

**Central Bank of the Republic of Azerbaijan**

**Financial Statements  
for the year ended 31 December 2021**

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# Independent Auditors’ Report

## To the Management Board of the Central Bank of the Republic of Azerbaijan

### Opinion

We have audited the financial statements of the Central Bank of the Republic of Azerbaijan (the “Bank”), which comprise the statement of financial position as at 31 December 2021, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2021, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

### Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors’ Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (*IESBA Code*) together with the ethical requirements that are relevant to our audit of the financial statements in the Republic of Azerbaijan, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Key Audit Matters

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

Classification of debt securities	
Please refer to the Note 7 in the financial statements.	
The key audit matter	How the matter was addressed in our audit
<p>Operations with financial instruments represent a core business of the Bank and debt securities constitute a majority of the Bank's assets.</p> <p>We paid particular attention to the matter of classification of debt securities in accordance with the IFRS 9 requirements.</p> <p>Due to the significance and diversity of portfolios of debt securities of the Bank, significant turnover of debt securities during the year and management judgement involved, this area is a key audit matter.</p>	<p>We analysed the definition of business models used to manage debt securities by making inquiries to responsible employees, reviewing the Bank's internal documentation and analyzing internal business processes on selected significant debt securities portfolios.</p> <p>We checked that the Bank has performed proper assessment whether contractual cash flows are solely payments of principal and interest by analyzing underlying documents for a sample of debt securities.</p> <p>For debt securities managed in the held-to-collect and sale business model we analyzed the information on frequency and volume of sales, reasons of such sales and assessed whether the sales are consistent with the held-to-collect and sale business model based on our understanding and publicly available market information.</p> <p>We also assessed whether the financial statements provide an appropriate disclosure of key classification and measurement principles for debt securities in accordance with IFRS 9.</p>

### 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 IFRS, 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 basis of accounting. In discharging this responsibility, the management considers the provisions of article 14 of the Law of the Republic of Azerbaijan "On the Central Bank of the Republic of Azerbaijan", which states that the Bank cannot be declared bankrupt and that any shortfall in capital will be covered by the issuance of securities by the Government of the Republic of Azerbaijan.

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



## Auditors' 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 auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

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

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



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

The engagement partner on the audit resulting in this independent auditors' report is:

A handwritten signature in blue ink, appearing to read 'Andrey Kouznetsov'. The signature is written in a cursive style and is enclosed within a large, thin, blue oval shape.

Andrey Kouznetsov

"KPMG Audit Azerbaijan" LLC

Baku, The Republic of Azerbaijan

26 April 2022

**Central Bank of the Republic of Azerbaijan****Statement of Financial Position**

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

	<b>Note</b>	<b>31 December 2021</b>	<b>31 December 2020</b>
<b>ASSETS</b>			
Cash and cash equivalents	4	6,838,991	5,615,273
Special Drawing Rights with the IMF	5	1,258,160	375,543
Derivative financial instruments	6	2,834	449
Debt securities	7	17,362,276	18,579,674
Loans to banks	8	356,281	399,408
Loans to non-bank credit organizations	9	20,014	25,330
Loans to Deposit Insurance Fund	10	236,600	207,222
Property and equipment	11	76,361	86,461
Intangible assets	12	70,218	73,527
Other financial assets	13	2,135	49,370
Other assets	14	186,698	73,713
<b>Total assets</b>		<b>26,410,568</b>	<b>25,485,970</b>
<b>LIABILITIES</b>			
Money in circulation	15	12,310,018	11,839,664
Short-term deposits of resident banks	16	-	2,713,336
Amounts due to government organisations	17	4,004,637	4,921,318
Amounts due to credit institutions	18	7,440,004	3,204,953
Amounts due to other organisations	19	11,410	9,066
Debt securities in issue	20	199,402	648,213
Liabilities on transactions with the IMF	5	1,261,131	378,505
Amounts due to international financial institutions	21	1,025	1,405
Derivative financial instruments	6	862	3,556
Other financial liabilities	22	10,875	142,259
Other liabilities		1,016	1,783
<b>Total liabilities</b>		<b>25,240,380</b>	<b>23,864,058</b>
<b>EQUITY</b>			
Charter capital	23	500,000	500,000
Capital reserves	23	526,968	526,968
Revaluation reserve for debt securities at FVOCI		(40,043)	(1,065)
Retained earnings		183,263	596,009
<b>Total equity</b>		<b>1,170,188</b>	<b>1,621,912</b>
<b>Total liabilities and equity</b>		<b>26,410,568</b>	<b>25,485,970</b>

The financial statements were approved by Management on 26 April 2022 and were signed on its behalf by:

Mr. Aftandil Babayev  
Deputy Governor

Ms. Sevda Amirova  
Director of Financial Management Department/  
Chief Accountant

**Central Bank of the Republic of Azerbaijan****Statement of Profit or Loss and Other Comprehensive Income***(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

	<b>Note</b>	<b>2021</b>	<b>2020</b>
Interest income calculated using the effective interest method	24	121,086	151,881
Other interest income	24	10,141	17,370
Interest expense	24	(166,457)	(149,127)
<b>Net interest (expense)/income</b>		<b>(35,230)</b>	<b>20,124</b>
Fee and commission income	25	20,488	10,251
Fee and commission expense	26	(3,835)	(6,501)
Gain on recognition of financial liabilities	27	7,487	52,447
Loss on initial recognition of financial assets	28	(6,415)	(75,742)
Net (losses) gains from debt securities at fair value through profit or loss		(16,185)	10,566
Net (losses) gains from disposals of securities measured at fair value through other comprehensive income		(35,394)	19,007
Net gains (losses) from derivative financial instruments		23,254	(14,588)
Net gains from investments in money market funds at fair value through profit or loss		133	4,320
Net (losses) gains from foreign exchange translation	29	(60,298)	66,044
Impairment of debt securities at fair value through other comprehensive income		90	(247)
Net (losses) gains from trading in currencies		(935)	1,981
Other operating income		5,306	46,677
Recovery of impairment loss	30	18,361	14,375
Administrative and other operating expenses	31	(79,573)	(96,229)
<b>(Loss) Profit for the year</b>		<b>(162,746)</b>	<b>52,485</b>
<b>Other comprehensive loss:</b>			
<i>Items that are or may be reclassified subsequently to profit or loss:</i>			
Debt securities at fair value through other comprehensive loss:	7		
- Net (losses) gains arising during the year		(74,372)	12,047
- Gains (losses) reclassified to profit or loss upon disposal		35,394	(19,007)
<b>Other comprehensive loss for the year</b>		<b>(38,978)</b>	<b>(6,960)</b>
<b>Total comprehensive (loss) income for the year</b>		<b>(201,724)</b>	<b>45,525</b>



**Central Bank of the Republic of Azerbaijan****Statement of Changes in Equity***(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

	<b>Charter fund</b>	<b>Capital reserves</b>	<b>Revaluation reserve for debt securities at FVOCI</b>	<b>Retained earnings</b>	<b>Total equity</b>
<b>Balance at 1 January 2020</b>	<b>500,000</b>	<b>526,958</b>	<b>5,895</b>	<b>1,543,524</b>	<b>2,576,377</b>
Profit for the year	-	-	-	52,485	52,485
<b>Other comprehensive loss</b>					
Revaluation reserve for debt securities at FVOCI:					
- Net change in fair value	-	-	12,047	-	12,047
- Net amount reclassified to profit or loss	-	-	(19,007)	-	(19,007)
Total other comprehensive loss	-	-	(6,960)	-	(6,960)
<b>Total comprehensive income / (loss) for the year</b>	<b>-</b>	<b>-</b>	<b>(6,960)</b>	<b>52,485</b>	<b>45,525</b>
<b>Transactions recorded directly in equity</b>					
Transfer to the State Budget	-	-	-	(1,000,000)	(1,000,000)
Other transactions	-	10	-	-	10
<b>Total transactions recorded directly in equity</b>	<b>-</b>	<b>10</b>	<b>-</b>	<b>(1,000,000)</b>	<b>(999,990)</b>
Balance as at 31 December 2020	<b>500,000</b>	<b>526,968</b>	<b>(1,065)</b>	<b>596,009</b>	<b>1,621,912</b>
<b>Balance at 1 January 2021</b>	<b>500,000</b>	<b>526,968</b>	<b>(1,065)</b>	<b>596,009</b>	<b>1,621,912</b>
Loss for the year	-	-	-	(162,746)	(162,746)
<b>Other comprehensive loss</b>					
Revaluation reserve for debt securities at FVOCI:					
- Net change in fair value	-	-	(74,372)	-	(74,372)
- Net amount reclassified to profit or loss	-	-	35,394	-	35,394
Total other comprehensive loss	-	-	(38,978)	-	(38,978)
<b>Total comprehensive loss for the year</b>	<b>-</b>	<b>-</b>	<b>(38,978)</b>	<b>(162,746)</b>	<b>(201,724)</b>
<b>Transactions recorded directly in equity</b>					
Transfer to the State Budget	-	-	-	(250,000)	(250,000)
Other transactions	-	-	-	-	-
<b>Total transactions recorded directly in equity</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(250,000)</b>	<b>(250,000)</b>
Balance as at 31 December 2021	<b>500,000</b>	<b>526,968</b>	<b>(40,043)</b>	<b>183,263</b>	<b>1,170,188</b>

**Central Bank of the Republic of Azerbaijan****Statement of Cash Flows***(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

	Note	2021	2020
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Interest receipts		133,968	166,336
Interest payments		(108,168)	(150,506)
Fee and commission receipts		20,488	10,251
Fee and commission payments		(3,835)	(6,501)
Net receipts / (payments) from trading in debt securities at FVTPL		15,533	(11,960)
Net receipts / (payments) from derivative financial instruments		18,175	(15,194)
Net payments / (receipts) from trading in foreign currencies		(935)	1,981
Other operating income receipts		4,060	4,994
Net receipts from investments in money market funds at fair value through profit or loss		133	4,320
Administrative and other operating expenses payments		(76,010)	(67,931)
<b>Cash flows used in operating activities before changes in operating assets and liabilities</b>		<b>3,409</b>	<b>(64,210)</b>
<b>(Increase)/decrease in operating assets</b>			
Debt securities at fair value through profit or loss		(40,086)	(2,167)
Special Drawing Rights with the IMF		(905,281)	53
Loans to banks		63,137	(113,521)
Loans to non-bank credit organizations		5,317	(6,463)
Loans to Deposit Insurance Fund		(20,000)	(280,000)
Other financial assets		(316)	303
Other assets		(2,498)	(5,658)
<b>Increase/(decrease) in operating liabilities</b>			
Money in circulation		470,354	1,434,151
Short-term deposits of resident banks		(2,765,000)	(310,000)
Amounts due to government organisations		(904,567)	2,181,730
Amounts due to credit institutions		4,248,668	461,414
Amounts due to other organisations		2,344	(2,064)
Debt securities in issue		(447,951)	(47,726)
Other financial liabilities		(1,324)	1,591
Other liabilities		(939)	(633)
<b>Net cash from operating activities</b>		<b>(294,733)</b>	<b>3,246,800</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Acquisition of debt securities at fair value through other comprehensive income	7	(4,812,820)	(13,558,864)
Proceeds from sale and redemption of debt securities at fair value through other comprehensive income	7	5,813,366	12,619,981
Proceeds from redemption of debt securities carried at amortised cost	7	6,905	12,984
Purchases of property, equipment	11	(11,013)	(23,390)
Purchases of intangible assets	12	(11,301)	(29,608)
Other assets (investments for the construction)		(77,088)	-
<b>Cash flows from (used in) investing activities</b>		<b>908,049</b>	<b>(978,897)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Transfers to the State Budget		(250,000)	(1,000,000)
Proceeds / (repayment) of IMF borrowings		905,305	(1)
Proceeds from amounts due to international financial institutions		311,765	231,371
Repayment of amounts due to international financial institutions		(312,145)	(231,410)
<b>Cash flows from (used in) financing activities</b>		<b>654,925</b>	<b>(1,000,040)</b>
<b>Net decrease in cash and cash equivalents</b>		<b>1,268,241</b>	<b>1,267,863</b>
Effect of exchange rate changes on cash and cash equivalents		(44,523)	38,098
Cash and cash equivalents at the beginning of the year		5,615,273	4,309,312
<b>Cash and cash equivalents at the end of the year</b>	4	<b>6,838,991</b>	<b>5,615,273</b>

## **Central Bank of the Republic of Azerbaijan**

*Notes to the Financial Statements for the year ended 31 December 2021*

*(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

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### **1 Background**

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2021 for the Central Bank of the Republic of Azerbaijan.

#### **Principal activity**

The Central Bank of the Republic of Azerbaijan (the "Bank") is the central bank of the Republic of Azerbaijan, and is wholly-owned by the Republic of Azerbaijan. It acts in accordance with the "Law on the Central Bank of the Republic of Azerbaijan" effective from 10 December 2004 (the "Law").

Article 4 of the Law sets out the goals of the Bank, which are as follows:

- The primary goal of the Bank is to ensure, within its power, the stability of prices;
- The goal of the Central Bank's activity shall also be to organize and ensure operation of centralized interbank and other unlicensed payment systems, as well as support the stability of the banking system
- Profit making is not a primary goal of the Bank.

Article 5 of the Law sets out the functions of the Bank as follows:

- Establish and implement the country's monetary and foreign exchange policy;
- Organize cash circulation; in accordance with paragraph 2 of article 19 of the Constitution and the Law: issue, put into circulation, and withdraw banknotes from circulation;
- Determine and declare the official exchange rate of Azerbaijani Manat;
- Implement foreign currency regulation and control;
- Maintain and manage the gold and foreign currency reserves at its disposal;
- Manage the drawing up of the reporting balance of payments and participate in the drawing-up of the projected balance of payments of the country;
- Develop the country's consolidated (public and non-public) foreign debt statistics and international investment balance, summarize and disseminate data;
- Organize, coordinate, regulate activities of and oversee centralized interbank and other unlicensed payment systems.

Pursuant to the Order no 1616 dated 28.11.2019 of the President of the Republic of Azerbaijan "On improving the management of regulation and supervision of financial services market" the Financial Market Supervisory Authority was abolished, its powers as defined in the laws of the Republic of Azerbaijan, including its rights and responsibilities in the areas of licensing, regulation and supervision, protection of rights of investors and consumers of financial services, as well as its property were transferred to the Bank.

In accordance with Article 14.1 of the Law, the Bank cannot be declared bankrupt. Any deficit in capital is to be covered by the securities issued by the Government of Azerbaijan Republic.

Pursuant to the legislation of the Republic of Azerbaijan and the international treaties acceded to by the Republic of Azerbaijan, the Bank represents the Republic of Azerbaijan in relations with the central banks of foreign states, as well as international financial and credit institutions in matters relating to the Bank's responsibilities.

The Bank may conclude agreements on cooperation with the central banks of foreign countries concerning various areas of its activities. It may also conclude clearing and settlement agreements and other agreements with foreign public and private clearing agencies, on its own behalf and on behalf of the Republic of Azerbaijan, if appropriately empowered.

The Bank may participate in the capital and activity of international organisations for the purpose of cooperation in monetary and foreign exchange policy.

## **Central Bank of the Republic of Azerbaijan**

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

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At 31 December 2021, the Management Board (the “Board”) of the Bank was composed of the following members:

<b>Name</b>	<b>Position</b>
Mr. Elman Rustamov	Governor
Mr. Alim Guliyev	First Deputy Governor
Mr. Aftandil Babayev	Deputy Governor
Mr. Vadim Khubanov	Deputy Governor

The responsibilities of the Board and Governor are presented in Article 22 of the Law.

The Bank’s main office is located at the following address: 90 Rashid Behbudov Street, Baku, AZ1014, Azerbaijan. The Bank had six regional branches in the Republic of Azerbaijan (2020: six).

### **Functional and presentation currency**

The functional currency of the Bank is Azerbaijani Manats (“AZN”) as being the national currency of the Republic of Azerbaijan. These financial statements are presented in thousands of AZN, rounded to nearest thousand, unless otherwise stated.

### **Operating Environment of the Bank**

In 2021, maintaining the macroeconomic and financial stability in the country was one of the main priorities of the Central Bank of the Republic of Azerbaijan. The Central Bank performed its functions in accordance with its mandate, and macroeconomic stability has been achieved in the country as a result of measures taken in close coordination with the government.

In the context of a significant deterioration of the external background of inflation, the Central Bank tried to mitigate the impact of cost factors of inflation by pursuing an adequate monetary policy and managing price expectations. Interest rate corridor parameters have been revised taking into account the updated macroeconomic forecasts and risk balance.

During the year, the formation of a positive balance of payments surplus of the country against the background of high oil prices and a significant increase in non-oil exports allowed to maintain the stability of the national currency and build up strategic foreign exchange reserves by the end of the year. In the environment of equilibrium of the foreign exchange market, exchange rate stability created conditions for a significant balancing of inflation pressures coming from the external environment.

## **2 Basis of preparation**

### **Basis of measurement**

The financial statements are prepared on the historical cost basis except that financial instruments at fair value through profit or loss and financial instruments at fair value through other comprehensive income are stated at fair value.

### **Estimates and judgments**

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies is described in the following notes.

### **ECL measurement**

Measurement of ECLs is a significant estimate that involves determination of relevant methodology, models and data inputs. Details of ECL measurement are disclosed in Note 32. The following components have a major impact on credit loss allowance: definition of default, significant increase in credit risk (“SICR”), probability of default (“PD”), exposure at default (“EAD”) and loss given default (“LGD”). The Bank regularly

reviews the models and inputs to the models to reduce any differences between expected credit loss estimates and actual credit loss experience.

**Significant increase in credit risk (“SICR”)**

In order to determine whether there has been a significant increase in credit risk, the Bank compares the risk of a default occurring over the life of a financial instrument at the end of the reporting date with the risk of default at the date of initial recognition. The assessment considers relative increase in credit risk, all reasonable forward looking information available without undue cost and effort, which includes a range of factors of particular borrowers.

**Business model assessment**

The Bank classifies financial assets on the basis of the business model for managing the financial assets and cash flow characteristics. The business model is assessed on the basis of actual performance of the Bank for holding and managing financial assets at a level of financial assets groups and portfolios (sub-portfolio), as well as Management’s judgements. When assessing a business model, factors such as the purpose, strategic structure, risk parameters of financial assets, the relative significance of sources of income derived from the assets and the frequency and specific weight of purchase (sale) transactions to the portfolio are taken into account. In addition, future business expectations are also considered when determining the business model.

The Bank classifies financial assets as “hold to collect”, “hold to collect and sell” and “other business” model. Selling financial assets for i) monetary policy purposes, ii) re-balancing, iii) achieving higher returns; and iv) investment restrictions is an integral part of “hold to collect and sell” business model.

**Assessment whether cash flows are solely payments of principal and interest (“SPPI”)**

For the purpose of classification of financial assets the Bank assesses whether the cash flows represent solely payments of principal and interest (“SPPI”). The principal is the fair value of the financial asset at initial recognition, which may change over the life of a financial instrument. The interest is the compensation for the time value of money, credit risk and other risks associated with the outstanding principal, as well as the profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank’s claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.
- inverse floater condition

All the instruments that are included in “hold to collect” and “hold to collect and sell” business models passed SPPI tests.

### **3 Significant accounting policies**

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

#### **Foreign currency**

Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency rate of exchange ruling at the end of the reporting period. Gains and losses resulting from the translation of foreign currency transactions are recognized in current year profit or loss for the year. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

As of 31 December 2021, exchange rates for translation of foreign currency balances were as follows: US Dollar 1 = AZN 1.7000, Euro 1= AZN 1.9265, Pound Sterling 1 = AZN 2.2925 and Special Drawing Right 1 = AZN 2.3793 (31 December 2020: US Dollar 1 = AZN 1.7000, Euro 1= AZN 2.0890, Pound Sterling 1 = AZN 2.3021 and Special Drawing Right 1 = AZN 2.4485).

#### **Financial instruments - definitions and principles of recognition of financial instruments**

*Financial instrument* is any contract that gives rise to a financial asset of the Bank and a financial liability of another entity.

*Debt instrument* is an instrument that meets the definition of a financial obligation from the issuer's point of view, such as loans and fixed income securities.

*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. The best evidence of fair value is price in an active market.

*Transaction costs* are incremental costs that are directly attributable to the acquisition or issue of a financial instrument. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

*Amortised cost ("AC")* is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses. Accrued interest includes amortisation of any premium or discount to maturity amount at initial recognition using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium, are not presented separately and are included in the carrying values of related items in the statement of financial position.

*The effective interest method* is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date.

#### **Calculation of interest income and expense**

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

**Expected credit losses (“ECL”)** – the weighted average of credit losses with the respective risks of a default.

**12-month expected credit losses** – the portion of lifetime expected credit losses that represent the expected credit losses that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

**Lifetime expected credit losses** – the expected credit losses that result from all possible default events over the expected life of a financial instrument.

#### **Financial instruments – initial recognition**

Upon initial recognition, the Bank classifies its financial assets into the following categories: at amortised cost (AC), at fair value through other comprehensive income (FVOCI), and at fair value through profit or loss (FVTPL).

Financial assets at FVTPL are initially recorded at fair value. Financial assets at AC and at FVOCI are initially recorded at fair value adjusted for transaction costs.

Fair value at initial recognition is best evidenced by the transaction price. In circumstances where the fair value of a financial asset or liability at initial recognition is different from the transaction price, a gain or loss equal to the difference is immediately recognised in profit or loss if and only if the fair value measurement is evidenced by a quoted price in an active market for an identical asset or liability, or is based on a valuation technique that uses only data from observable markets. If the fair value measurement at initial recognition does not meet either of these conditions, then the difference is deferred and subsequently recognised as a gain or loss only to the extent it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability.

After the initial recognition, an ECL allowance is recognised for financial assets measured at AC and debt instruments measured at FVOCI.

#### **Financial assets – classification and subsequent measurement – measurement categories**

The classification and subsequent measurement of debt financial assets depends on: (i) the Bank’s business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

#### **Financial assets – classification and subsequent measurement – cash flow characteristics**

Where the business model is to hold assets to collect contractual cash flows or to hold contractual cash flows and sell, the Bank assesses whether the cash flows represent solely payments of principal and interest (“SPPI”). In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for credit risk, time value of money, other basic lending risks and profit margin.

The SPPI assessment is performed on initial recognition of an asset and it is not subsequently reassessed. Refer to Note 2 for critical judgements applied by the Bank in performing the SPPI test for its financial assets.

#### **Financial assets – reclassification**

Financial instruments are reclassified only when the business model for the portfolio changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model.

#### **Financial assets impairment – credit loss allowance for ECL**

The Bank measures, on a forward-looking basis, the ECL for financial instruments measured at AC and FVOCI and recognises credit loss allowance at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all information about past events, current conditions and forecasts of future conditions before the reporting date.

Debt instruments measured at AC are presented in the statement of financial position net of the allowance for ECL. For debt instruments at FVOCI, allowance for ECL is not recorded in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the revaluation reserve for debt securities at FVOCI. ECL and reversals for debt securities at FVOCI are recognised in profit or loss and other changes in carrying value are recognised in OCI.

**Central Bank of the Republic of Azerbaijan**

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

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The Bank applies a three stage model for impairment, based on changes in credit quality since initial recognition. A financial instrument that is not credit-impaired on initial recognition is classified in Stage 1. Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECL that results from default events possible within the next 12 months or until contractual maturity, if shorter ("12 Months ECL"). If the Bank identifies a significant increase in credit risk ("SICR") since initial recognition, the asset is transferred to Stage 2 and its ECL is measured based on ECL on a lifetime basis, that is, up until contractual maturity but considering expected prepayments, if any ("Lifetime ECL"). Refer to Note 32 for a description of how the Bank determines when a SICR has occurred. If the Bank determines that a financial asset is credit-impaired, the asset is transferred to Stage 3 and its ECL is measured as a Lifetime ECL. The Bank's definition of credit impaired assets and definition of default is explained in Note 32. Note 32 provides information about inputs, assumptions and estimation techniques used in measuring ECL, including an explanation of how the Bank incorporates forward-looking information in the ECL models.

**Financial assets – write-off**

Financial assets are written-off, in whole or in part, when the Bank exhausted all practical recovery efforts in accordance with legislation. The write-off represents a derecognition event.

**Financial assets – derecognition**

The Bank derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Bank has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

**Financial assets – modification**

The Bank modifies the contractual terms of the financial assets and assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: significant change in interest rate, credit enhancement that significantly affects the credit risk associated with the asset or a significant extension of a loan when the borrower is not in financial difficulties.

If the modified terms are substantially different, the rights to cash flows from the original asset expire and the Bank derecognises the original financial asset and recognises a new asset at its fair value. The date of renegotiation is considered to be the date of initial recognition for subsequent impairment calculation purposes, including determining whether a SICR has occurred. Any difference between the carrying amount of the original asset derecognised and fair value of the new substantially modified asset is recognised in profit or loss.

**Financial liabilities – measurement categories**

Other financial liabilities are classified at AC, except for financial liabilities at FVTPL (derivatives).

**Financial liabilities – derecognition**

The Bank shall remove a financial liability (or a part of a financial liability) from its statement of financial position when, and only when, it is extinguished – i.e when the obligation specified in the contract is discharged or cancelled or expires.

If the Bank purchases its own debt, it is removed from the statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from early retirement of debt.

**Derivative financial instruments**

Derivative financial instruments include swaps, futures and forwards.

Derivatives are initially recognized at fair value on the date when a derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative. Changes in the fair value of derivatives are recognized immediately in profit or loss.



**Central Bank of the Republic of Azerbaijan***Notes to the Financial Statements for the year ended 31 December 2021**(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

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**Cash and cash equivalents**

Cash and cash equivalents are short-term items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents consist of cash on hand in foreign currency and unrestricted balances on correspondent accounts including overnight deposits and deposits with a maturity of three months from origination as well as investments on money market funds. Cash and cash equivalents other than investments on money market funds are carried at amortized cost because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL. The investments on money market funds are required to be measured at FVTPL in accordance with IFRS 9 because the units give rise to cash flows that are not solely payments of principal and interest.

**Debt securities**

Based on the business model and the cash flow characteristics, the Bank classifies debt securities as carried at AC, FVOCI or FVTPL. Debt securities are carried at AC if they are held for collection of contractual cash flows and where those cash flows represent SPPI, and if they are not designated at FVTPL in order to significantly reduce an accounting mismatch.

Debt securities are carried at FVOCI if they are held for collection of contractual cash flows and for selling, where those cash flows represent SPPI, and if they are not designated at FVTPL. Interest income from these assets is calculated using the effective interest method and recognised in profit or loss. When the debt security is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from OCI to profit or loss.

Debt securities are carried at FVTPL if they do not meet the criteria for AC or FVOCI.

**Property and equipment**

Items of property and equipment are stated at historical cost less accumulated depreciation and impairment losses, where required.

Costs of minor repairs and day-to-day maintenance are expensed when incurred. Costs of replacing major parts or components of premises and equipment items are capitalized, and the replaced part is retired.

Gains and losses on disposals determined by comparing proceeds with carrying amount are recognized in profit or loss for the year (within other operating income or expenses).

**Depreciation**

Land and construction in progress are not depreciated. Depreciation on other items of property and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives. Depreciation of an asset begins when it is available for use. Estimated useful life is determined using the following annual depreciation rates:

	%
Buildings	3
Furniture and fixtures	20-25
Computer and communication equipment	25
Motor vehicles	15

**Intangible assets**

Bank's intangible assets have definite useful life and primarily include capitalized computer software and licenses.

Acquired intangible assets are stated at cost less accumulated amortization and impairment losses.

Amortization is charged to profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives range from 1 to 10 years.

**Investment property**

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in normal course of business, or for the use in production or supply of goods or services or for administrative purposes. Investment property is measured at fair value with any change recognized in profit or loss and included in "Other Assets".

## **Central Bank of the Republic of Azerbaijan**

*Notes to the Financial Statements for the year ended 31 December 2021*

*(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

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When the use of a property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

### **Money in circulation**

Money in circulation represents banknotes and coins issued by the Bank and in circulation in accordance with the Law and its function as a central bank. Banknotes and coins in circulation are recorded in the statement of financial position at their nominal value net of cash in the Bank's cash offices.

The costs of the production of notes and coins are expensed upon delivery by the suppliers to the Bank.

When notes and coins are returned to the Bank by the commercial banks they are removed from notes in circulation and depending on their condition or legal tender status, are held under the reserve funds of the Bank off-balance sheet.

### **Amounts due to government organisations and other organisations**

Amounts due to government organisations and other organisations are non-derivative liabilities and are carried at amortized cost.

### **Amounts due to credit institutions**

Amounts due to credit institutions are recorded when money or other assets are advanced to the Bank by counterparty banks. The non-derivative liability is carried at amortized cost. If the Bank purchases its own debt, the liability is removed from the statement of financial position.

### **Retirement and other benefit obligations**

The Bank does not have any pension arrangements in addition to the state pension system of Azerbaijan. In addition, the Bank has no post-retirement benefits or other significant compensation benefits requiring accrual. In accordance with the requirements of the Azerbaijan legislation, the Bank withholds amounts of pension contributions from employee salaries and pays them to the state pension fund. Upon retirement all retirement benefit payments are made by the state pension fund.

### **Charter fund and capital reserves**

The Bank's capital is comprised of its authorized paid-in charter fund and capital reserves.

### **Taxation**

The Bank is exempt from all taxes, except for taxes on employees' remuneration as a tax agent and social taxes, in accordance with the laws of the Republic of Azerbaijan.

### **Membership with the International Monetary Fund and other international financial institutions**

Based on the provision of Article 9 of the Law of the Republic of Azerbaijan on the Central Bank of the Republic of Azerbaijan, the Bank acts as an intermediary of the Government of the Republic of Azerbaijan in transactions related to the membership of the Republic of Azerbaijan in international financial organisations (e.g. IMF, World Bank), including payment of membership fees to such organisations.

The International Monetary Fund ("IMF") is an international organisation established to promote international monetary cooperation, exchange stability and orderly exchange arrangements; to foster economic growth and high levels of employment; and to provide temporary financial assistance to countries to help ease the balance of payments adjustments. In accordance with the presidential decree issued in 1992, the Bank acts as a depository agent in relations of the Republic of Azerbaijan with the IMF and the role of fiscal agent is performed by the Ministry of Finance of the Republic of Azerbaijan.

Quotas (capital subscriptions) are the primary source of IMF resources. The IMF receives its resources from its member countries. Each country's subscription (quota) is determined broadly on the basis of the economic size of the country and taking into account quotas of similar countries. A member's quota delineates basic aspects of its financial and organisational relationship with the IMF.

Membership fees payable to IMF are denominated in Special Drawing Rights ("SDR") and are revalued in AZN at the rate of exchange set by the IMF at year-end. Membership quota and securities issued by the Ministry of Finance of the Republic of Azerbaijan in respect of IMF quota are not presented in the statement of financial position as they do not represent the assets and liabilities of the Bank, but are disclosed in Note 5 to the financial statements.

**Central Bank of the Republic of Azerbaijan**

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

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General and special allocations received from the IMF to boost the liquidity of member countries are taken up by the Bank as an asset under SDR holdings with the IMF and on the other hand, as a liability to the Government of the Republic of Azerbaijan.

**Impairment of non-financial assets**

Non-financial assets are assessed at each reporting date for any indications of impairment. The recoverable amount of non financial assets is the greater of their fair value less costs to sell and value in use.

In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non financial assets are recognised in profit or loss and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss reversed is only reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

**Income and expense recognition**

Interest income and expense are recorded for all debt instruments on an accrual basis using the effective interest method. This method defers, as part of interest income or expense, all fees paid or received between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Loan origination fees, loan servicing fees and other fees that are considered to be integral to the overall profitability of a loan, together with the related transaction costs, are deferred and amortized to interest income over the estimated life of the financial instrument using the effective interest method.

Other fees, commissions and other income and expense items are recognized in profit or loss when the corresponding service is provided.

**New standards and interpretations not yet adopted**

A number of new standards and amendments to the standards are effective from 1 January 2022 and earlier application is permitted; however, the Bank has not early adopted the new or amended standards in preparing these financial statements.

The new and amended standards are not expected to have a significant impact on the Bank's financial statements.

**New amendments to standards effective from 1 January 2021**

As at 31 December 2021, the Bank has debt securities measured at FVOCI in the amount of AZN 228,865 with coupon rates that are linked to USD LIBOR. All these securities will be matured until the end of April 2023. The Bank does not expect any significant impact on its financial statements from the IBOR reform.

**Central Bank of the Republic of Azerbaijan***Notes to the Financial Statements for the year ended 31 December 2021**(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

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**4 Cash and cash equivalents**

The table below discloses the credit quality of cash and cash equivalents balances based on credit risk grades at 31 December 2021 and 2020.

	<b>31 December 2021</b>	<b>31 December 2020</b>
Cash on hand	1,973,210	2,627,388
<b>Nostro accounts with non-resident banks</b>		
- Rated excellent	2,896,749	1,998,520
- Rated good	250,699	49,882
<b>Total nostro accounts with non-resident banks</b>	<b>3,147,448</b>	<b>2,048,402</b>
<b>Cash equivalents</b>		
Short-term deposits with non-resident banks (rated excellent)	952,248	88,530
Investments in money market funds (rated excellent)	766,085	850,953
<b>Total cash equivalents</b>	<b>1,718,333</b>	<b>939,483</b>
<b>Total cash and cash equivalents</b>	<b>6,838,991</b>	<b>5,615,273</b>

Investments in money market funds are measured at FVTPL.

Nostro accounts and short-term deposits with non-resident banks are in Stage 1.

As at 31 December 2021 the Bank has 8 banks (2020: 2 banks), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2021 is AZN 4,687,173 thousand (2020: AZN 1,918,871 thousand).

Refer to Note 32 for the description of the Bank's credit risk grading system.

**Central Bank of the Republic of Azerbaijan**

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**5 Balances with the International Monetary Fund**

	31 December 2021	31 December 2020
<b>ASSETS</b>		
Special Drawing Rights (SDR) holdings	1,258,160	375,543
<b>Total assets with IMF</b>	<b>1,258,160</b>	<b>375,543</b>
<b>LIABILITIES</b>		
Current accounts	2,474	2,474
SDR allocations	1,258,657	376,031
<b>Total liabilities with IMF</b>	<b>1,261,131</b>	<b>378,505</b>

**SDR holdings**

SDR holdings represent the current account with the IMF used for borrowings and settlements with the IMF. Interest accrued in respect of SDR holdings is calculated using the rates set by the IMF on weekly basis in accordance with short-term market rates in major money markets.

**Current accounts**

The Bank maintains two separate accounts with the IMF for special purposes, account No. 1 and No. 2. Account No. 1 is used for paying commissions for transactions with the IMF, whereas account No.2 is used for covering expenses of IMF representatives during their visit to member countries.

**SDR allocation**

SDR allocation is an unconditional distribution of SDRs to member countries by the IMF. A general SDR allocation became effective since 28 August 2009. The allocation is designed to provide liquidity to the global economic system by supplementing the IMF member countries' foreign exchange reserves. General SDR allocation is determined proportionate to existing IMF quotas for each member country.

Additionally, on 10 August 2009, the Fourth Amendment to the IMF Articles of Agreement providing for a special one-time SDR allocation came into force to boost global liquidity. According to the Amendment, the special allocation was made to IMF members, including the Republic of Azerbaijan on 9 September 2009 in amount of SDR 34.3 million resulting total SDR allocation to be SDR 119.3 million for Azerbaijan.

To support the global economy, especially the economies of countries affected by the pandemic, the IMF has distributed the next general SDR to member countries in 2021. The general SDR allocation was made to the member countries in proportion to their existing quotas in the IMF and according to the current quota of Azerbaijan, an additional SDR 375.4 million was allocated.

Members and prescribed holders may use their SDR holdings to conduct transactions with the IMF. The Bank treats the allocation as foreign exchange liability.

**IMF Quota and securities held in custody in respect of IMF Quota**

The IMF Quota, in the amount of SDR 391.7 million (AZN 931,972 thousand and AZN 959,077 thousand as at 31 December 2021 and 2020 respectively) has remained unchanged since 25 February 2016 and represents the membership subscription of the Republic of Azerbaijan with the IMF. Securities were issued by the Government of the Republic of Azerbaijan to guarantee these amounts. These securities are held by the Bank for which IMF is acting as the beneficiary.

**Central Bank of the Republic of Azerbaijan**

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**6 Derivative financial instruments**

The fair value of derivative financial instruments as at 31 December 2021 and 2020 are as follows:

	Notional amount	31 December 2021		Notional amount	31 December 2020	
		Fair value			Fair value	
		Assets	Liabilities		Assets	Liabilities
Foreign exchange contracts	592,024	-	(862)	549,082	-	(3,530)
Futures contracts	43,572	345	-	18,941	-	(26)
SWAP contracts	338,019	2,489	-	31,366	449	-
<b>Total derivative financial instruments</b>	<b>973,615</b>	<b>2,834</b>	<b>(862)</b>	<b>599,389</b>	<b>449</b>	<b>(3,556)</b>

**Foreign currency contracts**

The table below summarizes, by major currencies, the contractual amounts of forward (including forward made on the basis of mutual settlement) exchange contracts outstanding, with details of the weighted average contractual exchange rates and remaining periods to maturity. Foreign currency amounts presented below are translated at rates ruling at the reporting date.

	Notional		Weighted average contractual exchange rates	
	31 December 2021	31 December 2020	31 December 2021	31 December 2020
	<b>Sell USD buy AZN</b> Less than 5 months	7,178	16,759	1.7946
<b>Buy USD sell EUR</b> Less than 3 months	286,083	280,801	1.1375	1.2239
<b>Sell USD buy EUR</b> Less than 3 months	114,084	104,545	0.8793	0.8173
<b>Buy USD sell GBP</b> Less than 3 months	70,451	55,256	1.3544	1.3671
<b>Sell USD buy GBP</b> Less than 3 months	31,619	23,508	0.7383	0.7316
<b>Buy USD sell CAD</b> Less than 3 months	40,830	37,302	0.7917	0.7850
<b>Sell USD buy CAD</b> Less than 3 months	10,687	7,652	1.2632	1.2740
<b>Buy USD sell other currencies</b> Less than 3 months	27,768	15,795	0.6475	0.5575
<b>Sell USD buy other currencies</b> Less than 3 months	3,324	7,464	4.2356	3.8463

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**7 Debt securities**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Debt securities mandatorily measured at FVTPL	953,367	958,818
Debt securities at FVOCI	6,919,668	8,124,710
Debt securities at AC	9,489,241	9,496,146
<b>Total debt securities</b>	<b>17,362,276</b>	<b>18,579,674</b>

The table below discloses debt securities at 31 December 2021 and 2020 by measurement categories and classes:

<b>31 December 2021</b>	<b>Debt securities mandatorily measured at FVTPL</b>	<b>Debt securities at FVOCI</b>	<b>Debt securities at AC</b>	<b>Total</b>
Agency	188,191	2,560,825	-	2,749,016
Supranational	56,911	885,660	-	942,571
Treasury	536,811	1,823,610	-	2,360,421
Local Authority	43,197	425,408	-	468,605
Corporate	83,621	786,204	-	869,825
Sovereign	2,831	93,466	-	96,297
Covered	41,805	-	-	41,805
Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan	-	344,495	-	344,495
JSCO Aqrarkredit	-	-	9,482,143	9,482,143
Ministry of Finance of the Republic of Azerbaijan	-	-	7,098	7,098
<b>Total debt securities</b>	<b>953,367</b>	<b>6,919,668</b>	<b>9,489,241</b>	<b>17,362,276</b>

<b>31 December 2020</b>	<b>Debt securities mandatorily measured at FVTPL</b>	<b>Debt securities at FVOCI</b>	<b>Debt securities at AC</b>	<b>Total</b>
Agency	176,687	3,588,626	-	3,765,313
Supranational	57,875	1,365,851	-	1,423,726
Treasury	580,700	1,287,564	-	1,868,264
Local Authority	34,448	851,370	-	885,818
Corporate	80,199	309,549	-	389,748
Sovereign	4,138	348,727	-	352,865
Covered	24,771	-	-	24,771
Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan	-	373,023	-	373,023
JSCO Aqrarkredit	-	-	9,482,143	9,482,143
Ministry of Finance of the Republic of Azerbaijan	-	-	14,003	14,003
<b>Total debt securities</b>	<b>958,818</b>	<b>8,124,710</b>	<b>9,496,146</b>	<b>18,579,674</b>

Included in Debt Securities at AC were securities of Joint-Stock Credit Organisation Aqrarkredit (Aqrarkredit JSCO) purchased by the Bank during 2015 with the nominal amount of AZN 2,500,000 thousand and, additionally, during 2016 AZN 7,500,000 thousand, bearing interest rate of 0.15% and maturing in 2045 (in total AZN 10,000,000 thousand). In 2017 Aqrarkredit JSCO repurchased the securities in the amount of AZN 517,896 thousand from the Bank.

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As at 31 December 2021, the outstanding balance of the securities in the portfolio of the Bank was AZN 9,482,104 thousand. Repayment of these securities is guaranteed by the Government of Azerbaijan. These securities were purchased based on Decrees of the President of Azerbaijan Republic № 570, dated 15 July 2015 on "Actions for improvement of International Bank of Azerbaijan OJSC's condition to prepare for the privatization of shares owned by government" and № 575 dated 07 August 2015 on "Approval of issue, volume, maturity and payment conditions of securities with government guarantee issued by Aqrarkredit JSCO", respectively. Refer to Note 36 for fair value disclosures.

**(a) Debt securities at FVTPL**

Debt securities mandatorily classified as at FVTPL by the Bank represent securities held for trading. Debt securities at FVTPL are carried at fair value, which also reflects any credit risk related write-downs and best represents the Bank's maximum exposure to credit risk. Debt securities at FVTPL have excellent credit risk grade.

**(b) Debt securities at FVOCI**

The table below contains an analysis of the credit risk exposure of debt securities measured at FVOCI at 31 December 2021 and 2020, for which an ECL allowance is recognised, based on credit risk grades. Refer to Note 32 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to debt securities at FVOCI:

	2021		2020	
	Stage 1	Total	Stage 1	Total
<b>Debt securities at FVOCI</b>				
Rated excellent	6,575,173	6,575,173	7,751,687	7,751,687
Rated good	344,495	344,495	373,023	373,023
<b>Total debt securities at FVOCI</b>	<b>6,919,668</b>	<b>6,919,668</b>	<b>8,124,710</b>	<b>8,124,710</b>
Loss allowance	(608)	(608)	(698)	(698)
<b>Total carrying value (fair value)</b>	<b>6,919,668</b>	<b>6,919,668</b>	<b>8,124,710</b>	<b>8,124,710</b>

Movements in the loss allowance for debt securities at FVOCI were as follows:

	2021		2020	
	Stage 1	Total	Stage 1	Total
<b>Debt securities at FVOCI</b>				
Balance at 1 January	698	698	451	451
Net remeasurement of loss allowance	(365)	(365)	(246)	(246)
New financial assets originated or purchased	275	275	493	493
<b>Balance at 31 December</b>	<b>608</b>	<b>608</b>	<b>698</b>	<b>698</b>

Movements in the gross carrying amounts of debt securities at FVOCI that contributed to changes in ECL were as follows:

	2021		2020	
	Stage 1	Total	Stage 1	Total
<b>Debt securities at FVOCI</b>				
Balance at 1 January	8,124,710	8,124,710	7,050,574	7,050,574
Debt securities repaid	(5,070,366)	(5,070,366)	(3,978,092)	(3,978,092)
Debt securities purchased	3,865,324	3,865,324	5,052,228	5,052,228
<b>Balance at 31 December</b>	<b>6,919,668</b>	<b>6,919,668</b>	<b>8,124,710</b>	<b>8,124,710</b>



**Central Bank of the Republic of Azerbaijan**

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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

**(c) Debt securities at AC**

The following table contains an analysis of debt securities at AC by credit quality at 31 December 2021 and 2020 based on credit risk grades and discloses the balances by stages for the purpose of ECL measurement. Refer to Note 32 for the description of credit risk grading system used by the Bank and the approach to ECL measurement, including the definition of default and SICR as applicable to debt securities at AC. The carrying amount of debt securities at AC at 31 December 2021 and 2020 below also represents the Bank's maximum exposure to credit risk on these assets:

	2021		2020	
	Stage 1	Total	Stage 1	Total
<b>Debt securities at AC</b>				
Rated good	9,489,241	9,489,241	9,496,146	9,496,146
<b>Total debt securities at AC</b>	<b>9,489,241</b>	<b>9,489,241</b>	<b>9,496,146</b>	<b>9,496,146</b>

These securities are issued in local currency, Azerbaijani manats, and repayment is guaranteed by the Government of Azerbaijan. Debt securities at AC are included in Stage 1 and assigned with good credit risk grade.

**8 Loans to banks**

	31 December 2021	31 December 2020
Loans to banks, gross	729,024	778,958
Loss allowance	(372,743)	(379,550)
<b>Loans to banks, net of loss allowance</b>	<b>356,281</b>	<b>399,408</b>

**Concentration of loans to banks**

As at 31 December 2021 and 2020, the Bank had no banks, whose balance exceed 10% of equity.

Gross carrying amount and loss allowance amount for loans to banks by classes at 31 December 2021 and 31 December 2020 are disclosed in the table below:

	31 December 2021			31 December 2020		
	Gross carrying amount	Loss allowance	Carrying amount	Gross carrying amount	Loss allowance	Carrying amount
Refinancing loans	729,024	(372,743)	356,281	778,958	(379,550)	399,408
<b>Total</b>	<b>729,024</b>	<b>(372,743)</b>	<b>356,281</b>	<b>778,958</b>	<b>(379,550)</b>	<b>399,408</b>

More detailed explanation of classes of loans to legal entities is provided below:

- Refinancing loans - are provided as part of implementing monetary policy of the Central Bank;
- Lender of last resort loans - In case of short-term solvency and liquidity gap of the banks, the Central Bank may grant lender of last resort loans to the banks for a period not exceeding 6 (six) months.

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The following tables disclose the changes in the loss allowance for loans to banks between the beginning and the end of the reporting period:

	2021				2020			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
<b>Refinancing loans</b>								
Balance at 1 January	2,317	11,597	365,636	379,550	22	12,378	426,138	438,538
Transfer to Stage 3	-	-	-	-	-	(4,884)	4,884	-
Net remeasurement of loss allowance	291	(9,178)	(9,458)	(18,345)	(22)	4,103	(22,135)	(18,054)
New financial assets originated or purchased	-	-	-	-	2,317	-	-	2,317
Write-offs	-	-	-	-	-	-	(55,998)	(55,998)
Unwinding of discount on present value of ECLs	-	-	11,538	11,538	-	-	12,747	12,747
<b>Balance at 31 December</b>	<b>2,608</b>	<b>2,419</b>	<b>367,716</b>	<b>372,743</b>	<b>2,317</b>	<b>11,597</b>	<b>365,636</b>	<b>379,550</b>

	2021				2020			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
<b>Lender of last resort loans</b>								
Balance at 1 January	-	-	-	-	-	-	15,861	15,861
Net remeasurement of loss allowance	-	-	-	-	-	-	1,146	1,146
New financial assets originated or purchased	-	-	-	-	-	-	-	-
Write-offs	-	-	-	-	-	-	(17,007)	(17,007)
Unwinding of discount on present value of ECLs	-	-	-	-	-	-	-	-
<b>Balance at 31 December</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

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Changes in the gross carrying amount of financial instruments during the period that contributed to changes in loss allowance were as follows:

	2021				2020			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
<b>Refinancing loans</b>								
Balance at 1 January	292,605	74,415	411,938	778,958	208,018	49,388	451,096	708,502
Transfer to Stage 2	-	-	-	-	(25,702)	25,702	-	-
Transfer to Stage 3	-	-	-	-	(25,727)	(5,502)	31,229	-
Repaid during the year	(43,708)	(11,105)	(6,659)	(61,472)	(8,240)	(3,082)	(27,136)	(38,458)
Issued during the year	-	-	-	-	144,256	7,909	-	152,165
Write-offs	-	-	-	-	-	-	(55,998)	(55,998)
Unwinding of discount on present value of ECLs	-	-	11,538	11,538	-	-	12,747	12,747
<b>Balance at 31 December</b>	<b>248,897</b>	<b>63,310</b>	<b>416,817</b>	<b>729,024</b>	<b>292,605</b>	<b>74,415</b>	<b>411,938</b>	<b>778,958</b>

	2021				2020			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
<b>Lender of last resort loans</b>								
Balance at 1 January	-	-	-	-	-	-	16,868	16,868
Repaid during the year	-	-	-	-	-	-	-	-
Issued during the year	-	-	-	-	-	-	139	139
Write-offs	-	-	-	-	-	-	(17,007)	(17,007)
Unwinding of discount on present value of ECLs	-	-	-	-	-	-	-	-
<b>Balance at 31 December</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

The credit loss allowance for loans to banks recognised in the period is impacted by a variety of factors, details of ECL measurement are provided in Note 32.

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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The credit quality of loans to banks carried at amortised cost is as follows at 31 December 2021 and 2020:

	2021				2020			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
<b>Refinancing loans</b>								
- Good	132,874	27,000	-	159,874	177,166	33,611	-	210,777
- Satisfactory	116,022	-	-	116,022	115,439	-	-	115,439
- Special monitoring	-	36,311	-	36,311	-	40,804	-	40,804
- Default	-	-	416,817	416,817	-	-	411,938	411,938
<b>Gross carrying amount</b>	<b>248,896</b>	<b>63,311</b>	<b>416,817</b>	<b>729,024</b>	<b>292,605</b>	<b>74,415</b>	<b>411,938</b>	<b>778,958</b>
Loss allowance	(2,608)	(2,419)	(367,716)	(372,743)	(2,317)	(11,597)	(365,636)	(379,550)
<b>Carrying amount</b>	<b>246,288</b>	<b>60,892</b>	<b>49,101</b>	<b>356,281</b>	<b>290,288</b>	<b>62,818</b>	<b>46,302</b>	<b>399,408</b>

For description of the credit risk grading used in the tables above refer to Note 32.

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The Bank's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Bank since the prior period. Description of collateral held for loans to banks is as follows at 31 December 2021:

	<u>Refinancing loans</u>	<u>Total</u>
Loans collateralised by:		
- government guaranteed	159,874	159,874
- commercial real estate	60,881	60,881
Carrying value of loans to banks secured	<u>220,755</u>	<u>220,755</u>
Unsecured exposures	<u>135,526</u>	<u>135,526</u>
<b>Total carrying value of loans to banks</b>	<b><u>356,281</u></b>	<b><u>356,281</u></b>

Information about collateral for loans to banks is as follows at 31 December 2020:

	<u>Refinancing loans</u>	<u>Total</u>
Loans collateralised by:		
- government guaranteed	210,777	210,777
- residential real estate	247	247
- commercial real estate	54,166	54,166
Carrying value of loans to banks secured	<u>265,190</u>	<u>265,190</u>
Unsecured exposures	<u>134,218</u>	<u>134,218</u>
<b>Total carrying value of loans to banks</b>	<b><u>399,408</u></b>	<b><u>399,408</u></b>

Information about collateral for loans to banks that are credit-impaired is as follows at 31 December 2021:

	<u>Refinancing loans</u>	<u>Total</u>
Loans collateralised by:		
- commercial real estate	26,989	26,989
Carrying value of loans to banks secured	<u>26,989</u>	<u>26,989</u>
Unsecured exposures	<u>22,112</u>	<u>22,112</u>
<b>Total carrying value of loans to banks</b>	<b><u>49,101</u></b>	<b><u>49,101</u></b>

Information about collateral for loans to banks that are credit-impaired is as follows at 31 December 2020:

	<u>Refinancing loans</u>	<u>Total</u>
Loans collateralised by:		
- residential real estate	247	247
- commercial real estate	24,959	24,959
Carrying value of loans to banks secured	<u>25,206</u>	<u>25,206</u>
Unsecured exposures	<u>21,096</u>	<u>21,096</u>
<b>Total carrying value of loans to banks</b>	<b><u>46,302</u></b>	<b><u>46,302</u></b>

All loans of the Bank other than unsecured loans are over-collateralized before discounting for time to sell and costs to sell.

### **Repossessed collateral**

During the year ended 31 December 2021, the Bank obtained certain assets by taking possession of collateral for loans to banks comprising real estate with a net carrying amount of AZN 1,242 thousand (as at 31 December 2020: AZN 41,640 thousand). The Bank's policy is to sell these assets as soon as it is practicable.

### **9 Loans to non-bank credit organisations**

Loans to non-bank credit organisations include low interest rate loans provided to non-bank credit organisations under the state guarantee as per the decree "On the additional measures related to the solution of problem loans of individuals in the Republic of Azerbaijan" signed by the President of the Republic of Azerbaijan on 28 February 2019.

### **10 Loans to Deposit Insurance Fund**

Loans to Deposit Insurance Fund include low interest rate loans provided to Azerbaijan Deposit Insurance Fund under the state guarantee to compensate money deposited by individuals in banks whose licenses have been revoked.

During 2021 and 2020, the Bank issued loans to Azerbaijan Deposit Insurance Fund in the amount of AZN 60,000 thousand and AZN 280,000 thousand, respectively with annual interest rate of 0.15%. During 2021, the principal amount of 40,000 thousand AZN was repaid. These loans were recorded at fair value on initial recognition calculated using the market interest rate of 6.25% (in 2020: 6.5%) See Note 28. As at 31 December 2021, the amortized carrying amount of these loans was AZN 236,600 thousand (as at 31 December 2020: AZN 207,222 thousand).

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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

**11 Property and equipment**

The following table provides information on the movement of property and equipment for the year ended at 31 December 2021:

	<b>Land</b>	<b>Buildings</b>	<b>Furniture and fixtures</b>	<b>Computers and communication equipment</b>	<b>Motor vehicles</b>	<b>Construction in progress</b>	<b>Total</b>
<b>Cost</b>							
<b>Balance at 1 January 2021</b>	15,976	51,546	64,880	39,121	3,289	7,123	181,935
Additions	-	-	892	857	73	-	1,822
Disposals	-	(20)	-	-	(109)	-	(129)
Transfers	-	-	-	-	-	-	-
<b>Balance at 31 December 2021</b>	<b>15,976</b>	<b>51,526</b>	<b>65,772</b>	<b>39,978</b>	<b>3,253</b>	<b>7,123</b>	<b>183,628</b>
<b>Depreciation</b>							
<b>Balance at 1 January 2021</b>	-	(21,451)	(50,878)	(20,682)	(2,463)	-	(95,474)
Depreciation for the year	-	(1,546)	(3,407)	(6,738)	(213)	-	(11,904)
Disposals	-	2	-	-	109	-	111
<b>Balance at 31 December 2021</b>	<b>-</b>	<b>(22,995)</b>	<b>(54,285)</b>	<b>(27,420)</b>	<b>(2,567)</b>	<b>-</b>	<b>(107,267)</b>
Carrying amount							
<b>At 31 December 2021</b>	<b>15,976</b>	<b>28,531</b>	<b>11,487</b>	<b>12,558</b>	<b>686</b>	<b>7,123</b>	<b>76,361</b>

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The following table provides information on the movement of property and equipment for the year ended at 31 December 2020:

	Land	Buildings	Furniture and fixtures	Computers and communication equipment	Motor vehicles	Construction in progress	Total
<b>Cost</b>							
<b>Balance at 1 January 2020</b>	15,976	51,831	56,712	31,796	3,301	7,123	166,739
Additions	-	-	8,194	7,321	-	-	15,515
Disposals	-	(285)	(22)	-	(12)	-	(319)
Transfers	-	-	(4)	4	-	-	-
<b>Balance at 31 December 2020</b>	<b>15,976</b>	<b>51,546</b>	<b>64,880</b>	<b>39,121</b>	<b>3,289</b>	<b>7,123</b>	<b>181,935</b>
<b>Depreciation</b>							
<b>Balance at 1 January 2020</b>	-	(19,910)	(48,969)	(15,104)	(2,216)	-	(86,199)
Depreciation for the year	-	(1,555)	(1,933)	(5,576)	(259)	-	(9,323)
Disposals	-	14	22	-	12	-	48
Transfers	-	-	2	(2)	-	-	-
<b>Balance at 31 December 2020</b>	<b>-</b>	<b>(21,451)</b>	<b>(50,878)</b>	<b>(20,682)</b>	<b>(2,463)</b>	<b>-</b>	<b>(95,474)</b>
Carrying amount							
<b>At 31 December 2020</b>	<b>15,976</b>	<b>30,095</b>	<b>14,002</b>	<b>18,439</b>	<b>826</b>	<b>7,123</b>	<b>86,461</b>



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**12 Intangible assets**

The following table provides information on the movement of intangible assets for the year ended at 31 December 2021:

	<b>Total intangible assets</b>
<b>Cost</b>	
Balance at 1 January 2021	124,468
Additions	11,301
Disposals	-
<b>Balance at 31 December 2021</b>	<b>135,769</b>
<b>Amortization</b>	
Balance at 1 January 2021	(50,941)
Amortization for the year	(14,610)
Disposals	-
<b>Balance at 31 December 2021</b>	<b>(65,551)</b>
Carrying amount	
<b>At 31 December 2020</b>	<b>70,218</b>

The following table provides information on the movement of intangible assets for the year ended at 31 December 2020:

	<b>Total intangible assets</b>
<b>Cost</b>	
Balance at 1 January 2020	94,860
Additions	29,608
Disposals	-
<b>Balance at 31 December 2020</b>	<b>124,468</b>
<b>Amortization</b>	
Balance at 1 January 2020	(40,464)
Amortization for the year	(10,477)
Disposals	-
<b>Balance at 31 December 2020</b>	<b>(50,941)</b>
Carrying amount	
<b>At 31 December 2020</b>	<b>73,527</b>

**13 Other financial assets**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Receivables from trade securities disposed	1,037	48,617
Amounts in the course of settlement	597	239
Loans to employees	550	579
Loss allowance	(49)	(65)
	<b>2,135</b>	<b>49,370</b>

Other financial assets are included in Stage 1 and assigned with good credit risk grade.

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	<b>31 December 2021</b>	<b>31 December 2020</b>
Prepayments to suppliers	85,495	24,344
Amount to be capitalized	50,600	-
Investment property	4,400	4,400
Reposessed collateral	45,705	44,464
Other non-financial assets	498	505
	<b>186,698</b>	<b>73,713</b>

**15 Money in circulation**

Money issued in circulation represents the amount of national currency of the Republic of Azerbaijan issued by the Bank. This comprises the AZN issued into circulation since 1 January, 2006, and old Azerbaijani Manats ("AZM") issued into circulation since the introduction of the national currency in 1992 and currently withdrawn from the circulation and commemorative coins.. The Azerbaijani Manat was denominated on 1 January 2006 and, starting from that date, AZN 5,000 is equal to AZN 1.

During the year ended 31 December 2021 the Bank accepted new banknotes and coins amounting to AZN 507,566 thousand from printing and minting companies (2020: AZN 3,378,007 thousand).

	<b>31 December 2021</b>	<b>31 December 2020</b>
Balance at the beginning of the year	11,839,664	10,405,513
Net amount of banknotes and coins put into circulation	470,354	1,434,151
<b>Balance at the end of the year</b>	<b>12,310,018</b>	<b>11,839,664</b>

**16 Short-term deposits of resident banks**

On 31 December 2021, the amount of deposits of resident banks was nil. All short-term deposits placed with the Bank by resident banks matured during 2021 and no new deposits were obtained during the year.

During 2020, the Bank obtained deposit in the amount of AZN 2,465,000 out of auction from IBAR with the annual interest rate of 3.5% (from June 2021 agreed to be 3.0%). The principal amount and the interest expenses associated with this deposit are recorded at fair value on initial recognition calculated by applying the Bank's corridor floor rate of 5.75%.

**17 Amounts due to government organisations**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Amounts due to the Central Treasury of the Republic of Azerbaijan	2,427,985	3,208,595
Amounts due to State Oil Fund of the Republic of Azerbaijan and Azerbaijan Deposit Insurance Fund	1,536,423	1,532,953
Other current/demand accounts	40,229	179,770
	<b>4,004,637</b>	<b>4,921,318</b>

Interest rate, currency and maturity analysis of amounts due to government organisations are disclosed in Note 32.

**18 Amounts due to credit institutions**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Current accounts	7,266,612	3,055,426
Mandatory reserves	173,392	149,527
	<b>7,440,004</b>	<b>3,204,953</b>

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**19 Amounts due to other organisations**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Public organisations	6,933	6,531
Other financial institutions	4,477	2,535
	<b>11,410</b>	<b>9,066</b>

**20 Debt securities in issue**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Short-term notes	199,402	648,213
	<b>199,402</b>	<b>648,213</b>

**21 Amounts due to international financial institutions**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Borrowings from International Development Association (IDA)	10	528
Amounts due to other international financial institutions	1,015	877
	<b>1,025</b>	<b>1,405</b>

**22 Other financial liabilities**

	<b>31 December 2021</b>	<b>31 December 2020</b>
Amounts payable for trading securities purchased	7,459	137,092
Amounts in the course of settlement	3,402	2,093
Other financial liabilities	14	3,074
	<b>10,875</b>	<b>142,259</b>

**23 Charter fund and reserves**

The Bank capital consists of its charter fund and capital reserves. The Charter fund of the Bank is AZN 500,000 thousand. The Bank's capital reserves shall not fall below its charter fund. At the end of the reporting year, Bank's capital reserves were AZN 526,968 thousand.

**24 Net interest income**

	<b>2021</b>	<b>2020</b>
<b>Interest income calculated using the effective interest method</b>		
Debt securities at FVOCI	84,421	117,994
Amortisation of loss on initial recognition of financial assets	15,791	2,962
Debt securities at AC	14,043	14,060
Loans to banks	4,982	6,892
Placements with non-resident banks	1,016	8,749
Loans to Deposit Insurance Fund	491	107
SDR holdings with the IMF	310	1,078
Other assets	32	39
	<b>121,086</b>	<b>151,881</b>

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**Other interest income**

Debt securities at FVTPL	10,052	15,690
Investments in money market funds	89	1,680
	<b>10,141</b>	<b>17,370</b>

**Interest expense**

Deposits of resident banks	76,224	111,973
Amortisation of gain on initial recognition of financial liabilities	59,934	-
Debt securities in issue	29,964	35,915
Liabilities on transactions with the IMF	332	1,131
Amounts due to international financial institutions	2	7
Amounts due to State Oil Fund of the Republic of Azerbaijan and Azerbaijan Deposit Insurance Fund	1	101
	<b>166,457</b>	<b>149,127</b>
	<b>(35,230)</b>	<b>20,124</b>

**25 Fee and commission income**

	<b>2021</b>	<b>2020</b>
Cash withdrawal	11,443	3,200
Settlement	9,045	6,894
Other	-	157
	<b>20,488</b>	<b>10,251</b>

**26 Fee and commission expense**

	<b>2021</b>	<b>2020</b>
Securities operations (management and custodian)	1,920	1,824
Service fee	1,830	1,615
Settlement	60	83
Cash withdrawal	-	2,963
Other	25	16
	<b>3,835</b>	<b>6,501</b>

**27 Gain on initial recognition of financial liabilities**

During 2020, the Bank obtained deposits from International Bank of Azerbaijan placed out of auction with an annual interest rate of 3.5%. These deposits were recorded at fair value on initial recognition calculated by applying the Bank's corridor floor rate of 5.75%. See Note 16. Therefore, the difference of AZN 52,447 thousand between the nominal value and fair value at the date of initial recognition was recognised as a gain. In connection with the change in the interest rate on the deposit in June 2021, modification gain of AZN 7,487 thousand was recognized and these amounts were fully amortized until maturity.

**28 Loss on initial recognition of financial assets**

During 2021 and 2020, loans were issued to Azerbaijan Deposit Insurance Fund with an annual interest rate of 0.15%, in order to return the protected deposits of individuals in banks whose licences have been revoked, in accordance with the requirements of the legislation. These loans were recorded at fair value on initial recognition calculated by applying the Bank's refinancing rates of 6.25% and 6.50%, respectively. See Note 10. Therefore, the difference of AZN 6,415 thousand and AZN 75,742 thousand between the nominal value and fair value at the date of initial recognition was recognised as a loss during 2021 and 2020, respectively and these amounts will be fully recovered till the end of the loan period.

**Central Bank of the Republic of Azerbaijan***Notes to the Financial Statements for the year ended 31 December 2021**(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)***29 Net losses/(gains) from foreign exchange translation**

During 2021 the excess of negative unrealized exchange rate differences which arose during daily revaluation of balances in foreign currency over positive exchange rate differences constituted AZN 60,298 thousand as a loss (2020: AZN 66,044 thousand as a gain).

**30 Recovery of impairment loss**

	<b>2021</b>	<b>2020</b>
Loans to banks	18,345	14,591
Other financial assets	16	(216)
	<b>18,361</b>	<b>14,375</b>

**31 Administrative and other operating expenses**

	<b>2021</b>	<b>2020</b>
Staff costs	22,103	21,217
Amortisation of software and other intangible assets	14,610	10,477
Depreciation of premises and equipment	11,904	9,323
Software maintenance	8,703	8,302
Banknotes and coin production	8,116	31,207
Contributions to Social Security Pension Fund	4,785	4,658
Security	1,854	1,864
Social	1,084	1,049
Repair and maintenance	1,057	1,223
Communication	1,054	913
Insurance	832	101
Office supplies	722	734
Heating and lighting	630	578
Contributions to Mandatory Health Insurance	428	-
Representation	208	102
Business travel	166	114
Audit	138	327
Literature, printing and membership fee	135	147
Utilities	56	48
Donations to Armed Forces Assistance Fund and the Coronavirus Response Fund of the Republic of Azerbaijan	-	1,500
Consultancy (under contract with "Rotshchild & Cie" Bank)	-	834
Other	988	1,511
	<b>79,573</b>	<b>96,229</b>

## **32 Risk management**

Bank's risks are classified in the following four categories:

- *Strategic (policy) risks* – are the risks related to the monetary policy, financial stability, and other strategic issues arising out of mandate. Strategic (policy) Risk Management is implemented by Bank's Management Board, Monetary Policy Committee and Financial Stability Committee;
- *Financial risks* – is targeted at the identification, management of credit, market and liquidity risks. Financial Risk Management is performed by Management Board of the Bank, Investment Committee, Foreign Exchange Reserves Management Department in accordance with relevant rules and procedures. Risk management policy and procedures are regularly reviewed considering the changes in the market condition, offered products and services and innovations in the advanced practice;
- *Operational risks* – are the risks arising out of the intentional or careless behavior of employees of Bank's units and Bank's project team, non-adequacy of the internal processes, deficiency in the technical equipment, as well as software and technical platforms of the information system, and external events. In accordance with the principles of the Basel Committee on Corporate Management Department, it is carried out on the basis of 3 lines of defense.

The first line of defense consists of the Bank's all structural units of the model, the second and the third lines include the Corporate Management Department and the Internal Audit Department, respectively. Functions of the Bank's corporate management department include preparation, development, communication and training of the policy and methodology documents for the Bank's Operational Risks Management (ORM) system and relevant supporting systems; coordination, facilitation, monitoring and reporting of the ORM process and as well as the preparation of risk profile of the Bank's consolidated operations.

- *Reputational risks* – are the risks arising out of the personal life, behavior and communication of Bank's high-ranking officials (Members of the Management Board and General Directors), as well as discrepancy between the Bank's goals and activities and the public opinion. Reputational losses in the result of inefficient management of strategic (policy), financial, operational risks are not considered as reputational risks. Those losses are considered as one of the risk impact categories within the strategic (policy), financial, operational risks management. Bank's reputational risks are managed by the Management Board, General Directors and International Cooperation and Communications Department.

### **Financial risk management policies and procedures**

Risk management of the Bank is a critical component of its banking activities. Risk is inherent in the Bank's activities but it is managed through a process of ongoing identification, measurement and daily monitoring, subject to risk limits and other controls.

The Management Board is ultimately responsible for identifying and controlling risks; however, there are separate business units responsible for managing and monitoring the various risks:

*Management Board.* The Management Board is ultimately responsible for controlling of risk management system. The Management Board is responsible for the overall risk management approach, risk tolerance levels and for approving the main principles of risk management.

*Investment Committee.* The Investment Committee is responsible for the preparation of "Key directions of Foreign Currency Assets management of the Central Bank of Azerbaijan Republic" in accordance with "Rules of Foreign Currency Assets management of the Central Bank of Azerbaijan Republic", and adoption of "Operational Investment Strategy on Foreign Currency Assets management of the Central Bank of Azerbaijan Republic", as well as control over foreign currency assets management

*Foreign Exchange Reserves Management Department.* The Risk Management Unit of the Foreign Exchange Reserves Management Department regularly controls the limits and exposures set for management of foreign currency assets in accordance with the "Regulations for Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan", "Main Directions for Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan", and "Operational Investment Strategy for Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan."

## Central Bank of the Republic of Azerbaijan

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

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

There are also special committees and commissions within the Bank for conducting operations and control such as the Credit Committee, and Regular Commission on determination of official exchange rates of the Bank, and others.

The risk related to the Bank's foreign currency assets is a significant risk. Segregation of duties, procedures and reporting for risk management are regulated by the "Guidelines on Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan" and "Instruction on operations for maintenance and management of currency reserves of the Central Bank of the Republic of Azerbaijan". Acceptable limits on managed risks are stipulated in the "Guidelines on Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan", "Main Directions of Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan", "Operational Investment Strategy for Management of Foreign Currency Assets of the Central Bank of the Republic of Azerbaijan" and "Investment Rules for Management of Assets by Foreign Managers". The respective documents are defined by the Investment Committee and approved by the Management Board.

### Credit risk

The Bank is exposed to credit risk, which is the risk that one party will incur a loss because the other party failed to comply with its financial obligations. Exposure to credit risk arises as a result of the Bank's lending and other transactions with counterparties. Credit risk is managed and controlled through proper selection of investment assets, credit quality of investment assets and setting limits on the amount of investment per investment asset.

In accordance with the investment guidelines of the Bank, only investment instruments with short-term ratings of not less than A-2 (Standard & Poor's), F-2 (Fitch) or P-2 (Moody's) and long-term ratings of not less than A- (Standard & Poor's, Fitch) or A3 (Moody's) may be used for management of the Bank's assets. At the same time, the maximum amount invested in corporations, state agencies without government guarantees and regional self-governing authorities is defined as 5% of the investment portfolio. Subject to the terms of the investment instrument, minimal credit rating is defined as A- / A3 (Standard & Poor's, Fitch, Moody's) for investment instruments with a term of up to twelve months, and A / A2 (Standard & Poor's, Fitch, Moody's) for deposits with a term over twelve months. When different credit ratings are designated by the various agencies, the rating meeting the minimum required level for this asset is used.

In 2021 and 2020, loans granted to credit institutions as part of monetary policy were secured by relevant collaterals. Exposure to credit risk is managed by obtaining collateral with the value of not less than the amount defined under the "Rules on loan issuance to the banks by the Central Bank of the Republic of Azerbaijan" depending on the type of collateral. In order to monitor credit risk exposures, the Financial Market Operations Department regularly controls overdue loan balances and produces appropriate reports.

*Credit risk grading system.* For measuring credit risk and grading financial instruments by the amount of credit risk, the Bank applies two approaches – an Internal Risk-Based (IRB) rating system or risk grades estimated by external international rating agencies (Standard & Poor's - "S&P", Fitch, Moody's). Internal and external credit ratings are mapped on an internally defined master scale with a specified range of probabilities of default as disclosed in the table below:

Master scale credit risk grade	Corresponding ratings of external international rating agencies (S&P)	Corresponding PD interval
Excellent	AAA to A-	0,01% - 0,2%
Good	BBB+ to B+	0,21% - 3%
Satisfactory	B, B-	3,1% - 10%
Special monitoring	CCC+ to CC-	10,1% - 99,9%
Default	C, D-I, D-II	100%

Each master scale credit risk grade is assigned a specific degree of creditworthiness:

- *Excellent* – strong credit quality with low expected credit risk;

## **Central Bank of the Republic of Azerbaijan**

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- *Good* – adequate credit quality with a moderate credit risk;
- *Satisfactory* – moderate credit quality with a satisfactory credit risk;
- *Special monitoring* – facilities that require closer monitoring and remedial management; and
- *Default* – facilities in which a default has occurred.

If the borrower is not provided with credit ratings by the leading international rating agencies, a credit rating is assigned by the Bank using the CAEL rating system and these ratings are estimated by management. Relevant credit rating is estimated based on the borrower's financial ratios such as: the Tier 1 capital ratio, Non-Performing Loans Ratio, Return on Equity and Return on Assets. The Bank monitors adverse changes in economic and business conditions in the longer term that may impact the ability of borrowers to fulfil contractual cash flow obligations at each reporting date.

### **Expected credit loss (ECL) measurement**

*ECL* is a probability-weighted estimate of the present value of future cash shortfalls. An *ECL* measurement is unbiased and is determined by evaluating a range of possible outcomes. *ECL* measurement is based on four components used by the Bank: Probability of Default (“PD”), Exposure at Default (“EAD”), Loss Given Default (“LGD”) and Discount Rate.

*EAD* represents the expected exposure in the event of a default. The Bank derives the *EAD* from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortisation. The *EAD* of a financial asset is its gross carrying amount at the time of default.

*PD* is an estimate of the likelihood of default to occur over a given time period. *LGD* is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the Bank would expect to receive, including from any collateral. It is usually expressed as a percentage of the *EAD*. The expected losses are discounted to present value at the end of the reporting period. The discount rate represents the effective interest rate (“*EIR*”) for the financial instrument or an approximation thereof.

Expected credit losses are modelled over instrument's *lifetime period*. The *lifetime period* is equal to the remaining contractual period to maturity of debt instruments, adjusted for expected prepayments, if any.

Management models *Lifetime ECL*, that is, losses that result from all possible default events over the remaining lifetime period of the financial instrument. The *12-month ECL*, represents a portion of lifetime *ECLs* that result from default events on a financial instrument that are possible within 12 months after the reporting period, or remaining *lifetime period* of the financial instrument if it is less than a year.

*Forward looking macroeconomic information* is used in the estimates of lifetime expected credit losses. For the financial instruments that remaining lifetime period is less than a year, long term macroeconomic development does not play significant role in shaping risk profiles and no forward looking adjustment is implemented.

The Bank considers a financial instrument to have experienced a *significant increase in credit risk* when one or more of the following criteria have been met:

- contractual payment is overdue for 31-90 days (90-s day inclusive) except for debt securities for which overdue more than 1 day is considered to be a significant increase in credit risk, unless it is due to technical operating reasons
- financial assets are downgraded by the leading international credit rating agencies of the long-term credit rating by 3 grades since initial recognition
- bank does not meet capital and liquidity prudential requirements that cause credit risk according to the issued latest audit report
- evidences that other institutions (except for the Bank) filed lawsuits against the borrower that may deteriorate their financial position.

The Bank decided to use the low credit risk assessment exemption for the financial instruments which have “Excellent” credit risk grade.

The Bank defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:



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- the credit rating of a financial asset is downgraded to “D” (C) by leading international rating agencies
- licence of the borrower to operate in banking industry is revoked
- the payment of principal amount and interest on loans past due over 90 days
- when the borrower’s loans are restructured due to significant deterioration in a bank's position
- the Bank raises claims against the borrower in accordance with the law

For purposes of disclosure, the Bank fully aligned the definition of default with the definition of credit-impaired assets. The default definition stated above is applied to all types of financial assets of the Bank, except for debt securities for which the criterion of 7 days or less is applied.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of two payments (six months). This period of two payments (six months) has been determined based on an analysis that considers the likelihood of a financial instrument returning to default status after curing.

The amount of ECL that is recognised in these financial statements depends on whether the credit risk of the borrower has increased significantly since initial recognition. This is a three-stage model for ECL measurement. A financial instrument that is not credit-impaired on initial recognition and its credit risk has not increased significantly since initial recognition has a credit loss allowance based on 12-month ECLs (Stage 1). If a SICR since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit-impaired and the loss allowance is based on lifetime ECLs. If a financial instrument is credit-impaired, the financial instrument is moved to Stage 3 and loss allowance is based on lifetime ECLs. The consequence of an asset being in Stage 3 is that the entity ceases to recognise interest income based on gross carrying value and applies the asset’s effective interest rate to the carrying amount, net of ECL, when calculating interest income.

If there is evidence that the SICR criteria are no longer met, the instrument is transferred back to Stage 1. If an exposure has been transferred to Stage 2 based on a qualitative indicator, the Bank monitors whether that indicator continues to exist or has changed.

The Bank performs ECL assessment on an individual basis for all financial assets based on external ratings.

The ECL is determined by predicting credit risk parameters (EAD, PD and LGD) for each future year during the lifetime period for each individual exposure.

### ***The key principles of calculating the credit risk parameters***

The EADs are determined based on the expected payment profile including contractual principal plus interest. EAD is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis for amortising products. This will also be adjusted for any expected overpayments made by a borrower. Early repayment or refinancing assumptions are also incorporated into the calculation.

LGD represents the Bank’s expectation of the extent of loss on a defaulted exposure. LGD varies by the type of counterparty, type and seniority of the claim, and the availability of collateral or other credit support. The 12-month and lifetime LGDs are determined based on the factors that impact the expected recoveries after a default event. The approach to LGD measurement for the loans to banks is as follows: LGD is calculated based on the history of cash inflows for the last five financial years from realisation of the collaterals pledged against licensed removed banks since 2010.

### ***Principles of assessment based on external ratings***

Certain exposures have external credit risk ratings and these are used to estimate credit risk parameters PD and LGD from the default and recovery statistics published by the respective rating agencies. This approach is applied for the debt securities in foreign currencies and short-term deposits.

The Bank regularly reviews its methodology and assumptions to reduce any difference between the estimates and the actual loss of credit.

### **Market risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises currency risk, interest rate risk and other price risks.

**Central Bank of the Republic of Azerbaijan**

*Notes to the Financial Statements for the year ended 31 December 2021*

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Market risk arises from open positions in interest rate and equity financial instruments, which are exposed to general and specific market movements and changes in the level of volatility of market prices and foreign currency rates.

**Interest rate risk**

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes but may also reduce or create losses in the event that unexpected movements occur. The main objective when managing the interest rate risk is to maintain stable return on investments while not exceeding the risk levels that can be undertaken per investment policies.

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**Interest rate gap analysis**

Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the interest gap position for major financial instruments as at 31 December 2021 is as follows:

	<b>Less than 3 months</b>	<b>3-6 months</b>	<b>6-12 months</b>	<b>More than 1 year</b>	<b>Non-interest bearing</b>	<b>Carrying amount</b>
<b>31 December 2021</b>						
<b>ASSETS</b>						
Cash and cash equivalents	1,718,333	-	-	-	5,120,658	6,838,991
Special Drawing Rights with the IMF	1,258,160	-	-	-	-	1,258,160
Derivative Financial Instruments	-	-	-	-	2,834	2,834
Debt securities						-
- Debt securities at AC	116	6,982	-	9,482,143	-	9,489,241
- Debt securities at FVOCI	2,326,086	718,137	1,234,286	2,641,159	-	6,919,668
- Debt securities mandatorily measured at FVTPL	953,367	-	-	-	-	953,367
Loans to banks	16,995	166,720	65,983	106,583	-	356,281
Loans to non-bank credit organizations	-	-	6,671	13,343	-	20,014
Loans to Deposit Insurance Fund	-	-	-	236,600	-	236,600
Other financial assets	1	7	71	471	1,585	2,135
<b>Total Financial Assets</b>	<b>6,273,058</b>	<b>891,846</b>	<b>1,307,011</b>	<b>12,480,299</b>	<b>5,125,077</b>	<b>26,077,291</b>
<b>LIABILITIES</b>						
Money in circulation	-	-	-	-	12,310,018	12,310,018
Amounts due to government organisations	2,577	-	-	-	4,002,060	4,004,637
Amounts due to credit institutions	-	-	-	-	7,440,004	7,440,004
Amounts due to other organisations	-	-	-	-	11,410	11,410
Debt securities in issue	199,402	-	-	-	-	199,402
Liabilities on transactions with the IMF	1,261,131	-	-	-	-	1,261,131
Amounts due to international financial institutions	1,015	10	-	-	-	1,025
Derivative financial instruments	-	-	-	-	862	862
Other financial liabilities	-	-	-	-	10,875	10,875
<b>Total Financial Liabilities</b>	<b>1,464,125</b>	<b>10</b>	<b>-</b>	<b>-</b>	<b>23,775,229</b>	<b>25,239,364</b>

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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

Interest rate risk is managed principally through monitoring interest rate gaps. A summary of the interest gap position for major financial instruments as at 31 December 2020 is as follows:

	<b>Less than 3 months</b>	<b>3-6 months</b>	<b>6-12 months</b>	<b>More than 1 year</b>	<b>Non-interest bearing</b>	<b>Carrying amount</b>
<b>31 December 2020</b>						
<b>ASSETS</b>						
Cash and cash equivalents	939,483	-	-	-	4,675,790	5,615,273
Special Drawing Rights with the IMF	375,543	-	-	-	-	375,543
Derivative Financial Instruments	-	-	-	-	449	449
Debt securities						-
- Debt securities at AC	233	-	-	9,495,913	-	9,496,146
- Debt securities at FVOCI	2,325,300	903,748	1,464,497	3,431,165	-	8,124,710
- Debt securities mandatorily measured at FVTPL	958,818	-	-	-	-	958,818
Loans to banks	18,623	50,589	6,297	323,899	-	399,408
Loans to non-bank credit organizations	-	-	-	25,330	-	25,330
Loans to Deposit Insurance Fund	-	-	-	207,222	-	207,222
Other financial assets	2	9	50	518	48,791	49,370
<b>Total Financial Assets</b>	<b>4,618,002</b>	<b>954,346</b>	<b>1,470,844</b>	<b>13,484,047</b>	<b>4,725,030</b>	<b>25,252,269</b>
<b>LIABILITIES</b>						
Money in circulation	-	-	-	-	11,839,664	11,839,664
Short-term deposits of resident banks	300,304	-	2,413,032	-	-	2,713,336
Amounts due to government organisations	1,325	-	-	-	4,919,993	4,921,318
Amounts due to credit institutions	-	-	-	-	3,204,953	3,204,953
Amounts due to other organisations	-	-	-	-	9,066	9,066
Debt securities in issue	648,213	-	-	-	-	648,213
Liabilities on transactions with the IMF	378,505	-	-	-	-	378,505
Amounts due to international financial institutions	1,133	-	254	18	-	1,405
Derivative financial instruments	-	-	-	-	3,556	3,556
Other financial liabilities	-	-	-	-	142,259	142,259
<b>Total Financial Liabilities</b>	<b>1,329,480</b>	<b>-</b>	<b>2,413,286</b>	<b>18</b>	<b>20,119,491</b>	<b>23,862,275</b>

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**Interest rate sensitivity analysis**

The management of interest rate risk based on interest rate gap analysis is supplemented by monitoring the sensitivity of financial assets and liabilities. An analysis of sensitivity of profit or loss and equity to changes in interest rates (repricing risk) based on a simplified scenario of a 100 basis point (bp) symmetrical fall or rise in all yield curves and positions of interest-bearing assets and liabilities existing as at 31 December 2021 and 2020 is as follows:

	<b>2021</b>	<b>2020</b>
100 bp parallel fall	(40,794)	(13,519)
100 bp parallel rise	40,794	13,519

An analysis of the sensitivity of profit or loss and equity as a result of changes in the fair value of financial instruments at fair value through profit or loss and financial assets at fair value through other comprehensive income due to changes in the interest rates, based on positions existing as at 31 December 2021 and 2020 and a simplified scenario of a 100 bp symmetrical fall or rise in all yield curves, is as follows:

	<b>2021</b>		<b>2020</b>	
	<b>Net profit or loss</b>	<b>Equity</b>	<b>Net profit or loss</b>	<b>Equity</b>
100 bp parallel fall	16,778	97,898	16,203	114,375
100 bp parallel rise	(17,641)	(105,538)	(16,962)	(123,659)

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The table below displays average effective interest rates for interest bearing assets and liabilities as at 31 December 2021 and 2020. These interest rates are an approximation of the yields to maturity of these assets and liabilities.

	31 December 2021				31 December 2020			
	Average effective interest rate, %				Average effective interest rate, %			
	AZN	USD	EUR	Other currencies	AZN	USD	EUR	Other currencies
<b>Interest bearing assets</b>								
Cash and cash equivalents	-	0.17	(0.56)	-	-	0.35	(0.50)	-
Special Drawing Rights with the IMF	-	-	-	0.08	-	-	-	0.08
Debt securities								
-Debt securities at AC	0.15	-	-	-	0.15	-	-	-
-Debt securities at FVOCI	3.04	0.71	0.42	0.91	3.04	1.29	0.80	0.95
-Debt securities mandatorily measured at FVTPL	-	0.91	0.56	1.27	-	1.48	0.85	1.46
Loans to banks (nominal interest rate)	2.40	-	-	-	2.35	-	-	-
Loans to non-bank credit organizations (nominal interest rate)	0.10	-	-	-	0.10	-	-	-
Loans to Deposit Insurance Fund	6.48	-	-	-	6.25	-	-	-
Other financial assets	5.54	-	-	-	6.18	-	-	-
<b>Interest bearing liabilities</b>								
Short-term deposits of resident banks	-	-	-	-	5.75	-	-	-
Amounts due to government organisations	-	-	(0.50)	-	-	-	(0.50)	-
Debt securities in issue	6.01	-	-	-	5.88	-	-	-
Liabilities on transactions with the IMF	-	-	-	0.08	-	-	-	0.08

**Central Bank of the Republic of Azerbaijan***Notes to the Financial Statements for the year ended 31 December 2021**(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)***Currency risk**

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. Subject to the currency structure of assets, the value of assets of the Bank is exposed to risk of changes in exchange rates of main foreign currencies.

The foreign currency assets of the Bank are primarily maintained in US Dollars, Euro and Pound Sterling. Currency composition of assets was defined by the "Main Directions for Management of Currency Assets of the Central Bank of the Republic of Azerbaijan" approved by the resolution of the Management Board dated 12 December 2018. This document is taken as a basis by the Foreign Exchange Reserves Management Department of the Bank, who is the major body responsible for management of the currency risk.

Currency risk is managed through diversification of foreign currency portfolio and determination of the following parameters:

- foreign currencies subject to management;
- maximum share of the managed currency in the total assets denominated in foreign currencies (minimum volume for the base currency).

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2021:

	USD	EUR	Other foreign currencies	Total
<b>ASSETS</b>				
Cash and cash equivalents	5,923,511	881,502	33,978	6,838,991
Special Drawing Rights with the IMF	-	-	1,258,160	1,258,160
Debt securities	6,877,660	415,095	235,785	7,528,540
Derivative financial instruments	2,834	-	-	2,834
Other financial assets	1,472	-	-	1,472
<b>Total assets</b>	<b>12,805,477</b>	<b>1,296,597</b>	<b>1,527,923</b>	<b>15,629,997</b>
<b>LIABILITIES</b>				
Amounts due to government organisations	1,680,251	18,351	2,347	1,700,949
Amounts due to credit institutions	1,500,067	302,085	21,718	1,823,870
Amounts due to other organisations	1	-	-	1
Liabilities on transactions with the IMF	-	-	1,258,657	1,258,657
Amounts due to international financial institutions	10	-	-	10
Derivative financial instruments	862	-	-	862
Other financial liabilities	7,460	2,567	-	10,027
<b>Total liabilities</b>	<b>3,188,651</b>	<b>323,003</b>	<b>1,282,722</b>	<b>4,794,376</b>
<b>Net recognized position</b>	<b>9,616,826</b>	<b>973,594</b>	<b>245,201</b>	<b>10,835,621</b>
The effect of derivatives	325,294	(171,999)	(93,419)	59,876
<b>Net position</b>	<b>9,942,120</b>	<b>801,595</b>	<b>151,782</b>	<b>10,895,497</b>

**Central Bank of the Republic of Azerbaijan**

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2020:

	USD	EUR	Other foreign currencies	Total
<b>ASSETS</b>				
Cash and cash equivalents	4,641,538	913,414	60,321	5,615,273
Special Drawing Rights with the IMF	-	-	375,543	375,543
Debt securities	8,001,169	515,042	194,294	8,710,505
Derivative financial instruments	449	-	-	449
Other financial assets	48,617	110	-	48,727
<b>Total assets</b>	<b>12,691,773</b>	<b>1,428,566</b>	<b>630,158</b>	<b>14,750,497</b>
<b>LIABILITIES</b>				
Amounts due to government organisations	1,861,431	394,346	3,196	2,258,973
Amounts due to credit institutions	1,198,948	268,191	21,570	1,488,709
Amounts due to other organisations	6	-	-	6
Liabilities on transactions with the IMF	-	-	376,031	376,031
Amounts due to international financial institutions	528	-	-	528
Derivative financial instruments	3,556	-	-	3,556
Other financial liabilities	137,092	1,659	-	138,751
<b>Total liabilities</b>	<b>3,201,561</b>	<b>664,196</b>	<b>400,797</b>	<b>4,266,554</b>
<b>Net recognized position</b>	<b>9,490,212</b>	<b>764,370</b>	<b>229,361</b>	<b>10,483,943</b>
The effect of derivatives	260,592	(176,256)	(69,729)	14,607
<b>Net position</b>	<b>9,750,804</b>	<b>588,114</b>	<b>159,632</b>	<b>10,498,550</b>

A weakening of the AZN, as indicated below, against the following currencies at 31 December 2021 and 2020 would have increased equity and profit or loss by the amounts shown below. This analysis is based on foreign currency exchange rate variances that the Bank considered to be reasonably possible at the end of the reporting period. The analysis assumes that all other variables, in particular interest rates, remain constant.

	31 December 2021	31 December 2020
10% appreciation of USD against AZN (2020: 10%)	994,212	975,080
10% appreciation of EUR against AZN (2020: 10%)	80,160	58,811

A strengthening of the AZN against the above currencies at 31 December 2021 and 2020 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

**Liquidity risk**

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. Management of the liquidity risk by the Bank is based on keeping the liquidity at required level for meeting the requirements of the Bank in any condition.

In order to implement the monetary policy, the Bank maintains operational liquid tranche from its foreign currency assets. Liquidity risk management consists of identifying the liquid assets and determining the minimum liquidity limits of foreign currency assets over its investment period.

The table below shows liabilities at 31 December 2021 by their remaining contractual maturity. The amounts of liabilities disclosed in the maturity table are the contractual undiscounted cash flows, foreign currency payments are translated using the spot exchange rate at the end of the reporting period.



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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The maturity analysis of financial instruments at 31 December 2021 is as follows:

	<b>Demand and less than 1 month</b>	<b>From 1 to 6 months</b>	<b>From 6 to 12 months</b>	<b>From 1 to 5 years</b>	<b>More than 5 years</b>	<b>No maturity</b>	<b>Total</b>
<b>LIABILITIES</b>							
Money in circulation	-	-	-	-	-	12,310,018	12,310,018
Amounts due to government organisations	4,004,637	-	-	-	-	-	4,004,637
Amounts due to credit institutions	7,440,004	-	-	-	-	-	7,440,004
Amounts due to other organisations	11,410	-	-	-	-	-	11,410
Debt securities in issue	200,000	-	-	-	-	-	200,000
Liabilities on transactions with the IMF	-	-	-	-	-	1,261,131	1,261,131
Amounts due to international financial institutions	1,015	10	-	-	-	-	1,025
Gross Settled Derivatives							-
- Inflow	(592,024)	-	-	-	-	-	(592,024)
- Outflow	592,886	-	-	-	-	-	592,886
Other financial liabilities	10,875	-	-	-	-	-	10,875
<b>Total potential future payments for financial obligations</b>	<b>11,668,803</b>	<b>10</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>13,571,149</b>	<b>25,239,962</b>

**Central Bank of the Republic of Azerbaijan**

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The maturity analysis of financial instruments at 31 December 2020 is as follows:

	<b>Demand and less than 1 month</b>	<b>From 1 to 6 months</b>	<b>From 6 to 12 months</b>	<b>From 1 to 5 years</b>	<b>More than 5 years</b>	<b>No maturity</b>	<b>Total</b>
<b>LIABILITIES</b>							
Money in circulation	-	-	-	-	-	11,839,664	11,839,664
Short-term deposits of resident banks	300,736	-	2,550,316	-	-	-	2,851,052
Amounts due to government organisations	4,921,318	-	-	-	-	-	4,921,318
Amounts due to credit institutions	3,204,953	-	-	-	-	-	3,204,953
Amounts due to other organisations	9,066	-	-	-	-	-	9,066
Debt securities in issue	649,978	-	-	-	-	-	649,978
Liabilities on transactions with the IMF	-	-	-	-	-	378,505	378,505
Amounts due to international financial institutions	1,133	-	254	18	-	-	1,405
Gross Settled Derivatives							
- Inflow	(568,023)	-	-	-	-	-	(568,023)
- Outflow	571,579	-	-	-	-	-	571,579
Other financial liabilities	142,259	-	-	-	-	-	142,259
<b>Total potential future payments for financial obligations</b>	<b>9,232,999</b>	<b>-</b>	<b>2,550,570</b>	<b>18</b>	<b>-</b>	<b>12,218,169</b>	<b>24,001,756</b>

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The table below shows the maturity analysis of financial assets at their carrying amounts and based on their contractual maturities, except for debt securities measured at fair value which are readily saleable if it should be necessary to meet cash outflows on financial liabilities. Such financial assets are included in the maturity analysis based on their expected date of disposal. Impaired loans are included at their carrying amounts net of impairment provisions, and based on the expected timing of cash inflows.

The table below shows the maturity analysis of the amounts recognized in the statement of financial position as at 31 December 2021:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Overdue	Total
<b>ASSETS</b>								
Cash and cash equivalents	6,838,991	-	-	-	-	-	-	6,838,991
Special Drawing Rights with the IMF	-	-	-	-	-	1,258,160	-	1,258,160
Derivative financial instruments	2,834	-	-	-	-	-	-	2,834
Debt securities	1,031,694	853,809	2,006,177	3,710,495	9,760,101	-	-	17,362,276
Loans to banks	-	5,724	195,876	106,583	-	-	48,098	356,281
Loans to non-bank credit organizations	-	-	6,671	13,343	-	-	-	20,014
Loans to Deposit Insurance Fund	-	-	-	-	236,600	-	-	236,600
Other financial assets	1,585	1	78	14	457	-	-	2,135
<b>Total financial assets</b>	<b>7,875,104</b>	<b>859,534</b>	<b>2,208,802</b>	<b>3,830,435</b>	<b>9,997,158</b>	<b>1,258,160</b>	<b>48,098</b>	<b>26,077,291</b>
<b>LIABILITIES</b>								
Money in circulation	-	-	-	-	-	12,310,018	-	12,310,018
Amounts due to government organisations	4,004,637	-	-	-	-	-	-	4,004,637
Amounts due to credit institutions	7,440,004	-	-	-	-	-	-	7,440,004
Amounts due to other organisations	11,410	-	-	-	-	-	-	11,410
Derivative financial instruments	862	-	-	-	-	-	-	862
Debt securities in issue	199,402	-	-	-	-	-	-	199,402
Liabilities on transactions with the IMF	-	-	-	-	-	1,261,131	-	1,261,131
Amounts due to international financial institutions	1,015	-	10	-	-	-	-	1,025
Other financial liabilities	10,875	-	-	-	-	-	-	10,875
<b>Total financial liabilities</b>	<b>11,668,205</b>	<b>-</b>	<b>10</b>	<b>-</b>	<b>-</b>	<b>13,571,149</b>	<b>-</b>	<b>25,239,364</b>
<b>Net position</b>	<b>(3,793,101)</b>	<b>859,534</b>	<b>2,208,792</b>	<b>3,830,435</b>	<b>9,997,158</b>	<b>(12,312,989)</b>	<b>48,098</b>	<b>837,927</b>

Liquidity risk denominated in local currency is regularly assessed and managed by the Bank.

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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The table below shows the maturity analysis of the amounts recognized in the statement of financial position as at 31 December 2020:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	More than 5 years	No maturity	Overdue	Total
<b>ASSETS</b>								
Cash and cash equivalents	5,615,273	-	-	-	-	-	-	5,615,273
Special Drawing Rights with the IMF	-	-	-	-	-	375,543	-	375,543
Derivative financial instruments	449	-	-	-	-	-	-	449
Debt securities	1,203,384	1,056,670	2,599,572	3,876,520	9,843,528	-	-	18,579,674
Loans to banks	7,444	10,954	56,886	323,899	-	-	225	399,408
Loans to non-bank credit organizations	-	-	-	25,330	-	-	-	25,330
Loans to Deposit Insurance Fund	-	-	-	-	207,222	-	-	207,222
Other financial assets	48,791	2	59	47	471	-	-	49,370
<b>Total financial assets</b>	<b>6,875,341</b>	<b>1,067,626</b>	<b>2,656,517</b>	<b>4,225,796</b>	<b>10,051,221</b>	<b>375,543</b>	<b>225</b>	<b>25,252,269</b>
<b>LIABILITIES</b>								
Money in circulation	-	-	-	-	-	11,839,664	-	11,839,664
Amounts due to government organisations	4,921,318	-	-	-	-	-	-	4,921,318
Short-term deposits of resident banks	300,304	-	2,413,032	-	-	-	-	2,713,336
Amounts due to credit institutions	3,204,953	-	-	-	-	-	-	3,204,953
Amounts due to other organisations	9,066	-	-	-	-	-	-	9,066
Derivative financial instruments	3,556	-	-	-	-	-	-	3,556
Debt securities in issue	648,213	-	-	-	-	-	-	648,213
Liabilities on transactions with the IMF	-	-	-	-	-	378,505	-	378,505
Amounts due to international financial institutions	1,133	-	254	18	-	-	-	1,405
Other financial liabilities	142,259	-	-	-	-	-	-	142,259
<b>Total financial liabilities</b>	<b>9,230,802</b>	<b>-</b>	<b>2,413,286</b>	<b>18</b>	<b>-</b>	<b>12,218,169</b>	<b>-</b>	<b>23,862,275</b>
<b>Net position</b>	<b>(2,355,461)</b>	<b>1,067,626</b>	<b>243,231</b>	<b>4,225,778</b>	<b>10,051,221</b>	<b>(11,842,626)</b>	<b>225</b>	<b>1,389,994</b>

## **Central Bank of the Republic of Azerbaijan**

Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

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### **33 Management of capital**

The capital of the Bank comprises the residual value of the Bank's assets after deduction of all its liabilities.

The Bank's objectives when managing capital are to maintain an appropriate level of capital to ensure economic independence of the Bank and ability to perform its functions. The Bank considers total capital under management to be equity disclosed in the statement of financial position.

No external capital requirements exist for the Bank as the central bank, except for the size of the charter fund and minimum amount of capital reserves stipulated by the Law of the Republic of Azerbaijan on "the Central Bank of the Republic of Azerbaijan" (the "Law").

As disclosed in Note 23, at 31 December 2021 the authorized and fully paid charter fund of the Bank was AZN 500,000 thousand (31 December 2020: AZN 500,000 thousand).

The Bank has made total loss in the amount of AZN 162,746 thousand (2020: AZN 52,485 thousand profit) for the year ended 31 December 2021. Based on the article 12 of the Law, reporting year profit shall, in the first place, be directed to formation of capital reserves of the Bank. Upon formation of capital reserves and approval of the Bank's annual financial statements by the auditor's opinion, a clear balance of realized gains shall be transferred to the state budget (including to the Guarantee Fund for Liabilities on Government Debt and Guarantee coordinating with the relevant executive authority based upon an appeal by the relevant executive authority).

There was transfer to the State Budget amounting to AZN 250 million in 2021 (2020: AZN 1,000 million).

### **34 Contingencies**

#### **Litigations**

In the ordinary course of business, the Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations.

### **35 Related party transactions**

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

Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

Main government entities operating with the Bank include the Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan, Ministry of Finance, International Bank of Azerbaijan, State Oil Fund of Azerbaijan, Aqrarkredit JSCO, Azerbaijan Deposit Insurance Fund and AzerTurk Bank.

#### **Transactions with the members of the Management**

Total remuneration included in personnel expenses for the years ended 31 December 2021 and 2020 is as follows:

	<u>2021</u>	<u>2020</u>
Short-term employee benefits (salary)	1,146	1,256

According to the Decree 1616 of the President of the Republic of Azerbaijan on "Improvement of the management of the system of regulation and supervision in the financial services market" dated 28 November 2019, the Financial Markets Supervisory Authority was abolished and structural changes were made and the number of managers in upper management was increased due to transfer of powers of the financial markets supervisory authority defined by laws of the Republic of Azerbaijan, including licensing, regulation and supervision in the financial services market, and duties and responsibilities on protection of rights of investors and consumers of financial services to the Bank.

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**Transactions with government-related entities**

The Bank is a public legal entity, and in the ordinary course of business operates with various state owned companies. Significant transactions with government owned companies include loans to banks and other government owned institutions, investment securities, promissory notes from government, placements by government and credit institutions and interest income and expenses.

The outstanding balances and the related average effective interest rates as at 31 December 2021 and related profit or loss amounts of transactions for the year ended 31 December 2021 with other related parties are as follows:

	Government bodies of Azerbaijan		Entities under government control		Total
	Amount	Effective interest rate, %	Amount	Effective interest rate, %	Amount
<b>Statement of financial position</b>					
<b>ASSETS</b>					
Debt securities					
-Debt securities at AC	7,099	0.15	9,482,143	0.15	9,489,242
-Debt securities at FVOCI	-	-	344,495	from 3.0 to 3.25	344,495
Loans to banks (nominal interest rates)	-	-	113,699	from 0.1 to 0.5	113,699
Loans to Deposit Insurance Fund	-	-	236,600	6.48	236,600
<b>LIABILITIES</b>					
Amounts due to government organisations	2,429,732	-	1,574,905	-	4,004,637
Short-term deposits of resident banks	-	-	-	-	-
Amounts due to credit institutions	-	-	2,548,122	-	2,548,122
Amounts due to other organisations	6,930	-	4,480	-	11,410
Liabilities on transactions with the IMF	1,261,131	-	-	-	1,261,131
Amounts due to international financial institutions	1,025	-	-	-	1,025
Debt securities in issue	-	-	32,080	6.01	32,080
<b>Profit (loss)</b>					
Interest income	14	-	41,671	-	41,685
Interest expense	-	-	(138,060)	-	(138,060)

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Notes to the Financial Statements for the year ended 31 December 2021

(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The outstanding balances and the related average effective interest rates as at 31 December 2020 and related profit or loss amounts of transactions for the year ended 31 December 2020 with other related parties are as follows:

	Government bodies of Azerbaijan		Entities under government control		Total
	Amount	Effective interest rate, %	Amount	Effective interest rate, %	Amount
<b>Statement of financial position</b>					
<b>ASSETS</b>					
Debt securities					
-Debt securities at AC	14,003	0.15	9,482,143	0.15	9,496,146
-Debt securities at FVOCI	-	-	373,023	from 3.0 to 3.25	373,023
Loans to banks	-	-	113,502	from 0.1 to 0.5	113,502
Loans to Deposit Insurance Fund	-	-	207,222	6.50	207,222
<b>LIABILITIES</b>					
Amounts due to government organisations	3,213,012	-	1,708,306		4,921,318
Short-term deposits of resident banks	-	-	2,423,994	5.75	2,423,994
Amounts due to credit institutions	-	-	212,967	-	212,967
Amounts due to other organisations	6,529		2,537		9,066
Liabilities on transactions with the IMF	378,505	-	-	-	378,505
Amounts due to international financial institutions	1,405	-	-	-	1,405
Debt securities in issue	-	-	84,034	from 5.76 to 6.01	84,034
<b>Profit (loss)</b>					
Interest income	31	-	30,071	-	30,102
Interest expense	-	-	(91,533)	-	(91,533)

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Notes to the Financial Statements for the year ended 31 December 2021

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**36 Financial assets and liabilities: fair values and accounting classifications****Accounting classifications and fair values**

For the purposes of measurement, IFRS 9 “Financial Instruments” classifies financial assets into the following categories: (a) financial assets at FVTPL; (b) debt instruments at FVOCI, (c) financial assets at AC.

The following table provides a reconciliation of financial assets with these measurement categories as of 31 December 2021:

	Financial assets measured at AC	Financial assets measured at FVOCI	Financial assets measured at FVTPL	Total
<b>ASSETS</b>				
<b>Cash and cash equivalents</b>	6,072,906	-	766,085	6,838,991
<b>Debt securities</b>				
Agency	-	2,560,825	188,191	2,749,016
Supranational	-	885,660	56,911	942,571
Treasury	-	1,823,610	536,811	2,360,421
Local Authority	-	425,408	43,197	468,605
Corporate	-	786,204	83,621	869,825
Sovereign	-	93,466	2,831	96,297
Covered	-	-	41,805	41,805
Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan	-	344,495	-	344,495
JSCO Aqrarkredit	9,482,143	-	-	9,482,143
Ministry of Finance of the Republic of Azerbaijan	7,098	-	-	7,098
<b>Loans to banks</b>				
- Refinancing loans	356,281	-	-	356,281
<b>Loans to non-bank credit organizations</b>	20,014	-	-	20,014
<b>Loans to Deposit Insurance Fund</b>	236,600	-	-	236,600
<b>Special Drawing Rights with the IMF</b>	1,258,160	-	-	1,258,160
<b>Derivative financial instruments</b>	-	-	2,834	2,834
<b>Other financial assets:</b>				
- Receivables from trade securities disposed	1,037	-	-	1,037
- Loans to employees	542	-	-	542
- Amounts in course of settlement	556	-	-	556
<b>TOTAL FINANCIAL ASSETS</b>	<b>17,435,337</b>	<b>6,919,668</b>	<b>1,722,286</b>	<b>26,077,291</b>



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(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)

The following table provides a reconciliation of financial assets with these measurement categories as of 31 December 2020:

	Financial assets measured at AC	Financial assets measured at FVOCI	Financial assets measured at FVTPL	Total
<b>ASSETS</b>				
<b>Cash and cash equivalents</b>	4,764,320	-	850,953	5,615,273
<b>Debt securities</b>				
Agency	-	3,588,626	176,687	3,765,313
Supranational	-	1,365,851	57,875	1,423,726
Treasury	-	1,287,564	580,700	1,868,264
Local Authority	-	851,370	34,448	885,818
Corporate	-	309,549	80,199	389,748
Sovereign	-	348,727	4,138	352,865
Covered	-	-	24,771	24,771
Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan	-	373,023	-	373,023
JSCO Aqrarkredit	9,482,143	-	-	9,482,143
Ministry of Finance of the Republic of Azerbaijan	14,003	-	-	14,003
<b>Loans to banks</b>				
- Refinancing loans	399,408	-	-	399,408
- Lender of last resort loans	25,330	-	-	25,330
<b>Loans to non-bank credit organizations</b>	207,222	-	-	207,222
<b>Special Drawing Rights with the IMF</b>	375,543	-	-	375,543
<b>Derivative financial instruments</b>	-	-	449	449
<b>Other financial assets:</b>				
- Receivables from trade securities disposed	48,617	-	-	48,617
- Loans to employees	555	-	-	555
- Amounts in course of settlement	198	-	-	198
<b>TOTAL FINANCIAL ASSETS</b>	<b>15,317,339</b>	<b>8,124,710</b>	<b>1,810,220</b>	<b>25,252,269</b>

The estimates of fair value are intended to approximate 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. However given the uncertainties and the use of subjective judgment, the fair value should not be interpreted as being realisable in an immediate sale of the assets or transfer of liabilities. The fair value of a liability reflects its non-performance risk.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. 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. For all other financial instruments the Bank determines fair values using other valuation techniques. The chosen valuation technique incorporates all the factors that market participants would take into account in these circumstances.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

## **Central Bank of the Republic of Azerbaijan**

*Notes to the Financial Statements for the year ended 31 December 2021*

*(Amounts are presented in thousands of Azerbaijani Manats, unless otherwise stated)*

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Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist, Black-Scholes and polynomial option pricing models and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index prices and expected price volatilities and correlations. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

The Bank uses widely recognized valuation models for determining the fair value of common and more simple financial instruments, like interest rate and currency swaps that use only observable market data and require little management judgment and estimation. Observable prices and model inputs are usually available in the market for listed debt and equity securities, exchange traded derivatives and simple over the counter derivatives like interest rate swaps.

There were no changes in valuation techniques as at 31 December 2021 (2020: none).

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 or loss on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

### **Fair value hierarchy**

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: quoted market price (unadjusted) in an active market for an identical instrument;
- Level 2: inputs other than quotes prices included within Level 1 that are observable either directly (i.e., as prices) or indirectly (i.e., derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data;
- Level 3: inputs that are unobservable. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Where third-party information, such as broker quotes or pricing services are used to measure fair value, the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of IFRS, is assessed and documented. This includes:

- verifying that the broker or pricing service is approved by the Bank for use in pricing the relevant type of financial instrument;
- understanding how the fair value has been arrived at the extent to which it represents actual market transactions;
- when prices for similar instruments are used to measure fair value, how these prices have been adjusted to reflect the characteristics of the instrument subject to measurement;
- where a number of quotes for the same financial instrument have been obtained, how fair value has been determined using those quotes.

Fair value measurements are those that the accounting standards require or permit in the statement of financial position at the end of each reporting period. The table below analyses financial instruments measured at fair value at 31 December 2021, by the level in the fair value hierarchy into which the recurring

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fair value measurement is categorised. The amounts are based on the values recognized in the statement of financial position:

	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
<b>Financial assets</b>			
Cash and cash equivalents	-	766,085	766,085
Debt securities			-
- Agency	2,749,016	-	2,749,016
- Supranational	942,571	-	942,571
- Treasury	2,360,421	-	2,360,421
- Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan	344,495	-	344,495
- Local Authority	468,605	-	468,605
- Corporate	869,825	-	869,825
- Sovereign	96,297	-	96,297
- Covered	41,805	-	41,805
Derivative financial instruments	-	2,834	2,834
	<b>7,873,035</b>	<b>768,919</b>	<b>8,641,954</b>
<b>Financial liabilities</b>			
Derivative financial instruments	-	862	862

The table below analyses financial instruments measured at fair value at 31 December 2020, by the level in the fair value hierarchy into which the recurring fair value measurement is categorized. The amounts are based on the values recognized in the statement of financial position:

	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
<b>Financial assets</b>			
Cash and cash equivalents	-	850,953	850,953
Debt securities			-
- Agency	3,765,313	-	3,765,313
- Supranational	1,423,726	-	1,423,726
- Treasury	1,868,264	-	1,868,264
- Mortgage and Credit Guarantee Fund of the Republic of Azerbaijan	373,023	-	373,023
- Local Authority	885,818	-	885,818
- Corporate	389,748	-	389,748
- Sovereign	352,865	-	352,865
- Covered	24,771	-	24,771
Derivative financial instruments	-	449	449
	<b>9,083,528</b>	<b>851,402</b>	<b>9,934,930</b>
<b>Financial liabilities</b>			
Derivative financial instruments	-	3,556	3,556

The valuation of level 1 securities is regularly performed by the Bank using available sources.

Derivative products valued using a valuation technique with market-observable inputs are mainly currency forward (including forward made on the basis of mutual settlement) exchange and swap contracts. The fair value of forward foreign exchange and swap contracts is determined using forward exchange rates at the balance sheet date.

There were no transfers between Level 1 and Level 2 during the year.

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**Assets and liabilities not measured at fair value but for which fair value is disclosed**

The table below analyses financial instruments not measured at fair value at 31 December 2021, by the level in the fair value hierarchy:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total fair values</u>	<u>Total carrying amount</u>
<b>ASSETS</b>					
Cash and cash equivalents	-	6,072,906	-	6,072,906	6,072,906
Special Drawing Rights with the IMF	-	1,258,160	-	1,258,160	1,258,160
Debt securities:					
<i>JSCO Aqrarkredit</i>	-	-	9,482,143	9,482,143	9,482,143
<i>Ministry of Finance of the Republic of Azerbaijan</i>	-	7,098	-	7,098	7,098
Loans to banks	-	300,822	46,669	347,491	356,281
Loans to non-bank credit organizations	-	20,610	-	20,610	20,014
Loans to Deposit Insurance Fund	-	236,600	-	236,600	236,600
Other financial assets	-	2,135	-	2,135	2,135
<b>LIABILITIES</b>					
Money in circulation	12,310,018	-	-	12,310,018	12,310,018
Short-term deposits of resident banks	-	-	-	-	-
Amounts due to government organisations	-	4,004,637	-	4,004,637	4,004,637
Amounts due to credit institutions	-	7,440,004	-	7,440,004	7,440,004
Amounts due to other organisations	-	11,410	-	11,410	11,410
Debt securities in issue	-	199,402	-	199,402	199,402
Liabilities on transactions with the IMF	-	1,261,131	-	1,261,131	1,261,131
Amounts due to international financial institutions	-	1,025	-	1,025	1,025
Other financial liabilities	-	10,875	-	10,875	10,875

The table below analyses financial instruments not measured at fair value at 31 December 2020, by the level in the fair value hierarchy:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total fair values</u>	<u>Total carrying amount</u>
<b>ASSETS</b>					
Cash and cash equivalents	-	4,764,320	-	4,764,320	4,764,320
Special Drawing Rights with the IMF	-	375,543	-	375,543	375,543
Debt securities:					
<i>JSCO Aqrarkredit</i>	-	-	9,482,143	9,482,143	9,482,143
<i>Ministry of Finance of the Republic of Azerbaijan</i>	-	14,003	-	14,003	14,003
Loans to banks	-	303,733	44,407	348,140	399,408
Loans to non-bank credit organizations	-	20,610	-	20,610	25,330
Loans to Deposit Insurance Fund	-	207,222	-	207,222	207,222
Other financial assets	-	49,370	-	49,370	49,370
<b>LIABILITIES</b>					
Money in circulation	11,839,664	-	-	11,839,664	11,839,664
Short-term deposits of resident banks	-	2,713,336	-	2,713,336	2,713,336
Amounts due to government organisations	-	4,921,318	-	4,921,318	4,921,318
Amounts due to credit institutions	-	3,204,953	-	3,204,953	3,204,953
Amounts due to other organisations	-	9,066	-	9,066	9,066
Debt securities in issue	-	648,213	-	648,213	648,213
Liabilities on transactions with the IMF	-	378,505	-	378,505	378,505
Amounts due to international financial institutions	-	1,405	-	1,405	1,405
Other financial liabilities	-	142,259	-	142,259	142,259

The fair values in level 2 and 3 fair value hierarchies were estimated using the discounted cash flows valuation technique, except for JSCO Agrarkredit. The fair value of unquoted fixed interest rate instruments

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was estimated based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity.

**37 Subsequent events**

On 11 January 2022, the Bank obtained deposit in the amount of AZN 2,340,000 out of auction from IBAR with the annual interest rate of 3.0%, with a one year term.