

# JSC m2 Real Estate

## Consolidated financial statements

*For the year ended 31 December 2016  
with independent auditor's report*

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## Independent auditor's report

To the Shareholder and the Supervisory Board of  
JSC M2 Real Estate

### *Opinion*

We have audited the consolidated financial statements of JSC M2 Real Estate and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

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

### *Basis for opinion*

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

### *Key audit matters*

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

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

## Valuation of investment property

Investment property includes buildings held for earning rental income and land plots with a currently undetermined future use or with a view of future redevelopment. Investment property is measured initially at cost including transaction costs. Subsequent to initial recognition, investment property is measured at fair value.

The measurement of investment property at fair value was a matter of most significance in our audit because of the significance of the balance of investment property to the consolidated financial statements (30% of total Group's assets) and the complexity and judgemental nature of estimation processes and assumptions used.

We evaluated the competence, capabilities and objectivity of the external experts involved by the Group's management in the valuation process.

We gained an understanding of internal controls implemented around the estimation process.

We evaluated management's assumptions used (rental income, square meters to be developed, discount rate, market prices per square meter) by comparing them to available market information and official registry records.

We involved our valuation experts to evaluate the assumptions used in the valuation of investment property. We also performed physical observation of these assets.

We analyzed the disclosures in the consolidated financial statements in respect of the fair value of investment property.

Note 10 describes the details of investment properties and discloses details of the fair valuation and significant assumptions.

### *Responsibilities of management and the Supervisory Board for the consolidated financial statements*

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

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

The Supervisory Board is responsible for overseeing the Group's financial reporting process.

### *Auditor's responsibilities for the audit of the consolidated financial statements*

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

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

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

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

From the matters communicated with the Supervisory Board, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's 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 auditor's report is Ruslan Khoroshvili.

A handwritten signature in blue ink, appearing to read 'R. Khoroshvili', followed by a horizontal line.

EY Georgia LLC  
Kote Abkhazi 44, 0105, Tbilisi, Georgia

4 April 2017

## Consolidated statement of comprehensive income

For the year ended 31 December

*(Thousands of Georgian Lari)*

	Notes	2016	2015
Sales of inventory property	5	96,347	44,893
Cost of sales - inventory property	6	(82,403)	(39,744)
Profit on sale of inventory property		13,944	5,149
Rental income	5	2,778	1,785
Property operating expense		(224)	(251)
Net rental income		2,554	1,534
Net gain from revaluation of investment property	10	2,553	16,702
Other revenue	5	191	285
Employee benefits expense	7	(1,498)	(943)
Other general and administrative expenses	8	(2,026)	(2,076)
Depreciation	12	(243)	(185)
Marketing and advertising expense		(2,339)	(2,785)
Non-recurring expenses		(407)	(323)
Operating profit		12,729	17,358
Finance income		715	386
Finance expense		(210)	(1,030)
Net foreign exchange gain/(loss)		1,143	(836)
Profit before income tax expense		14,377	15,878
Income tax expense	9	(3,473)	(2,798)
Profit for the year		10,904	13,080
Other comprehensive income to be reclassified to profit or loss in subsequent periods:			
Revaluation gain on shares of BGEO held for settlement of the Group's cash-settled share based transactions		286	-
Other comprehensive income not to be reclassified to profit or loss in subsequent periods:			
Exchange difference on translation of operations to presentation currency		15,252	-
Total comprehensive income for the year		26,442	13,080

Signed and authorised for release on behalf of the management of the Group

Chief Executive Officer

Irakli Burdiladze

Chief Financial Officer

Giorgi Natroshvili

4 April 2017

*The accompanying notes on pages 5-29 are an integral part of these consolidated financial statements.*

## Consolidated statement of financial position

As at 31 December

*(Thousands of Georgian Lari)*

	<i>Notes</i>	<i>2016</i>	<i>2015 (reclassified)*</i>
<b>Assets</b>			
<b>Non-current assets</b>			
Investment property	10	112,439	109,855
Investment property under construction	10	1,390	–
Inventory property	11	95,105	32,921
Deferred tax assets	9	–	2,704
Property and equipment, net	12	7,050	1,370
Prepayments and other assets	13	19,297	19,039
		<u>235,281</u>	<u>165,889</u>
<b>Current assets</b>			
Inventory property	11	17,904	65,114
Prepayments and other assets	13	22,288	18,872
Investment securities available for sale	14	2,842	2,120
Trade and other receivables	14	703	2,338
Cash at bank	14	93,210	27,989
		<u>136,947</u>	<u>116,433</u>
<b>Total assets</b>		<u><u>372,228</u></u>	<u><u>282,322</u></u>
<b>Equity</b>			
	15		
Share capital		4,180	4,180
Share premium		85,467	85,003
Translation and other reserves		15,538	–
Retained earnings		28,498	17,594
<b>Total equity</b>		<u>133,683</u>	<u>106,777</u>
<b>Non-current liabilities</b>			
Loans received	14	31,153	1,107
Debt securities issued	14	64,910	47,050
Deferred revenue	16	67,414	31,861
Deferred tax liabilities	9	–	2,358
Retention payable to general contractor	14	1,376	3,198
		<u>164,853</u>	<u>85,574</u>
<b>Current liabilities</b>			
Loans received	14	11,665	2,179
Debt securities issued	14	38,167	1,258
Deferred revenue	16	10,511	72,577
Current income tax liabilities		3,127	1,484
Trade and other payables	14	3,821	6,533
Retention payable to general contractor	14	564	2,073
Other current liabilities		5,837	3,867
		<u>73,692</u>	<u>89,971</u>
<b>Total liabilities</b>		<u>238,545</u>	<u>175,545</u>
<b>Total equity and liabilities</b>		<u><u>372,228</u></u>	<u><u>282,322</u></u>

\*Please refer to Note 3.1.

The accompanying notes on pages 5-29 are an integral part of these consolidated financial statements.



## Consolidated statement of changes in equity

For the year ended 31 December

*(Thousands of Georgian Lari)*

	<i>Share capital</i>	<i>Pooling reserve</i>	<i>Share premium</i>	<i>Translation and other reserves</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 1 January 2015	2,782	742	71,813	–	4,514	79,851
Total comprehensive income for the year	–	–	–	–	13,080	13,080
Share issue	742	(742)	–	–	–	–
Contribution of assets by entities under common control	656	–	10,987	–	–	11,643
Share based payments (Note 15)	–	–	2,203	–	–	2,203
At 31 December 2015	<u>4,180</u>	<u>–</u>	<u>85,003</u>	<u>–</u>	<u>17,594</u>	<u>106,777</u>
Total comprehensive income for the year	–	–	–	15,538	10,904	26,442
Compensation to the ultimate parent for acquired treasury shares	–	–	(2,613)	–	–	(2,613)
Share based payments (Note 15)	–	–	3,077	–	–	3,077
At 31 December 2016	<u><u>4,180</u></u>	<u><u>–</u></u>	<u><u>85,467</u></u>	<u><u>15,538</u></u>	<u><u>28,498</u></u>	<u><u>133,683</u></u>

The accompanying notes on pages 5-29 are an integral part of these consolidated financial statements.

## Consolidated statement of cash flows

For the year ended 31 December

*(Thousands of Georgian Lari)*

	Notes	2016	2015
Operating activities			
Profit before income tax expense		14,377	15,878
<i>Non-cash adjustments to reconcile profit before income tax expense to operating profit before changes in working capital</i>			
(Gain)/loss from foreign exchange differences on financing and investing activities		(2,553)	(16,702)
Loss from foreign exchange differences		(3,408)	836
Depreciation	12	243	185
Finance income		(715)	(386)
Finance expense		210	1,030
Share based payments		192	112
Other		44	3
Operating profit before changes in working capital		<u>8,390</u>	<u>956</u>
<i>Working capital adjustments</i>			
Change in inventory property		23,682	(15,964)
Change in deferred revenue		(34,845)	29,401
Change in retention payable to the constructor		(3,993)	2,555
Change in prepayments and other current and non-current assets		746	(19,677)
Change in trade and other payables and other current liabilities		(1,909)	2,260
Change in trade and other receivables		1,565	(1,837)
Cash flows used in operations		<u>(6,364)</u>	<u>(2,306)</u>
Interest received		715	386
Interest paid		(6,784)	(6,299)
Income tax paid		(297)	(1,566)
Net cash flows (used in) / from operating activities		<u>(12,730)</u>	<u>(9,785)</u>
Investing activities			
Acquisition of investment property	10	(2,281)	(11,075)
Proceeds from sale of investment property		1,606	-
Capital expenditures on investment property	10	(1,076)	(2,546)
Acquisition of property and equipment		(3,602)	(584)
Capital expenditures on investment property under construction	10	(1,253)	(937)
Acquisition of investment securities available for sale		(479)	(729)
Redemption of bank deposits		-	13,101
Net cash flows used in investing activities		<u>(7,085)</u>	<u>(2,770)</u>
Cash flows from financing activities			
Proceeds from debt securities issued		57,649	44,707
Repayment of debt securities issued		(15,220)	(33,972)
Proceeds from borrowings		39,724	-
Compensation to the ultimate parent for acquired treasury shares		(2,613)	-
Repayment from borrowings		(2,238)	-
Net cash flows from financing activities		<u>77,302</u>	<u>10,735</u>
Effect of exchange rate changes on cash and cash equivalents		7,734	5,912
Net increase in cash and cash equivalents		<u>65,221</u>	<u>4,092</u>
Cash and cash equivalents at 1 January	14	27,989	23,897
Cash and cash equivalents at 31 December	14	<u>93,210</u>	<u>27,989</u>

## Material non-cash transactions

In 2016 year the Group incurred borrowings costs with total amount GEL 9,098 (2015: 6,419) of which GEL 3,990 (2015: 3,639) has been capitalized as a part of investment property, GEL 4,898 (2015: 1,750) was capitalized as a part of inventory property and GEL 210 (2015: 1,030) recognized in the consolidated statement of comprehensive income.

The Group incurred employee share based compensation expenses with total amount of GEL 3,396 (2015: 2,628) of which GEL 3,204 (2015: 2,516) has been capitalized as a part of inventory property and GEL 192 (2015: 112) recognized in the consolidated statement of comprehensive income.

In 2016 land and buildings with total amount of GEL 17,470 was transferred from investment property to inventory property. In 2015 commercial properties of GEL 937 were transferred from inventory property to investment property.

In 2016 land and building with total amount of GEL 1,572 were transferred from investment property to property and equipment.

*The accompanying notes on pages 5-29 are an integral part of these consolidated financial statements.*

(Thousands of Georgian Lari)

## 1. Background

JSC m2 Real Estate (the "Company") is a joint stock company incorporated on 27 September 2006. The legal address of the Company is 29, I. Chavchavadze Ave, 0179, Tbilisi, Georgia. The Company, together with subsidiaries indicated in this note, is referred to as the "Group". Historically, the Group's principal activities included development and sales of mainly residential apartments and investment property management. In 2016 the Company made a strategic decision to expand into hospitality business and initiated construction of two hotels in Georgia.

JSC BGEO Investments is a 100% shareholder of the Company. The Group is ultimately owned and controlled by the BGEO Group PLC ("the BGEO"). The BGEO is incorporated in the United Kingdom and listed on the London Stock Exchange.

The Group included the following subsidiaries:

<i>Subsidiary</i>	<i>31 December 2016</i>	<i>31 December 2015</i>	<i>Country</i>	<i>Date of incorporation</i>	<i>Industry</i>
LLC Tamarashvili 13	100.00%	100.00%	Georgia	3 November 2011	Real estate
LLC m2 at Kazbegi	100.00%	100.00%	Georgia	21 May 2013	Real estate
LLC m2 at Nutsubidze	100.00%	100.00%	Georgia	21 May 2013	Real estate
LLC m2 at Tamarshvili	100.00%	100.00%	Georgia	21 May 2013	Real estate
LLC m2 at Hippodrome	100.00%	100.00%	Georgia	6 July 2015	Real estate
LLC m2 Skyline	100.00%	100.00%	Georgia	24 July 2015	Real estate
LLC M Square Park	100.00%	100.00%	Georgia	15 September 2015	Real estate
LLC Optima Saburtalo	100.00%	100.00%	Georgia	15 September 2015	Real estate
LLC Optima Isani	100.00%	100.00%	Georgia	25 July 2014	Real estate
LLC M2	100.00%	100.00%	Georgia	12 February 2014	Hospitality/Real estate
LLC m2 Residential	100.00%	100.00%	Georgia	17 August 2015	Real estate
LLC m2 Hospitality	100.00%	100.00%	Georgia	17 August 2015	Hospitality/Real estate
LLC Caucasus Autohouse	100.00%	100.00%	Georgia	29 March 2011	Real estate
LLC Land	100.00%	100.00%	Georgia	3 October 2014	Real estate
LLC m2 at Vake	100.00%	–	Georgia	3 August 2016	Real estate
LLC m2 at Chavchavadze	100.00%	–	Georgia	5 September 2016	Real estate
LLC m2 Commercial Properties	100.00%	–	Georgia	1 March 2016	Property management

## 2. Basis of preparation

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

The consolidated financial statements have been prepared on a historical cost basis, except for investment property and investment securities available for sale, which are carried at fair value.

The consolidated financial statements are presented in Georgian Lari and all values are rounded to the nearest thousand except as otherwise indicated.

### 3.1. Summary of significant accounting policies

#### Adoption of new or revised standards and interpretations

No new or revised IFRS during the year had an impact on the Group's financial position or performance.

The Group has not early adopted any standard, interpretation or amendment that has been issued but is not yet effective. The accounting policies adopted in the preparation of the consolidated financial statements are consistent with those followed in the preparation of the Group's consolidated financial statements for the year ended 31 December 2015, except of changes in assessment of the Group's functional currency and certain reclassifications discussed below.

(Thousands of Georgian Lari)

## 3.1. Summary of significant accounting policies (continued)

## Reclassifications

During year ended 31 December 2016 the Group reconsidered presentation of its consolidated statement of financial position accounts for the purpose of more accurate presentation of property and equipment. The presentation of comparative figures has been adjusted to confirm to the presentation of the current year amounts:

<i>Affected item of the consolidated statement of financial position as of 31 December 2015</i>	<i>As previously reported</i>	<i>Reclassification</i>	<i>As reclassified</i>
Property and equipment, net	–	1,370	1,370
Prepayments and other assets	20,409	(1,370)	19,039

## Functional and presentation currencies

In 2016 the Group performed a re-assessment of its functional currency in accordance with International Accounting Standard 21 - *Effects of Changes in Foreign Exchange Rates* (IAS 21) and determined that US Dollar ("USD") was its functional currency, due to the following:

- ▶ Continued volatility in USD/GEL exchange rate, exposing deep Dollarization of the Georgian economy and reversing the slow de-Dollarization trend;
- ▶ Revenue streams are becoming more diversified and predominantly denominated in USD. During the second half of 2016, the Group entered the new business line, hotel business, and initiated three hotel construction projects, of which, two started during the second half of 2016. Revenues in hotel business in Georgia are denominated in USD. In addition, the Group's portfolio of yielding assets - leased out commercial spaces - increased significantly during the second half of 2016;
- ▶ Share of the Group's borrowings denominated in USD is constantly increasing;
- ▶ Communication, planning, execution and reporting of the Group's business activities to the stakeholders have predominantly moved into USD.

As the result, the Group changed its functional currencies, from Georgia Lari ("GEL") to USD starting 1 October 2016 and this has been accounted for prospectively from that date. Share capital, share premium, retained earnings, assets and liabilities of the Group were translated to USD based on GEL-USD exchange rate of 2.3297 on 1 October 2016. Subsequently, share capital and share premium are maintained at the same historical rate. If GEL remained functional currency of the Group, revenue from sale of inventory property and net income would be GEL 96,208 and GEL 3,816 respectively.

As discussed above, the Group's functional currency was GEL before 1 October 2016, and USD thereafter. 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 into functional currency at functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are charged to consolidated income statement to net foreign exchange gain/(loss). Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Differences between the contractual exchange rate of a certain transaction and official exchange rate of the National Bank of Georgia ("NBG") on the date of the transaction are included in net foreign exchange gain/loss.

In accordance with statutory requirement the Group's presentation currency is GEL. Items in the consolidated financial statements are translated to presentation currency based on following principles: assets and liabilities are translated into GEL at the rate of exchange ruling at the reporting date, income and expenses are translated at the exchange rates at the dates of the transactions (or at the average rate for the period when this is a reasonable approximation) and equity components are maintained at the rate of exchange ruling at the date of change in functional currency. The exchange differences arising on the translation are taken to other comprehensive income.

The official NBG exchange rates at 31 December 2016 and 31 December 2015 were 2.6468 and 2.3949 GEL to 1 USD, respectively.

(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Basis of consolidation

Subsidiaries, which are those entities which are controlled by the Group, are consolidated. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee;
- The ability to use its power over the investee to affect its returns.

Generally, there is a presumption that a majority of voting rights results in control. To support this presumption and when the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement(s) with the other vote holders of the investee;
- Rights arising from other contractual arrangements;
- The Group's voting rights and potential voting rights.

Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealised gains on transactions between group companies are eliminated in full; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognises the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests; recognises the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss.

#### Common control business combinations

Combinations of businesses under common control are accounted for using the pooling of interest method. Under this method, amounts are presented in the financial statements after the business combination as combined amounts of the two entities from the beginning of the earliest period presented. Assets and liabilities of an acquired entity are recognised in the financial statements of a combined entity similarly to consolidation of the corresponding items of a subsidiary in the financial statements of a parent company after eliminating all intergroup balances and transactions. Any difference between the combined amounts and consolidated amounts of assets and liabilities determined under the pooling of interest method is recognised as changes in equity. No goodwill arises on the combination of businesses under common control accounted for under the pooling of interest method.

#### Revenue recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duty. The Group has concluded that it is the principal in all of its revenue arrangements since it is the primary obligor in all of the revenue arrangements, it has pricing latitude and is also exposed to inventory and credit risks.

The specific recognition criteria described below must also be met before revenue is recognized.

#### *Rental income*

The Group is the lessor in operating leases. Rental income arising from operating leases on investment property is accounted for on a straight-line basis over the lease terms and is included in revenue in the income statement due to its operating nature.

(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Revenue recognition (continued)

##### *Sales of inventory property*

Sales of inventory property agreements are considered as an arrangements for sale of goods thus respective revenue from sale of inventory is recognized when all of the following conditions are satisfied:

- The entity has transferred to the buyer the significant risks and rewards of ownership of the goods;
- The entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the entity; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

It is the Group's common practice to market developments before the start of construction and this activity then continues throughout the construction period. A typical arrangement will involve a buyer entering into a sales agreement with a developer to acquire a specific unit upon completion of construction. In certain cases, respective conditions are met before the transfer of legal ownership on an inventory property to a buyer is completed.

#### Finance income

Finance income is recognized as it accrues using the effective interest rate (EIR) method. EIR is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability. Finance income is included in finance income in the income statement.

#### Taxation

Current income tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date in Georgia.

Deferred tax assets and liabilities are calculated in respect of temporary differences using the liability method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are re-assessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the reporting date.

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

Georgia also has various operating taxes that are assessed on the Group's activities. These taxes are included as a component of other general and administrative expenses.

(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Investment property

Investment property includes buildings held for earning rental income and land plots held for a currently undetermined future use or with a view of future redevelopment for future use as investment property.

Investment property is measured initially at cost including transaction costs. Transaction costs include transfer taxes, professional fees for legal services and initial leasing commissions to bring the property to the condition necessary for it to be capable of operating. The carrying amount also includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met and borrowing costs.

Subsequent to initial recognition, investment property is stated at fair value. Gains or losses arising from changes in the fair values are charged to profit or loss in the year in which they arise.

Transfers are made to investment property when, and only when, there is a change in use, evidenced by commencement of an operating lease. Transfers are made from investment property when, and only when, there is a change in use, evidenced by commencement of development with a view to sale.

#### Investment property under construction

Units of commercial spaces in construction projects in progress that are designated for renting out are classified as investment property under construction and are carried at cost as fair value of such units cannot be reliably estimated until completion of the construction.

#### Property and equipment

Property and equipment are carried at cost less accumulated depreciation and any accumulated impairment in value. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. Impairment losses are recognised in the consolidated profit or loss as an expense.

Depreciation of an asset begins when it is available for use. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Buildings	100
Furniture and fixtures	5-10
Computers and other office equipment	5
Motor vehicles	5

The asset's residual value, useful life and methods are reviewed, and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in general and administrative expenses unless they qualify for capitalization.

An item of property and equipment is derecognised upon disposal or when no further future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognizing of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated profit or loss in the period the asset is derecognised.

Assets under construction comprises costs directly related to construction of property and equipment including an appropriate allocation of directly attributable variable and fixed overheads that are incurred in construction. Depreciation of these assets, on the same basis as similar property assets, commences when the assets are ready for use.

Leasehold improvements are amortized over the life of the related leased asset.

(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Operating leases

Where the Group is a lessor in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Group, the total lease payments are charged to profit or loss on a straight-line basis over the lease term.

#### Financial assets

##### *Initial recognition*

Financial assets in the scope of IAS 39 are classified as either loans and receivables or available for sale financial assets, as appropriate. When financial assets are recognized initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets upon initial recognition.

##### *Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortized cost using the effective interest rate (EIR) method, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortization is included in finance income in the statement of profit or loss.

Rent and other receivables are recognized at their original invoiced value. Where the time value of money is material, receivables are carried at amortized cost.

##### *Available for sale financial assets*

Available for sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified in any of the preceding categories. After initial recognition available for sale financial assets are measured at fair value with unrealized gains or losses being recognized in other comprehensive income until the investment is derecognized or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is charged to profit or loss.

#### Fair value measurements

The Group measures certain financial instruments such as investment securities available for sale, and non-financial assets such as investment property, at fair value at the end of each reporting period. Also, fair values of financial instruments measured at amortized cost are disclosed in the financial statements.

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 fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The Group is able to access the principal or the most advantageous market at the measurement date.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.



(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Fair value measurements (continued)

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs significant to the fair value measurement as a whole:

- Level 1 – quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- Level 2 – valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;
- Level 3 – valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

Fair value of assets included in Level 3 of the fair value hierarchy may be subject to change once and if observable relevant transactions are available.

For assets and liabilities that are recognized in the financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

#### Financial liabilities

Financial liabilities that the Group has, including short-term loan received, trade and other payables and retention payable to general contractor, are initially recognized at fair value plus directly attributable transaction costs.

After initial recognition, these are measured at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

#### Inventory property

Property acquired or being constructed for sale in the ordinary course of business, rather than to be held for rental or future redevelopment, is held as inventory and is measured at the lower of cost and net realisable value. Cost includes:

- Cost of land; when land is reclassified from investment property its fair value as of reclassification date regarded as its cost;
- Amounts payable to the contractor for construction;
- Borrowing costs, planning and design costs, costs of site preparation, professional fees for legal services, insurance expenses, construction overheads, administrative overheads and other related costs.

Net realisable value is the estimated selling price in the ordinary course of the business, based on market prices at the reporting date and discounted for the time value of money if material, less costs to completion and the estimated costs of sale.

The cost of inventory recognised in profit or loss on disposal is determined with reference to the specific costs incurred on the property sold and an allocation of any non-specific costs based on the relative size of the property sold.

#### Prepayments

Prepayments are carried at cost less provision for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group.

(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Share-based payment transactions

Senior executives of the Group receive share-based remuneration settled in equity instruments of the Group's ultimate parent, the BGEO. Grants are made by both the BGEO and the Group. Grants that the Group does not have a liability to settle as accounted as equity-settled transactions (even if the Group may subsequently recharge the cost of the award to the settling entity, which is recognized as equity deduction at respective payment date). Other grants are accounted for as cash-settled transactions.

#### *Equity-settled transactions*

The cost of equity settled transactions with employees is measured by reference to the fair value at the date on which they are granted.

The cost of equity settled transactions is recognized together with the corresponding increase in additional paid in capital, over the period in which the performance and/or service conditions are fulfilled, ending on the date when the relevant employee is fully entitled to the award ("the vesting date"). The cumulative expense recognized for equity settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group's best estimate of the number of equity instruments that will ultimately vest. Settlements to the Parent for the shares granted to the employees of the Group are accounted as a reduction in share premium.

#### *Cash-settled transactions*

The cost of cash-settled transactions is measured initially at fair value at the grant date based on market. This fair value is expensed over the period until the vesting date with recognition of a corresponding liability. The liability is re-measured to fair value at each reporting date up to, and including the settlement date, with changes in fair value recognized in employee benefits expense.

#### Segment reporting

As at 31 December 2016, the chief operating decision maker evaluates the whole Group as a single operating segment, real estate business. The chief operating decision maker evaluates performance based on revenue, profit before tax and net profit measured in accordance with IFRS. Segment assets and liabilities are measured in accordance with IFRS.

All of Group's assets and liabilities are concentrated in Georgia and revenue from external customers is received from the operations in Georgia. There were no external customers that accounted for more than 10% of Group's revenue in 2016 and 2015.

#### Share capital

##### *Ordinary shares*

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction from the proceeds in equity. Any excess of the fair value of consideration received over the par value of shares issued is recognised as share premium.

##### *Contribution of assets*

The Parent or entities under common control, from time to time, contributes land plots and buildings to the capital of the Group in exchange for the Company's shares. The Group measures the property received, and the corresponding increase in equity at the fair value of the land plots and buildings received.

#### Borrowing costs

Borrowing costs comprise interest expense calculated using the effective interest method and exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

Borrowing costs directly attributable to the acquisition or construction of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of the respective assets. All other borrowing costs are expensed in the period in which they occur.

(Thousands of Georgian Lari)

### 3.1. Summary of significant accounting policies (continued)

#### Borrowing costs (continued)

As the Group borrows funds specifically for the purpose of each development project, amount of borrowing costs eligible for capitalisation is determined as the actual borrowing costs incurred on that borrowing during the period of property development phase.

#### Operational cycle

The Group's normal operating cycle is not clearly identifiable therefore it is assumed to be twelve months. Assets and liabilities are classified as current if they are expected to be realised or settled within twelve months after the reporting date. All other assets and liabilities are classified as non-current.

### 3.2. Significant accounting judgements, estimates and assumptions

The preparation of the Group's financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent liabilities, at the reporting date. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

#### Judgements other than estimates

In the process of applying the Group's accounting policies, management has made the following judgements, which have the most significant effect on the amounts recognised in the consolidated financial statements:

##### *Classification of property*

The Group determines whether a property is classified as investment property, inventory property or property, plant and equipment:

- Investment property comprises land and buildings (principally offices and retail property) that are not occupied substantially for use by, or in the operations of, the Group, nor for sale in the ordinary course of business, but are held primarily to earn rental income, capital appreciation or for future redevelopment before exact details of use are not yet determined;
- Inventory property comprises property that is held for sale in the ordinary course of business. Principally, this is residential property that the Group develops and intends to sell before or on completion of construction.
- Property, plant and equipment comprises owner occupied buildings, office furniture and fixtures, computer equipment, transport and leasehold improvements used to support Group's ordinary business activities.

#### Estimates

##### *Measurement of fair value of investment properties*

The fair value of investment properties is determined by independent professionally qualified appraisers. Fair value is determined using a combination of the internal capitalization method (also known as discounted future cash flow method) and the sales comparison method.

The Group performs valuation of its investment properties with a sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. Results of this valuation, as well as valuation inputs and techniques are presented in note 10. While the secondary market in Georgia provides adequate market information for fair value measurements for small and medium sized properties, valuation of large and unique properties involves application of various observable and unobservable inputs to determine adjustments to the available comparable sale prices. These estimates and assumptions are based on the best available information, however, actual results could be different.

(Thousands of Georgian Lari)

#### 4. Standards issued but not yet effective

Up to the date of approval of the consolidated financial statements, certain new standards, interpretations and amendments to existing standards have been published that are not yet effective for the current reporting period and which the Group has not early adopted. Such standards that are expected to have an impact on the Group, or the impacts of which are currently being assessed are as follows:

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

IFRS 15 was issued in May 2014 and establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The new revenue standard will supersede all current revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application is required for annual periods beginning on or after 1 January 2018, when the IASB finalises their amendments to defer the effective date of IFRS 15 by one year. Early adoption is permitted.

The Company made IFRS 15 impact assessment and elected early adoption of new revenue recognition standard from 1 January 2017 using modified retrospective method, according to which cumulative effect of initially applying the standard will be recognized as at 1 January 2017, the initial application date. Thus 2017 opening balances will be adjusted for the contracts that were not completed as of 1 January 2017.

The management performed the analysis and concluded that the Group satisfies performance obligation per IFRS 15 and shall recognise revenue from sale of inventory property over time. As a result, as of 1 January 2017 the Company will start recognising revenue from sale of inventory property during the property construction period. The Group is currently assessing the impact of IFRS 15 on its consolidated financial statements.

##### *IFRS 9 Financial Instruments*

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* that replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions. The Group is currently assessing the impact of IFRS 9.

##### *IAS 7 Disclosure Initiative – Amendments to IAS 7*

The amendments to IAS 7 *Statement of Cash Flows* are part of the IASB's *Disclosure Initiative* and require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. On initial application of the amendment, entities are not required to provide comparative information for preceding periods. These amendments are effective for annual periods beginning on or after 1 January 2017, with early application permitted. Application of amendments will result in additional disclosure provided by the Group.

##### *IFRS 16 Leases*

IFRS 16 was issued in January 2016 and it replaces IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement Contains a Lease*, SIC-15 *Operating Leases-Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

*(Thousands of Georgian Lari)*

## 4. Standards issued but not yet effective (continued)

*IFRS 16 Leases (continued)*

Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under IFRS 16 is substantially unchanged from today's accounting under IAS 17. Lessors will continue to classify all leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases.

IFRS 16 also requires lessees and lessors to make more extensive disclosures than under IAS 17.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted, but not before an entity applies IFRS 15. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. The standard's transition provisions permit certain reliefs.

The Group is currently assessing the impact of IFRS 16 on its consolidated financial statements.

Other standards and interpretations issued but not yet effective are not expected to have an impact on the Group.

## 5. Revenue

	<u>2016</u>	<u>2015</u>
Revenue from the sale of inventory property		
Residential area	91,755	43,792
Commercial area	1,273	461
Parking lot area	3,319	640
	<u>96,347</u>	<u>44,893</u>
Rental income	2,778	1,785
Other revenue	191	285
Revenue	<u><u>99,316</u></u>	<u><u>46,963</u></u>

## 6. Cost of sales – inventory property

	<u>2016</u>	<u>2015</u>
Residential area cost of sales	75,291	37,352
Commercial area cost of sales	703	228
Parking lot cost of sales	6,409	2,164
Total cost of sales	<u><u>82,403</u></u>	<u><u>39,744</u></u>

## 7. Salary and employee benefits expenses

	<u>2016</u>	<u>2015</u>
Share-based compensation expense	3,396	2,628
Salary and other employee benefits	2,092	1,623
Cash bonus	1,203	870
Total employee benefits	<u><u>6,691</u></u>	<u><u>5,121</u></u>
Employee benefits expense	1,498	943
Employee benefits capitalized in inventory (Note 11)	5,193	4,178
Total employee benefits	<u><u>6,691</u></u>	<u><u>5,121</u></u>

*(Thousands of Georgian Lari)*

## 8. Other general and administrative expenses

	<u>2016</u>	<u>2015</u>
Rent	594	711
Legal and other professional services	362	401
Corporate hospitality	238	43
Office supplies	175	192
Operating taxes	126	43
Utility	112	65
Repair and maintenance	110	41
Security	87	131
Communication	75	92
Insurance	64	84
Personnel training and recruitment	53	65
Charity	–	167
Other expenses	30	41
Total other general and administrative expenses	<u>2,026</u>	<u>2,076</u>

## 9. Income tax

Georgian legal entities must individually file tax declarations. The statutory corporate income tax rate applicable to the Group's income was 15% in years ended 31 December 2016 and 31 December 2015.

Income tax expense of GEL 3,473 (2015: 2,798) for the year ended 31 December 2016 comprised of deferred tax expense of GEL 346 (2015: deferred tax expense of GEL 1,826) and of current income tax expense of GEL 3,127 (2015: GEL 972).

In May 2016, the parliament of Georgia approved a change in the current corporate taxation model which is applicable starting from 1 January 2017 for the Group. The new model implies zero rate on retained earnings and 15% tax rate on distributed earnings. The Group considers that the new regime was substantively enacted in 2016 and thus has re-measured its deferred tax assets and liabilities and fully wrote them off to the income tax expense as of 31 December 2016.

The effective income tax rate differs from the statutory income tax rates. As at 31 December 2016 and 2015 a reconciliation of the income tax expense based on statutory rates with the actual expense is as follows:

	<u>2016</u>	<u>2015</u>
Profit before income tax expense	14,377	15,878
Statutory tax rate	15%	15%
Theoretical income tax expense	<u>(2,157)</u>	<u>(2,382)</u>
Georgian tax code change effect	(1,412)	–
Non-deductible expenses less non-taxable income	96	(41)
Expiration of tax losses carried forward	<u>–</u>	<u>(375)</u>
Income tax expense	<u>(3,473)</u>	<u>(2,798)</u>

(Thousands of Georgian Lari)

## 9. Income tax (continued)

Deferred tax assets and liabilities as at 31 December 2016 and 31 December 2015 and their movements for the respective years is as follows:

	1 January 2015	Origination and reversal of temporary differences in statement of comprehen- sive income	31 December 2015	Origination and reversal of temporary differences in statement of comprehen- sive income	31 December 2016
Tax effect of deductible temporary differences					
Inventory property	814	4,776	5,590	(5,590)	–
Trade and other receivables	6	(6)	–	–	–
Tax loss carry forward	2,040	504	2,544	(2,544)	–
Trade and other payables	104	–	104	(104)	–
Gross deferred tax asset	<u>2,964</u>	<u>5,274</u>	<u>8,238</u>	<u>(8,238)</u>	<u>–</u>
Tax effect of taxable temporary differences					
Investment property	(1,112)	(2,505)	(3,617)	3,617	–
Deferred revenue	320	(4,329)	(4,009)	4,009	–
Trade and other receivables	–	(266)	(266)	266	–
Deferred tax liability	<u>(792)</u>	<u>(7,100)</u>	<u>(7,892)</u>	<u>7,892</u>	<u>–</u>
Net deferred tax asset/(liability)	<u>2,172</u>	<u>(1,826)</u>	<u>346</u>	<u>(346)</u>	<u>–</u>

## 10. Investment property and investment property under construction

## Investment property

The table below shows movements in investment property during 2016:

	2016			
	Retail properties	Land	Other	Total
At 1 January	50,091	59,105	659	109,855
Acquisitions	2,281	–	–	2,281
Net gain from revaluation	2,553	–	–	2,553
Capital expenditure	1,076	–	–	1,076
Borrowing costs	102	3,888	–	3,990
Disposals	(1,648)	–	–	(1,648)
Transfer to property and equipment (Note 12)	–	(1,572)	–	(1,572)
Transfer to inventory property (Note 11)	(5,617)	(11,853)	–	(17,470)
Currency translation effect	6,330	6,957	87	13,374
At 31 December	<u>55,168</u>	<u>56,525</u>	<u>746</u>	<u>112,439</u>

The table below shows movements in investment property during 2015:

	2015			
	Retail properties	Land	Other	Total
At 1 January	24,538	38,086	689	63,313
Contribution to share capital	11,643	–	–	11,643
Acquisitions	2,977	8,098	–	11,075
Net gain/(loss) from revaluation	7,502	9,230	(30)	16,702
Capital expenditure	2,494	52	–	2,546
Borrowing costs	–	3,639	–	3,639
Transfer from inventory property (Note 11)	937	–	–	937
At 31 December	<u>50,091</u>	<u>59,105</u>	<u>659</u>	<u>109,855</u>

(Thousands of Georgian Lari)

## 10. Investment property and investment property under construction (continued)

### Investment property (continued)

As of 31 December 2015 included in investment property are units of commercial space under construction amounting to GEL 937 that were reclassified from inventory property due to change in the Group's intention of future use. In 2016, the properties were completed and are kept for earning rental income. As at 31 December 2016, investment property under construction is presented as a separate line item in the consolidated statement of financial position.

Retail properties represent office buildings rented out. Included into other investment properties are the buildings not rented out but held for capital appreciation purposes. Most of Group's investment properties are located in Tbilisi, Georgia as at 31 December 2016 and 2015.

As at 31 December 2016, investment property of GEL 75,602 (2015: 4,823) was pledged as collateral under the loans received from international financial institution and Georgian banks (Note 14).

### Fair value measurement of investment property

Investment properties are stated at fair value. The fair value represents the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. The date of latest valuation performed by independent appraiser is 31 December 2016. The valuation was performed by an accredited independent valuator with a recognized and relevant professional qualification and with recent experience in the locations and categories of the investment property being valued. The valuation models in accordance with those recommended by the International Valuation Standards Committee have been applied and are consistent with the principles in IFRS 13. Investment property valuation belongs to Level 3 of fair value hierarchy.

Market comparison and income approaches were used to value the investment properties.

#### *Market comparison approach*

This method is based on the direct comparison of the subject property to another property object, which has been sold or has been entered on the sale registry. Adjustments to value are determined based on the following considerations in the order of priority: 1) funding conditions; 2) sale conditions; 3) market conditions; 4) location; and 5) physical indices.

#### *Income approach*

Income approach is a valuation method that appraisers and real estate investors use to estimate the value of income producing real estate. It is based upon the premise of anticipation i.e., the expectation of future benefits. Under the income approach, the value of property is estimated based on the income that the property can be expected to generate. Income capitalization converts anticipated cash flows into present value by "capitalizing" net operating income by a market derived "capitalization rate". A capitalization rate is a rate of return on investment. It is used by real estate investors as a benchmark for determining how much they should pay for a property.



(Thousands of Georgian Lari)

## 10. Investment property and investment property under construction (continued)

## Fair value measurement of investment property (continued)

For the purpose of fair value disclosures, the Group identified three classes of investment properties – retail properties, land and other properties. The following table shows descriptions of significant unobservable inputs to valuation as well as sensitivity of the inputs:

<i>Class of investment properties</i>	<i>Fair value 2016</i>	<i>Valuation technique</i>	<i>Significant unobservable inputs</i>	<i>Range (weighted average)</i>	<i>Type</i>	<i>Total area, square meters</i>	<i>Sensitivity of the input to fair value, GEL</i>
Retail properties	39,596	Market approach	Price per square meter, GEL	0.1-3.4 (0.1)	Building Land	21,511 273,130	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
	15,572	Market approach;	Rent price per square meter, USD	8-19.8 (11.3)	Building	1,725	Increase (decrease) in the rent rate per square meter or decrease (increase) in the capitalization rate would result in increase (decrease) in fair value
		Income approach	Capitalization rate	9.00%-10.0% (9.12%)			
Land	56,525	Market approach	Price per square meter, GEL	0.1-1.3 (0.4)	Land	135,565	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Other	746	Market approach	Price per square meter, GEL	0.06-0.09 (0.07)	Building Land	489 10,766	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Total	<u>112,439</u>					<u>443,186</u>	

<i>Class of investment properties</i>	<i>Fair value 2015</i>	<i>Valuation technique</i>	<i>Significant unobservable inputs</i>	<i>Range (weighted average)</i>	<i>Type</i>	<i>Total area, square meters</i>	<i>Sensitivity of the input to fair value, GEL</i>
Retail properties	40,513	Market approach	Price per square meter, GEL	0.1-3.4 (0.2)	Building Land	22,755 273,388	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
	7,840	Income approach;	Rent price per square meter, USD	15.5-37 (35)	Building	3,384	Increase (decrease) in the rent rate per square meter or decrease (increase) in the capitalization rate would result in increase (decrease) in fair value
		market approach	Capitalization rate	10.0%-11.2% (10.7%)			
Land	59,105	Market approach	Price per square meter, GEL	0.1-7.1 (0.4)	Land	155,036	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Other	659	Market approach	Price per square meter, GEL	0.05-0.08 (0.05)	Building Land	489 10,766	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Total	<u>108,117</u>					<u>465,818</u>	

As of 31 December 2015 included in investment property were units of commercial space under construction amounting to GEL 1,738 that are measured at cost due to inability to determine their fair value reliably during construction stage. In 2016, the properties were completed and gain on revaluation at the date of completion was recognized in the consolidated statement of comprehensive income. As at 31 December 2016, investment property under construction is presented as a separate line item in the consolidated statement of financial position.

*(Thousands of Georgian Lari)*

## 10. Investment property and investment property under construction (continued)

## Investment property under construction

A summary of movement in investment property under construction is set out below:

	<i>Investment property under construction</i>
Balance at 1 January 2016	–
Capital expenditure	1,253
Currency translation effect	137
Balance at 31 December 2016	<u>1,390</u>

## 11. Inventory property

The carrying amount of inventory property allocated to each of the Group's projects is as follows:

	<u>2016</u>	<u>2015</u>
New Hippodrome	50,439	20,583
Skyline	–	6,182
Optima Saburtalo	7,557	6,156
Kazbegi ave. 15	28,313	–
Chavchavadze ave. 50	8,796	–
Non-current inventory property	<u>95,105</u>	<u>32,921</u>
Chubinasvili 69	59	67
Tamarashvili st. 13	193	2,550
Kazbegi ave. 25	25	19,677
Nutsubidze (Vazha Pshavela ave. 71)	–	6,737
Tamarashvili st. 06	1,431	21,931
Skyline	12,165	–
Optima Isani	4,031	14,152
Current inventory property	<u>17,904</u>	<u>65,114</u>
Inventory property	<u>113,009</u>	<u>98,035</u>

A summary of movement in inventory property is set out below:

	<u>2016</u>	<u>2015</u>
Balance at 1 January	98,035	77,311
Land and building transferred from investment property (Note 10)	17,470	–
Transfer from prepayments and other assets	3,497	–
Construction costs incurred	53,624	55,477
Borrowing costs	4,898	1,750
Employee benefits capitalized (Note 7)	5,193	4,178
Inventory reclassified to investment property (Note 10)	–	(937)
Currency translation effect	12,695	–
Disposals recognized in cost of sales (Note 6)	(82,403)	(39,744)
Balance at 31 December	<u>113,009</u>	<u>98,035</u>

As of 31 December 2016 the Group had commitments of GEL 197,530 (2015: GEL 137,731) relating to completion of four construction projects (2015: five construction projects).

(Thousands of Georgian Lari)

## 12. Property and equipment

The movements in property and equipment were as follows:

	<i>Buildings</i>	<i>Furniture and fixtures</i>	<i>Computers</i>	<i>Motor vehicles</i>	<i>Leasehold improvements</i>	<i>Assets under construction</i>	<i>Total</i>
Gross book value							
1 January 2015	36	307	566	108	282	-	1,299
Additions	6	62	216	61	759	-	1,104
Disposals	-	(2)	(1)	(7)	(327)	-	(337)
31 December 2015	42	367	781	162	714	-	2,066
Additions	30	96	68	73	345	3,215	3,827
Transfer from investment property (Note 10)	-	-	-	-	-	1,572	1,572
Disposals	-	(44)	(75)	(28)	-	-	(147)
Translation effect	6	60	103	28	143	476	816
31 December 2016	78	479	877	235	1,202	5,263	8,134
Accumulated depreciation							
1 January 2015	-	125	314	35	37	-	511
Depreciation charge	1	57	99	21	7	-	185
31 December 2015	1	182	413	56	44	-	696
Depreciation charge	1	70	89	57	26	-	243
Translation effect	4	28	75	14	24	-	145
31 December 2016	6	280	577	127	94	-	1,084
Net book value							
1 January 2015	36	182	252	73	245	-	788
31 December 2015	41	185	368	106	670	-	1,370
31 December 2016	72	199	300	108	1,108	5,263	7,050

(Thousands of Georgian Lari)

## 12. Property and equipment (continued)

As at 31 December 2016, assets under construction represents Ramada Ankori hotel, which is constructed by the Group in Kazbegi 15.

## 13. Prepayments and other assets

At 31 December prepayments and other assets comprised of the following:

	2016	2015, As reclassified
Prepayments for inventory properties	17,858	15,022
VAT prepayment	–	1,786
Intangible assets	167	84
Other non-current assets	1,272	2,147
Prepayments and other assets, non-current	<u>19,297</u>	<u>19,039</u>
Prepayments for inventory properties	1,288	6,896
VAT prepayment	18,427	11,092
Other current assets	2,573	884
Prepayments and other assets, current	<u>22,288</u>	<u>18,872</u>
Total prepayments and other assets	<u><u>41,585</u></u>	<u><u>37,911</u></u>

VAT prepayments are expected to be recovered upon completion of respective construction projects when revenue from inventory property disposal are reported in respective tax declarations.

## 14. Financial instruments

## Financial instruments overview

*Investment securities available for sale*

As of 31 December 2016 included into investment securities available for sale:

- A minority unquoted share in a company with cost of GEL 1,301 (2015: GEL 1,145) carried at cost less impairment (2015: measured at cost);
- Shares of BGEO held for settlement of the Group's cash-settled share based transactions with fair value of GEL 1,541 (2015: GEL 975). BGEO's shares are categorized within Level 1 of the fair value hierarchy (2015: Level 1).

*Loans received*

	<i>Currency</i>	<i>Maturity</i>	<i>31 December 2016</i>	<i>31 December 2015</i>
Borrowing from international financial institutions	USD	15 December 2019	39,135	–
Borrowing from local commercial bank	USD	8 July 2026	2,565	–
Borrowing from local commercial bank	GEL	23 March 2017	1,118	3,286
Total borrowings			<u><u>42,818</u></u>	<u><u>3,286</u></u>

Total interest for 2016 comprised GEL 9,098 (2015: 6,419) of which GEL 3,990 (2015: 3,639) has been capitalized as a part of investment property, GEL 4,898 (2015: 1,750) was capitalized as a part of inventory property and GEL 210 (2015: 1,030) recognized in the consolidated statement of comprehensive income.

Some borrowings are received upon certain conditions, such as maintaining different limits for leverage, capital investments, minimum amount of immovable property and others. At 31 December 2016 and 2015 the Group complied with all these lender covenants.

(Thousands of Georgian Lari)

## 14. Financial instruments (continued)

### Financial instruments overview (continued)

#### Loans received (continued)

As at 31 December 2016 the Group had undrawn loan commitment of USD 15 million (2015: USD 30 million) from international financial institution.

#### Debt securities issued

In October 2016 the Group completed issuance of 3-year local bonds of USD 25 million, registered on Georgian Stock Exchange. The bonds were issued at par carrying 7.5% coupon rate per annum with semi-annual payments. In 2016 the Group partially repaid the bonds issued in March 2015 on amount of USD 6,311. No significant gain or loss was incurred as a result of early redemption.

In March 2015 the Group completed issuance of 2-year local bonds of USD 20 million, registered on Georgian Stock Exchange. The bonds were issued at par carrying 9.5% coupon rate per annum with semi-annual payments. Starting from January 2016 coupon rate was changed to 9.025%. In 2015, the Group repaid the bonds issued in April and June 2014 at their respective maturity dates with respective amounts of USD 5 million and USD 10 million.

#### Retention payable to general contractor

Included in retention payable to general contractor as of 31 December 2016 and 2015 are performance and guarantee retentions related to the Group's ongoing construction projects.

Performance guarantee retention represents 5% of total amount due to a constructor which is retained by the Group and is due at the project completion date. It is intended to serve as a guarantee for completion of construction activities. As of 31 December 2016 current portion of performance guarantee retention comprised GEL 0 (2015: GEL 2,073) whilst non-current portion of performance guarantee retention comprised GEL 688 (2015: GEL 0)

Guarantee retention represents 5% of total amount due to a constructor which is retained by the Group and is due in one year after the project completion date. It is intended to serve as a guarantee for any subsequent faults identified in the completed project. As of 31 December 2016 current portion of guarantee retention comprised GEL 564 (2015: GEL 0) whilst non-current portion of guarantee retention comprised GEL 688 (2015: GEL 3,198).

#### Trade and other payables:

Trade and other payables of the Group are mostly comprised of construction payables for projects under development. These payables are mostly denominated in USD and are due from 3 to 6 months from the reporting date.

	<u>2016</u>	<u>2015</u>
Construction payables	3,733	5,790
Marketing and advertising	88	743
Trade and other payables	<u>3,821</u>	<u>6,533</u>

### Risks arising from financial instruments

In the course of its ordinary activity the Group is exposed to currency, interest rate, credit and liquidity risks. The Group's senior management oversees the management of these risks.

#### Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates.

The Group's currency risk and open currency position are analyzed and managed by its ultimate parent, which uses derivatives and other instruments to manage exposures resulting from changes in foreign currencies on a consolidated level of BGEO Group.

As at 31 December 2016, the Group's functional currency is USD and the Group's monetary assets and liabilities are denominated in USD except of insignificant balances in GEL. As a result, the management assessed that foreign currency risk is not significant as at 31 December 2016.

(Thousands of Georgian Lari)

## 14. Financial instruments (continued)

## Risks arising from financial instruments (continued)

*Credit risk*

Credit risk is the risk that counterparty will not meet its obligations under a financial instrument or customer contract, leading to a financial loss.

As of 31 December 2016 the Group has no other significant financial assets subject to credit risk except for:

- Cash at bank:

As at 31 December 2016 GEL 82,792 (2015: 27,983) was kept with a bank under common control having a ratings of "BB-/B" from Standard & Poor's, "B1/NP" (FC) & "Ba3/NP" (LC) from Moody's and "BB-/B" from Fitch Ratings. GEL 5,177 was kept with local commercial banks having a ratings of "B1/NP" (FC) & "Ba3/NP" (LC) from Moody's and "BB-/B" from Fitch Ratings. Remaining GEL 5,241 was kept with local commercial bank with no available credit ratings. Respective bank accounts do not bear any interest except current accounts with a bank under common control, on which annual interest 3.5% was accrued on USD accounts during the second half of 2016. The Group's cash at bank is immediately available upon demand.

- Trade and other receivables:

Trade and other receivables of the Group are mostly comprised of receivables from sale of inventory property. These receivables are mostly denominated in USD and are due from 3 to 6 months from the reporting date. No significant trade and other receivable are either past due or impaired as at 31 December 2016 and 2015.

*Liquidity risk*

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances. The Group's liquidity risk is analyzed and managed by the Group's management.

The table below summarizes the maturity profile of the Group's financial liabilities based on contractual undiscounted repayment obligations:

<i>Financial liabilities</i> <i>As at 31 December 2016</i>	<i>Less than</i> <i>3 months</i>	<i>3 to</i> <i>12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
Loans received	1,240	13,627	35,703	1,648	52,218
Trade and other payables	3,821	–	–	–	3,821
Debt securities issued	37,845	4,976	79,096	–	121,917
Retention payable to general contractor	–	564	1,376	–	1,940
<b>Total</b>	<b>42,906</b>	<b>19,167</b>	<b>116,175</b>	<b>1,648</b>	<b>179,896</b>

<i>Financial liabilities</i> <i>As at 31 December 2015</i>	<i>Less than</i> <i>3 months</i>	<i>3 to</i> <i>12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
Loans received	609	1,772	1,130	–	3,511
Trade and other payables	6,533	–	–	–	6,533
Debt securities issued	2,256	2,294	50,692	–	55,242
Retention payable to general contractor	–	2,073	3,198	–	5,271
<b>Total</b>	<b>9,398</b>	<b>6,139</b>	<b>55,020</b>	<b>–</b>	<b>70,557</b>

*Interest rate risk*

Interest rate risk arises from the possibility that changes in interest rates will affect the fair value of the financial instruments or the future cash flows on financial instruments. In 2016 the Group had floating interest rate on borrowings from international financial institution linked to LIBOR and is therefore exposed to interest rate risk. However no reasonably expected change in LIBOR would have a material impact on the consolidated income statement. In 2015 the Group was not exposed to interest rate risk.

(Thousands of Georgian Lari)

## 14. Financial instruments (continued)

## Fair value of financial instruments

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability. The Group uses the following hierarchy for determining and disclosing the fair value:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following tables show analysis of assets and liabilities measured at fair value or for which fair values are disclosed by level of the fair value hierarchy. It also includes a comparison by class of the carrying amounts and fair values of the Group's financial instruments that are carried in the financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities carried at cost:

	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total fair value 31 December 2016</i>	<i>Carrying value 31 December 2016</i>	<i>Unrecog- nised gain (loss) 31 December 2016</i>
<b>Assets measured at fair value</b>						
Investment properties	–	–	112,439	112,439	112,439	–
Investment securities available for sale	1,541	–	–	1,541	1,541	–
<b>Assets for which fair values are disclosed</b>						
Trade and other receivables	–	–	703	703	703	–
<b>Liabilities for which fair values are disclosed</b>						
Loans received	–	42,649	–	42,649	42,818	169
Debt securities issued	–	100,963	–	100,963	103,077	2,114
Trade and other payables	–	–	3,821	3,821	3,821	–
Retention payable to general contractor	–	–	1,940	1,940	1,940	–
	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total fair value 31 December 2015</i>	<i>Carrying value 31 December 2015</i>	<i>Unrecog- nised gain (loss) 31 December 2015</i>
<b>Assets measured at fair value</b>						
Investment properties	–	–	108,117	108,117	108,117	–
Investment securities available for sale	975	–	–	975	975	–
<b>Assets for which fair values are disclosed</b>						
Trade and other receivables	–	–	2,338	2,338	2,338	–
<b>Liabilities for which fair values are disclosed</b>						
Loans received	–	3,511	–	3,511	3,286	(225)
Debt securities issued	–	49,335	–	49,335	48,308	(1,027)
Trade and other payables	–	–	6,533	6,533	6,533	–
Retention payable to general contractor	–	–	5,271	5,271	5,271	–

(Thousands of Georgian Lari)

## 14. Financial instruments (continued)

### Fair value of financial instruments (continued)

For a description of the determination of fair value for investment properties and investment securities available for sale please refer to notes 10 and 14, above.

Carrying value of cash and cash equivalents as at 31 December 2016 and 2015 approximates its fair value due to short term nature (available on demand).

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

- *Assets for which fair value approximates carrying value* – For financial assets and financial liabilities that are liquid or have a short term maturity (less than three months) it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to variable rate financial instruments.
- *Fixed rate financial instruments* – The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates offered for similar financial instruments.

## 15. Equity

Ordinary shares issued and fully paid as at 31 December 2016 and 2015 were 417,994,663. Each share has a nominal value of 0.01 Georgian Lari as of 31 December 2016 and 2015.

### Capital management

The Group's objectives when managing capital (which it defines as reported net assets in its IFRS consolidated financial statements) are:

- To safeguard the Group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- To maintain sufficient size to make the operation of the Group cost-efficient.

To achieve these goals the Group performs a detailed analysis of each potential project setting an individual minimal requirement for internal rate of return considering the cost of borrowed funds and level of own capital available.

The Group was in compliance with all externally imposed capital requirements as at 31 December 2016.

### Share-based payments

In February 2016 the BGEO Remuneration Committee resolved to award 32,000 ordinary shares of BGEO to the CEO of the Group. The Group considers 12 February 2016 as the grant date. The Group estimates that the fair value of the shares awarded was GEL 57.8 per share. Shares awarded are subject to two-year vesting with continuous employment being the only vesting condition for the award. The Group does not have an obligation to settle this award but it is expected that BGEO will recharge the cost of the BGEO shares to be purchased for its settlement to the Group.

In May 2016 the Group's Supervisory Board resolved to award 6,300 ordinary shares of BGEO to thirteen of the employees of the Group. The Group estimates that the fair value of the shares awarded in May 2016 was GEL 75.13 per share. Shares awarded are subject to three-year vesting with continuous employment being the only vesting condition for the award.

In February 2015 the Group's Supervisory Board resolved to award 19,000 ordinary shares of BGEO to the members of Supervisory Board of the Group. The Group estimates that the fair value of the shares awarded in February 2015 was GEL 57.41 per share. Shares awarded are subject to two-year vesting with continuous employment being the only vesting condition for the award.

In May 2015 the Group's Supervisory Board resolved to award 15,800 ordinary shares of BGEO to three employees of the Group. The Group estimates that the fair value of the shares awarded in May 2015 was GEL 64.47 per share. Shares awarded are subject to three-year vesting with continuous employment being the only vesting condition for the award.



(Thousands of Georgian Lari)

## 15. Equity (continued)

## Share-based payments (continued)

In August 2015 the BGEO Supervisory Board resolved to award 105,000 ordinary shares of BGEO to the CEO of the Group. Shares will be formally awarded in the year following the service year in annual installments of 30,000 shares (last installment – 15,000 shares), each installment subject to four-year vesting with continuous employment being the only vesting condition for the award. The Group considers 24 August 2015 as the grant date. The Group estimates that the fair value of the shares awarded on 24 August 2015 was Georgian Lari 59.17 per share. The Group does not have an obligation to settle this award but it is expected that BGEO will recharge the cost of the BGEO shares to be purchased for its settlement to the Group.

In May 2014 the Group's Supervisory Board resolved to award 8,100 ordinary shares of BGH to three employees of the Group. Shares awarded are subject to three-year vesting with continuous employment being the only vesting condition for the award.

In February 2014 the BGH's Supervisory Board resolved to award 18,000 ordinary shares of BGH to the members of Supervisory board of the Group. Shares awarded to the members of Supervisory board are subject to 2-year vesting with continuous employment being the only vesting condition for both awards. The Group considers 24 February 2014 as the grant date. The Group estimates that the fair value of the shares awarded on 24 February 2014 was Georgian Lari 67.90 per share.

*Summary*

The fair value of cash settled share-based awards as of 31 December 2016 comprised Georgian Lari 97.44 per share. The Group's cash settled share-based payment expense for the year ended 31 December 2016 comprised GEL 319 (2015: GEL 425), respective liability at fair value amounted to GEL 292 (2015: GEL 254) as of 31 December 2016.

The weighted average fair value of equity settled share-based awards at the grant date comprised Georgian Lari 57.80 per share in year ended 31 December 2016 (31 December 2015: Georgian Lari 58.90 per share). The Group's equity settled share-based payment expense for the year ended 31 December 2016 comprised GEL 3,077 (31 December 2015: GEL 2,203).

Fair value of the BGEO's ordinary shares as of 31 December 2016 and as of grant dates was determined based on observable market prices adjusted for expected dividends that shall be paid off to entitled persons at vesting date.

In 2016 and 2015 all the awards were exercised on the dates when vesting conditions became met; based on decision of the Group's supervisory board, awards of 3,567 BGEO's ordinary shares vested immediately in 2016 as two employees left the Group.

## 16. Deferred revenue

	<u>2016</u>	<u>2015</u>
New Hippodrome	47,649	27,782
Kazbegi 15	15,167	–
Chavchavadze	4,598	–
Skyline	–	4,079
Non-current deferred revenue	<u>67,414</u>	<u>31,861</u>
Skyline	10,186	–
Tamarashvili st. 6	325	31,281
Kazbegi 25	–	27,073
Vazha-Pshavela 71	–	3,460
Tamarashvili 13	–	480
Optima Isani	–	10,283
Current deferred revenue	<u>10,511</u>	<u>72,577</u>
Deferred revenue	<u><u>77,925</u></u>	<u><u>104,438</u></u>

Deferred revenue of the Group consists of gross advances received from customers for purchase of residential property, including 18% VAT to be settled when the construction is finalized.

*(Thousands of Georgian Lari)*

## 17. Commitments and contingencies

## Taxation

Applicable tax regulations are often unclear and not large number of precedents have been established. This creates tax risks in Georgia, substantially more significant than typically found in countries with more developed tax systems. Management believes that the Group is in substantial compliance with the tax laws affecting its operations. However, the risk remains that relevant authorities could take differing positions with regard to interpretative issues.

## Capital commitments

As of 31 December 2016 the Group had commitments of GEL 10,467 (2015: GEL 23,222) relating to completion of construction contracts for Kazbegi 15 residential and hotel mixed used project.

## Lease commitments

The Group's commitments as lessee comprise following:

	<i>31 December 2016</i>	<i>31 December 2015</i>
Operating lease commitments (lessee)		
- Not later than 1 year	624	619
- Later than 1 year but not later than 5 years	672	1,173
Total	<u>1,296</u>	<u>1,792</u>

The Group's commitments as lessor comprise following:

	<i>31 December 2016</i>	<i>31 December 2015</i>
Operating lease commitments (lessor)		
- Not later than 1 year	4,029	1,769
- Later than 1 year but not later than 5 years	9,971	3,808
- Later than 5 years	9,654	2,972
Total	<u>23,654</u>	<u>8,549</u>

(Thousands of Georgian Lari)

## 18. Related party transactions

The volumes of related party transactions, outstanding balances at the year end, and related expenses and income for the year are as follows:

	2016			2015		
	Parent <sup>1</sup>	Entities under common control <sup>2</sup>	Key management personnel	Parent	Entities under common control	Key management personnel
Balances as at 31 December						
Cash and cash equivalents at 31 December	–	82,792	–	–	27,986	–
Trade and other payables	–	–	–	–	27	–
Deferred Income	–	–	2,344	–	–	1,369
Debt securities issued	29,280	11,155	1,173	–	2,196	192
Transactions for the year ended 31 December						
Interest expense on debt securities issued	524	529	100	–	156	14
Revenue from sale of inventory property	–	–	117	–	–	–
Transaction costs paid related to bonds issue	–	1,167	–	–	889	–
Finance income	–	715	–	–	–	–
Finance expenses	–	–	–	80	–	–
Employee benefits expense	–	–	4,217	–	–	3,682
Rental income	–	623	–	52	37	–
Rental expense	–	120	–	183	120	–
Other general and administrative expense	–	112	–	–	150	–
Insurance expense	–	64	–	–	138	–

<sup>1</sup> As at 31 December 2016 and 2015 and in the years then ended Parent includes BGEO Group PLC, JSC BGEO Group and BGEO Investments figures.

<sup>2</sup> Entities under common control include BGEO Group PLC subsidiaries.

Total number of key management personnel members receiving employee benefits in 2016 amounted to 4 persons (2015: 4), CEO and 3 deputies. Other transactions with key management personnel include above mentioned 4 employees and total 3 members of supervisory board.

Compensation of key management personnel comprised the following:

	2016	2015
Share-based compensation	3,366	2,314
Salary	601	328
Cash bonus	250	208
Termination benefits	–	832
	<u>4,217</u>	<u>3,682</u>

## 19. Events after the reporting period

In January 2017, the Group repaid one borrowing from local commercial bank with outstanding balance of GEL 1,117 as at 31 December 2016.

In March 2017, the Group repaid 2-year local bonds issued in March 2015, out of which USD 6,311 was partially repaid in 2016. The total paid amount in 2017 amounted to USD 13,689.