officer | Chief Financial Officer | Chairman

Designed and produced by Group Origin

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