

**“AZERALUMINIUM” LIMITED
LIABILITY COMPANY**

**The International Financial Reporting Standards
Preliminary Financial Statements
and Independent Auditors’ Report
For the Year Ended December 31, 2020**

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020

The following statement is made with a view to distinguishing respective responsibilities of the management and those of the independent auditors in relation to the International Financial Reporting Standards ("IFRS") preliminary financial statements of "Azeraluminium" Limited Liability Company (the "Company").

Management is responsible for the preparation of the preliminary financial statements that present fairly the financial position of the Company as at December 31, 2020, the results of its operations, changes in equity and cash flows for the year then ended, in accordance with the basis set out in the "Basis of preparation" paragraph of the Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021.

In preparing the preliminary financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether accounting policies have been followed, subject to any material departures disclosed and explained in the preliminary financial statements; and
- Preparing the preliminary financial statements on a going concern basis, unless it is inappropriate to presume that the Company will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Company;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Company, and which enable them to ensure that the preliminary financial statements of the Company comply with IFRSs;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Company; and
- Detecting and preventing fraud, errors and other irregularities.

The preliminary financial statements for the year ended December 31, 2020 was authorized for issue on September 13, 2021 by the management of the Company.

On behalf of the Management Board:


Maxim Javadov
Director

September 13, 2021
Baku, the Republic of Azerbaijan




Jalal Habibov
Finance Director

September 13, 2021
Baku, the Republic of Azerbaijan

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INDEPENDENT AUDITORS' REPORT

To the Shareholder and Management of "Azeraluminium" Limited Liability Company:

Opinion

We have audited the preliminary financial statements of "Azeraluminium" Limited Liability Company (the "Company") for the year ended December 31, 2020, which comprises the preliminary statement of financial position as at December 31, 2020, and the preliminary statement of comprehensive income, preliminary statement of changes in equity and preliminary statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying preliminary financial statements for the year ended December 31, 2020 have been prepared, in all material respects, in accordance with the basis set out in the "Basis of preparation" paragraph of the Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Preliminary Financial Statements section of our report. We are independent of the Company 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.

Emphasis of Matter

Basis of preparation

We draw attention to the Note 2 to the preliminary financial statements which explains why there is a possibility that the preliminary financial statements may require adjustment before constituting a complete set of IFRS financial statements. Moreover, we draw attention to the fact that, under IFRS only a complete set of financial statements with comparative financial information and explanatory notes can provide a fair presentation of the Company's financial position, results of operations and cash flows in accordance with IFRSs. Our opinion is not qualified in respect of this matter.

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

Management is responsible for the preparation and fair presentation of the preliminary financial statements in accordance with the basis set out in the “Basis of preparation” paragraph of the Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021, and for such internal control as management determines is necessary to enable the preparation of preliminary financial statements that is free from material misstatement, whether due to fraud or error.

In preparing the preliminary financial statements, management is responsible for assessing the Company’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 Company or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

Auditors’ Responsibilities for the Audit of the Preliminary Financial Statements

Our objectives are to obtain reasonable assurance about whether the preliminary financial statements as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditors’ report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this preliminary 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 preliminary 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 Company’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 Company’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors’ report to the related disclosures in the preliminary financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors’ report. However, future events or conditions may cause the Company to cease to continue as a going concern;
- Evaluate the overall presentation, structure and content of the preliminary financial statements, including the disclosures, and whether the preliminary financial statements represent the underlying transactions and events in a manner that achieves fair presentation.



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

Baker Tilly Azerbaijan

September 13, 2021
Baku, the Republic of Azerbaijan

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF FINANCIAL POSITION AS AT DECEMBER 31, 2020 (In Azerbaijani Manats)

	Notes	December 31, 2020	January 1, 2020
ASSETS			
Non-current assets:			
Property, plant and equipment	8	222,335,070	223,052,833
Intangible assets	8	12,098	7,214
Prepayment for property, plant and equipment	9	113,492	-
Total non-current assets		222,460,660	223,060,047
Current assets:			
Inventories	10	42,984,495	53,797,268
Trade and other receivables	11	23,100,452	20,150,591
Cash and cash equivalents	12	21,068,442	29,856,328
Other current assets	13	15,274,184	12,662,907
Total current assets		102,427,573	116,467,094
TOTAL ASSETS		324,888,233	339,527,141
LIABILITIES AND EQUITY			
LIABILITIES:			
Non-current liabilities:			
Deferred tax liability	21	914,206	727,996
Trade and other payables	14	-	14,091,471
Total non-current liabilities		914,206	14,819,467
Current liabilities:			
Trade and other payables	14	38,997,135	40,475,624
Total current liabilities		38,997,135	40,475,624
Total liabilities		39,911,341	55,295,091
EQUITY:			
Charter capital	15	282,243,699	282,189,099
Other capital	16	-	54,600
Retained earnings		2,733,193	1,988,351
Total equity		284,976,892	284,232,050
TOTAL LIABILITIES AND EQUITY		324,888,233	339,527,141

On behalf of the Management Board:

Maxim Javadov
Director

September 13, 2021
Baku, the Republic of Azerbaijan



Jalal Habibov
Finance Director

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 40 are an integral part of this preliminary statement of financial position.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER 31, 2020

(In Azerbaijani Manats)

	Notes	Year ended December 31, 2020
Revenue	17	172,821,145
Cost of sales	18	<u>(160,298,646)</u>
Gross profit:		<u>12,522,499</u>
General and administrative expenses	19	(4,150,853)
Selling and distribution cost		(5,840,913)
Finance cost	20	<u>(1,632,000)</u>
Operating profit:		<u>898,733</u>
Other income, net		<u>32,319</u>
Profit before income tax		<u>931,052</u>
Income tax expense	21	<u>(186,210)</u>
Net profit for the year		<u>744,842</u>
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		<u>744,842</u>

On behalf of the Management Board:

Maxim Javadov
Director

September 13, 2021
Baku, the Republic of Azerbaijan

Jalal Habibov
Finance Director

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 40 are an integral part of these preliminary financial statements.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

	Charter capital	Other capital	Retained earnings	Total equity
January 1, 2020	282,189,099	54,600	1,988,351	284,232,050
Transfer	54,600	(54,600)	-	-
Total comprehensive income for the year	-	-	744,842	744,842
December 31, 2020	282,243,699	-	2,733,193	284,976,892

On behalf of the Management Board:

Maxim Javadov
Director

September 13, 2021
Baku, the Republic of Azerbaijan

Jalal Habibov
Finance Director

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 40 are an integral part of these preliminary financial statements.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

	Notes	Year ended December 31, 2020
CASH FLOWS FROM OPERATING ACTIVITIES:		
Profit before income tax		931,052
Adjustments to reconcile profit before income tax to net cash flows:		
Depreciation and amortization expenses	8	10,777,778
Finance costs	20	1,632,000
Gain from extinguishment of liabilities		(42,476)
Operating cash flows before working capital changes:		13,298,354
Changes in operating assets and liabilities:		
Change in trade and other receivables		(2,949,861)
Change in inventories		10,812,773
Change in trade and other payables		(15,527,484)
Change in other current assets		(2,611,277)
Finance costs paid	20	(1,632,000)
Net cash inflow from operating activities		1,390,505
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant and equipment		(10,178,391)
Net cash used in investing activities		(10,178,391)
NET DECREASE IN CASH AND CASH EQUIVALENTS		(8,787,886)
CASH AND CASH EQUIVALENTS, <i>at the beginning of the year</i>	12	29,856,328
CASH AND CASH EQUIVALENTS, <i>at the end of the year</i>	12	21,068,442

On behalf of the Management Board:

Maxim Javadov
Director

September 13, 2021
Baku, the Republic of Azerbaijan



Jalal Habibov
Finance Director

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 40 are an integral part of these preliminary financial statements

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 *(In Azerbaijani Manats)*

1. INTRODUCTION

“Azeraluminium” Limited Liability Company (the “Company”) was established in 2018 and registered by the Ministry of Economy of the Republic of Azerbaijan on April 16, 2018 with tax identification number 1305481501 as a limited liability company.

The structure of shareholding of the Company as at December 31, 2020 and January 1, 2020 was as followings:

	December 31, 2020 Ownership interest, %	January 1, 2020 Ownership interest, %
“Azerbaijan Industrial Corporation” Open Joint Stock Company	100.00	100.00
Total	100.00	100.00

The ultimate controlling party of the Company is the “Azerbaijan Industrial Corporation” Open Joint Stock Company.

Principal activities

The Company is a leading company in the field of non-ferrous metallurgy of the Republic of Azerbaijan and the only primary aluminium producer in the South Caucasus. The principal activities of the Company are concentrated in the aluminum complex and other facilities. These activities include production of primary aluminium and by-products, such as continuous casting coils, ingots and cold-rolled products using innovations of modern technologies in the production process. Overall production process meets requirements of the highest international standards, so it is widely used and applied in various markets across the world.

Registered address and place of business:

The Company is domiciled in the Republic of Azerbaijan. The Company’s registered legal address is Yasamal region, Tbilisi Avenue, Apartment 35, Baku, the Republic of Azerbaijan. The principal place of business of the Company is Yevlakh Highway 53, AZ2000, Ganja, the Republic of Azerbaijan.

Operating Environment of the Company

In March 2020 the World Health Organization (WHO) announced that the spread of the COVID-19 virus across the globe was a pandemic. Significant restrictions on travel and movement of individuals and the closure of non-essential businesses have either been imposed in most countries or have happened as a result of the pandemic. This has led to significant declines in GDP in most if not all large economically strong countries in which the Republic of Azerbaijan is in a trade relationship. The global economy was negatively impacted by the coronavirus pandemic (COVID-19) spread in the first half of 2020. Starting from June 2020 many countries including the Republic of Azerbaijan demonstrated improvement in the signs of pandemic and certain restrictions were lifted subsequently. As a result, recovery in global financial and commodity markets observed. However, subsequently the number of reported cases significantly increased in the Republic of Azerbaijan, and the government introduced new restrictions from mid-December 2020.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

The restrictive lock-down measures to combat COVID-19 in the country significantly reduced economic activity and aggregate spending levels. Certain segments of the economy, such as hotels, transport, travel, entertainment and many other businesses also international trade much affected by these measures. The government introduced support packages in the form of subsidized lending tools, payments to unemployed individuals and other subsidies to the entrepreneurs during the year to compensate for the economic slowdown caused by the pandemic.

The first months of 2020 have seen significant global market turmoil triggered by the outbreak of the novel coronavirus. As a result of the COVID-19 outbreak in the first half of 2020, aluminium prices continued to deteriorate. This factor had an adverse impact on the revenue and profitability of the Company during second and third quarter of 2020. By the start of December 2020 aluminium prices have mostly recovered back to the pre-COVID level which was also supported by the recovery of the global aluminium demand and production. During the first half of 2021 the aluminum prices increased by 15-20%. The global demand and production of aluminium is also expected to demonstrate positive trends but may be affected by further COVID-19 developments.

The Company's operations are conducted in the Republic of Azerbaijan. Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks. The future stability of Azerbaijan's economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Government as well as crude oil prices and stability of Azerbaijani Manat. Although the economy of the Republic of Azerbaijan is particularly sensitive to oil and gas prices, during recent years the Government of the Republic of Azerbaijan initiated major economic and social reforms to accelerate the transition to a more balanced economy and reduce dependence on the oil and gas sector. GDP in Azerbaijan was USD 42.6 billion during the year 2020, according to the State Statistical Committee of the Republic of Azerbaijan. In the long-term, the Azerbaijan GDP is projected to trend around USD 50 billion in 2021 and USD 51 billion in 2022, according to our econometric models.

The government continued its monetary policy with respect to the stability of Azerbaijani Manat as well as allocated foreign currency resources which stabilized Azerbaijani Manat. This policy continued in 2020 with the aim of maintaining macroeconomic stability. The Central Bank of the Republic of Azerbaijan has changed the refinancing rate several times during the year and the range was between 7.25% - 6.25% with a steady decrease in rates.

The Company's management is monitoring changes in the macroeconomic environment and taking precautionary measures it considers necessary in order to support the sustainability and development of the Company's business in the foreseeable future.

International credit rating agencies regularly evaluate the credit rating of the Republic of Azerbaijan. Fitch and S&P evaluated the rating of the Republic of Azerbaijan as “BB+”. Moody's Investors Service set “Ba2” credit rating for the country.

In September 2020, the escalation of unresolved conflict in Karabakh region (located in the southwest, which is internationally recognized as part of the Republic of Azerbaijan) resulted in clashes between the Republic of Azerbaijan and Armenian forces in occupied territories. In response, both countries introduced a curfew and military mobilization. Although the military actions mainly occurred in the western part of the Republic of Azerbaijan, some businesses were affected by the curfew which covered all the territories of the Republic of Azerbaijan including the capital Baku, to a certain degree. A complete ceasefire and a cessation of all hostilities in the zone of the Karabakh conflict were achieved on November 10, 2020. The level of macroeconomic effects in which the state involvement in liberated regions is uncertain as of reporting date.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

These events and conditions described above created a level of uncertainty and risk that companies have not encountered before. The above-mentioned events had a significant effect on the financial results of the Company during the year ended December 31, 2020 and in the subsequent period.

The future economic growth of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory and political developments. The Management is unable to predict, all developments in the economic environment which would have an impact on the Company's operations and consequently what effect, if any, they could have on the financial position of the Company. The management is currently performing sensitivity analyses under different oil price scenarios and elaborating relevant action plans for maintaining the sustainability of the business.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

The financial year of the Company ends on the last day of December. In previous years, the accounts have been prepared under Generally Accepted Accounting Principles of the Republic of Azerbaijan (“AZ GAAP”). Effective from January 1, 2020 the Company produces its financial statements in accordance with International Financial Reporting Standards (“IFRSs”).

The preliminary financial statements have been prepared on the basis of IFRSs issued as at the date of this report and expected to be applicable by December 31, 2021. IFRS are subject to ongoing review or possible amendment by interpretative guidance from the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) and are therefore still subject to change. The preliminary financial statements will be updated and restated as necessary for any such changes should they occur.

Basis of preparation

First time adoption of IFRS

The rules for first time adoption of IFRS are set out in IFRS 1 “First Time Adoption of International Financial Reporting Standards”. IFRS 1 requires an entity to comply with each IFRS effective at the reporting date for its first full set of IFRS financial statements. As a general principle IFRS 1 requires the standards effective at the reporting date to be applied retrospectively.

However, retrospective application is prohibited in some areas, particularly where retrospective application would require judgements by management after the outcome of the particular transaction is already known. In addition, a number of limited optional exemptions from full retrospective application of IFRS are granted where the cost of compliance is deemed to exceed the benefits to users of the financial statements. The exemptions are divided into:

- Mandatory exemptions;
- Optional exemptions.

The Company applied all mandatory exemptions. The optional exemptions chosen by the management include:

- Fair value or revaluation as deemed cost – The Company elected to use the fair value amount as deemed cost for property, plant and equipment at the date of transfer of these assets to the Company by the shareholder.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Going concern

This preliminary financial statements have been prepared on the assumption that the Company is a going concern and will continue in operation for the foreseeable future.

Management views the Company as continuing in business for the foreseeable future with neither the intention nor the necessity of liquidation, ceasing trading or seeking protection from creditors pursuant to laws or regulations of the Republic of Azerbaijan.

Accordingly, assets and liabilities are recorded on the basis that the Company will be able to realize its assets and discharge its liabilities in the normal course of business. Some financial reporting frameworks contain an explicit requirement for management to make a specific assessment of the Company's ability to continue as a going concern, and standards regarding matters to be considered and disclosures to be made in connection with going concern.

Management's assessment of the going concern assumption involves making a judgment, at a particular point in time, about the future outcome of events or conditions which are inherently uncertain.

Current versus non-current classification

The Company presents assets and liabilities in the preliminary financial statements based on current/non-current classification. An asset is current when it is:

- Expected to be realized or intended to be sold or consumed in the normal operating cycle;
- Held primarily for the purpose of trading;
- Expected to be realized within twelve months after the reporting period; or
- Cash or cash equivalent unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current.

A liability is current when:

- It is expected to be settled in the normal operating cycle;
- It is held primarily for the purpose of trading;
- It is due to be settled within twelve months after the reporting period; or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Company classifies all other liabilities as non-current.

Deferred tax assets and liabilities are classified as non-current assets and liabilities.

Other basis of presentation criteria

These preliminary financial statements are presented in Azerbaijani Manats (“AZN”), unless otherwise indicated. The preliminary financial statements have been prepared under the historical cost convention, except property, plant and equipment and intangible assets which are stated at fair value as deemed cost.

The adoption of IFRS has resulted in changes to the Company's accounting policies. The amended accounting policies are:

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Property, plant and equipment and intangible assets

Property, plant and equipments are stated in the preliminary statement of financial position at fair value as deemed cost, being the fair value at the date of revaluation, determined from market-based evidence by appraisal undertaken by professional independent appraisers, less any subsequent accumulated depreciation and impairment losses.

The estimated useful life, residual values and amortization method will be reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

At the end of each reporting period, the Company reviews the carrying amounts of its property, plant and equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

An item of property, plant and equipment and intangible assets is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit and loss accounts.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

The cost of periodic relining of electrolyzers is capitalised and depreciated over the expected production period.

The cost of replacing a part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in the statement of income as incurred.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Property, plant and equipment and intangible assets are generally depreciated on a straight-line basis over their estimated useful lives as follows. The land is not depreciated.

Buildings and similar constructions	20-50 years
Machinery and equipment	7-20 years
Electrolysers	5-15 years
Vehicles	5-7 years
Others	7-15 years
Intangible assets	2-10 years

The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

The residual value of an asset may increase to an amount equal to or greater than the asset's carrying amount. If it does, the asset's depreciation charge is zero unless and until its residual value subsequently decreases to an amount below the asset's carrying amount.

Taxation

Deferred taxes

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

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized. Deferred tax is charged or credited in the statement of comprehensive income, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred income tax assets and deferred income tax liabilities are offset and reported net on the preliminary statement of financial position if:

- The Company has a legally enforceable right to set off current income tax assets against current income tax liabilities; and
- Deferred income tax assets and the deferred income tax liability relate to income taxes levied by the same taxation authority on the same taxable entity.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Value added tax

The difference of output VAT and claimable input VAT is payable to the state budget within 20 days following the reporting month. Output value added tax related to sales is payable to tax authorities upon receipt of payment in return to such sales. Input VAT is generally recoverable against output VAT upon receipt of the electronic invoice. The tax authorities permit the settlement of VAT on a net basis.

VAT related to sales and purchases is recognized in the preliminary statement of financial position on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on weighted average cost principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

Financial instruments

Financial assets and financial liabilities are recognized in the Company's preliminary statement of financial position when the Company becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss.

Financial assets

All regular way purchases or sales of financial assets are recognized and derecognized on a trade date basis. All recognized financial assets are measured subsequently in their entirety at either amortised cost or fair value, depending on the classification of the financial assets.

Classification of financial assets

Debt instruments that meet the following conditions are measured subsequently at amortised cost:

- the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Debt instruments that meet the following conditions are measured subsequently at fair value through other comprehensive income (FVTOCI):

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- the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling the financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

By default, all other financial assets are measured subsequently at fair value through profit or loss (FVTPL).

Despite the foregoing, the Company may make the following irrevocable election/designation at initial recognition of a financial asset:

- the Company may irrevocably elect to present subsequent changes in fair value of an equity investment in other comprehensive income if certain criteria are met; and
- the Company may irrevocably designate a debt investment that meets the amortised cost or FVTOCI criteria as measured at FVTPL if doing so eliminates or significantly reduces an accounting mismatch

Amortized cost and effective interest method

The effective interest method is a method of calculating the amortized cost of a debt instrument and of allocating interest income over the relevant period. For financial assets other than purchased or originated credit-impaired financial assets (i.e. assets that are credit-impaired on initial recognition), the effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) excluding expected credit losses, through the expected life of the debt instrument, or, where appropriate, a shorter period, to the gross carrying amount of the debt instrument on initial recognition.

For purchased or originated credit-impaired financial assets, a credit-adjusted effective interest rate is calculated by discounting the estimated future cash flows, including expected credit losses, to the amortised cost of the debt instrument on initial recognition.

The amortized cost of a financial asset is the amount at which the financial asset is measured at initial recognition minus the principal repayments, plus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, adjusted for any loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any loss allowance.

Interest income is recognized using the effective interest method for debt instruments measured subsequently at amortised cost and at FVTOCI. For financial assets other than purchased or originated credit-impaired financial assets, interest income is calculated by applying the effective interest rate to the gross carrying amount of a financial asset, except for financial assets that have subsequently become credit-impaired. For financial assets that have subsequently become credit-impaired, interest income is recognized by applying the effective interest rate to the amortised cost of the financial asset. If, in subsequent reporting periods, the credit risk on the credit-impaired financial instrument improves so that the financial asset is no longer credit-impaired, interest income is recognized by applying the effective interest rate to the gross carrying amount of the financial asset.

The Company's majority of financial assets were classified as financial assets measured subsequently at amortized cost. The Company's financial liabilities were classified as financial liabilities measured subsequently at amortized cost. The Company does not choose to classify any financial liabilities as measured at fair value through profit or loss.

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Impairment of financial assets

The Company applies the expected credit loss model to financial assets measured at amortized cost or at fair value through other comprehensive income.

The allowance for expected credit losses for a financial asset is measured at an amount equal to the lifetime expected credit losses if the credit risk on that financial asset has increased significantly since initial recognition.

If, at the reporting date, the credit risk on a financial asset has not increased significantly since initial recognition, the allowance for expected credit losses for that financial asset (except trade and other receivables, where the simplified approach is elected) is measured at an amount equal to 12-month expected credit losses. For trade and other receivables, whether they contain a significant financing component or not, measurement based on lifetime expected credit losses are applied.

The Company utilizes an internal model to assess expected credit losses. The model was developed in accordance with IFRS 9 and designed to assess credit risk exposure of counterparties taking into account the characteristics of financial assets by assigning scoring system to counterparties. Assigned score is returning PD (Probability of Default) on individual basis. Move of the asset from one score band to lower score band is considered significant increase in credit risk among other criteria.

Fair value measurement

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

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

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

The Company 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.

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

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

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For assets and liabilities that are recognized in the financial statements on a recurring basis, the Company 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.

De-recognition of financial assets

The Company derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

Financial liabilities and equity

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recognized at the proceeds received, net of direct issue costs.

Repurchase of the Company's own equity instruments is recognized and deducted directly in equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company's own equity instruments.

Financial liabilities

All financial liabilities are measured subsequently at amortised cost using the effective interest method or at FVTPL.

Financial liabilities are classified as at FVTPL when the financial liability is (i) contingent consideration of an acquirer in a business combination, (ii) held for trading or (iii) it is designated as at FVTPL.

Financial liabilities that are not (i) contingent consideration of an acquirer in a business combination, (ii) held-for-trading, or (iii) designated as at FVTPL, are measured subsequently at amortised cost using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or (where appropriate) a shorter period, to the amortised cost of a financial liability.

De-recognition of financial liabilities

The Company removes a financial liability (or a part of a financial liability) from its preliminary statement of financial position when, and only when, it is extinguished - ie when the obligation specified in the contract is discharged or cancelled or expires.

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An exchange between an existing borrower and lender of debt instruments with substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10 per cent different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognized as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortized over the remaining term of the modified liability.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the preliminary statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Trade and other receivables

Trade and other receivables are carried at amortized cost using the effective interest method. The Company uses a provision matrix to calculate expected credit losses for trade and other receivables and contract assets. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography, product type, customer type and rating, and coverage by letters of credit and other forms of credit insurance).

The provision matrix is initially based on the Company's historical observed default rates. The Company will calibrate the matrix to adjust the historical credit loss experience with forward-looking information. For instance, if forecast economic conditions (i.e., gross domestic product) are expected to deteriorate over the next year which can lead to an increased number of defaults in the manufacturing sector, the historical default rates are adjusted. At every reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analyzed. Where applicable, the Company relies on default rates derived from external rates of counterparties.

The assessment of the correlation between historical observed default rates, forecast economic conditions and expected credit losses is a significant estimate. The amount of expected credit losses is sensitive to changes in circumstances and of forecast economic conditions. The Company's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future.

Advances to suppliers

Advances to suppliers are carried at cost less provision for impairment. An advance is classified as non-current when the goods or services relating to the advance are expected to be obtained after one year, or when the advance relates to an asset which will itself be classified as non-current upon initial recognition.

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Advances to acquire assets are transferred to the carrying amount of the asset once the Company has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Company. Other advances are written off to profit and loss accounts when the goods or services relating to the advances are received. If there is an indication that the assets, goods or services relating to an advance will not be received, the carrying value of the advance is written down accordingly and a corresponding impairment loss is recognized in profit and loss accounts.

VAT deposit account

The Value Added Tax (“VAT”) deposit account system is introduced in 2008 by the Ministry of Taxes of the Republic of Azerbaijan which aims prevention of VAT misuse. From January 1, 2008 on the basis of amendments to the Tax Code, the amount of VAT refund is considered the tax amount which is paid, according to the submitted VAT invoices to the taxpayer’s VAT deposit account in the framework of transactions carried out in this account.

By the support of this module the taxpayer pays the amount of VAT indicated on the VAT invoices to the VAT deposit account of another taxpayer. At the same time tax obligations to the state budget regarding all kinds of taxes and VAT amounts on the import transactions which is necessary to be paid to the customs committee, can be paid by taxpayers through the VAT deposit account. Information about paid amounts is transferred by the tax authority to the Main State Treasury (“MST”) and then to the Central Bank of the Republic of Azerbaijan (“CBRA”). CBRA on the basis of information submitted by the Main State Treasury ensures the transformation of amounts to the relevant local treasury authorities. The tax authority ensures inclusion of amounts which is noted in the submitted information to the taxpayer’s personal files. The current system is connected with the Automated Tax Information System maintained by the State Tax Service under the Ministry of Economy of the Republic of Azerbaijan. At the same time online exchange of information was organized with the MST and CBRA.

Implementation of the VAT deposit account makes it possible to timely control payments and refunded VAT amounts. Taxpayers who have tax debts can only transfer these amounts to the state budget. Taxpayers can make payments to the state budget without visiting banks, to the VAT deposit account of other taxpayers and to the customs committee through the deposit account. The State Tax Service under the Ministry of Economy of the Republic of Azerbaijan automatically controls all transactions carried out through the deposit account using special software.

Use of balances in the VAT deposit account is restricted and can be used only for transactions connected with VAT and other applicable taxes.

Charter capital

Charter capital is the amount of capital contributed by the shareholder of the Company. The Company may increase or decrease its charter capital within approval of the shareholder.

Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised.

The details of significant accounting policies in relation to the Company’s various goods and services are set out below:

Sales of goods: comprise sale of primary aluminium, alloys, alumina and other products.

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Customers obtain control of the goods supplied when the goods are delivered to the point when risks are transferred based on Incoterms delivery terms stated in the contract. Invoices are generated and revenue is recognised at that point in time. Invoices are usually payable within 30 days or in advance.

Under certain Group sale contracts the final price for the goods shipped is determined a few months later than the delivery took place. Under current requirements the Company determines the amount of revenue at the moment of recognition based on estimated selling price at the date of the invoice issued. At price finalisation the difference between estimated price and actual one is recognised as other revenue.

Rendering of transportation services: as part of sales of goods the Company also performs transportation to the customer under contract terms. In certain cases, the control for goods delivered is transferred to customer at earlier point than the transportation is completed. In these cases, rendering of transportation services from when the control of goods has transferred is considered as a separate performance obligation.

Employee benefits

Wages, salaries, contributions to the Republic of Azerbaijan state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Company.

Foreign currency translation

The functional currency of the Company is the currency of the primary economic environment, in which it operates. The Company's functional currency is AZN.

Monetary assets and liabilities denominated in foreign currencies are translated into AZN at the appropriate spot rates of exchange of the CBRA ruling at the end of reporting date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transaction.

Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

The exchange rates at reporting date used by the Company in the preparation of the preliminary statement of financial position are as follows:

	December 31, 2020	January 1, 2020
1 USD	1.7000 AZN	1.7000 AZN
1 EUR	2.0890 AZN	1.9035 AZN

Contingent liabilities and assets

Contingent liabilities are not recognized in the preliminary statement of financial position. They are disclosed in the notes to the preliminary statement of financial position unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets are not recognized in the preliminary statement of financial position but disclosed when an inflow of economic benefits is probable.

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3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The preparation of preliminary statement of financial position requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and disclosure of contingent liabilities during the reporting period.

As a result of the uncertainties inherent in business activities, many items in preliminary statement of financial position cannot be measured with precision but can only be estimated. Estimation involves judgments based on the latest information available when the preliminary statement of financial position was prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Company. Such changes are reflected in the assumptions when they occur.

The most significant estimates relate to the depreciable lives of property, plant and equipment, impairment of non-financial and financial assets, fair value of financial instruments, provision for obsolete inventory, provision for tax and legal contingencies and deferred taxation. Actual results could differ from these estimates.

Judgments

In the process of applying Company's accounting policies, the management has made the following judgments, apart from those involving estimates, which have the most significant effect on the amounts recognized in the preliminary statement of financial position.

Fair value of property, plant and equipment and intangible assets

Property, plant and equipment and intangible assets were measured at fair value as deemed costs at the date when these assets were transferred to the Company.

Fair value of property, plant and equipments was assessed using the market approach method which involves analysis of market sales prices for similar property, plant and equipments which was also equal to the fair value of property, plant and equipment under IFRS 13.

Useful life of property, plant and equipment and intangible assets

The Company assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors". These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and intangible assets and on depreciation and amortization recognized in profit and loss accounts.

Impairment of property, plant and equipment and other non-financial assets

The Company assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Company makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If no such transactions can be identified, an appropriate valuation model is used.

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The Company bases its impairment calculation on detailed budgets and forecast calculations which are prepared separately for each of the Company's cash-generating units (CGU) to which the individual asset is allocated. These budgets and forecast calculations generally cover the period of 5 years. For longer periods, a long-term growth rate is determined and applied to project future cash flows after the fifth year. As at December 31, 2020 accumulated impairment loss on a property, plant and equipment amounted to nil.

Inventory valuation

Inventory is valued at the lower of cost or net realizable value. The Company records an allowance to reduce the carrying value of obsolete and slow-moving inventory to net realizable value, when appropriate. The actual value realized on disposition of such inventory may differ from the net realizable value; any such difference could have a significant impact on future operating results.

Recoverability of VAT

At each reporting date the Company assesses the recoverability of VAT arising on purchase of goods and services. The Company can only receive these amounts through an offset against future VAT liability or collection from the tax authorities. In assessing the recoverability of the VAT receivable, the Company considers information from the internal tax department regarding projected VAT liability, correspondence with government tax authorities, and historical recovery experience.

The actual amount of VAT recovery could differ materially from the Company's estimate and this could materially impact operating results.

Fair value measurement of financial instruments

A number of the Company's accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities.

The Company has an established control framework with respect to the measurement of fair values.

When measuring the fair value of an asset or a liability, the Company uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

- *Level 1:* quoted prices (unadjusted) in active markets for identical assets or liabilities;
- *Level 2:* inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- *Level 3:* inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

Current taxes

Azerbaijani tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Company's entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Company's entities may be assessed additional taxes, penalties and interest, which can be significant.

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Periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As at December 31, 2020, the management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Company's tax, currency and customs positions will be sustained.

Deferred taxes

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

4. ADOPTION OF NEW AND REVISED STANDARDS AND INTERPRETATIONS

In the current year, the Company has adopted all of the applicable new and revised Standards and Interpretations issued by the IASB and the IFRIC of the IASB that are relevant to its operations and effective for the year ending December 31, 2021.

On May 15, 2020 IASB has published **“Covid-19-Related Rent Concessions (Amendment to IFRS 16)”** amending the standard to provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification.

The changes in Covid-19-Related Rent Concessions (Amendment to IFRS 16) amend IFRS 16 to:

- provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification;
- require lessees that apply the exemption to account for COVID-19-related rent concessions as if they were not lease modifications;
- require lessees that apply the exemption to disclose that fact; and
- require lessees to apply the exemption retrospectively in accordance with IAS 8, but not require them to restate prior period figures.

The amendment is effective for annual reporting periods beginning on or after June 1, 2020. Earlier application is permitted. The impact of adoption of this standard had no effect on the financial statements.

Unless otherwise disclosed, the new adopted standards did not have material effect on the financial statements of the Company.

5. STANDARDS AND INTERPRETATIONS ISSUED AND NOT YET ADOPTED

At the date of authorization of these financial statements, other than the Standards and Interpretations adopted by the Company in advance of their effective dates, the following Interpretations were in issue but not yet effective.

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IFRS 17 “Insurance contracts” – was issued in May 2017 and replaced IFRS 4 “Insurance contracts”. The new standard establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the standard. An entity shall apply IFRS 17 “Insurance Contracts” to insurance contracts, including reinsurance contracts, it issues; reinsurance contracts it holds; and investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts.

IFRS 17 is effective for annual reporting periods beginning on or after January 1, 2023. Earlier application is permitted if both IFRS 15 Revenue from Contracts with Customers and IFRS 9 Financial Instruments have also been applied. This standard is not applicable to the Company.

Amendments to IAS 1 to clarify the classification of liabilities – In January 2020 the IASB has issued **“Classification of Liabilities as Current or Non-Current (Amendments to IAS 1)”** providing a more general approach to the classification of liabilities under IAS 1 based on the contractual arrangements in place at the reporting date. The amendments in Classification of Liabilities as Current or Non-Current (Amendments to IAS 1) affect only the presentation of liabilities in the statement of financial position – not the amount or timing of recognition of any asset, liability income or expenses, or the information that entities disclose about those items.

The amendments are effective for annual reporting periods beginning on or after January 1, 2023 and are to be applied retrospectively. Earlier application is permitted. The Company is currently assessing the impact the amendments will have on the current practice and whether existing loan agreements may require renegotiation.

Reference to the Conceptual Framework – Amendments to IFRS 3 In May 2020, the IASB issued **Amendments to IFRS 3 “Business Combinations” – Reference to the Conceptual Framework**. The amendments are intended to replace a reference to the Framework for the Preparation and Presentation of Financial Statements, issued in 1989, with a reference to the Conceptual Framework for Financial Reporting issued in March 2018 without significantly changing its requirements. The Board also added an exception to the recognition principle of IFRS 3 to avoid the issue of potential ‘day 2’ gains or losses arising for liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 Levies, if incurred separately. At the same time, the Board decided to clarify existing guidance in IFRS 3 for contingent assets that would not be affected by replacing the reference to the Framework for the Preparation and Presentation of Financial Statements. The amendments are effective for annual reporting periods beginning on or after January 1, 2022 and apply prospectively.

Property, Plant and Equipment: Proceeds before Intended Use – Amendments to IAS 16 In May 2020, the IASB issued **Property, Plant and Equipment – Proceeds before Intended Use**, which prohibits entities deducting from the cost of an item of property, plant and equipment, any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognizes the proceeds from selling such items, and the costs of producing those items, in profit or loss. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 and must be applied retrospectively to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented when the entity first applies the amendment. The amendments are not expected to have a material impact on the Company.

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Onerous Contracts – Costs of Fulfilling a Contract – Amendments to IAS 37 In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making. The amendments apply a “directly related cost approach”. The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract. The amendments are effective for annual reporting periods beginning on or after January 1, 2022.

IFRS 1 “First-time Adoption of International Financial Reporting Standards” – Subsidiary as a first-time adopter. As part of its 2018-2020 annual improvements to IFRS standards process, the IASB issued an amendment to IFRS 1 “First-time Adoption of International Financial Reporting Standards”. The amendment permits a subsidiary that elects to apply paragraph D16(a) of IFRS 1 to measure cumulative translation differences using the amounts reported by the parent, based on the parent’s date of transition to IFRS. This amendment is also applied to an associate or joint venture that elects to apply paragraph D16 (a) of IFRS 1. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted.

IFRS 9 Financial Instruments – Fees in the “10 per cent” test for de-recognition of financial liabilities. As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued an amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other’s behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted. The Company will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

“IAS 41 Agriculture” – Taxation in fair value measurements. As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued an amendment to IAS 41 Agriculture. The amendment removes the requirement in paragraph 22 of IAS 41 that entities exclude cash flows for taxation when measuring the fair value of assets within the scope of IAS 41. An entity applies the amendment prospectively to fair value measurements on or after the beginning of the first annual reporting period beginning on or after January 1, 2022 with earlier adoption permitted. The amendments are not expected to have impact on the Company.

IFRS 10 “Consolidated Financial Statements” and IAS 28 (amendments) Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – The amendments to IFRS 10 and IAS 28 deal with situations where there is a sale or contribution of assets between an investor and its associate or joint venture. Specifically, the amendments state that gains or losses resulting from the loss of control of a subsidiary that does not contain a business in a transaction with an associate or a joint venture that is accounted for using the equity method, are recognized in the parent’s profit or loss only to the extent of the unrelated investors’ interests in that associate or joint venture.

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Similarly, gains and losses resulting from the re-measurement of investments retained in any former subsidiary (that has become an associate or a joint venture that is accounted for using the equity method) to fair value are recognized in the former parent's profit or loss only to the extent of the unrelated investors' interests in the new associate or joint venture. The effective date of the amendments has yet to be set by the IASB; however, earlier application of the amendments is permitted.

Unless otherwise disclosed, the new pronounced standards are not expected to have a material effect on the financial statements of the Company.

6. BALANCES AND TRANSACTIONS WITH RELATED PARTIES

Related parties are defined in IAS 24 “Related Party Disclosures”. Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. The Company's immediate parent is “Azerbaijan Industrial Corporation” Open Joint Stock Company, which is fully owned by the Government of the Republic of Azerbaijan.

The Company applied the exemption in paragraph 25 of IAS 24 “Related Party Disclosures” regarding the disclosure requirement for government related entities.

A reporting entity is exempt from the disclosure requirements of paragraph 18 of IAS 24 “Related Party Disclosures” in relation to related party transactions and outstanding balances, including commitments, with:

- (a) a government that has control or joint control of, or significant influence over, the reporting entity; and
- (b) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity.

The nature of transactions with government related entities include purchase of electricity, gas, petrol and receiving other services.

During the year ended December 31, 2020, the remuneration of key management personnel included salaries, discretionary bonuses and other short-term benefits totalling AZN 73,606.

7. FIRST TIME ADOPTION OF IFRS

The Company first adopted IFRSs in 2020, with the date of effective transition to IFRSs as at January 1, 2020. The Company's preliminary statement of financial position is reconciled with previously adopted GAAP of the Republic of Azerbaijan (the “previous GAAP”) frameworks as follows.

The effect of transition to IFRS and correction of errors made to the opening IFRS statement of financial position as at January 1, 2020 is as follows:

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Preliminary statement of financial position	Notes	Previous GAAP (as presented)	Effect of transition to IFRS/ errors	IFRS (as adjusted)
		January 1, 2020	January 1, 2020	January 1, 2020
Property, plant, equipment	a	222,718,505	334,328	223,052,833
Inventories	a	54,131,596	(334,328)	53,797,268
Trade and other receivables	b	19,679,572	471,019	20,150,591
Cash and cash equivalents	b,c	30,680,555	(824,227)	29,856,328
Other current assets	c,d	13,159,699	(496,792)	12,662,907
Deferred tax liability	e	(590,052)	(137,944)	(727,996)
Trade and other payables	d	(55,417,095)	850,000	(54,567,095)
Charter capital	f	(282,243,699)	54,600	(282,189,099)
Other capital	f	-	(54,600)	(54,600)
Retained earnings	e	(2,126,295)	137,944	(1,988,351)

Explanations for the correction of errors and effect of transition:

- Difference is due to correction for reclassification of fixed assets recorded in inventory balance;
- Blocked bank account reclassified from cash and cash equivalents to trade and other receivables;
- VAT deposit account reclassified from cash and cash equivalents to other current assets;
- The Company made reclassification between other current assets and trade and other payables;
- The Company has adjusted for deferred tax liability to comply with IFRS;
- The Company reclassified charter capital balance to other capital in relation with properties transferred by shareholder but not yet registered as charter capital.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

**NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)**

(In Azerbaijani Manats)

8. PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

	Buildings and similar constructions	Machinery and equipment	Electrolysers	Vehicles	Equipment to be installed	Others	Total	Intangible assets	Total
Fair value as deemed cost/initial cost									
January 1, 2020	66,600,546	102,549,243	67,633,723	556,136	-	610,512	237,950,160	33,275	237,983,435
Additions	2,758,588	1,936,483	3,269,598	-	1,557,679	531,551	10,053,899	11,000	10,064,899
December 31, 2020	<u>69,359,134</u>	<u>104,485,726</u>	<u>70,903,321</u>	<u>556,136</u>	<u>1,557,679</u>	<u>1,142,063</u>	<u>248,004,059</u>	<u>44,275</u>	<u>248,048,334</u>
Accumulated depreciation and amortization									
January 1, 2020	(3,313,847)	(7,235,185)	(4,219,329)	(79,240)	-	(49,726)	(14,897,327)	(26,061)	(14,923,388)
Charge for the year	(1,299,656)	(5,074,025)	(4,321,159)	(48,763)	-	(28,059)	(10,771,662)	(6,116)	(10,777,778)
December 31, 2020	<u>(4,613,503)</u>	<u>(12,309,210)</u>	<u>(8,540,488)</u>	<u>(128,003)</u>	<u>-</u>	<u>(77,785)</u>	<u>(25,668,989)</u>	<u>(32,177)</u>	<u>(25,701,166)</u>
Net book value									
December 31, 2020	<u>64,745,631</u>	<u>92,176,516</u>	<u>62,362,833</u>	<u>428,133</u>	<u>1,557,679</u>	<u>1,064,278</u>	<u>222,335,070</u>	<u>12,098</u>	<u>222,347,168</u>
January 1, 2020	<u>63,286,699</u>	<u>95,314,058</u>	<u>63,414,394</u>	<u>476,896</u>	<u>-</u>	<u>560,786</u>	<u>223,052,833</u>	<u>7,214</u>	<u>223,060,047</u>

As at December 31, 2020 and January 1, 2020, included in property, plant and equipment there were neither any assets with restrictions on title, nor any assets that were pledged as security for liabilities.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

9. PREPAYMENT FOR PROPERTY, PLANT AND EQUIPMENT

As at December 31, 2020, prepayment for property, plant and equipment includes advance to supplier for purchase of office furniture and fixtures in the amount of AZN 113,492 (January 1, 2020: nil).

10. INVENTORIES

Inventories comprise:

	December 31, 2020	January 1, 2020
Raw materials	9,181,811	21,253,468
Work-in-process	1,723,208	1,505,690
Finished goods	26,022,290	24,113,337
Spare parts	4,998,233	5,877,504
Others	1,058,953	1,047,269
Total inventories	42,984,495	53,797,268

11. TRADE AND OTHER RECEIVABLES

Trade and other receivables comprise:

	December 31, 2020	January 1, 2020
Trade receivables from customers	23,100,452	19,679,572
Restricted bank account	-	471,019
Total trade and other receivables	23,100,452	20,150,591

12. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise:

	December 31, 2020	January 1, 2020
Cash at banks	21,068,442	27,266,059
Cash on hand	-	2,590,269
Total cash and cash equivalents	21,068,442	29,856,328

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

13. OTHER CURRENT ASSETS

	December 31, 2020	January 1, 2020
Advance to suppliers	5,415,697	5,789,816
Tax receivables	6,081,896	3,807,320
VAT recoverable	3,768,007	2,712,563
VAT deposit account	8,584	353,208
Total other current assets	15,274,184	12,662,907

14. TRADE AND OTHER PAYABLES

	December 31, 2020	January 1, 2020
Interest bearing trade payables for inventories	10,319,076	30,957,234
Trade payables for inventories and other services	24,744,822	18,663,594
Amount due to related party	2,970,204	2,970,204
Other payables	200,000	-
Total financial payables	38,234,102	52,591,032
Advance received	763,033	1,976,063
Total trade and other payables	38,997,135	54,567,095
Current portion of trade and other payables	38,997,135	40,475,624
Non-current portion of trade and other payables	-	14,091,471
Total trade and other payables	38,997,135	54,567,095

15. CHARTER CAPITAL

As at December 31, 2020, charter capital amounted to AZN 282,243,699 and consists of 100 shares with AZN 2,822,436.99 face value per share (January 1, 2020: AZN 282,189,099 and consists of 100 shares with AZN 2,821,890.99 face value per share). During 2020, the Company registered other capital amounting AZN 54,600 as charter capital.

16. OTHER CAPITAL

As at December 31, 2020, other capital was nil. As at January 1, 2020, other capital amounted to AZN 54,600 and consisted of asset transferred to the Company by shareholder but not yet registered as charter capital.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

17. REVENUE

Revenue comprises:

	Year ended December 31, 2020
Sales of primary aluminium	85,725,031
Sales of foil and other aluminium products	85,675,304
Other revenues	<u>1,420,810</u>
Total revenue	<u><u>172,821,145</u></u>

18. COST OF SALES

Cost of sales comprises:

	Year ended December 31, 2020
Material expenses	108,143,664
Utility expenses	31,330,188
Depreciation expense	10,739,184
Staff cost	10,192,079
Taxes other than income tax	2,020,002
Change in finished goods and work-in-progress	<u>(2,126,471)</u>
Total cost of sales	<u><u>160,298,646</u></u>

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

19. GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses comprise:

	Year ended December 31, 2020
Staff cost	1,599,737
Meal expenses	515,253
Security expense	327,897
Covid-19 related expenses	235,000
Rent expense	204,707
Repair and maintenance expense	165,185
Business trip expense	160,222
Insurance expense	159,232
Bank charge	132,309
Professional fee	129,867
Transportation expense	97,047
Communication expense	83,839
Depreciation expense	38,594
Representation expense	34,835
Office supplies	32,793
Advertising expenses	32,132
Other expenses	202,204
Total general and administrative expenses	4,150,853

20. FINANCE COST

For the year ended December 31, 2020, finance cost in the amount of AZN 1,632,000 was related to interest bearing trade payables to Noble Resources Limited for inventories.

21. INCOME TAX

The Company measures and records its current income tax liability and its tax bases related to assets and liabilities in accordance with the statutory tax regulations of the Republic of Azerbaijan where the Company operates, which differ from IFRS.

The Company is subject to certain permanent tax differences due to non-tax deductibility of certain expenses and certain income being treated as non-taxable for tax purposes.

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

Temporary differences as at December 31, 2020 and January 1, 2020 relate mostly to different methods/timing of income and expense recognition as well as to temporary differences generated by taxation bases' differences for certain assets.

Tax legislation of the Republic of Azerbaijan in particular may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result the Company may be assessed additional taxes, penalties and interest which could be material for this preliminary statement of financial position.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

Temporary differences as at December 31, 2020 and January 1, 2020 comprise:

	December 31, 2020	January 1, 2020
Deductible temporary differences:		
Tax loss carry forward	33,054,627	20,590,479
Other current assets	82,487	-
Total deductible temporary differences	33,137,114	20,590,479
Taxable temporary differences:		
Property, plant and equipment	(37,598,742)	(24,230,457)
Trade and other payables	(109,403)	-
Total taxable temporary differences	(37,708,145)	(24,230,457)
Net taxable temporary differences	(4,571,031)	(3,639,978)
Net deferred tax liability at statutory tax rate of 20%	(914,206)	(727,996)

Relationships between tax expenses and accounting profit for the year ended December 31, 2020 as follows:

	Year ended December 31, 2020
Profit before income tax	931,052
Theoretical tax charge at statutory rate of 20%	(186,210)
Income tax expense	(186,210)
Current income tax expense	-
Change in the deferred income tax liability	(186,210)
Income tax expense	(186,210)
Deferred tax liability	
Balance brought forward	(727,996)
Change in the deferred tax liability for the period charged to profit and loss accounts	(186,210)
Balance carried forward	(914,206)

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

22. COMMITMENTS AND CONTINGENCIES

Legal proceedings

From time to time and in the normal course of business, claims against the Company were received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in this preliminary statement of financial position.

Taxation

Commercial legislation and tax legislation of the Republic of Azerbaijan in particular may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result, the Company may be assessed additional taxes, penalties and interest.

The Company believes that it has already made all tax payments, and therefore no allowance has been made in the preliminary statement of financial position. Tax years remain open to review by the tax authorities for three years.

23. FINANCIAL RISK MANAGEMENT

Management of risk is fundamental to the Company's business and is an essential element of its operations. The main risks inherent to the Company operations are those related to:

- Credit risk;
- Liquidity risk;
- Market risk.

The Company recognizes that it is essential to have efficient and effective risk management processes in place. To enable this, the Company has established a risk management department. The main purpose of this department is to protect the Company from risk and allow it to achieve its performance objectives. Through the risk management framework, the Company manages the following risks:

Credit risk

The Company is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

Maximum exposure

The Company's maximum exposure to credit risk varies significantly and is dependent on both individual risks and general market economy risks.

Geographical concentration

Assets, liabilities and credit related commitments have been based on the country, in which the counterparty is located. Balances with counterparties located in the Republic of Azerbaijan actually outstanding to/from companies of these counterparties are allocated to the caption "The Republic of Azerbaijan". Cash on hand, precious metals and premises and equipment have been allocated based on the country, in which they are physically held.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The geographical concentration of the Company’s financial assets and liabilities as at December 31, 2020 is set out below:

	The Republic of Azerbaijan	OECD countries	Other non-OECD countries	December 31, 2020 Total
FINANCIAL ASSETS				
Trade and other receivables	341,226	20,767,914	1,991,312	23,100,452
Cash and cash equivalents	21,068,442	-	-	21,068,442
TOTAL FINANCIAL ASSETS	21,409,668	20,767,914	1,991,312	44,168,894
FINANCIAL LIABILITIES				
Trade and other payables	27,692,307	216,594	10,325,201	38,234,102
TOTAL FINANCIAL LIABILITIES	27,692,307	216,594	10,325,201	38,234,102
NET POSITION	(6,282,639)	20,551,320	(8,333,889)	5,934,792

The geographical concentration of the Company’s financial assets and liabilities as at January 1, 2020 is set out below:

	The Republic of Azerbaijan	OECD countries	Other non-OECD countries	January 1, 2020 Total
FINANCIAL ASSETS				
Trade and other receivables	749,512	16,951,635	2,449,444	20,150,591
Cash and cash equivalents	29,856,328	-	-	29,856,328
TOTAL FINANCIAL ASSETS	30,605,840	16,951,635	2,449,444	50,006,919
FINANCIAL LIABILITIES				
Trade and other payables	18,781,259	10,347	33,799,426	52,591,032
TOTAL FINANCIAL LIABILITIES	18,781,259	10,347	33,799,426	52,591,032
NET POSITION	11,824,581	16,941,288	(31,349,982)	(2,584,113)

Liquidity risk

Liquidity risk is defined as the risk when the maturity of financial assets and liabilities does not match. Liquidity risk is managed by the Finance Department of the Company. The liquidity management of the Company requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring balance sheet liquidity ratio.

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The liquidity risk of the Company's financial assets and liabilities as at December 31, 2020 are set out below:

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	December 31, 2020 Total
FINANCIAL ASSETS					
Trade and other receivables	14,405,020	8,695,432	-	-	23,100,452
Cash and cash equivalents	21,068,442	-	-	-	21,068,442
Total financial assets	35,473,462	8,695,432	-	-	44,168,894
FINANCIAL LIABILITIES					
Trade and other payables	26,664,668	3,439,692	8,129,742	-	38,234,102
Total financial liabilities	26,664,668	3,439,692	8,129,742	-	38,234,102
Liquidity gap	8,808,794	5,255,740	(8,129,742)	-	5,934,792
Cumulative liquidity gap	8,808,794	14,064,534	5,934,792	5,934,792	

The liquidity risk of the Company's financial assets and liabilities as at January 1, 2020 are set out below:

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	January 1, 2020 Total
FINANCIAL ASSETS					
Trade and other receivables	8,678,585	11,000,987	471,019	-	20,150,591
Cash and cash equivalents	29,856,328	-	-	-	29,856,328
Total financial assets	38,534,913	11,000,987	471,019	-	50,006,919
FINANCIAL LIABILITIES					
Trade and other payables	17,711,255	3,779,692	17,008,614	14,091,471	52,591,032
Total financial liabilities	17,711,255	3,779,692	17,008,614	14,091,471	52,591,032
Liquidity gap	20,823,658	7,221,295	(16,537,595)	(14,091,471)	(2,584,113)
Cumulative liquidity gap	20,823,658	28,044,953	11,507,358	(2,584,113)	

A further analysis of the liquidity and interest rate risks is presented in the following tables in accordance with IFRS 7. The amounts disclosed in these tables do not correspond to the amounts recorded in the preliminary statement of financial position as the presentation below includes a maturity analysis for financial liabilities that indicates the total remaining contractual payments (including interest payments), which are not recognized in the preliminary statement of financial position under the effective interest rate method.

The liquidity risk of the Company's financial assets and liabilities in accordance with IFRS 7 as at December 31, 2020 are set out below:

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	December 31, 2020 Total
Financial liabilities					
Trade and other payables	26,784,927	3,586,177	8,475,960	-	38,847,064
Total potential future payments for financial liabilities	26,784,927	3,586,177	8,475,960	-	38,847,064

The liquidity risk of the Company's financial assets and liabilities as at January 1, 2020 are set out below:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	January 1, 2020 Total
Financial liabilities					
Trade and other payables	17,791,737	3,940,656	17,732,952	14,574,363	54,039,708
Total potential future payments for financial liabilities	17,791,737	3,940,656	17,732,952	14,574,363	54,039,708

Currency risk

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

The currency risk of the Company's financial assets and liabilities as at December 31, 2020 are set out below:

	AZN	USD	EUR	Other	December 31, 2020 Total
FINANCIAL ASSETS					
Trade and other receivables	341,226	22,759,226	-	-	23,100,452
Cash and cash equivalents	83,832	20,839,148	14,670	130,792	21,068,442
TOTAL FINANCIAL ASSETS	425,058	43,598,374	14,670	130,792	44,168,894
FINANCIAL LIABILITIES					
Trade and other payables	15,185,297	23,047,109	-	1,696	38,234,102
TOTAL FINANCIAL LIABILITIES	15,185,297	23,047,109	-	1,696	38,234,102
OPEN CURRENCY POSITION	(14,760,239)	20,551,265	14,670	129,096	5,934,792

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The currency risk of the Company's financial assets and liabilities as at January 1, 2020 are set out below:

	AZN	USD	EUR	Other	January 1, 2020 Total
FINANCIAL ASSETS					
Trade and other receivables	278,492	19,872,099	-	-	20,150,591
Cash and cash equivalents	2,610,754	27,230,696	14,878	-	29,856,328
TOTAL FINANCIAL ASSETS	2,889,246	47,102,795	14,878	-	50,006,919
FINANCIAL LIABILITIES					
Trade and other payables	6,947,590	45,633,095	10,347	-	52,591,032
TOTAL FINANCIAL LIABILITIES	6,947,590	45,633,095	10,347	-	52,591,032
OPEN CURRENCY POSITION	(4,058,344)	1,469,700	4,531	-	(2,584,113)

24. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Company using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Republic of Azerbaijan continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

The fair value of financial assets and liabilities recognized at cost or amortized cost in the preliminary statement of financial position as at December 31, 2020 is presented below:

	December 31, 2020	
	Carrying value	Fair value
Trade and other receivables	23,100,452	23,100,452
Cash and cash equivalents	21,068,442	21,068,442
Trade and other payables	38,234,102	38,234,102

“AZERALUMINIUM” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The fair value of financial assets and liabilities recognized at cost or amortized cost in the preliminary financial statements as at January 1, 2020 is presented below:

	January 1, 2020	
	Carrying value	Fair value
Trade and other receivables	20,150,591	20,150,591
Cash and cash equivalents	29,856,328	29,856,328
Trade and other payables	52,591,032	52,591,032

The following table sets out the fair values of financial instruments not measured at fair value and analyzes them by the level in the fair value hierarchy into which each fair value measurement as at December 31, 2020 is categorized below:

		Fair value measurement using				
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed						
Trade and other receivables	Amortized cost	December 31, 2020	-	-	23,100,452	23,100,452
Cash and cash equivalents	Amortized cost	December 31, 2020	21,068,442	-	-	21,068,442
Liabilities for which fair values are disclosed						
Trade and other payables	Amortized cost	December 31, 2020	-	-	38,234,102	38,234,102

The following table sets out the fair values of financial instruments not measured at fair value and analyzes them by the level in the fair value hierarchy into which each fair value measurement as at January 1, 2020 is categorized below:

		Fair value measurement using				
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed						
Trade and other receivables	Amortized cost	January 1, 2020	-	-	20,150,591	20,150,591
Cash and cash equivalents	Amortized cost	January 1, 2020	29,856,328	-	-	29,856,328
Liabilities for which fair values are disclosed						
Trade and other payables	Amortized cost	January 1, 2020	-	-	52,591,032	52,591,032

**“AZERCOTTON AGRO-INDUSTRIAL
COMPLEX” LIMITED LIABILITY
COMPANY**

**The International Financial Reporting Standards
Preliminary Financial Statements
and Independent Auditors’ Report**
For the Year Ended December 31, 2020

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020

The following statement is made with a view to distinguishing respective responsibilities of the management and those of the independent auditors in relation to the International Financial Reporting Standards ("IFRS") preliminary financial statements of "Azercotton Agro-Industrial Complex" Limited Liability Company (the "Company").

Management is responsible for the preparation of the preliminary financial statements that present fairly the financial position of the Company as at December 31, 2020, the results of its operations, changes in equity and cash flows for the year then ended, in accordance with the basis set out in the "Basis of preparation" paragraph of Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021.

In preparing the preliminary financial statements, management is responsible for:

- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether accounting policies have been followed, subject to any material departures disclosed and explained in the preliminary financial statements; and
- Preparing the preliminary financial statements on a going concern basis, unless it is inappropriate to presume that the Company will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Company;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the preliminary financial statements of the Company, and which enable them to ensure that the preliminary financial statements of the Company comply with IFRS;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Company; and
- Detecting and preventing fraud, errors and other irregularities.

The preliminary financial statements for the year ended December 31, 2020 were authorized for issue on September 27, 2021 by the Management of the Company.

On behalf of the Management Board:


Bahruz Jamalov
Director
September 27, 2021
Baku, the Republic of Azerbaijan

Orkhan Khalafov
Deputy Finance Manager

September 27, 2021
Baku, the Republic of Azerbaijan

INDEPENDENT AUDITORS' REPORT

To the Shareholder and Management of "Azercotton Agro-Industrial Complex" Limited Liability Company:

Opinion

We have audited the preliminary financial statements of "Azercotton Agro-Industrial Complex" Limited Liability Company (the "Company") for the year ended December 31, 2020, which comprises the preliminary statement of financial position as at December 31, 2020, and the preliminary statement of comprehensive income, the preliminary statement of changes in equity and the preliminary statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying preliminary financial statements for the year ended December 31, 2020 have been prepared, in all material respects, in accordance with the basis set out in the "Basis of preparation" paragraph of Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Preliminary Financial Statements section of our report. We are independent of the Company 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.

Emphasis of Matter

Basis of preparation

We draw attention to Note 2 to the preliminary financial statements which explain why there is a possibility that the preliminary financial statements may require adjustment before constituting a complete set of IFRS financial statements. Moreover, we draw attention to the fact that, under IFRS only a complete set of financial statements with comparative financial information and explanatory notes can provide a fair presentation of the Company's financial position, results of operations and cash flows in accordance with IFRS. Our opinion is not qualified in respect of this matter.

Comparative information

We also draw attention to Note 6 to the preliminary financial statements which indicate that the comparative information presented as at January 1, 2020 has been restated. Our opinion is not qualified in respect of this matter.

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

Management is responsible for the preparation and fair presentation of the preliminary financial statements in accordance with the basis set out in the “Basis of preparation” paragraph of Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021, and for such internal control as management determines is necessary to enable the preparation of preliminary financial statements that is free from material misstatement, whether due to fraud or error.

In preparing the preliminary financial statements, management is responsible for assessing the Company’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 Company or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

Auditors’ Responsibilities for the Audit of the Preliminary Financial Statements

Our objectives are to obtain reasonable assurance about whether the preliminary financial statements as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditors’ report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these preliminary 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 preliminary 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 Company’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 Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the preliminary financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern;
- Evaluate the overall presentation, structure and content of the preliminary financial statements, including the disclosures, and whether the preliminary financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

Baker Tilly Azerbaijan

September 27, 2021

Baku, the Republic of Azerbaijan

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF FINANCIAL POSITION

AS AT DECEMBER 31, 2020

(In Azerbaijani Manats)

	Notes	December 31, 2020	January 1, 2020 (restated)
ASSETS			
Non-current assets:			
Property, plant and equipment	9	102,023,938	87,917,397
Prepayment for property, plant and equipment	10	163,064	943,017
Deferred tax assets	11	1,439,648	1,301,655
Loan receivables	12	-	2,970,204
Total non-current assets		103,626,650	93,132,273
Current assets:			
Inventories	13	87,133,812	67,599,819
Trade and other receivables	14	2,852,756	1,319,661
Loan receivables	12	3,200,204	-
Cash and cash equivalents	15	1,330,698	9,147
Other current assets	16	1,636,926	1,190,467
Total current assets		96,154,396	70,119,094
TOTAL ASSETS		199,781,046	163,251,367
LIABILITIES AND EQUITY			
LIABILITIES:			
Non-current liabilities:			
Deferred income	17	5,456,638	4,990,298
Lease liability	18	15,250,592	2,510,382
Total non-current liabilities		20,707,230	7,500,680
Current liabilities:			
Deferred income	17	318,549	277,239
Lease liability	18	686,566	779,563
Amount due to shareholder	19	10,800,000	13,000,000
Borrowings	20	19,890,000	-
Trade and other payables	21	15,193,449	10,146,288
Total current liabilities		46,888,564	24,203,090
Total liabilities		67,595,794	31,703,770
EQUITY:			
Charter capital	22	132,475,688	29,000,100
Other capital	23	-	103,882,158
Accumulated losses		(290,436)	(1,334,661)
Total equity		132,185,252	131,547,597
TOTAL LIABILITIES AND EQUITY		199,781,046	163,251,367

On behalf of the Management Board:

Bahrur Jamalov
Director

September 27, 2021

Baku, the Republic of Azerbaijan

Orkhan Khalafov
Deputy Finance Manager

September 27, 2021

Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 44 are an integral part of these preliminary financial statements.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF COMPREHENSIVE INCOME FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

	Notes	Year ended December 31, 2020
Revenue	24	78,088,567
Cost of sales	25	<u>(71,869,331)</u>
Gross profit		<u>6,219,236</u>
General and administrative expenses	26	<u>(4,105,734)</u>
Operating profit		<u>2,113,502</u>
Other income	27	488,971
Finance costs	28	<u>(1,297,192)</u>
Profit before income tax		<u>1,305,281</u>
Income tax expense	11	<u>(261,056)</u>
Net profit for the year		<u>1,044,225</u>
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		<u><u>1,044,225</u></u>

On behalf of the Management Board:


Bahruz Jamalov
Director

September 27, 2021
Baku, the Republic of Azerbaijan


Orkhan Khalafov
Deputy Finance Manager

September 27, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 44 are an integral part of these preliminary financial statements.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

**PRELIMINARY STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2020
(In Azerbaijani Manats)**

	Charter capital	Other capital	Accumulated losses	Total equity
January 1, 2020 (restated)	29,000,100	103,882,158	(1,334,661)	131,547,597
Transfer (state registration of charter capital)	103,475,588	(103,475,588)	-	-
Decrease in other capital	-	(406,570)	-	(406,570)
Total comprehensive income for the year	-	-	1,044,225	1,044,225
December 31, 2020	132,475,688	-	(290,436)	132,185,252

On behalf of the Management Board:


Bahruz Jamalov
 Director
 September 27, 2021
 Baku, the Republic of Azerbaijan


Orkhan Khalafov
 Deputy Finance Manager
 September 27, 2021
 Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 44 are an integral part of these preliminary financial statements.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY


PRELIMINARY STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

	Notes	Year ended December 31, 2020
CASH FLOWS FROM OPERATING ACTIVITIES:		
Profit before income tax		1,305,281
Adjustments to reconcile profit before income tax to net cash flows:		
Depreciation expenses	9	3,306,955
Subsidy income related to the acquisition of assets	27	(318,549)
Finance costs	28	1,297,192
Operating cash flows before working capital changes		5,590,879
Changes in operating assets and liabilities:		
Change in inventories		(19,533,993)
Change in trade and other receivables		(1,533,095)
Change in other current assets		(446,460)
Change in trade and other payables		6,479,561
Cash outflow from operations		(9,443,108)
Income tax paid		(1,739,339)
Net cash generated by operating activities		(11,182,447)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant and equipment		(3,504,962)
Loan to related parties		(230,000)
Net cash used in investing activities		(3,734,962)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings	20	19,890,000
Interest paid on borrowings	20	(540,526)
Lease payments	18	(910,514)
Repayment of amount due to shareholder	19	(2,200,000)
Net cash from financing activities		16,238,960
NET INCREASE IN CASH AND CASH EQUIVALENTS		1,321,551
CASH AND CASH EQUIVALENTS, <i>at the beginning of the year</i>	15	9,147
CASH AND CASH EQUIVALENTS, <i>at the end of the year</i>	15	1,330,698

Non-cash transactions

Investing and financing transactions that did not require the use of cash and cash equivalents and were excluded from the cash flow statement during the year ended December 31, 2020 included additions to assets purchased on lease and as subsidies received from the Government in the amount of AZN 12,801,061 and transfer of equipment to related companies in the amount of AZN 406,570 through reduction of other capital. The future cash outflows relating to leases that have not yet commenced are disclosed in Note 17.

On behalf of the Management Board:


Bahruz Jamalov
Director

September 27, 2021
Baku, the Republic of Azerbaijan


Orkhan Khalafov
Deputy Finance Manager

September 27, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 44 are an integral part of these preliminary financial statements.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

1. INTRODUCTION

“Azercotton Agro-Industrial Complex” Limited Liability Company (the “Company”) was established in 2018 and registered by the Ministry of Economy of the Republic of Azerbaijan on May 25, 2018 with tax identification number 1305532271 as a limited liability company.

The structure of shareholding of the Company as at December 31, 2020 and January 1, 2020 was as followings:

	December 31, 2020 Ownership interest, %	January 1, 2020 Ownership interest, %
“Azerbaijan Industrial Corporation” Open Joint-Stock Company	100.00	100.00
Total	100.00	100.00

The ultimate controlling party of the Company is the “Azerbaijan Industrial Corporation” Open Joint-Stock Company.

Principal activities

The Company specializes in the collection and processing of raw cotton. Revenue is mainly generated by the sale of cotton fiber, cotton seeds, linter, chemical substances and refined oil. Cotton is bought from farmers who harvest from cotton plantations in their own land areas. Cotton plantations are concentrated in the Aran economic region of the country, as the climate is highly favorable for cotton growing. The company’s main trade partners are Russia, Turkey, Iran, the Netherlands, the United Kingdom and etc.

Registered address and place of business:

The Company is domiciled in the Republic of Azerbaijan. The Company’s registered legal address is Yasamal region, Tbilisi Avenue, Apartment 35, Baku, the Republic of Azerbaijan. The principal place of business of the Company is the Aran economic region, the Republic of Azerbaijan.

Operating Environment of the Company

In March 2020, the World Health Organization (WHO) announced that the spread of the COVID-19 virus across the globe was a pandemic. Significant restrictions on travel and movement of individuals and the closure of non-essential businesses have either been imposed in most countries or have happened as a result of the pandemic. This has led to significant declines in GDP in most if not all large economically strong countries with which the Republic of Azerbaijan is in a trade relationship. The global economy was negatively impacted by the coronavirus pandemic (COVID-19) spread in the first half of 2020. Starting from June 2020 many countries including the Republic of Azerbaijan demonstrated improvement in the signs of the pandemic and certain restrictions were lifted subsequently. As a result, a recovery in global financial and commodity markets was observed. However, subsequently, the number of reported cases significantly increased in the Republic of Azerbaijan, and the government introduced new restrictions from mid-December 2020.

The restrictive lock-down measures to combat COVID-19 in the country significantly reduced economic activity and aggregate spending levels. Certain segments of the economy, such as hotels, transport, travel, entertainment and many other businesses also international trade much affected by these measures.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Oil prices have decreased significantly due to the substantial reduction in oil consumption in the pandemic environment but demonstrated stable growth during the second quarter of 2020. The government introduced support packages in the form of subsidized lending tools, payments to unemployed individuals and other subsidies to entrepreneurs during the year to compensate for the economic slowdown caused by the pandemic.

The Company's operations are conducted in the Republic of Azerbaijan. Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks. The future stability of Azerbaijan's economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Government as well as crude oil prices and the stability of Azerbaijani Manat. Although the economy of the Republic of Azerbaijan is particularly sensitive to oil and gas prices, in recent years, the Government of the Republic of Azerbaijan initiated major economic and social reforms to accelerate the transition to a more balanced economy and reduce its dependence on the oil and gas sector. GDP in Azerbaijan was USD 42.6 billion during the year 2020, according to the State Statistical Committee of the Republic of Azerbaijan. In the long-term, GDP in Azerbaijan is projected to trend around USD 50 billion in 2021 and USD 51 billion in 2022, according to our econometric models.

The government continued its monetary policy with respect to the stability of Azerbaijani Manat as well as allocated foreign currency resources which stabilized Azerbaijani Manat. This policy continued in 2020 with the aim of maintaining macroeconomic stability. The Central Bank of the Republic of Azerbaijan has changed the refinancing rate several times during the year and the range was between 7.25% - 6.25% with a steady decrease in rates.

The Company's management is monitoring changes in the macroeconomic environment and taking precautionary measures it considers necessary in order to support the sustainability and development of the Company's business in the foreseeable future.

International credit rating agencies regularly evaluate the credit rating of the Republic of Azerbaijan. "Fitch" and "S&P" evaluated the rating of the Republic of Azerbaijan as "BB+". "Moody's Investors Service" set a "Ba2" credit rating for the country.

In September 2020, the escalation of unresolved conflict in the Karabakh region (located in the southwest, which is internationally recognized as part of the Republic of Azerbaijan) resulted in clashes between the Republic of Azerbaijan and Armenian forces in occupied territories. In response, both countries introduced a curfew and military mobilization. Although the military actions mainly occurred in the western part of the Republic of Azerbaijan, some businesses were affected by the curfew which covered all the territories of the Republic of Azerbaijan including the capital Baku, to a certain degree. A complete ceasefire and a cessation of all hostilities in the zone of the Karabakh conflict were achieved on November 10, 2020. The level of macroeconomic effects in which the state involvement in liberated regions is uncertain as of reporting date.

These events and conditions described above created a level of uncertainty and risk that companies have not encountered before. The above-mentioned events had a significant effect on the financial results of the Company during the year ended December 31, 2020 and in the subsequent period.

The future economic growth of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory and political developments. The Management is unable to predict, all developments in the economic environment which would have an impact on the Company's operations and consequently what effect, if any, they could have on the financial position of the Company. The management is currently performing sensitivity analyses under different scenarios and elaborating relevant action plans for maintaining the sustainability of the business.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

The financial year of the Company ends on the last day of December. In previous years, the accounts have been prepared under the Generally Accepted Accounting Principles of the Republic of Azerbaijan (“AZ GAAP”). Effective from January 1, 2020 the Company produces its financial statements in accordance with International Financial Reporting Standards (“IFRS”).

The preliminary financial statements have been prepared on the basis of IFRS issued as at the date of this report and expected to be applicable by December 31, 2021. IFRS are subject to ongoing review or possible amendment by interpretative guidance from the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) and are therefore still subject to change. The preliminary financial statements will be updated and restated as necessary for any such changes should they occur.

Basis of preparation

First-time adoption of IFRS

The rules for first-time adoption of IFRS are set out in IFRS 1 “First-Time Adoption of International Financial Reporting Standards”. IFRS 1 requires an entity to comply with each IFRS effective at the reporting date for its first full set of IFRS financial statements. As a general principle IFRS 1 requires the standards effective at the reporting date to be applied retrospectively.

However, a retrospective application is prohibited in some areas, particularly where the retrospective application would require judgements by management after the outcome of the particular transaction is already known. In addition, a number of limited optional exemptions from full retrospective application of IFRS are granted where the cost of compliance is deemed to exceed the benefits to users of the financial statements. The exemptions are divided into:

- Mandatory exemptions;
- Optional exemptions.

The Company applied all mandatory exemptions. The optional exemptions are chosen by the management include:

- Fair value or revaluation as deemed cost – The Company elected to use the fair value amount as deemed cost for property, plant and equipment at the date of transfer of these assets to the Company by the shareholder.

Going concern

These preliminary financial statements have been prepared on the assumption that the Company is a going concern and will continue in operation for the foreseeable future.

Management views the Company as continuing in business for the foreseeable future with neither the intention nor the necessity of liquidation, ceasing trading or seeking protection from creditors pursuant to laws or regulations of the Republic of Azerbaijan.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Accordingly, assets and liabilities are recorded on the basis that the Company will be able to realize its assets and discharge its liabilities in the normal course of business. Some financial reporting frameworks contain an explicit requirement for management to make a specific assessment of the Company's ability to continue as a going concern, and standards regarding matters to be considered and disclosures to be made in connection with going concern.

Management's assessment of the going concern assumption involves making a judgment, at a particular point in time, about the future outcome of events or conditions which are inherently uncertain.

Current versus non-current classification

The Company presents assets and liabilities in the preliminary financial statements based on current/non-current classification. An asset is current when it is:

- Expected to be realized or intended to be sold or consumed in the normal operating cycle;
- Held primarily for the purpose of trading;
- Expected to be realized within twelve months after the reporting period; or
- Cash or cash equivalent unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current.

A liability is current when:

- It is expected to be settled in the normal operating cycle;
- It is held primarily for the purpose of trading;
- It is due to be settled within twelve months after the reporting period; or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Company classifies all other liabilities as non-current.

Deferred tax assets and liabilities are classified as non-current assets and liabilities.

Other basis of presentation criteria

These preliminary financial statements are presented in Azerbaijani Manats (“AZN”), unless otherwise indicated. The preliminary financial statements have been prepared under the historical cost convention.

The adoption of IFRS has resulted in changes to the Company's accounting policies. The amended accounting policies are:

Property, plant and equipment

Property, plant and equipment are stated in the preliminary statement of financial position at cost, less any subsequent accumulated depreciation and impairment losses.

The estimated useful life, residual values and amortization method will be reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

At the end of each reporting period, the Company reviews the carrying amounts of its property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit and loss accounts.

Property, plant and equipment are generally depreciated on a straight-line basis over their estimated useful lives as follows. The land is not depreciated.

Buildings and similar constructions	20-50 years
Machinery and equipment	7-20 years
Vehicles	5-7 years
Others	7-15 years
Right-of-use asset	depends on the lease term

The residual value of an asset is the estimated amount that an entity would currently obtain from the disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of age and in the condition expected at the end of its useful life.

The residual value of an asset may increase to an amount equal to or greater than the asset's carrying amount. If it does, the asset's depreciation charge is zero unless and until its residual value subsequently decreases to an amount below the asset's carrying amount.

Inventories

Inventories are measured at the lower of cost and net realizable value. The cost of inventories is based on the weighted average cost principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Financial instruments

Financial assets and financial liabilities are recognized in the Company's preliminary statement of financial position when the Company becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss.

Financial assets

All regular-way purchases or sales of financial assets are recognized and derecognized on a trade date basis. All recognized financial assets are measured subsequently in their entirety at either amortized cost or fair value, depending on the classification of the financial assets.

Classification of financial assets

Debt instruments that meet the following conditions are measured subsequently at amortized cost:

- the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Debt instruments that meet the following conditions are measured subsequently at fair value through other comprehensive income (FVTOCI):

- the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling the financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

By default, all other financial assets are measured subsequently at fair value through profit or loss (FVTPL).

Despite the foregoing, the Company may make the following irrevocable election/designation at initial recognition of a financial asset:

- the Company may irrevocably elect to present subsequent changes in fair value of an equity investment in other comprehensive income if certain criteria are met; and
- the Company may irrevocably designate a debt investment that meets the amortized cost or FVTOCI criteria as measured at FVTPL if doing so eliminates or significantly reduces an accounting mismatch.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Amortized cost and effective interest method

The effective interest method is a method of calculating the amortized cost of a debt instrument and of allocating interest income over the relevant period. For financial assets other than purchased or originated credit-impaired financial assets (i.e., assets that are credit-impaired on initial recognition), the effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) excluding expected credit losses, through the expected life of the debt instrument, or, where appropriate, a shorter period, to the gross carrying amount of the debt instrument on initial recognition.

For purchased or originated credit-impaired financial assets, a credit-adjusted effective interest rate is calculated by discounting the estimated future cash flows, including expected credit losses, to the amortized cost of the debt instrument on initial recognition.

The amortized cost of a financial asset is the amount at which the financial asset is measured at initial recognition minus the principal repayments, plus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount, adjusted for any loss allowance. The gross carrying amount of a financial asset is the amortized cost of a financial asset before adjusting for any loss allowance.

Interest income is recognized using the effective interest method for debt instruments measured subsequently at amortized cost and at FVTOCI. For financial assets other than purchased or originated credit-impaired financial assets, interest income is calculated by applying the effective interest rate to the gross carrying amount of a financial asset, except for financial assets that have subsequently become credit-impaired. For financial assets that have subsequently become credit-impaired, interest income is recognized by applying the effective interest rate to the amortized cost of the financial asset. If, in subsequent reporting periods, the credit risk on the credit-impaired financial instrument improves so that the financial asset is no longer credit-impaired, interest income is recognized by applying the effective interest rate to the gross carrying amount of the financial asset.

The Company's majority of financial assets were classified as financial assets measured subsequently at amortized cost. The Company's financial liabilities were classified as financial liabilities measured subsequently at amortized cost. The Company does not choose to classify any financial liabilities as measured at fair value through profit or loss.

Impairment of financial assets

The Company applies the expected credit loss model to financial assets measured at amortized cost or at fair value through other comprehensive income.

The allowance for expected credit losses for a financial asset is measured at an amount equal to the lifetime expected credit losses if the credit risk on that financial asset has increased significantly since initial recognition.

If, at the reporting date, the credit risk on a financial asset has not increased significantly since initial recognition, the allowance for expected credit losses for that financial asset (except trade and other receivables, where the simplified approach is elected) is measured at an amount equal to 12-month expected credit losses. For trade and other receivables, whether they contain a significant financing component or not, measurements based on lifetime expected credit losses are applied.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

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The Company utilizes an internal model to assess expected credit losses. The model was developed in accordance with IFRS 9 and designed to assess the credit risk exposure of counterparties taking into account the characteristics of financial assets by assigning a scoring system to counterparties. The assigned score is returning PD (Probability of Default) on an individual basis. Move of the asset from one score band to a lower score band is considered a significant increase in credit risk among other criteria.

Fair value measurement

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

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

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

The Company 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.

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

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

For assets and liabilities that are recognized in the financial statements on a recurring basis, the Company 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.

De-recognition of financial assets

The Company derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

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NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Financial liabilities and equity

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recognized at the proceeds received, net of direct issue costs.

Repurchase of the Company's own equity instruments is recognized and deducted directly in equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company's own equity instruments.

Financial liabilities

All financial liabilities are measured subsequently at amortized cost using the effective interest method or at FVTPL.

Financial liabilities are classified as at FVTPL when the financial liability is (i) contingent consideration of an acquirer in a business combination, (ii) held for trading or (iii) it is designated as at FVTPL.

Financial liabilities that are not (i) contingent consideration of an acquirer in a business combination, (ii) held-for-trading, or (iii) designated as at FVTPL, are measured subsequently at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or (where appropriate) a shorter period, to the amortized cost of financial liability.

De-recognition of financial liabilities

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

An exchange between an existing borrower and lender of debt instruments with substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

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The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10 percent different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognized as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortized over the remaining term of the modified liability.

Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the preliminary statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Trade and other receivables

Trade and other receivables are carried at amortized cost using the effective interest method. The Company uses a provision matrix to calculate expected credit losses for trade and other receivables and contract assets. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography, product type, customer type and rating, and coverage by letters of credit and other forms of credit insurance).

The provision matrix is initially based on the Company's historical observed default rates. The Company will calibrate the matrix to adjust the historical credit loss experience with forward-looking information. For instance, if forecast economic conditions (i.e., gross domestic product) are expected to deteriorate over the next year which can lead to an increased number of defaults in the manufacturing sector, the historical default rates are adjusted. At every reporting date, the historically observed default rates are updated and changes in the forward-looking estimates are analyzed. Where applicable, the Company relies on default rates derived from external rates of counterparties.

The assessment of the correlation between historically observed default rates, forecast economic conditions and expected credit losses is a significant estimate. The amount of expected credit losses is sensitive to changes in circumstances and forecast economic conditions. The Company's historical credit loss experience and forecast of economic conditions may also not be representative of the customer's actual default in the future.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, cash in transit, current accounts with banks and short-term placements with banks with an original maturity of three months or less.

Trade and other payables

Trade and other payables are accrued when the counterparty performs its obligations under the contract and are carried at amortized cost using the effective interest method.

Advances to suppliers

Advances to suppliers are carried at cost less provision for impairment. An advance is classified as non-current when the goods or services relating to the advance are expected to be obtained after one year, or when the advance relates to an asset which will itself be classified as non-current upon initial recognition.

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Advances to acquire assets are transferred to the carrying amount of the asset once the Company has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Company. Other advances are written off to profit and loss accounts when the goods or services relating to the advances are received. If there is an indication that the assets, goods or services relating to an advance will not be received, the carrying value of the advance is written down accordingly and a corresponding impairment loss is recognized in profit and loss accounts.

Taxation

Deferred taxes

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method.

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

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized. Deferred tax is charged or credited in the statement of comprehensive income, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred income tax assets and deferred income tax liabilities are offset and reported net on the preliminary statement of financial position if:

- The Company has a legally enforceable right to set off current income tax assets against current income tax liabilities; and
- Deferred income tax assets and the deferred income tax liability related to income taxes levied by the same taxation authority on the same taxable entity.

Value added tax

The difference between output VAT and claimable input VAT is payable to the state budget within 20 days following the reporting month. Output value added tax related to sales is payable to tax authorities upon receipt of payment in return for such sales. Input VAT is generally recoverable against output VAT upon receipt of the electronic invoice. The tax authorities permit the settlement of VAT on a net basis.

VAT related to sales and purchases is recognized in the preliminary financial statements on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, an impairment loss is recorded for the gross amount of the debtor, including VAT.

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(In Azerbaijani Manats)

VAT deposit account

The Value Added Tax (“VAT”) deposit account system was introduced in 2008 by the Ministry of Taxes of the Republic of Azerbaijan which aims prevention of VAT misuse. From January 1, 2008 on the basis of amendments to the Tax Code, the amount of VAT refund is considered the tax amount which is paid, according to the submitted VAT invoices to the taxpayer’s VAT deposit account in the framework of transactions carried out in this account.

By the support of this module the taxpayer pays the amount of VAT indicated on the VAT invoices to the VAT deposit account of another taxpayer. At the same time, tax obligations to the state budget regarding all kinds of taxes and VAT amounts on the import transactions which is necessary to be paid to the customs committee, can be paid by taxpayers through the VAT deposit account. Information about paid amounts is transferred by the tax authority to the Main State Treasury (“MST”) and then to the Central Bank of the Republic of Azerbaijan (“CBRA”). CBRA on the basis of information submitted by the Main State Treasury ensures the transformation of amounts to the relevant local treasury authorities. The tax authority ensures the inclusion of amounts which is noted in the submitted information in the taxpayer’s personal files.

The current system is connected with the Automated Tax Information System maintained by the State Tax Service under the Ministry of Economy of the Republic of Azerbaijan. At the same time online exchange of information was organized with the MST and CBRA.

Implementation of the VAT deposit account makes it possible to timely control payments and refunded VAT amounts. Taxpayers who have tax debts can only transfer these amounts to the state budget. Taxpayers can make payments to the state budget without visiting banks, to the VAT deposit account of other taxpayers and to the customs committee through the deposit account. The State Tax Service under the Ministry of Economy of the Republic of Azerbaijan automatically controls all transactions carried out through the deposit account using special software.

Use of balances in the VAT deposit account is restricted and can be used only for transactions connected with VAT and other applicable taxes.

Leases

A lease is a contract or part of a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration. Control is considered to exist if the customer has the right to obtain substantially all economic benefits from the use of an unidentified asset and the right to direct the use of that asset.

At lease commencement, the Company recognizes a right-of-use asset and lease liability for all leases except for short-term and low-valued items.

The right-of-use asset is initially measured at cost and measured subsequently at cost less accumulated depreciation and impairment losses.

The lease liability is initially measured at the present value of future lease payments. Subsequently, lease liabilities are adjusted for interest and lease payments.

The management of the Company utilized certain judgement in the determination of lease terms, based on past history.

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Charter capital

Charter capital is the amount of capital contributed by the shareholder of the Company. The Company may increase or decrease its charter capital within the approval of the shareholder.

Revenue from Contracts with Customers

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers.

The core principle of IFRS 15 is that the Company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognizes revenue when or as a performance obligation is satisfied, i.e., when ‘control’ of the goods or services underlying the particular performance obligation is transferred to the customer.

Revenue principally comprises sales of cotton products to external customers. Revenue excludes duty, excise and other taxes related to sales in the period and is stated after deducting rebates, returns and other similar discounts and payments to direct and indirect customers. Revenue is recognised when control of the goods is transferred to a customer; this is usually evidenced by a transfer of the significant risks and rewards of ownership upon delivery to the customer, which in terms of timing is not materially different from the date of shipping.

Employee benefits

Wages, salaries, contributions to the Republic of Azerbaijan state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Company.

Subsidy income

Subsidies received from the Government are recognized where there is reasonable assurance that the subsidy will be received and all attached conditions will be complied with. When the subsidy relates to an expense item, it is recognized as income on a systematic basis over the periods that the related costs, for which it is intended to compensate, are expensed. When the subsidy relates to an asset, it is recognized as income in equal amounts over the expected useful life of the related asset. When the Company receives subsidies for non-monetary assets, the asset and the subsidy are recorded at nominal amounts and released to profit or loss over the expected useful life of the asset, based on the pattern of consumption of the benefits of the underlying asset by equal annual installments.

Foreign currency translation

The functional currency of the Company is the currency of the primary economic environment, in which it operates. The Company’s functional and presentation currency is AZN.

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Monetary assets and liabilities denominated in foreign currencies are translated into AZN at the appropriate spot rates of exchange of the CBRA ruling at the end of the reporting date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transaction.

Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

The exchange rates at reporting date used by the Company in the preparation of the preliminary financial statements are as follows:

	December 31, 2020	January 1, 2020
1 USD	1.7000 AZN	1.7000 AZN
1 RUB	0.0231 AZN	0.0274 AZN

Contingent liabilities and assets

Contingent liabilities are not recognized in the preliminary financial statements. They are disclosed in the notes to the preliminary financial statements unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets are not recognized in the preliminary financial statements but are disclosed when an inflow of economic benefits is probable.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The preparation of the preliminary financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and disclosure of contingent liabilities during the reporting period.

As a result of the uncertainties inherent in business activities, many items in the preliminary financial statements cannot be measured with precision but can only be estimated. Estimation involves judgments based on the latest information available when the preliminary financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Company. Such changes are reflected in the assumptions when they occur.

The most significant estimates relate to the depreciable lives of property, plant and equipment, impairment of non-financial and financial assets, fair value of financial instruments, provision for obsolete inventory, provision for tax and legal contingencies and deferred taxation. Actual results could differ from these estimates.

Judgments

In the process of applying the Company's accounting policies, the management has made the following judgments, apart from those involving estimates, which have the most significant effect on the amounts recognized in the preliminary financial statements.

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Fair value of property, plant and equipment

Property, plant and equipment were measured at fair value as deemed costs at the date when these assets were transferred to the Company.

The fair value of property, plant and equipment was assessed using the market approach method which involves an analysis of market sales prices for a similar property, plant and equipment which was also equal to the fair value of property, plant and equipment under IFRS 13.

Useful life of property, plant and equipment

The Company assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 “Accounting Policies, Changes in Accounting Estimates and Errors”. These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and intangible assets and on depreciation and amortization recognized in profit and loss accounts.

Impairment of property, plant and equipment and other non-financial assets

The Company assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Company makes an estimate of the asset’s recoverable amount. An asset’s recoverable amount is the higher of an asset’s or cash-generating unit’s fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects a current market assessment of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If no such transactions can be identified, an appropriate valuation model is used.

The Company bases its impairment calculation on detailed budgets and forecast calculations which are prepared separately for each of the Company’s cash-generating units (CGU) to which the individual asset is allocated. These budgets and forecast calculations generally cover the period of 5 years. For longer periods, a long-term growth rate is determined and applied to project future cash flows after the fifth year. As at December 31, 2020 accumulated impairment loss on a property, plant and equipment amounted to nil.

Inventory valuation

Inventory is valued at the lower of cost or net realizable value. The Company records an allowance to reduce the carrying value of obsolete and slow-moving inventory to net realizable value, when appropriate. The actual value realized on the disposition of such inventory may differ from the net realizable value; any such difference could have a significant impact on future operating results.

Recoverability of VAT

At each reporting date, the Company assesses the recoverability of VAT arising on the purchase of goods and services. The Company can only receive these amounts through an offset against future VAT liability or collection from the tax authorities. In assessing the recoverability of the VAT receivable, the Company considers information from the internal tax department regarding projected VAT liability, correspondence with government tax authorities, and historical recovery experience.

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The actual amount of VAT recovery could differ materially from the Company’s estimate and this could materially impact operating results.

Fair value measurement of financial instruments

A number of the Company’s accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities.

The Company has an established control framework with respect to the measurement of fair values.

When measuring the fair value of an asset or a liability, the Company uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

- *Level 1:* quoted prices (unadjusted) in active markets for identical assets or liabilities;
- *Level 2:* inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices);
- *Level 3:* inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

Current taxes

Azerbaijani tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Company’s entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Company’s entities may be assessed additional taxes, penalties and interest, which can be significant.

Periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As at December 31, 2020, the management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Company’s tax, currency and customs positions will be sustained.

Deferred taxes

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

Lease term and estimating incremental borrowing rate

The Company determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised. The Company has several lease contracts that include extension and termination options. The Company applies judgement in evaluating whether it is reasonably certain whether or not to exercise the option to renew or terminate the lease. That is, it considers all relevant factors that create an economic incentive for it to exercise either the renewal or termination. After the commencement date, the Company reassesses the lease term if there is a significant event or change in circumstances that is within its control that affects its ability to exercise or not to exercise the option to renew or to terminate.

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Where the Company cannot readily determine the interest rate implicit in the lease, it uses its incremental borrowing rate ('IBR') to measure lease liabilities. The IBR is the rate of interest that the Company would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR, therefore, reflects what the Company 'would have to pay', which requires estimation when no observable rates are available or when they need to be adjusted to reflect the terms and conditions of the lease. The IBR utilized by the management as at December 31, 2020 was 7% (January 1, 2020: 9.25%).

Revenue recognition

Revenues from sales of goods are recognized at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped. If the Company agrees to transport goods to a specified location, revenue is recognized when the goods are passed to the customer at the destination point.

Sales of services are recognized in the accounting period in which the services are rendered, by reference to the stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Gross sales are shown net of VAT but including discounts. Discounts are provided on a discretionary basis depending on commercial terms.

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of goods received in a barter transaction cannot be measured reliably, the revenue is measured at the fair value of the goods or service given up.

4. ADOPTION OF NEW AND REVISED STANDARDS AND INTERPRETATIONS

In the current year, the Company has adopted all of the applicable new and revised Standards and Interpretations issued by the IASB and the IFRIC of the IASB that are relevant to its operations and effective for the year ending December 31, 2021.

On May 15, 2020 IASB has published **“COVID-19-Related Rent Concessions (Amendment to IFRS 16)”** amending the standard to provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification.

The changes in COVID-19-Related Rent Concessions (Amendment to IFRS 16) amend IFRS 16 to:

- provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification;
- require lessees that apply the exemption to account for COVID-19-related rent concessions as if they were not lease modifications;
- require lessees that apply the exemption to disclose that fact; and
- require lessees to apply the exemption retrospectively in accordance with IAS 8, but not require them to restate prior period figures.

The amendment is effective for annual reporting periods beginning on or after June 1, 2020. Earlier application is permitted. The impact of adoption of this standard had no effect on the financial statements.

Unless otherwise disclosed, the new adopted standards did not have material effect on the preliminary financial statements of the Company.

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5. STANDARDS AND INTERPRETATIONS ISSUED AND NOT YET ADOPTED

At the date of authorization of these preliminary financial statements, other than the Standards and Interpretations adopted by the Company in advance of their effective dates, the following Interpretations were in issue but not yet effective.

IFRS 17 “Insurance contracts” – was issued in May 2017 and replaced IFRS 4 “Insurance contracts”. The new standard establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the standard. An entity shall apply IFRS 17 “Insurance Contracts” to insurance contracts, including reinsurance contracts, it issues; reinsurance contracts it holds; and investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts.

IFRS 17 is effective for annual reporting periods beginning on or after January 1, 2023. Earlier application is permitted if both IFRS 15 ‘Revenue from Contracts with Customers’ and IFRS 9 ‘Financial Instruments’ have also been applied. This standard is not applicable to the Company.

Amendments to IAS 1 to clarify the classification of liabilities – In January 2020 the IASB issued “Classification of Liabilities as Current or Non-Current” (Amendments to IAS 1) providing a more general approach to the classification of liabilities under IAS 1 based on the contractual arrangements in place at the reporting date. The amendments in “Classification of Liabilities as Current or Non-Current” (Amendments to IAS 1) affect only the presentation of liabilities in the statement of financial position – not the amount or timing of recognition of any asset, liability income or expenses, or the information that entities disclose about those items.

The amendments are effective for annual reporting periods beginning on or after January 1, 2023 and are to be applied retrospectively. Earlier application is permitted. The Company is currently assessing the impact the amendments will have on the current practice and whether existing loan agreements may require renegotiation.

Reference to the Conceptual Framework – Amendments to IFRS 3. In May 2020, the IASB issued **Amendments to IFRS 3 “Business Combinations” – Reference to the Conceptual Framework.** The amendments are intended to replace a reference to the Framework for the Preparation and Presentation of Financial Statements, issued in 1989, with reference to the Conceptual Framework for Financial Reporting issued in March 2018 without significantly changing its requirements. The Board also added an exception to the recognition principle of IFRS 3 to avoid the issue of potential ‘day 2’ gains or losses arising for liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 “Levies”, if incurred separately. At the same time, the Board decided to clarify existing guidance in IFRS 3 for contingent assets that would not be affected by replacing the reference to the Framework for the Preparation and Presentation of Financial Statements. The amendments are effective for annual reporting periods beginning on or after January 1, 2022 and apply prospectively.

Property, Plant and Equipment: Proceeds before Intended Use – Amendments to IAS 16 In May 2020, the IASB issued **Property, Plant and Equipment – Proceeds before Intended Use**, which prohibits entities from deducting from the cost of an item of property, plant and equipment, any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognizes the proceeds from selling such items, and the costs of producing those items, in profit or loss. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 and must be applied retrospectively to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented when the entity first applies the amendment. The amendments are not expected to have a material impact on the Company.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Onerous Contracts – Costs of Fulfilling a Contract – Amendments to IAS 37. In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making. The amendments apply a “directly related cost approach”. The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract. The amendments are effective for annual reporting periods beginning on or after January 1, 2022.

IFRS 1 “First-time Adoption of International Financial Reporting Standards” – Subsidiary as a first-time adopter. As part of its 2018-2020 annual improvements to the IFRS standards process, the IASB issued an amendment to IFRS 1 “First-time Adoption of International Financial Reporting Standards”. The amendment permits a subsidiary that elects to apply paragraph D16(a) of IFRS 1 to measure cumulative translation differences using the amounts reported by the parent, based on the parent’s date of transition to IFRS. This amendment is also applied to an associate or joint venture that elects to apply paragraph D16 (a) of IFRS 1. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted.

IFRS 9 Financial Instruments – Fees in the “10 percent” test for de-recognition of financial liabilities. As part of its 2018-2020 annual improvements to the IFRS standards process the IASB issued an amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other’s behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted. The Company will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

“IAS 41 Agriculture” – Taxation in fair value measurements. As part of its 2018-2020 annual improvements to the IFRS standards process the IASB issued an amendment to IAS 41 Agriculture. The amendment removes the requirement in paragraph 22 of IAS 41 that entities exclude cash flows for taxation when measuring the fair value of assets within the scope of IAS 41. An entity applies the amendment prospectively to fair value measurements on or after the beginning of the first annual reporting period beginning on or after January 1, 2022 with earlier adoption permitted. The amendments are not expected to have a material impact on the Company.

IFRS 10 “Consolidated Financial Statements” and IAS 28 (amendments) “Sale or Contribution of Assets between an Investor and its Associate or Joint Venture” – The amendments to IFRS 10 and IAS 28 deal with situations where there is a sale or contribution of assets between an investor and its associate or joint venture. Specifically, the amendments state that gains or losses resulting from the loss of control of a subsidiary that does not contain a business in a transaction with an associate or a joint venture that is accounted for using the equity method, are recognized in the parent’s profit or loss only to the extent of the unrelated investors’ interests in that associate or joint venture.

Similarly, gains and losses resulting from the re-measurement of investments retained in any former subsidiary (that has become an associate or a joint venture that is accounted for using the equity method) to fair value are recognized in the former parent’s profit or loss only to the extent of the unrelated investors’ interests in the new associate or joint venture. The effective date of the amendments has yet to be set by the IASB; however, earlier application of the amendments is permitted.

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Unless otherwise disclosed, the newly pronounced standards are not expected to have a material effect on the preliminary financial statements of the Company.

6. RESTATEMENTS

During the year ended December 31, 2020, the Management identified certain errors in the financial statements of prior year. These errors were corrected retrospectively as described below.

	As previously reported January 1, 2020	Restatement amount January 1, 2020	As restated January 1, 2020
Deferred tax assets	71,623	1,230,032	1,301,655
Inventories	73,749,979	(6,150,160)	67,599,819
(Retained earnings)/accumulated losses	(3,585,466)	4,920,128	1,334,662

7. BALANCES AND TRANSACTIONS WITH RELATED PARTIES

Related parties are defined in IAS 24 “Related Party Disclosures”. Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. The Company’s immediate parent is “Azerbaijan Industrial Corporation” Open Joint-Stock Company, which is fully owned by the Government of the Republic of Azerbaijan.

The Company applied the exemption in paragraph 25 of IAS 24 “Related Party Disclosures” regarding the disclosure requirement for government-related entities.

A reporting entity is exempt from the disclosure requirements of Paragraph 18 of IAS 24 “Related Party Disclosures” in relation to related party transactions and outstanding balances, including commitments, with:

- (a) a government that has control or joint control of, or significant influence over, the reporting entity; and
- (b) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity.

The nature of transactions with government-related entities includes the purchase of electricity, gas, petrol and receiving other services.

Additionally, the Company granted loan (Note 11) to and obtained borrowing from related parties (Notes 18 and 19).

During the year ended December 31, 2020, the remuneration of key management personnel included salaries, discretionary bonuses and other short-term benefits totalling AZN 73,606.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

8. FIRST TIME ADOPTION OF IFRS

The Company first adopted IFRS in 2020, with the date of effective transition to IFRS as at January 1, 2020. The Company’s preliminary IFRS statement of financial position is reconciled with previously adopted GAAP of the Republic of Azerbaijan (the “previous GAAP”) frameworks as follows.

The effect of the transition to IFRS and correction of errors made to the preliminary IFRS statement of financial position as at January 1, 2020 is as follows:

Preliminary IFRS Statement of financial position	Notes	Previous GAAP (as presented)	Effect of transition to IFRS/ errors	IFRS (as adjusted)
		January 1, 2020	January 1, 2020	January 1, 2020
Property, plant and equipment	a, b, c	89,453,904	(1,536,507)	87,917,397
Prepayment for property, plant and equipment	d	-	943,017	943,017
Deferred tax (liability)/asset	e	(129,500)	1,431,155	1,301,655
Inventories	a	74,281,204	(6,681,385)	67,599,819
Trade and other receivables	d	1,785,438	(465,777)	1,319,661
Other current assets	d, f	1,898,593	(708,129)	1,190,464
Lease liability	b	-	(3,289,945)	(3,289,945)
Trade and other payables	b, f	(14,994,198)	4,847,910	(10,146,288)
Charter capital	g	(132,882,258)	103,882,158	(29,000,100)
Other capital	g	-	(103,882,158)	(103,882,158)
Retained earnings	b, c, e	(4,124,998)	5,459,661	1,334,661

Explanations for the correction of errors and effect of transition:

- The Company reclassified certain balances between property, plant and equipment and inventory in accordance with the recognition requirement of IAS 16;
- The Company recognized right-of-use asset and lease liability according to IFRS 16;
- The Company recognized impairment loss for property, plant and equipment;
- The Company reclassified certain balances between trade and other receivables, other current assets and prepayment for property, plant and equipment;
- The Company has adjusted for deferred tax asset to comply with IFRS;
- The Company netted off certain tax balances;
- The Company reclassified between charter capital and other capital for properties transferred by shareholder but not yet registered as charter capital.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Deferred taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

Temporary differences as at December 31, 2020 and January 1, 2020 relate mostly to different methods/timing of income and expense recognition as well as to temporary differences generated by taxation bases' differences for certain assets.

The tax legislation of the Republic of Azerbaijan, in particular, may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result, the Company may be assessed additional taxes, penalties and interest which could be material for these preliminary financial statements.

Temporary differences as at December 31, 2020 and January 1, 2020 comprise:

	December 31, 2020	January 1, 2020 (restated)	January 1, 2020
Deductible temporary differences:			
Property, plant and equipment	339,999	67,310	67,310
Inventories	6,150,160	6,150,160	-
Deferred income	85,842	-	-
Lease liability	1,047,471	290,805	290,805
Total deductible temporary differences	7,623,472	6,508,275	358,115
Taxable temporary differences			
Trade and other receivables	(425,231)	-	-
Total taxable temporary differences	(425,231)	-	-
Net deductible temporary differences	7,198,241	6,508,275	358,115
Net deferred tax asset at 20 %	1,439,648	1,301,655	71,623

	Year ended December 31, 2020
Profit before income tax	1,305,281
Theoretical tax charge at the statutory rate of 20%	(261,056)
Income tax expense	(261,056)

	Year ended December 31, 2020
Current income tax expense	(399,049)
Change in the deferred income tax asset	137,993
Income tax expense	(261,056)

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

9. PROPERTY, PLANT AND EQUIPMENT

	Buildings and similar constructions	Machinery and equipment	Vehicles	Others	Construction in progress	Total
Initial cost						
January 1, 2020	30,222,425	43,481,068	17,044,560	576,648	-	91,324,701
Additions	-	16,437,493	244,646	87,784	1,050,143	17,820,066
Disposals	-	-	(426,160)	-	-	(426,160)
December 31, 2020	30,222,425	59,918,561	16,863,046	664,432	1,050,143	108,718,607
Accumulated depreciation						
January 1, 2020	(714,361)	(1,903,974)	(769,929)	(19,040)	-	(3,407,304)
Charge for the year	(757,614)	(1,857,957)	(651,209)	(40,175)	-	(3,306,955)
Eliminated on disposal	-	-	19,590	-	-	19,590
December 31, 2020	(1,471,975)	(3,761,931)	(1,401,548)	(59,215)	-	(6,694,669)
Net book value						
December 31, 2020	28,750,450	56,156,630	15,461,498	605,217	1,050,143	102,023,938
January 1, 2020	29,508,064	41,577,094	16,274,631	557,608	-	87,917,397

As at December 31, 2020 and January 1, 2020, included in property, plant and equipment there were neither any assets with restrictions on title, nor any assets that were pledged as security for liabilities.

As at December 31, 2020, the carrying amount of the machinery and equipment category of property, plant and equipment includes AZN 15,269,225 for the right-of-use assets related to machinery and vehicles to be used in farming (January 1, 2020: AZN 2,969,835).

10. PREPAYMENT FOR PROPERTY, PLANT AND EQUIPMENT

As at December 31, 2020, prepayment for property, plant and equipment amounted to AZN 163,064 and consisted of prepayments made for machinery and vehicles to be used in farming in the future periods (January 1, 2020: AZN 943,017).

11. DEFERRED TAX ASSET

The Company measures and records its current income tax liability and its tax bases related to assets and liabilities in accordance with the statutory tax regulations of the Republic of Azerbaijan where the Company operates, which differ from IFRS.

The Company is subject to certain permanent tax differences due to non-tax deductibility of certain expenses and certain income being treated as non-taxable for tax purposes.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

**NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)**
(In Azerbaijani Manats)

	December 31, 2020	January 1, 2020 (restated)	January 1, 2020
Deferred income tax asset			
Beginning of the year	1,301,655	-	-
Change in the deferred income tax asset for the period credited to profit and loss accounts	137,993	1,301,655	71,623
End of the year	1,439,648	1,301,655	71,623

12. LOAN RECEIVABLES

As at December 31, 2020, loan receivables include interest-free AZN-dominated loans to related party companies in the amount of AZN 3,200,204 (January 1, 2020: AZN 2,970,204). Loans will be repaid in 2021.

The Management believes that the carrying amount of loan receivables is recoverable.

13. INVENTORIES

Inventories comprise:

	December 31, 2020	January 1, 2020 (restated)	January 1, 2020
Raw materials	44,735,710	35,399,816	38,868,147
Finished goods	35,653,171	27,372,313	30,054,142
Spare parts	3,868,622	1,977,305	1,977,305
Other materials and supplies	2,876,309	2,850,385	2,850,385
Total inventories	87,133,812	67,599,819	73,749,979

14. TRADE AND OTHER RECEIVABLES

	December 31, 2020	January 1, 2020
Trade receivables	702,510	112,173
Other receivables	2,150,246	1,207,488
Total trade and other receivables	2,852,756	1,319,661

As at December 31, 2020 and January 1, 2020 included in other receivables the amounts of AZN 1,722,959 and AZN 1,101,195, respectively, represent receivables from the Government of the Republic of Azerbaijan for goods provided and services rendered to the cotton farmers.

The Management believes that the carrying amount of trade and other receivables is recoverable.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

15. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise:

	December 31, 2020	January 1, 2020
Cash at banks in USD	988,271	-
Cash at banks in AZN	341,665	8,243
Cash at banks in RUB	762	904
Total cash and cash equivalents	1,330,698	9,147

16. OTHER CURRENT ASSETS

	December 31, 2020	January 1, 2020
Deferred expenses	808,448	384,306
Advance to suppliers	720,738	696,604
VAT recoverable	107,740	109,557
Total other current assets	1,636,926	1,190,467

VAT recoverable relates to purchases which have not been settled at the reporting date. VAT recoverable is reclaimable against VAT on sales upon payment for the purchases.

Deferred expenses include costs associated with the farming process for which the Company will generate income in the future periods.

Advance to suppliers includes prepayments made to suppliers for the purchase of goods and services.

17. DEFERRED INCOME

As at December 31, 2020, deferred income included unamortized part of subsidy received from the Government related to the acquisition of property, plant and equipment in the amount of AZN 5,775,187 (January 1, 2020: AZN 5,267,537).

18. LEASE LIABILITIES

	December 31, 2020	January 1, 2020
Lease liabilities (current)	686,566	779,563
Lease liabilities (non-current)	15,250,592	2,510,382
Total lease liabilities	15,937,158	3,289,945

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Future minimum lease payments at December 31, 2020 were as follows:

	Minimum lease payments due			
	Within one year	One to five years	Over five years	Total
Lease payments	961,092	16,115,816	2,842,511	19,919,419
Finance charges	(274,526)	(3,603,786)	(103,949)	(3,982,261)
Net present value as at December 31, 2020	686,566	12,512,030	2,738,562	15,937,158

Future minimum lease payments at January 1, 2020 were as follows:

	Minimum lease payments due			
	Within one year	One to five years	Over five years	Total
Lease payments	1,020,978	3,596,044	-	4,617,022
Finance charges	(241,415)	(1,085,662)	-	(1,327,077)
Net present value as at January 1, 2020	779,563	2,510,382	-	3,289,945

A reconciliation of the opening and closing amounts of lease liabilities with relevant cash and non-cash changes from financing activities is stated below:

	As at January 1, 2020	Addition	Cash flow	Reclassification	Non-cash changes	As at December 31, 2020
			Principal/ Interest paid		Interest expense	
Non-current portion	2,510,382	12,801,061	-	(60,851)	-	15,250,592
Current portion	779,563	-	(910,514)	60,851	756,666	686,566
	3,289,945	12,801,061	(910,514)	-	756,666	15,937,158

19. AMOUNT DUE TO SHAREHOLDER

As at December 31, 2020, the amount due to shareholder includes a short-term interest-free AZN-dominated loan from shareholder in the amount of AZN 10,800,000 (January 1, 2020: AZN 13,000,000). During the year ended December 31, 2020, the Company repaid AZN 2,200,000 out of total debt.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

20. BORROWINGS

Borrowings comprise:

	December 31, 2020	January 1, 2020
“International Bank of Azerbaijan” OJSC	11,390,000	-
“Kapital Bank” OJSC	8,500,000	-
Total borrowings	19,890,000	-

On December 30, 2019, the Company signed a credit line agreement with “Kapital Bank” OJSC in the amount of USD 5,000,000 bearing interest of 6% per annum. The loan matured in 2020 and the Company signed an addendum to the main agreement. According to the addendum, the maturity date is prolonged till December 2021 and the annual interest rate was reduced from 6% to 5%.

On December 27, 2019, the Company signed a credit line agreement with “International Bank of Azerbaijan” OJSC (the ultimate controlling party of the bank is the Government of the Republic of Azerbaijan) in the amount of USD 2,500,000 bearing interest of 6% per annum and maturing in 2020. On August 25, 2020, the Company signed the supplemental agreement in the amount of USD 5,000,000 bearing interest of 6% per annum and maturing in 2021.

A reconciliation of the opening and closing amounts of borrowings with relevant cash and non-cash changes from financing activities is stated below:

	Amount
January 1, 2020	-
Cash flows	
Proceeds from borrowings	19,890,000
Interest paid on borrowings	(540,526)
Non-cash changes	
Interest expense	540,526
December 31, 2020	19,890,000

21. TRADE AND OTHER PAYABLES

	December 31, 2020	January 1, 2020
Trade payables	1,799,028	3,666,940
Payable for property, plant and equipment	-	92,110
Total financial payables	1,799,028	3,759,050
Advance received	10,583,208	3,920,859
Tax payables	2,127,196	1,903,479
Employee related payables	684,017	562,900
Total trade and other payables	15,193,449	10,146,288

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NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

22. CHARTER CAPITAL

As at December 31, 2020, charter capital amounted to AZN 132,475,688 consisting of 10 shares with AZN 13,247,568.80 face value per share (January 1, 2020: AZN 29,000,100 and consists of 10 shares with AZN 2,900,010 face value per share). In 2020, the Company registered other capital amounting to AZN 103,475,588 as charter capital.

23. OTHER CAPITAL

As at December 31, 2020, the other capital was nil. As at January 1, 2020, other capital amounted to AZN 103,882,158 and consisted of the asset transferred to the Company by shareholder but not yet registered as charter capital. In 2020, the Company registered other capital amounting AZN 103,475,588 as charter capital. Also, during 2020 the other capital of the Company was decreased in the amount of AZN 406,570 through the withdrawal of properties by the decision of the shareholder.

24. REVENUE

Revenue comprises:

	Year ended December 31, 2020
Sales of cotton fiber	53,961,673
Sales of cotton seeds	9,880,575
Revenue from provision of services	6,272,571
Sales of chemical substances	6,238,258
Other revenues	1,735,490
Total revenue	78,088,567

25. COST OF SALES

Cost of sales comprises:

	Year ended December 31, 2020
Material expenses	65,488,442
Staff costs	8,513,144
Depreciation expenses	3,195,166
Utility expenses	1,244,438
Change in finished goods	(8,280,857)
Other costs	1,708,998
Total cost of sales	71,869,331

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NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

26. GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses comprise:

	Year ended December 31, 2020
Staff costs	1,708,419
Sales and marketing expenses	660,151
Bank charges	641,668
Rent expenses	279,285
Business trip expenses	150,773
Depreciation expenses	111,789
Fuel expenses	99,797
Communication expenses	99,471
Professional fees	97,036
Insurance expenses	92,580
Repair and maintenance expenses	47,753
Office supplies	32,538
Transportation expenses	23,150
Security expenses	17,640
Other expenses	43,684
	<hr/>
Total general and administrative expenses	4,105,734 <hr/> <hr/>

27. OTHER INCOME

Other income comprises:

	Year ended December 31, 2020
Subsidy income related to acquisition of assets	318,549
Other	170,422
	<hr/>
Total other income	488,971 <hr/> <hr/>

28. FINANCE COSTS

Finance costs comprise:

	Year ended December 31, 2020
Interest on borrowings	540,526
Interest on lease liability	756,666
	<hr/>
Total finance costs	1,297,192 <hr/> <hr/>

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

29. COMMITMENTS AND CONTINGENCIES

Legal proceedings

From time to time and in the normal course of business, claims against the Company were received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in these preliminary financial statements.

Taxation

Commercial legislation and tax legislation of the Republic of Azerbaijan, in particular, may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result, the Company may be assessed additional taxes, penalties and interest.

The Company believes that it has already made all tax payments, and therefore no allowance has been made in the preliminary financial statements. Tax years remain open to review by the tax authorities for three years.

30. FINANCIAL RISK MANAGEMENT

Management of risk is fundamental to the Company's business and is an essential element of its operations. The main risks inherent to the Company operations are those related to:

- Credit risk;
- Liquidity risk;
- Market risk.

The Company recognizes that it is essential to have efficient and effective risk management processes in place. To enable this, the Company has established a risk management department. The main purpose of this department is to protect the Company from risk and allow it to achieve its performance objectives. Through the risk management framework, the Company manages the following risks:

Credit risk

The Company is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

Maximum exposure

The Company's maximum exposure to credit risk varies significantly and is dependent on both individual risks and general market economy risks.

Geographical concentration

Assets, liabilities and credit-related commitments have been based on the country, in which the counterparty is located. Balances with counterparties located in the Republic of Azerbaijan actually outstanding to/from companies of these counterparties are allocated to the caption "The Republic of Azerbaijan". Cash on hand, precious metals and premises and equipment have been allocated based on the country, in which they are physically held.

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NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The geographical concentration of the Company's financial assets and liabilities as at December 31, 2020 is set out below:

	The Republic of Azerbaijan	OECD countries	Other non-OECD countries	December 31, 2020 Total
FINANCIAL ASSETS				
Loan receivables	3,200,204	-	-	3,200,204
Trade and other receivables	2,153,903	698,853	-	2,852,756
Cash and cash equivalents	1,330,698	-	-	1,330,698
TOTAL FINANCIAL ASSETS	6,684,805	698,853	-	7,383,658
FINANCIAL LIABILITIES				
Lease liabilities	15,937,158	-	-	15,937,158
Amount due to shareholder	10,800,000	-	-	10,800,000
Borrowings	19,890,000	-	-	19,890,000
Trade and other payables	750,382	917,948	130,698	1,799,028
TOTAL FINANCIAL LIABILITIES	47,377,540	917,948	130,698	48,426,186
NET POSITION	(40,692,735)	(219,095)	(130,698)	(41,042,528)

The geographical concentration of the Company's financial assets and liabilities as at January 1, 2020 is set out below:

	The Republic of Azerbaijan	OECD countries	Other non-OECD countries	January 1, 2020 Total
FINANCIAL ASSETS				
Loan receivables	2,970,204	-	-	2,970,204
Trade and other receivables	1,287,193	32,468	-	1,319,661
Cash and cash equivalents	9,147	-	-	9,147
TOTAL FINANCIAL ASSETS	4,266,544	32,468	-	4,299,012
FINANCIAL LIABILITIES				
Lease liabilities	3,289,945	-	-	3,289,945
Amount due to shareholder	13,000,000	-	-	13,000,000
Trade and other payables	2,183,540	1,504,360	71,150	3,759,050
TOTAL FINANCIAL LIABILITIES	18,473,485	1,504,360	71,150	20,048,995
NET POSITION	(14,206,941)	(1,471,892)	(71,150)	(15,749,983)

Liquidity risk

Liquidity risk is defined as the risk when the maturity of financial assets and liabilities does not match. Liquidity risk is managed by the Finance Department of the Company. The liquidity management of the Company requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring the balance sheet liquidity ratio.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The liquidity risk of the Company's financial assets and liabilities as at December 31, 2020 is set out below:

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	December 31, 2020 Total
FINANCIAL ASSETS						
Loan receivables	30,000	66,000	3,104,204	-	-	3,200,204
Trade and other receivables	1,129,797	-	1,722,959	-	-	2,852,756
Cash and cash equivalents	1,330,698	-	-	-	-	1,330,698
Total financial assets	2,490,495	66,000	4,827,163	-	-	7,383,658
FINANCIAL LIABILITIES						
Lease liabilities	118,849	214,240	353,477	12,512,030	2,738,562	15,937,158
Amount due to shareholder	10,800,000	-	-	-	-	10,800,000
Borrowings	11,390,000	-	8,500,000	-	-	19,890,000
Trade and other payables	1,799,028	-	-	-	-	1,799,028
Total financial liabilities	24,107,877	214,240	8,853,477	12,512,030	2,738,562	48,426,186
Liquidity gap	(21,617,382)	(148,240)	(4,026,314)	(12,512,030)	(2,738,562)	(41,042,528)
Cumulative liquidity gap	(21,617,382)	(21,765,622)	(25,791,936)	(38,303,966)	(41,042,528)	

The liquidity risk of the Company's financial assets and liabilities as at January 1, 2020 is set out below:

	Up to 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	January 1, 2020 Total
FINANCIAL ASSETS						
Loan receivables	-	-	-	2,970,204	-	2,970,204
Trade and other receivables	112,173	-	1,207,488	-	-	1,319,661
Cash and cash equivalents	9,147	-	-	-	-	9,147
Total financial assets	121,320	-	1,207,488	2,970,204	-	4,299,012
FINANCIAL LIABILITIES						
Lease liabilities	64,964	129,927	584,672	2,510,382	-	3,289,945
Amount due to shareholder	13,000,000	-	-	-	-	13,000,000
Trade and other payables	3,468,270	290,780	-	-	-	3,759,050
Total financial liabilities	16,533,234	420,707	584,672	2,510,382	-	20,048,995
Liquidity gap	(16,411,914)	(420,707)	622,816	459,822	-	(15,749,983)
Cumulative liquidity gap	(16,411,914)	(16,832,621)	(16,209,805)	(15,749,983)	(15,749,983)	

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

Further analysis of the liquidity and interest rate risks is presented in the following tables in accordance with IFRS 7. The amounts disclosed in these tables do not correspond to the amounts recorded in the preliminary statement of financial position as the presentation below includes a maturity analysis for financial liabilities that indicates the total remaining contractual payments (including interest payments), which are not recognized in the preliminary statement of financial position under the effective interest rate method.

The liquidity risk of the Company's financial assets and liabilities in accordance with IFRS 7 as at December 31, 2020 are set out below:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	December 31, 2020 Total
Financial liabilities						
Borrowings	11,432,500	85,000	8,882,500	-	-	20,400,000
Lease liabilities	123,897	284,265	552,930	16,115,816	2,842,511	19,919,419
Total potential future payments for financial liabilities	11,556,397	369,265	9,435,430	16,115,816	2,842,511	40,319,419

The liquidity risk of the Company's financial assets and liabilities in accordance with IFRS 7 as at January 1, 2020 is set out below:

	Demand and less than 1 month	From 1 to 3 months	From 3 to 12 months	From 12 months to 5 years	Over 5 years	December 31, 2020 Total
Financial liabilities						
Lease liabilities	85,081	170,163	765,734	3,596,044	-	4,617,022
Total potential future payments for financial liabilities	85,081	170,163	765,734	3,596,044	-	4,617,022

Currency risk

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

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) (In Azerbaijani Manats)

The currency risk of the Company's financial assets and liabilities as at December 31, 2020 is set out below:

	AZN	USD	RUB	December 31, 2020 Total
FINANCIAL ASSETS				
Loan receivables	3,200,204	-	-	3,200,204
Trade and other receivables	2,153,903	698,853	-	2,852,756
Cash and cash equivalents	341,665	988,271	762	1,330,698
TOTAL FINANCIAL ASSETS	5,695,772	1,687,124	762	7,383,658
FINANCIAL LIABILITIES				
Lease liabilities	15,937,158	-	-	15,937,158
Amount due to shareholder	10,800,000	-	-	10,800,000
Borrowings	-	19,890,000	-	19,890,000
Trade and other payables	750,382	1,048,646	-	1,799,028
TOTAL FINANCIAL LIABILITIES	27,487,540	20,938,646	-	48,426,186
OPEN CURRENCY POSITION	(21,791,768)	(19,251,522)	762	(41,042,528)

The currency risk of the Company's financial assets and liabilities as at January 1, 2020 is set out below:

	AZN	USD	RUB	January 1, 2020 Total
FINANCIAL ASSETS				
Loan receivables	2,970,204	-	-	2,970,204
Trade and other receivables	1,287,192	32,469	-	1,319,661
Cash and cash equivalents	8,243	-	904	9,147
TOTAL FINANCIAL ASSETS	4,265,639	32,469	904	4,299,012
FINANCIAL LIABILITIES				
Lease liabilities	3,289,945	-	-	3,289,945
Amount due to shareholder	13,000,000	-	-	13,000,000
Trade and other payables	2,183,540	1,575,510	-	3,759,050
TOTAL FINANCIAL LIABILITIES	18,473,485	1,575,510	-	20,048,995
OPEN CURRENCY POSITION	(14,207,846)	(1,543,041)	904	(15,749,983)

31. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

The estimated fair values of financial instruments have been determined by the Company using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Republic of Azerbaijan continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

The fair value of financial assets and liabilities recognized at cost or amortized cost in the preliminary financial statements as at December 31, 2020 is presented below:

	December 31, 2020	
	Carrying value	Fair value
Loan receivables	3,200,204	3,200,204
Trade and other receivables	2,852,756	2,852,756
Cash and cash equivalents	1,330,698	1,330,698
Lease liabilities	15,937,158	15,937,158
Amount due to shareholder	10,800,000	10,800,000
Borrowings	19,890,000	19,890,000
Trade and other payables	1,799,028	1,799,028

The fair value of financial assets and liabilities recognized at cost or amortized cost in the preliminary financial statements as at January 1, 2020 is presented below:

	January 1, 2020	
	Carrying value	Fair value
Loan receivables	2,970,204	2,970,204
Trade and other receivables	1,319,661	1,319,661
Cash and cash equivalents	9,147	9,147
Lease liabilities	3,289,945	3,289,945
Amount due to shareholder	13,000,000	13,000,000
Trade and other payables	3,759,050	3,759,050

“AZERCOTTON AGRO-INDUSTRIAL COMPLEX” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued)

(In Azerbaijani Manats)

The following table sets out the fair values of financial instruments not measured at fair value and analyzes them by the level in the fair value hierarchy into which each fair value measurement as at December 31, 2020 is categorized below:

			Fair value measurement using			
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed						
Loan receivables	Amortized cost	December 31, 2020	-	-	3,200,204	3,200,204
Trade and other receivables	Amortized cost	December 31, 2020	-	-	2,852,756	2,852,756
Cash and cash equivalents	Amortized cost	December 31, 2020	1,330,698	-	-	1,330,698
Liabilities for which fair values are disclosed						
Lease liability	Amortized cost	December 31, 2020	-	-	15,937,158	15,937,158
Amount due to shareholder	Amortized cost	December 31, 2020	-	-	10,800,000	10,800,000
Borrowings	Amortized cost	December 31, 2020	-	-	19,890,000	19,890,000
Trade and other payables	Amortized cost	December 31, 2020	-	-	1,799,028	1,799,028

The following table sets out the fair values of financial instruments not measured at fair value and analyzes them by the level in the fair value hierarchy into which each fair value measurement as at January 1, 2020 is categorized below:

			Fair value measurement using			
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed						
Loan receivables	Amortized cost	January 1, 2020	-	-	2,970,204	2,970,204
Trade and other receivables	Amortized cost	January 1, 2020	-	-	1,319,661	1,319,661
Cash and cash equivalents	Amortized cost	January 1, 2020	9,147	-	-	9,147
Liabilities for which fair values are disclosed						
Lease liability	Amortized cost	January 1, 2020	-	-	3,289,945	3,289,945
Amount due to shareholder	Amortized cost	January 1, 2020	-	-	13,000,000	13,000,000
Trade and other payables	Amortized cost	January 1, 2020	-	-	3,759,050	3,759,050

**“AZERSILK” LIMITED LIABILITY
COMPANY**

**The International Financial Reporting Standards
Preliminary Financial Statements
and Independent Auditors' Report**
For the Year Ended December 31, 2020

“AZERSILK” LIMITED LIABILITY COMPANY

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020

The following statement is made with a view to distinguishing respective responsibilities of the management and those of the independent auditors in relation to the International Financial Reporting Standards ("IFRS") preliminary financial statements of "AzerSilk" Limited Liability Company (the "Company").

Management is responsible for the preparation of the preliminary financial statements that present fairly the financial position of the Company as at December 31, 2020, the results of its operations, changes in equity and cash flows for the year then ended, in accordance with the basis set out in the "Basis of preparation" paragraph of the Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021.

In preparing the preliminary financial statements, management is responsible for:

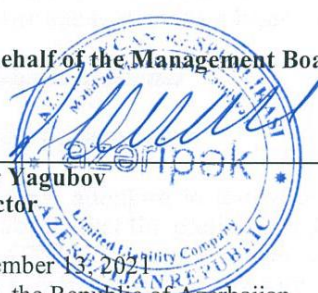
- Selecting suitable accounting principles and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether accounting policies have been followed, subject to any material departures disclosed and explained in the preliminary financial statements; and
- Preparing the preliminary financial statements on a going concern basis, unless it is inappropriate to presume that the Company will continue in business for the foreseeable future.

Management is also responsible for:


- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Company;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Company, and which enable them to ensure that the preliminary financial statements of the Company comply with IFRSs;
- Maintaining statutory accounting records in compliance with legislation and accounting standards of the Republic of Azerbaijan;
- Taking such steps as are reasonably available to them to safeguard the assets of the Company; and
- Detecting and preventing fraud, errors and other irregularities.

The preliminary financial statements for the year ended December 31, 2020 was authorized for issue on September 13, 2021 by the management of the Company.

On behalf of the Management Board:


Zaur Yagubov
Director

September 13, 2021
Baku, the Republic of Azerbaijan


Muzaffar Umarov
Chief Accountant

September 13, 2021
Baku, the Republic of Azerbaijan

INDEPENDENT AUDITORS' REPORT

To the Shareholder and Management of "AzerSilk" Limited Liability Company:

Opinion

We have audited the preliminary financial statements of "AzerSilk" Limited Liability Company (the "Company") for the year ended December 31, 2020, which comprises the preliminary statement of financial position as at December 31, 2020, and the preliminary statement of comprehensive income, preliminary statement of changes in equity and preliminary statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying preliminary financial statements for the year ended December 31, 2020 have been prepared, in all material respects, in accordance with the basis set out in the "Basis of preparation" paragraph of the Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Preliminary Financial Statements section of our report. We are independent of the Company 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.

Emphasis of Matter

Basis of preparation

We draw attention to the Note 2 to the preliminary financial statements which explains why there is a possibility that the preliminary financial statements may require adjustment before constituting a complete set of IFRS financial statements. Moreover, we draw attention to the fact that, under IFRS only a complete set of financial statements with comparative financial information and explanatory notes can provide a fair presentation of the Company's financial position, results of operations and cash flows in accordance with IFRSs. Our opinion is not qualified in respect of this matter.

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

Management is responsible for the preparation and fair presentation of the preliminary financial statements in accordance with the basis set out in the “Basis of preparation” paragraph of the Note 2 to the preliminary financial statements, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at December 31, 2021, and for such internal control as management determines is necessary to enable the preparation of preliminary financial statements that is free from material misstatement, whether due to fraud or error.

In preparing the preliminary financial statements, management is responsible for assessing the Company’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 Company or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company’s financial reporting process.

Auditors’ Responsibilities for the Audit of the Preliminary Financial Statements

Our objectives are to obtain reasonable assurance about whether the preliminary financial statements as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditors’ report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this preliminary 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 preliminary 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 Company’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 Company’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors’ report to the related disclosures in the preliminary financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors’ report. However, future events or conditions may cause the Company to cease to continue as a going concern;
- Evaluate the overall presentation, structure and content of the preliminary financial statements, including the disclosures, and whether the preliminary financial statements represent the underlying transactions and events in a manner that achieves fair presentation.



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

Baker Tilly Azerbaijan

September 13, 2021
Baku, the Republic of Azerbaijan

“AZERSILK” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF FINANCIAL POSITION

AS AT DECEMBER 31, 2020

(In Azerbaijani Manats)

	Notes	December 31, 2020	January 1, 2020
ASSETS			
Non-current assets:			
Property, plant and equipment	8	3,132,668	3,325,223
Total non-current assets		3,132,668	3,325,223
Current assets:			
Inventories	9	7,531,557	6,099,462
Trade receivables	10	-	72,687
Cash and cash equivalents	11	606,727	27,647
Other current assets	12	6,125	9,833
Total current assets		8,144,409	6,209,629
TOTAL ASSETS		11,277,077	9,534,852
LIABILITIES AND EQUITY			
LIABILITIES:			
Current liabilities:			
Trade and other payables	13	312,245	316,861
Amount due to shareholder	14	3,438,447	1,955,947
Total current liabilities		3,750,692	2,272,808
Total liabilities		3,750,692	2,272,808
EQUITY:			
Charter capital	15	8,119,579	5,161,696
Other capital	16	-	2,425,235
Accumulated loss		(593,194)	(324,887)
Total equity		7,526,385	7,262,044
TOTAL LIABILITIES AND EQUITY		11,277,077	9,534,852

On behalf of the Management Board:

Zaur Yagubov
Director

September 13, 2021
Baku, the Republic of Azerbaijan

Muzaffar Umarov
Chief Accountant

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 34 are an integral part of these preliminary financial statements.


“AZERSILK” LIMITED LIABILITY COMPANY

**PRELIMINARY STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED DECEMBER 31, 2020**

(In Azerbaijani Manats)

	Notes	Year ended December 31, 2020
Revenue	17	2,327,313
Cost of sales	18	(2,122,336)
Gross profit:		204,977
General and administrative expenses	19	(647,164)
Other income	20	173,880
Loss before income tax		(268,307)
Net loss for the year		(268,307)
TOTAL COMPREHENSIVE LOSS FOR THE YEAR		(268,307)

On behalf of the Management Board:


Zaur Yagubov
Director

September 13, 2021
Baku, the Republic of Azerbaijan


Muzaffar Umarov
Chief Accountant

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 34 are an integral part of these preliminary financial statements.

“AZERSILK” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED DECEMBER 31, 2020

(In Azerbaijani Manats)

	Charter capital	Other capital	Accumulated loss	Total equity
January 1, 2020	<u>5,161,696</u>	<u>2,425,235</u>	<u>(324,887)</u>	<u>7,262,044</u>
Contribution by shareholder	-	532,648	-	532,648
Transfer	2,957,883	(2,957,883)	-	-
Total comprehensive loss for the year	<u>-</u>	<u>-</u>	<u>(268,307)</u>	<u>(268,307)</u>
December 31, 2020	<u><u>8,119,579</u></u>	<u><u>-</u></u>	<u><u>(593,194)</u></u>	<u><u>7,526,385</u></u>

On behalf of the Management Board:


Zaur Yagubov
Director

September 13, 2021
Baku, the Republic of Azerbaijan


Muzaffar Umarov
Chief Accountant

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 34 are an integral part of these preliminary financial statements.

“AZERSILK” LIMITED LIABILITY COMPANY

PRELIMINARY STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

	Notes	Year ended December 31, 2020
CASH FLOWS FROM OPERATING ACTIVITIES:		
Loss before income tax		(268,307)
Adjustments to reconcile loss before income tax to net cash flows:		
Depreciation expenses	8	<u>199,960</u>
Operating cash flows before working capital changes:		<u>(68,347)</u>
Changes in operating assets and liabilities:		
Change in trade receivables		72,687
Change in inventories		(1,432,095)
Change in other current assets		3,708
Change in trade and other payables		<u>(4,616)</u>
Net cash used in operating activities		<u>(1,428,663)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant and equipment		<u>(7,405)</u>
Net cash used in investing activities		<u>(7,405)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Contribution by shareholder		532,648
Loan received from shareholder		1,930,000
Repayment of loan to shareholder		<u>(447,500)</u>
Net cash inflow from financing activities		<u>2,015,148</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS		<u>579,080</u>
CASH AND CASH EQUIVALENTS, at the beginning of the year	11	<u>27,647</u>
CASH AND CASH EQUIVALENTS, at the end of the year	11	<u>606,727</u>

On behalf of the Management Board:

Zaur Yagubov
Director

September 13, 2021
Baku, the Republic of Azerbaijan

Muzaffar Umarov
Chief Accountant

September 13, 2021
Baku, the Republic of Azerbaijan

The accompanying notes on pages 9 to 34 are an integral part of these preliminary financial statements.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

1. INTRODUCTION

“AzerSilk” Limited Liability Company (the “Company”) was established on April 16, 2018 and registered by the Ministry of Economy of the Republic of Azerbaijan with tax identification number 1305481631 as a limited liability company.

The structure of shareholding of the Company as at December 31, 2020 and January 1, 2020 was as followings:

	December 31, 2020 Ownership interest, %	January 1, 2020 Ownership interest, %
“Azerbaijan Industrial Corporation” Open Joint Stock Company	100.00	100.00
Total	100.00	100.00

The ultimate controlling party of the Company is “Azerbaijan Industrial Corporation” Open Joint Stock Company.

Principal activities

The principal activities of the Company include collection of cocoon from farmers, processing, production and sale of silk and silk products, and implementation of other tasks related to the development of this industry.

Registered address and place of business:

The Company is domiciled in the Republic of Azerbaijan. The Company’s registered legal address is Yasamal region, Tbilisi Avenue, Apartment 35, Baku, the Republic of Azerbaijan. The principal place of business of the Company is Sheki city, the Republic of Azerbaijan.

Operating Environment of the Company

In March 2020 the World Health Organization (WHO) announced that the spread of the COVID-19 virus across the globe was a pandemic. Significant restrictions on travel and movement of individuals and the closure of non-essential businesses have either been imposed in most countries or have happened as a result of the pandemic. This has led to significant declines in GDP in most if not all large economically strong countries in which the Republic of Azerbaijan is in a trade relationship. The global economy was negatively impacted by the coronavirus pandemic (COVID-19) spread in the first half of 2020. Starting from June 2020 many countries including the Republic of Azerbaijan demonstrated improvement in the signs of pandemic and certain restrictions were lifted subsequently. As a result, recovery in global financial and commodity markets observed. However, subsequently the number of reported cases significantly increased in the Republic of Azerbaijan, and the government introduced new restrictions from mid-December 2020.

The restrictive lock-down measures to combat COVID-19 in the country significantly reduced economic activity and aggregate spending levels. Certain segments of the economy, such as hotels, transport, travel, entertainment and many other businesses also international trade much affected by these measures.

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Oil prices have decreased significantly due to the substantial reduction in oil consumption in the pandemic environment but demonstrated stable growth during the second quarter of 2020. The government introduced support packages in the form of subsidized lending tools, payments to unemployed individuals and other subsidies to the entrepreneurs during the year to compensate for the economic slowdown caused by the pandemic.

The Company's operations are conducted in the Republic of Azerbaijan. Azerbaijan continues economic reforms and development of its legal, tax and regulatory frameworks. The future stability of Azerbaijan's economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Government as well as crude oil prices and stability of Azerbaijani Manat. Although the economy of the Republic of Azerbaijan is particularly sensitive to oil and gas prices, during recent years the Government of the Republic of Azerbaijan initiated major economic and social reforms to accelerate the transition to a more balanced economy and reduce dependence on the oil and gas sector. GDP in Azerbaijan was USD 42.6 billion during the year 2020, according to the State Statistical Committee of the Republic of Azerbaijan. In the long-term, the Azerbaijan GDP is projected to trend around USD 50 billion in 2021 and USD 51 billion in 2022, according to our econometric models.

The government continued its monetary policy with respect to the stability of Azerbaijani Manat as well as allocated foreign currency resources which stabilized Azerbaijani Manat. This policy continued in 2020 with the aim of maintaining macroeconomic stability. The Central Bank of the Republic of Azerbaijan has changed the refinancing rate several times during the year and the range was between 7.25% - 6.25% with a steady decrease in rates.

The Company's management is monitoring changes in the macroeconomic environment and taking precautionary measures it considers necessary in order to support the sustainability and development of the Company's business in the foreseeable future.

International credit rating agencies regularly evaluate the credit rating of the Republic of Azerbaijan. Fitch and S&P evaluated the rating of the Republic of Azerbaijan as “BB+”. Moody's Investors Service set “Ba2” credit rating for the country.

In September 2020, the escalation of unresolved conflict in Karabakh region (located in the southwest, which is internationally recognized as part of the Republic of Azerbaijan) resulted in clashes between the Republic of Azerbaijan and Armenian forces in occupied territories. In response, both countries introduced a curfew and military mobilization. Although the military actions mainly occurred in the western part of the Republic of Azerbaijan, some businesses were affected by the curfew which covered all the territories of the Republic of Azerbaijan including the capital Baku, to a certain degree. A complete ceasefire and a cessation of all hostilities in the zone of the Karabakh conflict were achieved on November 10, 2020. The level of macroeconomic effects in which the state involvement in liberated regions is uncertain as of reporting date.

These events and conditions described above created a level of uncertainty and risk that companies have not encountered before. The above-mentioned events had a significant effect on the financial results of the Company during the year ended December 31, 2020 and in the subsequent period.

The future economic growth of the Republic of Azerbaijan is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory and political developments. The Management is unable to predict, all developments in the economic environment which would have an impact on the Company's operations and consequently what effect, if any, they could have on the financial position of the Company. The management is currently performing sensitivity analyses under different oil price scenarios and elaborating relevant action plans for maintaining the sustainability of the business.

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NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Introduction

The financial year of the Company ends on the last day of December. In previous years, the accounts have been prepared under Generally Accepted Accounting Principles of the Republic of Azerbaijan (“AZ GAAP”). Effective from January 1, 2020 the Company produces its financial statements in accordance with International Financial Reporting Standards (“IFRSs”).

The preliminary financial statements have been prepared on the basis of IFRSs issued as at the date of this report and expected to be applicable by December 31, 2021. IFRS are subject to ongoing review or possible amendment by interpretative guidance from the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) and are therefore still subject to change. The preliminary financial statements will be updated and restated as necessary for any such changes should they occur.

Basis of preparation

First time adoption of IFRS

The rules for first time adoption of IFRS are set out in IFRS 1 “First Time Adoption of International Financial Reporting Standards”. IFRS 1 requires an entity to comply with each IFRS effective at the reporting date for its first full set of IFRS financial statements. As a general principle IFRS 1 requires the standards effective at the reporting date to be applied retrospectively.

However, retrospective application is prohibited in some areas, particularly where retrospective application would require judgements by management after the outcome of the particular transaction is already known. In addition, a number of limited optional exemptions from full retrospective application of IFRS are granted where the cost of compliance is deemed to exceed the benefits to users of the financial statements. The exemptions are divided into:

- Mandatory exemptions;
- Optional exemptions.

The Company applied all mandatory exemptions. The optional exemptions chosen by the management include:

- Fair value or revaluation as deemed cost – the Company elected to use the fair value amount as deemed cost for property, plant and equipment at the date of transfer of these assets to the Company by the shareholder.

Going concern

This preliminary financial statements have been prepared on the assumption that the Company is a going concern and will continue in operation for the foreseeable future.

Management views the Company as continuing in business for the foreseeable future with neither the intention nor the necessity of liquidation, ceasing trading or seeking protection from creditors pursuant to laws or regulations of the Republic of Azerbaijan.

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Accordingly, assets and liabilities are recorded on the basis that the Company will be able to realize its assets and discharge its liabilities in the normal course of business. Some financial reporting frameworks contain an explicit requirement for management to make a specific assessment of the Company's ability to continue as a going concern, and standards regarding matters to be considered and disclosures to be made in connection with going concern.

Management's assessment of the going concern assumption involves making a judgment, at a particular point in time, about the future outcome of events or conditions which are inherently uncertain.

Current versus non-current classification

The Company presents assets and liabilities in the preliminary financial statements based on current/non-current classification. An asset is current when it is:

- Expected to be realized or intended to be sold or consumed in the normal operating cycle;
- Held primarily for the purpose of trading;
- Expected to be realized within twelve months after the reporting period; or
- Cash or cash equivalent unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current.

A liability is current when:

- It is expected to be settled in the normal operating cycle;
- It is held primarily for the purpose of trading;
- It is due to be settled within twelve months after the reporting period; or
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Company classifies all other liabilities as non-current.

Deferred tax assets and liabilities are classified as non-current assets and liabilities.

Other basis of presentation criteria

These preliminary financial statements are presented in Azerbaijani Manats (“AZN”), unless otherwise indicated. The preliminary financial statements have been prepared under the historical cost convention, except property, plant and equipment which is stated at fair value as deemed cost.

The adoption of IFRS has resulted in changes to the Company's accounting policies. The amended accounting policies are:

Property, plant and equipment

Property, plant and equipment are stated in the preliminary financial statements at fair value as deemed cost, being the fair value at the date of revaluation, determined from market-based evidence by appraisal undertaken by professional independent appraisers, less any subsequent accumulated depreciation and impairment losses.

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The estimated useful life, residual values and depreciation method will be reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

At the end of each reporting period, the Company reviews the carrying amounts of its property, plant and equipment to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit and loss accounts, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit and loss accounts.

Property, plant and equipment are generally depreciated on a straight-line basis over their estimated useful lives as follows. The land is not depreciated.

Buildings and similar constructions	40-70 years
Machinery and equipment	5-15 years
Vehicles	5-10 years
Others	5-10 years

The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life.

The residual value of an asset may increase to an amount equal to or greater than the asset's carrying amount. If it does, the asset's depreciation charge is zero unless and until its residual value subsequently decreases to an amount below the asset's carrying amount.

Inventories

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on weighted average cost principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads based on normal operating capacity.

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Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

Financial instruments

Financial assets and financial liabilities are recognized in the Company's preliminary financial statements when the Company becomes a party to the contractual provisions of the instrument. Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognized immediately in profit or loss.

Financial assets

All regular way purchases or sales of financial assets are recognized and derecognized on a trade date basis. All recognized financial assets are measured subsequently in their entirety at either amortised cost or fair value, depending on the classification of the financial assets.

Classification of financial assets

Debt instruments that meet the following conditions are measured subsequently at amortised cost:

- the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Debt instruments that meet the following conditions are measured subsequently at fair value through other comprehensive income (FVTOCI):

- the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling the financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

By default, all other financial assets are measured subsequently at fair value through profit or loss (FVTPL).

Despite the foregoing, the Company may make the following irrevocable election/designation at initial recognition of a financial asset:

- the Company may irrevocably elect to present subsequent changes in fair value of an equity investment in other comprehensive income if certain criteria are met; and
- the Company may irrevocably designate a debt investment that meets the amortised cost or FVTOCI criteria as measured at FVTPL if doing so eliminates or significantly reduces an accounting mismatch

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Amortized cost and effective interest method

The effective interest method is a method of calculating the amortized cost of a debt instrument and of allocating interest income over the relevant period. For financial assets other than purchased or originated credit-impaired financial assets (i.e. assets that are credit-impaired on initial recognition), the effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) excluding expected credit losses, through the expected life of the debt instrument, or, where appropriate, a shorter period, to the gross carrying amount of the debt instrument on initial recognition.

For purchased or originated credit-impaired financial assets, a credit-adjusted effective interest rate is calculated by discounting the estimated future cash flows, including expected credit losses, to the amortised cost of the debt instrument on initial recognition.

The amortized cost of a financial asset is the amount at which the financial asset is measured at initial recognition minus the principal repayments, plus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, adjusted for any loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any loss allowance.

Interest income is recognized using the effective interest method for debt instruments measured subsequently at amortised cost and at FVTOCI. For financial assets other than purchased or originated credit-impaired financial assets, interest income is calculated by applying the effective interest rate to the gross carrying amount of a financial asset, except for financial assets that have subsequently become credit-impaired. For financial assets that have subsequently become credit-impaired, interest income is recognized by applying the effective interest rate to the amortised cost of the financial asset. If, in subsequent reporting periods, the credit risk on the credit-impaired financial instrument improves so that the financial asset is no longer credit-impaired, interest income is recognized by applying the effective interest rate to the gross carrying amount of the financial asset.

The Company's majority of financial assets were classified as financial assets measured subsequently at amortized cost. The Company's financial liabilities were classified as financial liabilities measured subsequently at amortized cost. The Company does not choose to classify any financial liabilities as measured at fair value through profit or loss.

Impairment of financial assets

The Company applies the expected credit loss model to financial assets measured at amortized cost or at fair value through other comprehensive income.

The allowance for expected credit losses for a financial asset is measured at an amount equal to the lifetime expected credit losses if the credit risk on that financial asset has increased significantly since initial recognition.

If, at the reporting date, the credit risk on a financial asset has not increased significantly since initial recognition, the allowance for expected credit losses for that financial asset (except trade receivables, where the simplified approach is elected) is measured at an amount equal to 12-month expected credit losses. For trade and other receivables, whether they contain a significant financing component or not, measurement based on lifetime expected credit losses are applied.

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The Company utilizes an internal model to assess expected credit losses. The model was developed in accordance with IFRS 9 and designed to assess credit risk exposure of counterparties taking into account the characteristics of financial assets by assigning scoring system to counterparties. Assigned score is returning PD (Probability of Default) on individual basis. Move of the asset from one score band to lower score band is considered significant increase in credit risk among other criteria.

Fair value measurement

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

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

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

The Company 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.

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

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

For assets and liabilities that are recognized in the financial statements on a recurring basis, the Company 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.

De-recognition of financial assets

The Company derecognizes a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

Financial liabilities and equity

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

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Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recognized at the proceeds received, net of direct issue costs.

Repurchase of the Company's own equity instruments is recognized and deducted directly in equity. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company's own equity instruments.

Financial liabilities

All financial liabilities are measured subsequently at amortised cost using the effective interest method or at FVTPL.

Financial liabilities are classified as at FVTPL when the financial liability is (i) contingent consideration of an acquirer in a business combination, (ii) held for trading or (iii) it is designated as at FVTPL.

Financial liabilities that are not (i) contingent consideration of an acquirer in a business combination, (ii) held-for-trading, or (iii) designated as at FVTPL, are measured subsequently at amortised cost using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or (where appropriate) a shorter period, to the amortised cost of a financial liability.

De-recognition of financial liabilities

The Company removes a financial liability (or a part of a financial liability) from its preliminary financial statements when, and only when, it is extinguished - ie when the obligation specified in the contract is discharged or cancelled or expires.

An exchange between an existing borrower and lender of debt instruments with substantially different terms is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, a substantial modification of the terms of an existing financial liability or a part of it (whether or not attributable to the financial difficulty of the debtor) is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10 per cent different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognized as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortized over the remaining term of the modified liability.

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Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the preliminary financial statements if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liabilities simultaneously.

Trade and other receivables

Trade receivables are carried at amortized cost using the effective interest method. The Company uses a provision matrix to calculate expected credit losses for trade receivables and contract assets. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by geography, product type, customer type and rating, and coverage by letters of credit and other forms of credit insurance).

The provision matrix is initially based on the Company's historical observed default rates. The Company will calibrate the matrix to adjust the historical credit loss experience with forward-looking information. For instance, if forecast economic conditions (i.e., gross domestic product) are expected to deteriorate over the next year which can lead to an increased number of defaults in the manufacturing sector, the historical default rates are adjusted. At every reporting date, the historical observed default rates are updated and changes in the forward-looking estimates are analyzed. Where applicable, the Company relies on default rates derived from external rates of counterparties.

The assessment of the correlation between historical observed default rates, forecast economic conditions and expected credit losses is a significant estimate. The amount of expected credit losses is sensitive to changes in circumstances and of forecast economic conditions. The Company's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future.

Advances to suppliers

Advances to suppliers are carried at cost less provision for impairment. An advance is classified as non-current when the goods or services relating to the advance are expected to be obtained after one year, or when the advance relates to an asset which will itself be classified as non-current upon initial recognition.

Advances to acquire assets are transferred to the carrying amount of the asset once the Company has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Company. Other advances are written off to profit and loss accounts when the goods or services relating to the advances are received. If there is an indication that the assets, goods or services relating to an advance will not be received, the carrying value of the advance is written down accordingly and a corresponding impairment loss is recognized in profit and loss accounts.

VAT deposit account

The Value Added Tax (“VAT”) deposit account system is introduced in 2008 by the Ministry of Taxes of the Republic of Azerbaijan which aims prevention of VAT misuse. From January 1, 2008 on the basis of amendments to the Tax Code, the amount of VAT refund is considered the tax amount which is paid, according to the submitted VAT invoices to the taxpayer's VAT deposit account in the framework of transactions carried out in this account.

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By the support of this module the taxpayer pays the amount of VAT indicated on the VAT invoices to the VAT deposit account of another taxpayer. At the same time tax obligations to the state budget regarding all kinds of taxes and VAT amounts on the import transactions which is necessary to be paid to the customs committee, can be paid by taxpayers through the VAT deposit account. Information about paid amounts is transferred by the tax authority to the Main State Treasury (“MST”) and then to the Central Bank of the Republic of Azerbaijan (“CBRA”). CBRA on the basis of information submitted by the Main State Treasury ensures the transformation of amounts to the relevant local treasury authorities. The tax authority ensures inclusion of amounts which is noted in the submitted information to the taxpayer’s personal files. The current system is connected with the Automated Tax Information System maintained by the State Tax Service under the Ministry of Economy of the Republic of Azerbaijan. At the same time online exchange of information was organized with the MST and CBRA.

Implementation of the VAT deposit account makes it possible to timely control payments and refunded VAT amounts. Taxpayers who have tax debts can only transfer these amounts to the state budget. Taxpayers can make payments to the state budget without visiting banks, to the VAT deposit account of other taxpayers and to the customs committee through the deposit account. The State Tax Service under the Ministry of Economy of the Republic of Azerbaijan automatically controls all transactions carried out through the deposit account using special software.

Use of balances in the VAT deposit account is restricted and can be used only for transactions connected with VAT and other applicable taxes.

Charter capital

Charter capital is the amount of capital contributed by the shareholder of the Company. The Company may increase or decrease its charter capital within approval of the shareholder.

Revenue from Contracts with Customers

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers.

The core principle of IFRS 15 is that the Company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a 5-step approach to revenue recognition:

- Step 1: Identify the contract(s) with a customer.
- Step 2: Identify the performance obligations in the contract.
- Step 3: Determine the transaction price.
- Step 4: Allocate the transaction price to the performance obligations in the contract.
- Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognizes revenue when or as a performance obligation is satisfied, i.e. when ‘control’ of the goods or services underlying the particular performance obligation is transferred to the customer.

Employee benefits

Wages, salaries, contributions to the Republic of Azerbaijan state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits are accrued in the year in which the associated services are rendered by the employees of the Company.

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Taxation

Deferred taxes

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

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset is realized. Deferred tax is charged or credited in the statement of comprehensive income, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred income tax assets and deferred income tax liabilities are offset and reported net on the preliminary financial statements if:

- The Company has a legally enforceable right to set off current income tax assets against current income tax liabilities; and
- Deferred income tax assets and the deferred income tax liability relate to income taxes levied by the same taxation authority on the same taxable entity.

Value added tax

The difference of output VAT and claimable input VAT is payable to the state budget within 20 days following the reporting month. Output value added tax related to sales is payable to tax authorities upon receipt of payment in return to such sales. Input VAT is generally recoverable against output VAT upon receipt of the electronic invoice. The tax authorities permit the settlement of VAT on a net basis.

VAT related to sales and purchases is recognized in the preliminary financial statements on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

Foreign currency translation

The functional currency of the Company is the currency of the primary economic environment, in which it operates. The Company's functional currency is AZN.

Monetary assets and liabilities denominated in foreign currencies are translated into AZN at the appropriate spot rates of exchange of the CBRA ruling at the end of reporting date. Foreign currency transactions are accounted for at the exchange rates prevailing at the date of the transaction.

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Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

The exchange rates at reporting date used by the Company in the preparation of the preliminary financial statements are as follows:

	December 31, 2020	January 1, 2020
1 USD	1.7000 AZN	1.7000 AZN

Contingent liabilities and assets

Contingent liabilities are not recognized in the preliminary financial statements. They are disclosed in the notes to the preliminary financial statements unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets are not recognized in the preliminary financial statements but disclosed when an inflow of economic benefits is probable.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The preparation of preliminary financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, costs and disclosure of contingent liabilities during the reporting period.

As a result of the uncertainties inherent in business activities, many items in preliminary financial statements cannot be measured with precision but can only be estimated. Estimation involves judgments based on the latest information available when the preliminary financial statements was prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Company. Such changes are reflected in the assumptions when they occur.

The most significant estimates relate to the depreciable lives of property, plant and equipment, impairment of non-financial and financial assets, fair value of financial instruments, provision for obsolete inventory, provision for tax and legal contingencies and deferred taxation. Actual results could differ from these estimates.

Judgments

In the process of applying Company's accounting policies, the management has made the following judgments, apart from those involving estimates, which have the most significant effect on the amounts recognized in the preliminary financial statements.

Fair value of property, plant and equipment

Property, plant and equipment were measured at fair value as deemed costs at the date when these assets were transferred to the Company.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Fair value of property, plant and equipment was assessed using the market approach method which involves analysis of market sales prices for similar property, plant and equipment which was also equal to the fair value of property, plant and equipment under IFRS 13.

Useful life of property, plant and equipment

The Company assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 “Accounting Policies, Changes in Accounting Estimates and Errors”. These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and on depreciation recognized in profit and loss accounts.

Impairment of property, plant and equipment and other non-financial assets

The Company assesses at each reporting date whether there is any indication that an asset may be impaired. If any such indication exists, the Company makes an estimate of the asset’s recoverable amount. An asset’s recoverable amount is the higher of an asset’s or cash-generating unit’s fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, recent market transactions are taken into account, if available. If no such transactions can be identified, an appropriate valuation model is used.

The value in use analysis resulted in negative cash flows, therefore the Company determined the recoverable amount of assets using their fair values less cost of sales. As a result of such analysis no impairment recognized as at December 31, 2020.

Inventory valuation

Inventory is valued at the lower of cost or net realizable value. The Company records an allowance to reduce the carrying value of obsolete and slow-moving inventory to net realizable value, when appropriate. The actual value realized on disposition of such inventory may differ from the net realizable value; any such difference could have a significant impact on future operating results.

Recoverability of VAT

At each reporting date the Company assesses the recoverability of VAT arising on purchase of goods and services. The Company can only receive these amounts through an offset against future VAT liability or collection from the tax authorities. In assessing the recoverability of the VAT receivable, the Company considers information from the internal tax department regarding projected VAT liability, correspondence with government tax authorities, and historical recovery experience.

The actual amount of VAT recovery could differ materially from the Company’s estimate and this could materially impact operating results.

Fair value measurement of financial instruments

A number of the Company’s accounting policies and disclosures require the measurement of fair values, for both financial and non-financial assets and liabilities.

The Company has an established control framework with respect to the measurement of fair values.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

When measuring the fair value of an asset or a liability, the Company uses market observable data as far as possible. Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

- *Level 1:* quoted prices (unadjusted) in active markets for identical assets or liabilities;
- *Level 2:* inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- *Level 3:* inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

Current taxes

Azerbaijani tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Company's entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Company's entities may be assessed additional taxes, penalties and interest, which can be significant.

Periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As at December 31, 2020, the management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Company's tax, currency and customs positions will be sustained.

Deferred taxes

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

As at December 31, 2020 deferred tax asset was mainly due to tax losses carry forward. The Company assumes that future taxable profit will not be available against which the losses can be utilized. The Company did not recognize deferred tax asset as at December 31, 2020.

Revenue recognition

Revenues from sales of goods are recognized at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped. If the Company agrees to transport goods to a specified location, revenue is recognized when the goods are passed to the customer at the destination point.

Sales of services are recognized in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

Gross sales are shown net of VAT but including discounts. Discounts are provided on discretionary basis depending on commercial terms.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Revenues are measured at the fair value of the consideration received or receivable. When the fair value of goods received in a barter transaction cannot be measured reliably, the revenue is measured at the fair value of the goods or service given up.

4. ADOPTION OF NEW AND REVISED STANDARDS AND INTERPRETATIONS

In the current year, the Company has adopted all of the applicable new and revised Standards and Interpretations issued by the IASB and the IFRIC of the IASB that are relevant to its operations and effective for the year ending December 31, 2021.

On May 15, 2020 IASB has published “**COVID-19 – Related Rent Concessions (Amendment to IFRS 16)**” amending the standard to provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification.

The changes in COVID-19-Related Rent Concessions (Amendment to IFRS 16) amend IFRS 16 to:

- provide lessees with an exemption from assessing whether a COVID-19-related rent concession is a lease modification;
- require lessees that apply the exemption to account for COVID-19-related rent concessions as if they were not lease modifications;
- require lessees that apply the exemption to disclose that fact; and
- require lessees to apply the exemption retrospectively in accordance with IAS 8, but not require them to restate prior period figures.

The amendment is effective for annual reporting periods beginning on or after June 1, 2020. Earlier application is permitted. The impact of adoption of this standard had no effect on the financial statements.

Unless otherwise disclosed, the new adopted standards did not have material effect on the preliminary financial statements of the Company.

5. STANDARDS AND INTERPRETATIONS ISSUED AND NOT YET ADOPTED

At the date of authorization of these preliminary financial statements, other than the Standards and Interpretations adopted by the Company in advance of their effective dates, the following Interpretations were in issue but not yet effective.

IFRS 17 “Insurance contracts” – was issued in May 2017 and replaced IFRS 4 “Insurance contracts”. The new standard establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the standard. An entity shall apply IFRS 17 “Insurance Contracts” to insurance contracts, including reinsurance contracts, it issues; reinsurance contracts it holds; and investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts.

IFRS 17 is effective for annual reporting periods beginning on or after January 1, 2023. Earlier application is permitted if both IFRS 15 Revenue from Contracts with Customers and IFRS 9 Financial Instruments have also been applied. This standard is not applicable to the Company.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

Amendments to IAS 1 to clarify the classification of liabilities – In January 2020 the IASB has issued “**Classification of Liabilities as Current or Non-Current (Amendments to IAS 1)**” providing a more general approach to the classification of liabilities under IAS 1 based on the contractual arrangements in place at the reporting date. The amendments in Classification of Liabilities as Current or Non-Current (Amendments to IAS 1) affect only the presentation of liabilities in the statement of financial position – not the amount or timing of recognition of any asset, liability income or expenses, or the information that entities disclose about those items.

The amendments are effective for annual reporting periods beginning on or after January 1, 2023 and are to be applied retrospectively. Earlier application is permitted. The Company is currently assessing the impact the amendments will have on the current practice and whether existing loan agreements may require renegotiation.

Reference to the Conceptual Framework – Amendments to IFRS 3 – In May 2020, the IASB issued **Amendments to IFRS 3 “Business Combinations” – Reference to the Conceptual Framework**. The amendments are intended to replace a reference to the Framework for the Preparation and Presentation of Financial Statements, issued in 1989, with a reference to the Conceptual Framework for Financial Reporting issued in March 2018 without significantly changing its requirements. The Board also added an exception to the recognition principle of IFRS 3 to avoid the issue of potential ‘day 2’ gains or losses arising for liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 Levies, if incurred separately. At the same time, the Board decided to clarify existing guidance in IFRS 3 for contingent assets that would not be affected by replacing the reference to the Framework for the Preparation and Presentation of Financial Statements. The amendments are effective for annual reporting periods beginning on or after January 1, 2022 and apply prospectively.

Property, Plant and Equipment: Proceeds before Intended Use – Amendments to IAS 16 – In May 2020, the IASB issued **Property, Plant and Equipment – Proceeds before Intended Use**, which prohibits entities deducting from the cost of an item of property, plant and equipment, any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognizes the proceeds from selling such items, and the costs of producing those items, in profit or loss. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 and must be applied retrospectively to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented when the entity first applies the amendment. The amendments are not expected to have a material impact on the Company.

Onerous Contracts – Costs of Fulfilling a Contract – Amendments to IAS 37 – In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making. The amendments apply a “directly related cost approach”. The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract. The amendments are effective for annual reporting periods beginning on or after January 1, 2022.

IFRS 1 “First-time Adoption of International Financial Reporting Standards” – Subsidiary as a first-time adopter. As part of its 2018-2020 annual improvements to IFRS standards process, the IASB issued an amendment to IFRS 1 “First-time Adoption of International Financial Reporting Standards”. The amendment permits a subsidiary that elects to apply paragraph D16(a) of IFRS 1 to measure cumulative translation differences using the amounts reported by the parent, based on the parent’s date of transition to IFRS. This amendment is also applied to an associate or joint venture that elects to apply paragraph D16 (a) of IFRS 1. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

IFRS 9 Financial Instruments – Fees in the “10 per cent” test for de-recognition of financial liabilities. As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued an amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other’s behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment. The amendment is effective for annual reporting periods beginning on or after January 1, 2022 with earlier adoption permitted. The Company will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

“IAS 41 Agriculture” – Taxation in fair value measurements. As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued an amendment to IAS 41 Agriculture. The amendment removes the requirement in paragraph 22 of IAS 41 that entities exclude cash flows for taxation when measuring the fair value of assets within the scope of IAS 41. An entity applies the amendment prospectively to fair value measurements on or after the beginning of the first annual reporting period beginning on or after January 1, 2022 with earlier adoption permitted. The amendments are not expected to have a material impact on the Company.

IFRS 10 “Consolidated Financial Statements” and IAS 28 (amendments) Sale or Contribution of Assets between an Investor and its Associate or Joint Venture – The amendments to IFRS 10 and IAS 28 deal with situations where there is a sale or contribution of assets between an investor and its associate or joint venture. Specifically, the amendments state that gains or losses resulting from the loss of control of a subsidiary that does not contain a business in a transaction with an associate or a joint venture that is accounted for using the equity method, are recognized in the parent’s profit or loss only to the extent of the unrelated investors’ interests in that associate or joint venture.

Similarly, gains and losses resulting from the re-measurement of investments retained in any former subsidiary (that has become an associate or a joint venture that is accounted for using the equity method) to fair value are recognized in the former parent’s profit or loss only to the extent of the unrelated investors’ interests in the new associate or joint venture. The effective date of the amendments has yet to be set by the IASB; however, earlier application of the amendments is permitted.

Unless otherwise disclosed, the new pronounced standards are not expected to have a material effect on the financial statements of the Company.

6. BALANCES AND TRANSACTIONS WITH RELATED PARTIES

Related parties are defined in IAS 24 “Related Party Disclosures”. Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. The Company’s immediate parent is “Azerbaijan Industrial Corporation” Open Joint Stock Company, which is fully owned by the Government of the Republic of Azerbaijan.

The Company applied the exemption in paragraph 25 of IAS 24 “Related Party Disclosures” regarding the disclosure requirement for government related entities.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

A reporting entity is exempt from the disclosure requirements of paragraph 18 of IAS 24 “Related Party Disclosures” in relation to related party transactions and outstanding balances, including commitments, with:

- (a) a government that has control or joint control of, or significant influence over, the reporting entity; and
- (b) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity.

The nature of transactions with government related entities include purchase of electricity, gas, petrol and receiving other services.

During the year ended December 31, 2020, the remuneration of key management personnel included salaries, discretionary bonuses and other short-term benefits totalling AZN 71,500.

7. FIRST TIME ADOPTION OF IFRS

The Company first adopted IFRSs in 2020, with the date of effective transition to IFRSs as at January 1, 2020. The Company’s opening IFRS statement of financial position is reconciled with previously adopted GAAP of the Republic of Azerbaijan (the “previous GAAP”) frameworks as follows.

The effect of transition to IFRS and correction of errors made to the opening IFRS statement of financial position as at January 1, 2020 is as follows:

Opening IFRS statement of financial position	Notes	Previous GAAP (as presented)	Effect of transition to IFRS/ errors	IFRS (as adjusted)
		January 1, 2020	January 1, 2020	January 1, 2020
Property, plant and equipment	a	2,900,355	424,868	3,325,223
Inventories	a	6,524,330	(424,868)	6,099,462
Cash and cash equivalents	b	28,550	(903)	27,647
Other current assets	b	8,930	903	9,833
Charter capital	c	(7,586,931)	2,425,235	(5,161,696)
Other capital	c	-	(2,425,235)	(2,425,235)

Explanations for the correction of errors and effect of transition:

- a. Difference is due to correction for reclassification of fixed assets recorded in inventory balance;
- b. VAT deposit account is reclassified from cash and cash equivalents to other current assets;
- c. The Company reclassified between charter capital and other capital for properties transferred by shareholder but not yet registered as charter capital.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

8. PROPERTY, PLANT AND EQUIPMENT

	Buildings and similar constructions	Machinery and equipment	Vehicles	Others	Total
Fair value as deemed cost/initial cost					
January 1, 2020	1,939,662	1,448,129	91,414	19,760	3,498,965
Additions	-	-	-	7,405	7,405
December 31, 2020	1,939,662	1,448,129	91,414	27,165	3,506,370
Accumulated depreciation					
January 1, 2020	(39,188)	(108,072)	(20,688)	(5,794)	(173,742)
Charge for the year	(24,582)	(163,495)	(8,572)	(3,311)	(199,960)
December 31, 2020	(63,770)	(271,567)	(29,260)	(9,105)	(373,702)
Net book value					
December 31, 2020	1,875,892	1,176,562	62,154	18,060	3,132,668
January 1, 2020	1,900,474	1,340,057	70,726	13,966	3,325,223

As at December 31, 2020 and January 1, 2020, included in property, plant and equipment there were neither any assets with restrictions on title, nor any assets that were pledged as security for liabilities.

9. INVENTORIES

Inventories comprise:

	December 31, 2020	January 1, 2020
Work in progress	1,978,095	3,243,779
Semi-finished goods	4,386,002	1,900,085
Finished goods	1,062,159	857,375
Others	105,301	98,223
Total inventories	7,531,557	6,099,462

10. TRADE RECEIVABLES

As at December 31, 2020, there was no trade receivable from customers (January 1, 2020: AZN 72,687).

Trade receivables do not bear interest and are usually settled within up to 1 month and denominated in AZN. As at January 1, 2020, the geographical concentration of the Company's trade receivables was the Republic of Azerbaijan.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (In Azerbaijani Manats)

11. CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise:

	December 31, 2020	January 1, 2020
Cash at banks in AZN	1,979	25,754
Cash at banks in USD	604,354	460
Cash on hand	394	1,433
Total cash and cash equivalents	606,727	27,647

The geographical concentration of the Company's cash and cash equivalents was the Republic of Azerbaijan.

12. OTHER CURRENT ASSETS

	December 31, 2020	January 1, 2020
Advance to suppliers	6,125	8,378
Tax receivables	-	552
VAT deposit account	-	903
Total other current assets	6,125	9,833

13. TRADE AND OTHER PAYABLES

	December 31, 2020	January 1, 2020
Trade payables	109,371	110,228
Total trade payables	109,371	110,228
Employee related payables	60,426	91,589
Advanced received	96,333	88,954
Tax payables	46,115	26,090
Total trade and other payables	312,245	316,861

Trade payable balances are usually settled within up to 1 month and denominated in AZN. The geographical concentration of the Company's trade payables was the Republic of Azerbaijan.

14. AMOUNT DUE TO SHAREHOLDER

Amount due to shareholder includes short-term interest free AZN denominated loan from shareholder in the amount of AZN 3,438,447 (January 1, 2020: AZN 1,955,947).

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020

(In Azerbaijani Manats)

15. CHARTER CAPITAL

As at December 31, 2020, charter capital amounted to AZN 8,119,579 and consists of 100 shares with AZN 81,195.79 face value per share (January 1, 2020: AZN 5,161,696 and consists of 100 shares with AZN 51,616.96 face value per share). During 2020, the Company registered other capital amounting AZN 2,957,883 as charter capital.

16. OTHER CAPITAL

As at December 31, 2020, other capital was nil. As at January 1, 2020, other capital amounted to AZN 2,425,235 and consisted of asset transferred to the Company by shareholder but not yet registered as charter capital.

17. REVENUE

Revenue comprise:

	Year ended December 31, 2020
Revenue from sales of silk products	<u>2,327,313</u>
Total revenue	<u>2,327,313</u>

18. COST OF SALES

Cost of sales comprise:

	Year ended December 31, 2020
Material expenses	1,982,527
Staff costs	1,141,287
Depreciation expenses	195,424
Utility expenses	161,997
Fuel expenses	20,968
Repair and maintenance expenses	9,984
Insurance expenses	7,167
Change in finished / semi-finished goods and work in progress	(1,425,017)
Other costs	<u>27,999</u>
Total cost of sales	<u>2,122,336</u>

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 *(In Azerbaijani Manats)*

19. GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses comprise:

	Year ended December 31, 2020
Staff costs	486,793
Security expenses	90,533
Customs expenses	31,536
Bank charges	9,226
Insurance expenses	6,608
Depreciation expenses	4,536
Communication expenses	3,610
Other expenses	<u>14,322</u>
Total general and administrative expenses	<u>647,164</u>

20. OTHER INCOME

Other income in the amount of AZN 173,880 represents income from scrap metal sales.

21. COMMITMENTS AND CONTINGENCIES

Legal proceedings

From time to time and in the normal course of business, claims against the Company were received from customers and counterparties. Management is of the opinion that no material unaccrued losses will be incurred and accordingly no provision has been made in this preliminary financial statements.

Taxation

Commercial legislation and tax legislation of the Republic of Azerbaijan in particular may give rise to varying interpretations and amendments. In addition, as management's interpretation of tax legislation may differ from that of the tax authorities, transactions may be challenged by the tax authorities, and as a result, the Company may be assessed additional taxes, penalties and interest. The Company believes that it has already made all tax payments, and therefore no allowance has been made in the preliminary financial statements. Tax years remain open to review by the tax authorities for three years.

22. FINANCIAL RISK MANAGEMENT

Management of risk is fundamental to the Company's business and is an essential element of its operations. The main risks inherent to the Company operations are those related to:

- Credit risk;
- Liquidity risk;
- Market risk.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

The Company recognizes that it is essential to have efficient and effective risk management processes in place. To enable this, the Company has established a risk management department. The main purpose of this department is to protect the Company from risk and allow it to achieve its performance objectives. Through the risk management framework, the Company manages the following risks:

Credit risk

The Company is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

Maximum exposure

The Company's maximum exposure to credit risk varies significantly and is dependent on both individual risks and general market economy risks.

Geographical concentration

Assets, liabilities and credit related commitments have been based on the country, in which the counterparty is located. Balances with counterparties located in the Republic of Azerbaijan actually outstanding to/from companies of these counterparties are allocated to the caption "The Republic of Azerbaijan". Cash on hand, precious metals and premises and equipment have been allocated based on the country, in which they are physically held.

Geographical concentration of the Company's financial assets and liabilities as at December 31, 2020 and January 1, 2020 was disclosed in the relevant notes.

Liquidity risk

Liquidity risk is defined as the risk when the maturity of financial assets and liabilities does not match. Liquidity risk is managed by the Finance Department of the Company. The liquidity management of the Company requires considering the level of liquid assets necessary to settle obligations as they fall due; maintaining access to a range of funding sources; maintaining funding contingency plans and monitoring balance sheet liquidity ratio.

The liquidity risk of the Company's financial assets and liabilities as at December 31, 2020 and January 1, 2020 was disclosed in the relevant notes.

Currency risk

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

The currency risk related to the Company's financial assets and liabilities as at December 31, 2020 and January 1, 2020 was disclosed in the relevant notes.

23. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

The estimated fair values of financial instruments have been determined by the Company using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Republic of Azerbaijan continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

The fair value of financial assets and liabilities recognized at cost or amortized cost in the preliminary financial statements as at December 31, 2020 is presented below:

	December 31, 2020	
	Carrying value	Fair value
Cash and cash equivalents	606,727	606,727
Trade and other payables	109,371	109,371
Amount due to shareholder	3,438,447	3,438,447

The fair value of financial assets and liabilities recognized at cost or amortized cost in the preliminary financial statements as at January 1, 2020 is presented below:

	January 1, 2020	
	Carrying value	Fair value
Trade receivables	72,687	72,687
Cash and cash equivalents	27,647	27,647
Trade and other payables	110,228	110,228
Amount due to shareholder	1,955,947	1,955,947

The following table sets out the fair values of financial instruments not measured at fair value and analyzes them by the level in the fair value hierarchy into which each fair value measurement as at December 31, 2020 is categorized below:

Fair value measurement using						
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed						
Cash and cash equivalents	Amortized cost	December 31, 2020	606,727	-	-	606,727
Liabilities for which fair values are disclosed						
Trade and other payables	Amortized cost	December 31, 2020	-	-	109,371	109,371
Amount due to shareholder	Amortized cost	December 31, 2020	-	-	3,438,447	3,438,447

“AZERSILK” LIMITED LIABILITY COMPANY

NOTES TO THE PRELIMINARY FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2020 (Continued) *(In Azerbaijani Manats)*

The following table sets out the fair values of financial instruments not measured at fair value and analyzes them by the level in the fair value hierarchy into which each fair value measurement as at January 1, 2020 is categorized below:

			Fair value measurement using			
	Financial instrument classification	Date of valuation	Quoted prices in active markets (Level 1)	Significant observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Assets for which fair values are disclosed						
Trade receivables	Amortized cost	January 1, 2020	-	-	72,687	72,687
Cash and cash equivalents	Amortized cost	January 1, 2020	27,647	-	-	27,647
Liabilities for which fair values are disclosed						
Trade and other payables	Amortized cost	January 1, 2020	-	-	110,228	110,228
Amount due to shareholder	Amortized cost	January 1, 2020	-	-	1,955,947	1,955,947