INTESA SANPAOLO BANK ALBANIA SH.A.

Financial Statements as at and for the year ended

31 December 2017

(with independent auditors' report thereon)

Contents

KPMG

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Independent Auditors' Report

To the Shareholders of Intesa Sanpaolo Albania Sh.a

Opinion

We have audited the financial statements of Intesa Sanpaolo Albania Sh.a ("the Bank"), which comprise the statement of financial position as at 31 December 2017, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (IESBA Code) and with Institute of Authorized Chartered Auditors of Albania Code of Ethics (IEKA Code), together with the ethical requirements of the Law No. 10091, dated 5 March 2009 "On the statutory audit and the organization of the statutory auditors and chartered accountants professions", amended that are relevant to our audit of the financial statements in Albania, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code and IEKA Code.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information

Management is responsible for the other information. The other information comprises the information included in the annual report prepared by management in accordance with Article 53 of the Law. No. 9662, dated 18 December 2006 "On banks in the Republic of Albania", amended, but does not include the financial statements and our auditors' report thereon. The annual report is expected to be made available to us after the date of this auditors' report.

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

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

When we read the annual report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

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

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

Fatos Beqja
Statutory Auditor

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Tirana, Albania

Tirana, 05 March 2018

Intesa Sanpaolo Bank Albania Sh.a.

Statement of financial position

As at 31 December 2017

(in thousands of Lek)

	Notes	2017	2016
Assets			
Cash and cash equivalents	7	22,877,864	27,269,197
Loans and advances to banks	8	20,171,066	17,106,968
Financial investments available for sale	9	9,423,008	7,251,448
Financial investments held to maturity	10	49,110,119	50,729,433
Loans and advances to customers	11	46,557,253	42,542,151
Property and equipment	12	2,141,765	1,172,243
Intangible assets	13	528,695	591,902
Investment property	14	575,318	-
Deferred tax assets	18	174,247	82,092
Current tax assets		389,883	282,007
Inventory and other assets	15	2,296,937	2,500,378
Total Assets		**154,246,155**	**149,527,819**
Liabilities			
Due to banks	16	5,168,783	2,885,233
Due to customers	17	127,711,325	125,974,220
Current tax liabilities		-	25,259
Deferred tax liabilities	18	148,327	290
Provisions	19	468,695	350,379
Other liabilities	20	1,039,583	786,564
Total Liabilities		**134,536,713**	**130,021,945**
Equity			
Share capital	21	5,562,518	5,562,518
Share premium	21	1,383,880	1,383,880
Legal and regulatory reserves	22	1,825,623	1,825,623
Other reserve	23	831,461	1,643
Other comprehensive items	23	714,555	714,555
Retained earnings		9,391,405	10,017,655
Total Equity		**19,709,442**	**19,505,874**
Total Liabilities and Equity		**154,246,155**	**149,527,819**

The notes on pages 6 to 59 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

Statement of Profit or Loss and Other Comprehensive Income
For the year ended 31 December 2017
(in thousands of Lek)

	Notes	2017	2016
Interest income		4,280,758	4,825,966
Interest expense		(522,348)	(817,350)
Net interest income	24	**3,758,410**	**4,008,616**
Fee and commission income		953,439	910,143
Fee and commission expense		(250,720)	(204,494)
Net fee and commission income	25	**702,719**	**705,649**
Net other income	26	417,522	366,342
Other operating expenses, net	27	(270,161)	(278,023)
Operating income		**4,608,490**	**4,802,584**
Net impairment reversal on financial assets	11	46,003	398,713
Net impairment loss on off-balance sheet	19	(1,437)	(12,533)
Write down of inventory	15	(190,287)	(293,553)
Personnel expenses	28	(1,135,023)	(1,048,209)
Operating lease expenses	32	(159,658)	(164,626)
Depreciation and amortization	12,13,14	(311,101)	(324,257)
Impairment of investment property	14	(129,773)	-
Amortization of leasehold improvements	15	(7,863)	(7,751)
Other administration expenses	29	(733,227)	(614,400)
Provisions for risk and expenses	19	(50,928)	27,890
Total expenses		**(2,673,294)**	**(2,038,726)**
Net income before taxes		**1,935,196**	**2,763,858**
Income tax expense	30	(278,441)	(480,853)
Profit for the year		**1,656,755**	**2,283,005**
Other comprehensive income			
Change in fair value of available-for-sale investment securities, net of income tax		54,387	1,384
Change in fair value of functional properties, net of income tax		775,431	-
Other comprehensive income for the year, net of tax		**829,818**	**1,384**
Total comprehensive income for the year, net of tax		**2,486,573**	**2,284,389**

The notes on pages 6 to 59 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

Statement of changes in equity
For the year ended 31 December 2016
(in thousands of Lek)

	Share capital	Share premium	Legal and regulatory reserves	Other reserves	Other comprehensive items	Retained earnings	Total
Balance at 1 January 2016	**5,562,518**	**1,383,880**	**1,825,623**	**259**	**714,555**	**9,945,745**	**19,432,580**
Profit for the year	-	-	-	-	-	2,283,005	**2,283,005**
Other comprehensive income							
Net change in fair value of available-for-sale investment securities, net of tax	-	-	-	1,384	-	-	**1,384**
Total comprehensive income for the year	**-**	**-**	**-**	**1,384**	**-**	**2,283,005**	**2,284,389**
Transaction with owners, recorded directly in equity							
Dividends to equity holders	-	-	-	-	-	(2,211,095)	**(2,211,095)**
Total contributions by and distribution to owners	**-**	**-**	**-**	**-**	**-**	**(2,211,095)**	**(2,211,095)**
Balance at 31 December 2016	**5,562,518**	**1,383,880**	**1,825,623**	**1,643**	**714,555**	**10,017,655**	**19,505,874**

The notes on pages 6 to 59 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

Statement of changes in equity (continued)
For the year ended 31 December 2017
(in thousands of Lek)

	Share capital	Share premium	Legal and regulatory reserves	Other reserves	Other comprehensive items	Retained earnings	Total
Balance at 1 January 2017	**5,562,518**	**1,383,880**	**1,825,623**	**1,643**	**714,555**	**10,017,655**	**19,505,874**
Profit for the year						1,656,755	**1,656,755**
Other comprehensive income							**-**
Net change in fair value of available-for-sale investment securities, net of tax	-	-	-	54,387			**54,387**
Revaluation of Functional Properties, net of tax	-	-	-	775,431			**775,431**
Total comprehensive income for the year	**-**	**-**	**-**	**829,818**	**-**	**1,656,755**	**2,486,573**
Transaction with owners, recorded directly in equity							
Dividends to equity holders	-	-	-	-	-	(2,283,005)	**(2,283,005)**
Total contributions by and distribution to owners	**-**	**-**	**-**	**-**	**-**	**(2,283,005)**	**(2,283,005)**
Balance at 31 December 2017	**5,562,518**	**1,383,880**	**1,825,623**	**831,461**	**714,555**	**9,391,405**	**19,709,442**

The notes on pages 6 to 59 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

Statement of cash flows
For the year ended 31 December 2017

(in thousands of Lek)

	2017	2016
Net profit for the year	**1,656,755**	**2,283,005**
Adjustments for:		
Depreciation and amortization	294,703	324,257
Changes in investment property	(721,489)	-
Impairment of investment property	146,171	-
Disposal of property and equipment	72,784	56
Net impairment reversal on loans and advances to customers	(46,003)	(398,713)
Write down of inventory	190,287	293,553
Net interest income	(3,758,410)	(4,008,616)
Net impairment loss on off-balance sheet items	1,437	12,533
Tax expense	278,441	480,853
Changes in		
Loans and advances to banks	(3,064,098)	6,795,969
Loans and advances to customers	(3,392,194)	(1,331,849)
Due to banks	2,283,550	932,201
Due to customers	1,808,924	7,234,443
Inventory and other assets	(94,722)	(716,232)
Other liabilities and provisions	344,639	(49,942)
Deferred tax asset	(200,031)	11
Deferred tax liability	26,857	85,453
Interest received	3,703,854	4,642,223
Interest paid	(594,167)	(919,699)
Income taxes paid	(195,824)	(566,270)
Net cash (used)/from in operating activities	**(1,258,536)**	**15,093,236**
Cash flows from investing activities		
Acquisition of property and equipment	(232,001)	(160,978)
Acquisition of intangible assets	(129,529)	(134,648)
Net collections from investment securities held to maturity	1,619,313	1,135,137
Net acquisitions of investments securities available-for-sale	(2,107,575)	(2,794,020)
Net cash used in investing activities	**(849,792)**	**(1,954,509)**
Cash flows from financing activities		
Dividends paid	(2,283,005)	(2,210,888)
Net cash used in financing activities	**(2,283,005)**	**(2,210,888)**
Net increase in cash and cash equivalents	**(4,391,333)**	**10,927,839**
Cash and cash equivalents at 1 January	27,269,197	16,341,358
Effect of exchange rate fluctuations on cash and cash equivalents held	-	-
Cash and cash equivalents at 31 December	**22,877,864**	**27,269,197**

The notes on pages 6 to 59 are an integral part of these financial statements.
On behalf of the Bank, these financial statements are signed on 5 March 2018 by:

Silvio Pedrazzi
Chief Executive Officer

Julian Cela
Chief Financial Officer

Notes to the financial statements for the year ended 31 December 2017

1. Reporting entity

Intesa Sanpaolo Bank Albania Sh.a, (the “Bank”), is a company domiciled in Albania. The Bank’s registered office is at “Ismail Qemali” street, no.27, and operates through a network of 31 branches and agencies, located in different cities of Albania: Tirana, Durres, Vlora, Elbasan, Fier, Berat, Gjirokastra, Korca, Lushnja, Shkoder, Lezhe, Kavaje (2016: 31 branches and agencies).

The Bank was incorporated on May 1998, and is primarily involved in banking activities in Albania. The Bank started operations on 24 September 1998.

The Bank had 576 employees as at 31 December 2017 (2016: 578).

2. Basis of accounting

(a) Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB). These financial statements were authorized for issue by Management on 22 February 2018 for approval by the Supervisory Board.

(b) Basis of measurement

The financial statements are prepared on the amortized or historical cost basis except for Available-for-sale financial assets and own used properties, which are stated at fair value.

(c) Functional and presentation currency

The financial statements are presented in Lek, which is the Bank’s functional and presentation currency. Except as indicated otherwise, financial information presented in Lek has been rounded to the nearest thousand.

3. Significant accounting policies

The accounting policies set out below have been consistently applied to all periods presented in these financial statements by the Bank, except for the changes explained in Note 3(a).

(a) Changes in accounting policy

As at 31 December 2017, the Bank elected to measure its own used properties at fair value. The change was considered as voluntary and based on IAS 8 with the transition from amortized cost criterion to the revaluation model, have been accounted prospectively.

(b) Foreign currency

Transactions in foreign currencies are translated into the functional currency at the spot exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortized cost in foreign currency translated at the spot exchange rate at the end of the year. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated to the functional currency at the spot exchange rate at the date that the fair value was determined.

Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of the transaction. Foreign currency differences arising on retranslation are generally recognized in profit or loss. Foreign currency differences arising from translation of available-for-sale equity instruments are recognized in other comprehensive income. Foreign currency differences arising from retranslation of transactions with owners are recorded directly in equity.

(c) Interest

Interest income and expense are recognized in profit or loss using the effective interest method. The ‘effective interest rate’ is the rate that exactly discounts estimated future cash payments and receipts through the expected life of the financial asset or liability (or where appropriate, a shorter period) to the carrying amount of the financial asset or liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instruments, but no future credit losses.

The calculation of effective interest includes all fees paid or received, transaction costs and discounts or premiums that are an integral part of the effective interest rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Interest income and expense presented in the statement of profit and loss include:

- Interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis; and
- Interest on available-for-sale investment securities calculated on an effective interest basis.

(d) Fees and commissions

Fees, commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate (see (c)).

Other fee and commission income, including account servicing fees, investment management fees, sales commission and placement fees are recognized as the related services are performed. If a loan commitment is not expected to result in a draw-down of a loan, then the related loan commitment fees are recognized on a straight line basis over the commitment period.

Other fee and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

3. Significant accounting policies (continued)

(e) Leases

The determination of whether an arrangement is a lease or contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease. Lease incentives received are recognized as an integral part of the total lease expense, over the term of the lease. If the Bank is the lessor in a lease agreement that transfers substantially all of the risks and rewards incidental to ownership of the asset to the lessee, then the arrangement is classified as a finance lease and a receivable equal to the net investment in the lease is recognised and presented within loans and advances. All leases are classified as operating leases.

(f) Income Tax

Income tax expense comprises current and deferred tax. It is recognized in profit or loss except to the extent that it relates to items recognized directly in equity or in OCI. Interest and penalties related to income taxes, including uncertain tax treatments, are accounted for under IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

(i) Current Tax

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. The amount of current tax payable or receivable is the best estimate of the tax amount expected to be paid or received that reflects uncertainty related to income taxes, if any. It is measured using tax rates enacted or substantively enacted at the reporting date.

Current tax assets and liabilities are offset only if certain criteria are met.

(ii) Deferred Tax

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax assets are recognized for unused tax losses and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Future taxable profits are determined based on the reversal of relevant taxable temporary differences. If the amount of taxable temporary differences is insufficient to recognize a deferred tax asset in full, then future taxable profits, adjusted for reversals of existing temporary differences, are considered, based on the business plans. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized; such reductions are reversed when the probability of future taxable profits improves.

Unrecognized deferred tax assets are reassessed at each reporting date and recognized to the extent that it has become probable that future taxable profits will be available against which they can be used.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date.

The measurement of deferred tax reflects the tax consequences that would follow from the manner in which the Bank expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset only if certain criteria are met.

3. Significant accounting policies (continued)

(g) Financial assets and financial liabilities

(i) Recognition

The Bank initially recognizes loans and advances, deposits and borrowings on the date on which they are originated. Regular purchases and sales of financial assets are recognized on the trade date on which the Bank commits to purchase or sell the asset. All other financial assets and liabilities are initially recognized on the trade date on which the Bank becomes a party to the contractual provisions of the instrument. A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit and loss, transaction costs that are directly attributable to its acquisition or issue.

(ii) Classification

Financial Assets

The Bank classifies its financial assets in one of the following categories:

- loans and receivables, subsequently measured at amortized cost;
- held-to-maturity, subsequently measured at amortized cost; or
- available-for-sale, subsequently measured at fair value.

See notes 3 (g), (h) and (i).

Financial liabilities

The Bank classifies its financial liabilities as other financial liabilities, subsequently measured at amortized cost.

See notes 3 (o) and (p).

(iii) De-recognition

Financial Assets

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognized) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in other comprehensive income is recognized in profit or loss. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognized as a separate asset or liability.

The Bank enters into transactions whereby it transfers assets recognized on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognized. Examples of such transactions are securities lending and sale and repurchase transactions.

3. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(iii) De-recognition (continued)

Financial liabilities

The Bank derecognizes a financial liability when its contractual obligations are discharged, cancelled or expire.

(iv) Off-setting

Financial assets and liabilities are offset and the net amount is presented in the statement of financial position when, and only when, the Bank has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from Bank's similar transactions such as in the trading activity.

(v) Amortized cost measurement

The amortized cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between the initial amount recognized and the maturity amount, minus any reduction for impairment.

(vi) 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 in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognized in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is entirely supported by observable market data or the transaction is closed out.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Bank recognizes transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

3. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(vii) Identification and measurement of impairment

At each reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss, are impaired. A financial asset or a group of financial assets is individually impaired when objective evidence or judgmental criteria demonstrate that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows on the asset(s) that can be estimated reliably.

Objective evidence that financial assets are impaired can include: significant financial difficulty of the borrower or issuer; default or delinquency by a borrower; restructuring of a loan or advance by the Bank because of financial difficulties experienced by the client and on terms which the Bank would not otherwise consider; indications that a borrower or issuer will enter bankruptcy; the disappearance of an active market for a security, or other nationally or locally observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group; or a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets.

The Bank considers evidence of impairment for loans and advances and held-to-maturity investment securities at both specific asset and collective level. All individually significant loans and advances and held-to-maturity investment securities are assessed for individual impairment. Those financial assets found not to be individually impaired are then collectively assessed for impairment by grouping together loans and advances with similar risk characteristics.

In assessing collective impairment, the Group uses statistical modelling of historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, and makes an adjustment if current economic and credit conditions are such that the actual losses are likely to be greater or lesser than is suggested by historical trends. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets measured at amortized cost are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in profit or loss and reflected in an allowance account against loans and advances. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss. Expected cash flows from impaired loans and advances include the estimated proceeds from the realization of collateral. Proceeds from collateral are estimated by applying discounts (haircuts) to estimated market values and establishing a timeframe for collection, depending on the collateral type.

When possible the Bank seeks to restructure/renegotiate loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. If the terms of a financial asset are renegotiated or modified, or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then the asset is assessed for individual impairment. All customers with any restructured credit remain so for a period of at least 2 years from the restructuring date, independently from the payments performed pursuant to the new terms of repayments. Management continuously reviews renegotiated loans to ensure all criteria are met and to ensure future payments are likely to occur.

Impairment losses are recognized in profit or loss and are reflected in an allowance account against loans and advances or available-for-sale investment securities, if any. When an event occurring after the impairment was recognized causes the amount of impairment on loans and advances loss to decrease, the decrease in impairment loss is reversed through profit or loss.
In case of investments classified as available-for-sale, a significant or prolonged decline in the fair value of the instruments below its cost is considered in determining whether the assets are impaired. Impairment losses on available-for-sale investment securities are recognized by reclassifying the losses previously recognized in other comprehensive income to profit or loss. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss recognized previously in profit or loss.

3. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(vii) Identification and measurement of impairment (continued)

Changes in impairment provisions attributable to the application of the effective interest method are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized, then the impairment loss is reversed through profit or loss; otherwise any increase in fair value is recognized through other comprehensive income. Any subsequent recovery in the fair value of an impaired available-for-sale equity security is always recognized in other comprehensive income.

(h) Cash and cash equivalents

'Cash and cash equivalents' include notes and coins on hand, balances with banks, unrestricted balances held with central banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments. Cash and cash equivalents are classified as loans and receivables and carried at amortized cost in the statement of financial position.

(i) Loans and advances

'Loans and advances to banks and customers' are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. Loans and advances are initially measured at fair value and subsequently measured at amortized cost plus incremental direct transaction costs, using the effective interest method. After initial measurement, they are subsequently measured at amortized cost using effective interest rate, less allowance for impairment. The amortization is included in the interest income in profit or loss. The losses arising from impairment are recognized in profit or loss in net impairment loss on financial assets.

(j) Investment securities

Investment securities are initially measured at fair value plus, in case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as either held-to-maturity or available-for-sale.

(i) Held-to-maturity

'Held-to-maturity investments' are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity, which are not designated at fair value through profit or loss or available-for-sale.

Held-to-maturity investments are carried at amortized cost using the effective interest method less any impairment losses. Any sale or reclassification of more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale, and prevent the Bank from classifying investment securities as Held-to-maturity for the current and following two financial years.

(ii) Available-for-sale

'Available-for-sale investments' are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. Available-for-sale investments comprise equity securities and debt securities. Unquoted equity securities whose fair value cannot be measured reliably are carried at cost. All other available-for-sale investments are measured at fair value after initial recognition. Interest income is recognised in profit or loss using the effective interest method.

3. Significant accounting policies (continued)

(j) Investment securities (continued)

Foreign exchange gains or losses on available-for-sale debt security investments are recognized in profit or loss. Impairment losses are recognized in profit or loss. Other fair value changes, other than impairment losses, are recognized in other comprehensive income and presented in the fair value reserve within equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to profit or loss.

A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it would otherwise have met the definition of loans and receivables and if the Bank has the intention and ability to hold that financial asset for the foreseeable future or until maturity.

(k) Property and equipment

(i)Recognition and measurement

Equipment are measured at cost less accumulated depreciation and any accumulated impairment losses. Property are measured at revalued amounts, being the fair value at the date of revaluation less accumulated depreciation and any accumulated impairment losses (see Note 12). If significant parts of an item of property or equipment have different useful lives, then they are accounted for as separate items (major components) of property and equipment. Any gain or loss on disposal of an item of property and equipment is recognised within other income in profit or loss.

(ii) Subsequent costs

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Group. Ongoing repairs and maintenance are expensed as incurred.

(iii)Depreciation

Depreciation is calculated to write off the cost of items of property and equipment less their estimated residual values using the straight-line method over their estimated useful lives, and is generally recognised in profit or loss. Land and art work are not depreciated.

The estimated useful live for the current and comparative periods are as follows:

	2017	2016
• Buildings	33 years	20 years
• IT and Electrical Equipment	4 to 8 years	4 to 8 years
• Furniture	3 to 10 years	3 to 10 years
• Other non-electrical assets	5 years	5 Years

(l) Intangible assets

Software, licenses and trademarks compose intangible assets and are stated at cost less accumulated amortization. Subsequent expenditure on intangible assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred. Amortization is charged on a straight-line basis in profit or loss over the estimated useful lives, from the date that it is available for use. The estimated useful lives for the current and comparative periods are as follows:

	2017	2016
• Software	5 years	5 years
• Licenses and trademarks	10 years	10 years

(m) Investment property

Investment property is initially measured at cost and subsequently at fair value, with any change therein recognised in profit or loss within other income.When the use of a property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

3. Significant accounting policies (continued)

(n) Inventory

Inventory comprises repossessed assets acquired through enforcement of security over non-performing loans and advances to customers which do not earn rental, and are not used by the Bank and are intended for disposal in a reasonably short period of time, without significant restructuring. Repossessed assets are measured at the lower of cost and net realizable value and any write-down is recognized in the profit or loss**.**

(o) Impairment of non-financial assets

At each reporting date, the Bank reviews the carrying amount of its non-financial assets (other than inventory and deferred tax assets) to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognized if the carrying amount of an asset exceeds its recoverable amount. The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate which reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognized in profit or loss. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(p) Deposits

Deposits are the Bank's sources of debt funding.

Deposits are initially measured at fair value plus directly attributable transaction costs, and subsequently measured at their amortized cost using the effective interest method.

When the Bank sells a financial asset and simultaneously enters into an agreement to repurchase the asset (or a similar asset) at a fixed price on a future date ("repo" or "stock lending"), the arrangement is accounted for as a deposit, and the underlying asset continues to be recognized in the Bank's financial statements.

(q) Provisions

A provision is recognized if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money, and where appropriate, the risks specific to the liability.

(r) Bank levies

A provision for bank levies is recognised when the condition that triggers the payment of the levy is met. If a levy obligation is subject to a minimum activity threshold so that the obligating event is reaching a minimum activity, then a provision is recognised when that minimum activity threshold is reached.

(s) Employee benefits

(i) Defined contribution plans

The Bank makes only compulsory social security contributions that provide pension benefits for employees upon retirement. In Albania, the local authorities are responsible for providing the legally set minimum threshold for pensions under a defined contribution pension plan. The Bank's contributions to the benefit pension plan are expensed in profit or loss as incurred.

(ii) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

3. Significant accounting policies (continued)

(t) New standards and interpretation not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2017. However, the Bank has not early applied the following new or amended standards in preparing these financial statements.

IFRS 9 – Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments. IFRS 9 is effective for annual periods beginning on or after 1 January 2018. It replaces IAS 39 Financial Instruments: Recognition and Measurement, that governed the classification and measurement of financial instruments up to 31 December 2017.

Based on assessments undertaken to date, the total estimated adjustment of the adoption of IFRS 9 on the opening balance of the Bank's equity at 1 January 2018 is approximately Lek 949 million, and it is related only to impairment requirements (see (ii)) representing:

— a reduction of approximately Lek 675 million related to loans and advances (performing and non-performing);

— a reduction of approximately Lek 265 million related to performing debt securities; and

— a reduction of approximately Lek 8.6 million related to off balance sheet items.

No assessment was performed with regard to deferred tax implications.

IFRS 9 is divided into the three sectors of classification and measurement of financial instruments, impairment, and hedge accounting.

(i) Classification – Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics. IFRS 9 includes three principal classification categories for financial assets: measured at amortised cost, Fair Value through Other Comprehensive Income (FVOCI) and Fair Value through Profit or Loss (FVTPL). It eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale.

Financial assets may be entered in the first two categories and therefore measured at amortised cost or fair value through other comprehensive income only if there is proof that they give rise to cash flows that are "solely payment of principal and interest" (SPPI test).
Equities are always entered in the third category and measured at fair value through profit and loss, except for when the entity opts (irrevocably, on first time recognition) to present the changes in value of shares not held for trading in an equity reserve that can never be transferred to profit and loss, even on disposal of the instrument (Financial assets measured at fair value through other comprehensive income without recycling).
No significant changes have been introduced for the classification and measurement of financial liabilities. The only change is the treatment of own credit risk: for financial liabilities designated at fair value (fair value option), the Standard states the changes in the fair value of the liabilities attributable to variations in own credit risk shall be recognised in net equity, unless that treatment creates and exaggerates an accounting mismatch in the period profit, while the residual sum of changes in the fair value of liabilities shall be recognised in the income statement (profit and loss).

Business model assessment

The Bank has made an assessment of the objective of the business model in which a financial asset is held at a portfolio level. Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment whether contractual cash flows are solely payments of principal and interest

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

3. Significant accounting policies (continued)

(t) New standards and interpretation not yet adopted (continued)

IFRS 9 – Financial Instruments (continued)

Impact assessment

The standard will affect the classification and measurement of financial assets held as at 1 January 2018 as follows.

- Loans and advances to banks and to customers that are classified as loans and receivables and measured at amortised cost under IAS 39 will in general also be measured at amortised cost under IFRS 9.
- Held-to-maturity investment securities measured at amortised cost under IAS 39 will in general also be measured at amortised cost under IFRS 9.
- Debt investment securities that are classified as available-for-sale under IAS 39 may, under IFRS 9, be measured at amortised cost, FVOCI or FVTPL, depending on the particular circumstances.

(ii) Impairment

With reference to impairment, assets measured at amortised cost or at fair value though other comprehensive income (other than equities) shall be subject to the new model based on expected loss, replacing the current incurred loss model, to recognise losses more promptly.
IFRS 9 replaces the ‘incurred loss’ model in IAS 39 with a forward-looking ‘expected credit loss’ model. This requires considerable judgement over how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. The introduction of the new regulations on impairment means:

– allocation of performing assets in different credit risk stages (staging), with corresponding adjustments based on 12-month expected losses (Stage 1), or lifetime (Stage 2) in the event of significant increase in credit risk (SICR) determined by a comparison of the Probability of Default at initial recognition and that at reporting date;
– allocation of non-performing assets in Stage 3, always adjusted according to lifetime expected losses;
– including forward-looking information in the calculation of Expected Credit Losses (ECL), also connected to changes in the macro-economic scenario.

Last, regarding hedge accounting, the new model – that does not apply to macro-hedging – aims to align accounting recognition with risk management and reinforce the disclosure of the risk management activities of the entity preparing the financial statements.

The approach to First Time Adoption (FTA) of IFRS 9

In the second half of 2017, the Bank began a “parallel running” of application of the new Standard that involved a modular, and increasingly complete, approach according to the availability of information and the necessary technological support. The aim of the parallel running is to check the correct implementation of the technology supporting the management of the changes introduced by IFRS 9 and a more accurate estimation of the impacts of FTA.

In the first quarter of 2017, the European Central Bank (ECB) conducted a “Thematic Review”, also involving Intesa Sanpaolo Group, focussed on the implementation of IFRS 9. Intesa Sanpaolo has received the final conclusions of the ECB stating that, in general, implementation of the new Standard is in line with the expectations of the Authority. The conclusions also contain some suggestions and recommendations (“findings”) already included in the implementation strategy for the new Standard. The findings refer mainly to the definition of internal policies regulations that – as usual – was concluded at the end of the project. In brief, the findings refer to the need to integrate procedures and define in detail internal rules and regulations (in particular those relating to the review and updating of approaches to determine SICR and calculation od expected loss) that are in force at the introduction of IFRS 9, and underline the importance of Internal Validation and back-testing. In this context, internal regulations – especially the Group Accounting Policies, the new Impairment Policy and the framework of the Group business model – have been updated and approved by the competent governance levels.

3. Significant accounting policies (continued)

(t) New standards and interpretation not yet adopted (continued)

IFRS 9 – Financial Instruments (continued)

Measurement of ECLs

ECLs are a probability-weighted estimate of credit losses and will be measured as follows:

– financial assets that are not credit-impaired at the reporting date: the present value of all cash shortfalls – i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive;

- financial assets that are credit-impaired at the reporting date: the difference between the gross carrying amount and the present value of estimated future cash flows;

Inputs into measurement of ECLs

The key inputs into the measurement of ECLs are: probability of default (PD); loss given default (LGD); and exposure at default (EAD). These parameters are derived from internally developed statistical models and other historical data that leverage regulatory models. They will be adjusted to reflect forward-looking information.

The actual impact of adopting IFRS 9 on 1 January 2018 may change because:

- IFRS 9 requires the Bank to revise its accounting processes and internal controls and these changes are not yet complete;
- although parallel runs were carried out in the second half of 2017, the new systems and associated controls in place have not been operational for a more extended period;
- the Bank has not finalised the testing and assessment of controls over its new IT systems and changes to its governance framework;
- the new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Bank finalises its first financial statements that include the date of initial application.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 is effective for annual periods beginning on or after 1 January 2018 with earlier application permitted. The new Standard provides a comprehensive framework that replaces existing revenue recognition guidance in IFRS, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes. Entities will adopt a five-step model to determine when to recognise revenue, and at what amount. The new model specifies that revenue should be recognised when (or as) an entity transfers control of goods or services to a customer at the amount to which the entity expects to be entitled. Depending on whether certain criteria are met, revenue is recognised:
over time, in a manner that depicts the entity's performance; or
at a point in time, when control of the goods or services is transferred to the customer.

IFRS 15 also establishes the principles that an entity shall apply to provide qualitative and quantitative disclosures which provide useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer.

Although it has not yet fully completed its initial assessment of the potential impact of IFRS 15 on the Bank's financial statements, management does not expect that the new Standard, when initially applied, will have material impact on the Bank's financial statements. The timing and measurement of the Bank's revenues are not expected to change under IFRS 15 because of the nature of the Bank's operations and the types of revenues it earns. However, this assessment may change as the Bank finalizes its processes and accounting policies conform to IFRS 15 requirements.

3. Significant accounting policies (continued)

(t) New standards and interpretation not yet adopted (continued)

IFRS 16 Leases

IFRS 16 replaces existing leases guidance, including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement Contains a Lease, SIC-15 Operating Leases – Incentives, and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. The new Standard introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases. The Standard is effective for annual periods beginning on or after 1 January 2019 with early adoption permitted for entities that apply IFRS 15 at or before the date of initial application of IFRS 16.

The Bank has completed an initial assessment of the potential impact of IFRS 16 on its financial statements but has not yet completed its detailed assessment. The actual impact of applying IFRS 16 on the financial statements in the period of initial application will depend on future economic conditions, including the Bank's discount rate at 1 January 2019, the composition of the Bank's lease portfolio at that date, the Bank's latest assessment of whether it will exercise any lease renewal options and the extent to which the Company chooses to use practical expedients and recognition exemptions.

So far, the most significant impact identified is that the Bank will recognise new assets and liabilities for its operating leases of vehicles. As at 31 December 2017, the Bank's future undiscounted lease payments under the contractual terms of existing operating leases amounted to Lek 339 million.

For the future undiscounted minimum lease payments under non-cancellable operating leases as at 31 December 2017 see Note 32. In addition, the nature of expenses related to those leases will now change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities.

Other standards

The following new or amended standards are not expected to have a significant impact on the Bank's financial statements:

- Annual Improvements to IFRSs 2014-2016 Cycle – Amendments to IFRS 1 and IAS 28;
- Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2);
- Transfers of Investment Property (Amendments to IAS 40);
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28);
- IFRIC 22 Foreign Currency Transactions and Advance Consideration;
- IFRIC 23 Uncertainty over Income Tax Treatments;
- Prepayment Features with Negative Compensation (Amendments to IFRS 9);
- Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28);
- Annual Improvements to IFRS 2015-2017 Cycle – Amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23);
- Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)

4. Financial Risk Management

The Bank is exposed to the following risks from financial instruments:

(a) credit risk
(b) liquidity risk
(c) market risk
(d) operational risk

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

Risk management framework

The Board of Directors of the Bank has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Bank's Governance Committees (Executive Directors Committee, Credit Committee, Financial Risk Committee, Operational Risk Committee, Credit Risk Governance Committee, Problematic Loans Committee and other committees) that have the authority for decision-making in their specified areas.

Risk Management Division is responsible for developing and monitoring the Bank's risk management policies in these areas. All the Bank's committees have both executive and non-executive members and report regularly to the Board of Directors on their activities. The Bank's risk management policies are established to identify and analyze the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered.

(a) Credit Risk

In the normal course of its business, the Bank is exposed to credit risk on its loans and advances to customers and financial institutions, investment securities and other off-balance-sheet items. Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers, debt securities, on funds with other financial institutions and other off-balance sheet items. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk). The Bank manages its exposure to credit risk on a regular basis by closely monitoring credit limits, its loan portfolio and concentration of exposure.

Management of credit risk

The Board of Directors has delegated responsibility for decision-making to Committees in Credit Area. The Risk Management Division, reporting to the CEO, is responsible for the oversight and management of the Bank's credit risk, including:

- *Formulating credit policies* in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- *Reviewing and assessing credit risk*. The Bank's Underwriting Department assesses all credit exposures, before facilities are committed to customers by the Bank. Renewals and reviews of facilities are subject to the same review process.
- *Limiting concentrations of exposure* to counterparties, geographies and industries (for loans and advances), and by issuer, credit rating band, market liquidity and country (for investment securities).

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

- *Developing and maintaining the Bank's risk classifications* in order to categorize exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The risk classification is used in determining where impairment may be required against specific credit exposures.

  According to the Bank's methodology, all exposures are classified between Performing and Non- Performing exposures (including Past Due, Unlikely to Pay and Doubtful). The Bank classifies the Non-Performing portfolio by analyzing the exposures based on a set of rules harmonized with the guidelines of Intesa Sanpaolo Group. These rules include objective evidence being: breach of contract (such as default or delinquency in interest or principal payments); significant financial difficulty of the borrower; and other significant adverse financial information relating to the customer.

- *Reviewing compliance* of business units with agreed exposure limits, including those for selected industries and product types. Detailed analyses are provided monthly to the Problem Assets Committee on the credit quality of customer exposures and specific actions are proposed.
- *Providing advice, guidance and specialist skills* to business units to promote best practice throughout the Bank in the management of credit risk.

Maximum Exposure to Credit Risk

The following table shows the current maximum exposure to credit risk for the applicable components of statement of financial position:

	Gross Maximum Exposure	
	31 December 2017	**31 December 2016**
Cash and cash equivalents (excluding cash on hand)	21,585,207	25,968,849
Loans and advances to banks	20,171,066	17,106,968
Financial assets available-for-sale	9,423,008	7,251,448
Financial assets held-to-maturity	49,110,119	50,729,433
Loans and advances to customers	46,557,253	42,542,151
Sundry debtors	62,045	57,462
Total on-balance-sheet risk	**146,908,698**	**143,656,311**
Undrawn credit commitments	5,832,819	4,977,785
Letters of credit	3,025,244	355,827
Guarantees in favor of customers	3,930,155	4,664,841
Total credit related commitments	**12,788,218**	**9,998,453**
Total Credit Risk Exposure	**159,696,916**	**153,654,764**

Where financial assets are recorded at fair value, the amounts shown represent the current credit risk exposure, but not the maximum risk exposure that could arise in the future as a result of changes in values. The Bank makes available to its customers guarantees which may require that the Bank makes payments on their behalf and enters into commitments to extend credit lines to secure their liquidity needs. Letters of credit and guarantees commit the Bank to make payments on behalf of customers in the event of a specific act or event, generally related to the import or export of goods, and payment and performance guarantees. Such commitments expose the Bank to similar credit risks, which are mitigated by the same control processes and policies. Every month, the Bank assesses the credit related commitments for impairment. Amounts subject to individual impairment assessment are non-cancellable commitments granted to non-performing customers or customers with restructured credit facilities.

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

Credit Quality by class of financial assets

The tables below show the credit quality of the financial assets exposed to credit risk, based on the Bank's internal ratings. In the Past Due classification below, loans and advances include exposures more than 90 days past due and collectively impaired. The collective impairment is allocated in accordance with the default rate of the group with similar credit risk characteristics where customers belong. The financial assets in the tables below are gross of impairment allowances for both financial years ended as at 31 December 2017 and 31 December 2016:

31 December 2017	Neither past due nor individually impaired	Past due, not individually impaired	Individually Impaired	Total
Cash and cash equivalents (excluding cash on hand)	21,585,207	-	-	21,585,207
Loans and advances to banks	20,171,066	-	-	20,171,066
Commercial lending	36,587,751	296,010	2,614,224	39,497,985
Mortgage lending	6,516,287	365,363	305,318	7,186,968
Consumer lending	1,792,917	64,054	362	1,857,333
Loans and advances to customers:	44,896,955	725,427	2,919,904	48,542,286
	86,653,228	**725,427**	**2,919,904**	**90,298,559**
Listed financial institutions	6,771,662	-	-	6,771,662
Unlisted financial institutions	2,651,346	-	-	2,651,346
Financial Assets available-for-sale:	9,423,008	-	-	9,423,008
Listed companies	4,267,587	-	-	4,267,587
Unlisted Government securities	44,842,532	-	-	44,842,532
Financial Assets held to maturity:	49,110,119	-	-	49,110,119
Total	**145,186,355**	**725,427**	**2,919,904**	**148,831,686**

31 December 2016	Neither past due nor individually impaired	Past due, not individually impaired	Individually Impaired	Total
Cash and cash equivalents (excluding cash on hand)	25,968,849	-	-	25,968,849
Loans and advances to banks	17,106,968	-	-	17,106,968
Commercial lending	31,954,224	365,585	4,719,307	37,039,116
Mortgage lending	5,931,119	647,781	468,523	7,047,423
Consumer lending	1,107,970	44,177	1,277	1,153,424
Loans and advances to customers:	38,993,313	1,057,543	5,189,107	45,239,963
	82,069,130	**1,057,543**	**5,189,107**	**88,315,780**
Listed financial institutions	6,163,714	-	-	6,163,714
Unlisted financial institutions	1,087,734	-	-	1,087,734
Financial Assets available-for-sale:	7,251,448	-	-	7,251,448
Listed companies	5,071,447	-	-	5,071,447
Unlisted Government securities	45,657,986	-	-	45,657,986
Financial Assets held to maturity:	50,729,433	-	-	50,729,433
Total	**140,050,011**	**1,057,543**	**5,189,107**	**146,296,661**

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

Credit Quality by class of financial assets (continued)

Loans and advances to customers are the only class of financial assets resulting in non-performing categories which are not necessarily subject to individual impairment assessment. During 2016, the Bank complied with the "Handbook on the Rules and Criteria for Classification of Credit Exposure for Consolidation Purposes" issued by the Group classifying loans and advances to customers in four main categories being a) performing; b) past due; c) unlikely to pay and d) doubtful.

Assessments for impairment are made in accordance with the ISP Individual Assessment Handbook according to which the performing category is subject to collective assessment for impairment, while the other three categories (non-performing) can be subject to either individual or collective assessment for impairment. A significance threshold is applied all non performing categories, based on which an individual assessment for impairment is performed for all exposures exceeding the threshold. Assessment on a portfolio basis using the statistical approach for impairment, is applied to the all non performing categories not exceeding the significance threshold.

An ageing analysis of loans considered neither past due not individually impaired and past due not individually impaired as at 31 December 2017 and 2016 is shown in the table below:

31 December 2017	Less than 30 days	31 to 60 days	61 to 90 days	Total
Loans and advances to customers:				
Commercial Lending	35,902,643	406,203	278,905	36,587,751
Mortgage Lending	6,259,560	143,697	113,030	6,516,287
Consumer Lending	1,755,114	24,798	13,005	1,792,917
Total	**43,917,317**	**574,698**	**404,940**	**44,896,955**

31 December 2016	Less than 30 days	31 to 60 days	61 to 90 days	Total
Loans and advances to customers:				
Commercial Lending	31,423,059	217,310	313,855	31,954,224
Mortgage Lending	5,528,523	293,809	108,787	5,931,119
Consumer Lending	1,079,297	21,414	7,259	1,107,970
Total	**38,030,879**	**532,533**	**429,901**	**38,993,313**

31 December 2017	91 to 180 days	more than 180 days	Total
Loans and advances to customers:			
Commercial lending	5,050	290,960	296,010
Mortgage lending	126,307	239,056	365,363
Consumer lending	19,297	44,757	64,054
Total	**150,654**	**574,773**	**725,427**

31 December 2016	91 to 180 days	more than 180 days	Total
Loans and advances to customers:			
Commercial lending	6,900	358,685	365,585
Mortgage lending	146,572	501,209	647,781
Consumer lending	14,411	29,766	44,177
Total	**167,883**	**889,660**	**1,057,543**

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

Credit Quality by class of financial assets (continued)

Impaired loans and securities

Impaired loans and securities are the ones for which the Bank determines that it is probable that it will be unable to collect all principal and interest due, according to the contractual terms of the agreement(s). The Bank classifies loans and advances to customers in performing and non-performing categories as described above and performs impairment tests for all loans that show objective evidence for impairment, estimating their discounted future cash flows and comparing them with the respective carrying amount of the loans. Within the non-performing categories, for individually significant exposures, individual assessment for impairment is performed. While for the non-performing exposures which are not individually significant an individual assessment on a portfolio basis is applied. Loans that do not show objective evidence for individual impairment are assessed collectively for impairment using indicative information on annual default dates, loss rates and loss confirmation period compiled by the Bank for the groups of loans with similar risk characteristics. Collective impairment is also applied to the non-performing individually significant exposures for which full recovery is expected under the individual assessment approach and to the exposures which are tested individually, but resulted with no need for individual impairment.

The impairment testing process for any individually significant securities, denominated in foreign currency, is triggered if the fair value is less than the carrying amount or if the issuer is delinquent in its debtor obligations or defaults on payments as demonstrated by a default, bankruptcy proceedings or a delinquency in interest or principal payments. Where any one of these events occurs, given the gravity and the irreversibility of the confirmed situation, an impairment loss should be recorded directly. If the fair value is not more than 20% less than the carrying amount and no other impairment indicators are identified no further impairment test is performed.

The impairment test is performed according to the rules defined in the ISP Group accounting policy.

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

Credit Quality by class of financial assets (continued)

Both collective assessment and individual assessment on portfolio basis are approaches to impairment evaluation based on statistical methods by using credit risk parameters which are estimated based on historical data for homogenous groups of assets.

Allowances for impairment

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio.

The main components of this allowance are a specific loss component that relates to individually significant exposures, as well as collectively assessed and less significant exposures, and a collective loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred, but have not been identified on loans subject to individual assessment for impairment.

The table below shows the net loans and advances to customers categorized within two main groups: Individually and collectively Impaired.

	Net Exposure to Loans and advances to customers	
Individually impaired	**31 December 2017**	**31 December 2016**
Gross amount	2,919,904	5,189,107
Allowance for impairment	(1,368,266)	(2,139,442)
Carrying amount	**1,551,638**	**3,049,665**
Collectively impaired		
Gross amount	45,622,382	40,050,856
Allowance for impairment	(616,767)	(558,370)
Carrying amount	**45,005,615**	**39,492,486**
Total carrying amount on Loans and advances to customers	**46,557,253**	**42,542,151**

Separate movements for both individual and collective impairments are presented in Note 11. Set out below is an analysis of the gross and net (of allowances for impairment) amounts of individually impaired loans by risk classification:

	Individually Impaired Loans and advances to customers	
	Gross	**Net**
31 December 2017		
Performing	-	-
Past Due	-	-
Unlikely to Pay	2,201,187	1,162,624
Doubtful	718,717	389,014
Total	**2,919,904**	**1,551,638**
31 December 2016		
Performing	-	-
Past Due	108,100	85,903
Unlikely to Pay	3,005,664	1,649,999
Doubtful	2,075,343	1,313,763
Total	**5,189,107**	**3,049,665**

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

Set out below is the carrying amount of restructured loans and advances to customers, net of impairment allowances, by product:

	31 December 2017	31 December 2016
Commercial lending	2,194,366	1,560,093
Mortgage lending	145,679	148,285
Consumer	543	-
Total	**2,340,588**	**1,708,378**

Write-off policy

The Bank writes off a loan (and any related allowances for impairment losses) when the Bank's Board of Directors determines that the loans are uncollectible. This is generally the case when the Board of Directors determines that significant changes in the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. The loan is classified as lost for regulatory reporting purpose for a period of at least 3 years. The Bank's policy is also in compliance with the amended Regulation no.62 dated 14.09.2011 "On Administration of Credit Risk for Banks and Foreign Banks Subsidiaries".

The estimated cash flows derived from the collateral, including guarantees securing the exposures, are usually the main source of future cash flows from non-performing loans. Some of the valuation parameters used for the calculation are:

- *Realizable value of collaterals*, which is estimated by reducing the appraised market value of the collateral with a discount factor. This takes into account the characteristics of similar groups of collaterals. It presumes an average recoverable value of specific collateral, based on the Bank's experience.
- *Timing of the expected cash flow*, which represents the expected recovery time (in years) for a specific type of collateral.

The recovery costs are deducted from estimated future cash flows. Collateral, generally, is not held over loans and advances to financial institutions, except when securities are held as part of reverse repurchase and securities borrowing activity. Usually, collateral is not held against investment securities, and no such collateral was held at 31 December 2017 and 2016. Estimates of fair value are based on the value of collateral assessed at the time of borrowing and are updated every three years. An estimate of the undiscounted and discounted fair value of collaterals and other security enhancements held against financial assets is shown below:

	Collateral of Loans and advances to customers 31 December 2017		Collateral of Loans and advances to customers 31 December 2016	
	Undiscounted	**Discounted**	**Undiscounted**	**Discounted**
Against individually impaired				
Property	6,141,972	1,904,991	10,509,462	3,117,472
Debt securities	-	-	729,694	88,135
Pledges and guarantees	1,330	532	94,414	8,778
Other	-	-	-	-
Total	**6,143,302**	**1,905,523**	**11,333,570**	**3,214,385**
Net carrying amount		**1,551,638**		**3,049,665**

The gross amount of collaterals includes the value of collaterals before testing the individually impaired loans. The net amount shows the present value of the same collaterals under this test.

Allowances for impairment

The table below shows the total amount of collaterals for the loans assessed under the category of collectively impaired. These collaterals do not undergo the same testing procedures as the above group. The information on the table below provides information on how much the collectively impaired loans and advances to customers are secured against their respective collaterals.

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

	Collateral of Loans and advances to customers 31 December 2017		Collateral of Loans and advances to customers 31 December 2016	
Against Collectively Impaired	**Undiscounted**	**Discounted**	**Undiscounted**	**Discounted**
Property	71,179,138	31,964,510	67,976,883	29,985,533
Pledges and guarantees	9,862,177	4,612,244	8,170,061	3,643,476
Cash	1,253,774	1,210,692	1,268,998	1,226,859
Debt securities	3,259,239	1,106,704	4,546,960	1,487,527
Other	-	-	-	-
Total	**85,554,328**	**38,894,150**	**81,962,902**	**36,343,395**
Net carrying amount		**45,005,615**		**39,492,486**

It is the Bank's policy to dispose of assets repossessed through the recovering process. The amounts collected from the proceeds are used to reduce or liquidate the carrying amount of the non-performing loans.

When the Bank holds repossessed assets in its ownership, their conversion into cash is the Bank's first aim, through marketing the properties for sale. If there is no satisfactory offer collected, the Bank's practice is to keep the asset for sale until receiving the best offer. The amounts of repossessed properties are disclosed in note 15. Depending on operational needs and the suitability of the asset to fulfill those needs, management may decide to make use of the property; in such cases a reclassification into property and equipment (see note 12) of the Bank is performed.

The Bank monitors concentration of credit risk by sector and location. An analysis of credit risk at the reporting date is shown below:

	Net Loans and advances to customers	
Concentration by sector	**31 December 2017**	**31 December 2016**
Services	19,654,305	17,012,528
Wholesale	8,195,500	9,016,937
Construction	2,486,583	2,802,533
Manufacturing	5,083,994	4,501,193
Real Estate	392,543	113,078
Other	2,083,305	1,289,844
Corporate	**37,896,230**	**34,736,113**
Mortgage	6,910,762	6,721,178
Consumer	1,750,261	1,084,860
Retail	**8,661,023**	**7,806,038**
Carrying amount	**46,557,253**	**42,542,151**

	Loans and advances to banks	
Concentration by sector	**31 December 2017**	**31 December 2016**
Bank	20,171,066	17,106,968
Carrying amount	**20,171,066**	**17,106,968**

	Financial Investments	
Concentration by sector	**31 December 2017**	**31 December 2016**
Sovereign	56,522,515	55,554,462
Bank	900,577	1,789,549
Other Financial l Institutions	1,110,035	636,870
Carrying amount	**58,533,127**	**57,980,881**

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

The credit quality of the maximum credit exposure of debt securities based on Moody's ratings, where applicable, and when the Moody's ratings for the exposure is not applicable the Bank uses the rating of the respective government is as follows:

	Financial Investments (debt securities)	
Sovereign	**31 December 2017**	**31 December 2016**
Rated Aaa	-	-
Rate Aa1	-	404,876
Rate Baa2	6,235,713	6,266,433
Rate B1	50,286,802	48,883,153
	56,522,515	**55,554,462**
Financial Institutions		
Rated Aaa	2,010,612	2,261,888
Rate Baa2		164,531
	2,010,612	**2,426,419**
Total carrying amount	**58,533,127**	**57,980,881**

Concentration of Credit Risk

The following concentrations of credit risk arise in the Bank's credit-risk portfolio.

	31 December 2017	**Exposure In %**	**31 December 2016**	**Exposure In %**
Republic of Albania securities	50,286,798	34%	48,883,153	34%
Balances with Central Bank of Albania	12,364,287	8%	12,235,288	9%
Total direct Albanian Sovereign risk	**62,651,085**	**42%**	**61,118,441**	**43%**
Largest bank	13,647,540	9%	13,224,058	9%
Largest customer	5,452,997	4%	5,715,588	4%
Total largest bank and customer	**19,100,537**	**13%**	**18,939,646**	**13%**
Total on-balance-sheet risk	**81,751,622**	**55%**	**80,058,087**	**56%**

The largest exposure toward the banks is exposure to the Group bank and the largest customer is a local state-owned company.

4. Financial Risk Management (continued)

(a) Credit Risk (continued)

Settlement risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honor its obligations to deliver cash, securities or other assets as contractually agreed. The settlement risk with financial institutions and government counterparties is included within a system of limits for all the transactions with such counterparties and is subject to daily monitoring, defined and regulated in the internal documents "ISBA Credit Autonomy Level" and "ISBA Rules for the management and maintenance of the FI-s limits" and the Central Bank of Albania regulation "On risk management arising from the large exposures of the Bank".

The Bank of Albania regulation "On risk management arising from the large exposures of Bank" was revised during 2014 and entered in force in March 2015. The Bank has been within the limits in accordance with Central Bank of Albania regulation up to 15 December 2017.

With the aim to prevent any breaches of local regulatory counterparty limits with Financial Institutions, generated by fluctuations of exchange rates, the bank has integrated warning level limits (soft limits), 23.4 % of regulatory capital for the exposures toward ISP Group and 18.7 % of regulatory capital for the exposures toward other Financial Institutions/Governments, as approved by FRCO on 24 January 2017.

During the year 2017, one breach of the soft limit related to ISP Exposure at the level of 23.44% (limit 23.4%) was reported. The bank decreased the nostros balances and entered within the limit the next day.

(b) Liquidity Risk

Liquidity risk is defined as the possibility that an institution is unable to meet its payment obligations due to its incapacity to liquidate assets or obtain adequate funding from the market (funding liquidity risk), or due to the difficulty of easily unwinding positions in financial assets without negatively and significantly affecting their price due to inadequate market depth or temporary market disruptions.

Management of liquidity risk

The Bank's approach to managing liquidity risk is to ensure, as much as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation. The Bank defines the guidelines for liquidity risk management and the contingency liquidity plan, which are subject to review by Group structures and approval by the Bank's Financial Risk Committee and Board of Directors. The Treasury and ALM Department is responsible for liquidity management and the Risk Management Division is responsible for monitoring indicators and verifying adherence to the limits.

The Bank's Regulation on Liquidity Risk Management is updated on 2017, approved from the Board of Director on September 2017. The new policy implements the latest regulatory provisions issued through the so-called 'Delegated Regulation' and by the Basel Committee (BCBS October 2014).

The Bank monitors liquidity, in accordance with this regulation, in order to manage its obligations when they fall due and activate emergency procedures in case of escalation.

A balanced ratio should be maintained between incoming sources and outflows, in both the short and medium-long term. This target is organized through the use of the following specific metrics "Liquidity Coverage Ratio up to 30 days" and "Net Stable Funding Ratio".

4. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

- **Liquidity Coverage Ratio (LCR)** up to 30 days**:** aims to ensure that the Bank maintains an adequate level of unencumbered high-quality liquid assets (HQLA) to meet its short term liquidity needs under liquidity stress scenario (LCR≥90%).
- **Net Stable Funding Ratio (NSFR):** aims to guarantee an adequate liquidity position over a medium/long-term time horizon. It establishes a minimum "acceptable" amount of funding over one year horizon in relation to the needs arising from the liquidity characteristics and the residual maturities of assets and off-balances exposures (NSFR≥90%).

Holding reserves of liquid assets (so-called Liquidity Buffer) is one of the main tools for mitigating liquidity risk. For the purpose of identifying and measuring this risk, both short and medium-long term, the classification of highly-liquid assets takes on crucial importance.

In its Liquidity Policy, the Bank projects a LCR indicator of up to 3 months by including the estimated market effect of specific acute liquidity tensions (at bank level) combined with a widespread and general market crisis, based on assumptions provided by the Group's guidelines.

A similar, but not identical, calculation is used to measure the Bank's compliance with the liquidity limits established by the Bank of Albania, which should be above 20% for all currencies and above 15% separately for the local currency and foreign currencies. Bank of Albania regulation requires that the Bank keeps 10% of its customer deposits with maturity less than 2 years as an obligatory reserve with the Bank of Albania.

All the above liquidity ratios are periodically monitored by the Bank with reference to the Group internal limits and guidelines and to the Bank of Albania requirements.

The level of Liquidity position of the bank, measured through the LCR and NSFR indicators, is LCR equal to 771% and NSFR equal to 223% at 31 December 2017 (Dec 2016: LCR = 811% and NSFR = 228%).

Meanwhile the regulatory indicators, as of end of December 2017, are at the levels of : Liquidity indicator in Total 48.4%, in ALL currency 96.6% and in Foreign currencies 23.6% (Dec 2016: Liquidity indicator in Total 50.2%, in ALL currency 96% and in Foreign currencies 24.8%). During the year 2017, the bank has been within the internal and regulatory limits.

4. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

The table enclosed shows the liquidity situation of the Bank as currently monitored by the Bank's management, based on internal local regulations and Group Liquidity Guidelines, as at 31 December 2017 and 2016. The information is not reconcilable as it is provided by management and adjusted as explained below. It considers the undiscounted cash flows in/out of the Bank for on and off-balance-sheet financial assets and liabilities, according to contractual maturity and not reflecting any retention history assumptions or earlier repayment. The classification of securities portfolio in Level 1 and 2 assets, is done based on the criteria's defined in ISBA Liquidity Risk policy, approved in Board of Directors on date 18 December 2017. The Level 3 assets are other securities positioned as per left maturity, as not liquid assets. Behavioral coefficients of ISP Group are applied for current accounts and overdrafts to customers, and drawdown percentages for off-balance-sheet categories such as committed credit lines and guarantees.

31 December 2017	Up to 1 month	1-3 months	3-12 months	1-5 years	> 5 years	Total
Assets (Cash Flow IN)	**68,641,423**	**22,454,255**	**15,102,287**	**39,180,519**	**10,369,030**	**155,747,514**
Net Cash	1,293,078	-	-	-	-	**1,293,078**
Minimum reserve requirements	-	-	-	11,836,076	-	**11,836,076**
Advances to banks	10,229,246	-	-	-	-	**10,229,246**
Held-to-maturity and Available-for-sale Securities – 1st Level Assets	43,765,534	-	-	-	-	**43,765,534**
Held-to-maturity and Available-for-sale Securities – 2nd Level Assets	-	-	-	-	-	**-**
Held-to-maturity and Available-for-sale Securities – 3rd Level Assets	93,544	12,118,492	1,446,639	4,229,310	294,210	**18,182,195**
Loans to banks	5,295,204	7,695,960	6,178,135	-	-	**19,169,299**
Loans and advances to customers (*gross performing loans*)	7,964,817	2,639,803	7,477,513	23,115,133	10,074,820	**51,272,086**
31 December 2017						
Liabilities (Cash flow OUT)	**(17,962,597)**	**(16,256,847)**	**(37,313,269)**	**(59,491,064)**	**(689,714)**	**(131,713,491)**
Deposits from banks and customers- Current accounts	(11,652,627)	(5,363,986)	(11,641,568)	(49,849,317)	**-**	**(78,507,498)**
Current accounts with banks	(866,149)	**-**	**-**	**-**	**-**	**(866,149)**
Current accounts with customers	(10,786,478)	(5,363,986)	(11,641,568)	(49,849,317)	**-**	**(77,641,349)**
Deposits from banks	(2,419,529)	**-**	**-**	**-**	**-**	**(2,419,529)**
Deposits from customers- Time deposits	(3,890,441)	(10,892,861)	(25,671,701)	(9,641,747)	(689,714)	**(50,786,464)**
Total gap on-balance sheet	**50,678,826**	**6,197,408**	**(22,210,982)**	**(20,310,545)**	**9,679,316**	**24,034,023**
Off-Balance sheet (Cash flow in)	-	-	-	-	-	-
Off- Balance sheet (Cash flow out)	(362,239)					**(362,239)**
Total gap off-balance sheet	**(362,239)**	**-**	**-**	**-**	**-**	**(362,239)**
Total gap 31 December 2017	**50,316,587**	**6,197,408**	**(22,210,982)**	**(20,310,545)**	**9,679,316**	**23,671,784**
Cumulated gap 31 December 2017	**50,316,587**	**56,513,995**	**34,303,013**	**13,992,468**	**23,671,784**	

4. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

31 December 2016	Up to 1 month	1-3 months	3-12 months	1-5 years	> 5 years	Total
Assets (Cash Flow IN)	**75,259,512**	**20,021,699**	**13,299,182**	**35,543,560**	**8,191,195**	**152,315,148**
Net Cash	1,302,925	-	-	-	-	**1,302,925**
Minimum reserve requirements	1,312,852	-	-	11,522,585	-	**12,835,437**
Advances to banks	12,457,383	-	-	-	-	**12,457,383**
Held-to-maturity and Available-for-sale Investment Securities – 1st line reserves	46,383,198	-	-	-	-	**46,383,198**
Other Held-to-maturity and Available-for-sale Investment Securities – 3rd line reserves	154,400	11,320,024	1,310,494	3,224,737	429,226	**16,438,881**
Loans to banks	6,070,335	6,795,073	5,628,130	-	-	**18,493,538**
Loans and advances to customers (gross performing loans)	7,578,419	1,906,602	6,360,558	20,796,238	7,761,969	**44,403,786**
31 December 2016	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**> 5 years**	**Total**
Liabilities (Cash flow OUT)	**(19,720,276)**	**(14,944,682)**	**(40,626,395)**	**(54,227,214)**	**(29,531)**	**(129,548,098)**
Deposits from banks and customers- Current accounts	(11,070,674)	(5,143,480)	(11,039,376)	(45,139,051)	-	**(72,392,581)**
Current accounts with banks	(1,008,354)	-	-	-	-	**(1,008,354)**
Current accounts with customers	(10,062,320)	(5,143,480)	(11,039,376)	(45,139,051)	-	**(71,384,227)**
Deposits from banks	(1,886,323)	-	-	-	-	**(1,886,323)**
Deposits from customers- Time deposits	(6,763,279)	(9,801,202)	(29,587,019)	(9,088,163)	(29,531)	**(55,269,194)**
Total gap on-balance sheet	**55,539,236**	**5,077,017**	**(27,327,213)**	**(18,683,654)**	**8,161,664**	**22,767,050**
Off- Balance sheet (Cash flow in)	-	-	-	-	-	
Off- Balance sheet (Cash flow out)	(250,025)	-	-	-	-	**(250,025)**
Total gap off-balance sheet	(250,025)	-	-	-	-	**(250,025)**
Total gap 31 December 2016	**55,289,211**	**5,077,017**	**(27,327,213)**	**(18,683,654)**	**8,161,664**	**22,517,025**
Cumulated gap 31 December 2016	**55,289,211**	**60,366,228**	**33,039,015**	**14,355,361**	**22,517,025**	

4. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

The information provided relates to cash flows deriving from financial off-balance-sheet liabilities, therefore it considerably differs from the face of the statement of financial position. The analysis does not include non-financial liabilities and equity, and comprises of cash flows of contractual interest.

The table below shows the Bank's financial contingent liabilities and financial commitments.

31 December 2017	**1 Month**	**1-3 Months**	**3-12 Months**	**1-5 Years**	**>5 Years**	**Total**
Commitments	5,832,819	-	-	-	-	**5,832,819**
Guarantees	6,955,399	-	-	-	-	**6,955,399**
31 December 2016						
Commitments	4,977,785	-	-	-	-	**4,977,785**
Guarantees	5,020,668	-	-	-	-	**5,020,668**

The Bank expects only a small part of the commitments to be demanded within one month and guarantees to be closed at maturity date. (Refer also to note 30 Commitment and contingencies)

Reconciliation between contingent liabilities and commitments maturity table and note 30 Commitment and contingencies is as follows:

	31 December 2017	**31 December 2016**
Commitments	**5,832,819**	**4,977,785**
Un-drawn credit facilities	5,832,819	4,977,785
Guarantees	**6,955,399**	**5,020,668**
Letters of credit	3,025,244	355,827
Guarantees in favor of customers	3,930,155	4,664,841

c) Market Risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

4. Financial Risk Management (continued)

c) Market Risk (continued)

(i) Exposure to Foreign Exchange rate risk

Foreign exchange rate risk is defined as the possibility that foreign exchange rate fluctuations will produce significant changes, both positive and negative, in the Bank's statement of financial position. The key sources of exchange rate risk consist of:

- Foreign currency loans and deposits held by corporate and retail customers;
- Investment securities in foreign currencies;
- Trading of foreign banknotes;
- Collection and/or payment of interest, commissions, administrative costs, etc. in foreign currencies.

The Bank's exposure to exchange rate risk is monitored on a daily basis by Market and Operational Risk Office ensuring compliance with the internal and regulatory limits. Internal regulations set limits for each open currency position, global open position, maximum loss and Value at Risk (VaR). A detailed analysis was carried out on a one year historical data in order to confirm/establish the aforementioned limits. The local regulatory limits refer to a maximum of 20% of the regulatory capital for each open currency position and 30% for the overall open currency position.

The VaR methodology introduced in the internal procedure is based on the weighted historical simulation technique. The weights used in the model are assigned employing an exponentially declining function with a decay factor of 0.992 and the time window covers a period of 250 days, which is in line with the Group Guidelines. The 1-day, 99% VaR was Lek 0.85 million as of 31 December 2017, with an average of Lek 0.6 million during the year (December 2016: Lek 1.7 million and average Lek 0.9 million).

The VAR model for FX is defined from the Parent Company, Market Risk department. For the time being there is not performed a back testing analysis for FX VaR from ISP Risk Management as the owner of the model. The VaR level was within the limit during 2017 and 2016, and the Stop Loss limit was within the limit during 2017 and 2016.

The Bank has been within the limits in accordance with Bank of Albania regulation during the year 2017.

Financial assets denominated in foreign currencies are disclosed in each relevant note to the financial statements.

4. Financial Risk Management (continued)

c) Market Risk (continued)

Assets	LEK	USD	EUR	OTHER	TOTAL
Cash and cash equivalents	2,014,710	5,371,312	13,869,975	1,621,867	22,877,864
Loans and advances to banks	4,061,958	1,154,041	14,955,067	-	20,171,066
Financial Investments Available-for-sale	506,750	1,665,257	6,905,646	345,355	9,423,008
Financial Investments Held-to-maturity	44,842,533	2,194,854	2,072,732	-	49,110,119
Loans and advances to customers	15,895,159	1,472,124	29,189,918	52	46,557,253
Property and equipment's	2,141,765	-	-	-	2,141,765
Intangible assets	528,695	-	-	-	528,695
Investment Property	575,318	-	-	-	575,318
Deferred tax assets	174,247	-	-	-	174,247
Current tax assets	389,883	-	-	-	389,883
Other assets	755,441	24,157	1,517,280	59	2,296,937
Total Assets (1)	**71,886,459**	**11,881,745**	**68,510,618**	**1,967,333**	**154,246,155**
Liabilities					
Due to Banks	4,079,009	-	1,069,235	20,539	5,168,783
Due to customers	47,318,723	11,882,062	66,608,759	1,901,781	127,711,325
Provisions	373,380	948	94,367	-	468,695
Other liabilities	845,730	14,016	178,843	994	1,039,583
Deferred tax liabilities	148,327	-	-	-	148,327
Net Equity	19,643,524	(3,838)	69,630	126	19,709,442
Total Liabilities (2)	**72,408,693**	**11,893,188**	**68,020,834**	**1,923,440**	**154,246,155**
Net FX Position at 31 December 2017 (1)-(2)	(522,234)	(11,443)	489,784	43,893	**-**
Off balance sheet Assets	11,034,158	5,747,136	112,042,308	374,875	**129,198,477**
Off balance sheet Liabilities	11,046,659	5,681,746	112,064,174	405,898	**129,198,477**
Net Off BSH FX Position at 31 December 2017	**(12,501)**	**65,390**	**(21,866)**	**(31,023)**	**-**
Total Net FX Position at 31 December 2017	**(534,735)**	**53,947**	**467,918**	**12,870**	**-**
Balance sheet Assets as at 31 December 2016	69,219,049	13,173,906	65,601,856	1,533,008	**149,527,819**
Balance sheet Liabilities as at 31 December 2016	70,296,508	13,157,397	64,538,466	1,535,448	**149,527,819**
Net Off BSH FX Position at 31 December 2016	**66,169**	**30,547**	**(105,407)**	**8,691**	**-**
Total Net FX Position at 31 December 2016	**(1,011,290)**	**47,056**	**957,983**	**6,251**	

4. Financial Risk Management (continued)

c) Market Risk (continued)

(ii) Exposure to Interest Rate risk

The principal Interest Rate risk to which the Bank's portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of the change in market interest rates. This risk arises primarily from securities portfolio, retail and corporate banking. Interest rate risk is managed principally through periodic monitoring of interest rate spreads between the Bank's assets and liabilities and also preparing related scenario analysis on interest rates for decision making purposes.

The method used to measure Interest Rate risk of the Bank's assets and liabilities is based on the sensitivity analysis. The measurement system adopted by the Bank must ensure that the risk profile can be examined from two distinctive but complementary points of view:

- the economic value perspective (EVE - Economic Value of Equity), that evaluates the impact of interest rates shocks (and their volatilities) on the present value of future cash flows;
- the net interest income perspective (NII - Net Interest Income), that evaluates the impact of interest rates shocks (and their volatilities) on net interest income.

The EVE perspective provides for an estimation of the medium-to-long term effects induced by interest rate movements; by contrast, the NII perspective provides for an estimation of the short term effects.

i) The sensitivity of the economic value (EVE) measures the change in the economic value of the Intesa Sanpaolo Bank Albania banking book as a result of a shock in the market yield curves, parallel and uniform shift of ±100 basis points. The change in the economic value reflects the changes in the value of all cash flows of the instruments in the balance sheet until their maturity, and is calculated as the difference between the present value of future cash flows recalculated following a shock in interest rates and the present value calculated at current interest rates.

This measure highlights the effect of the variation in market interest rates on the portfolio being measured, with the assumption of no future changes in the mix of assets and liabilities.

The Bank's financial assets and liabilities have mainly variable interest rate or have a re-pricing date of less than one year, except for Albanian Securities and for certain non-Albanian securities investment, which have coupon rates between 0.9 - 6.9% for USD denominated securities (2016: 0.9 - 6.9%), between 0.4 - 5.8% for EUR denominated securities (2016: 0.5 - 5.8%) and 0.7% for GBP denominated security (2016: 1.2 - 2.6%)

The Bank's Regulation on Interest Rate Risk Management, "ISBA Guidelines on the governance of IRRBB" and "ISBA Rules on the measurement and control of IRRBB" have been approved by the ISBA Board of Directors on May 3rd, 2017. The updated documents implements the latest regulatory provisions, recently defined in the Guidelines issued by the Parent Company, based on the EBA regulation (May 2015) and partly anticipating the regulatory framework provided by the Basel Committee on Banking Supervision (BCBS- April 2016) on interest rate risk in the banking book that will take effect from January 2018, and the provisions of the Central Bank of Albania guideline "On managing interest rate risk in the banking book", approved as per decision No. 33, dated 30 April 2013.Interest rate risk generated by the Bank's assets and liabilities, as measured through shift sensitivity of Fair Value analysis of ± 100 basis points, registered at the end of December 2017 a value of ALL -740 million (for +100 basis points) compared to the end of year 2016 ALL -710 million.

4. Financial Risk Management (continued)

c) Market Risk (continued)

(ii) Exposure to Interest Rate risk

The table below shows the currency breakdown of the shift sensitivity for the year end 2017 and 2016.

Shift sensitivity 31 December 2017	**Increase in basis points**	**Total**	**Sensitivity of Profit & Loss**	**Sensitivity of Equity**
EUR	00 b.p. / -100 b.p.	(204,532)/ 218,611	(156,362)/ 169,155	(48,169)/ 49,455
USD	00 b.p. / -100 b.p.	(133,350)/ 147,781	(127,991)/ 142,350	(5,358)/ 5,431
ALL	00 b.p. / -100 b.p.	(402,981)/ 421,762	(402,981)/ 421,762	
Other (GBP & CHF)	00 b.p. / -100 b.p.	567/(412)	970/(615)	(402)/ 202

Shift sensitivity 31 December 2016	**Increase in basis points**	**Total**	**Sensitivity of Profit & Loss**	**Sensitivity of Equity**
EUR	00 b.p. / -100 b.p.	(222,369)/ 225,848	(192,000)/ 218,504	(30,369)/7,343
USD	00 b.p. / -100 b.p.	(190,681)/ 211,274	(184,714)/ 205,247	(5,967)/ 6,027
ALL	00 b.p. / -100 b.p.	(292,471)/ 306,044	(292,471)/ 306,044	
Other (GBP & CHF)	00 b.p. / -100 b.p.	(4,703)/ 3,358	1,147/(1,571)	(5,849)/ 4,930

The limits on shift sensitivity of Fair Value for shock +100bp and the NII Sensitivity for shocks +/-50bp have been included as part of the RAF limits for ISBA 2017.
The limit for USD currency Shift sensitivity of Fair Value for shock +/-100bp has been increased to the level of EUR +/-2.8mln (from EUR +/-2.6mln).

II) The NII sensitivity records the NII effects generated by the market rates movement on the renewal/re-pricing of the banking book. It quantifies the short-term impact on the net interest income of a parallel, instantaneous, permanent shock of ±50 basis points to the interest rate curve. This measure highlights the effect of variations in market rates on the interest margin generated by the portfolio that is being measured, excluding potential effects deriving from the new operations and future changes in the mix of assets and liabilities. The reference time horizon is typically limited to 1 year and according to the hypothesis that the institution is able to continue its activities ("going concern" approach).

The Interest rate risk generated by the Bank's assets and liabilities, as measured through shift sensitivity of Net Interest Income analysis of ± 50 basis points, registered at 31 December 2017 a value of Lek 271 million (for +50 basis points) and a value of Lek -269 million (for -50 basis points).

A behavioral model for the NII sensitivity purposes, is introduced, which is applied to sight positions with customers in ALL and EUR defining the customer interest rate in the long-term and including the behavioral features and delayed reaction to market interest rates (in the short-term) resulting from the model. The implementation is finalized by the end of the year 2017.
The behavioral model is developed by ISP Financial and Market Risks Head Office Department, based on the ISBA historical data provided from the Local risk structure.

III) A different method used to measure Interest Rate risk is required by the Bank of Albania, which consists of quarterly monitoring of the interest rate risk exposure towards a parallel shock of ±200 basis points of the interest rate curve. For all the financial categories of assets and liabilities divided into either fixed or floating rate, their present value is calculated and is distributed in 14 time buckets. The total present value is then multiplied accordingly with the estimated modified duration of each time bucket. The limit for this exposure is 20% of the Bank's regulatory capital. For the year 2017 the Bank has been within the limit with the interest rate risk exposures at 31 December 2017 being 5.5% of the Bank's regulatory capital (31 December 2016: 2.7%).

The Bank has been within the limits in accordance with Bank of Albania regulation and the internal regulation during the year 2017.

4. Financial Risk Management (continued)

c) Market Risk (continued)

(ii) Exposure to Interest Rate risk

The tables below summarize the Bank's interest bearing financial assets and liabilities with both fixed and floating interest rates, as reported to Parent company and management of the Bank. The information is not reconcilable as it is provided by management and adjusted as per below.
Based on the management of Interest Rate risk regulation, each financial instrument is mapped to the repricing gap based on contractual undiscounted cash – flows or behavioral re-pricing date. The contractual includes instruments where the Bank knows exactly when the maturity or next re – pricing takes place.

31 December 2017		**O/N**	**0-3 months**	**3-18 months**	**18m - 3 years**	**3 - 5 years**	**>5 years**	**Total**
Assets	**Interest rate type**							
Loans and advances to banks	Fix	12,867,621	22,058,473	6,178,135	-	-	-	41,104,229
	Floating	-	-	-	-	-	-	-
Loans and advances to customers	Fix	16,280,964	918,699	2,637,672	2,617,980	1,524,981	846,001	24,826,297
	Floating	23,327,858	531,684	1,354,486	835,270	648,515	718,502	27,416,315
Financial investments HTM and AFS	Fix	-	9,269,812	19,340,583	7,336,175	11,944,592	2,744,323	50,635,485
	Floating	-	5,599,688	6,775,875	125,954	51,337	27,328	12,580,182
Other financial assets		-	-	-	-	-	-	-
Total financial assets		**52,476,443**	**38,378,356**	**36,286,751**	**10,915,379**	**14,169,425**	**4336154**	**156,562,508**
Liabilities								
Deposits to banks	Fix	(55,544)	(3,573,652)	-	(234,050)	-	-	(3,863,246)
	Floating	-	-	-	-	-	-	-
Due to customers	Fix	(77,942,515)	(14,819,937)	(29,822,156)	(3,579,196)	(1,584,429)	(689,714)	(128,437,947)
	Floating	-	-	-	-	-	-	-
Other liabilities		-	-	-	-	-	-	-
Total financial liabilities		**(77,998,059)**	**(18,393,589)**	**(29,822,156)**	**(3,813,246)**	**(1,584,429)**	**(689,714)**	**(132,301,193)**
Reprising gap		**(25,521,616)**	**19,984,767**	**6,464,595**	**7,102,133**	**12,584,996**	**3,646,440**	**24,261,315**

The behavioral includes instruments not amenable, whose residual life and/or interest rate have high levels of uncertainty that may depend on specific behaviors by customers, as the sight loans (advances to banks and advances to customers) and sight deposits (current accounts to customers) are positioned in the O/N (on demand) bucket, until the definition of behavioral coefficients.

The reprising gap is calculated according to the internal rules on Interest rate risk as the difference between interest-bearing assets and interest-bearing liabilities in a given time bucket. Other financial assets/liabilities, capital and reserves, are items not included in the reprising gap, not considered interest-bearing.

4. Financial Risk Management (continued)

c) Market Risk (continued)

Exposure to Interest Rate risk

31 December 2016		O/N	0-3 months	3-18 months	18m - 3 years	3 - 5 years	>5 years	Total
Assets	**Interest rate type**							
Loans and advances to banks	Fix	14,392,651	23,191,077	5,628,130	-	-	-	43,211,858
	Floating	-	-	-	-	-	-	-
Loans and advances to customers	Fix	14,441,060	239,215	2,511,475	1,747,695	1,765,700	907,058	21,612,203
	Floating	20,890,842	1,055,902	1,258,263	764,159	577,568	460,825	25,007,559
Financial investments HTM and AFS	Fix	-	6,301,061	18,974,143	5,843,442	7,432,874	3,420,119	41,971,639
	Floating	-	2,538,276	17,465,357	225,585	75,299	39,419	20,343,936
Other financial assets		-	-	-	-	-	-	-
Total financial assets		**49,724,553**	**33,325,531**	**45,837,368**	**8,580,881**	**9,851,441**	**4827421**	**152,147,195**
Liabilities								
Deposits to banks	Fix	(964,053)	(1,886,323)	-	-	-	-	(2,850,376)
	Floating	-	-	-	-	-	-	-
Due to customers	Fix	(71,949,704)	(15,999,004)	(32,763,905)	(5,885,522)	(25,755)	(29,531)	(126,653,421)
	Floating	-	-	-	-	-	-	-
Other liabilities		-	-	-	-	-	-	-
Total financial liabilities		**(72,913,757)**	**(17,885,327)**	**(32,763,905)**	**(5,885,522)**	**(25,755)**	**(29,531)**	**(129,503,797)**
Reprising gap		**(23,189,204)**	**15,440,204**	**13,073,463**	**2,695,359**	**9,825,686**	**4,797,890**	**22,643,398**

4. Financial Risk Management (continued)

d) Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, systems or external events. This definition includes: legal risk, or the risk of losses resulting from violations of law or regulations, from contractual or constructive liability or from other disputes; model risk, defined as the potential loss which can be suffered by an entity, resulting from decisions mainly based on the results of internal models, caused by errors occurred during their development, implementation or use; Compliance risk, defined as the risk to incur judicial or administrative penalties, relevant financial losses resulting from the violation of mandatory rules or self-regulation; ICT risk (Information and Communication Technology, or simply computer risk), defined as the risk to incur economic losses related to the use of information and communication technology. Strategic and reputational risks are excluded.

The Bank's Board of Directors has approved the guidelines on the overall operational risk management framework adopting a policy and an organizational process for measuring, managing and controlling operational risk. The Bank's Regulation on Guideline for Operational Risk Management is fully in compliance with the Group Guidelines on Operational Risk Management issued on December 2014.

The Bank's Operational Risk Management Committee (hereinafter as ORCO) is responsible for the management of the operational risk of the Bank in terms of reviewing operational risk governance documentation and approving changes, preparing policies, standards and methodologies regarding operational risk management. One of the tools introduced for the management of operational risk is the definition of Operational Risk Key Indicators (KRIs). The final list of KRIs and thresholds was approved in ISBA Operational Risk Committee on October 2015. Since their approval, the Internal KRIs have been monitored and reported on quarterly bases in the ORCO and BoD meetings. The Internal KRIs are subject of an annual review process in order to ensure that they are aligned with the dynamic of the operational context and the significant risks that the Bank faces. Any amendment on KRIs policy will be submitted in ORCO and BoD for approval.

The Bank's Risk Management Division is responsible for the identification, assessment, management and mitigation of operational risks, the verification of mitigation effectiveness and reporting to the Bank Senior Management and Group Risk Management with the aim of assessing the potential economic impact of particularly serious operational events.

The Bank carries out an annual assessment campaign set up by Intesa Sanpaolo Group, Self-Diagnosis process, which consists on the operational risk identification and assessment linked to the activity of each single unit within a structure.

The objectives of the Self Diagnosis process are to identify, measure, monitor, and mitigate operational risks. The Self Diagnosis process contributes to the spread of risk - control culture within the Bank. This process is composed of phases relative to the Assessment of the Business Environment, which determines the quality of each structure's risk control profile through the analysis of the importance and the level of management of risk factors in the operating context and phases relative to Scenario Analysis, which determine the size of each structure's risk profile by collecting estimated quantitative data from Business and Operational Units Responsible.

The Bank has the same responsibilities towards the Bank of Albania, based on the regulation on management of operational risk, entered into force on January 2011. The Bank reports regularly on the key indicators and classifications of effective operational losses as per business lines according to the regulatory requirements.

4. Financial Risk Management (continued)

e) Capital Management

The Bank's lead regulator, the Central Bank of Albania, sets and monitors capital requirements for the Bank. The Bank's policy is to maintain the capital base within limits, capitalizing all activity earnings so as to sustain future development of the business recognizing the impact of the level of capital on shareholders' return. The Bank recognizes the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

Implementing the current capital requirements, the Central Bank of Albania requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets and off balance sheet items, at a minimum level of 12%. During financial year 2017 the Bank achieved an adequacy ratio well above the minimum required which as at 31 December 2017 is calculated at 18.91% (2016: 17.57%).

The modified capital adequacy ratio, which represents the ratio of base capital to risk-weighted assets and off balance sheet items, is another limit set by the Central Bank of Albania at a level of 6%.

Throughout the period, there were no material changes in the Bank's management of capital and all externally imposed capital requirements were complied with.

In March 2015 new regulation on Capital Adequacy Ratio entered into force. The new regulation is based on Basel II criteria and is in line with the European Directives for Financial Institutions. Regardless that the new regulation and the countercyclical measures increase the level of risk weighted assets the Capital Adequacy Ratio remained well above the minimum level required during 2017.

	Note	31 December 2017	31 December 2016
Tier 1 capital - CET1			
Share capital	21	5,562,518	5,562,518
Share premium	21	1,383,880	1,383,880
Legal and regulatory reserves	22	1,825,623	1,825,623
Regulatory retained earnings		7,059,651	6,419,968
		15,831,672	15,191,989
Deductions:			
Regulatory intangible assets		(619,181)	(692,374)
Total qualifying Tier 1 capital		**15,212,491**	**14,499,615**
Risk-weighted assets:			
On and off balance sheet		70,887,267	72,470,562
Risk assets for operational risk		9,572,263	10,032,850
Total risk-weighted assets		**80,459,530**	**82,503,412**
Tier I capital to risk- weighted asset ratio		**18.91%**	**17.57%**

5. Use of estimates and judgments

The preparation of the financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Management discusses with the Group Management the development, selection and disclosure of the Bank's critical accounting policies and their application, and assumptions made relating to major estimation uncertainties. Information about assumptions and estimation uncertainties that have a significant risk of material adjustment within the next financial year and critical judgments in applying accounting policies that have the most significant effects on the amounts recognized in the financial statements are disclosed below. These disclosures supplement the commentary on financial risk management (see note 4).

(a) Impairment losses on loans and advances

The Bank reviews its individually significant loans and advances at each reporting date to assess whether an impairment loss should be recorded in profit or loss. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the Bank makes judgments about the borrower's financial situation and the net realizable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance. Loans and advances that have been assessed individually and result without need for provisions, and all the non-performing loans and advances below the significant threshold are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from loan portfolio (such as credit quality, levels of arrears, credit utilization, etc.) and other concentrations of risks and economic data. The impairment losses on loans and advances are disclosed in more details in note 11.

(b) Net realizable value of inventory

The Bank has established a policy with respect to the fair values of repossessed assets which are being measured at the lower of cost and net realizable value. The fair value measurement includes the use of external independent property values that have appropriate recognized statutory professional qualifications, which is subsequently reviewed from the Bank Management for significant unobservable inputs and any required write down adjustments.

(c) Held-to-maturity investments

The Bank follows the guidance of International Accounting Standard 39 Financial Instruments: Recognition and Measurement on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held to maturity. This classification requires significant judgment. In making this judgment, the Bank evaluates its intention and ability to hold such investments to maturity.

(d) Determination of control over investees

Management applies its judgment to determine whether the Bank controls investees. In assessing whether the Bank controls the investees, the Bank performs the power analysis and takes into consideration purpose and design of the investee, the evidence of practical ability to direct the relevant activities of the investees etc.

As a result, the Bank concluded that it does not control and therefore should not consolidate its special purpose vehicles and entities with receivables in default, as the Bank does not have power over the relevant activities of those entities.

5. Use of estimates and judgments (continued)

(e) Fair value of financial instruments

Where the fair values of financial assets and liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data when possible, and if they are not available, judgment is required to establish fair values. For financial instruments that are traded infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. The valuation of financial instruments is disclosed in more detail in note 6. The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

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

The analysis of financial instruments measured at fair value by hierarchy level is presented below:

31 December 2017	Level 1	Level 2	Level 3	Total
Financial investments Available-for-sale				
Quoted investments				
Government debt securities	4,764,697	-	2,140,949	**6,905,646**
Other debt securities	1,665,258	345,355	-	**2,010,613**
Unquoted investments	-	-	506,749	**506,749**
Total	**6,429,955**	**345,355**	**2,647,698**	**9,423,008**

31 December 2016	Level 1	Level 2	Level 3	Total
Financial investments Available-for-sale				
Quoted investments				
Government debt securities	4,099,821	-	-	**4,099,821**
Other debt securities	2,426,419	-	-	**2,426,419**
Unquoted investments	-	-	725,208	**725,208**
Total	**6,526,240**	**-**	**725,208**	**7,251,448**

During the year there were no transfers between the categories, as there were no changes in the methodology used in determining the levels of fair value hierarchy nor changes in market activities of financial instruments.

(f) Deferred tax assets

Deferred tax assets arising from tax losses and temporary differences are recognized as an asset when it is probable that future taxable income would be sufficient to allow the benefit of the loss to be realized. Judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits and future tax planning strategies. Refer to notes 3 (f) and 18 for more details.

(g) Litigation risk

The Bank Management has established an internal process with respect to recognition and measurement of provisions and contingencies due to actual or threatened litigations. Key assumptions about the likelihood and magnitude of an outflow of resources are based on the internal and external legal advice following the respective successful defense strategies against resulting actions. Each action and corresponding risk is assessed on its merits and the underlying constructive or legal obligation, and the estimate of cash outflows considered payable are independently approved from the Bank’s CEO. Management believes, that existing or potential future litigation are remote, however due to causes beyond legal background and framework further risks might be triggered.

6. Financial Assets and Liabilities

Accounting classification and fair values:

	Note	Carrying Amount				Fair Value			
		Held-to-maturity	Loans and advances to banks	Other financial liabilities	Total carrying amount	Level 1	Level 2	Level 3	Total
31 December 2017									
Loans and advances to banks	7	-	20,171,066	-	20,171,066	-	-	20,171,066	**20,171,066**
HTM Investments securities	10	49,110,119	-	-	49,110,119	4,691,391	-	45,628,746	**50,320,137**
Total		**49,110,119**	**20,171,066**	**-**	**69,281,185**	**4,691,391**	**-**	**65,799,812**	**70,491,203**
Deposits from customers	17	-	-	127,711,325	127,711,325	-	-	-	**128,077,040**
Total		**-**	**-**	**127,711,325**	**127,711,325**	**-**	**-**	**-**	**128,077,040**

	Note	Carrying Amount				Fair Value			
		Held-to-maturity	Loans and advances to banks	Other financial liabilities	Total carrying amount	Level 1	Level 2	Level 3	Total
31 December 2016									
Loans and advances to banks	7	-	17,106,968		17,106,968			17,106,968	**17,106,968**
HTM Investments securities	10	50,729,433	-		50,729,433	4,666,485	404,875	46,695,062	**51,766,422**
Total		**50,729,433**	**17,106,968**	**-**	**67,836,401**	**4,666,485**	**404,875**	**63,802,030**	**68,873,390**
Deposits from customers	17	-		125,974,220	125,974,220				**126,033,512**
Total		**-**	**-**	125,974,220	**125,974,220**	**-**	**-**	**-**	**126,033,512**

Held-to-maturity Albanian Government securities are fixed and floating rate bonds. The floating rate bond is given as the average yield of the last three Treasury Bill auctions with the maturity of one year plus the spread. The measurement of the fair value for these securities is performed using the mark-to-market model valuation technique, by discounting all future cash flows deriving from such instruments. The rest of the Held-to-maturity foreign securities denominated in foreign currencies represent Banks and Financial Institutions' securities whose fair value is measured according the "ISBA fair value internal rules".

Loans and advances to customers have carrying amount, which is considered also their fair value, as the major part of portfolio is based on floating interest rates. The fair value of Time Deposits from customers is re-priced using the net present value. The interest rates applied are the market interest rates published from Central Bank of Albania. These rates are an estimate of the market rates. The fair value of current accounts, savings accounts is considered to approximate their carrying amount, given they have short-term maturity.

7. Cash and cash equivalents

Cash and cash equivalents as at 31 December 2017 and 31 December 2016 are detailed as follows:

	31 December 2017	31 December 2016
Cash on hand	1,292,657	1,300,348
Current accounts with banks	10,222,150	12,413,055
Unrestricted balances with Bank of Albania	534,781	738,403
Money market placements	10,828,276	12,817,391
Total	**22,877,864**	**27,269,197**

8. Loans and advances to banks

Loans and advances to banks as at 31 December 2017 and 31 December 2016 are composed as follows:

	31 December 2017	31 December 2016
Compulsory reserve with central bank	11,829,506	11,496,885
Deposits with correspondent banks	8,341,560	5,610,083
Total	**20,171,066**	**17,106,968**

In accordance with the Bank of Albania requirements, the Bank should maintain a minimum of 10% of amounts due to customers with original maturities up to two years as a compulsory reserve with the Bank of Albania. Such reserves are maintained in currencies that match the related due to customers balances. The amount required to be deposited is calculated monthly in arrears. According to the Bank of Albania regulation 40% of this reserve in Lek is available for daily use by the Bank.

The remuneration interest rate of obligatory reserve denominated in Lek is 70% of repurchase agreements rate equal to 0.875% for 31 December 2017 (31 December 2016: 0.875%).

The remuneration interest rate of the obligatory reserve in EUR is equal to the European Central Bank base rate equal to minus 0.40% for EUR for 31 December 2017 (31 December 2016: minus 0.40%).

Deposits with banks comprise money market placements with an original maturity of over three months.

9. Financial investments available for sale

Financial investments available-for-sale as at 31 December 2017 and 31 December 2016 can be detailed as follows:

	31 December 2017	31 December 2016
Corporate issuers		
Bank issuers	**900,577**	**1,789,549**
Unlisted	-	362,527
Listed	900,577	1,427,022
Sovereign issuers		
Republic of Albania	**3,371,533**	**1,113,620**
Unlisted	2,651,346	725,207
Listed	720,187	388,413
EU member states	**4,040,862**	**3,711,409**
Listed	4,040,862	3,711,409
Other Financial Institutions	**1,110,036**	**636,870**
Listed	1,110,036	636,870
Total	**9,423,008**	**7,251,448**

The Bank reviews its debt securities classified as available-for-sale investments at each reporting date to assess whether there is any objective evidence that they are impaired.

10. Financial investments held to maturity

Financial investments held to maturity as at 31 December 2017 and 31 December 2016 can be detailed as follows:

	31 December 2017	31 December 2016
Corporate issuers		
Bank issuers	**-**	**-**
Listed	-	-
Sovereign issuers	**49,110,119**	**50,729,433**
Republic of Albania	**46,915,264**	**47,769,533**
Unlisted	44,842,532	45,657,986
Listed	2,072,732	2,111,547
US and EU member states	**2,194,855**	**2,959,900**
Listed	2,194,855	2,959,900
Total	**49,110,119**	**50,729,433**

As at 31 December 2017, Held to maturity investment securities with Republic of Albania of Lek 1,570 million (2016: Nil) have been pledged as collateral for Repurchase Agreements (see note 16).

11. Loans and advances to customers

Loans and advances to customers are composed as follows:

	31 December 2017	31 December 2016
Loans	33,003,031	31,493,287
Overdrafts	15,656,058	13,858,107
Deferred disbursement fees	(116,803)	(111,431)
Gross amount	**48,542,286**	**45,239,963**
Allowance for impairment	(1,985,033)	(2,697,812)
Total net amount	**46,557,253**	**42,542,151**

Movement in the allowance for impairment losses on loans and advances to customers is as follows:

	2017	2016
Specific allowance for impairment		
Balance at 1 January	**2,310,842**	**4,000,730**
Charge for the year	704,491	1,703,658
Recoveries	(806,908)	(2,121,069)
	(102,417)	**(417,411)**
Effect of movements in foreign exchange	(29,490)	(40,514)
Write-offs	(631,215)	(1,231,963)
Balance at 31 December	**1,547,720**	**2,310,842**
Collective allowance for impairment		
Balance at 1 January	**386,970**	**371,425**
Charge for the year	60,241	25,325
Recoveries	(3,827)	(6,627)
	56,414	**18,698**
Effect of movements in foreign exchange	(6,071)	(3,153)
Balance at 31 December	**437,313**	**386,970**
Total allowance for impairment	**1,985,033**	**2,697,812**
Total (reversal)/charge for the year	**(46,003)**	**(398,713)**

12. Property and Equipment

Property and Equipment as at 31 December 2017 and 31 December 2016 is as follows:

	Land and Building	IT and Electrical Equipment	Furniture and Fine Art Works	Other non-Electrical Assets	Assets acquired not put into use	Total
Cost						
Balance as at 1 January 2016	**1,643,522**	**1,272,832**	**181,974**	**246,135**	**79,584**	**3,424,047**
Additions	-	28,451	12,083	6,460	113,984	**160,978**
Disposals	-	(10,537)	(15,404)	(4,642)		**(30,583)**
Balance as at 31 December 2016	**1,643,522**	**1,290,746**	**178,653**	**247,953**	**193,568**	**3,554,442**
Additions	55,539	142,174	19,804	14,484	-	**232,001**
Disposals	-	(179,529)	-	-	(32,489)	**(212,018)**
Effect of revaluation	(13,920)	-	-	-	-	**(13,920)**
Balance as at 31 December 2017	**1,685,141**	**1,253,391**	**198,457**	**262,437**	**161,079**	**3,560,505**
Accumulated Depreciation						
Balance as at 1 January 2016	814,378	1,026,289	162,360	218,751	-	**2,221,778**
Depreciation for the year	78,033	97,004	5,529	10,382	-	**190,948**
Disposals	-	(10,500)	(15,402)	(4,625)	-	**(30,527)**
Balance as at 31 December 2016	**892,411**	**1,112,793**	**152,487**	**224,508**	-	**2,382,199**
Depreciation for the year	33,781	90,119	6,956	9,893	-	**140,749**
Disposals	-	(178,016)	-	-	-	**(178,016)**
Effect of revaluation	(926,192)	-	-	-	-	**(926,192)**
Balance as at 31 December 2017	**-**	**1,024,896**	**159,443**	**234,401**	**-**	**1,418,740**
Carrying amount						
At 1 January 2016	**829,144**	**246,543**	**19,614**	**27,384**	**79,584**	**1,202,269**
At 31 December 2016	**751,111**	**177,953**	**26,166**	**23,445**	**193,568**	**1,172,243**
At 31 December 2017	**1,685,141**	**228,495**	**39,014**	**28,036**	**161,079**	**2,141,765**

12. Property and Equipment (continued)

(i) Change in estimate

During 2017, the Bank conducted a technical and physical inspection of its own used property, which resulted in changes in their expected useful life. As a result the estimated useful live for Properties changed from 20 to 33 year. The effect of these changes on the actual and expected depreciation expense, included in 'depreciation and amortization' was as follows:

	2017	2018	2019	2020	2021	Later
Increase/(decrease) in depreciation expense	(45,713)	(33,888)	(22,316)	(22,207)	(22,207)	1,012,890

(ii) Change in accounting policy

As disclosed in note 3.a, as at 31 December 2017, the Bank revalued its own used properties, which resulted in a net increase of Lek 775 million recognized as an increase in revaluation reserves. The fair value of the properties and was determined by an external independent property experts appointed by the Parent Company, who have appropriate recognized professional qualifications and experience. The fair value was measured under the Sale and Leaseback assumptions and assessment by using market comparison and investment approaches as a valuation technique and have been categorized as a Level 3 fair value based on the inputs of the valuation technique used.

13. Intangible Assets

Intangible assets as at 31 December 2017 and 31 December 2016 are as follows:

	Software and Licenses	**Advances for Software**	**Total**
Cost			
Balance as at 1 January 2016	**1,474,693**	**98,744**	**1,573,437**
Additions during period	109,596	25,052	134,648
Transfers	-	-	**-**
Balance as at 31 December 2016	**1,584,289**	**123,796**	**1,708,085**
Additions during period	129,529	-	129,529
Transfers	-	(38,782)	(38,782)
Balance as at 31 December 2017	**1,713,818**	**85,014**	**1,798,832**
Amortization and Impairment Losses			
Balance as at 1 January 2016	**982,874**	-	**982,874**
Amortization charge for the year	133,309	-	133,309
Disposals	-	-	**-**
Balance as at 31 December 2016	**1,116,183**	**-**	**1,116,183**
Amortization charge for the year	153,954	-	153,954
Disposals	-	-	**-**
Balance as at 31 December 2017	**1,270,137**	**-**	**1,270,137**
Carrying amount			
At 1 January 2016	**491,819**	**98,744**	**590,563**
At 31 December 2016	**468,106**	**123,796**	**591,902**
At 31 December 2017	**443,681**	**85,014**	**528,695**

14. Investment property

The Bank holds investment property as consequence of acquisitions through enforcement of security over loans and advances. As at 31 December 2017, the investment property represent a foreclosed collateral repossessed during 2017 with a carrying amount of Lek 575,318 thousand, net of accumulated depreciation of Lek 129,773 thousand and impairment of Lek 16,397 thousand and that is leased to a third party. During 2017, investment property rentals of Lek 2,695 thousand have been recognized in other income.

Based on the agreement between parties the annual rent for the first year is calculated 2.8% of the historical cost. The annual rent change over the period based on the payment of instalment for purchase of the property.

15. Inventory and other assets

Other assets as at 31 December 2017 and 31 December 2016 are as follows:

	31 December 2017	31 December 2016
Inventory	2,038,503	2,298,654
Sundry debtors	62,045	57,462
ATM & POS transactions	47,009	31,743
Leasehold improvements	35,024	22,398
Prepayments	42,103	46,395
Cheques for collection	3,497	8,377
Others	68,756	35,349
Total	**2,296,937**	**2,500,378**

Inventory represents repossessed assets acquired in the process of collection of defaulted loans.The movement of "repossessed assets" item during the reporting period is presented as follows:

	2017	2016
At beginning of the period	**2,298,654**	**1,837,084**
Additions during period	323,007	1,076,525
Disposals of the period	(363,280)	(306,733)
Write down to net realizable value	(190,287)	(293,553)
Effect of movements in foreign exchange	(29,591)	(14,669)
At end of the period	**2,038,503**	**2,298,654**

The movement of leasehold improvements during the reporting period is presented as follows:

	31 December 2017	31 December 2016
At beginning of the period	**22,398**	**28,598**
Additions during period	20,489	1,551
Amortization of the period	(7,863)	(7,751)
At end of the period	**35,024**	**22,398**

16. Due to banks

Due to banks as at 31 December 2017 and 31 December 2016 are as follows:

	31 December 2017	31 December 2016
Correspondent banks		
Current accounts	**1,095,433**	**999,095**
Resident	842,147	888,890
Non-resident	253,286	110,205
Deposits	**2,685,329**	**1,886,138**
Resident	2,685,329	1,886,138
Non-resident	**-**	-
Repurchase Agreements	**1,388,021**	-
Total	**5,168,783**	**2,885,233**

As at 31 December 2017, Held to maturity investment securities with Republic of Albania of Lek 1,570 million (2016: Nil) have been pledged as collateral for Repurchase Agreements (see note 10).

17. Due to customers

Due to customers as at 31 December 2017 and 31 December 2016 are composed as follows:

	31 December 2017			31 December 2016		
Current accounts	**Local Currency**	**Foreign Currency**	**Total**	**Local Currency**	**Foreign Currency**	**Total**
Retail	6,917,594	15,040,946	21,958,540	6,774,797	12,844,916	19,619,713
Corporate	10,324,102	24,369,702	34,693,804	9,993,204	23,587,330	33,580,534
	17,241,696	**39,410,648**	**56,652,344**	**16,768,001**	**36,432,246**	**53,200,247**
Deposits						
Retail	29,094,349	37,573,426	66,667,775	30,335,152	38,208,519	68,543,671
Corporate	982,677	3,408,529	4,391,206	796,230	3,434,072	4,230,302
	30,077,026	**40,981,955**	**71,058,981**	**31,131,382**	**41,642,591**	**72,773,973**
Total	**47,318,722**	**80,392,603**	**127,711,325**	**47,899,383**	**78,074,837**	**125,974,220**

Balances due to customers by maturity and currency type are as follows:

	31 December 2017			31 December 2016		
	Local Currency	**Foreign Currency**	**Total**	**Local Currency**	**Foreign Currency**	**Total**
Current Accounts	**17,241,696**	**39,410,648**	**56,652,344**	**16,768,001**	**36,432,246**	**53,200,247**
Deposits						
On demand	3,437,765	15,969,919	19,407,684	3,183,356	13,285,724	16,469,080
One month	384,258	227,767	612,025	965,784	448,121	1,413,905
Three months	788,662	1,689,726	2,478,388	928,928	2,230,587	3,159,515
Six months	2,206,079	3,450,134	5,656,213	2,657,242	3,723,775	6,381,017
Nine months	767	7,317	8,084	2,282	7,442	9,724
Twelve months	9,942,163	16,939,399	26,881,562	12,514,768	18,936,722	31,451,490
Twenty four months	6,083,478	1,553,756	7,637,234	5,985,458	1,682,463	7,667,921
Other	7,233,854	1,143,937	8,377,791	4,893,564	1,327,757	6,221,321
	30,077,026	**40,981,955**	**71,058,981**	**31,131,382**	**41,642,591**	**72,773,973**
Total	**47,318,722**	**80,392,603**	**127,711,325**	**47,899,383**	**78,074,837**	**125,974,220**

17. Due to customers (continued)

For current accounts (for which is paid interest) and time deposits, the annual published interest rates applicable for the various fixed terms were:

2017	ALL (%)	USD (%)	EUR (%)
Current accounts and demand deposits	0.01 – 2.20	0.01 – 0.83	0.002 – 0.300
Time deposits – 1 month	0.40 – 0.50	0.05 – 0.05	0.002 – 0.002
Time deposits – 3 months	0.30 – 0.85	0.10 – 0.20	0.001 – 0.002
Time deposits – 6 months	0.35 – 1.05	0.15 – 0.25	0.003 – 0.005
Time deposits – 9 months	0.40 – 0.40	-	0.006 – 0.006
Time deposits – 10 months	1.20 – 1.20	-	-
Time deposits – 12 months	0.45 – 1.50	0.20 – 0.30	0.005 – 0.010
Time deposits – 15 months	1.50 – 1.50	-	-
Time deposits – 21 months	2.00 – 2.00	-	-
Time deposits – 24 months	1.15 – 2.00	0.20 – 0.30	0.020 – 0.050
Time deposits – 30 months	1.63 – 1.94	-	-
Time deposits – 36 months	1.20 – 2.40		0.070 – 0.100
Time deposits – 60 months	2.38 – 2.56		-
Time deposits – 84 months	3.41 – 3.60	-	-

2016	ALL (%)	USD (%)	EUR (%)
Current accounts and demand deposits	0.01 – 2.07	0.01 – 0.53	0.002 – 0.997
Time deposits – 1 month	0.40 – 0.90	0.05 – 0.05	0.002 – 0.030
Time deposits – 3 months	0.40 – 1.20	0.10 – 0.20	0.000 – 0.050
Time deposits – 6 months	0.45 – 1.50	0.15 – 0.25	0.000 – 0.050
Time deposits – 9 months	0.40 – 1.10		0.006 – 0.070
Time deposits – 12 months	0.60 – 1.90	0.20 – 0.30	0.000 – 0.100
Time deposits – 24 months	1.15 – 2.15	0.20 – 0.30	0.020 – 0.100
Time deposits – 36 months	1.20 – 2.40		0.070 – 0.100
Time deposits – 60 months	2.38 – 2.56		
Time deposits – 84 months	3.41 – 3.60		

All individual and cooperate customer deposits, in accordance with the Law No. 52, dated 25.05.2014 “On the Insurance of Deposits” amended, are protected without any cost for customers, up to the amount of Lek 2,500,000 (or in Lek equivalent if in foreign currency) with the Deposit Insurance Agency (DIA).

18. Deferred Tax

Recognized deferred tax assets and liabilities are attributable to the following:

	31 December 2017			31 December 2016		
	Assets	**Liabilities**	**Net**	**Assets**	**Liabilities**	**Net**
Financial assets available-for-sale	-	9,888	(9,888)	-	290	(290)
Investment Property	-	1,599	(1,599)	-	-	-
Repossessed assets	102,580	-	102,580	-	-	-
Properties	-	136,840	(136,840)	26,748	-	26,748
Equipment and intangible assets	71,667	-	71,667	55,344	-	55,344
Net deferred tax assets	**174,247**	**148,327**	**25,920**	**82,092**	**290**	**81,802**

Movements in temporary differences during the year are as follows:

31 December 2017	**Opening balance**	**Recognized in profit or loss**	**Recognized in other comprehensive income**	**Closing balance**
Financial assets available-for-sale	(290)	-	(9,598)	**(9,888)**
Investment Property	-	(1,599)	-	**(1,599)**
Repossessed assets	-	102,580	-	**102,580**
Properties	26,748	(26,748)	(136,840)	**(136,840)**
Equipment and intangible assets	55,344	16,323	-	**71,667**
Total	**81,802**	**90,556**	**(146,438)**	**25,920**
31 December 2016				
Financial assets available-for-sale	(46)	-	(244)	**(290)**
Property, equipment and intangible assets	82,103	(11)	-	**82,092**
Total	**82,057**	**(11)**	**(244)**	**81,802**

19. Provisions

Movements in provisions during the year are as follows:

	Tax Litigation	**Other Litigations**	**Off-Bsh & Other Provision**	**Total**
Balance at 1 January 2017	278,094	19,096	53,189	**350,379**
Provisions made during the year	-	50,928	76,131	**127,059**
Provisions used during the year	-	-	(7,607)	**(7,607)**
Effect of movements in foreign exchange		(321)	(815)	**(1,136)**
Balance at 31 December 2017	**278,094**	**69,703**	**120,898**	**468,695**

Provisions made during the year on off-bsh and other category include Lek 1,437 thousand and Lek 74,694 thousand. The current year charge of Lek 74,694 thousand relates to resolution plan law introduced during 2017 requiring that all second tier Banks in Albania contribute a premium of 0.5% of the respective total liabilities throughout a period of 10 years.

20. Other liabilities

Other liabilities as at 31 December 2017 and 31 December 2016 are composed as follows:

	31 December 2017	31 December 2016
Accrued expenses	243,147	542,032
Sundry creditors	14,931	151,123
Suspense accounts	380,969	17,749
Bank cheques issued and payments in transit	348,482	24,039
Other tax liabilities	32,969	33,759
Due to third parties	18,774	17,091
Other accrued expenses	311	771
Total	**1,039,583**	**786,564**

21. Share capital and share premium

The issued share capital comprises one class of shares as follows:

	Number of Shares (In number)	Nominal Value (In Lek)	Total Shares Value (In Lek)
Share Capital at 31 December 2017	**15,581,282**	**357**	**5,562,517,674**

Share premium represents the amount paid from the shareholder in excess of the registered share capital.

Intesa Sanpaolo S.p.A is the sole shareholder at 31 December 2017 and 31 December 2016.

22. Legal and regulatory reserves

As at 31 December 2017 and 31 December 2016, the reserves were:

	31 December 2017	31 December 2016
Regulatory reserve	1,130,983	1,130,983
Legal reserve	694,640	694,640
Total	**1,825,623**	**1,825,623**

The regulatory reserve was established according to the Central Bank of Albania regulation “On the Bank’s Regulatory Capital”, no.69, dated 18 December 2014. Banks and branches of foreign banks are required to create reserves of 1.25% to 2% of total risk-weighted assets, by appropriating one fifth of the profit after taxes and before payment of dividends, until the balance on this measure reaches at least 1.25% of total risk-weighted assets. At 31 December 2016, the regulatory reserve represented 1.45% of total risk-weighted assets (2015: 1.5%).

The provisions of the Commercial Law require the creation of reserves of 5% of the Bank’s net income after deduction of accumulated losses from previous years, until the balance of this reserve reaches 10% of the Bank’s share capital. At 31 December 2016, the balance represented 10% of the Bank’s share capital (2015: 10%). This threshold is not mandatory, when the existing reserves are not less than one tenth of the Bank’s share capital.

23. Other reserves

Other reserves

	31 December 2017	31 December 2016
Revaluation reserve	775,431	-
Fair Value reserve	56,030	1,643
Total	**831,461**	**1,643**

The revaluation reserve relates to the revaluation of owed used property. The fair value reserve comprises the cumulative net change in the fair value of available-for-sale financial assets until the assets are derecognised or impaired.

Other comprehensive items

Other comprehensive items represent the differences arising from the conversion of the Bank's share capital from USD to Lek. Out of this balance, the amount of Lek 297,666 thousand was received as at 1 January 2008 from the merger with former BIA, as raised by the same denomination currency change of the share capital.

24. Net Interest income

Interest income	**2017**	**2016**
Loans and advances to customers	2,094,262	2,284,667
Financial investments held to maturity	2,007,949	2,367,719
Loans and advances to banks	90,282	100,535
Financial investments-available-for-sale	88,265	73,045
Total interest income	**4,280,758**	**4,825,966**
Interest expenses		
Demand and time deposits	384,630	696,612
Deposits from banks	86,458	66,480
Current accounts of customers	51,260	54,258
Total interest expenses	**522,348**	**817,350**
Net interest income	**3,758,410**	**4,008,616**

25. Net fee and commission income

	2017	**2016**
Collection and payment services	427,937	436,714
Active current accounts	214,358	205,513
ATMs and POSs	260,015	214,865
Guarantees given	19,032	15,424
Unused/advanced liquidated credit lines	23,169	24,922
Arrangement fees and others	8,928	12,705
Fee and commission income	**953,439**	**910,143**
ATMs and POSs	221,124	191,957
Banking services-foreign branches	8,616	9,553
Collection and payment services	14,684	1,990
Guarantees received	6,296	994
Fee and commission expenses	**250,720**	**204,494**
Net fee and commission income	**702,719**	**705,649**

Fee and commissions do not include fees received for loans and advances to customers (transaction costs), which are adjusted on initial recognition for the carrying value of these financial assets as per effective interest rate method.

26. Net other income

	2017	2016
Foreign exchange gains	381,085	366,033
Other	36,437	309
Total	**417,522**	**366,342**

27. Other operating expenses, net

	2017	2016
Premium on deposits insurance	332,525	241,636
Loss on sale of fixed assets	6,031	100,866
(Gain)/loss on sundry net operational	(68,395)	(64,479)
Total	**270,161**	**278,023**

28. Personnel expenses

	2017	2016
Salaries	915,054	861,642
Personnel on secondment	110,617	59,175
Social Insurance	92,237	94,747
Training & similar	4,696	5,240
Termination indemnities and others	12,419	27,405
Total	**1,135,023**	**1,048,209**

29. Other administrative expenses

	2017	2016
Software maintenance	283,607	182,305
Telephone and electricity	57,985	82,214
Advertising and publications	26,968	30,627
Maintenance and repair	53,657	51,823
Stationery	48,299	35,695
Consulting, legal and professional fees	39,758	56,247
Security	54,161	38,237
Transport and security services	29,669	25,717
Travel and business trips	9,474	9,844
Insurance	15,170	23,052
Other	114,479	78,639
Total	**733,227**	**614,400**

30. Income tax expenses

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

	2017	2016
Current year	368,999	480,842
Current tax expense	**368,999**	**480,842**
Origination and reversal of temporary differences	(90,558)	11
Deferred tax expenses/(income)	**(90,558)**	**11**
Income tax expense	**278,441**	**480,853**

Reconciliation of the income tax expense with the accounting profit for the year ended 31 December 2017 and 2016 is presented as follows:

	2017		2016	
Accounting Profit before tax		**1,935,196**		**2,763,858**
Income tax at domestic corporate tax rate	15.00%	290,280	15.00%	414,579
Non-deductible expenses	4.07%	78,719	2.40%	66,263
Origination and reversal of temporary differences	(4.70%)	(90,558)	0.00%	11
Income tax Expense	**14.40%**	**278,441**	**17.37%**	**480,853**

Non-deductible expenses are detailed as follows:

	2017	2016
Representations & Sponsorships	199	1,151
Sundry operational losses	3,790	11,593
Rent Apartments	3,854	2,384
Personnel costs	6,303	103
Office Expenses	6,868	8,262
Provisions other	39,004	30,731
Litigation cases	50,928	64,653
Losses -Unrecoverable Loan & Od	163,261	158,686
Impairment assets through legal process	320,060	293,553
Recovery of accruals prior years	(48,632)	-
Depreciation and amortization Fixed Assets	(20,839)	9,720
Recognition of loss (expense) year 2013 (based on Tax Audit report)	-	(139,083)
Total	**524,796**	**441,753**
At 15%	**78,719**	**66,263**

The Bank 2017 prepaid income tax is in the amount of Lek 476,876 thousand (2016: Lek 455,583 thousand).

31. Commitments and contingencies

Commitments and contingencies as at 31 December 2017 and 31 December 2016 are as follows:

	31 December 2017	31 December 2016
Contingent Assets	**125,268,321**	**121,076,950**
Guarantees received from credit customers	108,866,527	109,250,300
Guarantees received from Government	5,200,000	5,200,000
Un-drawn credit facilities	5,832,819	4,977,785
Letters of credit	3,025,244	355,827
Money market future dated deals	246,806	241,793
Forward foreign exchange contracts	2,096,925	1,025,360
Other	-	25,885
Contingent Liabilities	**3,930,155**	**4,664,841**
Guarantees in favor of customers	3,930,155	4,664,841

Guarantees are mainly represented by bid and performance bonds. Guarantees and letters of credit are collateralized by cash and deposits. The Bank issues guarantees to its customers. These instruments bear a credit risk similar to that of loans granted.

Contingent assets, like letters of credit and un-drawn credit facilities, are off-balance sheet items representing future commitments where the Bank acts as the beneficiary. Forward foreign exchange contracts are off- balance sheet items used to offset currency fluctuations and the effect on the income statement is reflected on the maturity date when the contract is executed.

Litigation

The Bank is defending an action related to a partial payment of a bank guarantee amounting EUR 4,830 thousand. The guarantee was issued in favor of an Albanian entity upon the request of its parent company Intesa SanPaolo S.P.A. The Bank has successfully defended itself in a legal process, in which both the First Instance Court and Court of Appeal judged in favor of the Bank. The plaintiff has appealed to the Supreme Court which has not yet issued its decision. Management does not consider that there are any legal grounds for the existing judgments in its favor to be overturned. Nevertheless, given the complexity of the case, involving also the Italian Jurisdiction, and taking into consideration no other cases of that kind have been ever judged in the Albanian courts, some operational risks may occur.

32. Lease commitments and operating lease expenses

The Bank's operating lease commitments as lessee as at 31 December 2017 and 31 December 2016 are as follows:

	31 December 2017	31 December 2016
Less than one year	133,266	125,193
Between one and five years	205,805	229,081
More than five years	-	11,918
Total	**339,071**	**366,192**

The Bank has rental agreements with renewal options for its offices in Albania. During 2017, the amount of Lek 159,658 thousand was recognized as expense in respect of lease rentals (2016: Lek 164,626 thousand). Operating lease contracts are cancellable, if notified for a period of 180 days in advance.

33. Related parties

The Bank's immediate parent is Intesa Sanpaolo S.p.A, which ultimately holds a 100% interest. The Bank, therefore, considers that it has a related-party relationship, in accordance with International Accounting Standard 24 Related Party Disclosures ("IAS 24") with the following:
Shareholders and parties related to shareholders:

- Intesa Sanpaolo S.p.A and its subsidiaries and associates

Key management personnel and parties related to key management personnel:

- Supervisory Board members, Management Board members and other key management personnel defined as persons having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly, including any director (whether executive or otherwise) of the Bank, collectively "key management personnel", close family members of key management personnel, and companies and un-incorporated businesses controlled, or jointly controlled by key management personnel and/or their close family members. The following transactions have taken place during the year ended 31 December 2017 and 31 December 2016:

	ISP Group companies		Key management personnel and Other related parties	
	31 December 2017	**31 December 2016**	**31 December 2017**	**31 December 2016**
Assets at end of year	**12,082,176**	**12,197,494**	**107,904**	**155,476**
Loans and advances to credit institutions	12,069,161	12,152,936	-	-
Loans and advances to customers	-	-	107,904	155,476
Other assets	13,015	44,558		-
Liabilities at end of year	**1,356,097**	**61,242**	**401,259**	**403,570**
Loans and advances from credit institutions	1,310,245	44,170	-	-
Customer deposits	-	-	401,259	403,570
Invoices to be received	45,852	17,072		-
Off balance sheet	**5,194,836**	**2,843,263**	**-**	**-**
Letter of credit/Letter of Guarantees given	501,481	424,707		-
Letter of credit/Letter of Guarantees received	1,120,298	1,219,078	-	-
Foreign currency contracts	2,332,644	1,199,478	-	-
Commitments given	1,240,413			
Collaterals	-	-	-	-
Income for year ending	**99,022**	**90,457**	**2,974**	**4,002**
Interest income	55,372	40,799	2,404	3,533
Commission Income	43,650	49,658	570	469
Expenses for the year ending	**38,155**	**71,579**	**481**	**1,099**
Interest expense	19,507	10,007	481	1,099
Commission expense and others	18,648	19,276	-	-
Other Administrative Costs	**-**	42,296	-	-
Compensation of Key Managers			**151,866**	**136,797**
Net Salary			81,706	79,766
Net Bonus paid			17,905	20,652
Social & Health Insurance			4,997	4,254
Other expenses (Lecoip)			13,963	13,859
Other expenses			33,295	18,266

34. Subsequent events

The management of the Bank is not aware of any subsequent events that would require either adjustments or additional disclosures in the financial statements.