

**MIK HOLDING JSC AND ITS  
SUBSIDIARIES  
(Incorporated in Mongolia)**

**Audited consolidated financial statements  
31 December 2017**

**MIK HOLDING JSC AND ITS SUBSIDIARIES**  
**FOR THE YEAR ENDED 31 DECEMBER 2017**  
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## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Corporate Information

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Registered Office	: Sukhbaatar district, 1 <sup>st</sup> khoroo, Peace avenue-19, 10 <sup>th</sup> floor P.O.Box – 14210 – 215 Ulaanbaatar City, Mongolia
Board of Directors	: Mr. Munkhbaatar.M (Chairman) Mr. Ganbat.B Mr. Choijljalbuu.B Ms. Enkhtuya.B Mr. Gantumur.L Mr. Badamchuluun.D Mr. Khashchuluun.Ch Mr. Shijir.E Mr. Otgochuluu.Ch
Corporate Secretary	: Ms. Altantuya.Ts Ms. Maralmaa.Kh
Auditors	: Ernst & Young Mongolia Audit LLC Certified Public Accountants

## STATEMENT BY CHAIRMAN AND EXECUTIVES

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We, Munkhbaatar Myagmar, being the Chairman of the Board of Directors of MIK Holding JSC, Gantulga Badamkhatan, being the Chief Executive Officer, and Bat-Ulzii Molomjams, being the Chief Financial Officer, primarily responsible for the consolidated financial statements of MIK Holding JSC and its subsidiaries (herein collectively referred to as the "Group"), do hereby state that, in our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB").



Munkhbaatar Myagmar  
Chairman of the Board of Directors

A handwritten signature in blue ink, appearing to read "Gantulga".

Gantulga Badamkhatan  
Chief Executive Officer

A handwritten signature in blue ink, appearing to read "Bat-Ulzii".

Bat-Ulzii Molomjams  
Chief Financial Officer

Ulaanbaatar, Mongolia

Date: 07 MAR 2018





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## INDEPENDENT AUDITOR'S REPORT

### To the Shareholders of MIK Holding JSC

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#### Opinion

We have audited the consolidated financial statements of MIK Holding JSC and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the 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 consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

#### Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (the "IESBA Code"), 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 judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of the audit of the consolidated financial statements as a whole, and in forming the auditor's opinion thereon, and we do not provide a separate opinion on these matters. For each matters 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 financial 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.



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**INDEPENDENT AUDITOR'S REPORT (CONT'D.)**

**To the Shareholders of MIK Holding JSC (cont'd.)**

**Key Audit Matters (cont'd.)**

Key audit matters	How our audit addressed the key audit matters
<p><b><i>Impairment of purchased mortgage pool receivables</i></b></p> <p>The impairment of purchased mortgage pool receivables is estimated by the management through the application of judgement and use of highly subjective assumptions.</p> <p>Due to the significance of purchased mortgage pool receivables (representing over 90% of total assets) and the related estimation uncertainty, this is considered a key audit matter.</p> <p>The portfolio of purchased mortgage pool receivables which give rise to the greatest uncertainty are typically those where impairments are derived from collective models. The use of different modelling techniques and assumptions (including the probability of default, loss given default and loss discovery period) could produce significantly different estimates of loan loss provisions.</p> <p>Relevant disclosures are included in notes 2.4, 12 and 24.2 to the consolidated financial statements.</p>	<p>Our audit procedures included evaluating the methodologies, inputs and assumptions used by the Group in calculating collectively assessed impairment.</p> <p>We compared the Group's assumptions for collective impairment allowances to internal available historical data, externally available industry, financial and economic data, and our own assessments in relation to key inputs. We considered the appropriateness of the Group's revisions to estimates and assumptions and the consistency of judgement applied in the use of economic factors, loss discovery periods and the observation period for historical default rates.</p> <p>We also assessed the adequacy of the related disclosure in the notes to the consolidated financial statements.</p>
<p><b><i>Withholding tax liability against future dividend distribution from the Group's SPCs</i></b></p> <p>The Group has recorded withholding tax liabilities against future dividend distribution from the Group's Special Purpose Companies ("SPC"s) of MNT'000 13,800,402.</p> <p>Significant management judgement is required in the interpretation of the Mongolian tax legislation, in particular where it does not provide definitive guidance, and also in the determination of the amount of associated withholding tax liability, based upon the likely timing and level of distribution.</p> <p>Relevant disclosures are included in notes 2.4, 8 and 19 to the consolidated financial statements.</p>	<p>We have reviewed management's accounting policy in regards of withholding tax liabilities against future dividend distribution from the Group's SPCs. In evaluating management's assessment, we read the key terms and conditions of the SPCs' Articles of Charters, the respective law and Financial Regulatory Commission ("FRC") regulations in respect of SPC and the relevant Mongolian tax law, and made our own assessment on the appropriateness of the management's interpretation of the tax law and regulations.</p> <p>We also employed EY internal tax specialist to assist with our audit in evaluating management's assessment.</p> <p>We also assessed the adequacy of the related disclosure in the notes to the consolidated financial statements.</p>



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## INDEPENDENT AUDITOR'S REPORT (CONT'D.)

### To the Shareholders of MIK Holding JSC (cont'd.)

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#### **Other information included in the Annual Report**

The Directors are responsible for the other information. The other information comprises the other sections of the Annual Report not including the consolidated financial statements and the auditor's report thereon ("the Other Sections"), which are expected to be made available after that date.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and in doing so to consider whether the other information is materially inconsistent with the consolidated financial statements, or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this audit report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the Other Sections of the Annual Report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

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

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with 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.

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

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

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

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



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## INDEPENDENT AUDITOR'S REPORT (CONT'D.)

### To the Shareholders of MIK Holding JSC (cont'd.)

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#### Auditor's Responsibilities for the Audit of the Consolidated Financial Statements (cont'd.)

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 and business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period 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.





**INDEPENDENT AUDITOR'S REPORT (CONT'D.)**

**To the Shareholders of MIK Holding JSC (cont'd.)**

**Other Matter**

This report is made solely to the shareholders of the Group, as a body, in connection with the audit requested by shareholders in accordance with Article 94 of the Company Law of Mongolia and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

  
*Ernst & Young Mongolia Audit LLC*  
**ERNST & YOUNG MONGOLIA AUDIT LLC**  
Certified Public Accountants

  
**PETER MARKEY**  
Director

Ulaanbaatar, Mongolia  
Date: 7 March 2018

**MIK HOLDING JSC AND ITS SUBSIDIARIES****Consolidated Statement of Profit or Loss and Other Comprehensive Income**

For the year ended 31 December 2017

	Notes	2017 MNT'000	2016 MNT'000
Interest income	3	215,043,980	192,685,281
Interest expense	4	(125,386,232)	(113,557,241)
<b>Net interest income</b>		<u>89,657,748</u>	<u>79,128,040</u>
Fee and commission expense	5	(9,984,700)	(8,493,493)
Other operating income	6	69,156	149,548
<b>Total operating income</b>		<u>79,742,204</u>	<u>70,784,095</u>
Credit loss expense	12	(1,673,740)	(6,271,976)
<b>Net operating income</b>		<u>78,068,464</u>	<u>64,512,119</u>
Operating expenses	7	(7,027,586)	(5,622,382)
<b>Profit before tax</b>		<u>71,040,878</u>	<u>58,889,737</u>
Income tax expense	8	(11,877,891)	(8,151,844)
<b>Profit for the year, representing total comprehensive income</b>		<u><u>59,162,987</u></u>	<u><u>50,737,893</u></u>
<b>Earnings per share (MNT)</b>			
Basic and diluted earnings per share	9	<u>3,180.32</u>	<u>2,530.97</u>

**MIK HOLDING JSC AND ITS SUBSIDIARIES**

**Consolidated Statement of Financial Position**

**As at 31 December 2017**

	Notes	2017 MNT'000	2016 MNT'000
<b>ASSETS</b>			
Cash and bank balances	10	212,950,606	156,519,377
Mortgage pool receivables with recourse	11	29,825,565	28,639,946
Purchased mortgage pool receivables	12	2,518,056,150	2,122,227,156
Other assets	13	794,194	331,971
Property and equipment	14	14,527,014	14,689,287
Intangible assets	15	112,569	76,621
<b>TOTAL ASSETS</b>		<u>2,776,266,098</u>	<u>2,322,484,358</u>
<b>LIABILITIES</b>			
Borrowed funds	16	15,498,844	8,552,889
Collateralized bonds	17	2,576,010,489	2,165,576,045
Other liabilities	18	4,813,595	4,001,750
Income tax payable		3,639,426	1,009,039
Deferred tax liability	19	13,800,402	8,214,763
<b>TOTAL LIABILITIES</b>		<u>2,613,762,756</u>	<u>2,187,354,486</u>
<b>EQUITY</b>			
Ordinary shares	20	20,709,320	20,709,320
Share premium	20	52,225,115	52,225,115
Treasury shares	20	(47,055,136)	(24,057,436)
Retained earnings		136,624,043	86,252,873
<b>TOTAL EQUITY</b>		<u>162,503,342</u>	<u>135,129,872</u>
<b>TOTAL LIABILITIES AND EQUITY</b>		<u>2,776,266,098</u>	<u>2,322,484,358</u>

**MIK HOLDING JSC AND ITS SUBSIDIARIES**

**Consolidated Statement of Changes in Equity**

**For the year ended 31 December 2017**

	Notes	Ordinary shares MNT'000	Share premium * MNT'000	Treasury shares MNT'000	Retained earnings ** MNT'000	Total equity MNT'000
<b>At 1 January 2016</b>		20,709,320	52,225,115	–	40,510,068	113,444,503
Total comprehensive income		–	–	–	50,737,893	50,737,893
Repurchase of shares	20	–	–	(24,057,436)	–	(24,057,436)
Dividend declared	20	–	–	–	(4,995,088)	(4,995,088)
<b>At 31 December 2016 and 1 January 2017</b>		<u>20,709,320</u>	<u>52,225,115</u>	<u>(24,057,436)</u>	<u>86,252,873</u>	<u>135,129,872</u>
Total comprehensive income		–	–	–	59,162,987	59,162,987
Repurchase of shares	20	–	–	(22,997,700)	–	(22,997,700)
Dividends declared	20	–	–	–	(8,791,817)	(8,791,817)
<b>At 31 December 2017</b>		<u>20,709,320</u>	<u>52,225,115</u>	<u>(47,055,136)</u>	<u>136,624,043</u>	<u>162,503,342</u>

\* Included in share premium is share issuance cost amounting to MNT 124,670 thousand.

\*\* Included in retained earnings as at 31 December 2017 are restricted retained earnings of MNT 138,004,023 thousand (31 December 2016: MNT 82,147,627 thousand) that are attributable to the Group's SPCs. The restriction relates to the issuance of Residential Mortgage Backed Securities (referred to as "RMBS") (see note 1 below for further details), whereby the retained earnings of the SPCs that have issued RMBSs are restricted from distribution until their liquidation in accordance with their Articles of Charter and related FRC regulation.

**MIK HOLDING JSC AND ITS SUBSIDIARIES**

**Consolidated Statement of Cash Flows**

**For the year ended 31 December 2017**

	Notes	2017 MNT'000	2016 MNT'000
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
<b>Profit before tax</b>		71,040,878	58,889,737
Adjustments to reconcile profit before tax to net cash flows:			
Unrealised foreign exchange gain		(70,559)	(68,439)
Credit loss on purchased mortgage pool receivables	12	1,673,740	6,271,976
Loss on disposal of property and equipment	7	86	300
Depreciation of property and equipment	7	496,718	529,069
Write-off of property and equipment	7	–	3,149
Amortisation of intangible assets	7	54,586	61,188
Amortisation of deferred grants	6	(1,058)	(10,824)
Interest accrual on financial investments-held to maturity	3	–	(100,999)
<b>Operating profit before working capital changes</b>		<u>73,194,391</u>	<u>65,575,157</u>
Changes in operating assets and liabilities:			
Due from banks – placement with original maturities of more than three months		(84,591,223)	5,753,764
Mortgage pool receivables		211,431,147	156,593,466
Other assets		(462,223)	(143,756)
Collateralized bonds		(199,685,056)	(164,439,464)
Other liabilities		<u>812,903</u>	<u>472,428</u>
<b>Cash generated from operations</b>		699,939	63,811,595
Income tax paid		<u>(3,661,865)</u>	<u>(2,739,934)</u>
<b>Net cash flows (used in)/from operating activities</b>		<u>(2,961,926)</u>	<u>61,071,661</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Proceeds on disposal of property and equipment		63,000	684
Purchase of property and equipment	14	(397,531)	(588,386)
Purchase of intangible assets	15	(90,534)	(45,475)
Proceeds from financial investments-held to maturity		–	3,000,000
<b>Net cash flows (used in)/from investing activities</b>		<u>(425,065)</u>	<u>2,366,823</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Dividends paid		(8,791,817)	(4,995,088)
Proceeds from borrowed funds*		8,500,000	–
Repayment of borrowed funds*		(1,554,045)	(313,479)
Purchase of treasury shares		<u>(22,997,700)</u>	<u>(24,057,436)</u>
<b>Net cash flows used in financing activities</b>		<u>(24,843,562)</u>	<u>(29,366,003)</u>
<b>Net (decrease)/increase in cash and cash equivalents</b>		(28,230,553)	34,072,481
Effect of exchange rate changes on cash and cash equivalents		70,559	68,439
<b>Cash and cash equivalents at 1 January</b>		<u>140,253,713</u>	<u>106,112,793</u>
<b>Cash and cash equivalents at 31 December</b>	10	<u>112,093,719</u>	<u>140,253,713</u>
<b>OPERATIONAL CASH FLOW FROM INTEREST</b>			
Interest received		209,648,564	190,442,934
Interest paid		(120,750,529)	(111,150,110)

\* There is no non-cash changes for liabilities arising from financing activities.



## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

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#### 1. Corporate and Group information

Mongolian Mortgage Corporation HFC LLC (“MIK HFC”) was incorporated on 04 September 2006 under the Company Law of Mongolia, under the name of “Housing Finance Corporation” and renamed on 6 October 2006 as “Mongolian Mortgage Corporation HFC LLC”.

MIK Holding JSC (the “Company”) was incorporated on 23 April 2008 under the Company Law of Mongolia and was a wholly owned subsidiary of MIK HFC. The Company was previously known as SPC A LLC and renamed on 30 October 2015. The Company remained dormant since incorporation until the completion of the reorganization, in which the Company became the holding company of the companies now comprising the Group on 14 December 2015 and the principal activity of the Company became investment holding.

The Group’s principal place of business and the registered address is Sukhbaatar district, 1st khoroo, Peace Avenue-19, 10th floor, Ulaanbaatar City, Mongolia.

The Group’s objective is to develop a secondary market for mortgage loans in Mongolia by acquiring them from the commercial banks and thus providing the banking sector with additional liquidity, which can be used for further growth of mortgage lending. Its principal activities include purchases of mortgage loans issued by Mongolian commercial banks and the issuance of bonds, which are collateralized by the cash flows from the repayment of the mortgage pools.

The registered share capital of MNT 20,709,320 thousand (2016: MNT 20,709,320 thousand) consists of 20,709,320 (2016: 20,709,320) common shares at par value of MNT 1,000 (2016: MNT 1,000) each.

The Company is a joint stock company listed on the Mongolian Stock Exchange, incorporated and domiciled in Mongolia. The shareholders of the Group for the year ended 31 December 2017 are set out in Note 20.

The business activity of issuing asset backed securities became a licensed activity in Mongolia effective from 1 January 2011 in accordance with the Asset Backed Securities Law of Mongolia which was approved on 23 April 2010. On 14 March 2012, MIK HFC was granted, by the FRC, a special license for the issuance of asset backed securities.

2013, the Government of Mongolia together with Bank of Mongolia (“BoM”) initiated a price stabilization program which included a subsidy scheme for mortgage financing to create a stable environment for mortgage financing. Under the program, the commercial banks in Mongolia have been granted soft loans to fund the issuance of subsidized interest rate mortgage loans or refinance their existing loans with the subsidized interest rate mortgage financing.

On 14 June 2013, MIK HFC, BoM and 14 commercial banks signed an agreement to participate in this government program and on 30 October 2013, the Group established its first SPC, MIK Asset One SPC LLC, a wholly owned subsidiary, to purchase the subsidized interest rate mortgage loans bearing an interest rate of 8% from the commercial banks and in return to issue RMBS, which are collateralized by the cash flows and collaterals of these mortgage pools.

As of 31 December 2017, the Group had established fifteen (15) SPCs (2016: thirteen (13)) and of which thirteen (13) of these SPCs have purchased mortgage pools and issued RMBS (2016: nine (9)).

All SPCs are incorporated in Mongolia and the principal activities of the SPCs are mainly restricted to the purchase of mortgage loans, issuance of RMBS and restricted investment activities as governed by the Articles of the Charter of each SPC and relevant FRC regulations.

The consolidated financial statements of the Group were authorized for issue in accordance with the resolution of the Board of Directors on 7 March 2018.

#### 2. Significant accounting policies

##### 2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with IFRS as issued by IASB.

The consolidated financial statements of the Group have been prepared on a historical cost basis. The consolidated financial statements are presented in Mongolian Togrog, which is denoted by the symbol MNT, and all values are rounded to the nearest thousands, except when otherwise indicated.

## 2. Significant accounting policies (cont'd.)

### 2.1 Basis of preparation (cont'd.)

#### Presentation of financial statements

The Group presents its statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the reporting date (current) and more than 12 months after the reporting date (non-current) is presented in Note 22.

Financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position only when there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expense is not offset in the consolidated statement of profit or loss and other comprehensive income ("OCI") unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Group.

#### Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiaries as at 31 December 2017. A subsidiary is an entity (including structured entity), directly or indirectly, controlled by the Company. 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

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive incomes are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity, while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

### 2.2 Changes in accounting policies and disclosures

The accounting policies adopted are consistent with those of the previous financial year, except for the following standards and amendments to IFRS that became effective as of 1 January 2017:

#### New and amended standards and interpretations

- |                         |  |
|-------------------------|--|
| • Amendments to IAS 7   | <i>Statement of Cash Flows: Disclosure Initiative</i>  |
| • Amendments to IAS 12  | <i>Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses</i>  |
| • Amendments to IFRS 12 | <i>Disclosure of Interest in Other Entities: Clarification of the Scope of IFRS 12 from Annual Improvement Cycle – 2014-2016</i> |

2. Significant accounting policies (cont'd.)

2.2 Changes in accounting policies and disclosures (cont'd.)

(a) Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative

The amendments require entities to provide disclosure of changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). The Group does not have material non-cash changes in liabilities arising from financing activities.

The adoption of the new and amended standards and interpretations did not have any significant impact on the financial performance or position of the Group.

Standards issued but not yet effective

The Standards and Interpretations that are issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

- |   |   |
|---|---|
| • Amendments to IFRS 4                  | <i>Financial Instruments with IFRS 4 Insurance Contracts</i> <sup>1</sup>                                 |
| • Amendments to IAS 40                  | <i>Transfers of investment property</i> <sup>1</sup>  |
| • Amendments to IFRS 10 and IAS 28      | <i>Sale or Contribution of Assets between an Investor and its Associate or Joint Venture</i> <sup>4</sup> |
| • IFRS 9                                | <i>Financial Instruments</i> <sup>1</sup>   |
| • IFRS 15                               | <i>Revenue from Contracts with Customers</i> <sup>1</sup>   |
| • IFRS 16                               | <i>Leases</i> <sup>2</sup>  |
| • IFRS 17                               | <i>Insurance Contracts</i> <sup>3</sup>   |
| • IFRIC Interpretation 22               | <i>Foreign Currency Transactions and Advance Consideration</i> <sup>1</sup>                               |
| • IFRIC Interpretation 23               | <i>Uncertainty over Income Tax Treatment</i> <sup>2</sup>   |
| • Annual Improvements (2014-2016 cycle) | <i>Amendments to a number of IFRSs issued in December 2016</i> <sup>1</sup>                               |
| • Amendments to IFRS 2                  | <i>Classification and Measurement of Share-based Payment Transactions</i> <sup>1</sup>                    |

<sup>1</sup> Effective for annual periods beginning on or after 1 January 2018

<sup>2</sup> Effective for annual periods beginning on or after 1 January 2019

<sup>3</sup> Effective for annual periods beginning on or after 1 January 2021

<sup>4</sup> The effective date of this amendment is postponed indefinitely pending the outcome of IASB's research project on the equity method of accounting

Further information about those IFRSs that are expected to be applicable to the Group is as follows:

(b) Financial instruments

In July 2014, the IASB issued the final version of IFRS 9, bringing together all phases of the financial instruments project to replace IAS 39 and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment and hedge accounting. The Group expects to adopt IFRS 9 from 1 January 2018. The expected impacts arising from the adoption of IFRS 9 are summarised as follows:

(i) Classification and measurement

The Group does not expect that the adoption of IFRS 9 will have a significant impact on the classification and measurement of its financial assets. Specifically, mortgage pool receivables that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost upon adoption which is unchanged from the current accounting policy.

(ii) Impairment

IFRS 9 requires the Group to record expected credit losses on all of its debt securities, loans and receivables, either on a 12-month or lifetime basis. The Group is currently in the process of finalizing its model for IFRS 9 impairment. However based on the current assessment, the Group estimates that the financial impact on allowances for impairment losses of purchased mortgage pool receivables upon adoption will range from nil to a reduction in impairment losses of approximately 10%.

**2. Significant accounting policies (cont'd.)**

**2.2 Changes in accounting policies and disclosures (cont'd.)**

Standards issued but not yet effective (cont'd.)

(b) Revenue

IFRS 15 establishes a new 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 principles in IFRS 15 provide a more structured approach for measuring and recognising revenue. The standard also introduces extensive qualitative and quantitative disclosure requirements, including disaggregation of total revenue, information about performance obligations, changes in contract asset and liability account balances between periods and key judgments and estimates. The standard will supersede all current revenue recognition requirements under IFRSs. The interpretation does not have any material impact on the financial position or performance of the Group upon adoption on 1 January 2018.

(c) Date of the transaction for determining an exchange rate

IFRIC-Int 22 specifies the date of the transaction for determining an exchange rate to use for transactions that involve advance consideration paid or received in a foreign currency. The interpretation is effective for annual periods beginning on or after 1 January 2018. The interpretation did not have any material impact on the financial position or performance of the Group upon adoption on 1 January 2018.

(b) Income taxes

IFRIC-Int 23 supports the requirements in IAS 12 Income Taxes by specifying how to reflect the effects of uncertainty in accounting for income taxes. It is effective for annual periods beginning on or after 1 January 2019. In 2018, the Group will continue to assess the potential effect of IFRIC-Int 23 on its consolidated financial statements.

(c) Leases

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. 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 is effective for annual periods beginning on or after 1 January 2019. A lessee can choose to apply the standard using either a full retrospective or a modified retrospective approach. In 2018, the Group will continue to assess the potential effect of IFRS 16 on its consolidated financial statements.

**2.3 Summary of significant accounting policies**

**Foreign currency translation**

The consolidated financial statements are presented in Mongolian Togrog ("MNT"), which is also the Company and the subsidiaries' functional currency. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange at the statement of financial position date. All differences arising from settlement or translation of monetary items are taken to the consolidated profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates 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. The gain or loss arising on translation of non-monetary items measured at fair value is treated in line with the recognition of gain or loss on change in fair value of the item.

**2. Significant accounting policies (cont'd.)**

**2.3 Summary of significant accounting policies (cont'd.)**

**Financial instruments – initial recognition and subsequent measurement**

**(i) Date of recognition**

All financial assets and liabilities are initially recognised on the trade date, i.e., the date that the Group become a party to the contractual provisions of the instrument. This includes "regular way trades": purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

**(ii) Initial recognition of financial instruments**

Financial instruments are recognised initially at fair value, which is the fair value of the consideration given (in case of an asset) or received (in case of a liability). The initial measurement of financial instruments, except in the case of financial assets and financial liabilities at fair value through profit or loss ("FVPL"), includes transaction cost.

In terms of the IAS 39 classification, the Group's financial assets consist of financial investments classified as held to maturity and loans and receivables and its financial liabilities only consist of loans and borrowings.

**(iii) Loans and receivables**

The Group's loans and receivables consist mainly of the mortgage pool receivables. The mortgage pool receivables purchased from commercial banks are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- Those that the Group intends to sell immediately or in the near term and those that the Group upon initial recognition designates as at fair value through profit or loss.
- Those that the Group, upon initial recognition, designates as available for sale.
- Those for which the Group may not recover substantially all of its initial investment, other than because of credit deterioration.

After initial measurement, mortgage pool receivables are subsequently measured at amortised cost using the effective interest rate ("EIR"), less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortisation is included in "Interest income" in profit or loss. The losses arising from impairment are recognised in the profit or loss.

**(iv) Loans and borrowings**

The Group's loans and borrowings consist mainly of borrowed funds, the issued collateralized bonds and other liabilities. The substance of the contractual agreement of loans and borrowings results in the Group having an obligation either to deliver cash or other financial assets to the holder, or to satisfy the obligation other than by the exchange of fixed amount of cash or other financial assets for a fixed number of own equity shares.

Loans and borrowing are carried at amortised cost using the effective interest method of amortization.

**Derecognition of financial assets and financial liabilities**

**(i) Financial assets**

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- The rights to receive cash flows from the asset have expired.
- The Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either:
  - the Group has transferred substantially all the risks and rewards of the asset, or
  - the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset. In that case, the Group also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.



**2. Significant accounting policies (cont'd.)**

**2.3 Summary of significant accounting policies (cont'd.)**

**Derecognition of financial assets and financial liabilities (cont'd.)**

**ii) Financial liabilities**

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in consolidated statement of profit or loss.

**Determination of fair value**

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 principal or the most advantageous market must be accessible to by the Group.

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.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is 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

For assets and liabilities that are recognized in the consolidated 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.

An analysis of fair values of financial instruments and further details as how they are measured are provided in Note 25.

**Impairment of financial assets**

The Group assesses at each statement of financial position date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, the probability that they will enter bankruptcy or other financial reorganisation, default or delinquency in interest or principal payments and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

**(i) Financial assets carried at amortised cost**

For financial assets carried at amortised cost, the Group first assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

**2. Significant accounting policies (cont'd.)**

**2.3 Summary of significant accounting policies (cont'd.)**

**Impairment of financial assets (cont'd.)**

**(i) Financial assets carried at amortised cost (cont'd.)**

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred).

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Loans and receivables together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If written-off loans and receivable are later recovered, the recovery is recognized as income in profit or loss.

The present value of the estimated future cash flows is discounted at the financial asset's original EIR. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the new EIR determined at the reclassification date.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective impairment evaluation, financial assets are grouped on the basis of the Group's credit risk grouping that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors. The Group's collective impairment evaluation is computed based on historical loss experience of the each credit risk grouping. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

**Collateral repossessed**

Repossessed assets are initially recognised at the lower of their fair values less costs to sell and the amortised cost of the related outstanding loans on the date of the repossession, and the related loans and advances together with the related impairment allowances are derecognised from the statement of financial position. Subsequently, repossessed assets are measured at the lower of cost and fair value less costs to sell and are included in 'Other assets'.

**Recognition of income and expenses**

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

**(i) Interest income and expense**

For all financial instruments measured at amortised cost, interest income or expense is recorded using the EIR, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts.

The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded in profit or loss. However, for a reclassified financial asset for which the Group subsequently increases its estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the EIR from the date of the change in estimate.

**2. Significant accounting policies (cont'd.)**

**2.3 Summary of significant accounting policies (cont'd.)**

**Recognition of income and expenses (cont'd.)**

**(i) Interest income and expense (cont'd.)**

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

**(ii) Fee and commission expense**

Fee expense represents administration and fixed fee commission paid to the commercial banks. Fee expense is recognized when actual service has been provided.

Components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

**Cash and bank balances**

Cash and bank balances in the statement of financial position comprise cash at banks and on hand and short-term deposits with a maturity of three months or less, which are subject to an insignificant risk of changes in value.

For the purpose of the statement of cash flows, cash and cash equivalents comprises cash on hand, non-restricted current accounts with banks and amounts due from banks or with an original maturity of three months or less.

**Property and equipment**

All items of property and equipment are initially recorded at cost. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of any replaced part is derecognised. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Subsequent to recognition, property and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses.

Depreciation of other property and equipment is provided for on a straight-line basis to write off the cost of each asset to its residual value over the estimated useful life at the following annual rates:

Premises	40 years
Furniture and office equipment	10 years
Computers	3 years
Vehicles	10 years

The residual values, useful life and depreciation method are reviewed at each financial year-end to ensure that the amount, method and period of depreciation are consistent with previous estimates and the expected pattern of consumption of the future economic benefits embodied in the items of property and equipment.

An item of property and equipment is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. The difference between the net disposal proceeds, if any and the net carrying amount is recognised in profit or loss.

**Intangible assets**

The Group's intangible assets include the value of computer software.

An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Group.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortised over the useful economic life. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates.

The amortisation expense on intangible assets with finite lives is recognised in profit or loss in the expense category consistent with the function of the intangible asset. Amortisation is calculated using the straight-line method to write down the cost of intangible assets to their residual values over their estimated useful live of three years.

**2. Significant accounting policies (cont'd.)**

**2.3 Summary of significant accounting policies (cont'd.)**

**Impairment of non-financial assets**

The Company assess at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimate the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's (CGU) fair value less costs to sell and its value in use. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded subsidiaries or other available fair value indicators.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Company estimate the asset's or CGU's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of profit or loss and other comprehensive income.

**Leases**

The determination of whether an arrangement is (or contains) a lease is based on the substance of the arrangement at the inception of the lease. The arrangement is, or contains, a lease if fulfilment of the arrangement is dependent on the use of a specific asset (or assets) and the arrangement conveys a right to use the asset (or assets), even if that asset is (or those assets are) not explicitly specified in an arrangement.

**Group as a lessor**

Leases in which the Group does not transfer substantially all the risks and rewards of ownership of an asset are classified as operating leases. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

**Employee benefits**

**(i) Short term benefits**

Wages, salaries and other salary related expenses are recognised as an expense in the year in which the associated services are rendered by employees of the Group. Short term accumulating compensated absences such as paid annual leave are recognised when services are rendered by employees that increase their entitlement to future compensated absences, and short term non-accumulating compensated absences such as sick leave are recognised when absences occur.

**(ii) Defined contribution plans**

As required by law, companies in Mongolia make contributions to the government pension scheme, social and health fund. Such contributions are recognised as an expense in profit or loss as incurred.

**Provisions**

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The expense relating to any provision is presented in profit or loss net of any reimbursement.

**Taxes**

**(i) Current tax**

Current tax assets and liabilities for the current and prior years 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 by the statement of financial position date.

## 2. Significant accounting policies (cont'd.)

### 2.3 Summary of significant accounting policies (cont'd.)

#### Taxes (cont'd.)

##### (ii) Deferred tax

Deferred tax is provided on temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognized for all taxable temporary differences, except for:

- Where the deferred tax liability 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.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

- Where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition 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.
- In respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each statement of financial position 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 reassessed at each statement of financial position date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the statement of financial position date.

Deferred tax relating to items recognized outside profit or loss is recognized outside profit or loss. Deferred tax items are recognized in correlation to the underlying transaction either in other comprehensive income or directly in equity.

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.

#### Grants

Grants are recognised where there is reasonable assurance that the grant will be received and all attached conditions will be complied with. When the grant relates to an expense item, it is recognised as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate. When the grant relates to an asset, it is recognised as deferred income and released to income in equal amounts over the expected useful life of the related asset

When the Group receives non-monetary grants, the asset and the grant are recorded gross at nominal amounts and released to the income statement over the expected useful life and pattern of consumption of the benefit of the underlying asset by equal annual instalments. When loans or similar assistance are provided by governments or related institutions with an interest rate below the current applicable market rate, the effect of this favourable interest is regarded as additional government grants.

#### Equity

##### (i) Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are shown in equity as a deduction, net of tax, from the proceeds.

##### (ii) Treasury shares

Own equity instruments that are reacquired (treasury shares) are recognised at cost and deducted from equity. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of the Group's own equity instruments. Any difference between the carrying amount and the consideration, if reissued, is recognised in the share premium.

##### (iii) Retained earnings

Retained earnings represent accumulated profits or losses, reduced by dividend declarations. These may also include prior period adjustments and effects of changes in accounting policies.



## 2. Significant accounting policies (cont'd.)

### 2.3 Summary of significant accounting policies (cont'd.)

#### Earnings per share

Basic earnings per share is calculated by dividing the net profit for the year attributable to ordinary equity holders of the Parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share is calculated by dividing the net profit for the year attributable to ordinary equity holders of the Parent (after adjusting for interest on the convertible preference shares and interest on the convertible bond, in each case net of tax, if any) by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

#### Segment information

The Group is engaged in purchasing of mortgage pools and issuing RMBS securitized by those mortgage pools in Mongolia. Accordingly, the Group considers that it only has a single reportable segment from both business and geographic perspectives and therefore only provides relevant entity-wide information.

#### Transactions with related parties

A related party is a person or entity that is related to the Group:

A person or a close member of that person's family is related to a Group if that person:

- has control or joint control of the Group;
- has significant influence over the Group; or
- is a member of the key management personnel of the Group or of a parent of the Group.

An entity is related to a Group if any of the following conditions applies:

- The entity and the Group are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
- One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
- Both entities are joint ventures of the same third party.
- One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

The entity is a post-employment benefit plan for the benefit of employees of either the Group or an entity related to the Group. If the Group is itself such a plan, the sponsoring employers are also related to the Group.

- The entity is controlled or jointly controlled by a person identified in (a).
- A person identified in (a) (i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
- The entity, or any member of a group of which it is a part, provides key management personnel services to the Group or to the parent of the Group.

All material transactions and balances with the related parties are disclosed in the relevant notes to consolidated financial statements and the detail is presented in Note 23.

### 2.4 Significant accounting judgments, estimates and assumptions

In the process of applying the Group's accounting policies, management has exercised judgment and estimates in determining the amounts recognised in the consolidated financial statements. The most significant uses of judgment and estimates are as follows:

#### Impairment losses on loans and receivables

The Group reviews its individually significant loans and receivables at each statement of financial position date to assess whether an impairment loss should be recorded in the consolidated statement of profit or loss and other comprehensive income. In particular, management judgment is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and receivables that have been assessed individually and found not to be impaired and all individually insignificant loans and receivables are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as levels of arrears, credit utilisation, loan to collateral ratios, etc.), and judgments to the effect of concentrations of risks and economic data (including real estate prices indices and the performance of different individual groups).

The impairment loss on loans and receivables is recorded in the consolidated statement of profit or loss and disclosed in more detail in Notes 11 and 12.

**2. Significant accounting policies (cont'd.)**

**2.4 Significant accounting judgments, estimates and assumptions (cont'd.)**

**Deferred tax**

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

Significant management judgement is also required to determine the amount of withholding tax liability associated with the future dividend distribution of the Group's SPCs, based upon the likely timing and level of retained earnings.

Further details are given in notes 8 and 19 to the consolidated financial statements.

**3. Interest income and segment information**

During the year ended 31 December 2017 and 2016, the Group was engaged in a single business segment, which is the purchasing of mortgage pools and issuing RMBS securitized by those mortgage pools in Mongolia. There has been no single external customer that has contributed revenue exceeding 10% or more of the Group's revenue during the year ended 31 December 2017 and 2016.

	2017 MNT'000	2016 MNT'000
Purchased mortgage pool receivables (without recourse)	189,294,568	173,782,019
Bank balances	21,112,818	16,004,341
Mortgage pool receivables with recourse	4,636,594	2,797,922
Government treasury bill	–	100,999
	<u>215,043,980</u>	<u>192,685,281</u>

**4. Interest expense**

	2017 MNT'000	2016 MNT'000
Collateralized bonds	125,069,980	113,533,090
Borrowed funds	316,252	24,151
	<u>125,386,232</u>	<u>113,557,241</u>

**5. Fee and commission expense**

	2017 MNT'000	2016 MNT'000
Loan service fee	9,974,905	8,489,748
Bank service charge	9,795	3,745
	<u>9,984,700</u>	<u>8,493,493</u>

**6. Other operating income**

	2017 MNT'000	2016 MNT'000
Foreign exchange gain, net	9,800	69,954
Grant income (Note 18)	1,058	10,824
Other income	58,298	68,770
	<u>69,156</u>	<u>149,548</u>

## MIK HOLDING JSC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements – 31 December 2017

### 7. Operating expenses

	2017 MNT'000	2016 MNT'000
Personnel expenses*	4,118,939	2,737,063
Professional service fees	1,003,859	876,520
Other operating expenses	956,597	1,070,702
Depreciation expense (Note 14)	496,718	529,069
Entertainment expense	246,257	216,567
Utility expense	150,544	127,824
Amortisation of intangible assets (Note 15)	54,586	61,188
Write-off of property and equipment (Note 14)	–	3,149
Loss on disposal of property and equipment	86	300
	<u>7,027,586</u>	<u>5,622,382</u>
<b>* Personnel expenses</b>		
Salaries, wages and bonus	3,388,845	2,402,332
Contribution to social and health fund	382,713	295,488
Staff training	324,424	39,243
Others	22,957	–
	<u>4,118,939</u>	<u>2,737,063</u>

### 8. Income tax expense

The components of income tax expense for the years ended 31 December 2017 and 2016 are:

	2017 MNT'000	2016 MNT'000
<b>Current tax</b>		
Current income tax	6,292,252	3,662,297
<b>Deferred tax</b>		
Relating to origination of temporary differences (Note 19)	5,585,639	4,489,547
	<u>11,877,891</u>	<u>8,151,844</u>

The Group provides for income taxes on the basis of its income for financial reporting purposes, adjusted for items which are not assessable or deductible for income tax purposes. The income tax rate for profits of the Group are 10% (2016: 10%) for the first MNT3 billion (2016: MNT 3 billion) of taxable income, and 25% (2016: 25%) on the excess of taxable income over MNT 3 billion (2016: MNT 3 billion).

A reconciliation of income tax expense applicable to profit before tax at the statutory income tax rate to income tax expense at the effective income tax rate of the Group for the years ended 31 December are as follows:

	2017 MNT'000	2016 MNT'000
Profit before tax	71,040,878	58,889,737
Tax at statutory tax rate of 25% (2016: 25%)	17,760,220	14,722,434
Effect of principal repayment of collateralized bonds as tax deductible	(49,852,775)	(41,742,375)
Effect of expenses not deductible for tax purposes	576,636	1,643,776
Effect of income subject to lower tax rate	(4,940,880)	(951,362)
Effect of income not subject to tax	–	(25,250)
Deferred tax asset not recognized for tax losses	39,750,720	26,985,714
Deferred tax liability recognized for withholding tax on future dividend	5,585,639	4,489,547
Others	2,998,331	3,029,360
Tax expense for the year	<u>11,877,891</u>	<u>8,151,844</u>

The Group has tax losses of MNT'000 274,538,476 (2016: MNT'000 192,288,364) that are available to offset against future taxable profits for the next two financial years. The annual amount of tax loss deductible from taxable income is limited to 50% of the taxable income in a given year. The Group's tax losses are mainly arising from the SPCs.

As per Mongolian Corporate Income Taxation Law, the principal repayment of asset backed bonds issued by a licensed company (in the Group's case, the collateralised bonds issued) is deductible for tax purpose. As a result, it is uncertain whether the SPCs will generate future taxable profits.

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 8. Income tax expense (cont'd.)

Deferred tax assets arising from tax losses are not recognized as the Group is uncertain whether there would be sufficient taxable profit in the next two years available against which the tax losses carried forward can be utilized.

The effective income tax rate for the Group for the year ended 31 December 2017 is 16.72% (2016: 13.84%).

#### 9. Earnings per share

The following table shows the income and share data used in the basic and diluted earnings per share calculations:

	2017 MNT'000	2016 MNT'000
Profit for the year and total comprehensive income for the year (net of tax) attributable to equity holder of the Parent	<u>59,162,987</u>	<u>50,737,893</u>
Weighted average number of ordinary shares for basic and diluted earnings per share*	<u>18,602,831</u>	<u>20,046,815</u>
<b>Earnings per share</b>		
	MNT	MNT
Equity holders of the Parent for the year:		
Basic and diluted earnings per share	<u>3,180.32</u>	<u>2,530.97</u>

\* The weighted average number of shares takes into account the weighted average effect of changes in treasury share transactions during the year.

#### 10. Cash and bank balances

	2017 MNT'000	2016 MNT'000
Cash on hand	<u>2,938</u>	<u>3,377</u>
Term deposits	171,189,305	125,937,881
Trust accounts with banks	26,921,051	17,051,421
Collection accounts with banks	7,548,701	7,487,625
Current accounts with banks	<u>7,288,611</u>	<u>6,039,073</u>
	<u>212,947,668</u>	<u>156,516,000</u>
	<u>212,950,606</u>	<u>156,519,377</u>

All bank accounts are placed in commercial banks operating in Mongolia, and most of these commercial banks are shareholders of the Group. The trust accounts with banks represent current accounts where the collections made by commercial banks on behalf of the Group on the purchased mortgage pool receivables are accumulated and are deposited into the current accounts on monthly basis. The collection account is used for repayment of the RMBS. The carrying amount of cash and cash equivalents approximates fair value.

Bank balances amounting to MNT 3,159,637 thousand is collateralized for the loan obtained (Note 16).

The Group earns interest income at a rate of 7.9% to 17.95% (2016: 12.0% to 17.95%) per annum on term deposits.

#### Additional cash flow information

	2017 MNT'000	2016 MNT'000
Cash and bank balances	212,950,606	156,519,377
Less: Placement with banks with original maturities of more than three months	<u>(100,856,887)</u>	<u>(16,265,664)</u>
Total cash and cash equivalents for the consolidated statement of cash flow	<u>112,093,719</u>	<u>140,253,713</u>

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 11. Mortgage pool receivables with recourse

The Group acquires mortgage pool receivables with recourse from commercial banks, most of whom are shareholders of the Group, through the process similar to the acquisition of mortgage pool receivables without recourse (Note 12). However, in the case of mortgage pool receivables with recourse, the Group has the right to request from the respective commercial bank, when any individual mortgage loan is overdue more than 90 days, either to replace the defaulted loan with another performing mortgage loan with similar terms or to pay immediately in cash an amount equal to the carrying amount of the defaulted loan plus accumulated interest. Thus, mortgage pool receivables with recourse represent, in substance, loans issued to commercial banks in Mongolia, which are collateralized by related mortgage loan receivables of those commercial banks, as well as by the related residential properties that are used as collateral, as additional guarantee.

The Group applies similar procedure for assessment of individual mortgage loans, as in the case of mortgage pool receivables without recourse (Note 12). The Group performs credit quality analysis of the individual mortgage loans on each mortgage pool acquired. The Group also assesses the financial condition of the banks, as well as their general reputation in the Mongolian market.

	2017 MNT'000	2016 MNT'000
Mortgage pool receivables	29,738,506	28,625,648
Accrued interest receivables	87,059	14,298
	<u>29,825,565</u>	<u>28,639,946</u>

Past due but not impaired loan receivables are expected to be either fully paid by the respective commercial bank or replaced with another performing mortgage loan, if related loans become overdue more than 90 days. The ageing analysis of mortgage pool receivables is set out in Note 24.2. No impairment was noted under neither collective nor individual assessment mainly due to the fact that the Group has the right to enforce the selling commercial banks to purchase back the loans which were overdue or to replace with other performing loans of similar nature, which is evidenced by insignificant amount of loans which are past due over 90 days. Currently, the management is closely monitoring those loans and accordingly will consider if the Group would exercise its right.

In accordance with the Group's credit risk procedures, the ratio between the carrying amount of purchased loan and the fair value of collateral (apartment or other residential property) at the time of purchase of mortgage pools should not be greater than 70%. Collateral is analysed by the Group on an individual loan basis prior to inclusion of related loan in the acquired mortgage pool. In addition, the Group has first claim rights over all residential properties used as collateral (i.e. priority rights before other creditors).

#### 12. Purchased mortgage pool receivables

	2017 MNT'000	2016 MNT'000
Purchased mortgage pool receivables	2,518,132,429	2,123,071,639
Accrued interest receivables	11,630,846	9,188,902
<b>Total gross purchased mortgage pool receivables</b>	<u>2,529,763,275</u>	<u>2,132,260,541</u>
Allowance for impairment losses	(11,707,125)	(10,033,385)
<b>Net purchased mortgage pool receivables</b>	<u>2,518,056,150</u>	<u>2,122,227,156</u>

Purchased mortgage pool receivables represent mortgage loan receivables due from individual borrowers, purchased from Mongolian commercial banks, most of whom are shareholders of the Group. All significant risks and rewards related to these mortgage loans, including the rights to the related collateral, are fully transferred to the Group at acquisition of the mortgage pools.

For the purchase of these mortgage pool receivables, the Group follows credit risk procedures similar to the mortgage pool receivables with recourse (See Note 11). The Group performs credit quality analysis of the individual mortgage loans on each mortgage pool acquired. For credit risk policies and disclosures, please refer to Note 24.2.

#### Impairment allowance for purchased mortgage pool receivables

Allowance for impairment losses are fully related to collectively impaired loans as the management assessed that none of the loans were individually impaired.



**MIK HOLDING JSC AND ITS SUBSIDIARIES**

**Notes to the Consolidated Financial Statements – 31 December 2017**

**12. Purchased mortgage pool receivables (cont'd.)**

A reconciliation of the allowance for impairment losses for purchased mortgage pool receivables is as follows:

	2017 MNT'000	2016 MNT'000
At 1 January	10,033,385	3,762,258
Charge for the year	1,673,740	6,271,976
Write-off	–	(849)
At 31 December	<u>11,707,125</u>	<u>10,033,385</u>

**13. Other assets**

	2017 MNT'000	2016 MNT'000
Prepayments	599,406	168,654
Foreclosed properties	169,791	109,859
Consumables and office supplies	16,413	13,155
Other receivables	8,584	40,303
	<u>794,194</u>	<u>331,971</u>

**14. Property and equipment**

	Premises MNT'000	Furniture and office equipment MNT'000	Computers MNT'000	Vehicles MNT'000	Total MNT'000
<b>At 31 December 2017</b>					
<b>At cost</b>					
At 1 January 2017	14,458,594	294,247	357,644	570,802	15,681,287
Additions	–	61,692	139,438	196,401	397,531
Disposal	–	–	–	(105,000)	(105,000)
At 31 December 2017	<u>14,458,594</u>	<u>355,939</u>	<u>497,082</u>	<u>662,203</u>	<u>15,973,818</u>
<b>Accumulated depreciation</b>					
At 1 January 2017	641,555	63,932	215,352	71,161	992,000
Charge for the year (Note 7)	361,463	30,340	48,177	56,738	496,718
Disposal	–	–	–	(41,914)	(41,914)
At 31 December 2017	<u>1,003,018</u>	<u>94,272</u>	<u>263,529</u>	<u>85,985</u>	<u>1,446,804</u>
<b>Net carrying amount</b>	<u>13,455,576</u>	<u>261,667</u>	<u>233,553</u>	<u>576,218</u>	<u>14,527,014</u>

Premise with carrying amount of MNT 13,052,558 thousand is collateralized for the loan (See Note 16)

MIK HOLDING JSC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements – 31 December 2017

14. Property and equipment (cont'd.)

At 31 December 2016	Premises MNT'000	Furniture and office equipment MNT'000	Computers MNT'000	Vehicles MNT'000	Deposit for premises MNT'000	Total MNT'000
<b>At cost</b>						
At 1 January 2016	14,405,227	294,599	280,007	105,001	176,446	15,261,280
Additions	26,000	15,325	81,260	465,801	–	588,386
Write-off (Note 7)	–	(13,317)	(1,304)	–	–	(14,621)
Disposal	–	(3,294)	(2,319)	–	–	(5,613)
Reclassification	27,367	934	–	–	(28,301)	–
Transfer	–	–	–	–	(148,145)	(148,145)
At 31 December 2016	<u>14,458,594</u>	<u>294,247</u>	<u>357,644</u>	<u>570,802</u>	<u>–</u>	<u>15,681,287</u>
<b>Accumulated depreciation</b>						
At 1 January 2016	279,499	46,696	126,657	26,180	–	479,032
Charge for the year (Note 7)	362,056	29,714	92,318	44,981	–	529,069
Write-off (Note 7)	–	(10,168)	(1,304)	–	–	(11,472)
Disposal	–	(2,310)	(2,319)	–	–	(4,629)
At 31 December 2016	<u>641,555</u>	<u>63,932</u>	<u>215,352</u>	<u>71,161</u>	<u>–</u>	<u>992,000</u>
<b>Net carrying amount</b>	<u>13,817,039</u>	<u>230,315</u>	<u>142,292</u>	<u>499,641</u>	<u>–</u>	<u>14,689,287</u>

15. Intangible assets

	Computer software	
	2017 MNT'000	2016 MNT'000
<b>At cost</b>		
At 1 January	239,923	194,448
Additions	90,534	45,475
Total	<u>330,457</u>	<u>239,923</u>
<b>Accumulated amortization</b>		
At 1 January	163,302	102,114
Charge for the year (Note 7)	54,586	61,188
Total	<u>217,888</u>	<u>163,302</u>
<b>Net carrying amount</b>	<u>112,569</u>	<u>76,621</u>

16. Borrowed funds

	2017 MNT'000	2016 MNT'000
Loan from Ulaanbaatar City Bank LLC (Note 23)	7,022,151	–
Ministry of Finance of Mongolia	8,476,693	8,552,889
	<u>15,498,844</u>	<u>8,552,889</u>

The Group obtained a loan of MNT 7 billion from Ulaanbaatar City Bank LLC on 25 December 2017 to finance its purchase of the treasury shares (See Note 20). The loan bears interest rate of 16.5% and the loan principal is repayable monthly starting from 25 December 2017 until 25 December 2018. The loan is secured by the property (See Note 14), the accounts of MIK HFC placed with Ulaanbaatar City Bank LLC amounting to MNT 3,159,637 thousand and related income such as interest income and service fee income.

The sub-lending agreement between the Ministry of Finance and the Group was made on 3 January 2011. The Group has fully drawn the full amount of the loan in 2012. The loan bears nominal interest rate of 4% (2016: 4%) and the interest is payable on 30 May and 30 November of each year, while the principal is payable in 2020. The borrowing is not collateralized.

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 17. Collateralized bonds

	Interest rate	2017 MNT'000	2016 MNT'000
Senior bonds	4.5%	2,264,535,907	1,915,826,604
Junior bonds	10.5%	311,474,582	249,749,441
		<u>2,576,010,489</u>	<u>2,165,576,045</u>

The senior and junior bonds as at 31 December 2017 and 31 December 2016 represent bonds issued by MIK Asset One SPC LLC, MIK Asset Two SPC LLC, MIK Asset Three SPC LLC, MIK Asset Four SPC LLC, MIK Asset Five SPC LLC, MIK Asset Six SPC LLC, MIK Asset Seven SPC LLC, MIK Asset Eight SPC LLC, MIK Asset Nine SPC LLC, MIK Asset Ten SPC LLC, MIK Asset Eleven SPC LLC, MIK Asset Twelve SPC LLC and MIK Asset Thirteen SPC LLC to BoM and commercial banks on 23 December 2013, 8 July 2014, 7 November 2014, 30 January 2015, 10 June 2015, 21 August 2015, 11 December 2015, 5 February 2016, 22 April 2016, 1 February 2017, 17 May 2017 and 27 October 2017 respectively under the RMBS program of the government of Mongolia. The bonds are collateralized by the purchased mortgage pool receivables (see Note 12). The interest rates on the junior bonds and the senior bonds are 10.5% and 4.5% per annum respectively and are payable on a quarterly basis.

The principal payments of the senior bonds are payable on a quarterly basis and are equal to the quarterly principal repayment received from the purchased mortgage pool receivables acquired under the RMBS program. The principal of the junior bonds will only be redeemed after the full redemption of the principal of the senior bonds and the payments to junior bond holders are subordinate in right of payment and priority to the senior bonds. Commercial banks are to use the senior bonds to repay their loans from BoM.

The bonds are not publicly traded on an active market (such as the stock exchange), but are sold directly to commercial banks. The Group did not have any defaults of principal, interest or other breaches with respect to the collateralized bonds during 2017 and 2016.

The gross amount of purchased mortgage pool receivables used as collateral for the total collateralized bonds as of 31 December 2017 is MNT'000 2,529,763,275 (2016: MNT'000 2,132,260,541) (See Note 12).

#### 18. Other liabilities

	2017 MNT'000	2016 MNT'000
Deferred grant	77,427	78,485
Other payables	4,736,168	3,923,265
	<u>4,813,595</u>	<u>4,001,750</u>

Included in other payables are loan service fee payables to the banks for the collection of the purchased mortgage pool receivables.

Loan service fee is normally settled to the banks with the next quarterly coupon payment of the RMBS (See Note 23).

Movements in deferred grants are presented as follows:

	2017 MNT'000	2016 MNT'000
Balance at beginning of year	78,485	89,309
Recognised in profit or loss (Note 6)	(1,058)	(10,824)
	<u>77,427</u>	<u>78,485</u>

#### 19. Deferred tax liability

	2017 MNT'000	2016 MNT'000
At 1 January	8,214,763	3,725,216
Recognised in statement of comprehensive income (Note 8)	5,585,639	4,489,547
At 31 December	<u>13,800,402</u>	<u>8,214,763</u>

Deferred tax liability represents future withholding tax liabilities against the future dividend distribution of the SPCs upon liquidation.

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 20. Ordinary shares

The Company is a joint stock company established under the Company Law of Mongolia and listed on the Mongolian Stock Exchange on 24 December 2015. The total authorized share capital of the Company represents 30,000,000 ordinary shares (2016: 30,000,000) with nominal value of MNT 1,000 per share.

The movement in number of shares and amount of share capital during the years ended 31 December 2017 and 31 December 2016 are as follows:

	Number of outstanding shares of MNT 1,000 each	Ordinary shares MNT'000	Share premium MNT'000
<b>At 1 January/31 December 2016 and 1 January/31 December 2017</b>	<u>20,709,320</u>	<u>20,709,320</u>	<u>52,225,115</u>

There were 4,136,790 shares held as treasury shares as at 31 December 2017 (2016: 2,066,790). By excluding these shares, the total number of issued shares as at 31 December 2017 was 16,572,530 shares (2016: 18,642,530 shares). All issued ordinary shares are fully paid. Each ordinary share carries one vote.

On 16 March 2017 (2016: 18 March 2016), the Group declared cash dividends to its shareholders at MNT 471.6 per share (2016: MNT 241.2 per share) amounting to MNT 8,791,817 thousand (2016: MNT 4,995,088 thousand) from profit of MIK HFC.

The Group repurchased 2,070,000 shares (2016: 2,066,790 shares) in total from Trade and Development Bank LLC and Ulaanbaatar City Bank LLC at MNT 11,110 per share (2016: MNT 11,640) under the share sell and purchase agreements dated 22 December 2017 and 26 December 2017 (2016: 05 September 2016) amounting to MNT 22,997,700 thousand (2016: MNT 24,057,436 thousand). (Note 23)

The shareholders of the Group as of 31 December 2017 and 31 December 2016 and percentages of ownership are as follows:

	2017	2016
Ulaanbaatar City Bank LLC	26.13%	25.46%
Trade and Development Bank of Mongolia LLC	9.99%	20.66%
Capital Bank LLC	8.12%	8.12%
TDB Capital LLC	7.49%	7.50%
Golomt Bank LLC	5.57%	5.57%
Khan Bank LLC	1.02%	1.02%
XacBank LLC	1.02%	1.02%
Capitron Bank LLC	1.02%	1.02%
Chinggis Khaan Bank LLC	0.30%	0.30%
Others	0.08%	0.05%
United securities LLC	0.00%	–
Total private sector share	<u>60.74%</u>	<u>70.72%</u>
Development Bank of Mongolia	14.88%	14.88%
Bank of Mongolia	2.03%	2.03%
State Bank LLC	2.37%	2.39%
Total state share:	<u>19.28%</u>	<u>19.30%</u>
Treasury shares	<u>19.98%</u>	<u>9.98%</u>
Total	<u>100.00%</u>	<u>100.00%</u>

Financial and operating policy decisions, including strategic decisions, are made at the meetings of the Board of Directors (“BOD”). The members of the BOD are appointed at the Shareholders’ Meeting. As of 31 December 2017, each shareholder that has more than 1% of total shares of the Group, has the ability to nominate one member to the BOD, which consists of 9 members, including 3 independent members and representatives of the commercial banks and state owned banks. In addition, all bank shareholders have material transactions with the Group during 2017 and participated in the policy making procedures.

## 21. Contingent liabilities and commitments

### Legal claims

Litigation is a common occurrence in the financial services industry due to the nature of the business. The Group has an established protocol for dealing with such legal claims. Once professional advice has been obtained and the amount of damages can be reasonably estimated, the Group makes adjustments to account for any adverse effects which the claim may have on its financial standing. At the year end, the Group had no significant outstanding litigation.

### Tax legislation

Mongolian tax legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by tax authorities.

Mongolian tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged by tax authorities. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for five calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Mongolian transfer pricing legislation provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of all controllable transactions, including those related to domestic transfer pricing. In case of deviation of transaction terms from market terms, the tax authorities have the right to adjust taxable items and to impose additional taxes, fines and interest penalties. Given the brief nature of the current Mongolian transfer pricing rules, the impact of any such challenge cannot be reliably estimated. However, it may be significant to the financial position and/or the overall operations of the entity.

Mongolian tax legislation does not provide definitive guidance in certain areas, specifically in areas such as VAT, withholding tax, corporate income tax, personal income tax and other areas. From time to time, the Group adopts interpretations of such uncertain areas that reduce the overall tax rate of the Group. As noted above, such tax positions may come under heightened scrutiny as a result of recent developments in administrative and court practices. The impact of any challenge by the tax authorities cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the entity.

Management performs regular re-assessment of tax risks and its position may change in the future as a result of the change in conditions that cannot be anticipated with sufficient certainty at present.

### Assets pledged and restricted

Bonds issued by the Group are fully collateralised by the purchased mortgage pool receivables. As of 31 December 2017, the Group had mortgage pool receivables with the gross amount of MNT'000 2,529,763,275 (2016: MNT'000 2,132,260,541) pledged as collateral for the bonds. The related liabilities amount is MNT'000 2,576,010,489 as of 31 December 2017 (2016: MNT'000 2,165,576,045) (See Notes 12 and 17).

**22. Maturity analysis of assets and liabilities**

The table shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled. See Note 24.3 'Liquidity risk' for the Group's contractual undiscounted repayment obligations.

	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
<b>At 31 December 2017</b>			
<b>Financial assets</b>			
Cash and bank balances	212,950,606	–	212,950,606
Mortgage pool receivables with recourse	3,332,253	26,493,312	29,825,565
Purchased mortgage pool receivables	145,292,156	2,372,763,994	2,518,056,150
Other assets	8,584	–	8,584
	<u>361,583,599</u>	<u>2,399,257,306</u>	<u>2,760,840,905</u>
<b>Non-financial assets</b>			
Property and equipment	–	14,527,014	14,527,014
Intangible assets	–	112,569	112,569
Other assets	785,610	–	785,610
	<u>785,610</u>	<u>14,639,583</u>	<u>15,425,193</u>
<b>Total</b>	<u>362,369,209</u>	<u>2,413,896,889</u>	<u>2,776,266,098</u>
<b>Financial liabilities</b>			
Borrowed funds	7,058,072	8,440,772	15,498,844
Collateralized bonds	165,434,351	2,410,576,138	2,576,010,489
Other liabilities	4,727,014	–	4,727,014
	<u>177,219,437</u>	<u>2,419,016,910</u>	<u>2,596,236,347</u>
<b>Non-financial liabilities</b>			
Other liabilities	86,581	–	86,581
Income tax payable	3,639,426	–	3,639,426
Deferred tax liability	–	13,800,402	13,800,402
	<u>3,726,007</u>	<u>13,800,402</u>	<u>17,526,409</u>
<b>Total</b>	<u>180,945,444</u>	<u>2,432,817,312</u>	<u>2,613,762,756</u>
<b>Net</b>	<u>181,423,765</u>	<u>(18,920,423)</u>	<u>162,503,342</u>

MIK HOLDING JSC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements – 31 December 2017

22. Maturity analysis of assets and liabilities (cont'd.)

	Less than 12 months MNT'000	More than 12 months MNT'000	Total MNT'000
<b>At 31 December 2016</b>			
<b>Financial assets</b>			
Cash and bank balances	156,519,377	–	156,519,377
Mortgage pool receivables with recourse	3,040,474	25,599,472	28,639,946
Purchased mortgage pool receivables	123,740,781	1,998,486,375	2,122,227,156
Other assets	40,303	–	40,303
	<u>283,340,935</u>	<u>2,024,085,847</u>	<u>2,307,426,782</u>
<b>Non-financial assets</b>			
Property and equipment	–	14,689,287	14,689,287
Intangible assets	–	76,621	76,621
Other assets	291,668	–	291,668
	<u>291,668</u>	<u>14,765,908</u>	<u>15,057,576</u>
<b>Total</b>	<u>283,632,603</u>	<u>2,038,851,755</u>	<u>2,322,484,358</u>
<b>Financial liabilities</b>			
Borrowed funds	112,117	8,440,772	8,552,889
Collateralized bonds	139,021,425	2,026,554,620	2,165,576,045
Other liabilities	3,921,197	–	3,921,197
	<u>143,054,739</u>	<u>2,034,995,392</u>	<u>2,178,050,131</u>
<b>Non-financial liabilities</b>			
Other liabilities	80,553	–	80,553
Income tax payable	1,009,039	–	1,009,039
Deferred tax liability	–	8,214,763	8,214,763
	<u>1,089,592</u>	<u>8,214,763</u>	<u>9,304,355</u>
<b>Total</b>	<u>144,144,331</u>	<u>2,043,210,155</u>	<u>2,187,354,486</u>
<b>Net</b>	<u>139,488,272</u>	<u>(4,358,400)</u>	<u>135,129,872</u>

**MIK HOLDING JSC AND ITS SUBSIDIARIES**
**Notes to the Consolidated Financial Statements – 31 December 2017**
**23. Related party disclosures**

A number of the Group's transactions are entered into with related parties in the normal course of business.

As all shareholders have the right to appoint a director, management considers them to be related parties.

As at 31 December 2017, the Group has the following balances and transactions with related parties:

As at 31 December 2017	Bank Deposits		Collateralized Bonds			
	Outstanding	Interest	Issued during the year		Outstanding	Interest
	balances	income	senior bonds	junior bonds	balance	expense
	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000
Trade and Development Bank LLC	91,498,893	6,311,993	153,569,000	17,063,400	76,045,991	7,187,768
Golomt Bank LLC	24,038,569	1,686,773	121,383,000	13,486,800	83,366,657	7,979,459
Ulaanbaatar City Bank LLC	63,903,267	6,569,580	13,383,000	1,487,000	10,652,922	1,099,631
Chinggis Khaan Bank LLC	61,650	1,864	1,741,200	193,400	867,041	82,237
Capital Bank LLC	6,091,854	377,660	13,408,200	1,489,800	8,530,842	875,029
State Bank LLC	17,552,042	4,530,250	53,161,000	5,906,800	25,403,971	2,352,928
Xac Bank LLC	3,036,261	927,145	39,772,800	4,419,200	27,445,172	2,622,105
Khan Bank LLC	6,324,712	699,128	130,149,900	14,461,200	73,642,736	6,963,417
Capitron Bank LLC	246,087	4,769	6,769,100	752,200	2,393,491	166,508
<b>Total</b>	<b>212,753,335</b>	<b>21,109,162</b>	<b>533,337,200</b>	<b>59,259,800</b>	<b>308,348,823</b>	<b>29,329,082</b>
Bank of Mongolia	–	–	–	–	2,264,535,907	95,534,222
<b>Total</b>	<b>212,753,335</b>	<b>21,109,162</b>	<b>533,337,200</b>	<b>59,259,800</b>	<b>2,572,884,730</b>	<b>124,863,304</b>

**Mortgage pool portfolio**

As at 31 December 2017	Purchase of mortgage pool		Outstanding balance*		Interest income from mortgage pool*		Loan service fee
	with recourse	without recourse**	with recourse	without recourse	with recourse	without recourse	
	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	
Trade and Development Bank	5,370,059	170,632,476	5,222,119	608,872,138	358,417	45,411,347	2,441,870
Golomt Bank LLC	9,251,113	134,870,132	8,181,014	678,264,228	1,773,634	51,454,437	2,763,122
Ulaanbaatar City Bank LLC	200,853	14,870,178	2,689,918	83,895,536	429,362	6,656,656	410,149
Chinggis Khaan Bank LLC	–	1,934,673	–	7,578,735	62,896	566,788	25,795
Capital Bank LLC	–	14,898,247	4,629,641	76,240,909	509,799	5,825,123	284,357
State Bank LLC	–	59,068,060	5,148,230	207,476,986	887,645	14,995,537	755,192
Xac Bank LLC	–	44,192,142	2,797,394	226,228,250	485,654	17,055,188	869,335
Khan Bank LLC	–	144,611,257	–	599,030,028	3,701	44,430,955	2,281,497
Capitron Bank LLC	–	7,521,474	1,157,249	16,031,044	62,885	1,210,237	56,453
<b>Total</b>	<b>14,822,025</b>	<b>592,598,639</b>	<b>29,825,565</b>	<b>2,503,617,854</b>	<b>4,573,993</b>	<b>187,606,268</b>	<b>9,887,770</b>



MIK HOLDING JSC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements – 31 December 2017

23. Related party disclosures (cont'd.)

As at 31 December 2016

	Bank Deposits		Collateralized Bonds			
	Outstanding	Interest	Issued during the year		Outstanding	Interest
	balances	income	senior bonds	junior bonds	balance	expense
	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000
Trade and Development Bank LLC	45,143,653	4,763,627	54,938,700	6,104,400	58,666,199	5,983,486
Golomt Bank LLC	19,436,123	1,603,575	49,245,700	5,471,800	69,607,543	7,119,131
Ulaanbaatar City Bank LLC	50,652,933	4,947,563	14,778,700	1,642,000	9,132,415	914,333
Chinggis Khaan Bank LLC	56,989	680	2,222,300	246,900	670,752	61,884
Capital Bank LLC	1,109,302	76,019	9,063,400	1,007,000	7,468,874	751,873
State Bank LLC	14,113,755	1,291,850	20,434,000	2,270,400	19,386,812	1,973,761
Xac Bank LLC	19,674,524	1,694,398	36,735,400	4,081,700	22,936,079	2,322,577
Khan Bank LLC	5,850,242	1,622,071	73,376,000	8,152,800	58,905,200	6,000,636
Capitron Bank LLC	140,169	2,246	596,200	66,200	1,170,642	119,628
<b>Total</b>	<b>156,177,690</b>	<b>16,002,029</b>	<b>261,390,400</b>	<b>29,043,200</b>	<b>247,944,516</b>	<b>25,247,309</b>
Bank of Mongolia	–	–	–	–	1,915,826,604	88,101,415
<b>Total</b>	<b>156,177,690</b>	<b>16,002,029</b>	<b>261,390,400</b>	<b>29,043,200</b>	<b>2,163,771,120</b>	<b>113,348,724</b>

Mortgage pool portfolio

As at 31 December 2016

	Purchase of mortgage pool		Outstanding balance		Interest income from mortgage pool*		Loan service fee
	with recourse	without recourse**	with recourse	without recourse	with recourse	without recourse	
	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	
Trade and Development Bank	613,153	61,043,170	502,111	490,597,559	32,625	40,012,514	2,028,318
Golomt Bank LLC	6,165,108	54,717,570	5,414,538	602,746,000	332,547	49,277,362	2,430,799
Ulaanbaatar City Bank LLC	3,165,449	16,420,807	3,279,941	78,338,790	380,962	6,347,092	350,548
Chinggis Khaan Bank LLC	672,872	2,469,300	658,848	6,069,305	20,737	437,329	16,853
Capital Bank LLC	4,238,061	10,070,577	5,551,294	66,358,420	422,100	5,264,214	228,191
State Bank LLC	5,602,291	22,704,525	7,200,930	163,170,720	793,382	13,653,498	636,113
Xac Bank LLC	–	40,817,218	3,816,161	199,039,015	648,514	16,091,998	764,062
Khan Bank LLC	–	81,528,951	20,279	501,420,755	6,100	40,697,002	1,939,726
Capitron Bank LLC	1,795,735	662,469	1,649,909	9,604,950	138,364	790,412	38,484
<b>Total</b>	<b>22,252,669</b>	<b>290,434,587</b>	<b>28,094,011</b>	<b>2,117,345,514</b>	<b>2,775,331</b>	<b>172,571,421</b>	<b>8,433,094</b>

\* Outstanding balance/interest income from mortgage pool with/without recourse represents the principal/interest income from individual borrowers that are passed through to the Group via the commercial banks.

\*\* Difference between issuance of RMBS (senior and junior) and the purchased mortgage pool (without recourse) is the cash payment of the Group to the respective commercial banks amounting to MNT 1,639 thousand (2016: MNT 987 thousand).

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 23. Related party disclosures (cont'd.)

##### Borrowings

The Group obtained loans of MNT 1.5 billion and MNT 7 billion from Ulaanbaatar City Bank LLC on 1 May 2017 and 25 December 2017 with interest rates of 19.2% and 16.5% per annum, respectively. The loan principal of MNT 1.5 billion was full repaid while the other loan's principal is repayable monthly starting from 25 December 2017 until 25 December 2018. The loan is secured by the property (See Note 14) and accounts of MIK HFC placed with Ulaanbaatar City Bank LLC and related incomes such as current account income, deposits, future interest incomes and service fee income (See Note 10). Interest expense for these borrowings amounted to MNT'000 54,817 (2016: Nil).

##### Other payables

Other payables include loan service fee payable to the banks for the collection of the purchased mortgage pool receivables as follows.

	2017 MNT'000	2016 MNT'000
Trade and Development Bank LLC	1,086,304	792,711
Golomt Bank LLC	1,194,192	976,197
Ulaanbaatar City Bank LLC	176,159	148,279
Chinggis Khaan Bank LLC	11,810	8,773
Capital Bank LLC	130,464	90,950
State Bank LLC	340,126	257,600
Xac Bank LLC	417,024	318,935
Khan Bank LLC	967,115	737,314
Capitron Bank LLC	24,766	14,779
<b>Total</b>	<u>4,347,960</u>	<u>3,345,538</u>

Loan service fee is normally settled with the banks with the next quarterly coupon payment of the RMBS.

##### Repurchase of shares

The Group repurchased 2,070,000 shares (2016: 2,066,790 shares) in total from Trade and Development Bank LLC and Ulaanbaatar City Bank LLC at MNT 11,110 per share (2016: MNT 11,640) under the share sell and purchase agreements dated 26 December 2017 (2016: 05 September 2016) amounting to MNT 22,997,700 thousand (2016: MNT 24,057,436 thousand) (See Note 20).

##### Compensation to key management personnel

	2017 MNT'000	2016 MNT'000
Short-term employees benefits		
• Salaries, incentives and allowances	476,346	512,110
• Contribution to social and health fund	50,679	55,627
	<u>527,025</u>	<u>567,737</u>

##### Terms and conditions of transactions with related parties

The above mentioned outstanding balances arose from the ordinary course of the Group's business. The interest charged to and by related parties are at normal commercial rates in relation to bank deposits, borrowings and mortgage pools and at the rates specified in the RMBS. There have been no guarantees provided or received for any related party receivables or payables. For the year ended 31 December 2017 and 31 December 2016, the Group has no provision for doubtful debts against the amounts due from related parties.

## 24. Risk management

### 24.1 Introduction

The Group's business activities expose it to the following major categories of financial risk:

- Credit risk. Credit risk is the potential for financial loss resulting from the failure of a borrower or institutional counterparty to honor its financial or contractual obligations, resulting in a potential loss of earnings or cash flows.
- Liquidity risk. Liquidity risk is the risk that the Group will not be able to meet its funding obligations in a timely manner.
- Market risk. Market risk is the exposure generated by adverse changes in the value of the Group's financial assets caused by a change in interest rates or foreign exchange rates.
- Operational risk. Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems, corporate governance, or from external events.

The Group seeks to manage those risks by using an established risk management framework that continues to evolve as the Group grows and expands its business. This risk management framework is intended to provide the basis of the principles that govern the Group's risk management activities.

### Risk management structure

The Company has its dedicated BOD appointed by its shareholders. The BOD is responsible for the oversight of asset management and execution of responsibility through the board committee system, which includes the following standing committees: the Risk Committee ("RC"), the Finance and Audit Committee ("FAC"), and the Operations and Legal Committee ("OLC").

The RC oversees general risk-related policies, including review of the Group-level risk policies and limits, performance against these policies and limits, and the sufficiency of risk management capabilities. In addition to overseeing liquidity risk and market risk in association with the RC, the FAC reviews the Group's system of internal controls, and approves purchases of pools of mortgage loan receivables. The OLC oversees operational risk and legal compliance.

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

### 24.2 Credit risk

The Group's credit risk exists primarily from the pools of mortgage loan receivables that it has purchased. In regards to mortgage loan receivables, the credit risk is the risk of not receiving principal or interest on a timely basis due to the borrowers not making payments on time.

The procedures include thorough due diligence to ensure that the commercial banks comply with the quality standards based on those established by the BoM and the use of an assessment model that utilises both qualitative and quantitative measurements related to the overall quality of mortgage loans to be purchased.

The Group also has developed eligibility criteria for the loan receivables that they can acquire. The criteria are set for the borrower, loan, collateral asset and loan documents based on Mongolian Law and the requirements set by BoM. The loan files for every loan receivable to be purchased are checked for completeness for each borrower, and management has procedures and policy in place to ensure that the eligibility criteria are met.

After the pool of loan receivables are purchased, the Group receives daily settlement reports and reconciles the information, on a monthly basis. A consolidated quality report is obtained from the loan origination banks. These reports are used to closely monitor the performance of the loan origination banks in collecting loan payments on behalf of the Group. In addition, follow ups are made with the loan origination banks on any loans with slow repayment history. The policies and procedures for selecting loan receivables for purchase have been approved and are monitored by the RC.

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 24. Risk management (cont'd.)

##### 24.2 Credit risk (cont'd.)

##### Maximum exposure to credit risk without taking account of any collateral and other credit enhancements

The table below shows the maximum exposure to credit risk for the components of the statement of financial position. The maximum exposure is shown gross, before the effect of mitigation through the use of collateral agreements.

	Gross maximum exposure	
	2017 MNT'000	2016 MNT'000
Bank balances	212,947,668	156,516,000
Mortgage pool receivables with recourse	29,825,565	28,639,946
Purchased mortgage pool receivables	2,529,763,275	2,132,260,541
Other assets	8,584	44,483
<b>Total credit risk exposure</b>	<b>2,772,545,092</b>	<b>2,317,460,970</b>

##### Collateral and other credit enhancements

Purchased mortgage pool receivables are collateralized by residential properties pledged under the mortgage loan agreements between the originating financial institutions and the individual mortgage loan borrowers.

The fair value of the properties held as collateral by the Group as at 31 December 2017 was MNT'000 4,912,954,949 (31 December 2016: MNT'000 3,773,155,494).

##### Credit quality per class of financial assets

	Note	Neither past due nor impaired MNT'000	Past due but not individually impaired				Total ** MNT'000
			Less than 30 days MNT'000	31 to 60 days MNT'000	61 to 90 days MNT'000	More than 91 days MNT'000	
<b>At 31 December 2017</b>							
Bank balances	10	212,947,668	–	–	–	–	212,947,668
Mortgage pool loan receivables with recourse*	11	26,116,467	2,741,762	507,373	430,475	29,488	29,825,565
Purchased mortgage pool receivables	12	2,368,811,136	109,189,349	14,978,798	6,626,230	30,157,762	2,529,763,275
Other assets	13	8,584	–	–	–	–	8,584
<b>Total</b>		<b>2,607,883,855</b>	<b>111,931,111</b>	<b>15,486,171</b>	<b>7,056,705</b>	<b>30,187,250</b>	<b>2,772,545,092</b>
<b>At 31 December 2016</b>							
Bank balances	10	156,516,000	–	–	–	–	156,516,000
Mortgage pool loan receivables with recourse*	11	26,889,099	1,473,297	159,609	18,398	99,543	28,639,946
Purchased mortgage pool receivables	12	1,981,467,031	107,294,046	17,209,181	8,114,278	18,176,005	2,132,260,541
Other assets	13	40,303	–	–	–	4,180	44,483
<b>Total</b>		<b>2,164,912,433</b>	<b>108,767,343</b>	<b>17,368,790</b>	<b>8,132,676</b>	<b>18,279,728</b>	<b>2,317,460,970</b>

\* The Group has the right to enforce the selling commercial banks to purchase back the loans which were overdue or to replace with other performing loans of similar nature. Currently, the management is closely monitoring those loans and accordingly will consider if the Group would exercise its right.

\*\* As at 31 December 2017 and 2016, none of the financial assets are individually impaired.

The credit quality of the portfolio is primarily monitored based on ageing reports and is analysed through monitoring delays in payment (particularly over 90 days) in subsequent periods.

## MIK HOLDING JSC AND ITS SUBSIDIARIES

### Notes to the Consolidated Financial Statements – 31 December 2017

#### 24. Risk management (cont'd.)

##### 24.2 Credit risk (cont'd.)

The Group purchases only performing mortgage loans (i.e. loans without delays). Thus, management believes that credit quality of purchased mortgage pools is adequate.

In accordance with the Group's credit risk procedures, the ratio between the carrying amount of purchased loans and the fair value of collateral (apartment or other residential property) at the time of purchase of the mortgage pools should not be greater than 70% and the Group has the first claim over all residential properties used as collateral.

##### 24.3 Liquidity risk

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. For managing the Group's liquidity risk, certain methods outlined below have been implemented.

##### Exposure to liquidity risk

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to current liabilities. However, the Group's repayment schedule of bonds is directly related to the collection of the repayments from the purchased mortgage pools; the Group has assessed that its exposure to liquidity risk is insignificant.

##### Analysis of financial liabilities by remaining contractual maturities

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2017 and 31 December 2016 based on contractual undiscounted repayment obligations.

	On demand	Less than 3 months	3 to 6 months	6 months to 1 year	1 to 5 years	Over 5 years	Total undiscounted financial liabilities
	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000
<b>At 31 December 2017</b>							
Borrowed funds	–	2,006,051	2,117,644	3,837,055	9,116,034	–	17,076,784
Collateralised bonds	–	84,376,638	71,317,566	142,821,088	1,136,965,677	2,684,607,294	4,120,088,263
Other liabilities	4,727,014	–	–	–	–	–	4,727,014
<b>Total</b>	<u>4,727,014</u>	<u>86,382,689</u>	<u>73,435,210</u>	<u>146,658,143</u>	<u>1,146,081,711</u>	<u>2,684,607,294</u>	<u>4,141,892,061</u>
<b>At 31 December 2016</b>							
Borrowed funds	–	–	168,815	168,815	9,791,296	–	10,128,926
Collateralised bonds	–	65,281,811	56,455,350	111,580,905	896,733,055	2,086,731,374	3,216,782,495
Other liabilities	3,921,197	–	–	–	–	–	3,921,197
<b>Total</b>	<u>3,921,197</u>	<u>65,281,811</u>	<u>56,624,165</u>	<u>111,749,720</u>	<u>906,524,351</u>	<u>2,086,731,374</u>	<u>3,230,832,618</u>

The above tables show the Group's exposure to liquidity risk based on the contractual maturities of financial liabilities; however, if prepayments are made by the individual borrowers, it shortens the contractual maturity. In this case, the contractual maturity of the bonds is proportionally affected as the contractual principal repayment of the bond is equal to the principal repayment of mortgage pools and ultimately will not have significant impact on the overall liquidity of the Group.

## MIK HOLDING JSC AND ITS SUBSIDIARIES

Notes to the Consolidated Financial Statements – 31 December 2017

### 24. Risk management (cont'd.)

#### 24.4 Market risk

As noted previously, market risk is the risk that changes in market conditions, such as changes in interest rates and foreign exchange rates will affect the Group's income or the value of its holdings of financial assets. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk. The Group has no significant concentration of market risk.

#### Currency risk

Currency risk is the possibility of financial loss to the Group arising from adverse movements in foreign exchange rates. The Group's management sets limits on the level of exposure by currencies, which are monitored on a frequent basis.

The Group has no significant foreign currency denominated assets and liabilities.

#### Interest rate risk

Given that interest rates of the financial assets and liabilities are fixed due to the nature of the Group's operation, the Group's exposure to interest rate risk is limited.

As at 31 December 2017 and 31 December 2016, the Group's interest bearing assets (bank balances, mortgage pool receivables with recourse and purchased mortgage pool receivables without recourse) and interest bearing liabilities (borrowed funds and collateralised bonds) have fixed interest rates and are not subject to repricing until they mature.

The table presents the aggregated amounts of the Group's interest bearing financial assets and liabilities at carrying amounts, categorised by their maturity dates.

	Less than 3 months	3 to 6 months	6 months to 1 year	1 to 5 years	Over 5 years	Total
At 31 December 2017	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000	MNT'000
Total financial assets	187,723,522	55,428,697	118,419,857	613,303,985	1,785,953,322	2,760,829,383
Total financial liabilities	66,574,583	34,894,454	71,023,388	608,673,231	1,810,343,677	2,591,509,333
Net interest sensitivity gap	<u>121,148,939</u>	<u>20,534,243</u>	<u>47,396,469</u>	<u>4,630,754</u>	<u>(24,390,355)</u>	<u>169,320,050</u>
<b>At 31 December 2016</b>						
Total financial assets	172,311,003	49,044,325	61,941,926	526,783,585	1,497,302,262	2,307,383,101
Total financial liabilities	52,548,123	29,055,161	57,530,258	522,727,450	1,512,267,942	2,174,128,934
Net interest sensitivity gap	<u>119,762,880</u>	<u>19,989,164</u>	<u>4,411,668</u>	<u>4,056,135</u>	<u>(14,965,680)</u>	<u>133,254,167</u>

#### 24.5 Operational risk

Operational risk is the risk of loss arising from systems failure, human errors, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, and lead to financial loss. The Group cannot expect to eliminate all operational risk, but through a dual control framework, segregation of duties between front-office and back office functions, controlled access to systems, authorization and reconciliation procedures, staff education and assessment processes, including the use of internal audit, the Group seeks to manage operational risk.

### 25. Fair value of financial instruments

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not recorded at fair value in the consolidated financial statements. The estimated fair values fall under Level 2 since the inputs used to estimate the fair value are all market observable.

**25. Fair value of financial instruments (cont'd.)**

**Financial instruments for which fair value approximates carrying value**

For financial assets and financial liabilities that are liquid or have short term maturity (less than one year), it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to bank balances. Based on fair value assessments performed by the management, the estimated fair values of instruments with maturity more than one year approximate their carrying amounts as shown in the statement of financial position. This is due principally to the fact that the current market rates offered for similar deposit products do not differ significantly from market rates at inception.

**Fixed rate financial instruments**

The carrying value of the Group's fixed rate financial assets and liabilities approximates the fair value by comparing market interest rates when they were first recognised with current market rates offered for similar financial instruments available in Mongolia.

**26. Capital management**

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and fulfil its obligations to the investors of the RMBS by effectively managing the subsidiaries. In order to maintain or adjust the capital structure, the Group may issue new shares, obtain borrowings, invest in permitted investments or issue bonds. The amount of equity capital that the Group managed as of 31 December 2017 was MNT'000 162,503,342 (as of 31 December 2016: MNT'000 135,129,872).

Included in retained earnings as at 31 December 2017 are restricted retained earnings of MNT'000 138,004,023 (31 December 2016: MNT'000 82,147,627) that are attributable to the Group's SPCs and are restricted from distribution until the liquidation of the respective SPCs in accordance with the Articles of Charter of each SPC and FRC regulation.

Since establishment of its subsidiaries, MIK Asset One SPC LLC, MIK Asset Two SPC LLC, MIK Asset Three SPC LLC, MIK Asset Four SPC LLC, MIK Asset Five SPC LLC, MIK Asset Six SPC LLC, MIK Asset Seven SPC LLC, MIK Asset Eight SPC LLC, MIK Asset Nine SPC LLC, MIK Asset Ten SPC LLC, MIK Asset Eleven SPC LLC, MIK Asset Twelve SPC LLC, MIK Asset Thirteen SPC LLC, MIK Asset Fourteen and MIK Asset Fifteen SPC LLC the Group's capital management structure focused on the management of the assets of the subsidiaries. Each year, upon settlement of the obligations of the Group, the BoD has resolved that any surplus funds are to be invested as follows:

- (a) securities issued or guaranteed by the Government of Mongolia or BoM;
- (b) accounts maintained with a qualified bank.

The BoD has also resolved that any such investments will be of short term maturity and denominated in Togrog.

The Group was not subject to any externally imposed capital requirements throughout 2017 and 2016.

**27. Subsequent events**

In January 2018, MIK Asset Fourteen SPC LLC, wholly owned subsidiary of the Company, has purchased mortgage pools from ten (10) commercial banks amounting to MNT 139,177,058 thousand. As consideration for the purchase of these mortgage pools, MIK Asset Fourteen SPC LLC has issued RMBS to these banks amounting to MNT 139,176,500 thousand.

**28. Mongolian translation**

These consolidated financial statements are also prepared in the Mongolian language. In the event of discrepancies or contradictions between the English version and the Mongolian version, the English version will prevail.