JSC m2 Real Estate

Consolidated financial statements

For the year ended 31 December 2017
with independent auditor's report

Contents

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Independent auditor's report

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

Opinion

We have audited the consolidated financial statements of JSC M2 Real Estate and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

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

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Key audit matters

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

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

Key audit matter	How our audit addressed the key audit matter
Revenue recognition	
Effective 1 January 2017 the Group has early adopted IFRS 15 *Revenue from Contracts with Customers* ahead of its mandatory effective date. The Group applied modified retrospective approach to transition and recognized an adjustment of GEL 31,182 thousands to inventory property and contract liability of GEL 31,801 thousands with corresponding effect on retained earnings as of 1 January 2017. From 1 January 2017 the Group's revenue from sale of inventory property is recognized over the period during which the inventory properties are being constructed, rather than at a point when all risks and rewards associated with inventory properties are passed to the buyer, as it was done under IAS 18. Revenue recognition was one of the matters of most significance to our audit due to significant impact of IFRS 15 on the financial statements, significant judgement involved in determination of transition of control to customers as well as the complexity and judgmental nature of estimation process and assumptions used when measuring percentage of completion of performance obligation satisfaction. The disclosures related to revenue and effects of adoption of IFRS 15 are presented in notes 3.1, 5 and 6 to the accompanying consolidated financial statements.	We obtained an understanding of the estimation and recognition process for revenue from sale of inventories. We assessed the design and tested the effectiveness of controls over revenue estimation and recognition process. We tested sales contracts and analysed contract conditions against revenue recognition requirements set out in IFRS 15. We involved in-house legal experts to understand the rights and obligations arising from contracts with customers including enforceability of the right to payment for performance completed to date. We assessed the calculation of percentage of completion in respect of contractual obligations. We analysed the disclosures related to effects of the adoption of IFRS 15 and significant judgements in revenue recognition.

Key audit matter	How our audit addressed the key audit matter
Valuation of investment property and investment property under construction	
Investment property and investment property under construction include completed assets and those buildings under construction held for earning rental income and land plots with a currently undetermined future use or with a view of future redevelopment. Investment property is measured initially at cost including transaction costs. Subsequent to initial recognition, investment property is measured at fair value. The measurement of investment property and investment property under construction at fair value was significant to our audit because of the materiality of the balances of investment property and investment property under construction to the consolidated financial statements (33% and 10% of total Group's assets, respectively) and the complexity and judgmental nature of estimation processes and assumptions used. Notes 11 and 12 describe the details of investment properties and investment property under construction, respectively, and disclose details of the fair valuation and significant assumptions.	We evaluated the competence, capabilities and objectivity of the external experts involved by the Group's management in the valuation process. We gained an understanding of internal controls implemented around the estimation process. We evaluated management's assumptions used (rental income, square meters to be developed, discount rate, market prices per square meter) by comparing them to available market information and official registry records. We involved our valuation experts to evaluate the assumptions used in the valuation of investment property and investment property under construction. We also performed physical observation of these assets. We analyzed the disclosures in the consolidated financial statements in respect of the fair value of investment property and investment property under construction.

Other information included in the Group's 2017 Annual Report

Other information consists of the information included in the Annual Report other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Annual Report is expected to be made available to us after the date of this auditor's report.

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

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

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

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

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

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

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

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

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

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

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

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

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

The engagement partner on the audit resulting in this independent auditor's report is Ruslan Khoroshvili.

Ruslan Khoroshvili

On Behalf of EY Georgia LLC

Tbilisi, Georgia

23 March 2018

Consolidated statement of comprehensive income

For the year ended 31 December

(Thousands of Georgian Lari)

	Notes	2017	2016
Sales of inventory property	5	92,643	96,347
Cost of sales – inventory property	6	(84,607)	(82,403)
Profit on sale of inventory property		8,036	13,944
Rental income	5	3,599	2,778
Property operating expense		(557)	(224)
Net rental income		3,042	2,554
Net gain from revaluation of investment property	11	1,183	2,553
Net gain from revaluation of investment property under construction	12	21,380	–
Net gain from revaluation		22,563	2,553
Other revenue	5	277	191
Employee benefits expense	7	(2,818)	(1,498)
Other general and administrative expenses	8	(2,906)	(2,026)
Depreciation and amortization		(508)	(243)
Marketing and advertising expense		(2,855)	(2,339)
Non-recurring items	9	(128)	(407)
Operating profit		24,703	12,729
Finance income		816	715
Finance expense		(186)	(210)
Net foreign exchange gain/(loss)		(117)	1,143
Profit before income tax expense		25,216	14,377
Income tax expense	10	(1,554)	(3,473)
Profit for the year		23,662	10,904
Other comprehensive income to be reclassified to profit or loss in subsequent periods			
Revaluation gain on investment securities available for sale		(51)	286
Other comprehensive income not to be reclassified to profit or loss in subsequent periods			
Exchange difference on translation of operations to presentation currency		(1,027)	15,252
Total comprehensive income for the year		22,584	26,442

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

Chief Executive Officer Irakli Burdiladze

Chief Financial Officer Giorgi Natroshvili

23 March 2018

The accompanying notes on pages 6-37 are an integral part of these consolidated financial statements.

Consolidated statement of financial position

As at 31 December

(Thousands of Georgian Lari)

	Notes	2017	2016
Assets			
Non-current assets			
Investment property	11	115,143	112,439
Investment property under construction	12	35,000	1,390
Inventory property	13	8,865	95,105
Property and equipment, net	14	49,641	7,050
Prepayments and other assets	15	7,400	19,297
		216,049	235,281
Current assets			
Inventory property	13	50,818	17,904
Prepayments and other assets	15	44,430	22,288
Investment securities available for sale	16	3,329	2,842
Contract assets with customers	16	1,008	–
Trade and other receivables	16	330	703
Time deposits with credit institutions		114	–
Cash at bank	16	34,751	93,210
		134,780	136,947
Total assets		350,829	372,228
Equity	17		
Share capital		4,180	4,180
Share premium		82,793	85,467
Translation reserve		14,460	15,538
Retained earnings		52,779	28,498
Total shareholders' equity		154,212	133,683
Non-controlling interests	22	10,418	–
Total equity		164,630	133,683
Non-current liabilities			
Loans received	16	42,885	31,153
Debt securities issued	16	64,121	64,910
Deferred revenue	18	–	67,414
Retention payable to general contractor	16	2,400	1,376
		109,406	164,853
Current liabilities			
Loans received	16	16,107	11,665
Debt securities issued	16	1,001	38,167
Deferred revenue	18	46,660	10,511
Current income tax liabilities		–	3,127
Trade and other payables	16	6,970	3,821
Retention payable to general contractor	16	2,361	564
Accruals for employee compensation		1,500	991
Other liabilities		2,194	4,846
		76,793	73,692
Total liabilities		186,199	238,545
Total equity and liabilities		350,829	372,228

The accompanying notes on pages 6-37 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity

For the year ended 31 December

(Thousands of Georgian Lari)

	Share capital	*Share premium*	*Translation reserve*	*Retained earnings*	*Total*	*Non-controlling interests*	*Total equity*
At 1 January 2016	4,180	85,003	–	17,594	106,777	–	106,777
Total comprehensive income for the year	–	–	15,538	10,904	26,442	-	26,442
Compensation to the ultimate parent for acquired treasury shares	–	(2,613)	–	–	(2,613)	–	(2,613)
Share based payments (Note 17)	–	3,077	–	–	3,077	–	3,077
At 31 December 2016	4,180	85,467	15,538	28,498	133,683	–	133,683
Effect from early adoption of IFRS 15 (Note 3.1)	–	–	–	619	619	–	619
At 1 January 2017 (restated)	4,180	85,467	15,538	29,117	134,302	–	134,302
Total comprehensive income for the year	–	–	(1,078)	23,662	22,584	–	22,584
Non-controlling interests arising on acquisition of subsidiary (Note 22)	–	–	–	–	–	10,562	10,562
Acquisition of non-controlling interest (Note 22)	–	–	–	–	–	(144)	(144)
Compensation to the ultimate parent for acquired treasury shares (Note 17)	–	(7,956)	–	–	(7,956)	–	(7,956)
Share based payments (Note 17)	–	5,282	–	–	5,282	–	5,282
At 31 December 2017	4,180	82,793	14,460	52,779	154,212	10,418	164,630

The accompanying notes on pages 6-37 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows

For the year ended 31 December

(Thousands of Georgian Lari)

	Notes	*2017*	*2016*
Operating activities			
Profit before income tax expense		25,216	14,377
Non-cash adjustments to reconcile profit before income tax expense to operating profit before changes in working capital			
Net gain from revaluation of investment property and investment property under construction	11,12	(22,563)	(2,553)
Loss from foreign exchange differences		117	(3,408)
Depreciation and amortization		508	243
Finance income		(816)	(715)
Finance expense		186	210
Share based payments		286	192
Other		(269)	44
Operating profit before changes in working capital		2,665	8,390
Working capital adjustments			
Change in inventory property		61,796	23,682
Change in deferred revenue		(30,374)	(34,845)
Change in retention payable to the constructor		2,767	(3,993)
Change in prepayments and other current and non-current assets		(10,779)	746
Change in trade and other payables, accruals for employee compensation and other current liabilities		1,172	(1,909)
Change in trade and other receivables		(642)	1,565
Cash flows used in operations		26,605	(6,364)
Interest received		816	715
Interest paid		(10,681)	(6,784)
Income tax paid		(4,854)	(297)
Net cash flows from /(used in) operating activities		11,886	(12,730)
Investing activities			
Acquisition of investment property	11	(1,401)	(2,281)
Proceeds from sale of investment property		–	1,606
Capital expenditure on investment property		(2,341)	(1,076)
Acquisition of property and equipment		(339)	(3,602)
Capital expenditure on investment property under construction		(9,483)	(1,253)
Capital expenditure on property and equipment		(15,792)	–
Acquisition of investment securities available for sale		(1,019)	(479)
Acquisition of subsidiaries	22	(12,748)	–
Net cash flows used in investing activities		(43,123)	(7,085)
Cash flows from financing activities			
Proceeds from debt securities issued		–	57,649
Repayment of debt securities issued		(34,099)	(15,220)
Proceeds from borrowings		32,117	39,724
Compensation to the ultimate parent for acquired treasury shares		(7,956)	(2,613)
Repayment from borrowings		(16,908)	(2,238)
Net cash flows from financing activities		(26,846)	77,302
Effect of exchange rate changes on cash and cash equivalents		(376)	7,734
Net increase in cash and cash equivalents		(58,459)	65,221
Cash and cash equivalents at 1 January	16	93,210	27,989
Cash and cash equivalents at 31 December	16	34,751	93,210

The accompanying notes on pages 6-37 are an integral part of these consolidated financial statements.

Consolidated statement of cash flows (continued)

Material non-cash transactions

In 2017 the Group incurred borrowings costs with total amount GEL 11,036 (2016: 9,098) of which GEL 3,396 (2016: 3,990) has been capitalized as a part of investment property, GEL 6,643 (2016: 4,898) was capitalized as a part of inventory property, GEL 552 (2016: 0) was capitalized as a part of investment property under construction, GEL 259 (2016: 0) was capitalized as a part of property and equipment and GEL 186 (2016: 210) recognized in the consolidated statement of comprehensive income.

Out of total employee share based compensation expense incurred in 2017 and 2016, GEL 2,760 (2016: 3,204) has been capitalized as a part of inventory property, GEL 2,826 (2016: 0) has been capitalized as a part of investment property and GEL 286 (2016: 192) recognized in the consolidated statement of comprehensive income.

In 2017 land and buildings with total amount of GEL 1,864 (2016: 17,470) was transferred from investment property to inventory property and GEL 3,005 (2016: 0) was transferred from investment property to property and equipment.

In 2017 apartments with total amount of GEL 706 were transferred from inventory property to investment property (2016: 0).

The accompanying notes on pages 6-37 are an integral part of these consolidated financial statements.

(Thousands of Georgian Lari)

1. Background

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

In 2016 the Company made a strategic decision to expand into hospitality business and initiated construction of two hotels in Georgia.

In 2017 the Group decided to build hotels on new locations one of them in Kutaisi which land was acquired by the Group in June. Apart of this the Group acquired a hotel under construction in December 2017. The property is located in Tbilisi on Gergeti st. Refer to Note 22.

In 2017 the Company acquired a construction company BK Construction LLC. Refer to Note 22. The Group's future intention is to build new projects through BK Construction LLC instead of other contractor construction companies. BK Construction LLC will also participate in other construction tenders that will help the group to generate new type of revenue – revenue from construction contracts.

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

The Group includes the following subsidiaries:

Subsidiary	*31 December 2017*	*31 December 2016*	*Country*	*Date of establishment*	*Date of acquisition*	*Industry*
LLC Tamarashvili 13	100.00%	100.00%	Georgia	3 November 2011	n/a	Real estate
LLC m2 at Kazbegi	100.00%	100.00%	Georgia	21 May 2013	n/a	Real estate
LLC m2 at Nutsubidze	100.00%	100.00%	Georgia	21 May 2013	n/a	Real estate
LLC m2 at Tamarashvili	100.00%	100.00%	Georgia	21 May 2013	n/a	Real estate
LLC m2 at Hippodrome	100.00%	100.00%	Georgia	6 July 2015	n/a	Real estate
LLC m2 Skyline	100.00%	100.00%	Georgia	24 July 2015	n/a	Real estate
LLC M Square Park	100.00%	100.00%	Georgia	15 September 2015	n/a	Real estate
LLC Optima Saburtalo	100.00%	100.00%	Georgia	15 September 2015	n/a	Real estate
LLC Optima Isani	100.00%	100.00%	Georgia	25 July 2014	n/a	Real estate
LLC M2	100.00%	100.00%	Georgia	12 February 2014	n/a	Hospitality/Real estate
LLC m2 Residential	100.00%	100.00%	Georgia	17 August 2015	n/a	Real estate
LLC m2 Hospitality	100.00%	100.00%	Georgia	17 August 2015	n/a	Hospitality/Real estate
LLC Caucasus Autohouse	100.00%	100.00%	Georgia	29 March 2011	n/a	Real estate
LLC Land	100.00%	100.00%	Georgia	3 October 2014	n/a	Real estate
LLC m2 at Vake	100.00%	100.00%	Georgia	3 August 2016	n/a	Real estate
LLC m2 at Chavchavadze	100.00%	100.00%	Georgia	5 September 2016	n/a	Real estate
LLC m2 Commercial Properties	100.00%	100.00%	Georgia	1 March 2016	n/a	Property management
LLC m2 at Melikishvili	100.00%	–	Georgia	15 May 2017	n/a	Hospitality
LLC m2 Kutaisi	100.00%	–	Georgia	15 May 2017	n/a	Hospitality
LLC BK Construction	100.00%	–	Georgia	18 May 2017	02 June 2017	Construction
LLC Kass 1	60.00%	–	Georgia	16 October 2014	26 December 2017	Hospitality

(Thousands of Georgian Lari)

2. Basis of preparation

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

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

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

3.1. Summary of significant accounting policies

Adoption of new or revised standards and interpretations

The accounting policies adopted in the preparation of the consolidated financial statements are consistent with those followed in the preparation of the Group's consolidated financial statements for the year ended 31 December 2016, apart from IFRS 15 Revenue from Contracts with Customers which the Group has adopted early starting 1 January 2017and certain reclassification discussed below.

Apart from early adoption of IFRS 15, no other new or revised IFRS during the year had an impact on the Group's financial position or performance.

Reclassifications

During year ended 31 December 2017 the Group reconsidered presentation of its consolidated statement of financial position accounts for the purpose of more detailed presentation of other liabilities – due to increased significance of accruals for employee compensation, it is now presented as a separate line in the consolidated statement of financial position. The presentation of comparative figures has been adjusted to confirm to the presentation of the current year amounts:

Affected item of the consolidated statement of financial positions as of 31 December 2016	As previously Reported	Reclassification	As reclassified
Accruals for employee compensation	–	991	991
Other liabilities	5,837	(991)	4,846

IFRS 15 Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, effective for the periods beginning on 1 January 2018 with early adoption permitted. IFRS 15 defines principles for recognizing revenue and is applicable to all contracts with customers. Under IFRS 15, revenue is recognized 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 standard also specifies a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers. IFRS 15 can be adopted using either a full retrospective or a modified retrospective approach.

The Group early adopted new revenue recognition standard effective from 1 January 2017 using modified retrospective approach. The impact of early adoption was GEL 619 increase to retained earnings.

The Group's revenue streams affected by transition to IFRS 15 included revenue from sale of inventory properties. For this revenue stream, part of the revenue was deferred under IFRS 15 requirements until satisfaction of respective performance obligations, which is expected over the completion progress.

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Adoption of new or revised standards and interpretations (continued)

Effect of early adoption on financial statements

The details of adjustments to opening retained earnings and other account were as follows:

Amounts in GEL'000, unless otherwise stated

Consolidated statement of financial position	*31 December 2016*	*1 January 2017*	*Effect of IFRS 15 adoption*
Assets			
Inventory property	113,009	81,827	(31,182)
Liabilities			
Deferred revenue	77,925	46,124	(31,801)
Equity			
Retained earnings	28,498	29,117	619

In accordance with new revenue standard requirements, the disclosure of the impact of adoption on the m2's consolidated income statement and financial position are as follows:

Amounts in GEL'000, unless otherwise stated

Consolidated statement of comprehensive income	*31 December 2017 (as reported)*	*Amount without IFRS 15 adoption*	*Effect of change*
Revenues			
Sales of inventory property	92,643	16,187	76,456
Costs of sale			
Cost of sales – inventory property	(84,607)	(15,116)	(69,491)
Profit on sale of inventory property	8,036	1,071	6,965

Consolidated statement of financial position	*31 December 2017 (as reported)*	*Amount without IFRS 15 adoption*	*Effect of change*
Assets			
Inventory property	59,683	160,356	(100,673)
Contract assets with customers	1,008	–	1,008
Liabilities			
Deferred revenue	46,660	153,909	(107,249)
Equity			
Retained earnings	29,117	28,498	619
Profit for the year	23,662	16,697	6,965

IAS 7 Disclosure Initiative – Amendments to IAS 7

The amendments to IAS 7 *Statement of Cash Flows* are part of the IASB's *Disclosure Initiative* and require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. On initial application of the amendment, entities are not required to provide comparative information for preceding periods. These amendments are effective for annual periods beginning on or after 1 January 2017, with early application permitted. Application of amendments resulted in additional disclosure provided by the Group (Note 16).

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Basis of consolidation

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

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

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

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

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

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

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

Revenue recognition

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

Sales of inventory property

Revenue from sale of inventory property is recognized over the time based on the progress towards complete satisfaction of a performance obligation using input method (proportion of costs incurred up to date to total expected project cost). Percentage of completion calculated based on total costs of the building is applied to apartment selling price to recognize revenue from apartment sale. Payment arrangements of the sale of developed real estate property usually include advance payment of part of transaction price and progress payments during the construction by the customer, such payments are recognized as deferred income. Financing component is usually immaterial.

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Rental income

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

Principal vs agent considerations

The Group has concluded that it is the principal in all of its revenue arrangements since it is the primary obligor in all of the revenue arrangements, it has pricing latitude and is also exposed to inventory and credit risks.

Finance income

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

Functional, reporting currencies and foreign currency translation

The consolidated financial statements are presented in Georgian Lari, which is the Group's presentation currency. Functional currency of each of the Group's entities is US Dollar Transactions in foreign currencies are initially recorded in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into functional currency at functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognized in the consolidated statement of comprehensive income as net foreign exchange gain/ (loss). Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. When a gain or loss on a non-monetary item is recognized in other comprehensive income, any exchange component of that gain or loss is recognized in other comprehensive income. Conversely, when a gain or loss on a non-monetary item is recognized in profit or loss, any exchange component of that gain or loss is recognized in profit or loss.

Differences between the contractual exchange rate of a certain transaction and the National Bank of Georgia ("NBG") exchange rate on the date of the transaction are included in Net foreign exchange gain/ (loss).

The official NBG exchange rate at 31 December 2017 and 31 December 2016 were 2.5922 and 2.6468 GEL to 1 USD respectively.

Taxation

The current income tax expense is calculated in accordance with the regulations in force in Georgia.

The annual profit earned by entities is not taxed in Georgia. Corporate income tax is paid on dividends, donations, abnormal losses, non-business related disbursements, etc. The corporate income tax arising from the payment of dividends is accounted for as a liability and expensed in the period in which dividends are declared, regardless of the actual payment date or the period for which the dividends are paid.

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

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Investment property

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

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

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

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

Investment property under construction

In 2017 the Group's management performed detailed review of facts and circumstances and concluded that fair value of certain items of the Group's investment property under construction became reliably measurable. As a result, as of 31 December 2017 investment property under construction is stated at fair value estimated by a qualified independent appraiser. Gains or losses arising from changes in the fair values are charged to profit or loss. Refer to Note 12.

Property and equipment

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

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

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

	Years
Buildings	100
Furniture and fixtures	5-10
Computers and other office equipment	5
Heavy construction equipment	5
Motor vehicles	5

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

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

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

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

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Operating leases

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

Financial assets

Initial recognition

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

Loans and receivables

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

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

Available for sale financial assets

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

Fair value measurements

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

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

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

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

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

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Fair value measurements (continued)

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

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

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

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

Financial liabilities

Financial liabilities that the Group has, including loans received, debt securities issued, trade and other payables, retention payable to general contractor and accruals for employee compensation, are initially recognized at fair value plus directly attributable transaction costs.

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

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

Inventory property

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

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

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

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

Prepayments

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

(Thousands of Georgian Lari)

3.1. Summary of significant accounting policies (continued)

Share-based payment transactions

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

Equity-settled transactions

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

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

Cash-settled transactions

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

Non-recurring items

The Group separately classifies and discloses the income and expenses that are non-recurring by nature.

Non-recurring items are such transactions and events that do not arise during the normal course of the Group and are different from ordinary activities in the way that cannot be reasonably expected to occur in the future and thus they should not be taken into account when making projections of the future results.

Share capital

Ordinary shares

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

Borrowing costs

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

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

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

Operational cycle

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

(Thousands of Georgian Lari)

3.2. Significant accounting judgements, estimates and assumptions

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

Judgements other than estimates

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

Classification of property

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

- Investment property comprises land and buildings (principally offices and retail property) that are not occupied substantially for use by, or in the operations of, the Group, nor for sale in the ordinary course of business, but are held primarily to earn rental income, capital appreciation or for future redevelopment before exact details of use are not yet determined;
- Inventory property comprises property that is held for sale in the ordinary course of business. Principally, this is residential property that the Group develops and intends to sell before or on completion of construction;
- Property, plant and equipment comprises owner occupied buildings, office furniture and fixtures, computer equipment, transport and leasehold improvements used to support Group's ordinary business activities.
- Special consideration is given to classification of the hotels and hotels under construction owned by the Group – detailed analysis of contractual arrangements with all the parties involved (hotel management company, hotel brand owner etc.) is performed on case by case basis.

Estimates

Measurement of fair value of investment properties and investment properties under construction

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

The Group performs valuation of its investment properties and investment properties under construction, as applicable, with a sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period. Results of this valuation, as well as valuation inputs and techniques are presented in Note 11 and 12. While the secondary market in Georgia provides adequate market information for fair value measurements for small and medium sized properties, valuation of large and unique properties involves application of various observable and unobservable inputs to determine adjustments to the available comparable sale prices. These estimates and assumptions are based on the best available information, however, actual results could be different.

4. Standards issued but not yet effective

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

Financial assets

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

(Thousands of Georgian Lari)

4. Standards issued but not yet effective (continued)

Financial assets (continued)

The Group plans to adopt the new standard on the required effective date and will not restate comparative information. During 2017, the Group has performed a detailed impact assessment of all three aspects of IFRS 9. This assessment is based on currently available information and may be subject to changes arising from further reasonable and supportable information being made available to the Group in 2018 when the Group will adopt IFRS 9. Overall, the Group expects no significant impact on its statement of financial position and equity as of 1 January 2018, as presented below.

IFRS 9 includes requirements for recognition and measurement, impairment and derecognition of financial assets.

Asset groups identified within the scope of IFRS 9 are cash and cash equivalents, amounts due from credit institutions, receivables from sales of assets, and trade and other receivables.

In summary, the impact of IFRS 9 adoption is expected to be, as follows:

Assets	Reason of adjustments	
Contract assets with customers	Impairment of financial assets	(97)
Total assets		(97)
Net impact on equity, Including		
Retained earnings	Impairment of financial assets	(97)
Total equity		(97)

Effect of IFRS9 on impairment for other financial assets is determined as insignificant.

IFRS 16 Leases

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

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

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

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

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

(Thousands of Georgian Lari)

4. Standards issued but not yet effective (continued)

IFRS 2 Classification and Measurement of Share-based Payment Transactions – amendments to IFRS 2

The IASB issued amendments to IFRS 2 *Share-based Payment* that address three main areas: the effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; the classification of a share-based payment transaction with net settlement features for withholding tax obligations; and accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash settled to equity settled.

On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. The amendments are effective for annual periods beginning on or after 1 January 2018, with early application permitted. The Group is assessing the potential effect of the amendments on its consolidated financial statements.

Transfers of Investment Property – amendments to IAS 40

The amendments clarify when an entity should transfer property, including property under construction or development into, or out of investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use. A mere change in management's intentions for the use of a property does not provide evidence of a change in use. Entities should apply the amendments prospectively to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. An entity should reassess the classification of property held at that date and, if applicable, reclassify property to reflect the conditions that exist at that date. Retrospective application in accordance with IAS 8 is only permitted if it is possible without the use of hindsight. Effective for annual periods beginning on or after 1 January 2018. Early application of the amendments is permitted and must be disclosed. The Group will apply amendments when they become effective. However, since Group's current practice is in line with the clarifications issued, the Group does not expect any effect on its consolidated financial statements.

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

IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration

The Interpretation clarifies that, in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognizes the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine the transaction date for each payment or receipt of advance consideration. Entities may apply the amendments on a fully retrospective basis. Alternatively, an entity may apply the Interpretation prospectively to all assets, expenses and income in its scope that are initially recognized on or after:

(i) The beginning of the reporting period in which the entity first applies the interpretation; or

(ii) The beginning of a prior reporting period presented as comparative information in the financial statements of the reporting period in which the entity first applies the interpretation.

The Interpretation is effective for annual periods beginning on or after 1 January 2018. Early application of interpretation is permitted and must be disclosed. However, since the Group's current practice is in line with the Interpretation, the Group does not expect any effect on its consolidated financial statements.

IFRIC Interpretation 23 Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 and does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately;
- The assumptions an entity makes about the examination of tax treatments by taxation authorities;
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates;
- How an entity considers changes in facts and circumstances.

(Thousands of Georgian Lari)

4. Standards issued but not yet effective (continued)

An entity must determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments. The approach that better predicts the resolution of the uncertainty should be followed. The interpretation is effective for annual reporting periods beginning on or after 1 January 2019, but certain transition reliefs are available. The Group will apply interpretation from its effective date. Since the Group operates in a complex multinational tax environment, applying the Interpretation may affect its consolidated financial statements and the required disclosures. In addition, the Group may need to establish processes and procedures to obtain information that is necessary to apply the Interpretation on a timely basis.

5. Revenue

	2017	*2016*
Revenue from the sale of inventory property		
Residential area	90,735	91,755
Commercial area	–	1,273
Parking lot area	1,908	3,319
	92,643	96,347
Rental income	3,599	2,778
Other revenue	277	191
Revenue	96,519	99,316

The IFRS 15 early adoption effect on revenue is presented in Note 3.1.

6. Cost of sales – inventory property

	2017	*2016*
Residential area cost of sales	82,076	75,291
Commercial area cost of sales	–	703
Parking lot cost of sales	2,531	6,409
Total cost of sales	84,607	82,403

The IFRS 15 early adoption effect on revenue is presented in Note 3.1.

7. Salary and employee benefits expenses

	2017	*2016*
Share-based compensation expense (Note 17)	6,192	3,396
Salary and other employee benefits	3,822	2,092
Cash bonus	1,500	1,203
Total employee benefits	11,514	6,691
Employee benefits expense	2,818	1,498
Employee benefits capitalized in inventory (Note 13)	5,182	5,193
Employee benefits capitalized in investment property (Note 11)	3,514	–
Total employee benefits	11,514	6,691

(Thousands of Georgian Lari)

8. Other general and administrative expenses

	2017	*2016*
Legal and other professional services	734	362
Rent	567	594
Corporate hospitality	306	238
Charity	301	–
Office supplies	191	175
Business trip expense	122	–
Operating taxes	113	126
Repair and maintenance	112	110
Insurance	105	64
Utility	81	112
Communication	75	75
Other expenses	74	30
Security	72	87
Personnel training and recruitment	53	53
Total other general and administrative expenses	2,906	2,026

9. Non-recurring items

List of events or transactions segregated by the Group from the results of regular operations and included it under non-recurring revenue and expenses as at 31 December 2017 and 2016 are presented below:

	2017	2016
Gain from bargain purchase (Note 22)	260	–
Non-recurring expenses related to completed projects	(388)	(407)
	(128)	(407)

10. Income tax

The Group's total income tax expense consists of income tax expense on intra-group dividends of GEL 622 and income tax expense on corrections of prior year taxable base of GEL 932.

In June 2016, amendments to the Georgian tax law in respect of corporate income tax became enacted. The amendments became effective from 1 January 2017 for all Georgian companies except the banks, insurance companies and microfinance organization, for which the effective date is 1 January 2019. Under the new regulation, corporate income tax is levied on profit distributed as dividends to the shareholders that are individuals or non-residents of Georgia, rather than on profit earned. The amount of tax payable on a dividend distribution is calculated as 15/85 of the amount of net distribution. The companies are able to offset corporate income tax liability arising from dividend distributions out of profits earned in 2008-2016 by the amount of corporate income tax paid for the respective period under the current regulation. Dividends distributions between Georgian resident companies is not subject to corporate income tax.

Following the enactment of the amendments, as at 31 December 2016 the Company reversed in full its deferred tax assets and liabilities based on IAS 12 *Income Taxes* requirement to measure deferred taxes at 0% tax rate applicable for undistributed profits starting from 1 January 2017.

In 2017 the Company recognized income tax charge on intra-group dividends of GEL 622 distributed from 2008-2016 profits in profit or loss, apart from this the Group corrected prior year declarations in total amount of increase in tax charge GEL 932 due to reflection of effect of functional currency change and correction of over-deducted cost of land. In 2016 the Company recognized income tax expense resulting from reversal of deferred tax assets and liabilities of GEL 346 in profit or loss.

(Thousands of Georgian Lari)

10. Income tax (continued)

The corporate income tax charge comprises:

	2017	2016
Current income tax charge	(1,554)	(3,127)
Deferred tax expense relating to origination and reversal of temporary differences	–	(346)
Total income tax charge	(1,554)	(3,473)

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual is as follows:

	2017	*2016*
Net dividends / Profit before tax	–	14,377
Statutory tax rate	15/85	15%
Theoretical income tax expense at the statutory rate	–	(2,157)
Tax accrued on intra-group dividends	(622)	–
Effect from change in tax legislation	–	(1,412)
Correction of prior year declaration	(932)	–
Non-deductible expenditures less non-taxable income	–	96
Income tax expense	(1,554)	(3,473)

11. Investment property

The table below shows movements in investment property during 2017:

	2017			
	Retail properties	*Land*	*Other*	*Total*
At 1 January	55,168	56,525	746	112,439
Acquisitions	–	1,401	–	1,401
Net gain from revaluation	673	505	5	1,183
Capital expenditure	70	3,514	–	3,584
Borrowing costs	–	3,396	–	3,396
Transfer to property and equipment (Note 14)	(220)	(3,005)	–	(3,225)
Transfer from/(to) inventory property (Note 13)	706	(1,864)	–	(1,158)
Currency translation effect	(1,130)	(1,335)	(12)	(2,477)
At 31 December	55,267	59,137	739	115,143

(Thousands of Georgian Lari)

11. Investment property (continued)

The table below shows movements in investment property during 2016:

	2016			
	Retail properties	*Land*	*Other*	*Total*
At 1 January	50,091	59,105	659	109,855
Acquisitions	2,281	–	–	2,281
Net gain from revaluation	2,553	–	–	2,553
Capital expenditure	1,076	–	–	1,076
Borrowing costs	102	3,888	–	3,990
Disposals	(1,648)	–	–	(1,648)
Transfer to property and equipment (Note 14)	–	(1,572)	–	(1,572)
Transfer to inventory property (Note 13)	(5,617)	(11,853)	–	(17,470)
Currency translation effect	6,330	6,957	87	13,374
At 31 December	55,168	56,525	746	112,439

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

As at 31 December 2017, investment property of GEL 112,035 (2016: 75,602) and investment property under construction of GEL 6,488 (2016: 0) was pledged as collateral under the loans received from international financial institution and Georgian banks (Note 16).

Fair value measurement of investment property

Investment properties are stated at fair value. The fair value represents the price that would be received to sell an asset in an orderly transaction between market participants at the measurement date. The date of latest valuation performed by independent appraiser for investment property and investment property under construction are 30 September 2017 and 31 December 2017, respectively. The valuation was performed by an independent valuator with a recognized and relevant professional qualification and with recent experience in the locations and categories of the investment property being valued. The valuation models in accordance with those recommended by the International Valuation Standards Committee have been applied and are consistent with the principles in IFRS 13. Investment property valuation belongs to Level 3 of fair value hierarchy.

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

Market approach

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

Income approach

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

(Thousands of Georgian Lari)

11. Investment property (continued)

Fair value measurement of investment property (continued)

For the purpose of fair value disclosures, the Group identified three classes of investment properties – retail properties, land and other properties. The following table shows descriptions of significant unobservable inputs to valuation as well as sensitivity of the inputs for 2017:

Class of investment properties	*Fair value 2017*	*Valuation technique*	*Significant unobservable inputs*	*Range (weighted average)*	*Type*	*Total area, square meters*
Retail properties	2,168	Market approach	Price per square meter, USD	0.7-1.2 (1.0)	Building	864
	19,456	Market approach/ Income approach	Price per square meter, USD	0.03-1.2 (0.9)	Building	15,211
			Capitalization rate	8.50%-10.50% (9.00%)	Land	28,327
	3,111	Cost approach/ Income approach	Price per square meter, USD	0.11 (0.11)	Building	2,380
			Capitalization rate	8.00% (8.00%)	Land	8,783
	13,026	Cost approach	Price per square meter, USD	0.02	Building	2,379
				(0.02)	Land	230,398
	17,506	Income approach	Capitalization rate	9.00%-9.50%	Building	6,798
				(9.00%)	Land	5,622
Land	59,137	Market approach	Price per square meter, USD	0.08-0.2	Building	392
				(0.1)	Land	138,297
Other	547	Market approach	Price per square meter, USD	0.02	Building	420
				(0.02)	Land	8,808
	192	Cost approach	Price per square meter, USD	0.03	Building	358
				(0.03)	Land	1,958
Total	115,143					450,995

Class of investment properties	*Fair value 2016*	*Valuation technique*	*Significant unobservable inputs*	*Range (weighted average)*	*Type*	*Total area, square meters*
Retail properties	39,596	Market approach	Price per square meter, GEL	0.1-3.4	Building	21,511
				(0.1)	Land	273,130
	15,572	Market approach; Income approach	Price per square meter, USD	8-19.8 (11.3)	Building	1,725
			Capitalization rate	9.00%-10.0% (9.12%)		
Land	56,525	Market approach	Price per square meter, GEL	0.1-1.3 (0.4)	Land	135,565
Other	746	Market approach	Price per square meter, GEL	0.06-0.09	Building	489
				(0.07)	Land	10,766
Total	112,439					443,186

(Thousands of Georgian Lari)

12. Investment property under construction

A summary of movement in investment property under construction during 2017:

	Retail	*Office*	*Kindergarten*	*Other*	*Total*
At 1 January	1,390	–	–	–	1,390
Net gain from revaluation	16,880	4,343	157	–	21,380
Capital expenditure	2,693	4,355	1,238	1,442	9,728
Borrowing costs	172	233	69	78	552
Currency translation effect	1,360	481	58	51	1,950
At 31 December	22,495	9,412	1,522	1,571	35,000

The table below shows movements in investment property under construction during 2016:

	Retail
Balance at 1 January	–
Capital expenditure	1,253
Currency translation effect	137
Balance at 31 December	1,390

For the purpose of fair value disclosures, the Group identified three classes of investment properties under construction – retail properties, offices, kindergarten. The following table shows descriptions of significant unobservable inputs to valuation as well as sensitivity of the inputs for 2017:

Class of investment properties under construction	*Fair value 2017*	*Valuation technique*	*Significant unobservable inputs*	*Range (weighted average)*	*Type*	*Total area, square meters*	*Sensitivity of the input to fair value, GEL*
Retail	22,495	Market approach	Rent price per square meter, USD	1.39-3.38 (2.43)	Building	3,979	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Office	9,412	Market approach	Rent price per square meter, USD	0.76 (0.76)	Building	4,778	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Kindergarten	1,522	Market approach	Rent price per square meter, USD	0.38-0.52 (0.45)	Building	1,314	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Other	1,571	Market approach	Rent price per square meter, USD	0.24 (0.24)	Building	2,577	Increase (decrease) in the price per square meter would result in increase (decrease) in fair value
Total	35,000					12,648	

(Thousands of Georgian Lari)

13. Inventory property

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

	2017	*2016*
Optima Saburtalo	7,530	7,557
Melikishvili ave. 10	1,335	–
New Hippodrome	–	50,439
Kazbegi ave. 15	–	28,313
Chavchavadze ave.50	–	8,796
Non-current inventory property	8,865	95,105
New Hippodrome	20,993	–
Kazbegi ave. 15	17,179	–
Skyline	8,250	12,165
Chavchavadze ave.50	4,221	–
Optima Isani	69	4,031
Chubinashvili 69	58	59
Tamarashvili. 13	48	193
Kazbegi ave. 25	–	25
Tamarashvili st. 06	–	1,431
Current inventory property	50,818	17,904
Inventory property	59,683	113,009

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

	2017	*2016*
Balance at 31 December 2016	113,009	98,035
Effect from early adoption of IFRS 15	(31,182)	–
Balance at 1 January 2017	81,827	98,035
Land and building transferred from investment property (Note 11)	1,864	17,470
Transfer from prepayments and other assets	–	3,497
Construction costs incurred	51,571	53,624
Borrowing costs	6,643	4,898
Employee benefits capitalized (Note 7)	5,182	5,193
Inventory reclassified to investment property (Note 11)	(706)	–
Currency translation effect	(2,091)	12,695
Disposals recognized in cost of sales (Note 6)	(84,607)	(82,403)
Balance at 31 December	59,683	113,009

As of 31 December 2017 the Group had commitments of GEL 124,174 (2016: GEL 197,530) relating to completion of five construction projects (2016: four construction projects).

(Thousands of Georgian Lari)

14. Property and equipment

The movements in property and equipment were as follows:

	Buildings	*Furniture and fixtures*	*Computers*	*Motor vehicles*	*Construction equipment*	*Leasehold improvements*	*Assets under construction*	*Total*
Gross book value								
1 January 2016	42	367	781	162	–	714	–	2,066
Additions	30	96	68	73	–	345	3,215	3,827
Transfer from investment property (Note 11)	–	–	–	–	–	–	1,572	1,572
Disposals	–	(44)	(75)	(28)	–	–	–	(147)
Translation effect	6	60	103	28	–	143	476	816
31 December 2016	78	479	877	235	–	1,202	5,263	8,134
1 January 2017	78	479	877	235	–	1,202	5,263	8,134
Additions	–	42	101	57	21	10	16,158	16,389
Acquisitions through business combination (Note 22)	–	–	–	44	2,446	–	20,365	22,855
Transfer from investment property (Note 11)	220	–	–	–	–	–	3,005	3,225
Translation effect	8	(9)	(15)	(2)	167	(25)	659	783
31 December 2017	306	512	963	334	2,634	1,187	45,450	51,386
Accumulated depreciation								
1 January 2016	1	182	413	56	–	44	–	696
Depreciation charge	1	70	89	57	–	26	–	243
Translation effect	4	28	75	14	–	24	–	145
31 December 2016	6	280	577	127	–	94	–	1,084
1 January 2017	6	280	577	127	–	94	–	1,084
Depreciation charge	–	70	118	39	239	9	–	475
Translation effect	–	13	24	6	30	113	–	186
31 December 2017	6	363	719	172	269	216	–	1,745
Net book value								
1 January 2016	41	185	368	106	–	670	–	1,370
31 December 2016	72	199	300	108	–	1,108	5,263	7,050
31 December 2017	300	149	244	162	2,365	971	45,450	49,641

(Thousands of Georgian Lari)

15. Prepayments and other assets

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

	2017	*2016*
Prepayments for investment properties	6,529	–
Prepayments for inventory properties	726	17,858
Intangible assets, net	145	167
Other non-current assets	–	1,272
Prepayments and other assets, non-current	7,400	19,297
Prepayments for inventory properties	18,306	1,288
VAT prepayment	16,753	18,427
Other current assets	6,060	2,573
Prepayments for property and equipment	3,311	–
Prepayments and other assets, current	44,430	22,288
Total prepayments and other assets	51,830	41,585

16. Financial instruments

Financial instruments overview

Investment securities available for sale

As of 31 December 2017 included into investment securities available for sale:

- A minority unquoted share in a company with cost of GEL 1,275 (2016: GEL 1,301) carried at cost less impairment (2016: carried at cost less impairment);
- Shares of BGEO held for settlement of the Group's cash-settled share based transactions with fair value of GEL 2,054 (including revaluation effect of GEL 235) (2016: GEL 1,541 (including revaluation effect of GEL 286)). BGEO's shares are categorized within Level 1 of the fair value hierarchy (2016: Level 1).

Loans received

	Currency	*Maturity*	*31 December 2017*	*31 December 2016*
Borrowing from international financial institutions	USD	15 December 2019	44,243	39,135
Borrowing from international financial institutions	USD	15 December 2026	12,473	–
Borrowing from local commercial bank	USD	8 July 2026	2,276	2,565
Borrowing from local commercial bank	GEL	23 March 2017	–	1,118
Total borrowings			58,992	42,818

Total interest for 2017 comprised GEL 5,081 (2016: 3,090) of which GEL 4,302 (2016: 2,880) was capitalized as a part of inventory property, GEL 334 was capitalized as a part of investment property under construction (2016: 0), GEL 259 (2016: 0) was capitalized as a part of property and equipment and GEL 186 (2016: 210) recognized in the consolidated statement of comprehensive income.

(Thousands of Georgian Lari)

16. Financial instruments (continued)

Financial instruments overview (continued)

Some borrowings are received upon certain conditions, such as maintaining different limits for leverage, capital investments, minimum amount of immovable property and others. At 31 December 2017 and 2016 the Group complied with all these lender covenants.

As at 31 December 2017 the Group had undrawn loan commitment of USD 1,9 million (2016: USD 15 million) from international financial institution.

Debt securities issued

Total interest for 2017 comprised GEL 5,955 (2016: 6,008) of which GEL 3,396 (2016: 3,990) has been capitalized as a part of investment property, GEL 2,341 (2016: 2,018) was capitalized as a part of inventory property, GEL 218 was capitalized as a part of investment property under construction (2016: 0).

In March 2017 the Group completely repaid the bonds issued in March 2015 of USD 13,689.

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

Retention payable to general contractor

Included in retention payable to general contractor as of 31 December 2017 and 2016 are performance and guarantee retentions related to the Group's on-going construction projects.

Performance guarantee retention represents 5% of total amount due to a constructor which is retained by the Group and is due at the project completion date. It is intended to serve as a guarantee for completion of construction activities. As of 31 December 2017 performance guarantee retention comprised GEL 2,361 (2016: GEL 688).

Guarantee retention represents 5% of total amount due to a constructor which is retained by the Group and is due in one year after the project completion date. It is intended to serve as a guarantee for any subsequent faults identified in the completed project. As of 31 December 2017 guarantee retention comprised GEL 2,400 (2016: GEL 1,252).

Trade and other payables

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

	2017	*2016*
Construction payables	6,653	3,733
Marketing and advertising	317	88
Trade and other payables	6,970	3,821

Risks arising from financial instruments

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

As at 31 December 2017 and 31 December 2016 the Group does not any significant financial instruments in the currencies, other than the functional currency.

(Thousands of Georgian Lari)

16. Financial instruments (continued)

Risks arising from financial instruments (continued)

Credit risk

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

As of 31 December 2017 and 2016 the Group has no other significant financial assets subject to credit risk except for:

- Cash at bank:

  As at 31 December 2017 GEL 26,570 (2016: 82,792) was kept with a bank under common control having a ratings of "BB-/B" from Standard & Poor's, "B1/NP" (FC) & "Ba3/NP" (LC) from Moody's and "BB-/B" from Fitch Ratings. GEL 1,974 was kept with local commercial banks having a ratings of "B1/NP" (FC) & "Ba3/NP" (LC) from Moody's and "BB-/B" from Fitch Ratings. Remaining GEL 6,207 was kept with local commercial bank with no available credit ratings. Respective bank accounts do not bear any interest except current accounts with a bank under common control, on which annual interest 1.00% was accrued on USD accounts during the 2017. The Group's cash at bank is immediately available upon demand.

- Trade and other receivables:

  Trade and other receivables of the Group are mostly comprised of receivables from sale of inventory property. These receivables are mostly denominated in USD and are due from 3 to 12 months from the reporting date. No significant trade and other receivable are either past due or impaired as at 31 December 2017 and 2016.

- Contract assets with customers:

  The Group's contract assets with customers are totally due to sale of inventory property. These contract assets are fully denominated in USD and are due from 3 to 12 months from the reporting date. No contract assets with customers are past due or impaired as at 31 December 2017.

Liquidity risk

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

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

Financial liabilities As at 31 December 2017	*Less than 3 months*	*3 to 12 months*	*1 to 5 years*	*Over 5 years*	*Total*
Loans received	103	20,834	43,122	8,789	72,848
Trade and other payables	6,970	–	–	–	6,970
Debt securities issued	–	4,859	69,666	–	74,525
Retention payable to general contractor	–	2,361	2,400	–	4,761
Total	7,073	28,054	115,188	8,789	159,104

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

(Thousands of Georgian Lari)

16. Financial instruments (continued)

Risks arising from financial instruments (continued)

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect the fair value of the financial instruments or the future cash flows on financial instruments. In 2017 and 2016 the Group had floating interest rate on borrowings from international financial institution linked to LIBOR and is therefore exposed to interest rate risk. However no reasonably expected change in LIBOR would have a material impact on the consolidated income statement.

Changes in liabilities arising from financing activities

	1 January 2017	*Cash flows*	*Foreign exchange movement*	*Accrual of Interest*	*31 December 2017*
Interest bearing loans and borrowings	42,818	10,639	454	5,081	58,992
Interest bearing Debt securities issued	103,077	(40,210)	(3,700)	5,955	65,122
Total liabilities from financing activities	145,895	(29,571)	(3,246)	11,036	124,114

	1 January 2016	*Cash flows*	*Foreign exchange movement*	*Accrual of Interest*	*31 December 2016*
Interest bearing loans and borrowings	3,286	34,884	1,558	3,090	42,818
Interest bearing Debt securities issued	48,308	38,247	10,514	6,008	103,077
Total liabilities from financing activities	51,594	73,131	12,072	9,098	145,895

17. Equity

Ordinary shares issued and fully paid as at 31 December 2017 and 2016 were 417,994,663. Each share has a nominal value of 0.01 Georgian Lari as of 31 December 2017 and 2016.

Pursuit to the new employee remuneration scheme discussed in this note below, the Group plans to introduce Class B shares, which will have entitle the shareholders to the rights different from currently issued Class A shares. No such shares have been issued in 2017.

Capital management

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

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

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

The Group did not have any externally imposed capital requirements as at 31 December 2017 and 2016.

Share-based payments

Awards made in BGEO shares

In February 2017 the BGEO Remuneration Committee resolved to award 20,000 ordinary shares of BGEO to the CEO of the Group. The Group considers 28 February 2017 as the grant date. The Group estimates that the fair value of the shares awarded was Georgian Lari 90.0 per share. Shares awarded are subject to two-year vesting with continuous employment being the only vesting condition for the award. The Group does not have an obligation to settle this award but it is expected that BGEO will recharge the cost of the BGEO shares to be purchased for its settlement to the Group.

(Thousands of Georgian Lari)

17. Equity (continued)

Share-based payments (continued)

Awards made in BGEO shares (continued)

In May 2017 the Group's Supervisory Board resolved to award 9,100 ordinary shares of BGEO to twelve of the employees of the Group. The Group estimates that the fair value of the shares awarded in May 2017 was Georgian Lari 116.58 per share. Shares awarded are subject to three-year vesting with continuous employment being the only vesting condition for the award.

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

In 2017, the Group contributed GEL 7,956 to BGEO to compensate the cost of the shares purchased for the purpose of settlement of the Group's share-based awards made in BGEO shares.

Awards made in the Company's shares

In 2017 the Group introduced new employee remuneration scheme for its key executives. Under this scheme, executives are awarded a) long-term deferred securities and b) equity compensation securities represented by equity instruments of the Company (Class B shares). Class B shares will entitle the holders to dividends and liquidation proceeds from the Company similar to those of the ordinary (Class A) shareholders, and provide limited voting rights on the annual shareholders meetings. Class B shares can only be sold to existing shareholders of the Group.

Both long-term deferred securities and equity compensation securities awards consist of guaranteed component, where the number of awarded shares is determined with reference to net asset value (NAV) growth for respective year, and discretionary component, determined annually by the Supervisory Board. Shares are awarded in 30 days after the completion of annual audit. Long-term deferred securities vest in 5 years with only vesting condition being continued employment in BGEO Group. Equity compensation securities vest immediately. Executive has a put option to sell shares to the controlling shareholder of the Group during 7 years following the vesting. After expiration of the put option, the controlling shareholder has a call option over the shares for further 12 months. Price for both put and call options is defined as NAV divided by number of shares based on latest annual audited financial statements. If neither of the options are exercised, class B shares are converted to ordinary (class A) shares of the Company.

The Group accounts for the awards under this scheme as equity-settled share-based transaction.

In 2017, new service agreements were signed with some of Group's executives that set out the terms of the awards under this scheme. The Group determined the dates of respective service agreement as the grant date for guaranteed portion of the award. The Group estimated total number of guaranteed Class B shares awarded to the executives under the terms of this scheme in 2017 as 5,259, subject to annual revision based on the updated NAV growth forecasts. Weighted average fair value of shares awarded in 2017 was Georgian Lari 0.35 per share, determined as Group's NAV per share based on contractual characteristics of Class B shares. In 2017, the Group recognized GEL 122 charge related to this scheme and GEL 2,122 was capitalized as a part of investment property

Summary

The fair value of cash settled share-based awards as of 31 December 2017 comprised Georgian Lari 124.51 per share. The Group's cash settled share-based payment expense for the year ended 31 December 2017 comprised GEL 910 (2016: GEL 319).

The weighted average fair value of equity settled share-based awards at the grant date comprised Georgian Lari 90.0 per share in year ended 31 December 2017 (31 December 2016: Georgian Lari 57.80 per share). The Group's equity settled share-based payment expense for the year ended 31 December 2017 comprised GEL 5,282 (31 December 2016: GEL 3,077).

(Thousands of Georgian Lari)

18. Deferred revenue

	2017	*2016*
New Hippodrome	–	47,649
Kazbegi 15	–	15,167
Chavchavadze	–	4,598
Non-current deferred revenue	–	67,414
New Hippodrome	31,034	–
Kazbegi 15	13,280	–
Chavchavadze	2,346	–
Skyline	–	10,186
Tamarashvili st. 6	–	325
Current deferred revenue	46,660	10,511
Deferred revenue	46,660	77,925

Deferred revenue of the Group consists of gross advances received from customers for purchase of residential property.

19. Fair value measurements

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability.

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

	Level 1	*Level 2*	*Level 3*	*Total fair value 31 December 2017*	*Carrying value 31 December 2017*	*Unrecognized gain (loss) 31 December 2017*
Assets measured at fair value						
Investment properties	–	–	115,143	115,143	115,143	–
Investment property under construction	–	–	35,000	35,000	35,000	–
Investment securities available for sale	2,054	–	–	2,054	2,054	–
Assets for which fair values are disclosed						
Trade and other receivables	–	–	330	330	330	–
Cash at bank	–	34,751	–	34,751	34,751	–
Liabilities for which fair values are disclosed						
Loans received	–	60,316	–	60,316	58,992	(1,324)
Debt securities issued	–	64,753	–	64,753	65,122	369
Trade and other payables	–	–	6,970	6,970	6,970	–
Retention payable to general contractor	–	–	4,297	4,297	4,761	464

(Thousands of Georgian Lari)

19. Fair value measurements (continued)

	Level 1	*Level 2*	*Level 3*	*Total fair value 31 December 2016*	*Carrying value 31 December 2016*	*Unrecognized gain (loss) 31 December 2016*
Assets measured at fair value						
Investment properties	–	–	112,439	112,439	112,439	–
Investment property under construction	–	–	1,390	1,390	1,390	–
Investment securities available for sale	1,541	–	–	1,541	1,541	–
Assets for which fair values are disclosed						
Trade and other receivables	–	–	703	703	703	–
Cash at bank	–	93,210	–	93,210	93,210	–
Liabilities for which fair values are disclosed						
Loans received	–	42,649	–	42,649	42,818	169
Debt securities issued	–	100,963	–	100,963	103,077	2,114
Trade and other payables	–	–	3,821	3,821	3,821	–
Retention payable to general contractor	–	–	1,658	1,658	1,940	282

For a description of the determination of fair value for investment properties, investment property under construction and investment securities available for sale please refer to Notes 11, 12 and 16.

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

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

20. Commitments and contingencies

Taxation

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

Capital commitments

As of 31 December 2017 the Group had no capital commitments related to government or state (2016: GEL 10,467).

Construction related commitments are disclosed in Note 12.

(Thousands of Georgian Lari)

20. Commitments and contingencies (continued)

Lease commitments

The Group's commitments as lessee comprise following:

	31 December 2017	*31 December 2016*
Operating lease commitments (lessee)		
Not later than 1 year	700	624
Later than 1 year but not later than 5 years	603	672
Total	1,303	1,296

The Group's commitments as lessor comprise following:

	31 December 2017	*31 December 2016*
Operating lease commitments (lessor)		
Not later than 1 year	4,616	4,029
Later than 1 year but not later than 5 years	11,088	9,971
Later than 5 years	9,663	9,654
Total	25,367	23,654

21. Related party transactions

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

	2017			*2016*		
	Parent[1]	*Entities under common control[2]*	*Key management personnel*	*Parent[1]*	*Entities under common control[2]*	*Key management personnel*
Balances as at 31 December						
Cash and cash equivalents at 31 December	–	26,570	–	–	82,792	–
Deferred Income	–	–	108	–	–	2,344
Debt securities issued	–	9,235	524	29,280	11,155	1,173
Prepayments	–	866	–	–	–	–
Transactions for the year ended 31 December						
Interest expense on debt securities issued	–	727	38	524	529	100
Revenue from sale of inventory property	–	–	143	–	–	117
Transaction costs paid related to bonds issue	–	–	–	–	1,167	–
Finance income	–	550	–	–	715	–
Employee benefits expense	–	–	6,871	–	–	4,217
Rental income	–	1,187	–	–	623	–
Rental expense	–	–	–	–	120	–
Insurance expense	–	194	–	–	64	–
Other general and administrative expense	–	102	–	–	112	–
Other revenue	–	183	–	–	–	–

1 As at 31 December 2017 and 2016 and in the years then ended Parent includes balances and transactions with BGEO Group PLC, JSC BGEO Group and JSC BGEO Investments.

2 Entities under common control include BGEO Group PLC subsidiaries except those included in Parent category.

(Thousands of Georgian Lari)

21. Related party transactions (continued)

Total number of key management personnel members receiving employee benefits in 2017 amounted to 5 persons (2016: 4), CEO and 4 deputies (2016: CEO and 3 deputies). Other transactions with key management personnel include above mentioned 5 employees and total 3 members of supervisory board (2016: 4 employees and 3 members of supervisory board).

Compensation of key management personnel comprised the following:

	2017	*2016*
Share-based compensation	5,777	3,366
Salary	844	601
Cash bonus	250	250
	6,871	4,217

22. Business combinations

Acquisition of BK Constructions LLC

On 2 June 2017 the Group purchased 100% share of BK Constructions LLC from BK Capital.

BK Constructions LLC is a company established in May 2017 and its main business areas are: construction, design, repair, restoration and drainage works, construction of multi-purpose complexes.

The fair values of aggregate identifiable assets and liabilities of BK Construction as at the date of acquisition were:

BK Construction LLC	Fair Value Recognized on acquisition
Assets	
Property and equipment	2,446
Total assets	2,446
Fair value of net assets	2,446
Goodwill arising on acquisition	(260)
Consideration paid	2,186
Cash paid	2,186
Net cash outflow	2,186

Consideration comprised GEL 2,186 cash payment, which has been fully paid as at reporting date.

Since acquisition BK Construction LLC has recorded GEL 609 loss for the year and no revenue. If the combination had taken place at the beginning of the year, the Group would have recorded GEL 23,662 profit for the year and GEL 96,519 revenue.

The difference between cash consideration and BK Construction's net assets was recognized as a gain from bargain purchase in non-recurring expenses.

Acquisition of Kass 1 LLC

The Group has acquire control over Kass 1 LLC ("Kass") as a result of acquisition of 50% share in the company on 26 December 2017 for a total consideration of GEL 10,562.

The main operating activity of Kass is hotel development.

(Thousands of Georgian Lari)

22. Business combinations (continued)

Accounting for Kass 1 LLC Acquisition / Business Combination (continued)

The provisional fair values of aggregate identifiable assets and liabilities of Kass as at the date of the acquisition were:

Kass 1 LLC	Fair Value Recognized on acquisition
Assets	
Cash and cash equivalents	1
Accounts receivable	14
Property under construction	20,409
Prepayments	803
Total assets	21,227
Liabilities	
Accounts payable	103
Total liabilities	103
Fair value of net assets	21,124
Non-controlling interest	10,562
Consideration paid [1]	10,562
The net cash outflow on acquisition was as follows:	
Cash paid	(10,562)
Cash acquired with the subsidiary	1
Net cash outflow	(10,561)

Consideration comprised GEL 10,562 cash payment, which has been fully paid as at reporting date.

The net assets presented above are estimated provisionally as at the acquisition date. The Group continues a thorough examination of these net assets and if identified, adjustments will be made to the net assets and amount of the goodwill during the 12-month period from the acquisition date, as allowed by IFRS 3 ‘Business Combinations’.

As the acquisition took place on 26 December 2017, it did not have material effect on Group’s profit for the year and revenue. If the combination had taken place at the beginning of the year, the Group would have recorded GEL 22,609 profit for the year and GEL 96,519 revenue.

The non-controlling interest in Kass was measured as the proportionate share of the net assets.

The acquisition is in line with m2’s strategy to pursue hotel development and capitalise on growing tourist activities in Georgia. Management considers that the deal will have a positive impact on the value of the Group.

On 29 December 2017 the shareholders’ meeting resolved to increase the charter capital of Kass by GEL 4,921 resulting in increase of the Group’s share in Kass by additional 10%. As a result of the equity transaction, the non-controlling interest of the Group decreased by GEL 144 and composed GEL 10,418 as at 31 December 2017.

(Thousands of Georgian Lari)

23. Segment information

For management purposes, the Group is organised into business units based on its products and services and has five reportable segments, as follows:

- Residential segment is engaged in offering customers affordable and premium housing;
- Yield generating segment entails managing the portfolio of yielding assets consisting of retained commercial spaces (ground floor) at its own residential developments and the ones acquired opportunistically;
- Property management segment – the maintenance of common areas through providing cleaning, security, and other. services at its own residential developments;
- Hospitality management – developing/operating hotels;
- Construction management relates to acquired construction arm and offering construction services.

Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

The Group's operations are primary concentrated in Georgia.

No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Group's total revenue at 31 December 2017 and 2016.

Year ended 31 December 2017	Property Management	Residential	Yielding Assets	Hospitality	Construction	Eliminations[1]	Consolidated
Sales of inventory property	–	92,643	–	–	–	–	92,643
Cost of sales – inventory property	–	(84,607)	–	–	–	–	(84,607)
Profit on sale of inventory property	–	8,036	–	–	–	–	8,036
Rental income	–	–	3,657	–	–	(58)	3,599
Property operating expense	–	–	(557)	–	–	–	(557)
Net rental income	–	–	3,100	–	–	(58)	3,042
Net gain from revaluation of investment property	–	206	977	–	–	–	1,183
Net gain from revaluation of investment property under construction	–	21,380	–	–	–	–	21,380
Net gain from revaluation	–	21,586	977	–	–	–	22,563
Other revenue, net	114	7,345	–	–	–	(7,182)	277
Employee benefits expense	(96)	(2,268)	(77)	(360)	(17)	–	(2,818)
Other general and administrative expenses	(18)	(2,788)	(88)	–	(12)	–	(2,906)
Depreciation	(3)	(238)	(18)	–	(249)	–	(508)
Marketing and advertising expense	(18)	(2,722)	(115)	–	–	–	(2,855)
Other operating income (net)	–	–	–	–	238	(238)	–
Non-recurring items	(2)	(305)	(13)	–	192	–	(128)
Operating profit	(23)	28,646	3,766	(360)	152	(7,478)	24,703
Finance income	5	789	22	–	–	–	816
Finance expense	–	(2)	(184)	–	–	–	(186)
Net foreign exchange gain/(loss)	–	(151)	(6)	–	40	–	(117)
Profit before income tax expense	(18)	29,282	3,598	(360)	192	(7,478)	25,216
Income tax expense	(8)	(1,500)	(46)	–	–	–	(1,554)
Profit for the year	(26)	27,782	3,552	(360)	192	(7,478)	23,662

(Thousands of Georgian Lari)

23. Segment information (continued)

Year ended 31 December 2016	Property Management	Residential	Yielding Assets	Hospitality	Construction	Elimination[1]	Consolidated
Sales of inventory property	–	97,820	–	–	–	(1,473)	96,347
Cost of sales – inventory property	–	(82,403)	–	–	–	–	(82,403)
Profit on sale of inventory property	–	15,417	–	–	–	(1,473)	13,944
Rental income	–	–	2,819	–	–	(41)	2,778
Property operating expense	–	–	(224)	–	–	–	(224)
Net rental income	–	–	2,595	–	–	(41)	2,554
Net gain from revaluation of investment property	–	2,553	–	–	–	–	2,553
Net gain from revaluation of investment property under construction	–	–	–	–	–	–	–
Net gain from revaluation	–	2,553	–	–	–	–	2,553
Other revenue, net	(110)	2,475	5	–	–	(2,179)	191
Employee benefits expense	(3)	(1,472)	(23)	–	–	–	(1,498)
Other general and administrative expenses	(5)	(1,903)	(118)	–	–	–	(2,026)
Depreciation	(1)	(236)	(6)	–	–	–	(243)
Marketing and advertising expense	(7)	(2,275)	(57)	–	–	–	(2,339)
Other operating income (net) Non-recurring items	(3)	(393)	(11)	–	–	–	(407)
Operating profit	(129)	14,166	2,385	–	–	(3,693)	12,729
Finance income	2	689	24	–	–	–	715
Finance expense	(1)	(202)	(7)	–	–	–	(210)
Net foreign exchange gain/(loss)	4	1,100	39	–	–	–	1,143
Profit before income tax expense	(124)	15,753	2,441	–	–	(3,693)	14,377
Income tax expense	(10)	(3,363)	(100)	–	–	–	(3,473)
Profit for the year	(134)	12,390	2,341	–	–	(3,693)	10,904

[1.] Inter-segment revenues are eliminated upon consolidation and reflected in the 'eliminations' column.

Net gain from revaluation of investment property and investment under construction is attributable to the residential segment, unless the respective revalued assets generate yield and are respectively included in yielding assets segments.

Administrative, interest, income tax and other operating income and expenses are allocated to the segments based at the proportionate share of the total revenue on the monthly bases, unless such income and expenses are directly attributable to the respective segments.

24. Events after the reporting period

On 2 January 2018, the Group obtained the remaining tranche in amount USD 1.9 mln under the loan agreement concluded with International Finance Corporation (IFC) (Note 16).