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TRANSLATION

Independent Auditor's Report

To the Shareholders of Banca Intesa a.d. Beograd

Opinion

We have audited the accompanying separate financial statements of Banca Intesa a.d. Beograd (the "Bank"), which comprise:

— the separate balance sheet as at 31 December 2019,

and, for the period from 1 January to 31 December 2019:

— the separate income statement;
— the separate statement of other comprehensive income;
— the separate statement of changes in equity;
— the separate cash flow statement;

and

— notes comprising a summary of significant accounting policies and other explanatory information (the "separate financial statements").

In our opinion, the accompanying separate financial statements give a true and fair view of the unconsolidated financial position of the Bank as at 31 December 2019 and of its unconsolidated financial performance and its unconsolidated cash flows for the financial year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

We conducted our audit in accordance with the Law on Auditing of the Republic of Serbia, the Decision on External Audit of Banks and applicable audit standards in the Republic of Serbia. Our responsibilities under those regulations are further described in the Auditor's Responsibility for the audit of the separate 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) together with the ethical requirements that are relevant to our audit of the separate financial statements in the Republic of Serbia and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA 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 Annual Business Report for the year ended 31 December 2019.

Our opinion on the separate financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report we do not express any form of assurance conclusion thereon.

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

Based solely on the work required to be undertaken in the course of the audit of the separate financial statements, in our opinion, the information given in the annual business report for the financial year for which the separate financial statements are prepared, is consistent with the separate financial statements.

In addition, if, based on the work we performed, we conclude that there is a material misstatement in the other information, we are required to report that fact. We have nothing to report in this regard.

Responsibility of Management and Those Charged with Governance for the separate financial statements

Management is responsible for the preparation of separate financial statements that give a true and fair view in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of separate financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the separate 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.

Auditor's Responsibility for the audit of the separate financial statements

Our objectives are to obtain reasonable assurance about whether the separate 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 the Law on Auditing of the Republic of Serbia, the Decision on External Audit of Banks and applicable audit standards in the Republic of Serbia 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 separate financial statements.

As part of an audit in accordance with the Law on Auditing of the Republic of Serbia, the Decision on External Audit of Banks and applicable audit standards in the Republic of Serbia, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

— Identify and assess the risks of material misstatement of the separate 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 on the audit of the separate financial statements to the related disclosures in the separate 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 on the audit of the separate financial statements. 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 separate financial statements, including the disclosures, and whether the separate 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.

KPMG d.o.o. Beograd

Signed on the Serbian original

Nikola Đenić
Certified Auditor

Katarina Kecko
Partner

Beograd, 6 March 2020

This is a translation of the original Independent Auditors' Report issued in the Serbian language. All due care has been taken to produce a translation that is as faithful as possible to the original. However, if any questions arise related to interpretation of the information contained in the translation, the Serbian version of the document shall prevail. We assume no responsibility for the correctness of the translation of the Bank's financial statements.

KPMG d.o.o. Beograd

Signed on the Serbian original

DRUŠTVO ZA KONSALTING I REVIZIJU D.O.O. KPMG 1 BEOGRAD

Nikola Đenić
Certified Auditor

Katarina Kecko
Partner

Belgrade, 6 March 2020

SEPARATE BALANCE SHEET as at 31 December 2019

in RSD thousand	**Note**	**December 31, 2019**	**December 31, 2018**
ASSETS			
Cash and assets held with the central bank	15, 2.14	97,392,634	86,962,607
Receivables under derivatives	16, 2.10	61,978	331,839
Securities	16, 2.9	108,307,660	92,872,485
Loans and receivables from banks and other financial organisations	17, 2.8	51,166,557	33,039,264
Loans and receivables from clients	17, 2.8	373,909,572	339,749,114
Investments in associated companies and joint ventures	16, 2.7	1,199,472	1,199,472
Intangible investments	18, 2.15	5,348,965	3,774,866
Property, plant and equipment	19, 2.16	9,953,027	7,951,099
Investment property	19, 2.16	776	30,995
Deferred tax assets	14, 2.21	683,199	704,800
Non-current assets held for sale and discontinued operations	19, 2.16	38,301	143,015
Other assets	20	4,568,751	4,315,623
TOTAL ASSETS		**652,630,892**	**571,075,179**
LIABILITIES			
Liabilities under derivatives	21, 2.10	7,869	21,497
Deposits and other liabilities to banks, other financial organisations and central bank	22, 2.11	66,347,915	49,031,251
Deposits and other financial liabilities to clients	22, 2.11	472,324,895	405,175,217
Provisions	23, 2.3	861,164	1,801,197
Current tax liabilities	14, 2.21	478,134	21,386
Deferred tax liabilities	14, 2.21	106,182	106,337
Other liabilities	24	12,437,666	8,317,108
TOTAL LIABILITIES		**552,563,825**	**464,473,993**
CAPITAL			
Share capital	25, 2.19	41,748,469	41,748,469
Retain earnings	25, 2.19	12,331,751	16,080,705
Reserves	25, 2.19	45,986,847	48,772,012
TOTAL CAPITAL		**100,067,067**	**106,601,186**
TOTAL CAPITAL SHORTFALL		**652,630,892**	**571,075,179**

Belgrade, 11 February 2020

Rada Radović	Dragica Mihajlović	Draginja Đurić
Head of Accounting Department	CFO	CEO

SEPARATE INCOME STATEMENT in the period from 1 January to 31 December 2019

in RSD thousand	**Note**	**2019.**	**2018.**
Interest income	3, 2.4	22,673,804	23,288,996
Interest expenses	3, 2.4	(2,285,616)	(2,871,147)
Net interest gains		**20,388,188**	**20,417,849**
Income from fees and commissions	4, 2.5	12,194,157	11,817,988
Expenses on fees and commissions	4, 2.5	(4,502,305)	(4,574,927)
Net gains from fees and commissions		**7,691,852**	**7,243,061**
Net gains from change in fair value of financial instruments	5, 2.7	185,803	318,162
Net (losses) / gains from derecognition of the financial instruments measured at fair value	6, 2.7	(2,495)	33,765
Net exchange rate gains and gains from agreed currency clause	7, 2.6	2,197,296	2,047,748
Net expenses on impairment of financial assets not measured at fair value through income statement	8, 2.7	(2,302,796)	(3,257,274)
Net (losses) / gains on derecognition of financial instruments carried at amortized cost	6, 2.7	(207,369)	630,253
Other operating income	9	119,295	234,068
Total net operating income		**28,069,774**	**27,667,632**
Salaries, salary compensations and other personal expenses	10, 2.20	(6,213,247)	(5,999,255)
Depreciation costs	11, 2.16	(1,577,139)	(1,057,751)
Other income	12	943,685	424,176
Other expenses	13	(7,284,638)	(7,800,633)
Profit before tax		**13,938,435**	**13,234,169**
Profit tax	14, 2.21	(1,608,976)	(630,059)
Profit after tax		**12,329,459**	**12,604,110**

Belgrade, 11 February 2020

Rada Radović	Dragica Mihajlović	Draginja Đurić
Head of Accounting Department	CFO	CEO

SEPARATE STATEMENT OF OTHER COMPREHENSIVE INCOME in the period from 1 January to 31 December 2019

in RSD thousand	**2019**	**2018**
Profit for the period	**12,329,459**	**12,604,110**
Components of other comprehensive income which cannot be reclassified to profit or loss:		
Decrease in revaluation reserves based on intangible assets and fixed assets	(881)	(10,523)
Negative effects of change in value of equity instruments measured at fair value through other comprehensive income	(1,568)	(1,477)
Components of other comprehensive income that may be reclassified to profit or loss:		
Positive / (negative) effects of change in value of debt instruments measured at fair value through other comprehensive income	1,212,502	(1,057,906)
Total positive / (negative) comprehensive income for the period	1,210,053	(1,069,906)
Total positive comprehensive income for the period	**13,539,512**	**11,534,204**

Belgrade, 11 February 2020

Rada Radović	Dragica Mihajlović	Draginja Đurić
Head of Accounting Department	CFO	CEO

SEPARATE STATEMENT OF CHANGES IN EQUITY in the period from 1 January to 31 December 2019

in RSD thousand	**Share capital and other equity**	**Premium on issue of shares**	**Reserves from profit and other reserves**	**Revaluation reserves**	**Retain earnings**	**Total**
Opening balance as at 1 January, 2018	**21,327,058**	**20,432,569**	**47,484,121**	**1,542,070**	**28,220,984**	**119,006,802**
Effects of the first implementation of IAS 9	-	-	-	815,727	(4,765,550)	(3,949,823)
Adjusted opening balance as at 1 January, 2018	**21,327,058**	**20,432,569**	**47,484,121**	**2,357,797**	**23,455,434**	**115,056,979**
Decrease in revaluation reserves based on intangible assets and fixed assets	-	-	-	(10,523)	-	(10,523)
Negative effects of change in value of equity instruments measured at fair value through other comprehensive income	-	-	-	(1,459)	-	(1,459)
Negative effects of change in value of debt instruments measured at fair value through other comprehensive income	-	-	-	(1,057,924)	-	(1,057,924)
Profit for the current year	-	-	-	-	12,604,110	12,604,110
Dividend payments	-	-	-	-	(20,034,339)	(20,034,339)
Other	(11,158)	-	-	-	55,500	44,342
Balance as at 31 December, 2018	**21,315,900**	**20,432,569**	**47,484,121**	**1,287,891**	**16,080,705**	**106,601,186**
Opening balance as at 1 January, 2019	**21,315,900**	**20,432,569**	**47,484,121**	**1,287,891**	**16,080,705**	**106,601,186**
Decrease in revaluation reserves based on intangible assets and fixed assets	-	-	-	(881)	-	(881)
Negative effects of change in value of equity instruments measured at fair value through other comprehensive income	-	-	-	(1,568)	-	(1,568)
Positive effects of change in value of debt instruments measured at fair value through other comprehensive income	-	-	-	1,212,502	-	1,212,502
Transfer from reserves of profit	-	-	(3,995,218)	-	3,995,218	-
Profit for the current year	-	-	-	-	12,329,459	12,329,459
Dividend payments	-	-	-	-	(20,075,923)	(20,075,923)
Other	-	-	-	-	2,292	2,292
Balance as at 31 December, 2019	**21,315,900**	**20,432,569**	**43,488,903**	**2,497,944**	**12,331,751**	**100,067,067**

Belgrade, 11 February 2020

Rada Radović
Head of Accounting Department

Dragica Mihajlović
CFO

Draginja Đurić
CEO

SEPARATE CASH FLOW STATEMENT in the period from 1 January to 31 December 2019

in RSD thousands	**2019**	**2018**
Cash inflow from operating activities	**37,954,869**	**37,224,968**
Interest	22,537,049	22,629,530
Fees	12,281,048	11,987,766
Other operating income	3,049,070	2,465,451
Dividends and profit sharing	87,702	142,221
Cash outflow from operating activities	**(19,996,129)**	**(21,463,677)**
Interest	(1,549,626)	(2,681,609)
Fees	(4,576,913)	(4,570,377)
Gross salaries, salary compensations and other personal expenses	(6,421,179)	(6,044,960)
Taxes, contributions and other duties charged to expenses	(146,041)	(173,653)
Other operating expenses	(7,302,370)	(7,993,078)
Net cash inflow from operating activities before an increase or decrease in financial assets and financial liabilities	**17,958,740**	**15,761,291**
Inflow from financial assets and increase in financial liabilities	**84,199,424**	**63,900,713**
Inflow from receivables under securities and other financial assets not intended for investment	-	37,652,977
Inflow from deposits and other financial liabilities to banks, other financial organisations, central bank and clients	84,199,424	26,247,736
Outflow from financial assets and decrease in financial liabilities	**(79,227,477)**	**(45,213,015)**
Outflow from loans and receivables from banks, other financial organisations, central bank and clients	(66,440,200)	(45,208,168)
Outflow from receivables under securities and other financial assets not intended for investment	(12,765,780)	-
Outflow from other financial liabilities	(21,497)	(4,847)
Net cash inflow from operating activities before profit tax	**22,930,687**	**34,448,989**
Profit tax paid	(1,130,627)	(1,438,889)
Dividends paid	(20,075,923)	(20,034,339)
Net cash inflow from operating activities	**1,724,137**	**12,975,761**
Cash inflow from investing activities	**37,416**	**1,497,867**
Investment in investment securities	-	-
Sale of intangible investments, property, plant and equipment	37,416	1,486,687
Sale of investment property	-	11,180
Cash outflow from investing activities	**(2,233,455)**	**(1,920,814)**
Purchase of intangible investments, property, plant and equipment	(2,233,455)	(1,920,814)
Net cash inflow from investing activities	**(2,196,039)**	**(422,947)**

Cash inflow from financing activities	**39,884,114**	**74,849,000**
Loans taken	39,884,114	74,849,000
Cash outflow from financing activities	**(41,860,634)**	**(76,829,827)**
Loans taken	(41,386,959)	(76,829,827)
Other outflow from financing activities	(473,675)	-
Net cash outflow / inflow from financing activities	**(1,976,520)**	**(1,980,827)**
TOTAL CASH INFLOW	**162,075,823**	**177,472,548**
TOTAL CASH OUTFLOW	**(164,524,245)**	**(166,900,561)**
TOTAL CASH INFLOW / OUTFLOW	(2,448,422)	10,571,987
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR	**59,790,479**	**49,358,882**
EXCHANGE RATE GAINS	426,252	363,111
EXCHANGE RATE LOSSES	(477,274)	(503,501)
CASH AND CASH EQUIVALENTS AT END-PERIOD (Note15)	**57,291,035**	**59,790,479**

Belgrade, 11February 2020

Rada Radović	Dragica Mihajlović	Draginja Đurić
Head of Accounting Department	CFO	CEO

BANCA INTESA

NOTES
TO THE SEPARATE FINANCIAL STATEMENTS

For the Year Ended 31 December 2019

CONTENT

1. CORPORATE INFORMATION

Banca Intesa Beograd a.d. Belgrade (hereinafter referred to as the "Bank") was established as a joint stock company, pursuant to the Memorandum on Association and Operations of Delta banka DD Belgrade dated 16 September 1991. On 19 September 1991, the National Bank of Yugoslavia issued a certificate and permission for the foundation of Delta banka DD Belgrade.

On 16 October 1991, the Bank was duly registered with the Commercial Court in Belgrade and subsequently commenced its operations.

Pursuant to the General Manager's Decision no. 18600 dated 7 November 2005, the Approval of National Bank of Serbia and the Decision of the Companies Register no. BD 98737/2005 dated 29 November 2005, the Bank changed its previous name into Banca Intesa a.d. Belgrade.

During the year ended 31 December 2007, the legal status change was carried out through a merger by absorption, whereby the acquirer was Banca Intesa a.d. Belgrade, and the acquired bank was Panonska banka a.d. Novi Sad. Upon registration of the procedure of merger by absorption with the Serbian Business Registers Agency, the Bank as the acquirer and the legal successor has continued to operate under its existing business name, while the acquired bank – Panonska banka a.d. Novi Sad ceased its operations without liquidation process, and its shares were withdrawn and cancelled.

During 2012, upon receipt of the previous approval of the National Bank of Serbia, the Bank's Assembly has adopted changes and amendments to the Memorandum of Association and the Articles of Association, by which it has harmonized its business and enactments with the provisions of the Law on Companies. The Serbian Business Registers Agency has registered these changes by rendering a Decision no. BD 85268/2012 dated 27 June 2012.

During 2015, upon receipt of the previous approval of the National Bank of Serbia, the Bank's Assembly has adopted changes and amendments to the Memorandum of Association and the Articles of Association, by which it has harmonized its business and enactments with the provisions of the Law on Banks. The Serbian Business Registers Agency has registered these changes by rendering a Decision no. BD 56475/2015 dated 26 June 2015.

Furthermore, in August 2015, shareholding structure of the Bank was changed and it reflects in the fact that the minority shareholder International Finance Corporation (IFC) sold its entire stake to majority shareholder Intesa Sanpaolo Holding International S.A. After this change the Bank had two shareholders, Intesa Sanpaolo Holding International S.A. and Intesa Sanpaolo S.p.A. Based on the previous change in the shareholding structure and upon the previous approval of the National Bank of Serbia, Bank's Assembly has adopted changes and amendments to the Memorandum of Association, which was registered with the Decision of the Serbian Business Registers Agency no. BD 2238/2016 dated 18 January 2016.

In December 2016, the shareholding structure of the Bank was changed once more and it reflects in the fact that the minority shareholder Intesa Sanpaolo S.p.A. sold its entire stake to majority shareholder Intesa Sanpaolo Holding International S.A. After this change the Bank has one shareholder and it is Intesa Sanpaolo Holding International S.A.

Based on the previous change of the shareholders structure of the Bank and upon receipt of the consent of the National Bank of Serbia, the Shareholders' Assembly has adopted changes and amendments of the Memorandum on Association. The change was registered at the Business Registers Agency under the decision no. BD 37271/2017 dated 5 May 2017.

The Bank is authorized by National Bank of Serbia and registered to perform the following operations: payment transactions, credit and deposit operations, issuance of payment cards; also, the Bank is registered for operations with securities, issuance of guarantees and other warranties. In accordance with articles of Law on banks, the Bank operates in accordance with principles of liquidity, security and profitability. In addition, the Bank is authorized for selling of investment units as well for representing insurance, with prior consent of National bank of Serbia.

As of 31 December 2019, the Bank operated through its Head Office located in Belgrade, Milentija Popovića 7b. The Bank network consists of associated organizational units as follows: 4 regional centers and 155 branches.

The Bank had 3,073 employees as of 31 December 2019 (31 December 2018: 2,995 employees).

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.1. Basis for the preparation and presentation of the separate financial statements

The separate financial statements of the Bank for the year ended 31 December 2019 (hereinafter: the "financial statements") have been prepared in accordance with International Financial Reporting Standards (IFRSs).

In accordance with the Law on Accounting, banks must keep their books of accounts and prepare financial statements in accordance with translated IFRSs, while, by the Law on Banks (article 50.2), it has been designated that, when compiling Annual Financial Statements, a bank should apply the IFRSs as of date which the competed authority has designed as the date of the application of these standards.

(a) New standards, amendments and interpretations to existing standards mandatory for the first time for the financial year beginning on 1 January 2019

IFRS 16 replaced IAS 17 Leasing requirements and its relevant guidelines and is effective for annual periods starting from 1. January 2019.

First time adoption effects of IFRS 16 are disclosed in the Note 2.23.

The application of the following and amended standards and IFRIC interpretations to existing standards mandatory for the first time for the financial year beginning on 1 January 2019, did not result in substantial changes to the Bank's accounting policies and did not have an materially significant impact on the Bank's accompanying separate financial statements:

- IFRIC 23 „Uncertainty over income tax treatments "(effective for annual periods starting from or after 1 January 2019). This interpretation is applied when determining taxable profit (loss), tax basis, unused tax losses, unused tax credits and tax rates, in case of uncertainties in respect of income tax treatment required by IAS 12.
- Amendments to IFRS 9 "Financial instruments" – Prepayment features with negative compensation (effective for annual periods starting from or after 1 January 2019). According to amendments, negative compensation may be regarded as "reasonable compensation" irrespective of the cause of the early termination. Financial assets with these prepayment features can therefore be measured at amortized cost or at FVOCI if they meet the other relevant requirements of IFRS 9.
- Amendments to IAS 28 "Investments in associates and joint ventures" - Long-term interests in Associated and Joint Ventures (effective for annual periods starting from or after 1 January 2019).Amendments clarify that entity applies IFRS9 in case of long-term interests in associates or joint ventures that create part of net investment in associate or joint venture, to which equity method is not applied.
- Annual Improvements to IFRS Standards "2015-2017" Cycle – IFRS 3, IFRS 11, IAS 12 and IAS 23, issued by the International Accounting Standards Board in December 2017 effective for annual periods starting from or after 1 January 2019).
- Plan amendment, curtailment or settlement (Amendments to IAS 19) – amendments of standard specify that if a plan amendment, curtailment or settlement occurs, than the current service cost and the net interest for the period after the remeasurement are determined using the assumptions used for the remeasurement. In addition, amendments to IAS 19 clarify the effect of a plan amendment, curtailment or settlement on the requirements regarding the asset ceiling.

(b) New standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Bank

At the time of the approval of the accompanying financial statements, the following new standards and interpretations that are applicable in the following reporting periods have been issued:

- Amendments to References to Conceptual Framework in IFRS Standards, effective from 1 January 2020 – amendments intend to provide more comprehensive conceptual framework, with the aim to provide to the International Accounting Standards Board complete set of tools for standards setting. It covers all aspects of standards setting, from the aim of financial reporting, through presentation and disclosure.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.1. Basis for the preparation and presentation of the separate financial statements (Continued)

(b) New standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Bank (Continued)

- Definition of a Business (Amendments to IFRS 3) effective from 1 January 2020 - The proposed amendments are intended to provide entities with clearer application guidance to help distinguish between a business and a group of assets when applying IFRS 3.
- Definition of Material (Amendments to IAS 1 and IAS 8) effective from 1 January 2020 – amendments relate to change in definition of materiality concept, practical guidelines in its application, with additional focus to application of materiality in accounting policies disclosures.
- Interest Rate Benchmark Reform (Amendments to IFRS 9, IAS 39 and IFRS 7) - effective from 1 January 2020 – amendments of relevant standards address uncertainties related to the market-wide reform of interbank offered rates (IBOR) and mainly relate to financial instruments that are qualified for hedge accounting.
- IFRS 17 Insurance Contracts - effective from 1 January 2021
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28) - Optional

The Bank’s Management is currently in the process of assessing the potential impact of the aforementioned standards and interpretations to the Bank’s financial statements, as well as the date of their entering into force.

The accompanying financial statements are separate financial statements, since they include unconsolidated captions of receivables, liabilities, operating results, changes in equity and cash flows of the Bank, excluding its subsidiaries – Intesa Leasing d.o.o. Belgrade and Intesa Invest, which are 100% owned by the Bank. The Bank recognizes its investment in this subsidiary at cost. Total asset of subsidiary Intesa Leasing is 2.44% (31.12.2018: 2.82%), while total assets of subsidiary Intesa Invest is 0.034% (31.12.2018: 0.038%) of the total Bank`s assets as at 31 December 2019.

In accordance with the provisions of IFRS 10 “Consolidated financial statements”, the Bank is exempted from preparation of consolidated financial statements, taking into consideration that the ultimate parent company, Intesa Sanpaolo S.p.A., regularly prepares and disclosed consolidated financial statements in accordance with IFRS adopted by EU. These financial statements are published on the official website of Intesa Sanpaolo Group: www.group.intesasanpaolo.com.

Although the Bank is obliged to prepare annual consolidated financial statements and submit them to the Business Registers Agency in accordance with the Law on accounting, still the Bank uses its right specified by Law on banks, article 55 paragraph 4, by which it does not include subsidiaries in annual audit of its consolidated financial statements, based on the consent of National bank of Serbia.

The Bank’s financial statements are stated in thousands of Dinars, unless otherwise stated. The Dinar (RSD) is the functional and official reporting currency of the Bank. All transactions in currencies other than functional currency are considered transactions in foreign currency.

The accompanying financial statements have been prepared under the going concern principle, which implies that the Bank will continue its operations in the foreseeable future.

In the preparation of these financial statements, the Bank has adhered to the principal accounting policies further described in Note 2.

2.2. Comparative data

Accounting policies and estimates relating to recognition and measurement of assets and liabilities, applied in the preparation of these financial statements, are consistent with those applied in the preparation of the annual financial statements of the Bank for the year31 December 2018, except for changes in accounting policies arising from application of IFRS 16, as presented in the Note 2.23.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.3. Significant accounting estimates and judgments

Use of estimates

The preparation and presentation of the financial statements requires the Bank's management to make estimates and reasonable assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of preparation of the financial statements, as well as income and expenses for the reporting period.

These estimates and assumptions are based on information available as of the date of the preparation of the financial statements. Actual results may differ from those estimates. The estimates and underlying assumptions are reviewed on an ongoing basis, while changes in estimates are recognized in the income statement in the periods in which they become known.

The estimates and assumptions that have a risk of causing material adjustments to the carrying amounts of assets and liabilities within the next financial year are addressed below.

Impairment of financial assets

The Bank recognizes impairment for expected credit losses for financial assets that are measured at amortized cost as well as for debt financial assets that are measured at fair value through other comprehensive income, lease receivables, loan commitments and issued guarantees. Carrying value of financial instruments measured at amortized cost is decreased by the amount of impairment for expected credit losses.

Judgments and estimates that the Bank uses as input in the expected credit loss model, together with the assessment on significant increase of credit risk, are disclosed in the Note 28.1. Credit risk.

Classification of financial assets

The Bank assesses business model within the assets are held. Besides, the Bank assesses if contractual cash flows of financial assets are solely payments of principal and interest (Note 2.7.2.).

Useful lives of intangible assets, property, plant and equipment ("tangible assets")

The determination of the useful lives of intangible assets, property, plant and equipment is based on historical experience with similar assets as well as on any anticipated technological development and changes influenced by wide range of economic or industry factors. The appropriateness of the estimated useful lives is reviewed annually, or whenever there is an indication of significant changes in the underlying assumptions that are basis for determination of useful life.

Due to the significant share of fixed assets in the total assets of the Bank, the impact of each change in these assumptions could materially affect the Bank's financial position, as well as the results of its operations.

Impairment of non-financial assets

At each reporting date the Bank's management reviews the carrying amounts of the Bank's intangible assets and property, plant and equipment presented in the financial statements. If there is any indication that such assets have been impaired, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying value, the carrying amount of the asset is reduced to its recoverable amount. An impairment review requires from management to make judgment concerning the cash flows, growth rates and discount rates of the cash generating units under review.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.3. Significant accounting estimates and judgments (Continued)

Provisions for litigations

The Bank is subject to a number of legal proceedings arising from its daily operations, which relate to commercial, contractual and labor disputes, which are resolved and considered in the course of regular business activity. The Bank regularly estimates the probability of negative outcomes to these matters, as well as the amounts of probable or reasonable estimated losses.

Reasonable estimates include judgments made by management, after considering information including notifications, settlements, estimates performed by the legal department, available facts, identification of other potentially responsible parties and their ability to contribute as well as prior experience.

A provision for litigation is recognized when it is probable that an obligation exists for which a reliable estimation can be made of the obligation after careful analysis of the individual matter (Note 23). The required provision may change in the future, due to new developments and as additional information becomes available. Commitments, as well as positions that do not meet the criteria for provision are disclosed, unless the possibility of transferring economic benefits is remote.

Deferred tax assets

Deferred tax assets are recognized for all unused tax credits to the extent that it is probable that expected future taxable profit will be available against which the unused tax credits can be utilized. The Bank’s management necessarily performs significant estimate in order to determine the amount of deferred tax assets that can be recognized, based on the period of occurrence, the amount of future taxable profit and strategy of tax planning strategy (Note 14(c)).

Retirement and other post-employment benefits

The costs of defined employee benefits payable upon termination of employment, i.e. retirement in accordance with the fulfilled legal requirements are determined based on the actuarial valuation. The actuarial valuation includes an assessment of the discount rate, future movements in salaries, mortality rates and fluctuation of employees. As these plans are long-term, significant uncertainties influence the outcome of the estimation. Additional information are disclosed in Note 23.

Leasing

Incremental borrowing rate used as discount rate in valuation of lease payables’ present value, is determined by analyzing internal sources of information on borrowings and is adjusted to reflect contractual lease terms and type of leased asset.

2.4. Interest income and interest expenses

Interest income and interest expenses, including penalty interest and other income and other expenses from interest-bearing assets, as well interest bearing liabilities are recognized on an accrual basis, based on obligatory terms defined by a contract between the Bank and its customers.

Interest income and interest expense are recognized in profit and loss using effective interest rate, presenting the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- The gross carrying amount of the financial asset (amortized cost before decrease for expected credit losses), or
- The amortized cost of the financial liability

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.4. Interest income and interest expenses (Continued)

When calculating effective interest rate for financial instruments that are not POCI (purchased originated credit impaired), the Bank assesses future cash flows taking into consideration all contractual terms of financial instruments, but not including expected credit losses. For POCI loans, credit-adjusted effective interest rate is calculated using estimated future cash flows including expected credit losses.

Interest income is recognized for financial assets measured at amortized cost as well as for debt instruments measured through other comprehensive income. Interest expense are recognized for financial liabilities measures at amortized cost.

Loan origination fee, as part of effective interest rate, is recognized in interest income and interest expense. Loan origination fees are calculated and collected upfront, while related income is deferred and discounted using the effective interest rate method, over the life of the loan.

After objective evidence of impairment have been identified and impairment recognized, interest income on these receivables is calculated on the amortized cost basis and by applying effective interest rate, which has been used to discount future cash flows for determining impairment losses.

2.5. Fee and commission income and fee and commission expenses

Fees and commissions income and expenses originating from providing or using the banking services are generally recognized on an accrual basis when the service has been provided.

Fees and commissions mostly comprise of fees for payment operations services, issued guarantees and other banking services.

Fee and commission income relating to current accounts and financial instruments maintenance services are recognized over time, when the service is provided.

Income relating to transaction fees are recognized in the moment of transaction occurrence.

A contract with a customer that results in recognition of financial instrument in the Bank's financial statements may be partially in the scope of IFRS 9 and partially in the scope of IFRS 15. If this is the case, then the Bank first applies IFRS 9 to separate and measure the part of the contract that is in the scope of IFRS 9 and then applies IFRS 15 to the residual.

2.6. Foreign currency translation

The items included in the Bank's financial statements are measured by using currency of the Bank's primary economic environment (functional currency). As disclosed in Note 2.1., the accompanying financial statements are stated in thousands of Dinars (RSD), which represents the functional and official reporting currency of the Bank.

Transactions denominated in foreign currency are translated into dinars at the official median exchange rate determined on the Interbank Foreign Currency Market, published by National Bank of Serbia, prevailing at the transaction date.

Assets and liabilities denominated in foreign currency at the balance sheet date are translated into dinars at the official median exchange rate determined on the Interbank Foreign Currency Market, published by National Bank of Serbia, prevailing at the balance sheet date (Note 31).

Foreign exchange gains or losses arising upon the translation of balance sheet items denominated in foreign currencies and transactions in foreign currencies are credited or charged as appropriate, to the income statement, as foreign exchange gains or losses within Net foreign exchange gains/Net foreign exchange losses and effects of contracted foreign currency clause (Note 7).

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.6. Foreign currency translation (Continued)

Gains and losses arising on translation of financial assets and liabilities indexed with the contracted foreign currency clause are credited or charged as appropriate, to the income statement, and presented within Net foreign exchange gains/Net foreign exchange losses and effects of contracted foreign currency clause (Note 7).

Commitments and contingencies denominated in foreign currency are translated into dinars at the official median exchange rate prevailing at the balance sheet date.

2.7. Financial instruments

2.7.1. Initial recognition of financial instruments

Financial instruments are initially measured at fair value, increased by transaction costs (except financial assets or financial liabilities measured at fair value through profit and loss), that are directly related to acquisition or issuance of financial asset or financial liability.

Financial assets and financial liabilities are recorded in the Bank's balance sheet in the moment when the Bank is contractually committed to the instrument. Acquisition or sale of financial assets is recorded as of the settlement date, presenting the date when asset is delivered to the counterparty.

In order to determine classification and measurement, all financial assets, except derivatives and equity investments, are analyzed by the Bank through the combination of business model managing the financial asset as well as characteristics of contractual cash flows.

2.7.2. Classification

i. Financial assets

At initial recognition, financial asset is classified in accordance with one of the following methods of measurement: at amortized cost, at fair value through other comprehensive income (FVOCI) or at fair value through profit and loss (FVTPL).

Financial asset is measured at amortized cost if it meets both of the following conditions and is designated as at FVTPL:

- Asset is held within a business model whose objective is to hold assets to collect contractual cash flows, and
- The contractual terms of the financial asset give rise on specified fates to cash flows that are solely payments of principal and interest

Debt instrument is measured as FVOCI only if it meets both the following conditions and is not designated as at FVTPL:

- The assets is held within the business model whose objective is achieved by both collecting contractual cash flows and selling contractual assets, and
- The contractual terms of the financial asset give rise on specified fates to cash flows that are solely payments of principal and interest

Debt instruments held with the aim to collect contractual cash flows and selling comprise treasury bills and the bonds of Republic of Serbia.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.7. Financial instruments (Continued)

2.7.2. Classification (continued)

On initial recognition of an equity instrument that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value through OCI, at the level of particular equity instrument. As of 31 December 2019, the Bank opt for FVOCI accounting of equity investment, other than investment in subsidiaries, since these instruments are not held for trading. This choice is made based on the each particular instrument in the moment of initial recognition and cannot be recalled.

Besides, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measures at amortized cost or at FVOCI as at FVTPL, if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

Then Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level, because this better reflects the way the business is managed, and information is provided to management.

The information considered includes policies and strategies for the portfolio, as well as their application in practice. In particular, it is important if management strategy is focused on earning contractual interest revenue, matching duration of the financial assets to the duration of liabilities that are funding those assets or realizing cash flows through the sale of the assets. Also, the Bank considers information on how the performance of the portfolio is evaluated and reported, together with information on risks affecting the performance of the portfolio and how they are managed. Besides, the Bank considers frequency, volume and timing of financial assets sales in prior periods, the reasons for sales and plans for future sales of financial assets.

Financial assets that are managed with the aim of trading, and whose performances are assessed based on the fair value, are measured as FVTPL since they are neither held in portfolio with the purpose to collect contractual cash flows nor they are held with the double purpose of collecting the contractual cash flows and selling.

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

For the purpose of this assessment, “principal” is defined as the fair value of the financial asset on initial recognition. ” Interest” is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for the other basic lending risks (e.g. liquidity risk, administrative costs), as well as profit margin.

In assessing whether contractual cash flows are solely payment of principal and interest (SPPI), the Bank considers the contractual terms of the instrument and analyses if they contain contractual terms that could change the timing or amount of contractual cash flows, resulting in fair value measurement of the instrument. Main contractual terms that are considered in assessment are: leverage features, extension and prepayment terms, characteristics that limit the Bank’s claim to cash flows to specified assets as well as features that modify consideration of time value of money, such as periodical reset of interest rates in case of financial assets with variable interest rate.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.7. Financial instruments (Continued)

2.7.2. Classification (continued)

Reclassifications

Financial assets are reclassified only in case when the business model for managing financial assets is changed. Reclassification is performed in line with the principles defined by IFRS.

Financial liabilities are not reclassified.

Financial liabilities

The Bank measured financial liabilities at amortized costs, except derivatives that are measured at FVTPL, where fair value adjustment is recognized in profit or loss.

2.7.3. Derecognition of financial assets and financial liabilities

Financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognized when any of the following criteria are fulfilled:

- the rights to receive cash flows from the asset have expired; or
- the Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a ‘pass-through’ arrangement;
- either the Bank has transferred substantially all the risks and rewards of the asset, or has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset;
- financial asset is written-off;
- subsequent changes of contractual cash-flows of financial asset occurred, resulting in significant modification of cash flows of financial asset (Note 2.7.4.).

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset, nor transferred control of the asset, the asset is recognized to the extent of the Bank’s continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Financial assets (Continued)

In case when financial asset is derecognized, cumulative gain or loss previously recognized in other comprehensive income is reclassified from equity to profit and loss in case of debt securities measured at FVOCI. However, in case of equity instruments measured at FVOCI, accumulated gain/loss recognized through other comprehensive income will not be recognized in profit and loss in the moment of derecognition but in equity.

Financial liabilities

A financial liability is derecognized when the obligation under the liability is satisfied, cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified such exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, while the difference in the respective carrying amounts is recognized in profit or loss.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.7. Financial instruments (Continued)

2.7.3. Derecognition of financial assets and financial liabilities (Continued)

The Bank ceases to recognize financial liability when the contractual terms are modified, while cash flows of modified liability are significantly changed. In that case, new financial liability is based on the modified terms and is recognized at fair value. Difference between carrying amount of financial liability and new financial liability with modified terms is recognized in profit and loss.

2.7.4. Modification of contractual cash flows

Financial assets

If contractual terms of financial asset are subsequently modified, the Bank evaluates whether the cash flows of the modified assets are substantially different. If so, then contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognized and a new financial asset is recognized at fair value.

Key criteria for significant modification are renegotiation of contracts with purpose to adjust to commercial terms, change in currency, change in debtor, negotiation of contractual clauses “pay if you can” or conversion debt to equity.

If the originally contracted cash flows of financial asset are subsequently contractually modified and such modification does not lead to derecognition of financial asset, the Bank recalculates gross carrying amount of financial asset as present value of renegotiated future cash flows, discounted at original effective interest rate and recognizes the amount, arising from adjustment with the new gross carrying amount, as modification gain or loss in profit and loss.

Abovementioned gains or losses are amortized during residual lifetime of modified financial asset.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.7. Financial instruments (Continued)

2.7.4. Modification of contractual cash flows (Continued)

Financial liabilities

The Bank derecognizes financial liability when contractual terms are modified and the cash flows of the modified liability are substantially different. In this case, new financial liability is based on the modified terms and is recognized at fair value. The difference between the carrying amount of the financial liability and new financial liability with modified terms is recognized in profit and loss.

Recognition of expected credit losses

Bank calculates expected credit losses for financial assets measured at amortized cost or for debt securities measured at fair value through other comprehensive income (FVOCI), loan commitments and issued guarantees. Carrying amount of financial instruments measured at amortized cost is decreased by the amount of expected credit losses.

Expected credit loss for financial assets measured at fair value through other comprehensive income (FVOCI) is recognized through other comprehensive income and income statement, and it should not decrease the carrying value of the asset in the balance sheet.

After the initial recognition, expected credit loss is calculated at every reporting date. Bank assesses, at each reporting date, the level of financial assets impairment for assets measured at amortized cost or at fair value through other comprehensive income (FVOCI), and as well as on contract assets. Bank's assessment is based on *"forward-looking"* expected credit loss (ECL) model.

Loss allowances is measured on either of the following bases:

- 12-month ECLs - these are ECLs that result from possible default events within the 12 months after the reporting date, and
- Lifetime ECLs - these are ECLs that result from all possible default events over the expected life of a financial instrument.

Lifetime ECL measurement applies if the credit risk of a financial asset at the reporting date has increased significantly since its initial recognition, while in the opposite case 12-month ECL measurement applies. The Bank may determine that a financial asset's credit risk has not increased significantly if the asset has low credit risk at the reporting date.

Details regarding credit risk policy are presented in Note 28.1 Credit Risk.

2.7.5. Impairment of financial assets and provisions for risks

Uncollectable receivables write-off

Financial assets' write-off / transferring to off-balance sheet is performed in accordance with the Procedure on Write-off of Uncollectable Receivables. The procedure relates to the write-off / transferring to off-balance sheet of receivables that meet the following criteria: delay in payment of receivable is more than 360 days; the Bank has failed to collect receivables despite the implementation of all activities of collection specified by its policies and procedures; judicial or extrajudicial procedures of settlement of receivables have been initiated; receivables are fully impaired. Exceptionally, receivables that do not fulfil the abovementioned requirements may be written-off / transferred to off-balance sheet if such decision is made by the competent authority, PAC (Problem Asset Committee), in accordance with the authorizations delegated by the Board of Directors. Off-balance exposure that are written-off during 2019 amount 5.71 billion dinars as of 31 December 2019 and are still subject of collection techniques.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.7. Financial instruments (Continued)

2.7.6. Renegotiated loans

If the Bank estimates that the problems of debtors and their delay in payment is temporary and that, under adjusted agreed conditions, the client could fulfil obligations toward Bank regularly, the Bank seeks to restructure loans rather than to activate collaterals. This may involve extending repayment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Renegotiated loans are continuously reviewed and monitored, to ensure that all criteria are met and that future payments are likely to occur.

2.8. Loans and receivables from banks and other financial organizations and Loans and receivables from customers (hereinafter: Loans and receivables)

Loans and receivables include:

- Loans and receivables valued at amortized cost. Initial recognition of these loans and receivables is at fair value increased by direct transactional costs, while subsequently they are measured at amortized cost using effective interest rate method (Note 2.7.2) and
- Loans and receivables measured at fair value through profit or loss, in accordance with business model or cash flow characteristics

As of 31 December 2019, the Bank's portfolio does not include loans that meet the criteria to be valued at fair value through profit or loss.

2.9. Securities

Securities caption in the Statement of financial position includes:

- Debt securities measured at fair value through other comprehensive income (FVOCI)

For debt securities measured at FVOCI, gains or losses are recognized in OCI, except interest income, expected credit losses and foreign exchange differences that are recognized in profit and loss.

When debt securities measured at FVOCI are derecognized, accumulated gain or loss previously recognized in OCI in equity is reclassified from equity to profit and losses.

- Equity investments measured at fair value through other comprehensive income, excluding investments in subsidiaries and associates

For equity investments that are accounted as FVOCI, changes in fair value after initial recognition are recognized in equity and are never recognized in profit and loss, not even on sale. Accumulated gains or losses recognized in other comprehensive income are transferred to retained earnings when equity investment is derecognized.
Equity investments that are accounted at FVOCI are not subject of impairment. Dividends on equity investments are accounted in profit and loss.

- Debt securities measures at fair value through profit and loss (FVTPL)

For debt securities measured at FVTPL, gains and losses from fair value adjustments are recorded through profit and loss and are not subject to impairment.

- Shares measured at fair value through profit and loss (FVTPL)

For shares measured at FVTPL, gains and losses on fair value adjustments are recognized through profit and loss.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.9. Securities (Continued)

Interest income on treasury government bonds of the Republic of Serbia is calculated and recognized daily in the income statement.

Dividend income in respect of investments in shares of other legal entities, and income from investments in equity instruments of other legal entities is recognized as income when the shareholder's right to receive payment is established.

2.10. Receivables from derivatives and Liabilities based on derivatives (hereinafter: derivatives)

The Bank has in its portfolio financial derivatives, for which foreign exchange rate is basic underlying variable. Derivatives used by the Bank are currency swap (FX swap) and currency forward (FX forward) contracts. For accounting purposes, derivatives are classified as financial instruments held for trading and are recorded in the balance sheet at fair value.

Derivatives are initially recognized when the Bank becomes a party to an agreement with the other contractual party (the agreement date). The notional amount of the derivative contract is recorded in the off-balance sheet, and initial positive or negative fair value of the derivative is recorded in the balance sheet as an asset or a liability. The initial recognition of fair value applies to cases when the market price for the same or a similar derivative on an organized market is available, and when the price differs from the price at which the Bank contracted the derivative. Hence, the derivatives contracted by the Bank with the customers operating in Serbia do not have initially recognized fair value, since there is no active market for similar derivatives in the country. When an active market for such derivatives develops, i.e. when the relevant market information becomes available, the Bank will recognize in the balance sheet (as asset or liability) and the income statement (initially positive or negative fair value) the difference between the market value of transactions and initial fair value of derivatives determined using valuation techniques.

In accordance with the existing accounting policy of the Bank, adjustments to fair value of financial instruments held for trading are recognized at the end of each month, and the effect of changes in fair value are recognized in the income statement as the increase or decrease of fair value. Derivatives are recognized as derivatives receivable or liabilities based on derivatives, depending on whether their fair value is positive or negative. Derivatives are derecognized at the moment of expiry of contracted rights and obligations arising from derivatives (exchange of cash flows), i.e. at termination date. At that moment, the ultimate effect fair value adjustment of currency financial derivatives (that the Bank currently solely as in derivatives portfolio) is recorded against realized foreign exchange differences, while all previously recognized changes in fair value (monthly recorded through unrealized foreign exchange gains/losses) are reversed.

Since there is neither an active market for derivatives in Serbia, nor a possibility for determining fair value of derivatives by reference to a quoted market price, the Bank uses the methodology of discounting future cash flows arising from derivatives in order to determine fair value. This methodology of calculation is generally accepted by market participants in countries that have developed markets with active trading in derivatives and the calculated fair value represents a reliable estimate of the fair value of derivatives that would be achieved on an active market.

The methodology mainly incorporates market factors (middle exchange rate, market interest rates and similar) to the best possible extent and is consistent with generally accepted methodologies for valuation of derivatives. At least once per month, the Bank performs back-testing and calibration of the implemented methodology for calculation of fair value by using market variables and alternative calculation methods.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.11. Deposits and other financial liabilities due to banks, other financial organizations and Central Bank and Deposits and other financial liabilities due to customers

Deposits and other financial liabilities due to banks, other financial organizations and central banks, as well as deposits and other financial liabilities due to customers are initially recognized at fair value decreased by transaction costs, except for financial liabilities at fair value through profit and loss. After initial recognition, mentioned financial liabilities are subsequently measured at amortized cost using the effective interest rate method.

Within this caption, borrowings are initially measured at fair value net of transaction costs incurred and are subsequently measured at amortized cost.

Borrowings are classified as current liabilities, unless the Bank has unconditional right to postpone the settlement of obligations for at least 12 months after the balance sheet date.

2.12. Other liabilities

Trade payables and other short-term operating liabilities are presented at nominal value.

2.13. Offsetting financial instruments

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

2.14. Cash and balances with central bank

Cash and balances with central bank, in Balance sheet, are comprised of cash in dinars and in foreign currency, i.e. is cash at gyro and current accounts, cash on hand and other cash in dinars and foreign currency, gold and other precious metals, deposited liquid surpluses and obligatory reserves in foreign currency held at accounts with the National Bank of Serbia. Mentioned assets are highly liquid financial assets with contractual maturity up to 3 months and bear insignificant risk of their fair value change.

Cash and cash equivalents are measured at amortised cost in the balance sheet statement.

2.15. Intangible assets

Intangible assets consist of software, licenses and intangible assets under construction. Intangible assets are carried at cost less any accumulated amortization.

Licenses are initially recognized at cost. They have limited useful life and are carried at cost less accumulated amortization. Amortization is calculated using the straight-line method in order to fully write off the cost of these assets over their estimated useful lives (from 5 to 10 years).

Computer software licenses are capitalized for costs incurred in acquiring and brining the specific software into use. These costs are amortized over their estimated useful lives (from 2 to 5 years).

Costs associated with software maintenance are recognized as an expense when incurred.

Costs that are directly associated with identifiable and unique software controlled by the Bank, and which will probably generate economic benefits exceeding costs beyond one year, are recognized as intangible assets. Direct costs include the salaries of the team that developed the software, as well as appropriate portion of related overheads.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.15. Intangible assets (Continued)

Amortization of intangible assets is calculated using the straight-line method to write down the cost of intangible assets over their estimated useful lives, in all accounting periods, as follows:

- Licenses and similar rights	10% - 20%
- Software except Core information system	20% - 50%
- Core information system	14.29%

Comparing to 2018, there were no changes in estimated useful lives of intangible assets.

Intangible assets include unamortized software in progress, since it is still not in use.

2.16. Property, plant, equipment, leased assets, investment property and non-current assets held for sale

(a) Property, plant and equipment

Fixed assets (property, plant and equipment) are tangible assets:

- that are held by the Bank for the own use in providing services within its registered business or for administrative purposes; and
- for which it is expected to be used more than one year period.

Property, plant and equipment are recognized as an asset:

- when it is probable that future economic benefits on the basis of such asset will inflow to the Bank, and
- when the cost of such asset can be reliably measured.

At initial recognition, property, plant and equipment are stated at cost.

Cost includes expenditure that is directly attributable to the acquisition of an asset.

Subsequent costs are included in the asset’s carrying amount or are recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the income statement of the financial period in which they are incurred.

Property, plant and equipment are subsequently measured at fair value using the revaluation model or at cost.

As of 31 December 2019 the revaluation model (fair value) was used for the subsequent measurement of real estate, while other tangible assets were subsequently measured at cost.

Revaluation is performed regularly, in a frequency sufficient for providing that the carrying amount does not differ significantly from the amount that would be obtained by applying the fair values model at the end of the reporting period.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.16.1. Property, plant and equipment and investment property (Continued)

(b) Investment property

As of 31 December 2019, the Bank owns property as investments for generating rental income and/or increase in the market value of the property.

In accordance with IAS 40, investment property is recognized as an asset if and only if:

- it is probable that the entity will in the future realize the economic benefits from investment property, and
- when the cost such asset can be reliably measured.

Investment property is initially measured at cost. Transaction costs are included in the initial measurement. Upon initial recognition, the investment property is measured at fair value. The gain or loss arising from the change in the fair value of an investment property is recognized in the income statement of the period in which it is incurred.

(c) Leased assets

Policy effective from 1 January 2019

At inception of a contract, the Bank assesses whether a contract is, one contains, a lease. A contract is, or contains lease, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Bank uses definition of lease in IFRS 16. This policy is applied for contracts entered into (or changed) on or after 1 January 2019.

Bank acting as lessee

At commencement or on modification of a contract that contains a lease component, the Bank allocates consideration in the contract to each lease component on the basis of its relative stand-alone price.
The Bank recognizes a right-to-use asset and lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to branches offices. Besides, cost of right-to-use asset also includes:

- all payments on lease performed up to the first day of lease term, reduced by eventually received incentives in respect of leasing;
- all initial direct costs generated by lessee and
- estimate of costs that lessee will generate with dismantling and removal of the property in question, restoration of the location of the property or restoration of the property as it is specified in the lease agreement itself. Liability for related costs for lessee occurs at the first day of lease term, or as a consequence of leased asset usage during the particular period.

Right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-to-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The Bank as lessee uses exemptions allowed by standard in a way that short-term lease (up to 1 year) and low-value lease (if the value of leased asset, when new, is below 5,000 EUR net of tax) are not recognized as right-of-use-assets, while all payments that occur in respect to such leases are recognized as expense for the period.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.16.1. Property, plant and equipment and investment property (Continued)

c) Leased assets (Continued)

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date. Future lease payments are discounted using the interest rate implicit if such rate is readily available. If rate is not easily determinable, the Bank uses incremental borrowing rate of lessee effective at the inception date of lease term.

Lease payments included in the measurement of the lease liability at commencement of lease comprise the following payments related to right-of-use assets during lease term, which are not settled by the commencement date:

- fixed payments, reduced by eventually received incentives in relation to lease;
- variable payments that depend on certain index or rate and which are initially measured using index or rate at the commencement date.
- amounts expected to be payable under residual value guarantee;
- the exercise price under a repurchase option that the Bank is reasonably certain to exercise;
- penalties for early termination of a lease, if lease term shows that the lessee used such option

After initial recognition, lease liabilities are subsequently measured in a way to:

- increase their carrying value, so that interest on lease liability is included
- decrease their carrying value by the amounts paid on leasing; and
- remeasure carrying value with the aim to include all eventual reassessments or changes in lease relevant for its reassessment

Interest on lease liabilities during the lease period will be equal to amount that brings constant periodical rate on the residual lease liability.

Lessee remeasures lease liability by discounting of revised lease payments at revised discount rate (for the remaining lease term) in case of one of the following:
- change in lease maturity
- change in the repurchase option of leased asset

Lease modifications

Lease modification is treated as separate lease when:
- such modification expands the lease scope, by adding the right to use of one or more assets, and at the same time
- rent is increased proportionately to stand-alone price of such expansion and all necessary adjustments of that stand-alone price, in order to reflect the circumstances of the particular contract

If modification of lease is not treated as separate lease, than with the effective date of such modification, the Bank applies standards and allocates compensation from modified contract, determines duration of modified lease term and remeasures lease liability by discounting revised lease payments at revised discount rate.

In case of modification that are is treated as separate lease, lease liability is remeasured in a way to:
- decrease carrying value of right-to-use asset, in order to reflect partial or complete termination of lease for those modifications which decrease the scope of lease. Any gain or loss in respect to partial or full lease termination is recognised in income statement;
- adjust right-to-use asset for all other lease modifications

The Bank discloses right-to-use assets in position Property, plant and equipment and they relate to lease of real estate, vehicles, ICT equipment and other equipment, while disclosed lease liability within item Other liabilities in financial statements.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.16. Property, plant, equipment and investment property and non-current assets held for sale (Continued)

(c) Leased assets (Continued)

Policy effective up to 1 January 2019

Up to 1 January 2019, the Bank applied IAS 17 for accounting of leases.

Finance leasing

Bank as a lessee

Finance leases, which transfer to the Bank substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the cost of lease object and recognized within property, plant and equipment, with the corresponding liability to the lessor included in other liabilities.
Lease payments are apportioned between finance charges and reduction of the lease liability, to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the income statement as interest expense.

The lease agreement specifies that the Bank can, but does not have to, obtain ownership of the leased asset after the expiration of the lease agreement.

Operating leasing

Bank as lessee

A lease is classified as an operating lease if it does not transfer to the Bank substantially all the risks and rewards incidental to ownership.

The total payments made under operating leases are recognized as expenses within the income statement, when incurred, using a straight-line basis over the period of the lease.

(d) Depreciation

Depreciation was calculated using the straight-line method applied to the cost of property, plant and equipment, using the following prescribed annual rates in order to write them off over their useful lives, in all accounting periods:

	2019	2018
Buildings	3-%-5%	3% - 5%
Computer equipment	20%	20%
Furniture and other equipment	7% - 25%	7% - 25%

Depreciation of right-of-use assets is calculated at rates that correspond the type of particular leased asset.

In determining the basis for depreciation, the depreciable values of assets equal their cost or revalued amount are not decreased by residual value, since the Bank assesses the residual values of assets as nil.

Calculation of depreciation of property and equipment commences at the beginning of the month following the month when an asset is put into use. Depreciation charge is recognized as expense for the period when incurred.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.16. Property, plant, equipment and investment property and non-current assets held for sale (Continued)

(d) Depreciation

The useful live of asset is reviewed periodically, and adjusted if necessary, at each balance sheet date. Change in the expected useful life of an asset is considered as a change in an accounting estimate.

Gains or losses from the disposal of property, plant and equipment are credited or debited in the income statement, included in other operating income or other expenses, respectively.

The calculation of depreciation for tax purposes is determined in accordance with the Law on Corporate Income Tax of the Republic of Serbia and the Rules on the Manner of Fixed Assets Classification in Groups and Depreciation for Tax Purposes, which gives rise to deferred taxes (Note 14(c)).

2.16.2. Non-current assets held for sale

In accordance with IFRS 5 “Non-current assets held for sale and discontinued operations”, the Bank classifies a fixed asset as a non-current asset held for sale if its carrying amount is expected to be recovered primarily through a sales transaction, rather than through further use. An asset classified as held for sale must be available for immediate sale in its present condition and its sale must be probable.

In order to make sale probable, management of the Bank must be committed to a plan to sell the asset and an active program to locate a buyer and completion of the plan must have been initiated, and the asset must be actively marketed for sale at a price that is reasonable in relation to its current fair value. The sale should occur within one year from the date of recognition. Events or circumstances out of the Bank’s control may prolong sale completion period to more than one year.

A non-current asset classified as held for sale is measured at the lower of: the:
- carrying amount; or
- fair value less costs to sell.

Once a non-current asset is recognized as a held-for sale it is no longer depreciated (Note 19).

2.17. Impairment of non-financial assets

In accordance with the adopted accounting policy, at each balance sheet date, the Bank’s management reviews the carrying amounts of the Bank’s intangible assets, property, plant and equipment and investment property.

If there is any indication that such assets have been impaired, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. If the recoverable amount of an asset is estimated to be less than its carrying value, the carrying amount of the asset is reduced to its recoverable amount, being the higher of an asset’s fair value less costs to sell and value in use. Impairment losses, representing the difference between the carrying amount and the recoverable amount of tangible and intangible assets, are recognized in the income statement as required by IAS 36 “Impairment of Assets”.

Non-financial assets (other than goodwill) that suffered impairment are reviewed for possible reversal of impairment at each reporting date.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.18. Provisions and contingencies

Provisions are recognized when the Bank has a present obligation, legal or constructive, as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

In order to be maintained, the best possible estimates are considered, determined and, if necessary, adjusted at each balance sheet date. When the outflow of the economic benefits is no longer probable in order to settle legal or constructive liabilities, provisions are derecognized in income. Provisions are taken into account in accordance with their type and they can be used only for the expenses they were initially recognized. Provisions are not recognized for future operating losses.

Contingent liabilities are not recognized in the financial statements. Contingent liabilities are disclosed in the notes to the financial statements (Note 29), unless the possibility of outflow of resources embodying economic benefits is remote.

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

2.19. Equity

Equity consists of share capital (ordinary shares), other capital, share premium, reserves from profit and retained earnings.

Dividends on ordinary shares are recognized as a liability in the period in which the decision on their payment has been made. Dividends for the year that are declared after the balance sheet date are disclosed as an event after the reporting period.

2.20. Employee benefits

(a) Employee taxes and contributions for social security

In accordance with the regulations prevailing in the Republic of Serbia, the Bank is obliged to pay taxes and contributions to various state social security funds. These obligations involve the payment of contributions on behalf of the employee and by the employer, in an amount calculated by applying specific rates prescribed by law.

The Bank is also legally obligated to withhold contributions from gross salaries to employees, and on their behalf to transfer the withheld portions directly to the appropriate government funds. The Bank has no legal obligation to pay further benefits due to its employees by the Pension Fund of the Republic of Serbia upon their retirement.

(b) Termination benefits arising from restructuring

Termination benefits are payable when employment is terminated or employee is voluntarily retired, or whenever an employee accepts voluntary redundancy in exchange for these benefits.

The Bank recognizes termination benefits when it is demonstrably committed to either: terminate the employment of current employees according to a detailed formal plan without possibility of withdrawal; or provide termination benefits as a result of an offer made to encourage voluntary redundancy in order to decrease number of employees.

(c) Other employee benefits - retirement benefits

In accordance with the Labor Law and Article 31 of the General Collective Agreement, the Bank is obligated to pay retirement benefits in the amount equal to 3 average salaries realized in the Republic of Serbia, according to the latest data published by the state authority responsible for statistics. The entitlement to these benefits usually depends on the employee remaining in service up to retirement age and/or the completion of a minimum service period. The expected costs of these benefits are accumulated over the period of employment.

Provision for retirement benefits and unused days of vacation are calculated by an independent actuary and are recognized in the balance sheet at the present value of discounted estimated future outflows (Note 23(c)).

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.21. Taxes and contributions

(a) Income tax

Current income tax

Current income tax represents the amount that is calculated and paid in accordance with the effective Corporate Income Tax Law of the Republic of Serbia. During the year, the Bank pays income tax in monthly instalments, based on the prior year's Tax return. Final tax base used for calculating income tax at the prescribed rate of 15% is disclosed in the Tax return.

In order to determine the amount of taxable income, accounting profit is adjusted for certain permanent differences, as defined by the tax regulations through Tax balance, which is to be submitted within 180 days after the end of the period for which the tax liability is determined, except in the case of status changes:

- of status changes resulting with taxpayer termination, when tax return is submitted within 60 days from the date of status change
- bankruptcy debtor or legal entity in liquidation, under which bankruptcy proceeding has been suspended due to sell of bankruptcy debtor as legal entity, or liquidation procedure has been terminated – tax return is submitted within 15 days from the date of the decision on termination of bankruptcy/liquidation proceedings validity.

Deferred income tax

Deferred income tax is recognized using the balance sheet method on temporary differences at the balance sheet date arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Tax rate enacted at the balance sheet date is used to determine the deferred income tax amount.

Deferred tax liabilities are recognized for all taxable temporary differences, except where the deferred tax liability arises from the initial recognition of goodwill or from an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and in respect of taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not be reversed in the foreseeable future.

Deferred tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profits will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized, except where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit, nor taxable profit or loss; and in respect of deductible temporary differences associated with investments in subsidiaries, associates and joint ventures when deferred tax assets are recognized only to the extent that it is probable that the temporary differences will be reversed in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.21. Taxes and contributions (Continued)

(a) Income tax (Continued)

Deferred income tax (Continued)

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on the official tax rates and regulations that have been enacted or substantively enacted as of the balance sheet date.

Current and deferred taxes are recognized as income or expense and are included in the profit for the period.

Deferred income taxes related to items that are recorded directly in equity are also recorded in equity.

Transfer pricing

Up to the date of Bank's financial statements, Tax balance for 2019 has not been submitted, considering that deadline for its submission is 180 days from the date for which the tax is determined. Bank has calculated tax effects in accordance with provisions of Corporate income tax law. Bank has not yet finished transfer pricing study, however, the management believes that there will not be material effects on 2019, since so far there were no or minimal corrections based on related parties transactions, and there was no significant changes of services types in 2019, compared to the previous year.

(b) Taxes and contributions not related to operating result

Taxes and contributions not related to operating result include property tax, value added tax, contributions on salaries charged to employer, as well as other taxes and contributions that are paid in accordance with the tax regulations of the Republic of Serbia and local tax regulations. These taxes and contributions are included within other expenses (Note 13).

2.22. Funds managed on behalf of third parties

The funds that the Bank manages on behalf of, and for the account of third parties, are disclosed within off-balance sheet items (Note 26). The Bank bears no risk in respect of repayment of these placements.

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.23. First time adoption of IFRS 16

The Bank applied IFRS 16 “Leases” starting from 1 January 2019, by using modified retrospective approach, where the value of right-of-use assets corresponds to the value of lease liability. Therefore, there are neither effects of the first time adoption within retained earnings as of 1 January 2019, nor change of comparative data and their disclosures since they are presented in line with IA 17 requirements.

In transferring to IFRS 16, the Bank applied IFRS 16 solely to the contracts that were identified as leasing by previous standard IAS 17.

Bank as lessee

As a lessee, the Bank leases business premises, cars and IT equipment. Up to 31 December 2018, this leasing was classified as operating lease by IAS 17, based on its assessment of whether the lease transferred substantially all of the risks and rewards incidental to ownership of the underlying asset to the Bank. Starting from 1 January 2019 and application of IFRS 16, the Bank recognizes right-of-use asset and relevant lease liability in order to account for the lease of business premises, cars and IT equipment in the balance sheet.

At commencement or modification of a contract that contains lease component, the Bank allocated the consideration in the contract to each lease component on the basis of its relative stand-alone price.

From the first time adoption of IFRS 16, lease liability is accounted at present value of future lease payments, discounted at incremental borrowing rate of the Bank as of 1 January 2019, as disclosed in the tables below.

Right-of-use asset is measured at its carrying amount as if IFRS 16 had been applied since the commencement date, discounted at the Bank’s incremental borrowing rate as of the first time adoption date.

The Bank used exemptions allowed by IFRS 16, and therefore did not recognize neither right-of-use asset nor related liability in case of lease with contractual maturity below 12 months from the date of the first time adoption of the standard, as well as in the case of low-value leases.

Effects of the first-time adoption IFRS 16

Effect of the first-time adoption on the financial statements is presented as follows:

	In thousand RSD 01.01.2019
Right-of-use assets within tangible assets	**2,185,877**
Deferred tax asset	-
Lease liability	**2,185,877**
Retained earning	-
Prepaid rents as of 31.12.2018	12,530

2. PREPARATION AND PRESENTATION BASIS OF THE SEPARATE FINANCIAL STATEMENTS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.23. First time adoption of IFRS 16 (Continued)

When measuring lease payments for leasing that is classified as operating, the Bank discounted lease payments by using incremental borrowing rate at 1.73%, as of 1 January 2019.

	In thousand RSD
	01.01.2019
Commitments for operating lease as of 31 December 2018 are disclosed in accordance with IAS 17 in the financial statements	2,969,385
Recognition exemption for low value assets	(75,146)
Recognition exemption for leases with less than 12 months at transition to IFRS 16	(34,730)
Tax effects (VAT and withholding tax)	(467,537)
Discount	(218,625)
Prepaid rent liability as of 31.12.2018	12,530
Total lease liability recognized as of 1 January 2019	**2,185,877**

2.24. IBOR reform of interest rates

In September 2019, the International Accounting Standards Board issued amendments to IAS 39, IFRS9 and IFRS 7 to address uncertainties related to the market-wide reform of interbank offered rates (IBOR reform). The amendments predominantly affect financial instruments qualifying for hedge accounting under IAS 39 and IFRS 9. They are effective for annual periods beginning on or after 1 January 2020. Since the Bank does not apply hedge accounting so far, these amendments are not applicable for the Bank’s operations.

Bank has material balance sheet positions tied to IBOR rates, predominantly EURIBOR. Since the project of IBOR reform evolution is run at the ISP Group level, the Bank is in constant communication with the Parent bank in this respect.

3. INTEREST INCOME AND INTEREST EXPENSES

(a) Interest income and expenses by sector structure are presented as follows:

In RSD thousand

	2019	2018
Interest income		
– Central bank and other banks	665,552	662,452
– Holding companies	-	1
– Corporate customers	5,251,302	5,146,798
– Retail customers	13,405,152	12,367,358
– Public sector	2,915,767	4,544,718
– Foreign banks and financial organizations	102,139	79,318
– Foreign entities	157,206	187,594
– Other customers	176,686	300,758
Total	**22,673,804**	**23,288,996**
Interest expenses		
– Central bank and other banks	(112,565)	(85,177)
– Corporate customers	(568,610)	(924,184)
– Retail customers	(447,515)	(415,245)
– Public sector	(845,863)	(1,054,612)
– Foreign banks and financial organizations	(282,316)	(271,469)
– Foreign entities	(4,181)	(12,984)
– Other customers	(24,566)	(107,476)
Total	**(2,285,616)**	**(2,871,147)**
Net interest income	**20,388,188**	**20,417,849**

Total interest income on impaired loans for the year ended 31 December 2019 amounts to RSD 183,523 thousand (2018: RSD 278,779 thousand).

(b) Interest income and expenses by type of financial instruments are presented as follows:

In RSD thousand

	2019	2018
Interest income		
Loans	19,148,832	18,100,502
REPO transactions	203,250	195,700
Obligatory reserves	326,461	376,805
Deposits	154,751	117,446
Securities	2,677,725	4,324,397
Other placements	162,785	174,146
Derivatives	102,801	-
Total	**22,673,804**	**23,288,996**
Interest expenses		
Loans	(287,964)	(313,113)
Deposits	(1,756,158)	(1,629,333)
Securities	(205,435)	(928,003)
Leasing	(35,616)	-
Other interest expenses	(443)	(698)
Total	**(2,285,616)**	**(2,871,147)**
Net interest income	**20,388,188**	**20,417,849**

3. INTEREST INCOME AND INTEREST EXPENSES (Continued)

(c) Interest income and expenses by measurement method are presented as follows:

		In RSD thousand
	2019	**2018**
Interest income		
Financial assets at amortized cost	19,996,080	18,964,600
Financial assets fair value through OCI	2,677,724	4,324,397
Total	**22,673,804**	**23,288,996**
Interest expenses		
Financial assets at amortized cost	(2,080,182)	(1,943,144)
Financial assets fair value through OCI	(205,434)	(928,003)
Total	**(2,285,616)**	**(2,871,147)**
Net interest income	**20,388,188**	**20,417,849**

Interest income calculated using the effective interest method as of December 31st, 2019 is 22.673,804 RSD (2019: 23,288,996 thousand of RSD) , it is refer on financial assets at amortized cost and Financial assets fair value through OCI.

4. FEE AND COMMISSION INCOME AND EXPENSES

In RSD thousand

	RETAIL		CUSTOMERS (except retail)		UKUPNO	
	2019	**2018**	**2019**	**2018**	**2019**	**2018**
Fee and commission income						
Fee for banking services:						
– Domestic payment transaction services	75,522	88,893	2,814,877	2,624,304	2,890,399	2,713,197
– International payment transaction services	132,825	114,377	801,417	771,436	934,242	885,813
– Loan operations	83,685	122,693	77,139	82,953	160,824	205,646
– Cards operations	23,626	11,421	4,506,870	4,402,419	4,530,496	4,413,840
Total	**315,658**	**337,384**	**8,200,303**	**7,881,112**	**8,515,961**	**8,218,496**
Commissions related to issued guaranties and letter of credits	155,800	172,093	604,809	599,004	760,609	771,097
Current accounts maintenance	1,993,618	1,870,569	485,757	464,998	2,479,375	2,335,567
Fees slips, EDB and Telekom	164,402	196,494	-	-	164,402	196,494
Other fee and commission	80,881	115,378	192,929	180,956	273,810	296,334
Total	**2,710,359**	**2,691,918**	**9,483,798**	**9,126,070**	**12,194,157**	**11,817,988**
Fee and commission expenses						
Payment services fee:						
– Domestic	-	-	(193,501)	(183,189)	(193,501)	(183,189)
– International	-	-	(169,569)	(167,991)	(169,569)	(167,991)
National Bank of Serbia’s fee and commission	-	-	(79,149)	(79,330)	(79,149)	(79,330)
Credit Bureau’s fees	-	-	(134,496)	(164,027)	(134,496)	(164,027)
Cards operations fee	-	-	(3,610,557)	(3,739,792)	(3,610,557)	(3,739,792)
Other fees and commissions	-	-	(315,033)	(240,598)	(315,033)	(240,598)
Total	**-**	**-**	**(4,502,305)**	**(4,574,927)**	**(4,502,305)**	**(4,574,927)**
Net fee and commission income	**2,710,359**	**2,691,918**	**4,981,493**	**4,551,143**	**7,691,852**	**7,243,061**

5. NET GAINS/LOSSES FROM CHANGES IN FAIR VALUE OF FINANCIAL INSTRUMENTS

In RSD thousand

	2019	2018
Gains from changes in value of:		
- currency swap	153,156	325,332
- forward	11,622	6,507
- financial instruments measured at fair value through profit and loss account- Securities	22,407	33,384
- gold and silver	16,317	7,642
- liabilities at arising from purchased shares-ISP	225	521
Total	**203,727**	**373,386**
Losses from changes in value of:		
- currency swap	(7,869)	(20,908)
- forward	-	(589)
- financial instruments measured at fair value through profit and loss account- Securities	(5,715)	(27,426)
- gold and silver	(4,256)	(5,917)
- liabilities at arising from purchased shares-ISP	(84)	(384)
Total	**(17,924)**	**(55,224)**
Net gains	**185,803**	**318,162**

6. NET GAINS/LOSSES ARISING FROM DERECOGNATION OF FINANCIAL INSTRUMENTS

a) Measured at fair value

		In RSD thousand
	2019	**2018**
Gains arising from derecognition of:		
- financial instruments measured at fair value through profit and loss	1,605	320
- financial instruments measured at fair value through OCI	-	38,532
Total	**1,605**	**38,852**
Losses arising from derecognition of:		
- financial instruments measured at fair value through profit and loss	(4,100)	-
- financial instruments measured at fair value through OCI	-	(5,087)
Total	**(4,100)**	**(5,087)**
Net gains/(losses)	**(2,495)**	**33,765**

b) Measured at amortized cost

		In RSD thousand
	2019	**2018**
Gains arising from derecognition of:		
- financial instruments measured at amortized cost	401,280	645,484
Total	**401,280**	**645,484**
Losses arising from derecognition of:		
- financial instruments measured at amortized cost	(608,649)	(15,231)
Total	**(608,649)**	**(15,231)**
Net gains/(losses)	**(207,369)**	**630,253**

Law on the conversion of housing loans indexed in CHF (Official Gazette RS no. 31/2019) is issued in May 2019. According to the obligation prescribed by this Law the Bank offered to its clients, with exposure indexed in CHF, conversion of the related remaining debt into debt linked to EUR currency, at conversion exchange rate and with relevant interest rate prescribed by this Law.

The Bank reversed impairment of loan exposures in CHF at the date of conversion through the gains arising from derecognition of financial instruments that are measured at amortised cost in the amount 167,236 thousand dinars. Within the same position, the Bank also recorded reversal of provisions for litigations in the amount 3,021 thousand dinars that related to loans in CHF which were converted into loans in EUR during 2019.

The conversion amount is reduced by 38%, out of which 23% at expense of the Bank while 15% is compensated by the Republic of Serbia through issuance of its bonds. The Bank recognised reduction of the debt conversion amount within losses arising from derecognition of financial instruments that are measured at amortised cost in the amount 570,803 thousand dinars. Within the same position, the Bank also recorded other receivables from clients related to the loans in CHF in the amount 1,760 thousand dinars.

7. NET FOREIGN EXCHANGE GAINS AND EFFECTS OF CONTRACTED FOREIGN CURRENCY CLAUSE

In RSD thousand

	2019	2018
Foreign exchange gains	19,038,175	19,889,523
Positive effects of contracted foreign currency clause application	2,034,026	2,834,849
Total	**21,072,201**	**22,724,372**
Foreign exchange losses	(15,718,266)	(17,574,493)
Negative effects of contracted foreign currency clause application	(3,156,639)	(3,102,131)
Total	**(18,874,905)**	**(20,676,624)**
Net gains	**2,197,296**	**2,047,748**

8. NET GAINS/LOSSES ARISING FROM IMPAIRMENT OF FINANCIAL ASSETS NOT CARRIED AT FAIR VALUE THROUGH PROFIT OR LOSS (Continued)

a) Overview by classes

	2019	2018
Revenue from reversal of impairment of financial assets at amortized cost	3,526,360	1,923,903
Revenue from reversal of provisions from off-balance sheet items	1,108,918	329,171
Revenues from collected written-off financial assets at amortized cost	398,69	391,038
Revenue from reversal of impairment of financial assets at fair value through OCI	110,982	537,587
Total	**5,144,951**	**3,181,699**
Impairment losses of financial assets at amortized cost	(7,034,984)	(5,583,180)
Provisions losses from off-balance sheet items	(210,687)	(683,726)
Written-off uncollectible financial assets at amortized cost	(40,879)	(95,313)
Impairment losses on financial assets at fair value through OCI	(161,197)	(76,754)
Total	**(7,447,747)**	**(6,438,973)**
Net impairment loss	**(2,302,796)**	**(3,257,274)**

(b) Movements in the allowance for impairment of financial assets and provisions for credit risk-weighted off-balance sheet items

Movements in the allowance for impairment of balance-sheet items and provisions during the years ended 31 December 2019 and 2018 were as follows:

Movements in the allowance for impairment and provisions in 2019	**In RSD thousand**
Opening balance – 1st January 2019	**18,082,825**
Charge for the year	7,245,671
Reversal of impairment losses and release of provisions during the year	(4,635,278)
Reversal of impairment losses and release of provisions during the year due to CHF loan conversion	(167,236)
Increase in provisions due to exchange rate changes	38,038
Reversal of provisions due to exchange rate changes	(75,658)
Transfer to off-balance sheet items	(5,938,028)
Sale (transfer) of receivables	(1,021,493)
Reversal of provisions due to passage of time (unwinding)	(183,523)
Closing balance - 31 December 2019	**13,345,319**

8. NET GAINS/LOSSES ARISING FROM IMPAIRMENT OF FINANCIAL ASSETS NOT CARRIED AT FAIR VALUE THROUGH PROFIT OR LOSS (Continued)

(b) Movements in the allowance for impairment of financial assets and provisions for credit risk-weighted off-balance sheet items (Continued)

Movements in the allowance for impairment and provisions in 2018	In RSD thousand
Opening balance – 31st December 2017	**16,076,970**
First time adoptions IFRS 9	3,949,823
Opening balance – 1st January 2018	**20,026,792**
Charge for the year	6,266,906
Reversal of impairment losses and release of provisions during the year	(2,253,073)
Increase in provisions due to exchange rate changes	102,814
Reversal of provisions due to exchange rate changes	(122,011)
Transfer to off-balance sheet items	(2,365,887)
Transfer from off-balance sheet items	-
Sale (transfer) of receivables	(3,293,937)
Reversal of provisions due to passage of time (unwinding)	(278,779)
Closing balance - 31 December 2018	**18,082,825**

9. OTHER OPERATING INCOME

In RSD thousand

	2019	2018
Property rental income	22,521	35,814
Reimbursed expenses	3,017	12,394
Income from dividends and equity interests	1,702	88,221
Income from fees from Credit biro	33,997	36,501
Income from IT services from foreign banks	25,055	25,459
Other income	33,003	35,679
Total	**119,295**	**234,068**

10. SALARIES, COMPENSATIONS AND OTHER PERSONAL EXPENSES

In RSD thousand

	2019	2018
Net salaries	3,813,325	3,661,969
Tax on employee benefits	468,547	448,299
Contributions on employee benefits	1,819,974	1,766,365
Expenses for temporary and occasional work	58,091	68,785
Other personal expenses	30,168	34,483
Provisions for retirement benefits and other employee benefits	23,142	19,354
Total	**6,213,247**	**5,999,255**

11. DEPRECIATION AND AMORTIZATION

In RSD thousand

	2019	2018
Depreciation and amortization:		
– Amortization of intangible assets (Note 18)	480,776	463,197
– Depreciation of fixed assets and investment property (Note 19)	1,096,363	594,554
Total	**1,577,139**	**1,057,751**

12. OTHER INCOME

In RSD thousand

	2019	2018
Release of unused provisions of liabilities	134,590	85,166
Gains from sales of fixed assets	20,488	20,323
Gains from use of write-offs assets and variable lease payments	383	-
Collected reported insurance damage	3,969	3,333
Surpluses	70,689	-
Other income	713,566	315,354
Total	**943,685**	**424,176**

13. OTHER EXPENSES

	2019	2018
Material, energy and spare parts	453,121	476,750
Professional services	1,396,072	1,320,187
Advertising, marketing and entertainment expenses	235,494	233,617
Mail and telecommunication expenses	364,322	328,624
Insurance premiums	2,725,359	2,518,336
Maintenance of property, plant and equipment	280,174	295,677
Rental cost	373,534	966,231
Fees and commissions	204,147	209,684
Taxes and contributions	95,543	129,650
IFRS 16 tax expenses	93,721	-
Physical-technical security	156,656	153,664
General and administrative expenses	277,007	286,653
Losses from write-offs, disposals and shortage of property, plant equipment and intangible assets	5,952	38,889
Losses from write-off property with right of use and variable lease payments	256	-
Expenses for provisions for liabilities	170,850	383,572
Impairment of lend plant equipment and intangible assets	76,575	82,096
Other expenses	375,855	377,003
Total	**7,284,638**	**7,800,633**

14. INCOME TAXES

(a) Components of income taxes

The components of income taxes are:

In RSD thousand

	2019	**2018**
Current income tax	1,587,375	1,073,267
Income from deferred tax assets and reduction of deferred tax liabilities	(144,482)	(744,547)
Expenses from reduction of deferred tax assets and creation of deferred tax liabilities	166,083	301,339
Total income tax expense	**1,608,976**	**630,059**

(b) Numerical reconciliation of income tax recognized in the income statement and profit for the year before tax multiplied by the prescribed income tax rate

In thousand RSD

	2019.	**2018.**
Profit before tax	**13,938,435**	**13,234,169**
Income tax at the rate of 15%	**2,090,765**	**1,985,125**
Tax effects of expense reconciliation – non-deductible expenses	2,981	3,300
Tax effects of revenue reconciliation – tax exempt income	(402,356)	(694,475)
Effects of temporary differences		
Tax effects of depreciation differences recognized for tax and statutory reporting	36,872	18,219
Payment to employees	318	550
Tax effects due to unpaid and paid taxes and similar tax duties	(3,008)	241
Tax effects in respect of real estate property impairments	11,486	(129,164)
Tax effects on the basis of created and used provisions for liabilities and charges	(4,405)	30,463
Tax effects of the first-time IFRS9 adoption	(142,966)	(142,966)
Other - capital gains/(losses)	(2,312)	1,974
Current income tax stated in the income statement	**1,587,375**	**1,073,267**
Effective tax rate	***11.39%***	***8.11%***

For the purpose of determining legal obligations arising from income tax for the period 1 January - 31 December 2019, the Bank has adjusted expenditure and income reported in the income statement in accordance with the legal provisions.

The most significant amount is tax exemption of interest income generated from debt securities issued by the Republic, local governments and the National Bank of Serbia, and they are excluded from the tax base in the total amounting to RSD 2,682,375 thousand, which resulted in a tax effect in the amount of RSD 402,356 thousand, for 2018 (31 December, 2018, tax base: RSD 4,543,832thousand; tax effect RSD 681,575 thousand).

Also, in accordance with the regulations, the Bank has decreased tax base for one fifth (second of five) of the IFRS 9 first time adoption tax effects (953,100 thousand RSD), registered at the date of the standard first application (1 January, 2018) by debiting Retained earnings from previous years in full amount of 4,765,550 thousand RSD, which resulted in tax effect of RSD 142,966 thousand.

For the remaining period (2020-2022), proportional tax base adjustments will be done in accordance with Corporate Income Tax law provisions, up to amount of total IFRS 9 FTA effects.

14. INCOME TAXES (Continued)

(c) Deferred Tax Assets

In accordance with IAS 12, ″Income Tax″, deferred tax assets and liabilities relate to taxable temporary differences between carrying amounts of tangible and intangible assets and their tax bases, temporary differences based on unpaid taxes that will be recognized in subsequent period, as well as for other temporary differences.

The most significant changes in deferred tax assets relate to the decrease of tax assets from using the first application of IFRS 9 effects, in the net amount of RSD 142,966 thousand, while the increase in tax assets relates to on the creation of a tax asset for the future tax credit calculated in the amount of 2% of the remaining debt (RSD 2,481,751 thousand) established in accordance with Article 14, paragraph 2 of the Law on Conversion of Housing Loans Indexed in Swiss francs, which represents a tax credit of RSD 49,635 thousand, and it will be proportionally used in the period 2020-2021.

Movements in deferred tax assets are shown in the next tables:

In RSD thousand

2019 In RSD thousand	**Balance as of 1 January**	**Recognized to income statement**	**Recognized to balance sheet**	**Balance as of 31 December**
Temporary differences of depreciation recognized for tax and statutory reporting	75,482	53,684	-	129,166
DTA in respect to payment to employees	619	318	-	937
Temporary differences based on unpaid and paid taxes and similar tax duties	15,313	(3,008)	-	12,305
DTA based on provisions for liabilities and charges	16,577	20,186	-	36,763
DTA based on real estate property impairment	24,451	550	-	25,091
DTA based on impairment of other assets	402	-	-	402
Tax effects of the first-time IFRS9 adoption	571,866	(142,966)	-	428,900
Tax credit in amount of 2% of remaining debt determined in accordance with Article 14, paragraph 2, Law on Conversion of housing loans indexed in CHF	-	49,635	-	49,635
Total	**704,800**	**(21,601)**	**-**	**683,199**

In RSD thousand

2018 In RSD thousand	**Balance as of 1 January**	**Recognized to income statement**	**Recognized to balance sheet**	**Balance as of 31 December**
Temporary differences of depreciation recognized for tax and statutory reporting	92,342	(16,860)	-	75,482
DTA in respect to payment to employees	69	550	-	619
Temporary differences based on unpaid and paid taxes and similar tax duties	15,072	241	-	15,313
DTA based on provisions for liabilities and charges	-	16,577	-	16,577
DTA based on real estate property impairments	153,706	(129,165)	-	24,541
DTA based on impairment of other assets	402	-	-	402
DTA based on the first-time IFRS9 adoption	-	571,866	-	571,866
Reclassification from the asset to the liability (real estate fair value (revaluation) model)	(108,194)	-	-	-
Total	**153,397**	**443,209**	**-**	**704,800**

14. INCOME TAXES (Continued)

(c) Deferred Tax Assets and Liabilities (Continued)

Movements in deferred tax liabilities were as follows:

2019 **In RSD thousand**	**Balance as of 1 January**	**Recognized to income statement**	**Recognized to balance sheet**	**Balance as of 31 December**
Deferred tax liabilities based on real estate fair value model	106,337	-	-	106,337
Sale of real estate property	-	-	(155)	(155)
Total	**106,337**	**-**	**(155)**	**106,182**

2018 **In RSD thousand**	**Balance as of 1 January**	**Recognized to income statement**	**Recognized to balance sheet**	**Balance as of 31 December**
Reclassification from the asset to the liability (real estate fair value model)	108,194	-	-	108,194
Sale of real estate property	-	-	(1,857)	(1,857)
Total	**108,194**	**-**	**(1,857)**	**106,337**

(d) Final current tax liability

Finally calculated current tax liabilities reported in the balance sheet at 31 December 2019 amount to RSD 478,134 thousand (31 December 2018: RSD 21.386 thousand), and has been created by decreasing the amount of current income tax liability by the amount of prepaid income taxes for 2019, paid during 2019.

15. CASH AND BALANCES WITH CENTRAL BANK

(a) Cash and balances with central bank

		In RSD thousand
	2019	**2018**
In RSD		
Gyro account	35,482,765	29,824,775
Cash on hand	12,160,459	9,122,225
Deposits of surplus liquid assets	12,000,000	-
Receivables for calculated interest, fee and commission based on cash and balances with central bank	-	13,649
Accruals on cash and cash equivalents with Central Bank	886	-
	59,644,110	**38,960,649**
In foreign currency		
Cash on hand	3,805,000	3,608,590
Other monetary assets	18,327	14,445
Obligatory reserves with the National Bank of Serbia	33,854,490	44,320,277
	37,677,817	**47,943,312**
Gold and precious metals	70,707	58,646
Balance as of 31 December	**97,392,634**	**86,962,607**

Obligatory dinar reserves with the National Bank of Serbia

The obligatory reserves in dinars is the minimal reserve in dinars allocated in accordance with the National Bank of Serbia's Decision on Banks' Required Reserves with the National Bank of Serbia ("Official Gazette of Republic of Serbia", no. 76/2018).

The Bank is required to calculate and allocate the obligatory reserves in RSD by applying 5% rate on the average daily balance of liabilities in RSD with contractual maturity up to 730 days, while 0% rate is applied on the average daily balance of liabilities in RSD with contractual maturity of over 730 days. These percentages are calculated on the average daily balance of liabilities in local currency during the preceding calendar month, and the bank allocates the calculated amount to its gyro account with the National Bank of Serbia. The Bank calculates the obligatory reserves in RSD on deposits in RSD, loans and securities, and other obligations in RSD, excluding dinar deposits received under transactions performed on behalf and for the account of third parties that are not in excess of the amount of the investment made from such deposits as defined by the Decision. The obligatory reserves in RSD is also calculated as part of the foreign currency obligatory reserves by applying 38%, as the dinar equivalent, to the calculated foreign currency obligatory reserves on liabilities in foreign currency, and on foreign currency clause- indexed dinar liabilities denominated in foreign currency with contractual maturity of up to 730 days, while 30% as the dinar equivalent, is applied on the calculated foreign currency obligatory reserves on liabilities in foreign currency and on foreign currency clause-indexed dinar liabilities denominated in foreign currency with contractual maturity of over 730 days.

During the accounting period, the Bank is required to maintain the average daily balance of the allocated obligatory reserves in dinars in the amount equal to the calculated obligatory reserves in dinars.

15. CASH AND BALANCES WITH CENTRAL BANK (Continued)

(a) Cash and balances with central bank (Continued)

Obligatory dinar reserves with the National Bank of Serbia (Continued)

As of 31 December 2019, calculated obligatory reserves in dinars amounted to RSD 33.480.110 thousand (31 December 2018: RSD 28,077,247 thousand) and were in accordance with the above-mentioned National Bank of Serbia's Decision.

At 31 December 2019 interest rate applied on the average amount of the allocated obligatory reserves in dinars, which does not exceed the amount of calculated obligatory reserves, was 0.75% per annum.

Foreign currency obligatory reserves with the National Bank of Serbia

In accordance with the Decision on Banks' Required Reserves with the National Bank of Serbia ((“Official Gazette of Republic of Serbia”, no. 76/2018), the Bank calculated foreign currency obligatory reserves on 31 December 2019, by applying 20% rate on the amount of the average daily balance of the liabilities in foreign currency, while 100% rate is applied on the average daily balance of foreign currency clause-indexed dinar liabilities denominated in foreign currency during the preceding calendar month with contractual maturity of up to 730 days (with the exceptions defined by the Decision), while 13% rate is applied for the liabilities in foreign currency, and 100% rate is applied on the foreign currency clause-indexed dinar liabilities denominated in foreign currency with contractual maturity of over 730 days. Therefore, 62% of the calculated foreign currency obligatory reserves is allocated based on the balance of the liabilities in foreign currency and based on the balance of foreign currency clause-indexed dinar liabilities denominated in foreign currency with contractual maturity up to 730 days, as well as 70% of the calculated foreign currency obligatory reserves based on the balance of the same kind of liabilities denominated in foreign currency with contractual maturity of over 730 days to the National Bank of Serbia's foreign currency accounts in euros.

During the accounting period, the Bank is required to maintain the average daily balance of the allocated foreign currency obligatory reserves in the amount equal to the calculated foreign currency obligatory reserves.

The National Bank of Serbia does not pay interest on the average balance amount of the allocated foreign currency obligatory reserves.

As of 31 December 2019, calculated foreign currency obligatory reserves amounted to EUR 351,991,257.05 (31 December 2018: EUR 303,795,645.37) and were in accordance with the above mentioned National Bank of Serbia's Decision.

15. CASH AND BALANCES WITH CENTRAL BANK (Continued)

(b) Overview of the differences between cash stated in the Statement of Cash Flows and Balance Sheet as of 31 December 2019:

In RSD thousand

	Balance sheet	Cash flows	Difference
In RSD			
Gyro account	35,482,765	35,482,765	-
Cash on hand	12,160,459	12,160,459	-
Excess liquidity deposited with the National Bank of Serbia	12,000,000	-	12,000,000
Accruals on cash and cash equivalents with Central Bank	886	-	886
	59,644,110	**47,643,224**	**12,000,886**
In foreign currency			
Cash on hand	3,805,000	3,805,000	-
Other monetary assets	18,327	18,327	-
Obligatory reserve with the NBS	33,854,490	-	33,854,490
Foreign currency accounts (balance-sheet item Loans and receivables from banks and other financial organizations/customers)	-	5,718,527	(5,718,527)
Cheques in foreign currency (balance-sheet item Loans and receivables from banks and other financial organizations/customers)	-	35,251	(35,251)
	37,677,817	**9,577,105**	**28,100,712**
Gold and other precious metals	70,707	70,707	-
Balance as of 31 December	**97,392,634**	**57,291,036**	**40,101,598**

(a) Cash flows do not include movements between items that make up cash or cash equivalents because these components are part of the entity's cash management, not part of their business, investment and financing activities. Cash management involves investing excess cash in cash equivalent.

15. CASH AND BALANCES WITH CENTRAL BANK (Continued)

(b) Overview of the differences between cash stated in the Statement of Cash Flows and Balance Sheet as of 31 December 2018 (Continued):

In RSD thousand

	Balance sheet	Cash flows	Difference
In RSD			
Gyro account	29,824,775	29,824,775	-
Cash on hand	9,122,226	9,122,226	-
Receivables for calculated interest, fee and commission based on cash and balances with central bank	13,649	-	13,649
	38,960,650	**38,947,001**	**13,649**
In foreign currency			
Cash on hand	3,608,590	3,608,590	-
Other monetary assets	14,445	14,445	-
Obligatory reserve with the NBS	44,320,276	-	44,320,276
Foreign currency accounts (balance-sheet item Loans and receivables from banks and other financial organizations/customers)	-	17,140,307	(17,140,307)
Cheques in foreign currency (balance-sheet item Loans and receivables from banks and other financial organizations/customers)	-	21,490	(21,490)
	47,943,311	**20,784,832**	**27,158,479**
Gold and other precious metals	58,646	58,646	-
Balance as of 31 December	**86,962,607**	**59,790,479**	**27,172,128**

c) Changes on financing activities, received loans

In RSD thousand

	2019	2018
Opening balance 1 January	26,646,176	27,835,553
Inflow from borrowings	3,599,688	6,878,998
Outflow from borrowings	(5,144,436)	(8,006,827)
Exchange Rate Effect	(139,521)	(61,548)
Closing balance - 31 December	**24,961,907**	**26,646,176**

16. FINANCIAL ASSETS CLASSIFICATION

a) Receivables from derivatives

In RSD thousand

	2019	2018
In RSD		
Financial derivatives	61,978	331,839
	61,978	**331,839**
Balance as of 31 December	**61,978**	**331,839**

16. FINANCIAL ASSETS CLASSIFICATION (Continued)

b) INVESTMENTS IN SUBSIDIARIES AND SECURITIES

In RSD thousand

	2019				2018			
	Securities carried at fair value through Profit and Loss	**Securities carried at fair value through OCI**	**Investments in subsidiaries**	**Total**	**Securities carried at fair value through Profit and Loss**	**Securities carried at fair value through OCI**	**Investments in subsidiaries**	**Total**
– Shares and equity investment	46,951	43,062	1,199,472	1,289,485	42,880	43,062	1,199,472	1,285,414
– Debt securities issued by the Republic of Serbia	844,686	102,706,935	-	103,551,621	372,221	89,449,904	-	89,822,125
- Accrued interest on debt securities issued by the Republic of Serbia	53,322	3,142,468	-	3,195,790	2,715	2,663,496	-	2,666,211
	944,959	**105,892,465**	**1,199,472**	**108,036,896**	**417,816**	**92,156,462**	**1,199,472**	**93,773,750**
Fer value adjustment	4,638	1,465,598	-	1,470,236	(6,665)	304,872	-	298,207
	4,638	**1,465,598**	**-**	**1,470,236**	**(6,665)**	**304,872**	**-**	**298,207**
Balance as of 31 December	**949,597**	**107,358,063**	**1,199,472**	**109,507,132**	**411,151**	**92,461,334**	**1,199,472**	**94,071,957**

16. FINANCIAL ASSETS CLASSIFICATION (Continued)

(c) SECURITIES AND INVESTMENTS PER SHARE

		In RSD thousand
	2019	**2018**
Investment in subsidiaries		
– Intesa Leasing d.o.o., Beograd share 100%	962,496	962,496
– Intesa Invest, Beograd share 100%	236,976	236,976
	1,199,472	**1,199,472**
Debt securities carried at fair value through profit and loss		
INTESA SANPAOLO	46,951	42,880
BONDS OF THE MINISTRY OF FINANCE OF THE REPUBLIC OF SERBIA	898,008	374,936
Fer value adjustment	4,638	(6,665)
	949,597	**411,151**
Debt securities carried at fair value through OCI		
BONDS OF THE MINISTRY OF FINANCE OF THE REPUBLIC OF SERBIA	105,849,403	92,113,399
Other	43,062	43,062
Fer value adjustment	1,465,598	304,872
	107,358,063	**92,461,333**
Balance as of 31 December	**109,507,132**	**94,071,956**

17. LOANS AND RECEIVABLES FROM BANKS, CUSTOMERS AND OTHER FINANCIAL ORGANIZATIONS

(a) LOANS AND RECEIVABLES FROM BANKS AND OTHER FINANCIAL ORGANIZATIONS

In RSD thousand

	2019	2018
In RSD		
Loans under reverse repo transactions	31,261,100	33,058
Receivables for calculated interest	-	5,061
Current account loans	70	98
Loans approved and due with one day (overnight)	-	500,000
Liquidity and current assets loans	5,710,065	3,974,756
Investment loans	293,632	6,301
Other loans	6,325	990,539
Other placements	1,763,900	591,220
Deferred income on receivables carried at amortized cost using the effective interest rate	(12,848)	(9,663)
Accrued interest calculated on the basis of loans, deposits and other placements	6,702	5,798
Total in RSD	**39,028,946**	**6,597,168**
In foreign currency		
Foreign currency accounts	5,720,666	17,143,725
Cheques	35,251	21,490
Other loans	2,633	2,709
Other non-purpose deposits	2,803,929	6,912,526
Special-purpose deposits	4,704	4,728
Other purpose deposits	43,509	-
Other placements	3,534,921	2,386,776
Accrued interest calculated on the basis of loans, deposits and other placements	15,408	14,215
Total in foreign currency	**12,161,021**	**26,486,169**
Gross loans and receivables	**51,189,967**	**3,083,337**
Less: Allowance for impairment		
– in RSD	(9,791)	(16,221)
– in foreign currency	(13,619)	(27,852)
	(23,410)	**(44,073)**
Balance as of 31 December	**51,166,557**	**33,039,264**

Other placements amounting to RSD 1,763,900 thousand as of 31 December 2019 (31 December 2018: RSD 591,220 thousand) and in foreign currency as of 31 December 2019 RSD 3,534, 921 (31 December 2018: RSD 2,386,776 thousand) refers to the purchase and sale of foreign currency.

17. LOANS AND RECEIVABLES FROM BANKS, CUSTOMERS AND OTHER FINANCIAL ORGANIZATIONS (Continued)

(b) LOANS AND RECEIVABLES FROM CUSTOMERS

In RSD thousand

	2019	2018
In RSD		
Receivables for calculated interest	1,231,438	2,142,985
Accrued fee and commission	115	-
Current account loans	5,763,414	5,835,607
Consumer loans	2,245,155	1,655,336
Liquidity and current assets loans	65,696,342	65,119,208
Investment loans	101,949,215	93,825,015
Mortgage loans	80,667,519	68,739,458
Cash loans	40,591,395	39,059,273
Other loans	59,675,730	54,588,042
Receivables based on factoring without the right of recourse and reverse factoring	3,189,871	2,137,817
Receivables based on factoring with the right of recourse	453,680	350,608
Placements based on acceptances, endorsements and payments made under guarantees	97,770	165,571
Placements on ceded receivables on other grounds	1,844,297	2,114,156
Deferred income on receivables carried at amortized cost using the effective interest rate	(1,110,914)	(1,134,067)
Accrued interest calculated on the basis of loans, deposits and other placements	837,211	599,328
Total in RSD	**363,132,238**	**335,198,337**
In foreign currency		
Interest receivable	127,531	108,965
Loans for payment of import of goods and services in foreign currency	19,196,319	16,704,146
Loans for the purchase of immovable property in the country approved to a natural person	16,293	17,506
Other loans	3,580,879	4,229,026
Receivables from factoring without recourse factoring and reverse	417,438	233,650
Accrued interest calculated on the basis of loans, deposits and other placements	56,220	47,571
Total in foreign currency	**23,394,680**	**21,340,864**
Gross loans and receivables	**386,526,918**	**356,539,201**
Less: Allowance for impairment		
– in RSD	(10,349,818)	(15,225,069)
– in foreign currency	(2,267,528)	(1,565,018)
	(12,617,346)	**(16,790,087)**
Balance as of 31 December	**373,909,572**	**339,749,114**

As of 31 December 2019 the Banks portfolio does not have loans and receivables measured at fair value

17. LOANS AND RECEIVABLES FROM BANKS, CUSTOMERS AND OTHER FINANCIAL ORGANIZATIONS (Continued)

(c) OVERVIEW BY TYPE OF CLIENT

	2019			2018		
	Short-term (up to one year)	**Long-term (more than one year)**	**Total**	**Short-term (up to one year)**	**Long-term (more than one year)**	**Total**
In RSD						
Loans and receivables						
– Central bank, banks and other financial sector and insurance	33,032,947	5,995,998	39,028,945	3,303,298	3,293,870	6,597,168
– Holding companies	-	122	122	-	-	-
– Corporate customers	35,457,824	135,202,448	170,660,272	40,502,420	116,790,110	157,292,530
– Retail customers	2,905,877	176,149,415	179,055,292	6,693,178	154,587,250	161,280,428
– Public sector	18,524	10,749,776	10,768,300	38,646	7,760,764	7,799,410
– Foreign entities	158	307,868	308,026	107	218,437	218,544
– Other customers- companies and other legal entities in bankruptcy	357,399	652,220	1,009,619	462,076	7,081,126	7,543,202
– Other customers-non profit institutions	6,321	410,484	416,805	9,405	534,016	543,421
– Other customers - non-budgeted legal entities and institutions	173,113	740,689	913,802	148,858	371,947	520,805
Total in RSD	**71,952,163**	**330,209,017**	**402,161,183**	**51,157,988**	**290,637,520**	**341,795,508**
In foreign currency						
– Central bank, banks and other financial sector and insurance	828,167	2,633	830,800	4,252,614	2,709	4,255,323
– Holding companies	-	664	664	-	317	317
– Corporate customers	1,597,304	15,695,627	17,292,931	102,100	14,711,179	14,813,279
– Retail customers	27,854	1,082,290	1,110,144	43,446	922,283	965,729
– Public sector	3,034	269,317	272,351	3,587	318,272	321,859
– Foreign banks and financial organizations	11,330,222	-	11,330,222	22,230,846	-	22,230,846
– Foreign entities	2,247,491	2,465,166	4,712,657	2,076,364	3,153,514	5,229,878
– Other customers	7	5,927	5,934	1,185	8,615	9,800
– Foreign entities	**16,034,079**	**19,521,624**	**35,555,703**	**28,710,142**	**19,116,889**	**47,827,031**
Total in foreign currency	**87,986,242**	**349,730,641**	**437,716,886**	**79,868,130**	**309,754,409**	**389,622,539**
Gross loans and receivables						
Less: Allowance for impairment - banks and other financial organizations	(20,422)	(2,989)	(23,411)	(42,170)	(1,903)	(44,073)
Less: Allowance for impairment- customers	(2,416,310)	(10,201,036)	(12,617,346)	(2,829,327)	(13,960,761)	(16,790,088)
	(2,436,732)	**(10,204,025)**	**(12,640,757)**	**(2,871,497)**	**(13,962,664)**	**(16,834,161)**
As at dan 31 December	**85,549,510**	**339,526,616**	**425,076,129**	**76,996,633**	**295,791,745**	**372,788,378**

17. LOANS AND RECEIVABLES FROM BANKS, CUSTOMERS AND OTHER FINANCIAL ORGANIZATIONS (Continued)

Short-term loans have been granted to companies for funding business activities within the following sectors: trade and services, manufacturing, construction, agriculture and food industry, as for the other purposes, with interest rates ranging from 2.78% and 10.5% per annum on RSD loans, and from 0.79% and 9.42% per annum on loans with the foreign currency clause and foreign currency loans.

Interest rates on the long-term loans to legal entities in RSD range from 2.9% and 6%, and on RSD long-term loans with the foreign currency clause, as well as on foreign currency loans, from 0.75% and 6.25% per annum.

Short-term loans to retail customers, have been approved with interest rates ranging from 4.99% to 15.00% per annum for loans with no currency clause.

Short-term loans to small business customers, have been approved with interest rates ranging from 4.50% to 14% per annum for loans with no currency clause, and from 2.7% do 10% per annum for loans with the foreign currency clause.

Interest rates on overdrafts on retail current accounts range from 29.85% per annum and for small corporate customers from 16.80% to 24% per annum.

Short-term loans to registered agriculture farmers have been approved with interest rates ranging from 4.99% to 9.9% per annum for loans with no currency clause, and from 5.5% do 6.5% per annum for loans with the foreign currency clause.

Long-term loans to retail customers have been granted as non-purpose loans, consumer goods purchase loans, renovation, adaptation and the purchase of the residential and business space for the period from 13 months to 30 years with interest rates ranging from 1.38% to 7.25% per annum for loans with the foreign currency clause, as well as from 4.24% to 15% for the loans with no currency clause.

Long-term loans to small businesses have been granted as non-purpose loans, consumer goods purchase loans, , for the period from 13 to 24 months with interest rate ranging from 4.30% to 14% per annum on loans without the foreign currency clause and from 2.5% to 10% per annum on loans with the foreign currency clause,while long-term loans for adaptation and the purchase of the residential and business space for the period from 13 months to 10 years with interest rates ranging from 2.70%+3m EURIBOR to 7.70%%+3M EURIBOR per annum for loans with the foreign currency clause.

Long-term loans to registered agriculture farmers have been granted as purpose loans (loans for fixed assets) i non-purpose loans (for the period from 12 months to maximum 24 months), and for working capital. Loans with a term of repayment over 24 months have been approved with interest rates ranging from 2.70% to 6.5%+6m EURIBOR, for loans with the foreign currency clause, i.e. from 4.49% to 9.9% for loans from 13 months to 24 months for loans with no currency clause.

18. INTANGIBLE ASSETS

In RSD thousand

	Licenses	**Software**	**Intangible assets under construction**	**Total**
COST				
Balance as of 1 January 2018	**483,323**	**3,009,828**	**1,739,818**	**5,232,969**
Additions during the year	-	-	1,659,851	1,659,851
Transfers	-	411,286	(411,286)	-
Disposals and write offs	-	(111,919)	-	(111,919)
Balance as of 31 December 2018	**483,323**	**3,309,195**	**2,988,383**	**6,780,901**
Additions during the year	**-**	-	2,054,875	2,054,875
Transfers	-	4,842,706	(4,842,706)	-
Balance as of 31 December 2019	**483,323**	**8,151,901**	**200,552**	**8,835,776**
ACCUMULATED AMORTIZATION				
Balance as of 1 January 2018	**483,305**	**2,139,091**	**-**	**2,622,396**
Amortization charge (Note 11)	**18**	**463,179**	**-**	**463,197**
Disposals and write offs	**-**	**(79,558)**		**(79,558)**
Balance as of 31 December 2018	**483,323**	**2,522,712**	**-**	**3,006,035**
Amortization charge (Note 11)	-	480,776	-	480,776
Balance as of 31 December 2019	**483,323**	**3,003,488**	**-**	**3,486,811**
Carrying value as of:				
– 31 December 2019	**-**	**5,148,413**	**200,552**	**5,348,965**
– 31 December 2018	**-**	**786,483**	**2,988,383**	**3,774,866**

The Bank has activated new Core information system/software, by its transferring from Intangible assets under construction to the Software in amount of RSD 3,554,795 thousand that represents the software value up to December 31, 2019, as well as its satellite software applications amounted to RSD 802,947 thousand.

19. PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY AND NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

(a) Property, plant and equipment and investment property

In RSD thousand

	Land and buildings	Equipment and equipment under finance lease	Leasehold improvements	Construction in progress	Total property, plant and equipment	Investment property
COST/REVALUATION						
Balance as of 1 January 2018	**6,758,393**	**3,989,075**	**758,271**	**18,373**	**11,524,112**	**51,251**
Additions during the year				693,388	693,388	
Transfers from construction in progress	52,660	420,080	97,296	(570,036)	-	-
Disposals and write offs	(12,558)	(264,605)	(39,475)	-	(316,638)	(11,018)
Effects of fair value appraisal as of 31 December 2018					-	(9,238)
Balance as of 31 December 2018	**6,798,495**	**4,144,550**	**816,092**	**141,725**	**11,900,862**	**30,995**
Right of use assets (effects of IFRS16 first-time adoption)	**2,108,929**	**76,949**	**-**	**-**	**2,185,878**	**-**
Balance as of 1 January 2019	**8,907,424**	**4,221,499**	**816,092**	**141,725**	**14,086,740**	**30,995**
Additions during the year	-	-	-	973,085	973,085	-
Transfers from construction in progress	407,356	559,249	125,381	(1,091,986)	-	
Transfer to Assets held for sale	-	-	-	-	-	(30,305)
Disposals and write-offs	(58,105)	(344,214)	-	-	(402,319)	
Other	(1,245)	-	-	-	(1,245)	86
Balance as of 31 December 2019	**9,255,430**	**4,436,534**	**941,473**	**22,824**	**14,656,261**	**776**

In RSD thousand

	Land and buildings	Equipment and equipment under finance lease	Leasehold improvements	Construction in progress	Total property, plant and equipment	Investment property
ACCUMULATED DEPRECIATION						
Balance as of 1 January 2018	**-**	**3,049,306**	**603,663**		**3,652,969**	**-**
Depreciation charge (Note 11)	237,517	286,923	70,114		594,554	
Disposals and write offs	(209)	(258,076)	(39,475)		(297,760)	
Balance as of 31 December 2018	**237,308**	**3,078,153**	**634,302**	**-**	**3,949,763**	**-**
Depreciation charge (Note 11)	664,220	355,003	77,140		1,096,363	-
Disposals and write/offs	(4,630)	(338,262)			(342,892)	-
Balance as of 31 December 2019	**896,898**	**3,094,894**	**711,442**	**-**	**4,703,234**	**-**
Carrying value as of:						
– 31 December 2019	**8,358,532**	**1,341,640**	**230,031**	**22,824**	**9,953,027**	**776**
– 31 December 2018	**6,561,187**	**1,066,397**	**181,790**	**141,725**	**7,951,099**	**30,995**

19. PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY AND NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS (Continued)

(a) Property, plant and equipment and investment property (Continued)

As of 31 December 2019 , the Bank has title deeds for property it owns and has no buildings pledged as collateral.

In accordance with the accounting policies changes from 2017 (passage from the cost model to the redetermination of value for measurement subsequent to initial disclosure of functional property; passage from accounting at cost to accounting at fair value for investment property), Parent bank has engaged the authorized appraisal company to assess fair value of the properties, at the level of the Intesa Sanpaolo Group, including Banca Intesa a.d. Beograd. On 31 December 2019, the authorized appraiser carried out the assessment of the properties fair value that Banca Intesa ad Beograd uses for its own business, and has concluded that market prices of real estates did not significantly oscillated (more than+/-10%) compared to the actual prices as of December 31, 2017, so that new assessment are not recorded as of December 31, 2019.

On the other hand, in accordance with IAS 40, for investment properties, there have been reassessment of its fair value as of December 31, 2019 performed, and positive and negative effects on this basis were recorded within profit and loss accounts.

If the Bank continued to apply cost model for real estate valuation, net present value would amount to RSD 5,837,744 thousand, at December 31, 2019 (31 December 2018: RSD 5,905,675 thousand).

(b) Right of use assets

Bank leases certain number of real estates for its branches, offices and other business premises. Lease contracts are typically concluded to the period of 5 years, with possibility of its renewal by the will of both contracting parties, as well as with the possibility to be terminated by the Lessee, with a contracted notice period of 30 or 60 days for most contracts. Bank has also leased certain number of cars, with contract period of 5 years, as well as one lease of an equipment (server) contract with useful life period of two years.

Information about right of use assets, amounts recognized in the income statement and cash flow are shown as follows:

In RSD thousand

COST	Automotive	Real estate	Equipment	Total
Balance as of 1 January 2019	**76,949**	**2,108,929**	**-**	**2,185,878**
Additions during the year	113,045	171,450	5,814	290,309
Disposals during the year	-	(16,640)	-	(16,640)
Balance as of 31 December 2019	**189,994**	**2,263,739**	**5,814**	**2,459,547**
ACCUMULATED DEPRECIATION				
Balance as of 1 January 2019	**-**	**-**	**-**	**-**
Depreciation charge (Note 11)	35,369	424,761	242	460,372
Contracts ending and disposals	-	(2,604)	-	(2,604)
Balance as of 31 December 2019	**35,369**	**422,157**	**242**	**457,768**
Carrying value as of:				
– 31 December 2019	**154,625**	**1,841,582**	**5,572**	**2,001,779**
– 1 January 2019	**76,949**	**2,108,929**	**-**	**2,185,878**

19. PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY AND NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS (Continued)

(b) Right of use assets (Continued)

Amount recognized in profit and loss
2019 – Leases under the IFRS 16

	In RSD thousand 2019.
Interest on lease liabilities (Napomena 3b)	35,616
Expenses relating short-term leases (exempt from the IFRS16, Note 13)	77,592
Expenses relating to leases of low-value asstes, excluding short-term leases of low-value assets (exempt from the IFRS16, Note 13)	295,942
Tax expenses – IFRS 16 (Note 13)	93,721
Net effects (gain) relating to variable payments and and right of use assets disposals (Note 12 and 13)	(127)

2018 – Operating leases under the IAS 17

In RSD thousand	**2018.**
Lease expense (Note 15)	966,231

Amounts recognized in statement of cash flows
In RSD thousand

	2019.
Total cash outflow for leases (IFRS 16)	461,383

(c) Non-current assets held for sale and discontinued operations

As it is disclosed in Note 2.17 (c), in accordance with the Bank's accounting policies, assets classified as non-current assets held for sale are measured at the lower of the:

- carrying value; or
- market (fair) value less costs to sell.

		In RSD thousanc
	2019	**2018**
Non-current assets held for sale	38,301	143,015
Balance as of 31 December 2019	**38,301**	**143,015**

Non-current assets are not depreciated as long as they are classified as assets held for sale.

20. OTHER ASSETS

		In RSD thousand
	2019	**2018**
Trade receivables	306	377
Other receivables	-	86,000
Receivables from employees	6,944	4,916
Receivables for overpaid taxes, except income tax	2,523	475
Advances paid	44,053	45,068
Other receivables from operating activities	3,130,972	2,452,713
Assets received through collection of receivables	245,366	332,395
Other assets	841,739	829,813
Interest receivable related to other assets:		
– in RSD	-	5
Fee and commission receivables related to other assets:		
– in RSD	298,928	163,305
– in foreign currency	10,608	16,814
Accrued interest expenses:		
– in RSD	331	579
Accrued other expenses:	-	
– in RSD		341,661
– in foreign currency	308,088	198
Other accruals:	-	
– in RSD	171,234	134,042
– in foreign currency	1	1
Total other assets	**5,061,093**	**4,408,362**
Less: Allowance for impairment	(492,342)	(92,739)
Balance as of 31 December	**4,568,751**	**4,315,623**

Other receivables from operating activities amounting to RSD 3,130,972 thousand as of 31 December 2019 (31 December 2018: RSD 2,452,713 thousand) mostly relate to receivables in RSD with respect to payment cards from other cards issuers - Master Card, VISA, DINA and AMEX in the amount of RSD 1,794,770 thousand, receivables from the Pension Fund RSD 424,376 thousand and receivable on claims refund in the amount of RSD 120,408 thousand (31 December 2018 mostly relate to receivables in RSD with respect to payment cards from other cards issuers - Master Card, VISA, DINA and AMEX in the amount of RSD 1,620,621 thousand).

21. LIABILITIES BASED ON DERIVATIVES

In RSD thousand

	2019	2018
Liabilities based on derivatives - swap	7,869	20,908
Liabilities based on derivatives - forward	-	589
Balance as of 31 December	**7,869**	**21,497**

22. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK

(a) DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK

In RSD thousand

	2019	2018
In RSD		
Transaction deposits	1,647,850	1,327,326
Deposits underlying granted loans	26,693	13,454
Special-purpose deposits	238,397	473,152
Other deposits (a)	5,447,566	1,408,365
Interest payable	17,146	2,758
Fee and commission payable	19	32
Total in RSD	**7,377,671**	**3,225,087**
In foreign currency		
Transaction deposits	611,468	657,885
Deposits underlying granted loans	1,646	948,393
Special-purpose deposits	4,117	399
Other deposits (b)	31,926,446	17,732,182
Borrowings	23,954,555	24,777,007
Other financial liabilities (c)	2,617,815	1,774,784
Interest payable	30,513	35,421
Accrued expenses for liabilities at amortized value, by applying the effective interest rate method	(176,316)	(119,907)
Total in foreign currency	**58,970,244**	**45,806,164**
Balance as of 31 December	**66,347,915**	**49,031,251**

(a) Other deposits amounting to RSD 5,447,566 thousand as of 31 December 2019 mostly related to one client belonging to sector of investment fund Management Company a dispose of deposit amounting to RSD 3,000,000 thousand.

(b) Other deposits in foreign currency amounting to RSD 31,926,446 thousand as of 31 December 2019 mostly related to one client belonging to foreign banks a dispose of deposit amounting to RSD 30,574,128 thousand.

(c) Other financial liabilities amounting to RSD 2,617,815 thousand as of 31 December 2019 (31 December 2019 RSD 1,774,784 thousand) mostly related to liabilities for outstanding payments received from foreign country in foreign currency amounting to RSD 2,617,000 thousand (31 December 2018 RSD 1,770,676 thousand).

22. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK (Continued)

(b) DEPOSITS AND OTHER LIABILITIES DUE TO CUSTOMERS

In RSD thousand

	2019	2018
In RSD		
Transaction deposits	124,496,102	107,136,250
Savings deposits	7,652,383	4,558,554
Deposits underlying granted loans	1,250,239	655,460
Special-purpose deposits	4,447,271	2,872,204
Other deposits	38,425,337	15,928,537
Deposits and loans due within one day (overnight)	1,660,783	1,080,055
Interest payable	759,947	402,340
Total in RSD	**178,692,062**	**132,349,190**
In foreign currency		
Transaction deposits	229,418,355	197,862,445
Savings deposits	49,895,134	57,218,806
Deposits underlying granted loans	5,019,799	5,270,750
Special-purpose deposits	2,234,824	3,003,673
Other deposits	5,699,167	6,923,988
Borrowings	1,019,623	1,869,169
Interest payable	345,931	392,986
Total in foreign currency	**293,632,833**	**272,541,817**
Balance as of 31 December	**472,324,895**	**405,175,217**

22. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK (Continued)

(c) DEPOSITS AND OTHER LIABILITIES TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK BY CONTRACTUAL MATURITY

In RSD thousand

	2019			2018		
	Short-term (up to one year)	**Long-term (more than one year)**	**Total**	**Short-term (up to one year)**	**Long-term (more than one year)**	**Total**
In RSD						
Transaction deposits	126,143,952	-	126,143,952	108,463,575	-	108,463,575
Saving deposits	5,346,864	2,305,519	7,652,383	3,809,966	748,588	4,558,554
Deposits related to granted loans	721,311	555,620	1,276,931	294,911	374,003	668,914
Special-purpose deposits	4,037,763	647,905	4,685,668	3,034,556	310,801	3,345,357
Other deposits	43,251,643	621,260	43,872,903	15,006,175	2,330,726	17,336,901
Overnight deposits and loans	1,660,783	-	1,660,783	1,080,055	-	1,080,055
Interest payable	777,093	-	777,093	405,097	-	405,097
Fee and commission payable	19	-	19	32	-	32
Total in RSD	**181,939,428**	**4,130,305**	**186,069,733**	**132,094,367**	**3,764,118**	**135,858,485**
In foreign currency						
Transaction deposits	230,029,822	-	230,029,822	198,520,330	-	198,520,330
Saving deposits	38,225,138	11,669,996	49,895,134	43,870,409	13,348,397	57,218,806
Deposits related to granted loans	3,523,285	1,498,160	5,021,445	4,770,470	1,448,673	6,219,143
Special-purpose deposits	1,735,171	503,770	2,238,941	864,486	690,631	1,555,117
Other deposits	36,443,532	1,182,081	37,625,613	24,270,743	385,427	24,656,170
Borrowings	12,270	24,961,907	24,974,178	-	26,646,176	26,646,176
Other financial liabilities	2,617,815	-	2,617,815	3,223,740	-	3,223,740
Interest payable	376,444	-	376,444	428,407	-	428,407
Accrued expenses for liabilities at amortized value, by applying the effective interest rate method		(176,316)	(176,316)	-	(119,907)	(119,907)
Total in foreign currency	**312,963,480**	**39,639,597**	**352,603,077**	**275,948,585**	**42,399,397**	**318,347,982**
Balance as of 31 December	**494,902,908**	**43,769,902**	**538,672,810**	**408,042,953**	**46,163,515**	**454,206,468**

22. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK (Continued)

(d) DEPOSITS AND OTHER LIABILITIES TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK BY TYPE OF CUSTOMERS

In RSD thousand

	2019			2018		
	Short-term (up to one year)	Long-term (more than one year)	Total	Short-term (up to one year)	Long-term (more than one year)	Total
In RSD						
– Central bank, banks and other financial sector and insurance	5,969,110	530,000	6,499,110	2,527,192	300,000	2,827,192
– Holding companies	2,946	-	2,946	2,906	-	2,906
– Corporate customers	89,717,407	1,266,708	90,984,115	70,236,244	2,656,952	72,893,196
– Retail customers	59,439,307	2,302,974	61,742,281	45,604,080	756,140	46,360,220
– Public sector	19,811,702	15,433	19,827,134	4,580,293	46,867	4,627,160
– Foreign banks and financial organizations	878,560	-	878,560	397,892	-	397,892
– Foreign entities	517,653	14,290	531,943	532,371	3,260	535,631
– Other customers – nonprofit institutions	3,743,107	-	3,743,107	3,148,322	-	3,148,322
– Other customers – public sector in bankruptcy	28,184	-	28,184	3,670,876	-	3,670,876
– Other customers- companies and other legal entities in bankruptcy	632,903	-	632,903	655,167	-	655,167
– Other customers –other financial organization in bankruptcy	1,474	-	1,474	241	-	241
Other customers - non-budgeted legal entities and institutions	1,197,075	900	1,197,975	738,781	900	739,681
Total in RSD	**181,939,428**	**4,130,304**	**186,069,732**	**132,094,365**	**3,764,119**	**135,858,484**
In foreign currency						
– Central bank, banks and other financial sector and insurance	1,966,663	2,822	1,969,486	1,610,062	2,837	1,612,899
– Holding companies	235	-	235	353	-	353
– Corporate customers	44,984,252	2,363,243	47,347,495	43,962,039	1,740,768	45,702,807
– Retail customers	223,429,186	12,186,000	235,615,186	203,292,549	13,839,691	217,132,240
– Public sector	422,861	1,021,998	1,444,859	999,171	1,871,551	2,870,722
– Foreign banks and financial organizations	33,124,791	23,765,968	57,000,759	19,536,167	24,657,101	44,193,268
– Foreign entities	3,881,575	233,714	4,115,289	4,035,097	236,272	4,271,369
– Other customers - nonprofit institutions	2,092,987	65,852	2,158,839	1,828,218	51,178	1,879,396
– Other customers – public sector in bankruptcy	94	-	94	4,960	-	4,960
– Other customers- companies and other legal entities in bankruptcy	2,808,848	-	2,808,848	565,364	-	565,356
Other customers - non-budgeted legal entities and institutions	-	141,988	141,988	114,606	-	114,606
Total in foreign currency	**312,963,481**	**39,639,597**	**352,603,078**	**275,948,586**	**42,399,398**	**318,347,984**
Balance as of 31 December	**494,902,909**	**43,769,901**	**538,672,810**	**408,042,951**	**46,163,517**	**454,206,468**

22. DEPOSITS AND OTHER LIABILITIES DUE TO BANKS, CUSTOMERS, OTHER FINANCIAL ORGANIZATIONS AND CENTRAL BANK (Continued)

On the corporate transaction deposits, the Bank pays interest at rates up to 60% of the annual reference interest rate depending on the currency and the amount of deposit.

On term deposits in RSD and foreign currency, the Bank pays interest at rates ranging up to 3.2% per annum, depending on the maturity period and the currency.

On special-purpose deposits of customers and natural persons the Bank does not pay interest.

On short-term retail deposits in RSD the interest is paid at rates ranging from 0% to 3.60% per annum, depending on the maturity period. Interest rates on short-term retail deposits in foreign currency range from 0.0% to 0.30% per annum, depending on the maturity period and the currency.

Long-term retail deposits in foreign currency are deposited at interest rates ranging from 0.01% to 0.70% per annum, depending on the maturity period and the currency. Long-term retail deposits in RSD are deposited at interest rates ranging from 4.00% to 5.50% per annum, depending on the maturity period.

23. PROVISIONS

In RSD thousand

	2019	2018
Provisions for off-balance sheet items (a)	321,027*	1,223,001
Provisions for employee benefits:		
– restructuring (b)	43,079	112,388
– long-term retirement benefits and unused days of vacation (c)	213,687	190,545
Provisions for litigations (Note 29 (a))	265,215	275,262
Provisions for liabilities coverage	18,156	-
Balance as of 31 December	**861,164**	**1,801,197**

*Of the total decrease of RSD 902 million compared to the same period in 2018, the amount of RSD 770 million relates to two clients and is the result of the expiry and closing of guarantees.

23. PROVISIONS (Continued)

		In RSD thousand
	2019	**2018**
Movements in provisions for off-balance sheet items		
Opening balance	1,223,001	902,184
First time adoption effect IFRS 9	-	(32,682)
Release of provisions	(1,108,918)	(337,594)
Release of provisions - exchange rate	(6,189)	(7,093)
Increase of provisions	210,687	683,726
Increase of provisions – exchange rate	2,447	14,459
Balance as of 31 December	**321,027**	**1,223,001**
Movements in provisions for restructuring		
Opening balance	112,388	23,525
Release of provisions directly from provisions	(69,309)	(22,850)
Increase of provisions	-	111,713
Balance as of 31 December	**43,079**	**112,388**
Movements in provisions for employee retirement benefits and unused days of vacation		
Opening balance	190,545	171,191
Increase of provisions	23,142	19,354
Balance as of 31 December	**213,168**	**190,545**
Movements in provisions for litigations		
Opening balance	275,262	180,394
Release of provisions through profit and loss	(134,590)	(85,166)
Release of provisions through profit and loss - CHF loan conversion	(3,021)	-
Release of provisions directly from provisions	(25,131)	(91,825)
Increase of provisions	152,695	271,859
Balance as of 31 December (Notes 29)	**265,215**	**275,262**
Movements in provisions liabilities		
Opening balance	-	-
Provisions	18,154	-
Balance as of 31 December	**18,154**	-

(a) According to the Bank's internal policy, provisioning for off-balance sheet items exposed to risk is performed in the same manner as for balance sheet assets, i.e. off-balance sheet items are classified into recoverability categories based on the estimation of the recoverable amount of receivables when it comes to outflow of resources and probability of outflow of resources.

(b) The project of considering and analyzing efficiency of business processes, which may lead to restructuring and decrease in number of employees (redundancies), which started, but is still not fully completed, therefore, the Bank made provisions in the same manner as in previous years, based on estimated number of employees that potentially could be redundant. For the purpose of estimate, available laws and regulations, as well as internal acts have been observed (Labor Law and Collective agreement).

(c) Long-term provision for retirement benefits has been recognized on the basis of an independent actuary's calculation at the balance sheet date in the amount of present value of estimated future cash outflows. The present value of estimated future cash outflows is calculated using the discount rate of 4% per annum, which reflects the long-term rate of return on high quality debt securities, Republic of Serbia bonds and treasury bonds of the Ministry of Finance Republic of Serbia.

23. PROVISIONS (Continued)

The provision was determined in accordance with the Bank's Collective Agreement, using the assumption of average salary increase rate of 4.3% per annum over the period for which the provision has been formed.

The provision for unused days of vacation is calculated on the basis of an independent actuary's report at the balance sheet date. In accordance with article 114 of the Labor Law in Republic of Serbia, during vacation an employee is entitled to compensation in the amount of average salary for the last twelve months. When calculating the provision for unused vacation days, the following factors are significant:

- average gross salary in the Bank, and
- number of unused days of vacation.

24. OTHER LIABILITIES

In RSD thousand

	2019	2018
Net salaries and compensations	130,365	252,215
Taxes, VAT, contributions and other duties payable, excluding income tax payable	525,469	358,174
Vendor liabilities	952,763	777,475
Advances received	132,106	296,225
Other liabilities (a)	2,990,347	3,128,525
	4,731,050	**4,812,614**
Accruals and deferred income		
Accrued liabilities for other expenses:		
– in RSD	572	836
– in foreign currency	-	12,970
Deferred interest income:		
– in RSD	3,091	129,153
Other deferred income:		
– in RSD	64,277	112,557
– in foreign currency	-	7,039
Other deferrals (b)		
– in RSD	3,672,180	1,579,838
– in foreign currency	1,894,460	1,552,769
	5,634,580	**3,395,162**
Long-term lease liabilities (c)	1,985,703	4,611
Total	**12,351,333**	**8,212,387**
Other tax liabilities	86,333	104,721
Balance as of 31 December	**12,437,666**	**8,317,108**

(a) Other liabilities in 2019 and 2018 mostly consist of non-invoiced services to suppliers and arrears payment for credit card obligations.

(b) Other accruals in foreign currency in 2019 and 2018 mostly consist of accruals accounts balances – buy or sales of foreign currency.

24. OTHER LIABILITIES (Continued)

(c) Financial liabilities for leased equipment as of 31 December 2019 and 2018 are as follows:

In RSD thousand

	2019		2018	
Minimal lease payments	**Present value**	**Contractual undiscounted cash flows**	**Present value**	**Contractual undiscounted cash flows**
Up to 1 year	4,865	5,183	3,646	4,003
From 1 to 5 years	1,989	2,002	965	1,186
Balance as of 31 December	**6,854**	**7,185**	**4,611**	**5,189**

In RSD thousand

	2019.	
Minimal lease payments	**Present value**	**Contractual undiscounted cash flows**
Up to 1 year	453,576	485,557
From 1 to 5 years	1,174,994	1,242,152
Over 5 years	350,279	362,763
Balance as of 31 December	**1,978,849**	**2,090,472**

In RSD thousand

	2018.
Minimal lease payments	**Contractual undiscounted cash flows**
Up to 1 year	629,912
From 1 to 5 years	1,590,362
Over 5 years	749,111
	2,969,385

25. EQUITY

(a) Equity structure

The Bank's equity as of 31 December 2019 consists of shares capital, share premium, reserves, revaluation reserves and current and previous year profit.

Structure of the Bank’s equity is presented in table below:

In RSD thousand

	2019	2018
Share capital – ordinary shares	21,315,900	21,315,900
Share premium	20,432,569	20,432,569
Reserves from profit	43,488,903	47,484,121
Fair value reserves of securities	1,896,248	685,313
Revaluation reserves arising from changes in fair value of buildings	601,696	602,578
Retained earnings	2,292	3,476,594
Current year profit	12,329,459	12,604,111
Balance as of 31 December	**100,067,067**	**106,601,186**

/i/ Share capital

As of 31 December 2019, the Bank’s registered share capital consists of 213,159 ordinary shares with nominal value of RSD 100 thousand per share.

The Bank’s shareholder as of 31 December 2019 and 2018 is presented in the table below:

Shareholder	Number of shares	Nominal share value (RSD thousand)	Share in %
ntesa Sanpaolo Holding International S.A., Luxembourg	213,159	21,315,900	100.00
Total	**213,159**	**21,315,900**	**100.00**

The amount of paid dividend during the period as well as related dividend per share are presented as follows:

	2019	2018
Paid dividend during the period (in thousand dinars)	20,075,923	20,034,339
Number of shares	213,159	213,159
Dividend per share (in thousand dinars)	**94.18**	**93.99**

/ii/ Share premium

Share premium amounting to of RSD 20,432,569 thousand as of 31 December 2019 (31 December 2018: RSD 20,432,569 thousand) is the result of the Bank’s status change, i.e. the merger of Panonska banka a.d. Novi Sad in the amount of RSD 2,989,941 thousand in 2007, as well as the result of the 4th, 5th and 6th issues of ordinary shares without public offer for the purpose of share capital increase.

25. EQUITY (Continued)

(a) Equity structure (Continued)

/iii/ Reserves

In RSD thousand

	2019	2018
Reserves from profit for estimated losses	43,488,903	47,484,121
Gains/losses from the change in the value of equity instruments	(3,045)	(1,478)
Gains/losses from the change in the value of debt instruments	1,899,293	686,791
Revaluation reserves arising from changes in fair value of buildings	601,696	602,578
Total	**45,986,847**	**48,772,012**

(b) Performance indicators – compliance with legal requirements

The Bank is required to reconcile the scope and the structure of its operations and risk placements with performance indicators prescribed by the Law on Banks and relevant decisions of the National Bank of Serbia passed on the basis of the aforementioned Law.

As of 31 December 2019, the Bank was in compliance with all prescribed performance indicators.

Performance indicators	**Prescribed**	**Realized**	
		31 December 2019	**31 December 2018**
Regulatory capital	Minimum EUR 10 million	EUR 695 miliona	EUR 608 miliona
Minimum ratio of the adequacy of the basic share capital specified by the bank	Minimum 4,5%	21.23%	19.76%
Minimum ratio of the adequacy of the basic capital specified by the bank	Minimum 6%	21.23%	19.76%
Minimum ratio of the adequacy of the capital specified by the bank	Minimum 8%	21.23%	19.76%
Permanent investments indicator	Maximum 60%	12.20%	11.12%
Indicator of large and the largest permissible loans	Maximum 400%	52.53%	62.14%
Liquidity ratio	Minimum 0.8	2.25	2.28
Acid-test ratio (quick ratio)	Minimum 0.5	1.64	1.83
Liquidity coverage ratio – LCR	Minimum 1.0	2.39	4.50
Foreign currency risk indicator	Maximum 20%	0.36%	2.95%
Exposure to a single entity or to a group of related parties	Maximum 25%	16.58%	22.29%
Bank's investment in non-financial legal entity	Maximum 10%	0,02%	0.02%
Risk concentration ratio		8.20%	n/a

26. OFF-BALANCE SHEET ITEMS

(a) Classification of off-balance sheet items by the classification category

In RSD thousand

	Off-balance sheet items to be exposed to credit risk 2019.	Provisions for Off-balance sheet items to be exposed to credit risk
Guarantees and other irrevocable commitments	85,601,716	(271,034)
Other off-balance sheet items	59,253,138	(49,994)
Balance as of 31 December	**144,854,854**	**(321,028)**

In RSD thousand

	Off-balance sheet items to be exposed to credit risk 2018.	Provisions for Off-balance sheet items to be exposed to credit risk
Guarantees and other irrevocable commitments	79,495,493	(1,152,707)
Other off-balance sheet items	60,978,308	(70,294)
Balance as of 31 December	**140,473,801**	**(1,223,001)**

(b) Guarantees and other irrevocable commitments

In RSD thousand

	2019	2018
Financial guarantees:		
– in RSD	7,070,416	7,782,591
– in foreign currency	9,430,974	11,162,132
	16,501,390	**18,944,723**
Commercial guarantees:		
– in RSD	24,819,488	23,230,871
– in foreign currency	4,550,403	5,106,913
	29,369,891	**28,337,784**
Uncovered letters of credit in foreign currency	799,351	823,060
Sureties and Acceptances	-	134
Sureties*	177,664	178,577
Irrevocable commitments for undisbursed loans	37,999,632	31,211,215
Other irrevocable commitments	753,788	-
	39,730,435	**32,212,986**
Balance as of 31 December	**85,601,716**	**79,495,493**

(c) Other off-balance sheet items

In RSD thousand

	2019	2018
Revocable commitments for undisbursed loans	59,253,138	60,978,308
Balance as of 31 December	**59,253,138**	**60,978,308**

27. RELATED PARTY DISCLOSURES

A number of banking transactions are entered into with the shareholder and other related parties in the ordinary course of business. The Bank realizes business transactions with its shareholder and other related party. The Bank enters into business relationship with Parent company and other members of Intesa Sanpaolo Group. Outstanding balances of receivables and liabilities as of 31 December 2019 and 2018, as well as income and expenses for the years then ended, resulting from transactions with the shareholder and other Bank's related parties within Intesa Sanpaolo Group, stated in RSD thousand, are presented as follows:

2019	Intesa Sanpaolo S.p.A., Italy, England,Ireland; Romania	Privredna banka d.d., Zagreb, Croatia	Intesa Leasing d.o.o., Belgrade	Vseobecna Uverova bank A.S., Slovakia	Banka Koper d.d., Slovenia	Intesa Sanpaolo Banka D.D. Bosnia and Herzegovina	CIB Bank, Hungary	Intesa Sanpaolo Holding International S.A., Luxemburg
Loans and receivables from banks and other financial organisations	4,981,379	36,203	5,986,533	21,262	21,504	19,208	-	-
Receivables from derivatives	50,356	-	-	-	-	-	-	-
Other assets	37,831	-	17,408	770	-	-	-	-
Total assets	**5,069,566**	**36,203**	**6,003,941**	**22,032**	**21,504**	**19,208**	**-**	**-**
Deposits and other liabilities due to banks, other financial organisations and Central bank	32,545,867	626,487	176,587	-	-	90	-	-
Deposits and other liabilities to customers	-	-	-	-	-	-	-	617
Liabilities based on hedging derivative instruments	7,869	-	-	-	-	-	-	-
Other liabilites	226,586	1,021	6,854	-	-	-		-
Total liabilities	**32,780,322**	**627,508**	**183,441**	**-**	**-**	**90**	**-**	**617**
Interest income	203,482	294	71,053	-	-	-	-	-
Fee and commission income	33,599	163	1,364	217	-	-	-	-
Net profit from changes in fair value of financial instruments	42,487	-	-	-	-	-	-	-
Other operating income	25,055	-	22,069	-	-	-	-	-
Total income	**304,623**	**457**	**94,486**	**217**	**-**	**-**	**-**	**-**
Interest expense	(10,185)	(2,891)	(2,113)	-	-	-	-	-
Fee and commission expenses	(90,052)	(5,354)	(53)	(1,041)	(2,738)	(447)	-	83
Net loss on foreign exchange rate and FX contracts	(347,295)	(204)	-	-	-	-	-	-
Other expenses	(550,172)	(25,827)	-	-	-	-	(5,678)	-
Total expenses	**(997,704)**	**(34,276)**	**(2,166)**	**(1,041)**	**(2,738)**	**(447)**	**(5,678)**	**83**
Off-balance sheet items - derivatives FX SWAPs	29,610,775	-	-	-	-	-	-	-
Off-balance sheet items - guarantees	293,767	-	-	58,432	-	-	-	-
Total off-balance sheet items	**29,904,542**	**-**	**-**	**58,432**	**-**	**-**	**-**	**-**

27. RELATED PARTY DISCLOSURES (Continued)

2018	Intesa Sanpaolo S.p.A., Italy, England, SAD; German; Ireland; Romania;Albania;Group Service	Privredna banka d.d., Zagreb, Croatia	Intesa Leasing d.o.o., Belgrade	Vseobecna Uverova bank A.S., Slovakia	Banka Koper d.d., Slovenia	Bank of Alexandria, Egypt	Intesa Sanpaolo Banka D.D. Bosnia and Herzegovina	CIB Bank, Hungary	Intesa Sanpaolo Holding International S.A., Luxemburg	Banca IMI S.p.a
Loans and receivables from banks and other financial organisations	8,981,589	82,951	4,509,034	71,556	20,737	-	11,892	-	-	-
Loans and receivables from customers		-	-	-	-	-	-	-	-	-
Receivables from derivatives	324,206	-	-	-	-	-	-	-	-	-
Other assets	40,976	817	101,354	154	26	-	10	-	-	-
Total assets	**9,346,771**	**83,768**	**4,610,388**	**71,710**	**20,763**	**-**	**11,902**	**-**	**-**	**-**
Deposits and other liabilities due to banks, other financial organisations and Central bank	19,891,045	1,119	932,181	-	-	-	91	-	707	-
Deposits and other liabilities to customers				-	-	-	-	-		-
Liabilities based on hedging derivative instruments	13,468	206		-	-	-	-	-	-	-
Other liabilites	217,224	17,021	4,611	-	-	-	-	2,127	-	-
Total liabilities	**20,121,737**	**18,346**	**936,792**	**-**	**-**	**-**	**91**	**2,127**	**707**	**-**
Interest income	74,544	-	41,315	-		-		-	-	-
Fee and commission income	36,738	3,115	1,213	636	131	-	24	-	82	-
Net profit from changes in fair value of financial instruments	324,206	-	-	-	-	-	-	-	-	-
Net profit on foreign exchange rate and FX contracts	24,436	-	-	-	-	-	-	-	-	-
Other operating income	25,460	-	103,322	-	-	-	-	-	-	-
Total income	**485,384**	**3,115**	**145,850**	**636**	**131**	**-**	**24**	**-**	**82**	**-**
Interest expense	(9,510)	(3,783)	(2,849)			-	-	-	-	-
Fee and commission expenses	(110,996)	(4,820)	-	(790)	(2,353)	-	(704)	-		-
Net loss from changes in fair value of financial instruments	(13,468)	(206)	-	-	-	-	-	-	-	-
Net loss on foreign exchange rate and FX contracts	(12,093)		-	-	-	-	-	-	-	-
Other expenses	(532,570)	(29,286)	-	-	-		-	(2,127)	-	
Total expenses	**(678,637)**	**(38,095)**	**(2,849)**	**(790)**	**(2,353)**	**-**	**(704)**	**(2,127)**	**-**	**-**
Off-balance sheet items - derivatives FX SWAPs	46,250,790	**622,311**	-		-	-	-	-	-	-
Off-balance sheet items - guarantees	3,265,060	21,493	-	1,818,757	-	31,117	-	4,962	-	-
Total off-balance sheet items	**49,515,850**	**643,804**	**-**	**1,818,757**	**-**	**31,117**	**-**	**4,962**	**-**	**-**

27. RELATED PARTY DISCLOSURES (Continued)

The above stated receivables and liabilities at the balance sheet date, as well as income and expenses arising from transactions with the related parties from the Intesa Sanpaolo Group, are the result of ordinary business activities.

Interest on the Bank's receivables and payables is calculated at the usual rates.

(a) Gross salaries and other benefits of the Executive Board's members and other key management personnel of the Bank, including the Board of Directors' members, during 2019 and 2018, are presented as follows:

		In RSD thousand
	2019	**2018**
Remunerations to the members of the Executive Board, Board of Directors and other key management of the Bank	261,175	284,225
Total	**261,175**	**284,225**

(b) Loans and receivables from the members of the Executive Board and the Board of Directors and other key management personnel of the Bank, are presented as follows:

		In RSD thousand
	2019	**2018**
Loans	59,839	61,561
Total allowances for impairment	(40)	(41)
Balance as of 31 December	**59,799**	**61,520**

28. RISK MANAGEMENT

Risk is an inherent part of the Bank's activities and cannot be eliminated completely. It is important to manage risks in such a way that they can be reduced to limits acceptable for all interested parties: shareholders, creditors, depositors, regulators. Risk management is the process of permanent identification, assessment, measurement, monitoring and controlling of the Bank's exposure to risks. An important part of risk management is reporting and mitigating risk. An adequate system of risk management is a critical element in ensuring the Bank's stability and profitability of its operations.

The Bank is exposed to the following major risks: credit risk, liquidity risk, interest rate risk, foreign currency risk, operational risk, risk of exposure toward a single entity or a group of related entities (concentration risk), risk of permanent investments, risk related to the country of origin of the entity to which the Bank is exposed and other risks.

The Board of Directors and the Executive Board are responsible for implementation of an adequate risk management system and for its consistent application.

The Bank's Board of Directors adopts the procedures for identification, measurement and assessment of risks, and is responsible for implementing a unique risk management system and supervision over that system.

The Bank's Executive Board is responsible for identifying, assessing and measuring risks the Bank is exposed to in its operations, and applies the principles of risk management approved by the Bank's Board of Directors. The Executive Board approves internal acts which define risk management and proposes strategies and policies for risk management to Audit Committee and Board of Directors.

28. RISK MANAGEMENT (Continued)

The Committee for monitoring business activities (Audit Committee) analyses and adopts proposals of policies and procedures with respect to risk management and internal controls, which are submitted to the Board of Directors for consideration and adoption. Furthermore, the Committee analyses and monitors the application and adequate implementation of adopted policies and procedures for risk management, and recommends new ways for their improvement, if necessary.

The Risk Management Department has been established in the Bank in order to implement a special and unique system for risk management, as well as to enable functional and organizational segregation of risk management activities from regular business activities. This department is directly responsible to the Executive Board.

The Bank has developed the comprehensive risk management system by introducing policies and procedures, as well as limits for risk levels acceptable for the Bank.

The Bank’s organizational parts authorized for risk management constantly monitor changes in regulations, while analyzing their influence on the risks at entity level of the Bank. They take necessary measures to make the Bank’s business activities and procedures fully compliant with new procedures within the scope of controlled risk. In addition, introduction of new services is followed by necessary market and economic analysis in order to optimize the relation between income and the provision for estimated risks.

28.1. Credit risk

Credit risk is the risk that credit beneficiaries will not be able to fulfil contractual obligations to the Bank.

Through its internal acts, policies and procedures, the Bank has implemented an adequate system of credit risk management, thus reducing credit risk to an acceptable level. The Bank manages credit risk through setting credit risk limits, establishing acceptable credit limits for individual customers or for groups of customers.

Credit risk is managed by the Bank at a counterparty specific level, group of related parties, and at total credit portfolio level. For the purpose of implementing the policy of optimal credit risk exposure, the Bank evaluates creditworthiness of each client, both at the moment of loan application, as well as through subsequent regular and continuous performance analysis.

Analysis of the client’s creditworthiness, timely settlement of liabilities in the past, value of collateral at customer level and at transaction level, is performed within the Credit Management Department.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)
Maximal exposure to credit risk

Maximal exposure to credit risk by the type of client as of 31 December 2019 and 2018 are presented as follows:

In RSD thousand

December 31st 2019	Balance sheet assets to be exposed to credit risk	Allowances for impairment for balance sheet assets to be exposed to credit risk	Balance sheet assets not to be exposed to credit risk	Balance sheet as of 2019
Cash and balances with Central Bank	97,392,634	-	-	97,392,634
Receivables from derivatives	-	-	61,978	61,978
Securities	105,913,950	(24)	2,393,734	108,307,660
Loans and receivables from banks and other financial organizations	51,189,968	(23,411)	-	51,166,557
Loans and receivables from banks	45,182,980	(20,421)	-	45,162,559
Loans and receivables from other financial organizations	6,006,988	(2,990)	-	6,003,998
Loans and receivables from customers	386,526,918	(12,617,346)	-	373,909,572
Investments in subsidiaries	-	-	1,199,472	1,199,472
Intangible assets	-	-	5,348,965	5,348,965
Property, plants and equipment	-	-	9,953,027	9,953,027
Investment property	-	-	776	776
Deferred tax assets	-	-	683,199	683,199
Non-current assets held for sale and discontinued operations	-	-	38,301	38,301
Other assets	3,136,623	(383,509)	1,815,637	4,568,751
TOTAL ASSETS:	**644,160,093**	**(13,024,290)**	**21,495,089**	**652,630,892**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)
Maximal exposure to credit risk

In RSD thousand

December 31st 2018	Balance sheet assets to be exposed to credit risk	Allowances for impairment for balance sheet assets to be exposed to credit risk	Balance sheet assets not to be exposed to credit risk	Balance sheet as of 2018
Cash and balances with Central Bank	86,962,607	-		86,962,607
Receivables from derivatives	-	-	331,839	331,839
Securities	92,199,341	(355,985)	1,029,129	92,872,485
Loans and receivables from banks and other financial organizations	33,083,337	(44,072)		33,039,265
Loans and receivables from banks	26,019,208	(41,851)	-	25,977,357
Loans and receivables from other financial organizations	7,064,129	(2,221)		7,061,908
Loans and receivables from customers	356,539,202	(16,790,088)	-	339,749,114
Investments in subsidiaries	-	-	1,199,472	1,199,472
Intangible assets	-	-	3,774,866	3,774,866
Property, plants and equipment	-	-	7,951,099	7,951,099
Investment property	-	-	30,995	30,995
Deferred tax assets	-	-	704,800	704,800
Non-current assets held for sale and discontinued operations	143,015	-	-	143,015
Other assets	3,281,821	(25,643)	1,059,445	4,315,623
TOTAL ASSETS:	**572,209,323**	**(17,215,788)**	**16,081,645**	**571,075,180**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Maximal exposure to credit risk (Continued)

Classification of off-balance sheet items is shown in Note 26.

Permanent monitoring of a client's internal rating, the level of risk with respect to each client, the necessary amount of reserve for risk coverage, concentration risk (large exposures), portfolio credit risk, the level of capital necessary for coverage of all credit risks is performed by the Risk Management Department.

The Bank established a special organizational unit, the Delinquency Management Department, in order to manage receivables with a problem in collectability in a timely manner.

The Credit Management Department, the Risk Management Department and the Delinquency Management Department are independent units in the Bank.

Principles prescribed by the National Bank of Serbia, as well as the Bank's internal procedures are applied in these analyses in order to anticipate potential risks that can arise in terms of a client's inability to settle liabilities when they fall due and according to contracted terms.

In that sense, an assessment of the level of required reserves level for potential losses, both at the moment of approval of certain loan, as well as through a continuous, portfolio analysis on a monthly level, are carried out. The analysis entails measuring the adequacy of provision/reserves according to client type, risk type, according to sub-portfolios and total portfolio of the Bank.

Decision making on exposure to credit risk is performed based on proposals provided by the Credit Management Department. The terms for approval of each corporate loan are determined individually, depending on the client type, purpose of loan, estimated creditworthiness and current market position. Types of collateral that accompany each loan are also determined according to a client's creditworthiness analysis, type of credit risk exposure, term of placement, as well as the amount of a particular loan. Conditions for loan approvals to retail clients and entrepreneurs are determined by defining standard conditions for different types of products.

Risk price for standard types of products is calculated according to the analysis of credit costs which the Bank had in the past and historical probability of getting into default status per the same or similar type of product. Risk price for the SME and Corporate segment is calculated on the basis of the client's internal rating or historically adjusted probability of getting into default status per each rating category.

Considering the importance of credit risk, dispersion of authorizations was carried out in respect of the decision making process related to loan approval activities. This dispersion is provided with prescribed limits up to which an authorized person or management body can make loan approval decisions. Organizational parts making decisions with respect to loan approvals, with different levels of authorizations, are as follows: branch managers, regional managers, Credit Management Department, Credit Board, Credit Committee, Executive Board and Board of Directors. For credit exposures exceeding the determined limit, approval of the Parent Bank is necessary.

The Bank manages credit risk by setting up limits with respect to period, amount and results of an individual customer's creditworthiness, through diversification of loans to a larger number of customers and contracting foreign exchange clauses and index-linking to a consumer price index in order to maintain the real value of loans.

Furthermore, the Bank manages credit risk through assessment and analysis of received collaterals, by providing allowances for impairment of financial assets, provisions for off-balance sheet items, reserves for estimated credit losses, as well as by determining the adequate price of a loan which covers the credit risk of a particular placement.

In addition to a clients' creditworthiness, risk limits are also set based on different types of collateral. Risk exposure toward a single debtor, including banks, is limited and includes balance sheet and off-balance sheet items exposures. Total risk exposure to a single customer (or a group of related parties) regarding exposure limits, is considered thoroughly and analyzed before executing a transaction.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Loan concentration risk

Loan concentration risk is the risk arising, directly or indirectly, from the Bank's exposure to the same or similar source or type of risk. The Bank controls loan concentration risk by limiting the exposure, which enables the diversification of the loan portfolio. In order to monitor more efficiently concentration risk, the Bank has determined three categories of limits: specific limits, general limits and regulatory limits.

Derivative financial instruments

Derivative financial instruments result in the Bank's exposure to credit risk when the fair value of such instruments is positive for the Bank.

Credit exposure arising from derivatives is calculated using the current exposure method, i.e. the sum of the positive fair value of the contract and the nominal value of the derivative multiplied by a coefficient which depends on the type and maturity of the financial derivative, as prescribed by the National Bank of Serbia.

The credit risk of derivatives is limited by determining maximum credit exposure arising from a derivative for each individual customer.

Derivative financial instruments (Continued)

In accordance with the above mentioned, as of 31 December 2019 and 31 December 2018 the Bank has the following exposures to counterparties:

In RSD thousand

	Nominal value	**Total exposure**
Total 2019	**30,069,632**	**370,200**
Currency (FX) Swap	29,575,742	353,639
By currency:		
AUD	757,240	17,795
CAD	643,286	6,433
CHF	4,986,418	57,451
EUR	11,829,836	147,534
GBP	1,541,118	21,395
NOK	119,017	1,624
RSD	8,257,000	84,203
SEK	392,641	3,926
USD	1,049,186	13,278
Currency(FX) Forward	**493,890**	**16,561**
By currency:		
EUR	493,890	16,561

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Derivative financial instruments (Continued)

Total 2018	**47,976,728**	**811,237**
Currency (FX) Swap	47,476,273	800,095
By currency:		
AUD	824,699	8,359
CAD	637,249	6,372
CHF	2,729,425	35,761
EUR	23,993,504	518,810
GBP	1,547,943	17,322
NOK	100,954	1,188
RSD	17,272,700	207,584
SEK	369,798	4,698
Currency (FX) Forward	500,455	11,142
By currency:		
EUR	417,227	9,722
USD	83,228	1,420

Stated amounts represent credit exposure on derivatives, calculated as the sum of the positive fair value of the contract and the nominal value of the derivative, multiplied by a coefficient prescribed by the National Bank Serbia. The amounts presented within the Note 26(d) represent fair value of derivatives in the Bank's books of account.

The Bank calculates capital requirements for credit valuation adjustment (CVA), in accordance with the new Decision on Capital Adequacy of Banks published by the National Bank of Serbia.

Adjustment of credit exposure, calculated only for derivative instruments, represents an adjustment to the mid-market valuation of the portfolio of transactions with a counterparty. This adjustment reflects the market value of the credit risk of that counterparty to the Bank.

During 2019 the exposure to the CVA risk was negligible. As of 31 December 2019, the Bank has the following exposure to the CVA risk:

	In RSD thousand **Total exposure**
Total 2019	16,154
Currency (FX) Swap	-
Currency (FX) Forward	**16,154**

Credit-related risks

The Bank issues guarantees and letters of credit to its clients, based on which the Bank commits to make payments on behalf of third parties. In this way the Bank is exposed to risks similar to credit risks, which can be mitigated by the same control processes and policies applied for credit risk.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Derivative financial instruments (Continued)

Collaterals and other instruments of credit risk protection

The amount and type of the collateral required depends on an assessment of credit risk of each customer. Terms of collateral with respect to each placement are determined by the analysis of a customer's creditworthiness, type of exposure to the credit risk, placement's maturity, as well as the amount itself.

Contractual authorization, as well as bills of exchange are provided by customers as standard collaterals while, depending on the assessment, additional collaterals may be required, such as real estate mortgages, movable property pledges, partial or entire coverage of placements with deposits, state guarantees, guarantees issued by another bank or a legal entity, pledging of securities, or joint loan contracting with another legal entity which then becomes the joint debtor.

In cases of real estate mortgages or movable property pledges, the Bank always obtains valuation of the assets, carried out by an authorized appraiser, in order to minimize potential risk. Decisions on placements to retail clients and small business (entrepreneurs) are mostly based on appraisal of standardized, previously defined conditions, using a scoring model, with additional analysis by credit analysts.

Assessment of impairment of financial assets

Bank applies expected credit losses model for valuating financial assets measured at amortized cost or fair value through other comprehensive income (FVOCI), except equity instruments. Banks performs this valuation on individual and collective basis.

- **Individual assessment of impairment**

The Bank performs an individual assessment of impairment for each individually significant loan or advance (for legal entities the amount over EUR 250,000) if it is in the status of default (materially significant amount overdue more than 90 days), i.e. if there is objective evidence that the loan has been impaired.

The level of impairment of loans is determined based on the projection of expected cash flows which shall be collected pursuant to contracts with clients, taking into consideration the assessment of financial position and creditworthiness of the client, the realizable value of collateral, as well as the timing of the expected cash flows from realization of collaterals, etc. In order to calculate expected credit loss different scenarios have been introduced (weighted by different probabilities) to assess future cash flows, with additional correction which take into consideration assessed macroeconomic impact (add-on).

Projected cash flows are discounted to their present value using the effective interest rate. Impairment loss is measured as the difference between the carrying amount of a loan and its estimated recoverable amount, being the present value of expected future cash flows. Individual assessment of the impairment of placements is performed at least semi-annually.

If new information becomes available that, as estimated by credit analysts, have an effect on the client's creditworthiness and the value of collateral, as well as the certainty of settling the liabilities toward the Bank, an extraordinary assessment of the impairment of a loan is performed.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Assessment of impairment of financial assets

- **Collective assessment of impairment**

The Bank has defined the criteria for classifying financial instruments into corresponding impairment stages (Stage 1, 2 and 3), depending on the level of increase in credit risk since initial recognition. The subject of the classification are financial instruments that are measured at amortized cost, as well as financial instruments valued at fair value through other comprehensive income (FVOCI). Stage 2 relates to exposures with a significant increase in credit risk (compared to the moment of initial recognition). The criteria defined by the Bank for detecting a significant increase in credit risk are:

1.) Days past due over 30 days,
2.) Forborne status,
3.) PM (*Proactive Management*) status and
4.) Significant increase in PD (*Probability of Default*).

Stage 3 consists of loans, where objective or subjective evidence that the loan has been impaired exists.

Objective evidence of impairment implies a continuous delay in payment of more than 90 days in a materially significant amount. The calculation of the material significance of the delay is determined at the client level in accordance with the provisions of Item 10 of the Guidelines for Identification the Default, of the National Bank of Serbia. The relative materiality threshold is 1% of total balance sheet exposure, while the absolute threshold differs depending on the exposure class (RSD 1,000 for debtors in the retail exposure class, and RSD 10,000 for other debtors). Subjective proof of the existence of default status i s based on Bank's assessment that the client will not be able to fully settle its obligations to the Bank, without considering collection from the collateral realization. The subjective assessment of the default status is based on quantitative and qualitative, internal and externally obtained information about the debtor (for example: number of days of current account blocking, bankruptcy / liquidation, sue and other adverse events and negative signs identified in the subjective assessment that indicate a significant deterioration of the client's financial condition and inability to settle liabilities completely). In addition to changing the rules of day past due calculation applied in the first quarter of 2019, which led to an increase in Stage 3 exposure of RSD 581 million, the Bank also applied (in accordance with the guidelines of the Parent Bank) other rules regarding a new definition of default status defined by the National Bank of Serbia Guidelines and the relevant EBA regulation ("Guidelines on the application of the definition of default under Article 178 of Regulation (EU) No 575/2013") in 2019 , where the most significant change was the introduction of the Probation Period lasting not less than 90 days for exposures in default status where the criteria that led the client to this status are no longer active. As of December 31, 2019, the total balance sheet exposure in the Probation Period amounts to RSD 439 million.

Different impairment stages result in different ways of calculating the expected credit losses:

- Stage 1 exposures the 12-month expected credit losses are calculated
- Stage 2 and Stage 3 exposures - *"lifetime"* expected credit losses

Bank has developed an internal methodology and calculated the risk parameters (EAD, PD, LGD, CCF). The discount rate used in the calculation is the effective interest rate of the individual contract.
In the context of calculating the lifetime expected credit losses, the Bank has developed a methodology for determining EAD (Exposure at Default) for all periods until the final maturity of a financial instrument. For amortizing products for which repayment plans are available, the future EAD is determined on the basis of repayment plans. For other products, EAD on the reporting date is used, with the credit conversion factors applied. Credit conversion factors, depending on the type of products and segments, can be regulatory or internally calculated on the basis of historical data on usage of available limits.

As the basis for calculating the *"lifetime"* PD parameter, the existing (Basel II) PD models have been used. The models have been adjusted in accordance with the requirements of IFRS 9:

- transition from TTC (Through the cycle) to PIT (Point in time) concept,
- introduction of coefficients (as PD corrections) that reflect the macroeconomic impact on the parameter for future periods, using three scenarios (baseline, best, adverse),
- *"lifetime"* projection (Markovian approach is used).

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Assessment of impairment of financial assets

For segments not covered by PD models, the historical default rates have been used as approximation, with additional (above mentioned) adjustments.

For clients/exposures subject to collective assessment, the LGD (*Loss Given Default)* parameter is calculated on the basis of average historical loss rates for defined segments, whereby obtained values are additionally corrected by coefficients representing a measure of the estimated macroeconomic impact on LGD for future periods. For the purpose of macroeconomic adjustment of the LGD parameter, three scenarios are used (baseline, best, adverse).

The Bank incorporates forward-looking information both into the assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and the measurement of Expected Credit Losses.

Inclusion of forward-looking information has been performed through the adjustment of PD and LGD values in order to consider the expectations of its change linked to macroeconomic environments that can occur in the future years with respect to reporting date.

- The macro adjustment of the PD is implemented stress coefficients obtained from an internally developed PD stress test model based on the regression equation, which quantifies the relationship between the deterioration of credit portfolio (changing probability of default) and changes in macro variables or variables that are identified as being relevant to the conditions in which the Bank operates. Model prioritizes variables with the greatest impact on credit risk (each macro variable affects the credit risk in varying degrees and time horizon). PD stress model has been developed especially for the segment of companies and individuals.

- The macro-conditioning has been carried out by using EBA Stress Test Coefficients in the absence of internally developed stress satellite models. Since EBA releases only Baseline and Adverse coefficients, Best scenario coefficients have been calculated internally on the basis of Group’s methodology defined for that purpose. The forward-looking elements are calculated for the next 2 years of the residual maturity with respect to the reporting date so that Baseline risk parameters are adjusted with Add-on which takes into account all three scenarios. EBA coefficients for Rest of the World have been used for macroeconomic conditioning of LGDs, since the coefficients are not available for the state of Serbia. The value of the coefficients varies depending on the exposure segment. The same coefficient values obtained from the Parent Bank come from the 2018 EBA stress test exercise.

Implemented PD for the purpose of calculating provisions for credit losses was obtained as a linear combination of changes in PD in the normal, adverse and best-case scenario. In all three scenarios, the values of the rate of change of current PD are obtained based on the PD satellite stress test model, which determines a linear relationship between the logarithmic change of the PD rate and the change in certain macroeconomic parameters that are recognized as statistically and economically relevant. In the case of change in the PD rate for corporate portfolio, the macroeconomic variables that are recognized as relevant are change in FX rate, change in the local Key Policy Rate and change in Real Wages. In the case of a change in PD rate for retail portfolio, macroeconomic variables that are recognized as relevant are change in FX rate, change in the market interest rate on the euro (Euribor 6m), change in Real wage and NPL rate for corporate portfolio (variable estimated by the model for corporate). Given that macroeconomic variables are non-stationary in nature, their mathematical transformations are used in the regressions (most often the yield rate calculated by the natural logarithm). In addition, change in particular macroeconomic variable does not have an immediate impact on credit risk, respectively on the probability of default, the PD stress test satellite model accepts such "delayed" impact. Thus, changes in macroeconomic variables that occurred in previous quarters were found to have the greatest impact on future projected PD. The extent to which each of the variables will affect changes in the default rate is defined by the estimates of the regression parameters.

Macroeconomic parameter values in the stress (adverse) and best-case scenario were obtained as 0.1 and 99.9 percentiles of the historical distribution of their values over the last 10 years (or shorter if the parameter series is not available), while values in the baseline scenario were obtained from Research Office.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

The values used in the above cases are:

Corporate

2019	FX rate	Key Policy Rate	Real wages
Baseline scenario	0.25%	0.5	2.62%
Adverse scenario	18.49%	8.47	-0.19%
Best scenario	-6.93%	-1.55	8.58%

2020	FX rate	Key Policy Rate	Real wages
Baseline scenario	0.25%	0.5	2.12%
Adverse scenario	-3.09%	-1.22	1.34%
Best scenario	2.23%	-0.31	11.20%

2021	FX rate	Key Policy Rate	Real wages
Baseline scenario	0.42%	0.75	1.97%
Adverse scenario	8.76%	0.5	3.63%
Best scenario	0.71%	-0.13	7.55%

Retail

2019	FX rate	NPL corporate	Real wages	Euribor 6m
Baseline scenario	0.25%	-0.16	2.62%	-0.18
Adverse scenario	18.49%	1.59	-0.19%	0.75
Best scenario	-6.93%	-0.72	8.58%	-1.71

2020	FX rate	NPL corporate	Real wages	Euribor 6m
Baseline scenario	0.25%	0.15	2.12%	0.3
Adverse scenario	-3.09%	2.96	1.34%	0.79
Best scenario	2.23%	-1.39	11.20%	-1.49

2021	FX rate	NPL corporate	Real wages	Euribor 6m
Baseline scenario	0.42%	0.19	1.97%	0.71
Adverse scenario	8.76%	0.01	3.63%	-0.2
Best scenario	0.71%	-0.53	7.55%	-1.6

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Based on the coefficients obtained from the internal PD stress model, macroeconomic conditioning of PD values used in the calculation of expected credit losses is performed for the next 3 years of remaining maturity relative to the reporting date, where values from the Baseline scenario are additionally adjusted for add-on "Which takes into account all three scenarios.

The macroeconomic conditioning of LGDs was done using EBA coefficients in the absence of internally developed models (since EBA relies only on Core and Adverse coefficients, the coefficients for the Favorable Scenario were calculated internally based on the Group's methodology written for this purpose). Forward-looking elements have been calculated for the next 3 years of remaining maturity over the reporting date, so the baseline scenario risk parameters are adjusted for an add-on that takes into account all three scenarios.

For exposures belonging to the segment "Low Default Portfolio" (states, local governments and banks), the parameters obtained internal models of Parent Bank, since the Bank in this part of the portfolio does not have enough historical data to make them herself charged.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(a) Portfolio quality

The Bank manages the quality of its financial assets using the internal classification of placements, which is in compliance with the standards of the Parent Bank.

The following tables present the quality of the portfolio (gross balance exposure and off-balance sheet exposure) as of 31 December 2019 and 2018 based on the Bank's rating system:

In RSD thousand

	Balance sheet assets to be classified						Off - balance sheet items to be classified				
	Loans to Customers			Loans to Banks						Total 2019*.	Total 2018*.
	Stage 1	*Stage 2*	*Stage 3*	*Stage 1*	*Stage 2*	*Stage3*	*Stage 1*	*Stage 2*	*Stage 3*		
Class:											
Performing	343,772,810	39,162,813	-	141,869,744	705,870	-	138,019,110	5,939,845	-	669,470,192	598,442,481
Past Due	-	-	778,045	-	-	-	-	-	43,042	821,087	467,013
Unl.to Pay	-	-	6,795,955	-	-	-	-	-	656,588	7,452,543	8,933,652
Doubtful	-	-	5,160,906	-	-	-	-	-	196,269	5,357,175	12,640,637
Total	**343,772,810**	**39,162,813**	**12,734,906**	**141,869,744**	**705,870**	**-**	**138,019,110**	**5,939,845**	**895,899**	**683,100,997**	**620,483,783**

In RSD thousand

	Allowances for impairment and provision customers			Allowances for impairment and provision banks			Total 2019*.	Total 2018*.
	Stage 1	*Stage 2*	*Stage 3*	*Stage 1*	*Stage 2*	*Stage 3*		
Class:								
Performing	1,967,118	3,373,312	-	11,939	8,482	-	5,360,851	5,353,169
Past Due	-	-	370,630	-	-	-	370,630	191,503
Unlikely to Pay	-	-	3,712,294	-	-	-	3,712,294	4,257,324
Doubtful	-	-	3,901,542	-	-	-	3,901,542	8,280,827
Total	**1,967,118**	**3,373,312**	**7,984,466**	**11,939**	**8,482**	**-**	**13,345,318**	**18,082,823**

Categories Past due, Unlikely to pay and Doubtful are non-performing receivables (impaired receivables).
* Total assets exposed to credit risk does not include securities relating to the bonds of the Republic of Serbia that are entirely classified as level 1

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

The following tables present the quality of the portfolio as of 31 December 2019 based on type of receivables:

In RSD thousand

Securities	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Bonds of the Republic of Serbia	105,913,950	-	-	105,913,950
Total	**105,913,950**	**-**	**-**	**105,913,950**
Loans to Customers	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balance sheet assets to be classified	196,575,068	22,489,802	6,910,205	225,975,075
Off - balance sheet items to be classified	111,970,768	4,968,292	618,662	117,557,722
Total	**308,545,836**	**27,458,094**	**7,528,867**	**343,532,797**
Loans to Retail	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balance sheet assets to be classified	147,197,742	16,673,011	5,824,701	169,695,454
Off - balance sheet items to be classified	25,017,463	951,415	277,237	26,246,115
Total	**173,443,857**	**17,624,426**	**6,101,937**	**195,941,569**
Loans to Banks	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balance sheet assets to be classified	141,869,744	705,870	-	142,575,614
Off - balance sheet items to be classified	1,030,879	20,138	-	1,051,017
Total	**142,900,622**	**726,009**	**-**	**143,626,631**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

The following table presents the quality of the portfolio for performing clients (gross balance exposure and off-balance sheet exposure) based on the Bank's internal rating as of 31 December 2019.

	Loans to Customers		Loans to banks		Balance sheet assets to be classified - Total	Off - balance sheet items to be classified		Total
Rating	**Stage 1**	**Stage 2**	**Stage 1**	**Stage 2**		**Stage 1**	**Stage 2**	
A	137,436,072	240,046	-	-	137,676,118	72,389,375	142,252	210,207,745
B	172,372,162	17,200,994	-	-	189,573,156	59,590,987	4,619,048	253,783,191
C	6,757,635	17,074,826	-	-	23,832,461	870,753	1,036,000	25,739,213
Satisfactory	240,261	3,633,455	-	-	3,873,716	-		3,873,715
Good	2,817,302	-	-	-	2,817,302	1,318,497	-	4,135,799
Not covered with models	13,661,238	201,260	136,753,344	-	150,615,842	1,405,165	106,779	152,127,786
I		-	3,124,460	-	3,124,460	-	-	3,124,460
M	-	-	1,149,387	-	1,149,387	-	-	1,149,387
R	-	-	117,570	705,870	823,440	-	-	823,440
S	10,488,140	812,232	724,983	-	12,025,355	2,444,333	35,766	14,505,455
	-	-	-	-	-	-	-	-
Total	**343,772,810**	**39,162,813**	**141,869,744**	**705,870**	**525,511,237**	**138,019,110**	**5,939,845**	**669,470,192**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Overview of stock and movement in the allowance for impairment and provisions in 2019 and 2018 by client type:

	Loans and receivables			In RSD thousand
Movement in the allowance for impairment and provisions in 2019	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Opening balance - 01.01.2019.	**2,462,295**	**2,891,057**	**12,729,653**	**18,082,825**
Transfer to stage 1	925,323	(793,031)	(132,292)	-
Transfer to stage 2	(273,220)	399,818	(126,598)	-
Transfer to stage 3	(58,364)	(259,061)	317,425	-
Re-measurement	1,109,814	969,958	1,640,432	**1,500,576**
New production *	1,425,644	1,951,381	1,091,738	**4,468,763**
Collection	1,392,625	1,778,328	(576,370)	**(3,747,323)**
Transfer to off balance	-	-	(5,938,028)	**(5,938,028)**
Sale of receivables	-	-	(1,021,493)	**(1,021,493)**
Closing balance - 31.12.2019.	**1,979,057**	**3,381,794**	**7,984,467**	**13,345,318**

	Securities (FVOCI)			In RSD thousand
Movement in the allowance for impairment and provisions in 2019	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Opening balance - 01.01.2019.	**355,964**	**-**	**-**	**355,964**
Opening balance - 01.01.2019.	1,362		-	**1,362**
New production	48,872	-	-	**48,872**
Collection			-	
Closing balance - 31.12.2019.	**406,198**	**-**	**-**	**406,198**

***** New production is the classification under the level of 31 December 2019, and not during the initial approval

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

In RSD thousand

Movement in the allowance for impairment and provisions in 2019	Banks Stage 1	Banks Stage 2	Banks Stage 3	Total 2019
Opening balance - 01.01.2019.	**42,021**	**3**	**19**	**42,043**
Transfer to stage 1	-	-	-	**-**
Transfer to stage 2	-	-	-	**-**
Transfer to stage 3	-	-	-	**-**
Re-measurement	(66)	-	-	**(66)**
New production	11,934	8,482	-	**20,416**
Collection	(41,950)	(3)	(19)	**(41,972)**
	-	-	-	**-**
	-	-	-	**-**
Closing balance - 31.12.2019.	**11,939**	**8,482**	**0**	**20,422**

Movement in the allowance for impairment and provisions in 2019	Retail Stage 1	Retail Stage 2	Retail Stage 3	Total 2019
Opening balance - 01.01.2019.	**1,201,191**	**1,608,562**	**3,121,298**	**5,931,051**
Transfer to stage 1	716,292	(584,332)	(131,960)	-
Transfer to stage 2	(166,029)	292,519	(126,490)	-
Transfer to stage 3	(43,503)	(232,933)	276,436	-
Re-measurement	(654,971)	419,758	1,158,236	923,023
New production	676,961	1,241,643	807,742	2,726,346
Collection	(853,562)	1,059,054	(347,442)	(2,260,058)
Transfer to off balance	-	-	(1,312,962)	(1,312,962)
	-	-	-	-
Closing balance - 31.12.2019.	**876,379**	**1,686,163**	**3,444,858**	**6,007,400**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Movement in the allowance for impairment and provisions in 2019	Corporate			
	Stage 1	**Stage 2**	**Stage 3**	**Total 2019**
Opening balance - 01.01.2019.	**1,219,084**	**1,282,492**	**9,608,154**	**12,109,730**
Transfer to stage 1	209,031	(208,699)	(332)	**-**
Transfer to stage 2	(107,191)	107,299	(108)	**-**
Transfer to stage 3	(14,861)	(26,128)	40,989	**-**
Re-measurement	(454,960)	550,200	482,378	**577,619**
New production	736,749	701,256	283,996	**1,722,001**
Collection	(497,113)	(719,271)	(228,909)	**(1,445,293)**
Transfer to off balance			(4,625,066)	**(4,625,066)**
Sale of receivables			(1,021,493)	**(1,021,493)**
Closing balance - 31.12.2019.	**1,090,739**	**1,687,149**	**4,539,609**	**7,317,497**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Movement in the allowance for impairment and provisions in 2018	Loans and receivables Stage 1	Stage 2	Stage 3	In RSD thousand Total 2018
Opening balance - 01.01.2018.	**2,185,395**	**2,718,517**	**15,122,880**	**20,026,792**
Transfer to stage 1	690,367	(600,281)	(90,086)	**-**
Transfer to stage 2	(155,088)	799,497	(644,409)	**-**
Transfer to stage 3	(45,577)	(366,099)	411,675	**-**
Re-measurement	(593,081)	672,210	3,835,573	**4,366,316**
New production	1,310,670	468,442	483,573	**1,779,112**
Collection	(930,391)	(801,228)	(728,945)	**(2,428,605)**
Transfer to off balance	-	-	(2,366,320)	**(2,366,320)**
Sale of receivables	-	-	(3,294,471)	**(3,294,471)**
Closing balance - 31.12.2018.	**2,462,295**	**2,891,058**	**12,729,471**	**18,082,825**

Movement in the allowance for impairment and provisions in 2018	Securities (FVOCI) Stage 1	Stage 2	Stage 3	In RSD thousand Total 2018
Opening balance - 01.01.2018.	**741,256**	**74,471**	**-**	**815,727**
Transfer to stage 1	(177,057)	(30,227)	-	**(207,284)**
New production	126,798	-	-	**126,798**
Collection	(335,033)	(44,244)	-	**(379,277)**
Closing balance - 31.12.2018.	**355,964**	-	-	**355,964**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

In RSD thousand

Movement in the allowance for impairment and provisions in 2018	Banks			
	Stage 1	Stage 2	Stage 3	Total 2018
Opening balance - 01.01.2018.	**43,647**	**-**	**11**	**43,658**
Transfer to stage 1	-	-	-	**-**
Transfer to stage 2	(1)	1	-	**-**
Transfer to stage 3	-	-	-	**-**
Re-measurement	(1)	2	8	**9**
New production	22,576	-	-	**22,576**
Collection	(24,201)	-	-	**(24,201)**
Closing balance - 31.12.2018.	**42,020**	**3**	**19**	**42,042**

Movement in the allowance for impairment and provisions in 2018	Retail			
	Stage 1	Stage 2	Stage 3	Total 2018
Opening balance - 01.01.2018.	**1,105,686**	**1,621,297**	**3,186,907**	**5,913,890**
Transfer to stage 1	503,553	(422,771)	(80,782)	**-**
Transfer to stage 2	(107,635)	193,486	(85,851)	**-**
Transfer to stage 3	(35,543)	(289,091)	324,634	**-**
Re-measurement	(434,694)	498,078	1,304,612	**1,259,660**
New production	520,532	360,300	228,831	**880,832**
Collection	(350,709)	(352,736)	(337,167)	**(703,445)**
Transfer to off balance	-	-	(1,419,886)	**(1,419,886)**
Closing balance - 31.12.2018.	**1,201,191**	**1,608,563**	**3,121,298**	**5,931,052**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Movement in the allowance for impairment and provisions in 2018	Corporate			
	Stage 1	Stage 2	Stage 3	Total 2018
Opening balance - 01.01.2018.	**1,036,062**	**1,097,220**	**11,935,962**	**14,069,244**
Transfer to stage 1	186,813	(177,510)	(9,303)	**-**
Transfer to stage 2	(47,452)	606,010	(558,558)	**-**
Transfer to stage 3	(10,034)	(77,007)	87,041	**-**
Re-measurement	(158,386)	174,129	2,530,953	**3,106,646**
New production	767,562	108,142	254,742	**875,704**
Collection	(555,481)	(448,492)	(391,778)	**(1,700,959)**
Transfer to off balance	-	-		**(946,434)**
Sale of receivables	-	-	(3,294,471)	**(3,294,471)**
Closing balance - 31.12.2018.	**1,219,084**	**1,282,492**	**9,608,154**	**12,109,730**

Based on bank's management assessment, loss from modification of financial assets which doesn't lead to derecognition in 2019, is not materially significant, and therefore it has not been recorded in profit and loss. Also in 2019, there are no financial assets which are credit impaired, and whose conditions have been significantly modified, so that asset has been derecognized and new financial instrument recognized (POCI).

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

Assessment of impairment of financial assets

(a) Maximum exposure to credit risk*

Analysis of the Bank's maximum exposure to credit risk, by geographical locations, before taking into account collaterals and other hedging funds, as of 31 December 2019 and 2018 is presented in the table below:

In RSD thousand

	Balance sheet assets to be classified*		**Off-balance sheet items to be classified****		**Total ** 2019**
	Loans to customers	***Loans to banks***	***Loans to customers***	***Loans to banks***	***Loans to customers and banks***
Serbia	372,273,172	131,272,854	140,541,397	217,739	644,305,163
Europe	23,207,090	10,505,480	3,224,150	530,830	**37,467,550**
America	21,672	646,539	7,527	62,519	**738,256**
Rest of the world	168,595	150,741	30,763	239,929	**590,028**
Total	**395,670,529**	**142,575,614**	**143,803,837**	**1,051,017**	**683,100,997**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

In RSD thousand

	Balance sheet assets to be exposed to credit risk*		Off-balance sheet items to be exposed to credit risk *		Total 2018
	Loans to customers	*Loans to banks*	*Loans to customers*	*Loans to banks*	*Loans to customers and banks*
Serbia	355,394,591	90,283,495	139,145,971	40,653	584,864,710
Europe	11,617,617	21,623,904	950,350	333,987	34,525,858
America	4,146	1,020,422	1,279	-	1,025,847
Rest of the world	11,813	53,994	1,561	-	67,368
Total	**367,028,167**	**112,981,815**	**140,099,161**	**374,640**	**620,483,783**

**Exposure relating to the Republic of Serbia bonds was excluded*
*** Maximum exposure to credit risk by off-balance sheet items is presented in the Note 26.*

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(a) Maximum exposure to credit risk* (Continued)

Analysis of the Bank's exposure to credit risk by industry sectors as of 31 December 2019 and 2018 is presented in the table below:

In RSD thousand

	Balance sheet assets to be exposed to credit risk*	Off-balance sheet items to be exposed to credit risk**	Total 2019
Industry	**216,825,030**	**117,434,179**	334,259,209
Trade	51,439,365	29,260,772	80,700,137
Transportation and communication	8,517,736	3,286,952	11,804,688
Construction	15,766,640	21,433,859	37,200,499
Services, tourism and accommodation services	6,718,628	526,335	7,244,963
Food and beverage production	14,805,224	4,522,316	19,327,540
Permanent goods production	17,434,044	8,766,317	26,200,361
Agriculture, hunting, fishing and forestry	15,659,200	5,681,604	21,340,804
Other	86,484,193	43,956,024	130,440,218
Banks	**142,575,614**	**1,051,017**	**14,972,897**
Local government	**9,150,046**	**123,543**	**9,273,589**
Retail loans	**169,695,454**	**26,246,115**	**195,941,568**
Mortgage loans	79,692,977	0	79,692,977
Other	90,002,476	26,246,115	116,248,591
	538,246,143	**144,854,854**	**683,100,997**

TRANSLATION NOTE: This is a translation of the original document issued in the Serbian language. All due care has been taken to produce a translation that is as faithful as possible to the original. However, if any questions arise related to interpretation of the information contained in the translation, the Serbian version of the document shall prevail.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

In RSD thousand

	Balance sheet assets to be exposed to credit risk*	Off-balance sheet items to be exposed to credit risk**	Total 2018
Industry	**209,202,832**	**114,690,794**	**323,893,626,**
Trade	46,426,279	25,312,191	71,738,470
Transportation and communication	9,181,529	3,968,616	13,150,145
Construction	18,541,503	23,836,616	42,378,119
Services, tourism and accommodation services	3,005,315	4,128,815	7,134,130
Food and beverage production	20,904,603	5,458,826	26,363,429
Permanent goods production	14,559,701	11,917,375	26,477,076
Agriculture, hunting, fishing and forestry	12,965,396	7,288,103	20,253,499
Other	83,618,506	32,780,252	116,398,758
Banks	**112,981,815**	**374,640**	**113,356,455**
Local government	**5,861,184**	**87,864**	**5,949,048**
Retail loans	**151,964,151**	**25,320,503**	**177,284,654**
Mortgage loans	67,789,954	0	67,789,954
Other	84,174,197	25,320,503	109,494,700
	480,009,982	**140,473,801**	**620,483,783**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(b) Portfolio quality (Continued)

Ageing analysis of unimpaired loans and receivables from customers

The ageing analysis of loans and receivables from customers past due, but not impaired, as well as loans and receivables not yet due and impaired receivables, as of 31 December 2019 and 2018 is presented as follows:

In RSD thousand

	Loans to customers and banks			Total 2019*
	Stage 1	*Stage 2*	*Stage 3*	
Receivables undue:	**472,966,846**	**34,030,215**	**2,379,321**	**509,376,382**
Receivables overdue:	**12,675,709**	**5,838,468**	**10,355,584**	**28,869,761**
01-30 days	12,675,709	3,838,805	140,045	16,654,559
31-60 days	-	1,298,794	125,420	1,424,214
61-90 days	-	700,869	175,545	876,414
>90 days	-	-	9,914,574	9,914,574
Total	**485,642,555**	**39,868,683**	**12,734,905**	**538,246,143**

***We apply the new definition of default applied in 2019. (detailed explanation in item 28.1)**

In RSD thousand

	Loans to customers and banks			Total 2018
	Stage 1	*Stage 2*	*Stage 3*	
Receivables undue:	**431,294,299**	**21,356,273**	**2,908,044**	**455,558,616**
Receivables overdue:	**4,688,416**	**2,144,040**	**17,618,910**	**24,451,366**
01-30 days	4,688,416	1,343,397	380,483	6,412,296
31-60 days	-	553,964	262,436	816,400
61-90 days	-	246,679	315,593	562,272
>90 days	-	-	16,660,398	16,660,398
Total	**435,982,715**	**23,500,312**	**20,526,954**	**480,009,982**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(b) Portfolio Quality (Continued)

Collateral analysis

Analysis of portfolio (balance sheet and off-balance sheet items), by the collateral type, as of 31 December 2019 and 2018 is presented below:

In RSD thousand

	Balance sheet assets to be exposed to credit risk*	`Off-balance sheet items to be exposed to credit risk**	Total 2019
Corporate loans:	**216,825,030**	**117,434,180**	**334,259,210**
Guaranteed by government	2,353,257	-	2,353,257
Secured by mortgage	22,460,975	3,237,767	25,698,742
Secured by deposit	2,278,023	672,616	2,950,639
Unsecured	189,732,775	113,523,798	303,256,572
Loans to banks:	**142,575,614**	**1,051,017**	**143,626,631**
Unsecured	142,575,614	1,051,017	143,626,631
Loans to local government:	**9,150,046**	**123,543**	**9,273,589**
Secured	59,304	-	59,304
Unsecured	9,090,741	123,543	9,214,284
Retail loans:	**169,695,454**	**26,246,115**	**195,941,568**
Secured by residential mortgage	71,034,220	-	71,034,220
Secured by non-residential mortgage	869,536	-	869,536
Secured by deposit	250,056	-	250,056
Unsecured	97,541,642	26,246,115	123,787,757
Total	**538,246,143**	**144,854,854**	**683,100,997**

In RSD thousand

	Balance sheet assets to be exposed to credit risk*	`Off-balance sheet items to be exposed to credit risk**	Total 2018
Corporate loans:	**209,202,832**	**114,690,793**	**323,893,625**
Guaranteed by government	3,878,400	1,026,260	4,904,660
Secured by mortgage	34,634,348	5,738,952	40,373,300
Secured by deposit	1,736,788	511,045	2,247,834
Unsecured	168,953,296	107,414,536	276,367,832
Loans to banks:	**112,981,815**	**374,640**	**113,356,455**
Unsecured	**112,981,815**	374,640	**113,356,455**
Loans to local government:	**5,861,184**	**87,864**	**5,949,048**
Secured	137,076	-	137,076
Unsecured	5,724,108	87,864	5,811,972
Retail loans:	**151,964,151**	**25,320,503**	**177,284,654**
Secured by residential mortgage	55,757,576	-	55,757,576
Secured by non-residential mortgage	2,535,060	-	2,535,060
Secured by deposit	395,602	-	395,602
Unsecured	93,275,913	25,320,503	118,596,416
Total	**480,099,982**	**140,473,801**	**620,483,783**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(b) Portfolio quality (Continued)

Collateral analysis (Continued)

All collaterals are presented up to the amount of receivables. Mortgage must meet the requirements of the National Bank of Serbia in order to be used as a collateral and those requirements are: to be registered, there must be an appraisal for the mortgaged property by the authorized appraiser not older than 3 years (except in the case of mortgaged residential real estate property where the amount of the outstanding bank exposure does not exceed 40% of its value), owner of the property cannot be under bankruptcy, appraised value of property reduced by all higher ranked receivables must be greater than the amount of receivables, receivables secured by the mortgage cannot be overdue for more than 720 days.
Loan to value ratio (LTV ratio) for mortgage loans as of 31 December 2019 and 2018 is as follows:

In RSD thousand

Mortgage LTV	2019.	Mortgage LTV	2018
< 50%	20,732,294	< 50%	16,345,916
51%-70%	27,851,754	51%-70%	21,796,133
71%-90%	27,260,909	71%-90%	23,004,366
91%-100%	1,506,657	91%-100%	1,829,340
> 100%	1,506,657	> 100%	4,814,199
Total	**79,692,978**	**Total**	**67,789,954**

Non-performing loan analysis

Balance sheet assets and allowances for impairment (NPL – categories: past due, unlikely to pay, doubtful and restructured) as of 31 December 2019 and 2018 are presented as follows:

In RSD thousand

	Balance sheet assets to be classified		**Off-balance sheet items to be classified**		**Total 2019**
Renegotiated loans:	***Loans to customers***	***Loans to banks***	***Loans to customers***	***Loans to banks***	***Net Balance sheet assets to be classified***
Loans	6,426,613	-	4,037,488	-	2,389,125
Allowances for impairment	6,308,292	-	3,807,609	-	2,500,684
Total	**12,734,906**	**-**	**7,845,097**	**-**	**4,889,809**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(b) Portfolio quality (Continued)

Collateral analysis (Continued)

	Balance sheet assets to be classified		Off-balance sheet items to be classified		In RSD thousand Total 2018
Renegotiated loans:	***Loans to customers***	***Loans to banks***	***Loans to customers***	***Loans to banks***	***Net Balance sheet assets to be classified***
Loans	15,888,042	-	8,971,782	-	6,916,260
Allowances for impairment	6,153,201	59	3,757,854	19	2,395,388
Total	**22,041,243**	**59**	**12,729,636**	**19**	**9,311,647**

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(b) Portfolio quality (Continued)

Renegotiated loans analysis

Balance sheet assets and allowances for impairment for renegotiated loans as of 31 December 2019 and 2018 are presented as follows:

In RSD thousand

	Balance sheet assets to be classified		Off-balance sheet items to be classified		Total 2019
	Loans to customers	*Loans to banks*	*Loans to customers*	*Loans to banks*	*Loans to customers and banks*
Renegotiated loans:					
Loans	3,710,107	-	-	-	3,710,107
Allowances for impairment	(1,415,547)	-	-	-	(1,415,547)
Total	**2,294,560**	**-**	**-**	**-**	**2,294,560**

In RSD thousand

	Balance sheet assets to be classified		Off-balance sheet items to be classified		Total 2018
	Loans to customers	*Loans to banks*	*Loans to customers*	*Loans to banks*	*Loans to customers and banks*
Renegotiated loans:					
Loans	11,596,967	-	63	-	11,597,030
Allowances for impairment	(5,536,334)	-	(1)	-	(5,536,335)
Total	**6,060,633**	**-**	**62**	**-**	**6,060,695**

Renegotiated loans are all loans for which previous conditions, as term, dynamics of settlement, interest rate and etc. have been changed in order to provide benefits for the client.

28. RISK MANAGEMENT (Continued)

28.1. Credit risk (Continued)

(b) Portfolio quality (Continued)

Credit conversion factor analysis

Credit conversion factors (CCF) for off-balance sheet items in the portfolio as of 31 December 2019 and 31 December 2018 are presented as follows:

In RSD thousand

	Off-balance sheet items to be classified			Total 2019.
	Corporate Loans	*Loans to Banks*	*Retail Loans*	*Loans to customers and banks*
CCF				
20%	80,624,019	745,757	-	81,369,776
27%	1,648,419	-	-	1,648,419
32%	6,347,602	-	-	6,347,602
39%	471,512	-	-	471,512
48%	1,656,804	-	18,944,202	20,601,006
50%	25,149,132	287,367	-	25,436,499
58%			7,289,489	7,289,489
100%	1,660,234	17,893	12,424	1,690,551
Ukupno	**117,557,722**	**1,051,017**	**26,246,115**	**144,854,854**

In RSD thousand

	Off-balance sheet items to be classified			Total 2018.
	Corporate Loans	*Loans to Banks*	*Retail Loans*	*Loans to customers and banks*
CCF				
20%	53,749,052	-	-	53,749,052
26%	5,418,914	-	-	5,418,914
27%	1,676,554	-	-	1,676,554
41%	511,003	-	-	511,003
47%	1,811,348	-	-	1,811,348
48%	-	-	17,998,494	17,998,494
50%	34,642,342	238,963	7,273,567	42,154,872
100%	16,969,448	135,677	48,438	17,153,563
Ukupno	**114,778,661**	**374,640**	**25,320,499**	**140,473,800**

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management

The Risk Management Department is responsible for measuring and monitoring liquidity and for the regular preparation of reports, which present the effects of the migration of various categories of assets and liabilities of the Bank to its liquid assets position. Liquidity risk management system is in compliance with measures and criteria determined by the Parent Bank, as well as regulations prescribed by the National Bank of Serbia.

In 2014, the Bank adopted and implemented requirements for monitoring and measuring liquidity risk, determined by the Parent Bank, and in that way implemented Basel III Standards on monitoring liquidity in its internal systems, i.e. implementation of EU regulations CRR/CRD IV and Delegated Act (EU) 2015/61 in 2015. These standards were implemented through the local Liquidity policy, which is completely in compliance with the Group standards and ERMASnet 5 technical solution, which provides standardized monitoring of liquidity risk on the level of ISP Group. Further, the Bank must monitor and report on liquidity indicators, which are determined by the local regulations.

Basic activities of the liquidity risk management include:

- planning of cash inflows and outflows;
- implementation and monitoring of liquidity indicators;
- measurement and monitoring of the Bank's liquidity;
- monitoring of liquidity crisis indicators; and
- preparation of the reports for the management.

Liquidity Risk management is done through monitoring following limits/indicators:

- Regulatory liquidity indicators: Liquidity coverage ratio – LCR (including LCR by significant currencies), Liquidity ratio and Narrow liquidity ratio.

Regulatory liquidity indicators

Liquidity Coverage Ratio – LCR

By applying the guidelines of the European Banking Authority (EBA) and Basel III regulations, as well as by respecting the specificities of the Serbian market and the macroeconomic environment, the National Bank of Serbia adopted a new Decision on Liquidity Risk Management by Banks at the end of 2016, introducing Liquidity Coverage Ratio (LCR) as a new regulatory liquidity indicator . The LCR indicator should provide adequate level of highly liquid assets (cash or assets which can be converted into cash with small or without any loss in value) in order to fulfil the Bank's needs for liquidity in the 30-day period of stress scenario.

The Decision on Liquidity Risk Management by Banks prescribed by National Bank of Serbia is almost fully harmonized with Basel III, i.e. the Commission Delegated Act Regulation (EU) 2015/91. However, there are some differences in the local LCR calculation that should be remarked:

- Excess liquidity on obligatory reserve account is calculated as of reporting date instead as average;
- There are no haircuts required for securities issued by the Serbian Government in local and foreign currencies;
- Higher outflow rates are applied only to retail deposits denominated in currencies other than dinar, euro and the currency of an EU member state. Namely, Euro and other EU member state currencies are treated as domestic currency in accordance with the regulation prescribed by the National Bank of Serbia;
- Shortage of required reserves is not treated as outflow; and
- Contractual inflows from exposures that are not past due for more than five days are included into the liquidity inflows (no five days threshold is applied by the EU regulations).

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

The LCR indicator required by the regulator was well above the required limit in 2019 with an average value that was more than fourth times higher than prescribed limit of 1.0 (100%).

LCR	31 December	Average	Maximum	Minimum
2019	2.39	4.52	7.00	2.39
2018	4.50	3.79	6.33	2.60

The Bank also calculates the LCR indicator by significant currencies in accordance with the Decision on Liquidity Risk Management by Banks prescribed by the National Bank of Serbia. LCR indicator is monthly reported to the ALCO board by the most significant currencies (RSD and EUR), As of 31 December 2019 LCR is 6.66 (2018: 8.40) for liquidity position in domestic currency and 0.51 (2018:1.33) for liquidity position in foreign currency (EUR).

Regulatory liquidity indicators (Continued)

Liquidity ratio and Narrow liquidity ratio

In 2019 the regulatory liquidity ratio and narrow regulatory liquidity ratio were significantly above the legally prescribed limit. Average regulatory liquidity ratio and narrow liquidity ratio were two times above the required level (at least 1.0 if calculated as the average of liquidity indicators for all working days within a month, or at least 0.7 if calculated as the average of narrow liquidity indicators for all working days within a month).

Liquidity ratio	31 December	Average	Maximum	Minimum
2019	2.25	2.22	2.59	1.81
2018	2.28	2.34	2.66	1.92

Narrow liquidity ratio	31 December	Average	Maximum	Minimum
2019	1.64	1.70	2.20	1.30
2018	1.83	1.88	2.25	1.40

Structure of the total liquidity reserves as of **31 December 2019** is presented in the following table:

			In RSD thousand
Liquidity reserves	**Carrying amount/ Fair value**	**Haircut**	**Available amount**
Required Central bank reserves in the amount above the amount required for the period	12,023,089	0%	12,023,089
- of which required reserves in local currency	12,023,089	0%	12,023,089
- of which required reserves in foreign currency	0	0%	0
Reverse repo transaction with Central Bank	31,261,100	0%	31,261,100
Cash and cash equivalents	15,965,459	0%	15,965,459
Available no-load government securities issued by the Republic of Serbia	108,243,114		58,551,143
- of which in local currency	68,886,726	50%	34,443,363
- of which in Euro	28,282,425	50%	14,141,213
- of which in Dollar	11,073,963	10%	9,966,567
Total liquidity reserves	**167,492,762**		**117,800,791**

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

Structure of the total liquidity reserves as of **31 December 2018** is presented in the following table:

In RSD thousand

Liquidity reserves	Carrying amount/ Fair value	Haircut	Available amount
Required reserves in the amount above the amount required for the period	13,560,464	0%	13,560,464
- of which required reserves in local currency	3,596,863	0%	3,596,863
- of which required reserves in foreign currency	9,963,601	0%	9,963,601
Reverse repo transaction with Central Bank	0	0%	0
Cash and cash equivalents	12,789,462	0%	12,789,462
Available no-load government securities issued by the Republic of Serbia	92,821,825		48,740,688
- of which in local currency	59,235,687	50%	29,617,844
- of which in Euro	27,761,703	50%	13,880,852
- of which in Dollar	5,824,435	10%	5,241,992
Total liquidity reserves	119,171,751		75,090,614

The liquidity reserves structure is as follows: reserves required by the central bank above the amount required for the period in domestic and foreign currency on which 0% haircut is applied, reverse repo transactions with the central bank, cash and cash equivalents (including gold) on which 0% haircut is applied, government bonds in domestic and foreign currency issued by the Republic of Serbia on which defined haircut of 10% i.e. 50% is applied.

As of 31 December 2019, available unencumbered financial assets issued by the Republic of Serbia amounted to RSD 108,243,114 thousand (2018: RSD 92,821,825 thousand), out of which RSD 68,886,726 thousand is in local currency (2018: RSD 59,235,687 thousand), RSD 28,282,425 thousand is in Euro (2018: RSD 27,761,703 thousand) and RSD 11,073,963 thousand is in USD (2018: RSD 5,824,435 thousand).

According to the Liquidity Risk Management Policy, foreign currency account balances are not a part of liquidity reserves, although they represent liquid assets that the Bank owns without restrictions.

As of 31 December 2019, on nostro accounts was RSD 5,720,666 thousand (2018: RSD 14,728,138 thousand, while the outstanding balance of foreign currency accounts with the National Bank of Serbia was RSD 2,415,587 thousand).

The currency structure of cash on nostro accounts at the reporting date was as follows: EUR – RSD 4,481,305 thousand (2018: RSD 13,295,569 thousand), USD – RSD 694,889 thousand (2018: RSD 1,022,852 thousand), GBP – RSD 87,178 thousand (2018: RSD 65,751 thousand), CAD – RSD 90,962 thousand (2018: RSD 53,235 thousand), AUD – RSD 65,757 thousand (2018: RSD 53,559 thousand), DKK – RSD 78,877 thousand (2018: RSD 59,161 thousand), CHF – RSD 154,771 thousand (2018: RSD 117,400 thousand), SEK – RSD 41,052 thousand (2018: RSD 24,480 thousand), RUB – RSD 7,356 thousand (2018: RSD 14,557 thousand) and other currencies – RSD 18,519 thousand (2018: RSD 21,575 thousand).

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

The following table presents the remaining maturity mismatch report as of **31 December 2018**:

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
ASSETS							
Cash and balances with Central Bank	97,392,634	-	-	-	-	-	97,392,634
Receivables from derivatives						61,978	61,978
Securities	63,934	10,254,461	31,631,804	66,356,849	-	612	108,307,660
Loans and receivables from banks and other financial organizations	44,876,911	1,009,974	3,576,184	1,650,919	43,305	9,264	51,166,557
Loans and receivables from customers	23,603,168	26,229,498	86,494,265	155,981,129	80,459,893	1,141,619	373,909,572
Investments in subsidiaries	-	-	-	-	-	1,199,472	1,199,472
TOTAL ASSETS	**165,936,647**	**37,493,933**	**121,702,253**	**223,988,897**	**80,503,198**	**2,412,945**	**632,037,873**

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

Maturity mismatch report as of **31 December 2019** (Continued)

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
LIABILITIES							
Liabilities based on derivatives						7,869	7,869
Deposits and other financial liabilities due to banks, other financial organizations and Central Bank	12,470,694	29,854,483	4,362,093	12,619,955	7,157,057	(116,367)	66,347,915
Deposits and other financial liabilities due to customers	378,563,613	32,662,879	46,441,619	12,591,138	959,592	1,106,054	472,324,895
TOTAL LIABILITIES	**391,034,307**	**62,517,362**	**50,803,712**	**25,211,093**	**8,116,649**	**997,556**	**538,680,679**
TOTAL EQUITY						**100,067,067**	**100,067,067**
TOTAL LIABILITIES AND EQUITY	**391,034,307**	**62,517,362**	**50,803,712**	**25,211,093**	**8,116,649**	**101,064,623**	**638,747,746**
OFF-BALANCE SHEET ITEMS	**2,373,173**	**8,035,078**	**23,578,697**	**54,370,757**	**19,759,888**	**36,737,261**	**144,854,854**
MATURITY MISMATCH	**(227,470,833)**	**(33,058,507)**	**47,319,844**	**144,407,047**	**52,626,661**		
CUMULATIVE MATURITY MISMATCH	**(227,470,833)**	**(260,529,340)**	**(213,209,496)**	**(68,802,449)**	**(16,175,788)**		

The remaining maturity mismatch report table as of 31 December 2019 presents future cash flows based on the highly conservative assumptions, which are that total a vista deposits will mature at the same time within the following month. The cumulative gap for illustrative purposes is shown by applying conservative assumptions since a vista deposits have been very stable source of funds by analyzing time series of a vista deposits during previous years.

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

Maturity mismatch report as of **31 December 2019** based on undiscounted cash flow (Continued)

	Carrying amount	Gross nominal value	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity
ASSETS								
Cash and balances with Central Bank	97,392,634	97,392,634	97,392,634					
Receivables from derivatives	61,978	61,978						61,978
Securities	108,307,660	117,180,527	1,006,476	11,633,457	33,526,252	71,013,730		612
Loans and receivables from banks and other financial organizations	51,166,557	51,292,176	44,887,673	1,030,475	3,628,474	1,690,829	45,461	9,264
Loans and receivables from customers	373,909,572	427,400,072	24,942,007	28,750,381	95,956,929	180,725,479	95,883,657	1,141,619
Investments in subsidiaries	1,199,472	1,199,472						1,199,472
TOTAL ASSETS	**632,037,873**	**694,526,859**	**168,228,790**	**41,414,313**	**133,111,655**	**253,430,038**	**95,929,118**	**2,412,945**

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

In RSD thousand

	Carrying amount	Gross nominal value	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity
LIABILITIES								
Liabilities based on derivatives	7,869	7,869						7869
Deposits and other financial liabilities due to banks, other financial organizations and Central Bank	66,347,915	67,558,748	12,484,192	29,933,392	4,592,720	13,191,578	7,473,233	(116,367)
Deposits and other financial liabilities due to customers	472,324,895	475,028,981	378,694,272	33,350,699	46,902,387	13,454,333	1,521,236	1,106,054
TOTAL LIABILITIES	**538,680,679**	**542,595,598**	**391,178,464**	**63,284,091**	**51,495,107**	**26,645,911**	**8,994,469**	**997,556**

The following table presents the remaining maturity mismatch report as of **31 December 2018**:

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over5 years	With non-defined maturity	Total
ASSETS							
Cash and balances with central bank	86,948,959					13,648	86,962,607
Receivables from derivatives						331,839	331,839
Securities	8,043,734	32,073,071	10,900,309	41,854,749		622	92,872,485
Loans and receivables from banks and other financial organizations	28,437,909	629,272	1,666,365	2,065,475	224,831	15,412	33,039,264
Loans and receivables from customers	13,691,369	25,461,799	81,530,888	141,254,057	61,951,346	15,859,655	339,749,114
Investments in subsidiaries						1,199,472	1,199,472
Total assets	**137,121,971**	**58,164,142**	**94,097,562**	**185,174,281**	**62,176,177**	**17,420,648**	**554,154,781**

28. RISK MANAGEMENT (Continued)

28.2. Liquidity risk and financial assets management (Continued)

Maturity mismatch report as of 31 December 2018 (Continued)

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
LIABILITIES							
Liabilities based on derivatives						21,497	21,497
Deposits and other liabilities due to banks, other financial organizations and central bank	3,789,517	18,084,914	4,872,970	12,447,380	8,143,384	1,693,086	49,031,251
Deposits and other liabilities due to customers	326,041,371	14,037,054	50,881,554	11,136,327	834,629	2,244,282	405,175,217
TOTAL LIABILITIES	**329,830,888**	**32,121,968**	**55,754,524**	**23,583,707**	**8,978,013**	**3,958,865**	**454,227,965**
TOTAL EQUITY						**106,601,186**	**106,601,186**
TOTAL LIABILITIES AND EQUITY	**329,830,888**	**32,121,968**	**55,754,524**	**23,583,707**	**8,978,013**	**110,560,051**	**560,829,151**
OFF-BALANCE SHEET ITEMS			**13,388,323**			**127,085,478**	**140,473,801**
MATURITY MISMATCH	**(192,708,917)**	**26,042,174**	**24,954,715**	**161,590,574**	**53,198,164**		
CUMULATIVE MATURITY MISMATCH	**(192,708,917)**	**(166,666,743)**	**(141,712,028)**	**19,878,546**	**73,076,710**		

The table on the analysis of the residual maturity of assets and liabilities of the Bank as at 31 December 2018 shows the future cash flows using extremely conservative assumptions, such as the maturity of all sight deposits in the next month. The cumulative gap for illustrative purposes is shown by applying conservative assumptions since a vista deposits have been very stable source of funds by analyzing time series of a vista deposits during previous years.

28. RISK MANAGEMENT (Continued)

28.3. Market risk

In 2019, the Bank acquired Trading Book (positions) and, therefore, was exposed to interest rate risk and price risk which could be caused by the Trading Book. Trading Book refers to portfolio of securities consisted of bonds and derivatives. In accordance with the Trading Book Policy, or the Group Guidelines and a document issued by the Basel Committee on Banking Supervision, the „Fundamental Review of the Trading Book", during 2018 portfolio of derivatives has been transferred from the Banking Book to the Trading Book, as derivatives held by the Bank are not instruments used for hedge accounting. During 2019 there was no registered breach of the limit defining the maximum allowed nominal value of bonds in the Trading Book. On the other hand, the Banking book was exposed to foreign currency risk, with registered limit breaches approved by two members of the Executive Board in 2019.

Foreign currency risk is the risk of occurrence of negative effects on the financial result and equity of the Bank due to changes in foreign currency exchange rates. Banking operations in different foreign currencies result in exposure to fluctuations in exchange rates of foreign currencies.

The Bank applies foreign currency risk monitoring system based on the first and the second class limits.

The first class limit is considered to be FX VaR limit, which is calculated and reported on a daily basis. Calculation methodology is regulated by the ISP Group, which applies EWMA historical method, with 99% confidence interval and one day time period. FX VaR is calculated on positions for each currency, due to the Parent Bank's requirements, as well as for the increase of volatility of some currencies, which the Bank has in its portfolio. However, the FX VaR is mostly determined by the volatility of EUR, since the portion of EUR of the total open FX position was 85% in average during 2019.

The second class limit is considered to be the limit of net open FX position, which represents difference between the currency sensitive assets and the currency sensitive liabilities. The second class limits exposure is calculated and reported on a daily basis. During 2019, the first class limit (FX VaR limit) and the second class limit (limit of net open FX position), remained unchanged. During 2019 breaches of the second class limits were registered (primarily due to the dividend payments in March and October), as the result of previously announced and agreed business actions which require that the open foreign currency position is not closed directly, but within few days.

During 2019, the Bank's foreign currency risk indicator was in compliance with the legally prescribed one, which represents 20% of the regulatory equity. As of 31 December 2019 regulatory indicator of foreign currency risk was 0.36%. Considering that the regulatory indicator for foreign exchange risk is below 2%, the Bank has not calculated capital requirement as of 31.12.2019.

28. RISK MANAGEMENT (Continued)

28.3. Market risk (Continued)

The following table presents the open foreign currency position as of **31 December 2019**:

In RSD thousand

		Open foreign currency position		
	Carrying amount	**Total**	**Trading book**	**Banking book**
Assets complied with market risks	**635,345,174**	**386,333,854**	**59,387**	**386,274,467**
Cash and balances with Central Bank	97,392,634	37,747,780		37,747,780
Securities	108,307,660	39,405,394	59,387	39,346,007
Loans and receivables from banks and other financial organizations	51,166,557	18,171,385		18,171,385
Loans and receivables from customers	373,909,572	290,221,105		290,221,105
Other assets	4,568,751	788,190		788,190
Liabilities complied with market risks	**551,110,476**	**358,416,227**		**358,416,227**
Deposits and other financial liabilities due to banks, other financial organizations and Central Bank	66,347,915	109,410,243		109,410,243
Deposits and other financial liabilities due to customers	472,324,895	244,565,280		244,565,280
Other liabilities	12,437,666	4,440,704		4,440,704
Off-balance sheet financial derivatives which impact FX position	(19,680,424)	(19,680,424)	(19,680,424)	
Allowances for impairment	(13,345,319)	(7,939,304)		(7,939,304)
Open net foreign currency position		**297,899**	**(19,621,037)**	**19,918,936**

The following table presents the open foreign currency position as of **31 December 2018**:

In RSD thousand

		Open foreign currency position		
	Carrying amount	**Total**	**Trading book**	**Banking book**
Assets complied with market risks	**556,939,093**	**369,018,505**	**377,599**	**368,640,906**
Cash and balances with central bank	86,962,607	48,001,330		48,001,330
Securities	92,872,485	33,619,690	377,599	33,242,091
Loans and receivables from banks and other financial organizations	33,039,264	32,074,717		32,074,717
Loans and receivables from customers	339,749,114	254,938,424		254,938,424
Other assets	4,315,623	384,344		384,344
Liabilities complied with market risks	**462,523,576**	**322,068,932**		**322,068,932**
Deposits and other liabilities due to banks, other financial organizations and central bank	49,031,251	47,466,754		47,466,754
Deposits and other liabilities due to customers	405,175,217	272,895,524		272,895,524
Other liabilities	8,317,108	1,706,654		1,706,654
Off-balance sheet financial derivatives which impact FX position	(36,070,984)	(36,070,984)	(36,070,984)	
Allowances for impairment	(18,082,825)	(8,755,686)		(8,755,686)
Open net foreign currency position		**2,122,903**	**(35,693,385)**	**37,816,288**

28. RISK MANAGEMENT (Continued)

28.3. Market risk (Continued)

Following table represents the currency structure of open net foreign currency position as of 31 December 2019 and 31 December 2018:

In RSD thousand

Net open foreign currency position	2019	2018
EUR	119,620	1,974,276
USD	32,090	37,978
CHF	8,397	(5,459)
Other currencies	67,828	58,090
Gold and other precious metals	69,963	58,018
Total	**297,898**	**2,122,903**

In EUR

Foreign currency VaR	31 December	Average	Maximum	Minimum
2019	4,450	9,027	79,089	891
2018	29,637	15,546	224,607	846

Following table represents effect of the change in the exchange rates on the Bank’s profit and regulatory capital:

In RSD thousand

Scenario	Effect 2019	Effect 2018
10% depreciation of RSD	29,790	212,290
20% depreciation of RSD	59,580	424,581

28.4. Interest rate risk

Interest rate risk is the risk of decrease in profit or net assets value of the Bank due to changes in market interest rates. The Bank’s exposure to interest rate risk depends on the ratio of the interest-sensitive assets and interest-sensitive liabilities.

Interest rate risk is calculated separately for the Banking Book (HTCS -portfolio of securities hold to collect and sell) and for the Trading Book (HFT -portfolio of securities held for trading, consisted of bonds and derivatives), respectively Banking Book (includes everything that is not classified as Trading Book).

ISP Group Methodology on the calculation of interest rate risk was changed at the beginning of 2014 and adopted by the Bank, through internal documents and ERMAS net 5 technical solution. Changes in the methodology included: treatment of the margin as fixed future cash flow; calculation of future cash flows by using FTP prices, instead of the contractual prices; modelling a vista deposits and discounting future cash flows by applying yield curves, modified by the expected loss. Applying the guidelines of the European Bank Authority (EBA) and Basel III regulations, the Parent Bank continuously improves the methodology and Guidelines relating to interest rate risk. In accordance with the EBA guidelines and the Parent Bank guidelines, in 2019 new methodologies were applied in the calculation of interest rate risk, such as currency aggregation, inclusion of non-performing loans in exposure and implementation of the prepayment model, The Bank's documents defining interest rate risk management, the Policy on management of interest rate risk in the Banking Book and the Rulebook - Measurement and control of interest rate risk in the Banking Book, were harmonized with the Parent Bank’ documents.

28. RISK MANAGEMENT (Continued)

28.4. Interest rate risk (Continued)

Measures used for assessment of interest rate risk on the Banking Book and on the basis of which there are established limits that are monitored on a monthly level are sensitivity of economic value of assets on 100 basis points interest rate change and sensitivity of income revenues and costs on change of on 50 basis points interest rate change. The Bank was in compliance with the prescribed limits by the Parent Bank in 2019.
Sensitivity of net asset value to change in market interest rates of +/- 100 basis points and, +/- 200 basis points, i.e. sensitivity of interest income and expenses to change of +/- 50, +/- 100 and, + / -200 basis is calculated, monitored and submitted to the ALCO Board as well as to the Parent Bank on a monthly basis. At the quarterly level, the Bank calculates these indicators in accordance with the six defined scenarios required by Basel III regulations, which are monitored and submitted to the ALCO Board and the Parent Bank.

During 2019 the interest rate risk VaR limit exposure on the Banking Book, was decreased on the Parent Bank's request while the interest rate VaR limit on the Trading Book has been increased due to the transfer of derivatives from Banking Book to Trading Book.

Interest rate risk is daily monitored and submitted for the financial assets hold to collect and sell (HTCS)as well as for portfolio of securities held for trading (HFT). For (HTCS), as well as for HFT porfolio the following ratios of interest rate risk are calculated and reported on a daily basis: IRR VaR, duration and stress test (change scenario by 100 bps and 200 bps).

Acceptable interest rate risk is limited to the highest possible value at interest rate risk (IRR VaR) for the portfolio of financial assets hold to collect and sell, as well as for the portfolio of securities held for trading.

Value at interest rate risk (IRR VaR) is considered to be the highest possible one day loss in the AFS securities portfolio and securities held for trading that the Bank could undertake under usual market movements in interest rates. IRR VaR calculation methodology is determined by the ISP Group regulations, which applies EWMA historical method with 99% confidence interval and one day time period. During 2019 there was no registered breach of the VaR limits referring to neither HTCS nor HFT portfolio.

28. RISK MANAGEMENT (continued)

28.4. Interest rate risk (continued)

The following table represents Reprising Gap report, i.e. the Bank's exposure to interest rate risk as of **31 December 2019**:

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
ASSETS							
Cash and balances with Central Bank	97,392,634						97,392,634
Receivables from derivatives						61,978	61,978
Securities	63,934	10,254,461	31,631,804	66,356,849		612	108,307,660
Loans and receivables from banks and other financial organizations	47,071,580	647,114	2,655,943	781,585	1,071	9,264	51,166,557
Loans and receivables from customers	159,752,861	49,120,501	77,786,381	78,591,787	7,516,423	1,141,619	373,909,572
Investments in subsidiaries						1,199,472	1,199,472
TOTAL ASSETS	**304,281,009**	**60,022,076**	**112,074,128**	**145,730,221**	**7,517,494**	**2,412,945**	**632,037,873**

28. RISK MANAGEMENT (Continued)

28.4. Interest rate risk (Continued)

Reprising Gap report, i.e. the Bank's exposure to interest rate risk as of **31 December 2019 (Continued)**

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
LIABILITIES							
Liabilities based on derivatives						7,869	7,869
Deposits and other financial liabilities due to banks, other financial organizations and Central Bank	12,608,435	33,446,419	5,858,588	8,876,779	5,674,061	(116,367)	66,347,915
Deposits and other financial liabilities due to customers	379,793,807	32,662,769	45,791,767	12,099,906	870,592	1,106,054	472,324,895
TOTAL LIABILITIES	**392,402,242**	**66,109,188**	**51,650,355**	**20,976,685**	**6,544,653**	**997,556**	**538,680,679**
TOTAL EQUITY						**100,067,067**	**100,067,067**
TOTAL LIABILITIES AND EQUITY	**392,402,242**	**66,109,188**	**51,650,355**	**20,976,685**	**6,544,653**	**101,064,623**	**638,747,746**
MATURITY MISMATCH	**(88,121,233)**	**(6,087,112)**	**60,423,773**	**124,753,536**	**972,841**		
CUMULATIVE MATURITY MISMATCH	**(88,121,233)**	**(94,208,345)**	**(33,784,572)**	**90,968,964**	**91,941,805**		

28. RISK MANAGEMENT (Continued)

28.4. Interest rate risk (Continued)

The following table represents Reprising Gap report, i.e. the Bank's exposure to interest rate risk as of **31 December 2018**:

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
ASSETS							
Cash and balances with central bank	86,948,959					13,648	86,962,607
Pledged financial assets - Assets encumbrance							
Receivables from derivatives						331,839	331,839
Securities	8,043,734	32,073,071	10,900,309	41,854,749		622	92,872,485
Loans and receivables from banks a and other financial organizations	31,123,806	540,927	1,172,944	186,175		15,412	33,039,264
Loans and receivables from customers	106,035,333	67,699,259	75,929,799	67,686,684	6,538,384	15,859,655	339,749,114
Investments in subsidiaries						1,199,472	1,199,472
Total assets	**232,151,832**	**100,313,257**	**88,003,052**	**109,727,608**	**6,538,384**	**17,420,648**	**554,154,781**

28. RISK MANAGEMENT (Continued)

28.4. Interest rate risk (Continued)

Reprising Gap report, i.e. the Bank's exposure to interest rate risk as of **31 December 2018 (Continued)**

In RSD thousand

	Up to 1 month	From 1 to 3 months	From 3 months to 1 year	From 1 to 5 years	Over 5 years	With non-defined maturity	Total
LIABILITIES							
Liabilities based on derivatives						21,497	21,497
Deposits and other liabilities due to banks, other financial organizations and central bank	3,799,517	22,986,246	3,821,241	9,828,821	6,902,340	1,693,086	49,031,251
Deposits and other liabilities due to customers	327,766,738	14,278,674	49,879,688	10,311,565	694,270	2,244,282	405,175,217
TOTAL LIABILITIES	**331,566,255**	**37,264,920**	**53,700,929**	**20,140,386**	**7,596,610**	**3,958,865**	**454,227,965**
TOTAL EQUITY						**106,601,186**	**106,601,186**
TOTAL LIABILITIES AND EQUITY	**331,566,255**	**37,264,920**	**53,700,929**	**20,140,386**	**7,596,610**	**110,560,051**	**560,829,151**
MATURITY MISMATCH	**(99,414,423)**	**63,048,337**	**34,302,123**	**89,587,222**	**(1,058,226)**		
CUMULATIVE MATURITY MISMATCH	**(99,414,423)**	**(36,366,086)**	**(2,063,963)**	**87,523,259**	**86,465,033**		

28. RISK MANAGEMENT (continued)

28.4. Interest rate risk (continued)

The table below presents the effects of change in interest rates on the Bank's net income and net assets, valued by applying the standard scenario and not taking into account assumptions on asymmetrical changes of the yield curve. The standard scenario implies parallel movement of the yield curve by 100bps and 200 bps on the Bank's net asset sensitivity and 50bps on net income sensitivity.

In RSD thousand

Sensitivity of the Bank's net assets on the change in interest rates	Increase by 100bps	Decrease by 100bps	Increase by 200bps	Decrease by 200bp
2019				
As of 31 December	(749,722)	1,026,448	(1,451,784)	2,511,829
Period average	(909,360)	1,172,009	(1,758,945)	2,601,527
Period maximum	(1,063,661)	1,453,890	(2,056,469)	3,109,783
Period minimum	(441,761)	456,288	(839,203)	911,296
2018				
As of 31 December	(367,607)	363,459	(697,511)	654,809
Period average	(579,629)	600,492	(1,114,254)	1,208,583
Period maximum	(961,003)	1,021,694	(1,851,320)	2,196,250
Period minimum	(270,014)	261,266	(504,757)	448,935

In RSD thousand

Sensitivity of the Bank's net income on the change in interest rates	Increase by 50bps	Decrease by 50bp
2019		
As of 31 December	722,879	(788,679)
Period average	662,855	(707,822)
Period maximum	722,879	(795,584)
Period minimum	563,401	(607,500)
2018		
As of 31 December	703,798	(729,319)
Period average	637,025	(639,733)
Period maximum	727,793	(729,319)
Period minimum	541,441	(541,900)

The following table represents value at risk for portfolio of *financial assets hold to collect and sell (HTCS)*:

In EUR

IRR AFS VaR	31 December	Average	Maximum	Minimum
2019	228,281	307,238	418,440	228,281
2018	276,810	383,230	497,569	276,810

The following table represents value at risk for *financial assets held for trading* portfolio:

In EUR

IRR HFT VaR	31 December	Average	Maximum	Minimum
2019	6,832	11,302	46,456	4,093
2018	7,736	16,283	26,626	1,269

28. RISK MANAGEMENT (Continued)

28.5. Operational risk

Operational risk is the risk of possible adverse effects on financial result and capital of the Bank caused by omissions (unintentional and intentional) in the employees' work, inadequate internal procedures and processes, inadequate management of information and other systems, as well as by unforeseeable external events. Operational risk shall also include legal risk.

The Bank's goal is to manage operational risk, in order to achieve balance between preventing financial loss and damage to the Bank's reputation, on one side, and economic profitability and innovation, on the other. The Bank's policy requires respecting all currently valid regulations.

The Bank has developed and implemented specific standards of operational risk management in the following areas:

- Operational risk identification, which comprises:
  - Collecting data on operational risks and losses – identification, registration and classification of data on the Bank's losses,
  - Integrated process of assessment of the Bank's exposure to operational risk;
  - Assessment of operational risk when implementing new product, process or system;
- Operational risk measuring;
- Monitoring and reporting on operational risk; and
- Mitigating operational risk.

At least once a year, Bank's Internal Audit performs independent assessment of adequacy of the operational risk management system. The results of this assessment are disclosed within the Audit Report, which includes all the findings and improvement suggestions.

For the purposes of capital requirements for operational risk calculation, the Bank applies the standardized approach. The capital requirement for operational risk, calculated by applying the standardized approach, amounts to RSD 4,344,143 thousand as of 31 December 2019 (31 December 2018: RSD 4,303,257 thousand).

28.6. Exposure risk

The Risk Management Department monitors, measures and reports to the competent boards of the Bank on the Bank's exposure to a single client or to a group of related clients, risk of investment in other legal entities and in fixed assets, country risk to which the Bank is exposed, as well as operational risk. In 2019, the Bank maintained compliance of the exposure risk and investment risk indicators and performed appropriate activities defined by relevant procedures and decisions on credit approval and investments in financial and non-financial assets, ensuring compliance of the Bank's placements and investments with indicators prescribed by the National Bank of Serbia as well as the investment limits prescribed by the Bank.

Exposure risks include the risk of the Bank's exposure to a single client or a group of related clients, as well as exposure risk toward related parties of the Bank.

In accordance with the Risk Management Policy, the Bank's management sets exposure limits, i.e. the concentration of placements to a single client or a group of related clients, and related parties of the Bank.

The Bank's management and relevant bodies and employees seek to ensure the compliance of the Bank's exposures with prescribed limits, i.e. exposure to a single client or a group of related clients does not exceed 25% of the Bank's equity, total amount of all large exposures does not exceed 400% of the Bank's equity.

28.7. Investment risks

Investment risks include the risk of investment in other legal entities and investment in fixed assets. In accordance with the National Bank of Serbia's regulations, the Risk Management Department monitors the Bank's investments and reports to the Executive Board. The Department also ensures that the Bank's investment in a single non-financial entity does not exceed 10% of the Bank's equity, and that the total investments of the Bank in non-financial entities and in fixed assets do not exceed 60% of the Bank's equity.

28. RISK MANAGEMENT (Continued)

28.8. Country risk

Country risk relates to the country of origin of the Bank's client and includes negative effects which may influence financial result and equity of the Bank, as the Bank might not be able to collect receivables from such a client, as a result of political, economic or social conditions in the client's country of origin. The Bank's exposure to country risk is low, due to insignificant share of non-residents in the total loan portfolio of the Bank.

28.9. Capital management

The objective of the Bank's capital management is to maintain the Bank's ability to continue operating into the foreseeable future, in order to maintain the optimal structure of capital with a view to decreasing the costs of capital and securing dividends for shareholders.

The Bank permanently manages its capital in order to:
- Ensure compliance with capital requirements set by the National Bank of Serbia;
- Ensure adequate level of capital in order to ensure operations as a going concern;
- Maintain capital at the level that will ensure future development of the business; and
- Maintain capital at the level that is adequate to cover internally assessed capital requirements for all significant risks identified in the Internal Capital Adequacy Assessment Process (ICAAP)

Capital adequacy, as well as use of the Bank's capital, is monitored on a monthly basis by the Bank's management. The Bank is obliged to calculate the following ratios and at any moment keeps them at levels that are not lower than prescribed:
- ratio of the adequacy of the basic share capital of the bank, which represents the percentage ratio of the basic share capital and risky assets of the bank - 4.5%;
- an indicator of the basic capital adequacy of the bank, which represents a percentage ratio of the basic capital and risky assets of the bank - 6%;
- Indicator of the adequacy of (total) capital of the bank, which represents the percentage ratio of capital and risky assets of the bank - 8%.

28. RISK MANAGEMENT (Continued)

28.9. Capital management (Continued)

The Bank's regulatory capital according to the Decision on Capital Adequacy of Banks as of 2019:

ITEM	**In RSD thousand 31 December 2019**
CAPITAL	**81,696,226**
Core capital	**81,696,226**
Common Equity Tier 1 capital	**81,696,226**
Common Equity Tier 1 capital instruments and the relevant issue premium	**41,748,469**
Paid amount of Common Equity Tier 1 capital instruments	21,315,900
Relevant issue premium with Common Equity Tier 1 capital instruments	20,432,569
Note: Retained earnings from preceding years which do not qualify for inclusion in Common Equity Tier 1 capital	2,292
Note: Profit of the current period which does not qualify for inclusion in Common Equity Tier 1 capital	12,331,751
Revaluation reserves and other unrealised gains/losses	**2,497,944**
Revaluation reserves and other unrealised gains/losses	2,500,990
(-) Unrealised losses	(3,045)
Reserves from profit, other reserves and reserves for general banking risks	**43,488,903**
Other reserves	43,488,903
(+/-) Regulatory adjustment of the value of Common Equity Tier 1 capital elements	**(108,297)**
(-) Additional value adjustments	(108,297)
(-) Other intangible investment reduced by associated deferred tax liabilities	**(5,348,965)**
(-) Other intangible investment before the reduction by associated deferred tax liabilities	(5,348,965)
(-) Any tax charge relating to Common Equity Tier 1 elements foreseeable at the moment of its calculation, except where the bank suitably adjusts the amount of Common Equity Tier 1 elements	**(284,437)**
(-) Gross amount of receivables from the borrower – natural person (other than a farmer or an entrepreneur) arising from extended consumer, cash or other loans where the level of the borrower's debt-to-income ratio before loan approval was higher than the percentage defined in accordance with the decision governing the classification of bank balance sheet assets and off-balance sheet items or where this percentage will be higher due to loan approval.	**(250,665)**
(-) Gross amount of receivables from the borrower – natural person (other than a farmer or an entrepreneur) arising from extended consumer, cash or other loans, other than the loans disclosed under this position which under the criterion agreed maturity qualify for the deduction from Common Equity Tier 1 prescribed by the decision governing bank capital adequacy*	**(46,725)**

28. RISK MANAGEMENT (Continued)

28.9. Capital management (Continued)

Item	In RSD thousand 31 December 2018
CAPITAL	**71,923,543**
TIER 1 CAPITAL	**71,923,543**
Common equity Tier 1 (CET) capital	**71,923,543**
Share premium	**41,748,469**
Capital instruments eligible as CET 1 capital and share premium	21,315,900
Share premium with CET 1 capital instruments	20,432,569
Profit	
Note: Retained earnings not eligible for inclusion in CET 1 capital	3,476,594
Note: Current period profit not eligible for inclusion in CET 1 capital	12,604,110
Revaluation reserves and other unrealized gains/losses	**1,287,891**
Revaluation reserves and other unrealized gains	1,393,230
(-) Unrealized losses	(105,339)
Reserves from profit, other reserves and reserves for general banking risks	**47,484,121**
Other reserves	47,484,121
(+/-) Adjustments to CET 1 due to prudential filters	**(93,132)**
(-) Additional value adjustments	(93,132)
(-) Other intangible assets before reduction for deferred tax liabilities	**(3,774,866)**
(-) Amount of taxes associated with CET 1 capital items which can be predicted at the time of capital calculation, unless the bank previously adjusted the amount of CET 1 capital items in the amount in which such taxes lower the amount up to which CET 1 capital items can be used to cover risks or losses	**(102,797)**
(-) Amount of required reserve for estimated losses on balance sheet assets and off-balance sheet items deducted from CET 1 capital	**(14,626,143)**

28.10. Fair value of financial assets and liabilities

The Bank's policy is to disclose information on the fair value of assets and liabilities, for which official market information is available and when their fair value significantly differs from their carrying amounts.

Determining fair value of the financial instruments, which are not carried at amortized cost must follow the principles, criteria and hierarchy prescribed by the Fair value policy, which is in accordance with ISP Group's requirements for determining fair value. Determining fair value of the financial instruments not carried at amortized cost respects the following hierarchy, which reflects credibility of the inputs used in determination of fair value:

- Level 1: inputs are the quoted market prices (without corrections) on active markets;
- Level 2: inputs other than quoted prices from level 1, but directly or indirectly (derived from prices) quoted on market. This category includes: market interest rates, CDS (credit default swap) market quotations, market prices of primary bonds issue or market exchange rates when determining value of the instrument.
- Level 3: inputs that are not information available on the market. This category includes each instrument, for which information on value is not directly or indirectly available on the market.

Implementation of the hierarchy is not optional, and the Bank cannot choose the information for determining fair value of financial instruments that are not carried at amortized cost, but it must respect the abovementioned hierarchy.

During 2019 there were no transition between levels during the year.

28. RISK MANAGEMENT (Continued)

28.10. Fair value of financial assets and liabilities (Continued)

Implementation of the hierarchy is not optional, and the Bank cannot choose the information for determining fair value of financial instruments that are not carried at amortized cost, but it must respect the abovementioned hierarchy.

Financial instruments not carried at amortized cost and on which Fair Value Policy is applied are:

- Securities (government FX bonds, government bonds issued by foreign governments etc. for which active and liquid market exists, which provides direct information about quoted market prices (Level 1);
- The Republic of Serbia treasury bonds, which are valued by discounting future cash flows by applying market non-risk yield curves, adjusted for country risk (at euro bonds) and liquidity risk (at RSD bonds, without direct quotation of maturity) (Level 2);
- Over-the-counter financial derivatives (FX swap and FX forward) which are valued by discounting future cash flows with market non-risk yield curves adjusted for country risk and (at Euro bonds) and liquidity risk (at RSD bonds without direct quotation of maturity) (Level 2);
- Shares and investments in legal entities, which are not sold on active markets and for which there is no reliable value, are carried at cost or last available information about value, reduced by impairment (Level 3)

During 2019 there were no transition between levels during the year.

28. RISK MANAGEMENT (Continued)

28.10. Fair value of financial assets and liabilities (Continued)

The following tables present value of financial instruments based on different information and in accordance with hierarchy within the Fair Value Policy:

Fair value as of **31 December 2019**:
In RSD thousand

	Level 1	Level 2	Level 3	Total
Assets				
Securities	11,122,970	97,169,151	15,539	108,307,660
Receivables from derivatives	-	61,978	-	61,978
Total	**11,122,970**	**97,231,129**	**15,539**	**108,369,638**
Liabilities				
Liabilities based on derivatives	-	7,869	-	7,869
Total	**-**	**7,869**	**-**	**7,869**

Fair value measurement for securities position is divided into three levels. Level 1 instruments refer to bonds issued by Republic of Serbia denominated in USD currency for which there is an active market that provides direct information on quoted market prices. Level 2 instruments refer to bonds issued by Republic of Serbia and financial derivatives which are valued by using discounting techniques on future contracted cash flows, applying market risk-free yields. Level 3 instruments refer to shares or equity held in legal entities that are not listed on the active market.

Fair value as of **31 December 2018**:

In RSD thousand

	Level 1	Level 2	Level 3	Total
Assets				
Securities	5,857,988	86,997,390	17,107	92,872,485
Receivables from derivatives	-	331,839	-	331,839
Total	**5,857,988**	**87,329,229**	**17,107**	**93,204,324**
Liabilities				
Financial liabilities at fair value through profit and loss held for trading	-	21,497	-	21,497
Total	**-**	**21,497**	**-**	**21,497**

The Bank's management considers that the carrying amounts stated in the accompanying financial statements are the most valid and useful reporting values under the present market conditions.

28. RISK MANAGEMENT (Continued)

28.10. Fair value of financial assets and liabilities (Continued)

The following table represents fair value of instruments not carried at fair value and classified by the appropriate levels of hierarchy:

In RSD thousand

31 December 2019	Level 1	Level 2	Level 3	Fair value	Carrying amount
Assets					
Cash and balances with Central Bank		97,392,634		97,392,634	97,392,634
Loans and receivables from banks and other financial organizations		51,906,598		51,906,598	51,166,557
Loans and receivables from customers		171,836,155	233,082,276	404,918,431	373,909,572
Total		**321,135,387**	**233,082,276**	**554,217,663**	**522,468,763**
Liabilities					
Deposits and other financial liabilities due to banks, other financial organizations and Central Bank		41,329,120	21,091,400	62,420,520	66,347,915
Deposits and other financial liabilities due to customers		412,425,122	69,959,945	482,385,067	472,324,895
Total		**453,754,242**	**91,051,345**	**544,805,587**	**538,672,810**

Fair valued Cash and balances with Central Bank are belonging to the Level 2 and are presented at their carrying amount.

Loans and receivables from banks and other financial organizations, deposits and other financial liabilities due to banks, other financial organizations and Central Bank are presented at their fair value calculated as discounting cash flows for deposits, or as discounting cash flows reduced by expected loss for loans. Given the short-term deposits with financial institutions (money market), i.e. transactions with highly rated financial institutions which are contracted at interest rates corresponding to the market, these positions belong to the Level 2.

Fair value for positions Loans and receivables from customers and Deposits and other financial liabilities due to customers are calculated as discounting techniques of future cash flows for deposits, or as discounting cash flows reduced by expected loss for loans. Doubtful loans are valued in the same manner as performing loans, while maturity estimated by the NPL Department is assigned to the total net exposure instead of initially contracted maturity. These positions belong to the Level 2 (up to one-year maturity) respectively Level 3 (if the maturity is over one year).

For the purposes of determining fair values, risk-free yield curves that correspond to the currency and maturity structure of the contracted cash flow are used. For maturities for which there are no market quotes of the BELIBOR yield curve, the yield equals the quoted value of the six-month BELIBOR, increased by the corresponding spread. Spread for a certain maturity is defined as the difference between the executed bond rate with same maturity in the primary market and the value of the six-month BELIBOR on the day of issue of the relevant bond. The European yield curve represents the EUR-STANDARD yield curve that is defined by the money market (for a maturity of up to one year) and the interest rate swap curve which is increased for the country's risk spread (for a maturity more than one year), where the country's risk spread is defined as the difference between issued Serbian and US risk-free bonds.

28. RISK MANAGEMENT (Continued)

28.10. Fair value of financial assets and liabilities (Continued)

In RSD thousand

31 December 2018	Level 1	Level 2	Level 3	Fair value	Carrying amount
Assets					
Cash and balances with central bank		86,962,607		86,962,607	86,962,607
Loans and receivables from banks and other financial organizations		25,580,087		25,580,087	33,039,264
Loans and receivables from customers			377,574,971	377,574,971	339,749,114
Total		**12,542,694**	**377,574,971**	**490,117,665**	**459,750,985**
Liabilities					
Deposits and other liabilities due to banks, other financial organizations and central bank		42,865,406		42,865,406	49,031,251
Deposits and other liabilities due to customers			404,521,698	404,521,698	405,175,217
Other liabilities					
Total		**42,865,406**	**404,521,698**	**447,387,104**	**454,206,468**

The Bank’s management assesses the risk, and in instances in which it estimates that the carrying amount of assets may not be realized, it recognizes a provision.

29. CONTINGENT LIABILITIES

(a) Litigations

As of 31 December 2019, the Bank is a defendant in a certain number of legal proceedings. Total estimated value of damage claims amounts to RSD 6,384,799 thousand (31 December 2018: RSD 6,237,522 thousand), including penalty interests and fees.

The final outcome of the ongoing legal proceedings is uncertain. As disclosed in Note 23, as of 31 December 2019 the Bank recognized the provision for potential losses that could arise from the aforementioned litigations in the total amount of RSD 265,215 thousand (31 December 2018: RSD 275,262 thousand). The Bank's management considers that no significant losses will arise from the ongoing litigations, other than those provided for.

The amount of the highest single litigation claims of RSD 5,491,509 thousand, for which the Bank did not recorded provision, is claimed by a physical person, who is the owner of the Bank's corporate debtor and guarantor for the loan granted to that corporate debtor. The Bank did not recognize provision for this litigation and according to the Bank's management opinion, claimant presented in ungrounded and arbitrarily manner, the facts based on which he claims not precise requirements for compensation damage, and it is expected that the Court will completely reject the claim. Nevertheless, the Bank will monitor change in circumstances at the end of each reporting period. The Bank is involved in a number of lawsuits as plaintiff related to collection of receivables. All disputed receivables from corporate and retail customers have been impaired and charged to the results of the current and previous years.

(b) Tax Risks

The tax system of the Republic of Serbia is in the process of continuous review and amendments. The tax period in the Republic of Serbia is considered to be open for five years. Under various circumstances, the tax authorities could have a different approach to certain issued and could assess additional tax liabilities together with related penalty interest and fees. The Bank's management believes that tax liabilities recognized in the accompanying financial statements are presented fairly.

30. RECONCILIATION OF OUTSTANDING BALANCES WITH COUNTERPARTIES

In accordance with Article 18 of the Law on Accounting, the Bank performed the process of reconciliation of outstanding liabilities and receivables with its debtors and creditors as of 30 September 2019, and it maintains credible documentation on the circularization process.

Out of the total of 3,878 submitted confirmations (IOS forms), 23 were disputed.

The balance of unreconciled outstanding receivables and liabilities is RSD 639.679thousand. The most significant amount relates to receivables from legal entities in bankruptcy (86.02% of the total unreconciled balance).

31. EXCHANGE RATES

The official median exchange rates of the National Bank of Serbia, determined at the Interbank Foreign Currency Market, used in the translation of balance sheet items denominated in foreign currencies, as of 31 December 2019 and 2018 into the functional currency (RSD), for the major foreign currencies were as follows:

In RSD

	2019	**2018**
EUR	117.5928	118.1946
USD	104.9186	103.3893
CHF	108.4004	104.9779
GBP	137.5998	131.1816
CAD	80.4108	75.8630
AUD	73.5185	72.9822
DKK	15.7359	15.8279
SEK	11.2183	11.5202
RUB	1.6919	1.4841

32. EVENTS AFTER THE REPORTING PERIOD

There have been no significant events after the reporting period, which would require disclosures in the Notes to the accompanying financial statements of the Bank as of and for the year ended 31 December 2019.

Belgrade, 11 February 2020.

Rada Radović	Dragica Mihajlović	Draginja Djurić
Head of Accounting Department	Chief Financial Officer	President of the Executive Board

BANCA INTESA BELGRADE

ANNUAL REPORT 2019

Content

1. Key Financial Indicators

Income Statement

RSD thousands

	2019	2018
Net interest income	**20,500,555**	20,487,856
Net fee and commission income	**7,691,852**	7,191,558
Profit before tax	**13,938,435**	13,234,169
Income tax	**(1,587,375)**	(1,073,267)
Net profit from deferred tax assets and liabilities	**(21,601)**	443,208
Profit after tax	**12,329,459**	12,604,110

Balance Sheet

	2019	2018
Cash and balances with Central Bank	**97,392,634**	86,962,607
Non-current assets held for sale and discontinued operations	**38,301**	143,015
Securities and receivables from derivatives	**108,369,638**	93,204,324
Loans and receivables from banks, other financial organisations and customers	**425,076,129**	372,788,378
Investments in subsidiaries	**1,199,472**	1,199,472
Intangible assets, property, plants and equipment and investment property	**15,302,768**	11,756,960
Other assets, current and deferred tax assets	**5,251,950**	5,020,423
Total assets	**652,630,892**	**571,075,179**
Financial liabilities based on derivatives	**7,869**	21,497
Deposits and other liabilities due to banks, other financial organisations, Central Bank and other customers	**538,672,810**	455,921,978
Provisions	**861,164**	1,801,197
Other liabilities and deferred tax liabilities	**13,021,982**	6,729,321
Total liabilities	**552,563,825**	**464,473,993**
Equity	**100,067,067**	**106,601,186**
Total liabilities and equity	**652,630,892**	**571,075,179**

Indicators

	2019	2018
Profit before tax/ Total assets	2.14%	2.32%
Profit before tax / Total equity	13.93%	12.41%
Interest income / Total assets	3.49%	4.09%
Interest expenses / Total liabilities	0.35%	0.50%
Capital adequacy ratio	21.23%	19.76%
Total assets per employee	212,376	190,676
Number of employees	3,073	2,995

2. Letter from the Chairman of the Board of Directors

Ladies and gentlemen,

Looking at the year behind us, it is evident that global economic activity continued its slowdown on the back of rising trade protectionism and geopolitical tensions that have also impacted future growth prospects. Uncertainty surrounding global value chains and international cooperation has led to shaken business confidence, placing a strain on trade growth, capital flows and investment. Amid such an environment, central banks across the globe have taken a more accommodative stance, with a wave of global monetary easing helping mitigate adverse effects on financial markets, while fostering growth through diminished costs of funding.

Against such a challenging international background, Serbia recorded solid economic performance, driven by a rise in consumption and public investments, as well as a record-high inflow of foreign direct investments. Owing to maintained fiscal discipline and continued public investment programs, monetary policy easing of the National Bank of Serbia and ongoing reformatory processes, the external and internal economic imbalances narrowed, strengthening Serbia's growth potential for the years to come.

Understanding that improved technological capability will further strengthen its capacity to support the expected economic expansion Banca Intesa embarked on the biggest development endeavor in its history, seeking to upgrade its core banking system. I am proud that the bank successfully completed a project of such complexity and magnitude, putting in place an advanced operating ecosystem that will support its business ambitions and place it firmly on the path of sustainable growth.

IT system upgrade will enable Banca Intesa to improve efficiency and bolster competitiveness by creating foundations for developing modern products and advanced services driven by digital technologies. Moreover, the project has confirmed Intesa Sanpaolo's long-term commitment to developing its business in the Serbian market and will provide the Group with valuable experience on how to continue with the implementation of its IT platform standard across the globe. I am pleased that during my first year as Chairman of Banca Intesa Board of Directors I am able to witness such exciting times for the bank.

Even though Banca Intesa was predominantly focused on IT platform modernization last year, it nonetheless remained dedicated to maintaining the trend of strong business and financial performance. Owing to the constant improvement of product offering and service quality, along with a stronger digital presence and implementation of the new branch network service model, the bank kept its leading market position in Serbia by all key performance indicators, commanding nearly 16% of the market in total assets and total loans, 15% in total capital and close to 17% in total customer deposits at the end of the third quarter. The bank boosted overall lending in 2019, supporting the country's economic expansion and helping households improve their quality of living. At the same time, it lifted its customer deposit base, reflecting the strong level of confidence that Serbian businesses and citizens place in Banca Intesa.

The bank maintained its sound business model, with a low risk profile and high liquidity and capital positions, as reflected in a loan-to-deposit ratio of 79.2% at the end of 2019 and a capital adequacy ratio of 21.2% at the end of the third quarter. Furthermore, it continued to strengthen operational efficiency, reducing the cost-to-income ratio to 46.5% in 2019. At the same time, further advancement of the loan approval system in combination with proactive loan management paved the way for a slowdown in NPL inflow, while efficient workout resulted in a further reduction of the NPL level. Based on the good performance across all major metrics, Banca Intesa's net profit before income tax rose 5.3% year-on-year to 13.9 billion dinars in 2019.

This success was achieved owing to the hard work and strong commitment of bank employees, guided by the Executive Board and the Board of Directors, who I would like to thank for their continued dedication and contribution to overall Group objectives. I am confident that Banca Intesa, with stable support from Intesa Sanpaolo, will continue to play a central role in the changing landscape of the Serbian banking sector in the years to come, providing a strong contribution to the expected further expansion of the domestic economy and helping improve the wellbeing of households and community in general.

Sincerely,

Ignacio Jaquotot,

Chairman of the Board of Directors

3. Foreword by the President of the Executive Board

Dear readers,

In the retrospective of Banca Intesa operations, 2019 will, no doubt, be remembered as the year in which we completed one of the biggest developmental and investment endeavors of the bank and put in place preconditions for sustainable growth in the future. Despite the fact that we channeled substantial resources towards upgrading our IT platform and operated in conditions of market consolidation, strengthening competition and new regulatory requirements, we managed to record excellent business results and reaffirm our leading market position by all key performance indicators – total assets, capital, loans and customer deposits.

From the economic point of view, the previous year was marked by positive macroeconomic trends and solid economic growth driven by a rise in consumption and public investments. Owing to the measures of the National Bank of Serbia (NBS), a low inflation rate was preserved, along with the relative stability of the dinar, which coupled with all-time high foreign direct investment inflow and employment growth contributed to maintaining a stable macroeconomic environment. As a result of such a setting, in combination with fiscal discipline and a stable monetary policy, leading global agencies improved Serbia's credit rating, while the country's risk premium fell to a record low.

In such circumstances, the central bank continued to lower its key policy rate, which was cut to its all-time low in the regime of targeted inflation. The NBS monetary policy easing allowed banks to keep lowering active interest rates in a move that helped further boost lending activity in the domestic market. Retail lending on market level went up 9.3% in December compared to end-2018, predominantly fueled by cash and housing loans, while corporate lending rose 9.1%. In the same period, overall deposits of the banking sector picked up 8.5% on the back of a high level in customer confidence, while the NPL level fell to record-low 4.58% in November, further strengthening the stability of the market.

For Banca Intesa, 2019 was a year of big accomplishments. In keeping with the requirements of the digital era and the needs of our customers, we completed the Constellation Serbia project, which marked the start of a new stage in the development of the bank and laid a foundation for building a sustainable business model. The migration to a new IT platform has cleared the way for further development through improved quality of products and services, better market agility and higher operational efficiency, which will enable us to be even more attentive to the needs of our customers.

Improved offering, digitalization of services and further expansion of the new service model in the branch network allowed Banca Intesa to post a 11.0% increase in lending to private individuals in December compared to end-2018, which was led by outstanding results in housing loans. At the same time, we bolstered customer deposits 12.9% as the result of the high level of trust that Banca Intesa enjoys in the market. The bank’s number one position in both loans and customer deposits was preserved on the corporate front as well owing to innovative products, strong relations with clients and a top-level service, with loans growing 6.2% and customer deposits 23.5%. In both segments we recorded an increase in the number of both users and transactions on e-channels, confirming the properness of our strategy that centers on progressive digitalization of business processes and services.

Corporate social responsibility was an inseparable element of Banca Intesa’s business strategy last year as well, as confirmed by the recognitions we won. We took the Virtus award for philanthropic contribution on the national level and were also recognized as a gender sensitive company. In addition, we continued to improve internal regulatory framework in line with international CSR standards, further strengthened our corporate volunteering culture and allocated substantial funds for cultural heritage preservation and promotion of culture, as well as for the work of welfare and educational institutions.

Looking back at what we accomplished in 2019, I would like to thank all bank employees for displaying exceptional commitment and teamwork and providing crucial contribution to achieving the goals set out in our business strategy. I would particularly like to extend my gratitude to our customers, shareholders and members of the Board of Directors for their trust and strong support in laying the foundation for developing a modern, agile and efficient bank that is keeping pace with the challenges of the technological revolution and the needs of its customers.

Respectfully,

Draginja Đurić,

President of the Executive Board

4. Macroeconomic Environment and the Banking Sector

- *Strong domestic demand helped the Serbian economy grow at solid rate in 2019, in spite of external weaknesses*
- *Muted inflation, prevailing appreciation pressures and good demand for government bonds created room for further monetary easing by NBS*
- *Resilient growth, preserved fiscal adjustment gains and contained public debt led to credit rating upgrade by S&P and Fitch, one notch away from investment grade*

Despite weaker global economic prospects, the past year was characterized by Serbia's steady economic performance supported by sustainable rise in private consumption and robust investments.

Inflation remained low and stable, allowing for further decline in key policy rate and consequently lower lending rates. As a result, strong credit growth at favourable conditions gave an additional support to the economy.

Serbia's risk premium dropped to a historical low reflecting the monetary and fiscal stability achieved while the country's credit rating was upgraded, by both S&P and Fitch, moving closer to investment grade.

Dinar was stable throughout the year and recognized as „realistically valued" being at the top of a JP Morgan ranking of 25 currencies of developing countries around the world. In addition, NBS interventions in the foreign exchange market which are used to prevent excessive short-term volatility of the dinar exchange rate against the euro have significantly contributed to boosting of the country's foreign exchange reserves to record-high levels. In such an environment, the local currency debt market has deepened, with the extension of the maturity of dinar government securities to ten years.

Foreign direct investments continued growing fifth year in a row, fully financing current account deficit, and remained well diversified and largely directed to export-oriented manufacturing and service sectors. Serbia was declared the world champion in attracting FDI in relation to the size of its economy, for the second time in three years by Financial Times Greenfield FDI Performance Index for 2019.

Foreign investors have been taking advantage of the country's productive and relatively low-cost labour but also its restored macroeconomic stability and improved business climate. Advancement of business environment was also confirmed by Serbia's progress on the latest Doing Business list by four notches where among 190 countries, Serbia ranked 44th, while achieving the best progress in the area of construction permit issuing (9th position).

Fiscal discipline has taken root, with the general government budget recording a surplus for three consecutive years, while the share of public debt in GDP recorded a faster-than-anticipated decline. Funds raised by issuing Eurobonds on the international market were intended for the payment of the earlier taken expensive debt while cutting down interest expenses.

Positive trends on the labour market continued with unemployment rate dropping to single-digit level (which is its lowest in decades), changes of set of tax laws that stimulate employment and solid increase in wages. However, the overall wage bill is now growing faster than nominal GDP, for a second year in a row, which deviates from the IMF's advice in this area.

IMF and Serbia successfully completed three reviews under the non-financing Policy Coordination Instrument. All quantitative targets set by IMF were met so far and implementation of structural reforms continued, albeit with delays in some areas.

The work toward EU accession advanced as Serbia opened two EU negotiation chapters in 2019, namely chapter 9 dealing with financial services and chapter 4 dealing with free movement of capital. So far, country has opened 18 out of 35 negotiations chapters with two temporarily closed.

Based on current macroeconomic trends and adopted policies, outlook for 2020 remains positive with expected solid growth of economic activity driven by private consumption, growth-supportive monetary policy and stable fiscal stance. Adopted 2020 budget represents an end to the process of consolidation of public finances and marks the start of the development stage. However, stronger commitment to structural reforms, further convergence toward EU and improvement of business environment remain the key challenges.

Macroeconomic environment

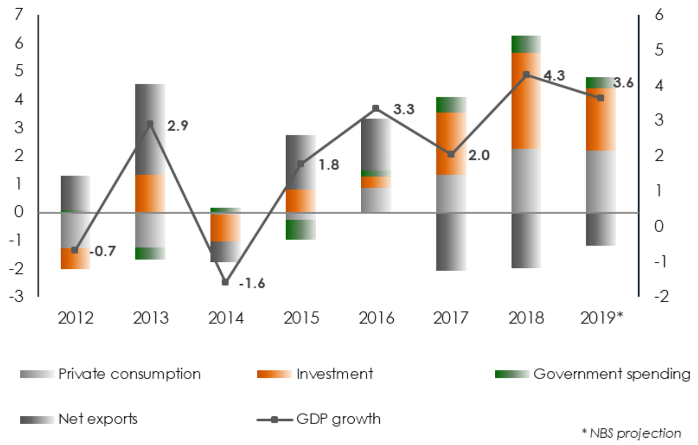
Economic activity

After recording the highest growth in decade of 4.4% y-o-y in 2018, economic activity moderated to average 2.8% y-o-y in the first half of 2019. However, real GDP accelerated considerably in the third quarter of 2019 to 4.8% y-o-y as domestic factors successfully compensated for the weaker external demand.

On the production side, the strongest contribution to growth in 3Q 2019 came from construction sector which grew by 35% y-o-y owing to intensified works on the transport and energy infrastructure, notably construction of the Serbian stretch of the Turkish Stream gas pipeline. Services also gave positive contribution as favourable trends in the labour market continued.

Considering the demand side, robust rise in consumption was driven by high real wage growth, solid employment gains and low interest rate environment, while the pick-up in investment reflected the current phase of the construction cycle.

Graph 1 – Contribution to the annual GDP growth rate (in %)



Source: NBS

Strong growth is expected to continue in 4Q 2019 driven by further development in construction, fixed investment and industrial production recovery. Overall, Serbia's economic growth in 2019 should be on the level of the average in Central and Eastern Europe.

According to National Bank of Serbia, economic activity is expected to grow by around 4% in 2020 driven by continued investment and final consumption growth, while the FDI inflow, channelled mostly to tradeable sectors and the increase in production capacities, with the expected modest rise in external demand, will facilitate faster growth in exports and reduce the negative contribution from net exports.

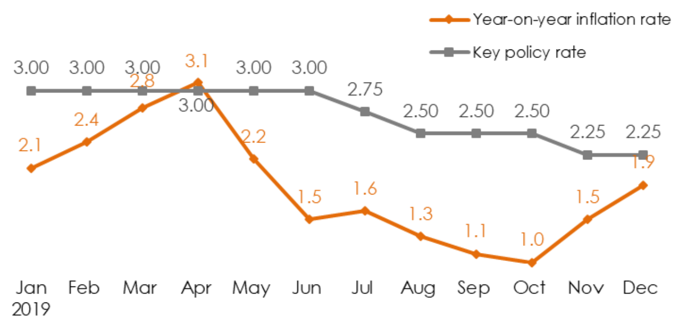
Inflation

Inflation was relatively stable in 2019. In the first few months of the year, CPI gradually approached the NBS target midpoint of 3%, measuring 3.1% y-o-y in April (which was the highest level in 2019), mainly due to the low base effect from vegetable prices which at the same time increased more than seasonally typical for this part of the year due to poor yields in Serbia and in the greater part of Europe.

As of May 2019, y-o-y inflation was on a downward path hoovering around and below the lower bound of the target tolerance band (3.0%±1.5 p.p.). Such inflation movements were predominantly driven by a lower contribution from fresh vegetables prices, with the onset of the new agricultural season, and by the fall in the prices of petroleum products resulting from a decline in global oil prices.

Core inflation has moved between 1.1% and 1.5% y-o-y throughout the year, suggesting that low inflationary pressures were of a more permanent nature.

Graph 2 – Year-on-year inflation dynamics and key policy rate trends (in %)



Source: NBS

Based on NBS projections, y-o-y inflation is expected to continue moving around the lower bound of the target tolerance band in the first half of 2020, and start gradually converging to the central midpoint of 3% afterwards as a result of rising aggregate demand and the anticipated acceleration in administered price growth.

Monetary policy

In 2019, NBS adequate monetary policy has kept inflation under control, while supporting economic activity and maintaining broad exchange rate stability. It was pursued in accordance with the "Monetary Policy Program of the National Bank of Serbia in 2019".

After being kept on hold (at 3.0%) in the first half of the year, the key policy rate was trimmed three times in 2019 by cumulative 75 basis points, to its lowest level in the inflation targeting regime (2.25%). Monetary policy easing during 2019 was motivated by weakened inflationary pressures, persistent appreciation pressure on dinar, reduced internal and external imbalances and the monetary policy accommodation of leading central banks.

In the current monetary relaxation cycle, which began in May 2013, the National Bank of Serbia lowered its key policy rate by 9.5 pp. Consequently, the effects of accommodative monetary stance had been transmitted into lower short-term interest rates, as well as deposit and lending rates, whereas dinar interest rate for corporate sector dropped by 12.3pp to 4.1% in October 2019 while households dinar interest rates decreased by 11.3pp recording a new minimum of 9.2% in October 2019.

The NBS continued to implement the floating exchange rate regime, intervening in the FX market in order to reduce excessive exchange rate volatility and maintain price and financial stability. Dinar remained relatively stable throughout the year with the EURRSD exchange rate hovering around 117.5 dinars per euro.

Required reserve rate remained unchanged since 2016, when it was reduced for the last time in order to foster credit activity (to 20% and 13% on liabilities with maturities up to and above 2 years, respectively). NBS uses required reserve as an important macro prudential tool within dinarisation strategy as it has maintained the beneficial treatment of dinar and long-term sources of funding for banks within the reserve requirement setup.

National Bank of Serbia will keep its cautious monetary policy stance in the coming years in order to support macroeconomic stability and sustainable economic growth, maintaining full coordination of monetary and fiscal policy measures. In addition, NBS will continue to closely monitor and analyse movements in the international financial and commodity markets and assess their impact on Serbia.

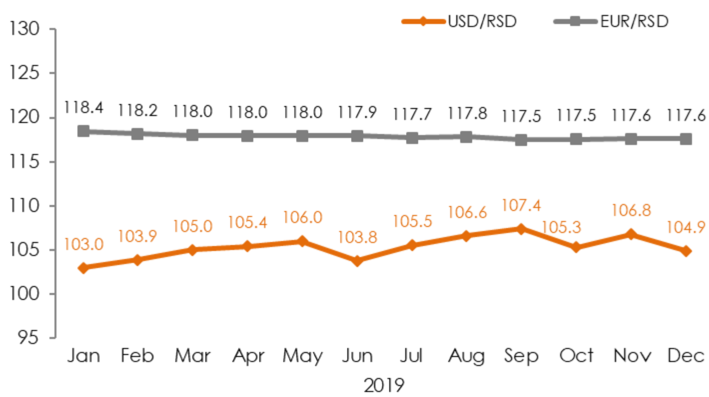
Dinar exchange rate

After modest depreciation pressures on the local FX market at the beginning of the year, mainly caused by the seasonally higher FX demand of energy importers, appreciation pressure prevailed during the rest of 2019, as it was the case over the past two years.

Overall in 2019, dinar appreciated against euro by 0.5% encouraged by enhanced macroeconomic fundamentals and improved country risk perception, which led to strong foreign direct investments inflow and elevated non-resident investment in government securities. Central bank mostly intervened on the purchase side in order to ease excessive short-term volatility of the exchange rate of dinar against euro and bought a net total of EUR 2,695mln. This provided a major contribution to the growth in NBS FX reserves, which increased to their highest level since 2000, when these data began to be monitored.

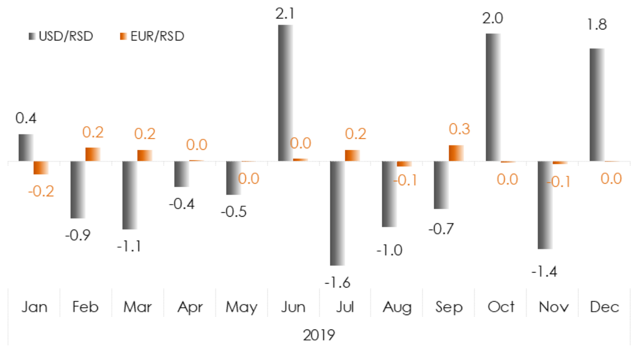
It is expected that stable macro and fiscal environment, strong capital inflows and increased dinar lending, will remain supportive for the dinar in 2020 that, steered with occasional NBS interventions, will remain at the similar level as in 2019.

Graph 1 - Dinar exchange rate trend



Source: NBS

Graph 2 - Monthly exchange rate changes (in %)



Source: NBS

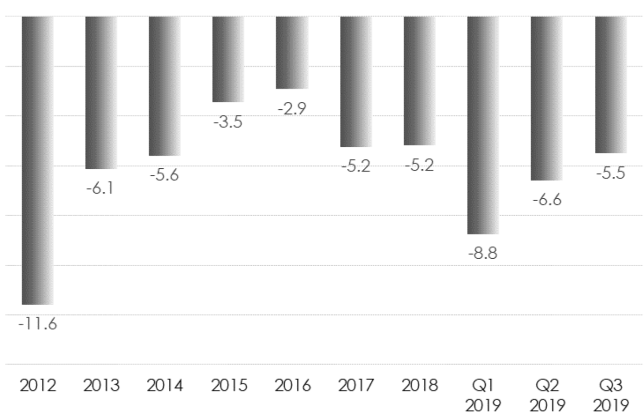
Current account deficit and external debt

Serbia's external balances have improved significantly since the global financial crisis, although the trend has somewhat reversed since 2017, partially on the back of ongoing investment cycle (higher imports of capital and intermediate goods), higher oil prices as well as further growth in domestic demand.

According to the projection of the National Bank of Serbia, the current account deficit will be around 5.5% of GDP at the end of 2019, and is expected to decline to around 4-5 percent of GDP over the medium term, as FDI inflows moderate and export performance gradually picks up.

The current account deficit will continue to be fully financed by net FDI, as it was the case in last five years, which is an indicator of long-term external sustainability.

Graph 3 - Current account deficit (in % of GDP)



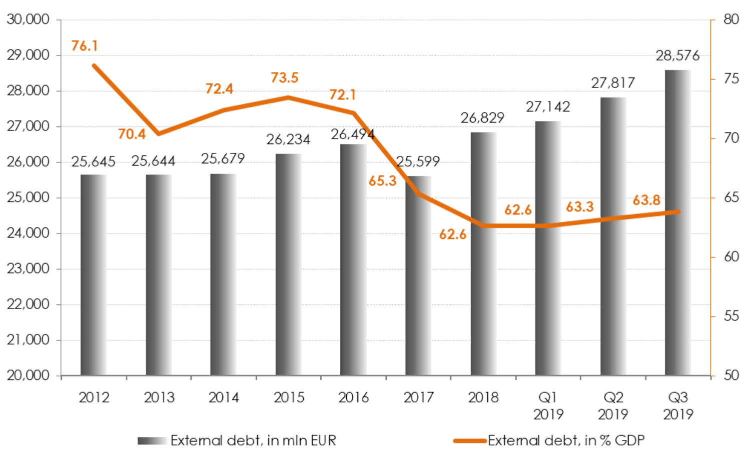
Source: NBS

External debt declined to its pre-crises level after peaking at almost 80% of GDP in 2012. Based on the latest available data, Serbia's external debt amounted to EUR 28.5billion or 63.8% of GDP at the end of 3Q of 2019, standing below the threshold of severe indebtedness, according to the World Bank criteria (80% of GDP). Sustainability of the current debt level was additionally supported by its favourable maturity structure as long-term liabilities dominate with a 95% share.

Indicators of external solvency remained at satisfactory levels. The ratio of external debt to exports of goods and services declined to 124.4% in 3Q2019 (vs. 126.0% at end-2018), staying below the sustainability bound under the World Bank criterion (220%). In fact, Serbia belongs to the group of less indebted countries according to this World Bank criterion, since the external debt to export ratio is below the 132% level.

According to the IMF projection published in the report on the completion of the second review under the Policy Coordination Instrument, Serbia's total external debt is projected to gradually decrease further over the medium-term falling below 60% of GDP.

Graph 4 - External debt



Source: NBS

Foreign direct investment

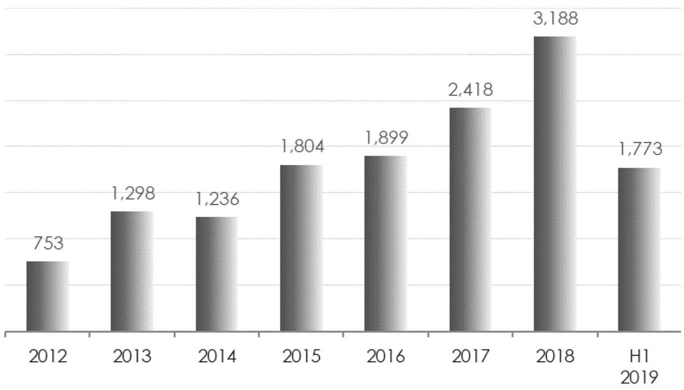
In the period January – October 2019, Serbia recorded a net-inflow of foreign direct investments in the amount of EUR 3.1 billion, which is 37.5% more than in the same period of the previous year, and a record for the calendar year.

This is the fifth year in a row in which Serbia has recorded steady growing trend of foreign direct investments and the fifth year in the row in which the net inflow of FDI is more than sufficient to cover the current account deficit.

FDI have remained diversified, in both project and geographical terms, and they are largely directed to the manufacturing sector (metals, motor vehicles, food/beverage and pharmaceutical industries) while most of the FDI came from Euro area.

The National Bank of Serbia expects stable foreign direct investment inflow to continue in the following year, supported by achieved macroeconomic stability, enhanced business environment, the country's further progress in the EU accession process, as well as improved overall country risk perception by investors.

Graph 5 - Foreign direct investment (in EUR million)



Source: NBS

Foreign trade

External trade in 2019 was under the adverse influence of dinar appreciation effects, fast growth of domestic demand, introduction of 100% tariffs on products delivered to Kosovo and Metohija as well as quotas on steel export to the EU and slowdown in the euro area, notably in Serbia's key trade partners (Germany and Italy).

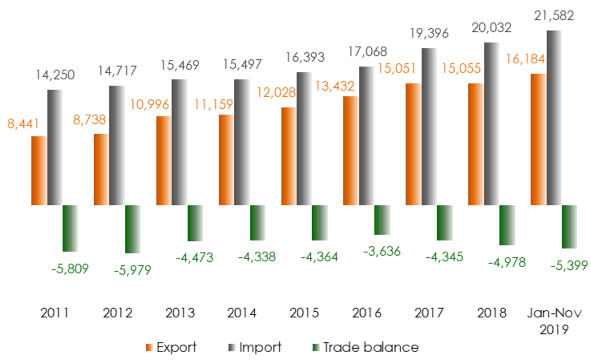
Despite abovementioned challenges, Serbian foreign trade recorded positive performance in first eleven months of 2019 reaching around EUR 37.8 billion, which is 7.6% higher compared to the previous year, while the export import coverage ratio was 75.0%. The exports of goods amounted to EUR 16.2 billion (+7.4%), while imports reached EUR 21.6 billion (+7.7%), resulting in a total trade deficit of EUR 5.4 billion (+8.6%).

Motor vehicles, trailers and semi-trailers were the most important export products with 11.6% share while electrical equipment took the second place with 9.6% share in total export.

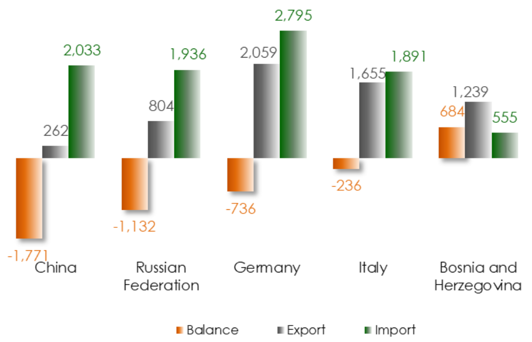
HBIS remained the top exporter with a total value of exported goods amounting to EUR 578 million in the period January-October 2019. However, it is to be seen to what extent the newly imposed import tariffs on steel products will affect HBIS's exports. Fiat came second with exports worth EUR 417 million, which is almost by half lower than in the previous year. Total value of exports of the 15 largest exporters amounted to around EUR 3.6 billion in the same period, which is 25% of total Serbian exports.

Around two-thirds of Serbia's foreign trade were directed towards EU countries, while CEFTA countries were the second most important trade partner with whom Serbia posted a high trade surplus with an export-import coverage ratio of 314.5%. The most important foreign trade partners in exports were Germany (EUR 2.06 billion), Italy (EUR 1.65 billion), and Bosnia and Herzegovina (EUR 1.24 billion), while the largest imports came from Germany (EUR 2.80 billion), China (EUR 2.03 billion), and Italy (EUR 1.89 billion).

Graph 6 - Foreign trade (EUR million)



Graph 7 - Foreign trade with major partners (EUR million)



Source: Statistical Office of the Republic of Serbia

Export is expected to speed up in coming period, on the back of a high FDI inflow in tradeable sectors and the expected recovery of external demand. The import of equipment and intermediate goods is expected to increase owing to the continuation of the investment cycle, while the higher standard of living of citizens and consumer demand will contribute to the rising import of consumer goods.

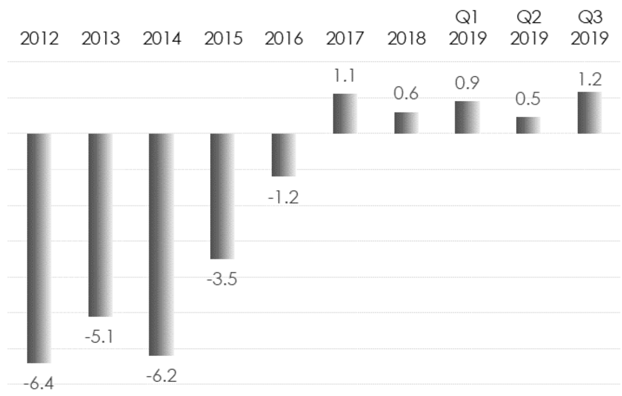
Fiscal policy

Favourable fiscal trends continued on the back of successfully implemented fiscal consolidation measures. In the first nine months of 2019, general government fiscal surplus reached RSD 35.1 billion or 0.9% of GDP.

As fiscal performance was better-than-planned, the Government adopted supplementary budget in last quarter of 2019. The available fiscal space was directed towards increase in public sector wages (in the range of 8 to 15 percent, on average 9.6 percent) and one-off payment to pensioners (in the amount of 5,000 dinars per pensioner, or 8.5 billion dinars in total) while part of the surplus would be used for capital investments.

According to the Ministry of Finance, the fiscal policy stance is likely to be slightly expansionary in the coming period. Serbian Parliament adopted 2020-budget, which is according to Fiscal Council relatively well planned. The budget envisages total revenues of RSD 1,314.5 billion and expenditure of RSD 1,334.7 billion, resulting in a projected deficit of RSD 20.2 billion or 0.3% of the GDP, which will ensure that the downward trajectory of public debt is maintained.

Graph 8 - Consolidated budget deficit (in % of GDP)



Source: NBS

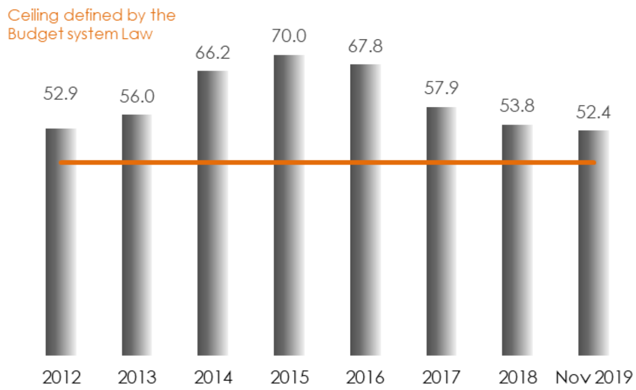
Fiscal discipline and strong economic growth continued enabling public debt to remain on a firm downward path. At the end of November 2019, the public debt amounted to EUR 24.1 billion, while the public debt/GDP ratio stood at 52.4%. The level of public debt was below the Maastricht ceiling of 60% of GDP, but at the same time above the legally prescribed limit of 45% of GDP.

A major share of public debt is still in foreign currency (EUR 44.2%, USD 19.9%), while 27.9% of public debt is denominated in RSD, making public debt dynamics sensitive to exchange rate shocks. However, currency risk was largely mitigated as government mostly borrowed on the domestic market by issuing long-term dinar securities (up to ten years).

In addition, the risk of refinancing was eased due to the maturing and early payment of a part of the debt under dollar-denominated Eurobonds, and the achieved lower interest rates on such borrowing. This was confirmed by successful issuance of the ten-year Eurobond in the international financial market, in the amount of EUR 550 million in November 2019. Funds raised will be used solely for the early payment of a portion of the expensive dollar bonds, issued in 2013 at the coupon rate of 4.87% while this latest Eurobond was sold at the lowest rate of return so far of 1.25%.

According to IMF, public debt is projected to remain on a firm downward path, while the debt profile will continue to improve, with increased maturity and a higher share of dinar-denominated debt.

Graph 9 – Public debt (in % of GDP)



Source: Public Debt Administration

Banking sector

At the end of 2019, the Serbian banking sector consists of 26 banks, of which 19 are foreign-owned, continuing the downward trend in number of the banks as a result of still ongoing process of market consolidation. On the other side, despite reducing the number of banks, the number of branches and banking sector employees increased compared to previous year.

The most significant change within banking sector during 2019 is the acquisition of Vojvođanska banka by Hungarian OTP Group, making it a member of one of the largest banking groups in the Central and Eastern European market. Following the completion of financial transaction in 2017, Vojvođanska banka and OTP Banka have begun operating as a single legal entity from April 2019, under the name Vojvođanska banka a.d. Novi Sad, significantly improving its position on the market.

In order to further strengthen its presence in the local market, the OTP Group continued the process of market consolidation by purchasing Societe Generale bank in September 2019, becoming its 100% owner. Shortly after, the name of the bank was changed into OTP bank under which it will operate until its final integration with Vojvođanska banka, which is expected to be completed by 2021.

Additionally, one more acquisition occurred in February 2019 when PPF Group has acquired a 100% stake in Serbia-based Telenor Banka from Telenor Group, which started operating under the new name Mobi Banka, from October 2019.

At the year-end, Government of the Republic of Serbia acquisited a 34.58% stake in Komercijalna Banka from its two stakeholders - IFC Capitalization Fund and The European Bank for Reconstruction and Development. As a result of the transaction, the Republic of Serbia acquired a 83.23% of the Komercijalna Banka's shares, which is one of prerequisites for the beginning of the privatization process.

Since the beginning of the year, the banking sector's total assets increased by 5.5%, reaching the amount of almost RSD 4.0 trillion (EUR 33.9 billion) in the third quarter.

Influenced by further easing of the monetary policy by the National Bank of Serbia, intensified competition among banks, as well as long-standing low interest rates, the increasing trend of credit demand continued in 2019.

Total customer lendings reached the amount of RSD 2,303 billion (EUR 19.6 billion) at the end of third quarter, indicating an increase of 6.6% from the beginning of the year, driven by higher placements to both business and households segments.

Favourable macroeconomic outlook and accelerated economic growth led to the stock of corporate loans equalled to RSD 1,205 billion in September 2019, indicating a growth of 5.4% compared to the beginning of the year (RSD 61.3 billion). As in previous period, it is mostly attributable to placements to trade, transport and construction companies.

Furthermore, the volume of newly issued loans to individuals sector keep growing, recording an increase of RSD 64.4 billion in the first nine months. Owing to high disbursement levels of mortgage and consumer loans which dominate within the sector, total retail loan portfolio is raised up to the level of RSD 1,076 billion at the end of third quarter.

Currency structure of loans is almost the same as in previous year. Local currency loans made 33% of total customer loans. New household loans were mainly placed in dinars positively affecting dinarization process. On the other side, euro-indexed and euro-denominated loans still make a dominant part of the foreign currency loans. Moreover, during 2019 the share euro and euro-indexed loans is pushed up due to strong growth of mortgages loans as well as conversion of CHF-indexed housing loans into euro-indexed loans.

Deposits from clients as a primary source of funding in Serbian banking sector record increasing trend for years. In the third quarter of 2019 they reached the volume of RSD 2,649 billion, which represents more than two thirds of the total market liabilities. By the end of September 2019, total deposits rose by 4.7% compared to the beginning of the year, driven by higher both local and foreign currency deposits. Besides them, another notable source of funding are deposits received from banks and other financial institutions. The euro is still the dominant currency, making up more than 90% of total FX and FX-indexed deposits while the rest of FX and FX-indexed deposits is mainly related to USD and CHF currencies.

Regarding maturity structure, as of November short term deposits reached almost 80% share in total deposits, out of which demand deposits remained dominant category.

Asset quality is continuously improving with trend of shrinking NPL ratios. The stock of NPLs continued to decrease in 2019, as a result of successful implementation of the NPL Resolution Strategy and the Decision on the Accounting Write-Off of Bank Balance Sheet Assets. Sustained with growth in lending, this resulted in the share of NPLs in total corporate loans reaching a new minimum of 3.7% in November, being lower 1.4pp from end-2018 level. The sectors which contributed the most are construction, real estate and trade. As well, NPLs of household segment also recorded a new minimum of 4.1% in November, as a result of declining trend of mortgages, credit cards and overdraft NPL shares.

Nevertheless, NPL reduction did not lead to a significant increase in the banking sector profitability. At the end of the third quarter 18 banks recorded positive results while total net income before tax amounted RSD 54.1 billion, being only 0.4% above the result achieve in the same period 2018. No significant progress was made due to the provision expenses which were recorded in the amount of RSD 3.8 billion at the end of September, while in the same period last year the market was characterized by provision release.

Although banks face profitability challenges, operating margin amounted to RSD 57.9 billion until September, which is 7.7% higher than the same period previous year, primarily driven by proficient cost controlling. Namely, in the same time horizon, operating costs decreased compared by 5.3% or more than RSD 4 billion in absolute amount. The savings are made predominantly within administrative expenses (-18.5%) while personnel expenses are only slightly reduced (-0.5%). On the revenues side, despite increasing lending activity, the growth was boosted predominantly through commission income which reached RSD 30.7 billion, being higher for RSD 1.4 billion (+4.9%) in comparison to the same period previous year. Despite low interest rate environment, interest income increased slightly to RSD 96.1 billion, being by RSD 0.7 billion (+0.7%) above previous year level.

At the end of the third quarter, return on assets (ROA) dropped by 0.2pp in comparison with September 2018, to the level of 1.9%, while return on equity (ROE) declined by 0.1pp in the same period, to 10.5%.

The banking sector in Serbia is well capitalised and highly liquid. The capital base is increased by RSD 20 billion (+2.9%) compared to the beginning of the year, while capital adequacy indicators of the banks are well above the regulatory threshold, which confirms stability of the financial system and safety of customer deposits. At the end of the third quarter, the capital adequacy ratio of the banking sector was 23.6%, increasing the confidence in the financial market as a whole.

In 2019, Banca Intesa has strengthened its leading position with the dominant market share in all key indicators. Particularly, at the end of the third quarter, Banca Intesa held 15.9% of total assets, 15.8% of customer loans and 16.7% of customer deposits. Furthermore, Banca Intesa has the largest amount of capital despite the significant amounts of dividends payouts in the recent period, taking more than 15% of market capital base. Additionally, the Bank ranks first in payment card and payment operations, with a growing client base of around 1.3 million clients. The Bank's widespread network, which consist of 155 branches, is strongly supported by the largest network of ATMs and POS terminals in the market.

5. Highlights of the Bank's Strategy and Planned Development

Banca Intesa Beograd aims to strengthen its leading position in the Serbian banking sector, by providing solid and sustainable value creation and distribution, while remaining committed to actively supporting Serbia's economic recovery.

In the period 2018-2021, the Bank's strategic objectives should result in a stronger market position driven by digital transformation, revenue growth through capturing new business opportunities, while simultaneously being committed to credit portfolio quality and maintaining cost discipline through rationalisation and efficiency enhancement.

Accomplishment of the Bank's objectives is summarised in the following five initiatives:

I Driving digital transformation while reviewing the role of the physical network

Exploitation of the full potential of digitalisation is foreseen as one of the key drivers of value creation and revenue growth in the following years. By embracing digitalisation, the Bank intends to enhance customer services providing convenience to customers along with time savings. The Bank will work on the further development of online products, services and experiences and will enhance digital relationships with clients by upgrading mobile and online applications and introducing new platforms for corporate clients. At the same time, the Bank will work on physical network optimisation and digital process improvement.

II Increasing revenues in a very competitive environment while improving fee based contribution

In a highly competitive environment, the Bank will focus on expanding lending activity and building a sound portfolio, while at the same time striving towards revenue growth leveraging new business opportunities. Several activities are planned to support this initiative such as active customers' boost and proactive sales approach. Moreover, the Bank will enhance product cross selling by leveraging ISP product factories and business cooperation with Intesa Sanpaolo Group in order to further improve the promotion of hedging and structured finance products and joint approach to debt capital markets. Leveraging COSME and InnovFin guarantee schemes with the EIF, the Bank will continue to respond successfully to the strong market demand for products with risk sharing features. In the upcoming years, the Bank will build new sources of fee-driven income by expanding into the wealth management market leveraging the newly established asset management company – Intesa Invest, as well as expanding the range of insurance products and utilising the growing market potential for life insurance product sales.

III Improving cost discipline

Based on its strong commitment to improve efficiency and simplify the operational model, the Bank will continue the process of cost optimisation through organisational and process review. Namely, the Bank will aim to maximise the efficiency of the business network through network organisation analysis and automation of business processes, application standardisation and rationalisation. Regarding the process review, this ICT project will enable the automation and digitalisation of business operations and processes in order to increase productivity, save time and guarantee higher service quality and at the same time reduce non-value-added activities.

IV Improving credit quality

The Bank will continue on the path of improving credit quality through proactive credit portfolio management and timely NPL reduction initiatives. The Bank will work on credit risk management improvement through harmonisation with Group methodologies, as well as on internal credit rating models for the purpose of converging to the standards of advanced approaches to credit risk measurement. Furthermore, the Bank will pursue the implementation of the ECA tool in order to harmonise with the Group practice and enhance efficiency. In addition, the Bank will improve credit management. Processes for identifying target industries will be improved aiming to align credit quality and commercial effort, particularly in respect to Small Business and SME segments, taking into account lending potential and positive business outlook in this segment. Also, further automation of the redesigned, revised and enhanced credit and underwriting process for SB and SME clients will be conducted, aiming at wider usage of internal ratings refined by credit criteria, by differentiating between types of credit processes and expanding the scope of clients to be processed. Proactive credit portfolio management and NPL management will be further strengthened, while a further reduction of non-performing exposures will come as a result of regular portfolio clean-ups taking into account legal and tax constraints, global review of all clients and further promotion of restructuring plans with more proactive approach towards clients

V Strengthening the Group operating model in the key areas

The Bank will focus on strengthening its relationship with the Parent Group through several initiatives. In the following years, one of the main goals related to integration with the Group will be implementation of strategic projects that will provide an adequate infrastructure for growing business needs and digitalisation era. This project will enhance steering and monitoring in business, control and support areas, and also further develop standardisation and economies of scale in IT Operations. Recognised as the most important asset of the Bank and one of the key enablers for Business Plan achievement, further staff development will be supported by several Group initiatives. The Bank will develop enablers to support performance through the new performance management assessment with the improved performance appraisal process and new incentive system and strive to assert the distinctiveness in employees.

6. Retail Banking

Individuals

- *The segment of housing loans recorded the highest growth ever*
- *A large number of clients offered their trust to Intesa Invest resulting in significant returns in the retail segment*
- *Introducing a new information platform as a reliable path to further digital enhancements and strengthen customer relationships*

The strategic orientation of Banca Intesa towards a continual development of service quality and business transparency, while striving to improve customer satisfaction, is reflected in the growth of primary client base at an annual rate of 2.4%. Consequently, during 2019, the Bank confirmed and further strengthened its leading market position, reflected in market shares in all key products offered to individuals, but also Bank significantly improved the offer of innovative products, enabling to meet the broader range of sophisticated financial needs of its customers.

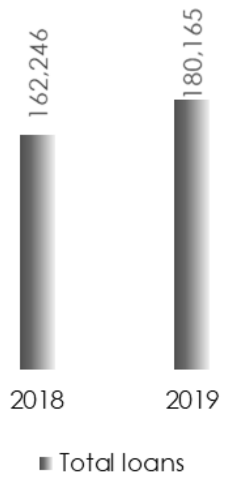
The previous year was marked by a significant increase in commercial and financial indicators, with the most dynamic growth achieved in the area of commercial lending to individuals.

With regard to achieved growth rates in all business segments, Banca Intesa managed to overcome all challenges imposed by the dynamic market in the past year as well. Through a number of innovations and improvements focusing on customer satisfaction and transparent communication of price and non-price elements of products and services, the Bank achieved cash loans in the amount of EUR 332 million (RSD 39.2 billion). Such business results contributed to retaining the Bank's market share in cash loans of 13.3%, while, at the same time, the number of clients with cash loans increased by 1.7% compared to the previous year.

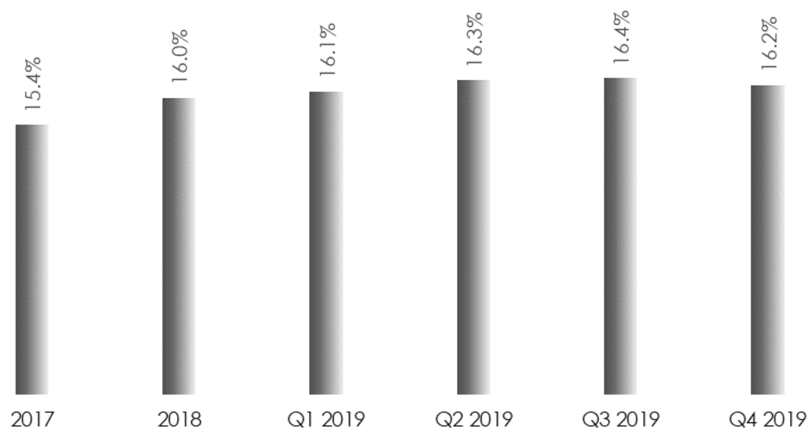
Regarding mortgage loans to individuals, the Bank achieved the highest increase ever, 39% in comparison to 2018 and reached EUR 164 million (RSD 19.3 billion). In 2019, the trend of dynamic increase of the market share continued, from 17.9% at the end of 2018 to 20.1%. In addition, the number of clients with mortgage loans increased by 13.5% compared to the previous year.

The perennial growth of active retail banking activities is the best proof that clients appreciate the high level of service and business policy focused on clients and their actual needs, as well as the principle of business transparency.

Graph 12 - Loans to individuals (in RSD million)

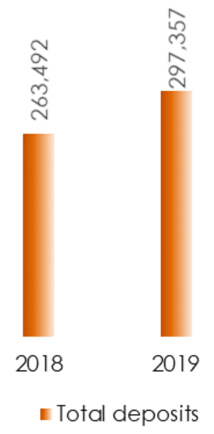


Graph 13 – Market share in loans to individuals

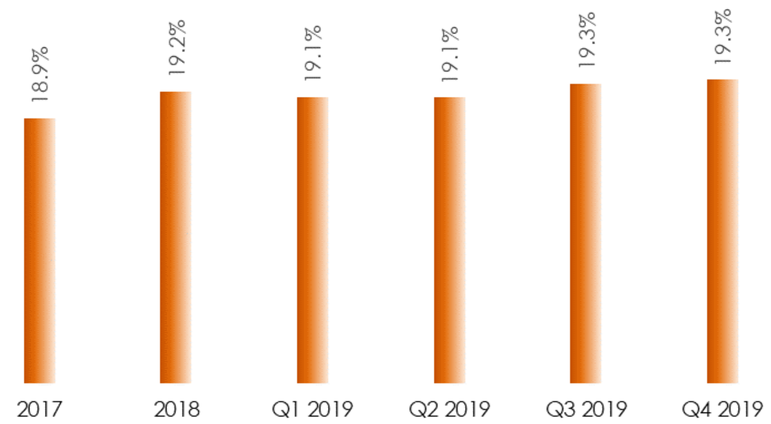


Considering liabilities to clients, in the past years the Bank posted an above-market-average growth of individual deposits. Compared to the previous year, individual deposits increased by RSD 33.9 billion in 2019, growing by 12.9%. The more dynamic growth of individual deposits than the market average resulted in a market share increase in this business segment from 19.2% in December 2018 to 19.3% in December 2019.

Graph 14 – Deposits of individuals (in RSD million)



Graph 15 – Market share in individuals' deposits



In conditions of low interest rates, clients have given significant trust to Intesa Invest Funds where, besides being able to generate an adequate return, constant availability of funds, reduced investment risk and professional asset management, the Bank provides unique expertise in the market to its clients, resulting in fundraising of EUR 53.2 million in 2019.

In the previous year the Bank implemented new business model in branches with exclusive goal to improve service quality and client satisfaction. New organizational and business model is based on both, improvement and increased functionality of branch layout and introduction of personal banking model for wider group of clients.

The event that marked the end of 2019 is introduction of new informational platform, Core system. Therefore, the Bank has created strong technological base that will further enhance digital transformation in all business aspects. The main goal is to improve internal processes and make them simpler and, in the same time, develop deeper interaction with clients.

Payment card business

During 2019, Banca Intesa maintained its leading position in payment card business with a market share of 22% in the number of delivered payment cards, 26% in the number of POS terminals, 54% in the number of internet POS terminals, as well as share of 26% in the total number of payment transactions completed in the country and abroad.

The number of transactions performed with Banca Intesa payment cards was on the rise in 2019 as well, both in the country and abroad, recording annual growth of 23% and 27%, respectively.

In terms of the POS terminals operations, including internet POS terminals, the number of transactions rose by 14%, while turnover volume increased by 17% in comparison with the previous year. In addition, Banca Intesa continued to harmonies and improve the acceptance network, constantly expanding the number of new users. Also, the entire network supports acceptance of contactless payment cards.

Moreover, the Bank has continued expanding the network of merchants where cardholders can pay in instalments, with increased share of instalment transactions in total sales. The number of transactions rose by 12% compared to the previous year, while the total sales volume increased by 14%.

In 2019, activities aimed at increasing the consumption of payment cards on the Internet and expanding the network of e-commerce traders continued, affecting the growth of the turnover of the Bank's e-commerce retailers of 80%, compared to the previous year.

The Bank continued with number of activities focused on the joined campaigne of the Bank and the merchants who provided significant discounts and benefits to Banca Intesa payment cardholders.

In 2019, it was introduced the possibility of contactless payment to all Banca Intesa payment cards, as well as the possibility of secure online payment, providing better user experience to clients.

Direct channels and e-services

In 2019, the Bank continued its strategic commitment to digitize significant number of processes. The introduction of digital innovation presumed complex set of activities that have a significant impact on both, the internal processes and the perception of clients of the Bank as a technological leader in our market.

During 2019 the main focus of the Bank was on the implementation of new information system (Flex Cube). The team has been dedicated to testing integration of a new core system of digital channels, analysing over 530 different testing scenarios in several test phases. After production, the team is intensely continuing to work on stabilisation of the system as a support point for colleagues from Banks business network and Contact centre.

The growth of digital platform users in both, individual and legal entities segment indicates that Bank in 2019, beside intense focus on implementation of new information system, succeeded to maintain the quality of services and customer satisfaction of digital clients.

Total number of active clients on the Intesa Online channel is close to 138 thousand in three-month period, while the number of users with login on monthly level is 105 thousand. In December 2019 total number of transactions carried out on the Intesa Online application was about RSD 4.8 billion, while the number of transactions in the same month reached roughly 420 thousand. The number and amount of transaction show the stable trend of increase on this channel in both, total volume and transactions type, i.e. payments, funds transfer and currency exchange operations.

Moreover, total number of active users of Intesa Mobi application have approached the number of 250 thousand in three-month time, while on monthly level this number exceeded 230 thousand. Transactions amount during December 2019 was around RSD 9.5 billion, while the transactions number reached 930 thousand. Compared to the previous year it is increase of 30% in comparison to the number of executed transactions YoY.

Around 40,000 clients, legal entities and entrepreneurs use the services of e-banking, while the share of payments executed through this channels is approximately 90% comparing to total payments at the Bank level.

In March 2019 there was a significant improvement in process of activation of e-banking service for legal entities, by introducing a simpler and more efficient customer activation process in the Bank's business network.

Banca Intesa's e-commerce service noted significant growth in all service elements in 2019. The number of merchants at the end of 2019 was 623, with close to 700 point of sales. Over 4 million transactions have been executed, which is 100% growth compared to the previous year. Total turnover was over RSD 15 billion, which represents an increase of over 80% compared to the previous year. Considering the law related to interbank fees, which came into force at the end of 2018, the Bank has adjusted the fees for e-commerce merchants, with an average commission of 1.65% at the end of 2019, compared to 2.29% at the end of 2018. Furthermore, at the end of 2019 net operating margin (from commissions) reached RSD 150 million, which represents a growth around 120% comparing to the previous year.

Business network

During 2019, intensive efforts were done to improve the business network through further implementation of the AGDM (Adopting Group Distribution Model) standards and assuring prerequisites for achieving goals defined by the AGDM project. Since the beginning of the project until the end of this year, 20 branches are aligned with modern trends in banking sector, as well as 13 self-service zones ("Zone 24"). New service model is implemented in 39 branches, covering 27% of the branches and 46% of Banca Intesa's net operating margin network. A total of 75 Upper Mass advisors cover 75,000 clients, representing 60% of total Upper Mass customer base.

Further implementation of ATS devices for depositing cash of legal entities continued, resulting in ATS network of 37 devices. By now, 51% of total amount of legal entities deposits is being placed on these machines in ATS branches, making 21% of total cash amount at the level of entire network.

Banca Intesa has successfully continued to renew ATM network, with the acquisition of additional ATMs and multifunctional devices. At the end of 2019, the ATM network counts 307 devices, out of which 109 external and 198 within Banca Intesa branches.

Customer survey confirmed quality of the new service model implementation, with high satisfaction score on all indicators among Upper Mass clients, such as meeting with an Upper Mass Advisor. Employees in rollout branches are fully accepting AGDM related changes, recognizing benefits for clients, but also their own work efficiency and carrier options.

At the Contact Centre, the year was according to expected trends, with focus on preparation for period after new core system role out in November. During stabilization period, additional inflow of calls was successfully handled due to several different methods applied (including IVR changes, external support during the peak periods etc.).

Small businesses and registered agricultural farms

- *Product and service quality upgrade*
- *Continual cooperation with renowned financial institutions*
- *Positive trend continued in all business segments*

In small business segment, which includes legal entities, entrepreneurs and registered agricultural farms 2019 was the year in which the Bank has committed its resources to business processes and prestigious product offering upgrade.

Dedication, innovation and individual approach are recognized in the market. Banca Intesa has confirmed its position as a market leader in the small business segment with a market share of 23.3% in the entrepreneur cluster. Moreover, market share of 12.0% in the agricultural segment, confirms that Banca Intesa is among the leading banks in the market in this segment of business.

During 2019 economic activity was supported by EUR 281 million of new production in the small business segment. These results can also be seen from perspective of growth in the number of financed clients that reached level of 28,000. Consequently, the loan portfolio recorded an increase of 6% (10% in the small business segment, and slight decline of 7% in the agricultural segment).

Small businesses

The Bank's operations in the small business segment are based on partnerships with small businesses. The aim is to provide them with a range of prestigious products and services that would facilitate their day-to-day operations and enable their faster growth, development and better competitiveness.

From 2019, small business customers have the opportunity to get more information about Intesa Invest and Intesa Leasing products and to apply for them through Bank's business network. Intesa Invest funds are an attractive and very interesting option for clients to channel their funds surplus as and represent an alternative to classic savings. During 2019, the market showed significant interest in investing primarily in the Dinar Investment Fund by donating its confidence to a professional team focused on stable returns. During 2019, EUR 24.9 million was invested into the funds with a final balance of EUR 14.4 million.

Appreciating the clients' time as one of their most important resources, the one-stop-shop offer is enriched with leasing products. Small business clients are enabled to obtain a pre-approved leasing product in a very short term based on the submitted invoice. Clients, with the assistance of a small business advisors, realized over EUR 4.4 million leasing placements.

Banca Intesa offers to the domestic economy extremely attractive lending options developed in cooperation with renowned international financial institutions, which cover businesses needs both for financing working capital and for the purpose of financing long-term business ventures. As a result of cooperation with the European Investment Fund (EIF), COSME loans are enabled to businesses since 2016 for financing working capital. They are characterized by favourable interest rates, extended repayment periods and relaxed collateral requirements. Thanks to these features, a more than EUR 55.5 million has been disbursed under this line. For investments in long-term innovative business projects, also in cooperation with the EIF, for the third year in a row, the Bank offers InnovFin investment loans particularly attractive due to the absence of a mandatory mortgages. It is invested more than EUR 2 million through this program. During 2019, the offer is expanded by additional products from the EIF line - EDIF invest and EDIF revolving, which represent additional products that complement attractive long-term investment options with relaxed security requirements. Through these products during 2019 businesses are supported by EUR 10 million placements.

Support to women's entrepreneurship represents a permanent commitment of the Bank. For the fourth year in a row segment of small business in cooperation with the European Bank for Support and Development (EBRD) offers to a female entrepreneurs a specially designed package of products that includes attractive loan with a fixed interest rate and relaxed collateral requirements, and additional benefits in areas of payment and digital banking. Through this Program in 2019 women in business have provided financial support for 355 business initiatives through EUR 3.6 million. In addition, as part of the promotion and support of women's entrepreneurship, Banca Intesa has taken a prominent part in the EBRD regional conference, highlighting a successful business practices of the Bank in this field, while successful entrepreneurial ventures of three Bank' clients were also rewarded.

Agriculture

As one of the leading banks in the Serbian market in terms of lending to farmers, Banca Intesa has supported registered farms with more than EUR 360 million since 2008, since operating in this segment.

Subsidised lending programme in cooperation with the Ministry of Agriculture Forestry and water management is very attractive lending option to farmers. Banca Intesa participated with around 17% in total amount and more than 23% in the total number of those approved loans. Moreover, the cooperation with the Guarantee Fund of AP Vojvodina continued with loans being granted to farmers based on credit lines contracted with this institution. As a result of all above mentioned activities, total loan portfolio reached volume of EUR 70.6 million, while total number of financed clients is 9,200.

The process improvements are continued with the aim to improve and raise the level of offer and customer experience in the segment of operating with registered agricultural farms. With the same idea, the Bank continued to work on opening new Farmer Centers and upgrading of existing ones, which proved to be extremely successful business models as specialized branches with a focus on servicing the needs of farmers.

In order to actively promote agricultural production, Banca Intesa has awarded the most successful farmers in three categories within the Intesa Farmer 2019 project: Intesa Farmer of the Year, Intesa Farmer Innovator and Intesa Young Farmer.

7. Corporate Banking

- Leader on domestic banking market
- Innovation as the basic postulate of successful business
- Clients' needs and expectations as the main drivers for business relationship improvement and achieving top-end performance

Macroeconomic indicators, during 2019, still show the preservation of the stability of the economic environment which contributed to the further growth of economic activity. Growth in economic activity has contributed to the budget surplus for fiscal 2019. Also, foreign and Government investments grew while the dinar exchange rate against the main currencies was stable with a tendency to strengthening. All of these factors have contributed to improving the overall business environment, increasing profitability and generating a stable business climate. In addition, during 2019, the country maintained its regional leadership in attracting foreign direct investment, which further contributed to the country's positive image, export potential and growth in business activity, as well as improving its credit rating.

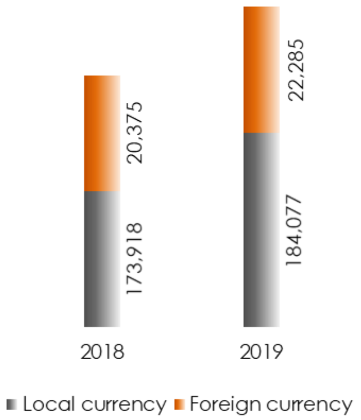
In a stable business environment, the National Bank of Serbia continued to pursue an expansionary monetary policy by further reducing its benchmark interest rate. Such monetary policy is in line with the low inflationary pressures and monetary policy of the European Central Bank, contributes to the growth of investment and economic activity in the country. The Government of the Republic of Serbia and the National Bank of Serbia continued to adopt measures and activities to increase dinarization and reduce foreign exchange risk, stimulating banks to make greater use of dinar sources of funds and growth of dinar loans in total loans, which resulted in further reduction of interest rate differences between dinar and foreign currency loans.

In the financial market, highly competitive conditions continue to prevail, as a result of the presence of a large number of commercial banks. Such conditions have significantly influenced banking products to be very affordable and thus provide easier and more favorable access to additional funds for businesses, both from their own bank sources and from various credit lines provided by domestic commercial banks in cooperation with foreign lenders.

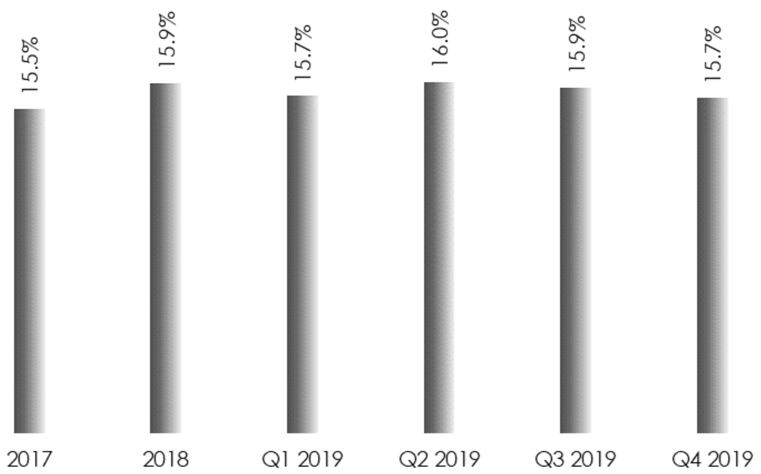
In 2019, the Corporate Business Division, in relationship with two renowned, international consulting firms, conducted an analysis of certain aspects of business in relation to competition. Although the structure of the banks in the two surveys was different, one involved 5 main competitors, while the other accounted for 13 banks, which represented 90% of the market, the results were similar. In both cases these independent analyzes have shown that Banca Intesa is a leader in many aspects of operations, both in terms of number of clients, volume of placements and different product categories, as well as parameters of profitability and efficiency of the sales network.

In line with positive market trends, the Corporate and SME Division continued with stability in operations during 2019 and recorded a 6.2% growth in the loan portfolio compared to the previous year, securing market share in total corporate loans of 15.7% at the end 2019. The annual growth of the credit portfolio, as well as new production of credit products, was above the average of the banking sector, which contributed to the preservation of the Bank's leading position in the business segment. With respect to deposit operations with corporate clients, the Bank is also constantly recording a dominant market position, resulting in a market share of 17.3% at the end of 2019. In the part of documentary business related to issued bank guarantees and letters of credit, relative stability is recorded comparing to previous year.

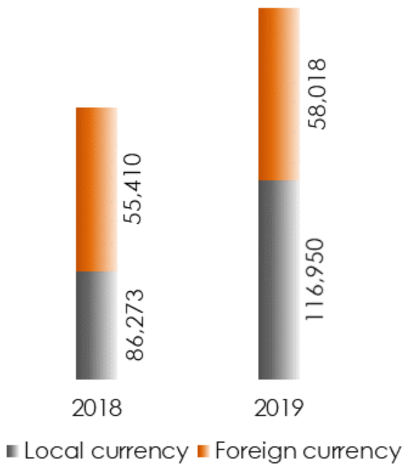
Graph 16 – Corporate loans (in RSD million)



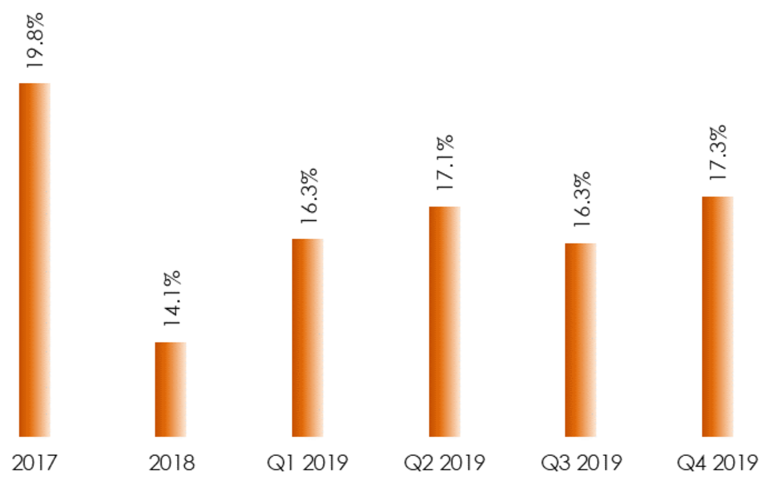
Graph 17 – Market share of the Bank in corporate loans



Graph 18 – Corporate deposits (in RSD million)



Graph 19 – Market share of the Bank in corporate deposits



The Corporate and SME Division is still the largest in the market by number of clients, as confirmed by various external surveys of the banking sector, and has about 7,000 active clients. This number represents more than three quarters of the total clients' base available on the market, out of which one half of clients are financed.

One of the key strategic pillars of the Bank, is continuance of the improvement of service quality and relationships with corporate clients. In this respect Bank introduces new ways of ensuring that clients' feedback is always heard and is relevant for further decision making. Owing to its strong client base and very good relationship with its clients, in order to collect objective feedback related to products and services, as well as sales network commitment and competences, the Bank continued with the *Instant Voice of Customer* project. This initiative is still focused onto customer satisfaction survey conducted among small and medium-sized enterprises, with the aim of using their answers and comments to optimize additionally the Bank's offer, business process and the quality of sales network in order to fulfil clients' expectations and satisfy their business needs.

During 2019, the demand of business entities for additional sources of financing continued to grow. In this respect in Corporate and SME Division growth was recorded in all segments, while the most significant growth was recorded in Segments for International clients and Large Domestic companies. In these segments, compared to the end of the previous year, the credit portfolio grew by 26% and 8.9%, respectively. Besides the nominal growth of credit portfolio, Corporate and SME Division has recorded the growth of both financed clients and clients active in other products.

In the Segment of Small and Medium-sized enterprises, beside annual growth of 7.5%, it is continued recognition of customer needs for the most efficient and simple credit process through the improvement of business processes, as well as attractive credit lines provided in cooperation with foreign lenders (EBRD, EIB ...). Thus, in 2019, a credit line was signed with the EBRD to finance the competitiveness of small and medium-sized enterprises. These are investment loans with a maturity of up to 60 months.

During 2019, the share of problematic loans recorded a further decline. It is expected that this trend will continue in the forthcoming period, which will further enhance the quality of the loan portfolio, as a result of responsible and prudent credit policy regarding the risks to which the Bank is exposed in its day-to-day operations.

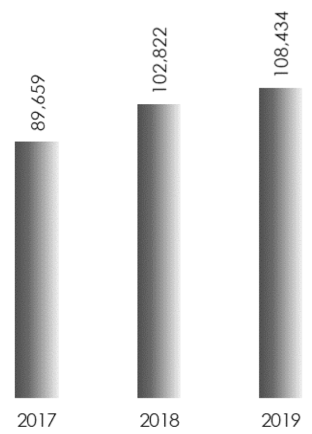
Transaction banking

The Bank continues to strengthen relationships with prominent corporate clients, providing them with higher-value services and, at the same time, promoting different transaction banking services. In line with mentioned, the Bank's clients are provided with the access to global transaction banking through ISP Group.

Moreover, the Bank continues to upgrade the *Payment Factory* service, which led to an increase in the number of leading multinational corporations that have decided to do business with Banca Intesa, relying on new services, extensive global network and wealth of experience. This service, which enables the centralization of payments, collection and reporting, is still unique on the domestic market.

The Bank continued to be committed to meeting specific needs of its diverse client base in export/import business with the aim of ensuring smooth performance of relevant trade and financing operations. In this respect, the volumes of documentary transactions as well as the number of transactions have maintained relative stability.

Graph 20 – Guarantees and other commitments (in RSD million)



Factoring

As an important model for providing short-term financing to clients, taking into consideration their needs, in 2019 the factoring new production volume reached EUR 151 million. Compared to the previous year, it is a growth of 22%, which resulted in a market share increase, confirming commitment to a proactive approach in providing services to customers.

In addition to planned and realized sales activities, activities related to support system and technical improvements continued. In line with this, during 2019 the Bank commenced with establishing of Factoring platform that will enable electronic connection of the Bank, suppliers and customers that will enhance swift and effective execution of factoring transactions.

Structured finance

Banca Intesa strives to be recognized and proven in the market as a reliable partner providing stable support to clients in project financing such as real estate and renewable energy sources.

The Bank has recognized the potential and advantages of this kind of financing and focused on clients and market leaders. Project finance activities were in line with the rules and principles of this kind of financing, bringing the multiple growth of the project finance portfolios, qualitatively and quantitatively. Project finance portfolio grew by 406% in 2019 compared to 2018 (EUR 90.9 million in 2019 vs EUR 22.4 million in 2018) while the total approved amount grew by 302% (EUR 172.9 million in 2019 vs EUR 57.3 million in 2018).

Additional benefit is that in 2019 new real estate projects were approved with good diversification (various residential and commercial real estate projects), totaling EUR 122.8 million while the main effects will be recognized in the 2020 result.

For 2020 the Bank will strive to additionally increase its profitability and volume of project finance portfolio through realisation of projects started in 2019. Together with this, Bank will increase market share through new qualitative projects that come from market potential and increase of relationship with domestic and international investors, together with optimisation of internal processes.

In addition, the Bank's operations comply with the Equator Principles, which ensure adequate risk management in financing transactions related to renewable energy sources.

EU Desk

Banca Intesa, as a financial intermediary, continued its successful cooperation with the European Investment Fund (EIF) on the implementation of available European Union programs, through which it provides easier access to financing for SMEs.

In 2019, the third annex of the COSME Agreement was signed, which, after three years of successful implementation, made available to clients an additional EUR 240 million in loans for permanent working capital with an EIF guarantee, raising the maximum available portfolio amount to a total of EUR 600 million. The offer has been further enriched through the WB EDIF Program, which has been well received by clients, extending the range of revolving loans and investment loans. With InnovFin now available to clients by the end of 2022, Banca Intesa is an absolute leader in the domestic market in terms of available portfolio size, number of clients supported, total sales realized, as well as the diversity of product offerings available through EU Programs.

The Bank pays close attention to the new Risk Sharing Programs, expected by early 2020, which, in cooperation with the EIF and other partners will open additional opportunities for financing more clients in different segments as well as individual transactions.

The current seven-year EU Financial Perspective ends next year, and the Bank has already undertaken the necessary activities to ensure continuity for each of these Programs through InvestEU (the Program that will be the successor to the current Programs in the next Financial Perspective).

8. Asset Management and Investment Banking

- The Bank continues to actively support the development of the bond market and the fiscal policy of the state, participating in primary and secondary auctions of government securities
- Maintained leadership position in foreign exchange trading operations
- Using education and product promotion timely, the Bank strives to eliminate foreign exchange risk for its clients

Further key policy rate reduction during 2019 and historically low interest rates in the Serbian money market resulted in a reduction of the yield on securities issued in the domestic market. In the previous year, the Ministry of Finance sold RSD 270 billion and EUR 646.6 million in primary auctions, which represents an increase in emission of local currency securities by 19.5% and increase of 14.5% in EUR denominated securities in comparison with 2018. In June 2019, the Republic of Serbia successfully issued the first government bond EUR-denominated on the international market in the amount of EUR 1 billion with 10 years maturity period. Yield was posted at 1.619% with strong demand in excess of EUR 6.4 billion. In the same time with the new Eurobond issue, it was carried out buy back option on Serbian USD Eurobonds. Republic of Serbia redeemed 1.1 billion Serbian USD Eurobond and saved over 3.8 billion dinars needed to be paid for the interest by the end of the payment period. In November, the Republic of Serbia sold EUR 550 million worth of ten-year Eurobond with recorded yield at 1.25% lower than initially posted in June 2019. This issuance was added to a EUR 1.0 billion issue of government securities first auctioned in June. In the same time on the international capital market Republic of Serbia redeemed SRB USD Eurobond in the amount of USD 589.7 million leaving behind USD 210.4 million notional amount to maturity.

In 2019, the Public Debt Administration announced buy back auctions and redeemed early RSD 30.1 billion of 3Y benchmark bonds, which mature in April 2020 and RSD 5 billion of 7Y bonds which mature in February 2022. Among the securities issued in 2019, the highest individual issuance volumes were reached on 3Y and 7Y local currency bonds, which were sold in primary auctions in the total amount of RSD 246.9 billion.

Regarding activities in the secondary market, investors were mainly focused on dinar bonds. Total turnover in both currencies (RSD and EUR) in the secondary market exceeded the amount of bonds sold in the primary auctions.

During 2019, Banca Intesa continually participated in primary and secondary auctions of government securities of the Republic of Serbia for its own account and on behalf of its customers, actively supporting the development of this key segment of the bond market and government fiscal policy. In terms of the interest rate decrease in the entire banking sector, there has been an increased interest of domestic and institutional clients to invest in securities as an alternative to deposit operations. In this regard, Banca Intesa applied a proactive approach in informing clients about the possibilities of investing in government securities and introduced its brokerage services to all interested institutional and individual investors.

During 2019, the Bank's portfolio remained diversified, so, apart from debt securities issued in domestic market in the Republic of Serbia, it includes dollar-denominated Eurobonds of the Republic of Serbia.

Serbia's risk premium, measured by EMBI, stood at 159 bps at end-2018 and decreased to 35 bps at end-2019. In December 2019, Serbia's risk premium recorded its historic low, standing at only 5 bps and designate the biggest fall in the region, indicating that the decline was also driven by domestic factors. This confirms investors' confidence in favorable macroeconomic prospects marked by years of internal and external imbalances and favorable growth prospects.

In September 2019, Rating agency Fitch upgraded Serbia's Long-Term Foreign and Local-Currency Issuer Default Ratings from BB to BB+. In December 2019, rating agency Standard and Poor's raised Serbia's credit rating to BB+ from BB, a step from investment grade. The outlook remains positive, which is a strong signal that further rating upgrades are possible in the short run.

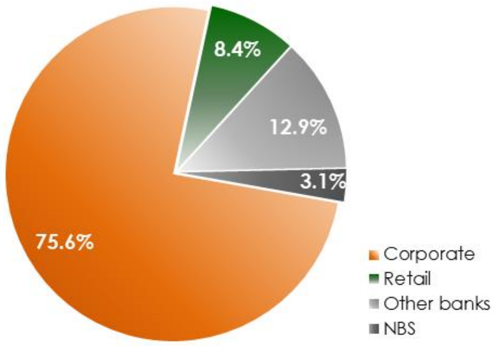
In 2019 Banca Intesa continued to be the leading bank regarding the offer of financial instruments for dinar and foreign currency liquidity management. Currency swap contracts and dinar-denominated bonds of the Republic of Serbia are available to customers, primarily intended for investors who prefer to completely or partially hedge the foreign exchange risk.

Banca Intesa retained its leading position in foreign exchange trading operations, with a market share of 13.3% in 2019. The Bank provided the EUR-NET Exchange Rate to its clients, which applies in transactions through the Intesa Mobi application and Intesa On-line e-banking service and represents the most favorable exchange rate since it follows trends in the interbank foreign exchange market in real time. During 2019, the volume of EUR-NET transactions posted a significant increase of 18.9%

Table 1 – Foreign exchange trading (in EUR million)

	2013	2014	2015	2016	2017	2018	2019
Corporate	3,058	2,772	2,915	3,340	3,567	4,012	**4,418**
Retail	242	229	226	321	379	431	**492**
Other banks	1,510	899	1,313	914	1,012	693	**754**
NBS	73	157	94	99	111	90	**183**
Total	4,883	4,057	4,548	4,674	5,069	5,226	**5,847**

Graph 21 – Customer shares in foreign exchange trading



The Bank continued to educate clients in the field of modern banking services, as well as to promote products aimed at enabling timely management of financial risks in the business, primarily foreign exchange risk.

9. Corporate Social Responsibility

- Banca Intesa continued to make efforts to further strengthen its corporate culture
- Financial inclusion as an important part of Banca Intesa's corporate social responsibility strategy
- In order to protect the environment successfully, several projects implemented to reduce direct negative environmental impact

Banca Intesa continued its strategic commitment of constant improvement of its corporate social responsibility (CSR) practices in 2019. The Bank provided support to the community by focusing on corporate philanthropy projects, but also by strengthening its corporate volunteering culture, supporting financial literacy initiatives, assisting cultural projects and cultural heritage conservation and a number of initiatives of a wider community and humanitarian character as well, through a direct financial support.

In 2019, the Bank responded to the needs of the market by creating ethical products and services, some of which stood out because of their social and environmental importance, while at the same time, taking care of customer satisfaction. In the environmental protection segment, the Bank has successfully implemented projects to reduce direct negative environmental impact, but also sought to reduce, through the application of international regulations in the process of managing socio-environmental risks in the credit process, the indirect impact of its business on the environment.

However, motivated employees are a key prerequisite for achieving good business results and strategic sustainability goals. With this in mind, in 2019, Banca Intesa continued its ongoing efforts to further strengthen its corporate culture, putting into effect various employee satisfaction projects, providing equal opportunities for development and advancement for everyone, thus creating an important sense of belonging to the Bank and the entire Group.

COMMUNITY

Corporate volunteering

Responsible business practices and responsible community relations would not be possible without the developed internal culture of Banca Intesa and the responsibility embodied in Bank's volunteers who understand that supporting those who need it, is also the most effective way to care for society.

Since 2013, the year when the corporate volunteering program „Intesa from the Heart“ was launched, the Bank has aimed to contribute to the community by donating time, talent and knowledge of its employees. Within this program, Banca Intesa also organized several volunteer initiatives in 2019 that brought together colleagues from all Regional Centers.

In 2019, the Bank also encouraged employees to support initiatives of social importance through individual volunteer programs. In cooperation with the United Nations Global Compact and the National Bank of Serbia, our volunteers gave a lecture specifically thought out for professors of high schools of economics, on the topic of “Benefits of Investing in Investment Funds”. At the same time we celebrated European Money Week, as well as the World Savings day, with the Association of Serbian Banks and Volunteer Lectures in Primary Schools.

Corporate philanthropy

Constantly following the needs of the community, in 2019, Banca Intesa allocated over RSD 10.2 million for philanthropic purposes (including in-kind giving), aiming them as a direct financial support for the implementation of projects in the field of culture and preservation of cultural heritage, as well as initiatives of social and educational importance.

Among the most significant initiatives are activities supporting the exhibitions and projects of the History museum of Serbia, the National Museum and the Museum of Contemporary Arts; renovations of the Holy Trinity church in Belgrade; support of the National Theater; assistance with the work of the National Organization of Disabled persons of Serbia; aiding the project for helping children without parental care of The Novak Djokovic Foundation and SOS Children's Villages of Serbia; assisting with the renovation of the premises of the Sremcica Social Institution for Children and Youth, as well as participating in humanitarian actions through fundraising with partner organizations such as BELHospice.

Numerous local cultural events such as the Smederevo Autumn, Zoran Radmilovic Day, Mokranjac Days, etc., were also supported, and initiatives to improve the life and health of the community were aided as well.

Participation in initiatives of importance for the improvement of education were realized through the support of the Center for Serbian Studies, Faculty of Philosophy, University of Belgrade, as well as the support of the Faculty of Law, University of Belgrade for the participation of students in competitions. During 2019, the Bank donated 345 used computers to educational, health and social institutions in Niš, Leskovac, Vranje, and throughout Vojvodina.

In addition, the Bank continued to help create a stable and independent financial support mechanism for the Paralympic Committee of Serbia, supporting the Committee with almost RSD 3.5 million in 2019.

As part of the traditional New Year's project "Wrap a gift, make someone smile", Banca Intesa, in cooperation with several civil society organizations, organized the first humanitarian Christmas fair for employees in the Bank’s headquarters, thus raising around RSD 250 thousands from the sales of handmade items, and collecting more than 300 kilograms of food and other goods in donations, all intended to support the most vulnerable social groups from all over Serbia. Banca Intesa launched this project as a joint employee initiative in 2010, and since then, thousands of packages and direct financial aid donations of more than RSD 2.6 million were collected exclusively by employees and delivered to various initiatives, institutions for social and medical care of children across the country.

During the year, the Bank successfully continued its strategic support of the Blood Transfusion Institute, organizing several voluntary blood donation activities on its premises, during which more than one hundred units of blood were donated by employees.

The significant social contribution of the Bank in the area of community support was also confirmed and recognized by the most renowned CSR award – Virtus. The award for the recognition of the company's wide philanthropic contribution was awarded to Banca Intesa by the Trag Foundation in cooperation with the United States Agency for International Development (USAID), the European Union, the Balkans' Democracy Fund, the S.C. Mot Foundation and the Rockefeller Brothers Foundation. The purpose of this prestigious award is to recognize and publicly acclaim companies, businesses and individual donors who strategically and in a long term, support the development of communities and society as a whole.

Financial inclusion and education

In 2019, financial inclusion continued to be an important part of Banca Intesa's corporate social responsibility strategy. During the year, the Bank also sought to make financial services equally accessible in economically underdeveloped parts of the country. The Bank ended the year with 20 AGDM branches offering advanced customer experience for clients by enhancing the advisory capacity of branch employees, who now, instead of simple banking transactions, are engaged in sales activities, thus strengthening partnerships with clients and helping them to responsibly plan their personal finances. Furthermore, this concept promotes and encourages an increased number of digital tools for banking, meeting further the clients demand and the dynamics of modern life. When renovating and opening new branches, Banca Intesa pays special attention to accessibility of facilities, that is, adjusting them to access people with disabilities wherever possible.

Additionally, the Bank remained committed to disseminating knowledge of economic and financial issues as well as promoting a culture of informed choice for its customers and the wider community. Celebrating World Savings Week, Banca Intesa continued its financial education program for the youngest, dedicating it to the importance of rational management and saving of resources through the promotion of a new concept of circular economy. A series of workshops entitled "Less Garbage - More Luck", were organized in November for about 120 first year students of St. Sava Elementary School in Pancevo, who attended a class dedicated to environmental protection and waste reduction. After the class, students were learning about recycling and circular economy through game and creativity. This concept was also introduced to the children of our employees in a specially organized workshop.

In addition to other inclusive products in 2019, it is important to emphasize the Bank's support to the Women's Entrepreneurship Development Program, within which the Bank continued to implement the project "Women in Business", with the allocation of funds from the EBRD credit line. During the year, 355 loans were approved for a total amount of approximately EUR 3.6 million.

ENVIRONMENT

Environmental protection is one of the pillars of sustainability to which Banca Intesa has been committed for years. With the same intensity as in previous years, 2019 was also marked by unremitting efforts to reduce the use of resources in the everyday course of business. Among other things, for the World Environment Day our Bank launched an internal „Greentesa" program aimed at promoting environmental conservation and responsible environmental behavior of employees. On the day of the launch, specially designed waste collection boxes were set up in the Bank's Main building, which began the process of increasing the amount of recycled materials generated within the Bank, primarily of paper, disposable plastic and batteries. The „Greentesa" initiative aims at reducing the consumption of resources - water, electricity, reducing the use of lifts while promoting walking, the use of stairs and making healthy lifestyle choices overall - and will continue in the coming years.

The purpose of marking World Environment Day (WED day) was to draw the attention of the internal public to the importance of environmental conservation and sustainability, as well as the idea of mobilizing individuals with local activities in order to jointly preserve and improve the quality of the natural environment. For several years now, this Global Initiative has been supported by the Home ISBD Division through various activities in its member banks.

With regard to the application of the principle of responsible financing, while taking into account the indirect impacts that the Bank has on the environment by providing financial support to society and individuals, as well as the potential risks that could be disturbed by social or environmental balance, Banca Intesa continued to apply international regulations throughout 2019 and a modern socio-environmental risk management system in the lending process.

WORK ENVIRONMENT

All activities related to the development and education of employees in 2019 have come up from the developmental needs of the employees so that professionalism, pursuit of excellence, development of an innovative way of thinking with a constant focus on clients, will continue to be the Bank's strategic focus.

With this in mind, over 13 days of training per employee have been carried out on average this year, together with mentoring services organized for each new employee. In total 23,496 days of classroom training were conducted, as well as more than 17,232 days of tutoring. Each employee attended an average of 6 programs on the e-Learning platform, and learning through the e-Learning system was done through 16 different e-Learning programs.

Employee development programs were also continued. The most significant of these in 2019 was the Constellation project - the introduction of a new core system for the needs of which as many as 3,363 employees received classroom training. At the same time, a number of specific programs for the various employee structures that have been developed in recent years have continued, including an innovative program of SBA academies to educate employees who are work or will be working with small businesses.

Activities concerning the two talent programs were also continued in 2019 - The international talent program within the Intesa Sanpaolo Group, in which the selected employees gain international experience over three to five years as well as additional knowledge in training conducted by the world's most eminent experts, as well as Bank's program aimed at developing the leadership of recognized managers called the "Treasure Leadership Talent Program" (TLT), which was finalized this year. This program features a specific approach to talent development, based on individual profiles and career goals.

Students in the final years of their studies had the opportunity to gain practical business experience by being part of the third generation of students attending Bank’s junior program, which is based on mentoring, specific work assignments, rotations and training of young colleagues.

In addition to investing in the professional development of employees, the Bank continued to recognize their personal needs, so that all full-time employees are not only covered with health insurance that includes treatment abroad in cases of serious illness, but they now also have the option of free medical examinations as well as specialized medical care, if necessary.

As a confirmation of the efforts of its gender-sensitive strategies and of the implemented initiatives concerning women's empowerment in the company and in the local community, Banca Intesa was awarded and recognized as one of the most gender-sensitive companies in the domestic market, by the Women’s Business Association of Serbia, at the end of 2019.

Projects for the children of employees

For the 15th consecutive year, Banca Intesa made it possible for 54 children of the Bank's employees to spend two weeks in Italy during summer holidays. Also, in cooperation with the Foundation for International Educational Exchange – Intercultural, the Bank once again supported the one-year study abroad program.

Sport competitions are a part of regular activities conducted by the Bank and Intesa Sanpaolo Group with the aim of getting to know each other's employees' children and strengthening team spirit. On this occasion, during 2019, roughly 160 children of employees participated in the Italian football camp, the International ISBD Children's Olympics, the Milos Teodosic basketball camp and other sport events.

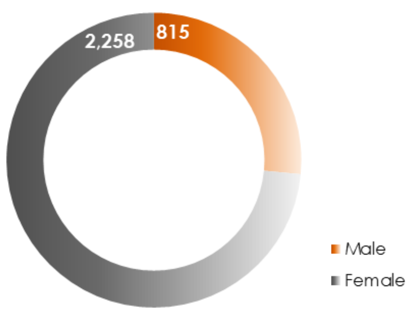
Educational, age and gender structure

The basis of the Bank's business success in 2019 was the mix of two energies – that of the newcomers and young colleagues on one hand, and the experience of senior colleagues, on the other.

Table 2 – Employee qualifications

Qualification level	up to 30 years	30-40 years	40-50 years	50-60 years	over 60 years	TOTAL
I				1		1
II				1		1
III		2	13	4		19
IV	95	157	247	181	9	689
V	1		4	2		7
VI	54	299	208	65	7	633
VII/1	273	744	539	133	12	1,701
VII/2		7	10	2	1	20
VIII		1		1		2
Total	**423**	**1,210**	**1,021**	**390**	**29**	**3,073**

Graph 22 – Gender structure



RESEARCH AND DEVELOPMENT ACTIVITIES

Customer satisfaction management

For Banca Intesa, customer satisfaction approach, defined through "Listening 100%" program, represents continuous process of listening to customers' needs through feedbacks received from the customers, whether they come in the form questions, complaints, suggestions or compliments and finally, through customer satisfaction surveys. However, these feedbacks represent only the beginning of continuous improvement process – feedbacks are thoroughly analyzed so that customers' needs are adequately interpreted. By doing so, customers actually become initiators of improvement activities. If we are to judge by the customer satisfaction surveys' results, the conclusion can be drawn that customers are successfully included in the development and improvement of products and services, definition of communication strategies, business network development but employee education and training as well.

What separates 2019, from the customer satisfaction surveys perspective is the wish to dedicate equal attention to all customers' segments. Therefore, 2019 could be described as the year with highest number of customer satisfaction surveys, which included all Consumer segments and sub-segments, than Small Business segment, SME and Large Corporate and Multinational segments. The methods that are in use for several years now, primarily European Customer satisfaction Index (ECSI) which is scientifically tested and affirmed, Mystery Shopper and focus groups aimed at customer satisfaction and experience measurements and finding the best ways to respond to customers' needs and expectations. Mystery Shopper survey is significant, among other things, because it enables each branch to be analyzed as a separate entity, so once results are obtained, "individual" improvement actions are conducted which directly influences customers' satisfaction and experience. Considering the success of such approach in service quality analysis, within 2019, it is expanded to a "market" level, meaning that Benchmarking Mystery Shopper was conducted. Namely, the approach enabled a little "sneak preview" of the branches of the Bank's competitors and accordingly an insight in the advantages and disadvantages, but at the same time position of the Bank and room for further improvement, bud also good things that should be nurtured in the future as well.

The approach toward customer satisfaction and improvement through focus groups, which are traditionally used as a tool in marketing researches, proved to be excellent source for definition of customer needs and expectations, but moreover the right place, i.e. method for their suggestions and requests to be listened but also acted upon.

Within 2019, it is continued with researches based on "instant feedback" method. The quality of this type of surveys lies in the speed – customer is contacted soon after interaction with Bank's employees, thus enabling feedbacks to be collected when experience is "fresh", which, in turn, enables swift reaction in removing the causes of dissatisfaction, but also improving satisfaction of each particular customer.

These results represent an excellent basis for better understanding of customer needs and expectations and consequent introduction of adequate improvements business processes, products and services. High customer satisfaction indices, NPS (Net Promoter Score) scores, positive feedbacks, confirm that the Bank managed, not only to build, but also to maintain strong relationship with its customers. At the same time, these results oblige the Bank to continue to build relationships based on mutual understanding and their "directions".

Product and service development

The Bank's development activities in 2019 have been focused on digital innovation and implementation of the new information system. Despite intensive involvement in this project, the Bank managed to maintain the quality of its products and services.

Production of the new information system created also space for the development of brand new functionalities in a field of client's cash management. The development of payment functionality that involves self-service devices, for individuals and legal entities, represents the way for reaching one of the main goals of the Bank, migration of the clients from branch to digital channels. It is estimated that this functionality, which is expected to be fully live in the beginning of 2020, will additionally contribute to the efficiency of cash management and increase customer satisfaction.

BizMobi service fully fulfilled expectations, considering that in 2019 the number of customers who activated the service reached 10,262 clients. The number of transactions carried out through BizMobi applications shows an upward trend of 17% per month. In December, through BizMobi applications clients have executed over 76,000 transactions, in amount of RSD 5.3 billion.

The Bank is continuing with implementation of regulatory project „Instant payment system on point of sale" which will enable our customers to execute payments via mobile application by scanning the QR code from POS terminal or any other merchant devices, or from the e-commerce point of sale. Clients will also be enabled to generate QR code within the mobile application, and in this case, the instant payment will be executed when the merchant scans the generated QR code. Instant payment at point of sale implies money transfer from the clients' bank account to the merchant's bank account in a few seconds. In this way, the Bank is supporting the cashless payments, at the same time providing lower costs for merchants and simple new functionalities for clients through existing mobile applications. Accordingly, the Bank will continue to support strategic projects of National bank of Serbia and maintain the key catalyst role in the implementation of digitalisation in our country.

10. Risk Management System

- *Historically low NPL achieved through the consistent implementation of efficient work-out strategy, improved credit approval and underwriting process, use of credit ratings and early warning systems as well as proactive management of deteriorated credit positions.*
- *Improved credit portfolio quality through the better rating distribution and higher coverage of portfolio by collaterals.*
- *Upgraded IFRS9 provisioning methodology through development and implementation of internal stress test models including macroeconomic (forward-looking) factors in risk parameters estimation.*
- *Successfully implemented new definition of Default in accordance with NBS Guidelines for the Identification of Default, and EBA Guidelines on the application of the definition of default.*

Banca Intesa continuously identifies, assesses, monitors and controls risks in compliance with the national and international banking, supervisory and accounting regulations, and ISP Group guidelines, providing integrated, prudent and consistent risk management system. The Bank’s Board of Directors established by its enactments an appropriate risk management and internal control system, which includes different corporate governance bodies and committees: – the Board of Directors, Executive Board, Audit Committee, Risk Management Committee, Problem Asset Committee (PAC), Credit Risk Governance Committee (CRGC), Assets and Liabilities Committee (ALCO), Operational Risk Committee (ORC) and Integrated Control Coordination Committee (ICCC). The functioning of the system is regulated by the policies and procedures adopted individually for each material risk type. In 2019, the Bank established new governing body, Risk Management Committee, with the primary goal to advise the Board of Directors on the Bank's overall current and future risk appetite and risk strategy and assist the Board of Directors in overseeing the implementation of that strategy. Risk Management Committee regularly monitors all material risk exposures through Tableau de Board of risks as well as single risk reports (Pillar I framework). Also, it has insight in ICAAP results, stress tests and other particular analyses of risk management function that report on risk profile and trends of bank’s business.

In addition, new organizational unit - Enterprise Risk Management Office has been formed under the CRO within the Risk Management Department with the main role to provide integrated approach in the preparation of ICAAP (Internal Capital Adequacy Assessment), ILAAP (Internal Liquidity Adequacy Assessment), Recovery Plans, integrated stress tests, setting and monitoring of RAF limits, assessing criticalities in conduction of the risk management functions and other assessments that combines multiple types of risk.

In order to maintain a system that complies with the highest quality standards and supports the decision-making process of governing bodies, the system underwent improvement during 2019. The enhanced risk management system continues to rely on the axioms of independence of the risk management function from risk-taking centres, promptness of information flows that support the decision-making process, as well as transparency and correctness of submitted information.

Main objectives of the risk management process are related to the protection of the Bank's capital and its optimal allocation, increase in economic value for shareholders, monitoring of risk limits and/or risk measures for all identified risks. The existing system of limits, defined in the Risk Appetite Framework (RAF), gives the highest priority to the monitoring and controlling minimum requirements related to capital adequacy, liquidity and operational risks. In addition, the RAF system covers credit concentration limits, limits of exposure to interest rate risk and funding limits. The indicators of profit stability, macroeconomic stability, credit quality and compliance and AML risks of the Bank were introduced as additional RAF measures. The Bank ensures the compliance of the strategic guidelines defined in the business strategy, capital plan, operating plan – budget and recovery plan, with the Bank's risk profile defined in the RAF system.

SREP (Supervisory Review Evaluation Process) is regular activity of the Supervisor performed according to Pillar 2 requirements of Basel Capital Accord (Basel 3). SREP report presents results of comprehensive risk assessment of a bank. The ultimate result of a SREP process is a specific requirement for additional capital buffer for a bank which should cover Pillar 2 risks and risks of all identified deficiencies in corporate governance, controls, information system, data quality and so forth.

The main conclusions of Supervisory Assessment given in 2019 were: that business model is sustainable in short - term and long - term and that it carries a Medium - Low risk to its business, Deficiencies related to Corporate governance and internal controls system carries Medium – Low risk, Risk related to capital is generally assessed as Medium – Low, Regarding credit risk, market risk, interest rate risk, operational risk which affect solvency and reliability of ICAAP, the Bank's exposure is assessed as Medium-Low risk, Risk related to liquidity is generally assessed as Medium – Low.

Consequently, in 2019, NBS has determined an additional regulatory capital requirement (SREP add-on) at the lower level compared to the previous SREP add-on rate.

Through the IFRS 9 project, the Bank developed and implemented a methodology and models for stage assignment and expected credit loss calculation (asset impairment). In accordance with the methodological approach proposed by the Parent Bank, the Bank has implemented the business model and SPPI tests of all balance sheet positions in order to properly classify assets and liabilities. The IT solution for classification and provisioning has been upgraded accordingly. Apart from regular annual update of risk parameters used for expected credit loss calculation, the Bank continued to further improve the methodology in 2019, through the development and implementation of internal stress test models to include projected macroeconomic impact on risk parameters and the level of expected credit losses.

The Bank has successfully implemented the new definition of Default (in accordance with NBS Guidelines for the Identification of Default, and EBA Guidelines on the application of the definition of default under Article 178 of Regulation (EU) No 575/2013) incorporating new regulatory requirements into its rules for the classification of credit exposures.

The AIRB Implementation project, whose aim is to develop and implement an advanced internal credit measurement system, is being conducted under the supervision of the Parent Bank. During the development, the models are subjected to the approval process comprised of several steps (formalised through pre-defined milestones), controlled by the ISP Foreign Banks Credit Risk Management Department (FBCRM). The Bank has already covered most of its credit portfolio by the internal credit rating system (corporates, small businesses, individuals, banks). The bank is in last stages of development of LGD and EAD models, which implementation will enable the Bank to have the full insight and apply for the approval by the supervisor to use models for regulatory purposes as well.

Risk management policies and procedures have been revised and updated for the purpose of their alignment with amendments of the domestic and international (EU) regulations, as well as the amended guidelines and policies of the Parent Group, recommendations/findings of the Bank's Internal Audit, Internal Validation and the NBS.

Credit risks

Credit risk is monitored on a number of levels: by assessing customers' creditworthiness prior to loan approval, monitoring regular settlement of their liabilities and creditworthiness during the whole credit lifecycle and also by collecting and managing due receivables.

During the year, the Bank performed regular monitoring and reporting activities, annual review of internal acts regulating the credit risk area and activities related to supporting the governing bodies in the decision-making process. During 2019 the bank has made important improvements of the risk management system.

The Bank has significantly decreased non-performing loans. The NPL volume and ratio were reduced to historical low outperforming the levels expected and defined in the Credit Strategy, Budget and NPL plan. Non-performing loans were reduced from EUR 163 million to EUR 101 million, or by 38%. The NPL ratio was reduced from 5.37% to 3.05% or by 2.32 percentage points. NPL reduction was a result of consistent implementation of effective workout strategies (transfer to off-balance, collection, return of NPLs to performing loans, portfolio sale), improved credit approval and underwriting process, use of credit rating and early warning systems, as well as proactive management of deteriorated credit positions;

New Definition of Default has been introduced. New regulatory requirements (regarding the new default definition) has been implemented respecting the timeline defined by the Parent Bank. The main changes brought by new regulation are: modification on the relevant thresholds for days past due calculation (the relative threshold of 1% on client level, and absolute threshold of RSD 1,000 or 10,000, depending on the client's regulatory segmentation), introduction of the probation period for exiting default status (the probation period lasts minimum 3 months from the moment that the obligor was no longer past due more than 90 days and has no active any other trigger of default). The implementation itself was carried out through the upgraded version of existing IT solution, enriched with new regulatory-compliant functionalities.

Also, further improvement of IFRS 9 models used for Expected Credit Losses calculation has been made. The major methodological improvement refers to implementation of internally developed PD satellite model instead of EBA stress test coefficients for the purpose of the macroeconomic conditioning of PD (inclusion of forward looking elements). In addition to this, the implementation of internal LGD stress test model (which was developed in 2019) is expected in the first quarter of 2020.

The Bank has implemented regulatory changes issued by NBS that came into force during 2019 (amended Decision on Capital Adequacy of Banks, amended Decision on the Classification of Bank Balance Sheet assets and Off-Balance Sheet Items, new Decision on Management of Concentration Risk, Guidelines for the Identification of Default). The implementation comprises update of the corresponding internal acts, adjustments of data marts, IT procedures, calculation engines and reporting system. The main changes introduced by the new regulations are dismissal of special reserves for loan losses, introduction of new deductibles from the regulatory capital, inclusion of new classification criteria (Debt-to-Income ratio - DTI>60%), and closer monitoring and limitation of cash, consumer and other loans to the individuals with contractual maturity over 2,920 days.

Parent bank has launched a multi-year project with intention to extend its Credit Risk Appetite (CRA) CRA framework to all subsidiaries, including the Banca Intesa Beograd. The main objectives/benefits of the project are: optimized credit strategies considering CRA as an additional driver, effective risk-based credit management, enhanced monitoring of credit portfolio quality, harmonized Group framework for assessing credit risk. CRA will be embedded in the RAF for 2020 through setting a new limits within which bank's business may operate. The CRA is applied to performing counterparties belonging to the regulatory segments Corporate. The idea is to divide clients into three clusters based on the Economic Value Added contribution to the bank. Clients which returns positive EVA to the bank, in both normal and stress conditions, are marked as "green". Clients which has positive EVA only in normal business conditions are classified in "yellow" cluster. Clients with negative EVA are marked as "red". The bank will define its credit risk appetited for exposures to yellow and red clients/clusters. There will be maximum amount of credit exposures that could be approved to yellow and red clusters, separately. Exposures to green clients would not be limited.

Internal reassessment and monitoring of value of real estate collaterals has been introduced. The bank has started with internal reassessment and statistical monitoring of residential real estate. Internal appraiser determines the market, construction and liquidation value of the real estate by applying a "desk-top" model of revaluation to each individual real estate in the portfolio that is the subject of the revaluation. Statistical monitoring of value of real estate collaterals is performed by applying the index of change in the value of real estate to the market value of residential real estate from the valuation of authorized appraisers. After quality controls the final value of the property from statistical monitoring is adopted. Properties that do not pass f controls are subject to revaluation by a certified appraiser. In addition to this, Bank performed monitoring of commercial real estate collateral based on publicly available statistical data. Purpose of monitoring is to determine whether there is a significant impairment of the market value of the property that serves as collateral in Banca Intesa Beograd. If available data indicates that the value of the property may have declined materially relative to general market prices, properties are subject to revaluation by a certified appraiser.

Also, improvement of IT system for consolidated credit risk and financial reporting (Finrep and Corep) to the Parent Company has been conducted.

In addition, improvement of the first and second-level credit controls performed by the Credit Quality Monitoring and Control Office, Credit Portfolio Analysis and Administration Department and Rating Desk, has been established.

During 2019 the Bank continued working on resolving recommendations of the National Bank of Serbia based on the diagnostic control of BIB Corporate FIRB request, included in the Action Plan. Most of the recommendations relate to the methodological framework for model development and implementation, which has been implemented by updating internal regulations. It is expected that the remaining findings will be resolved by the first quarter 2020. The reason for longer time to complete those particular recommendations, is their dependence on the implementation of the new Core System.

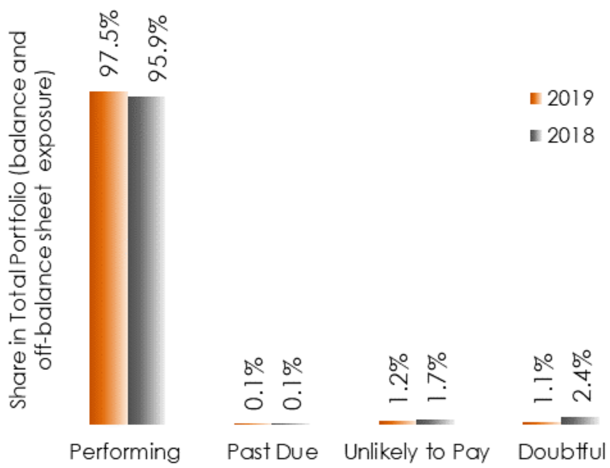
Within RADAR project, aiming to align internal risk data aggregation and reporting systems with the BCBS standard 239 (Principles for Effective Aggregation and Risk Reporting), the most important risk processes and reports are documented through the completion of defined templates that show the connections between risk data. Data control system over significant data for calculation risk measures has been improved (RWA, expected loss, ratings, default status, IRB segmentation, RAF limits, ICAAP). Data ownership, as well as business definitions of main risk measures, which are the basis for risk analysis processes from various aspects, are recorded in the Data Governance application, as the central business dictionary.

In 2019, Banca Intesa continued developing and updating its internal credit rating models for the purpose of converging to the standards of advanced credit risk measurement standards. PD models for Corporate, Individuals and Specialized Lending (SL) have been revised. IFRS9 lifetime PD models have been updated by improving the methodological approach and using of internal PD stress test models for estimation of forward looking components instead of EBA coefficients. The early warning models (EWS Corporate and Small Business models) have been updated. New SME Retail model has been developed that will replace current small business model for double-entry bookkeeping and new rating master scale for small business model for single-entry bookkeeping. Model for Registered Agriculture Households has been developed for the first time and will be used in credit process approval for this customer segment. Model for assessment loss given default and exposure of default (LGD and EAD models) for Individuals clients are in the final stage of development.

During the Corporate PD and SL model revision, recommendations of the National Bank of Serbia and Internal validation were considered and implemented.

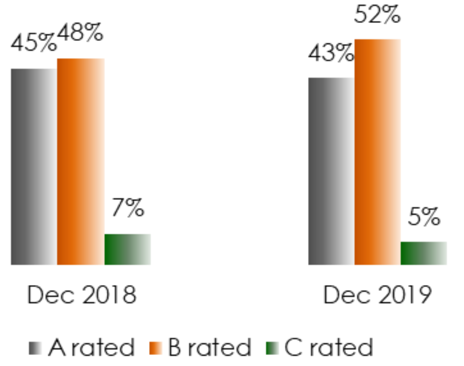
Development of a new methodology for calculating Cost of Risk as component of interest rates for loans to Corporate, SME and SB clients. The most important change in the new methodology is using Probability of Default (PD) for the purposes of IFRS 9, including forward looking elements into the PD estimation (macroeconomic conditioning), in order to consider the expectations of change of PD, linked to macroeconomic environments that can occur in the future years with respect to reporting date. IFRS 9 PD multiplied by LGD is used for calculating estimation of average expected losses during repayment period. The second relevant change in the new methodology is including component Cost of Capital through which unexpected losses are included in final interest rate.

Graph 23 – Credit portfolio quality by class (balance and off-balance sheet exposure)

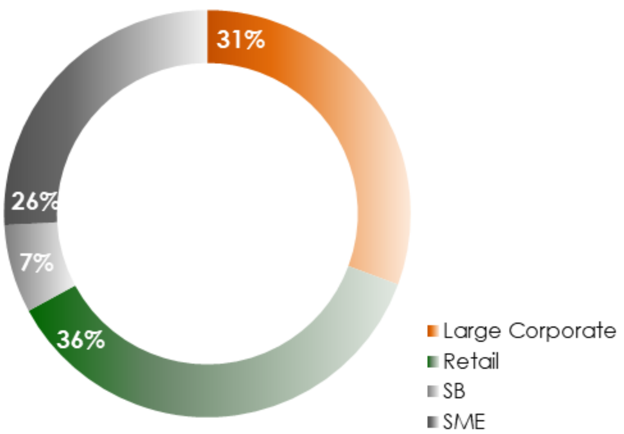


Apart from significant NPL reduction, the Bank also posted a large increase in new production. Credit portfolio growth was not achieved at the expense of higher credit risk; instead, the portfolio quality measured by rating distribution was improved owing to a consistent application of the Credit Strategy and Credit Policy. Low-risk clients account for 43%, medium-risk clients account for 52%, while high-risk clients account for 5% of all internally rated clients. If compared to the previous year, share of exposure related to good rating categories (A and B) increased by 2 percentage points.

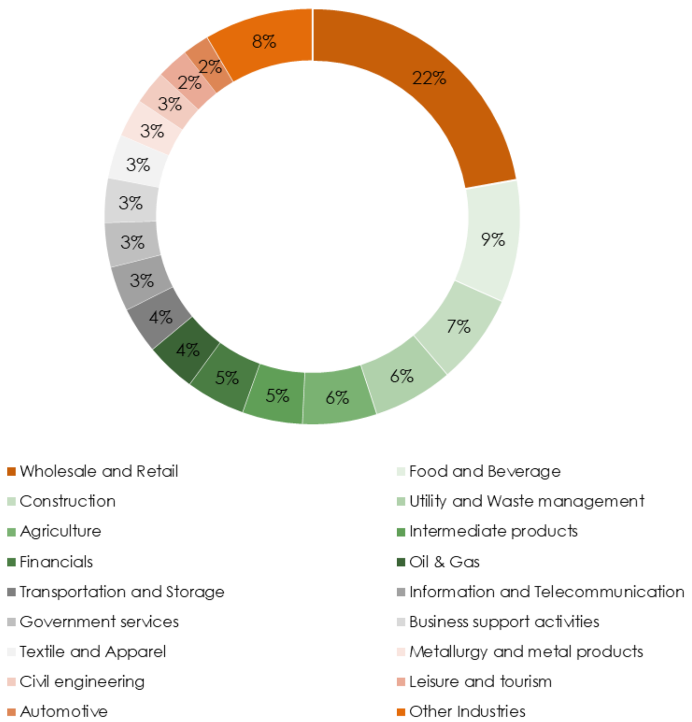
Graph 24 – Credit portfolio quality based on internal rating zones



Graph 25 – Portfolio distribution by segment



Graph 26 – Portfolio distribution by industry



Credit portfolio distribution by industry points to relatively good portfolio diversification. In accordance with the official industry classification (NACE) the largest portion of credit portfolio belongs to Wholesale and Retail (22%), Construction (9%) and Utility and Waste Management (7%).

Throughout 2019, the Bank performance was in line with the all Hard and Soft RAF risk appetite and tolerance limits defined by the Board of Directors, as well as within the regulatory limits defined by the National Bank of Serbia. Limit utilisation is monitored and reported on a regular basis to the business units, the Parent Group, and relevant corporate governance bodies.

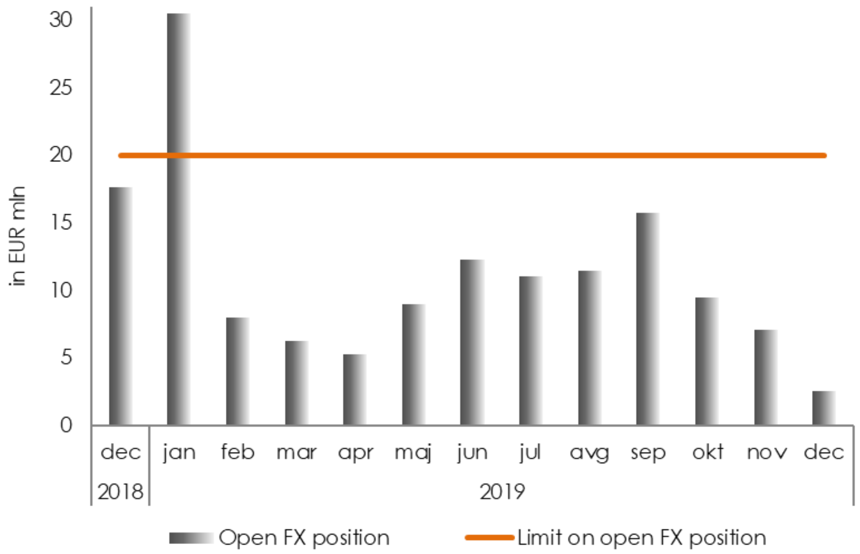
Market risks

The main sources of market risks to which the Bank is exposed in its operations are interest rate risk and foreign exchange risk.

General principles of market risk management are defined in accordance with regulatory rules, ISP Group standards, international best practices and standards, as well as internal acts. The system of market risk limits, defined in coordination with the Parent Group's relevant structures and approved by the Board of Directors, operationalises the market risk monitoring process. The system of limits is aligned with the strategic goals of the Bank, RAF system and regulatory requirements. Market risk limits utilisation is reported to the relevant functions of the Bank on a daily basis, while reporting to the ALCO is on a monthly level or more frequently, if necessary. The ALCO monitors market risk exposures on a strategic level and provides guidelines for general management of the Bank's balance sheet within its responsibility.

During 2019, the foreign exchange risk exposure was significantly below the maximum level prescribed by the regulator. Internally established limits for open foreign exchange position and foreign exchange Value at Risk were not revised. The position limits were breached on a few occasions (primarily due to the initial impact of IFRS 16 accounting standard in January/February and dividend payments in March and October) as a consequence of preapproved and agreed business actions requiring open FX position not to be closed immediately but in the short period of time.

Graph 27 – Trend of foreign exchange risk exposure

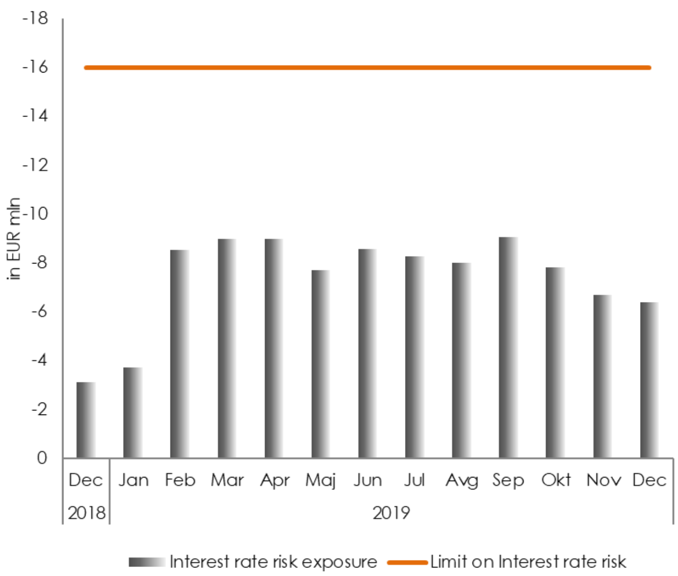


Regarding interest rate risk, the Trading Book was constantly within the defined limits for all risk measures: position, Value at Risk, duration.

As for the Banking Book, the position was below the prescribed limits throughout the year. The interest rate risk principles applied in the monitoring process were revised through the updated Policy on IRRBB Management and implementation of new regulatory requirements and Intesa Sanpaolo Group requirements.

New methodology related to currency aggregation, as well as prepayment model have been implemented for the first time in 2019.

Graph 28 – Trend of interest rate risk exposure

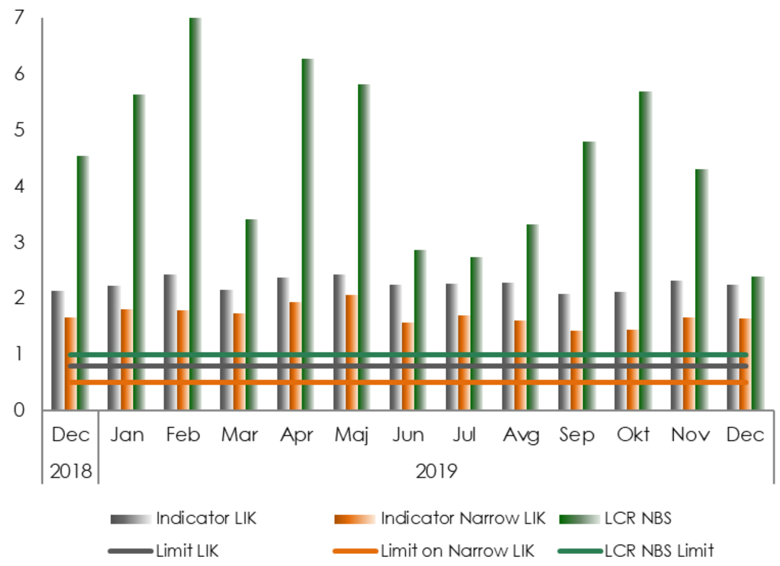


Liquidity risk

In the course of 2019, the liquidity level of Banca Intesa was above the minimum requirement and the Bank invested its excess liquidity in debt securities of the Republic of Serbia. All the liquidity indicators, regulatory ones and those defined by the Group, were within the set limits at all times.

The Bank was involved for the third time in the Group SSM (Single Supervisory Mechanism) Liquidity Exercise required by European Central Bank, in order to present its capability to provide adequate informational flows (liquidity reports) on daily basis in case of stress.

Graph 29 – Trend of regulatory liquidity indicators



Operational risks

Operational risk management is conducted in line with the methodology of the Parent Group, according to the model supported by appropriate IT solutions, enabling regular monitoring, assessment and reporting on operational risks.

Banca Intesa complies with the requirements related to the regulatory capital defined by the NBS and applies a standardised approach to the measurement of capital requirement for operational risk. The Risk Management Department regularly reports to the Operational Risk Committee, Executive Board, the Board of Directors and the Parent Group on operational risks and measures for their mitigation.

Operational risk identification, assessment and monitoring are undertaken through the process of collecting data on operational risks/losses and the process of assessment of exposure to operational risk. Data on operational risks/losses are analysed on a monthly basis, while the process of assessing the exposure to operational risk is carried out once a year, including a subjective assessment of operational risks for the period of 12 months. Various scenarios are analysed and the possibility and frequency of occurrence of operational risk are assessed, as well as the average and the worst possible loss in case of occurrence of each scenario. The process of operational risk exposure assessment also includes an evaluation of the business environment through an analysis of the level of risk factor management, identification of potential critical operational issues and mitigation actions proposed to reduce the operational risk exposure and ICT risk analysis, which applies to infrastructural services, IT governance, the Bank's applications, information security and business continuity.

By applying an advanced measurement model, the Parent Group calculates the level of expected and unexpected operational losses, i.e. the level of capital required to cover operational risks.

Operational risks in 2019 were at the similar level as previous year. The biggest operational risks appear as a result of errors in the processes of execution and management, but also due to external fraud and abuse. In the latest assessment of exposure to operational risk, for 2020, it was estimated that expected losses are much higher than in the previous year. This is mostly related to the expected increase in the number of lawsuits related to increased number of allegedly unlawful charged NKOSK insurance policy premium, NKOSK fee and loan approval fee, as well as to the expected potential losses that may result from the change of the information system.

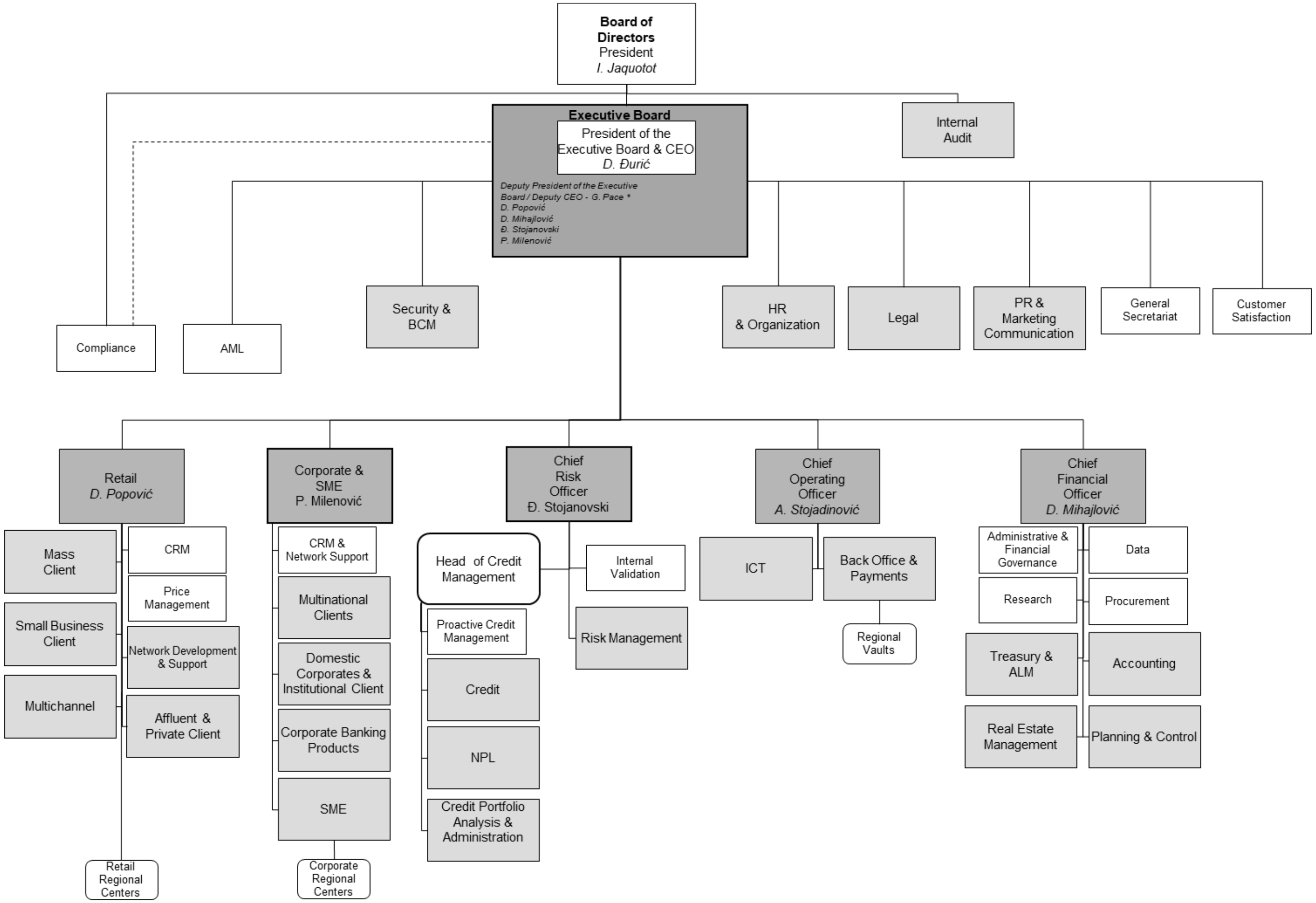
Operational risk management system is upgrade with introduction of Key Risk Indicators. IT is early warning system for operational risk that should support timely identification of increased operational risk and allow preventive actions that could mitigate identified risks.

During 2019, the Bank worked to spread culture and raise awareness of emerging risks. These are new risks or known risks that become apparent in new or unknown conditions. During the year, there were presentations organised for colleagues in order to present new challenges, and how changes in the society, environment and advances in new technologies could affect the banking industry.

11. Events after the Reporting Period

There have been no significant events after the reporting period, which would require disclosures in the Notes to the Financial Statements of the Bank as of and for the year ended 31 December 2019.

12. Organisational Chart



*Responsible for area under the authority of Chief Financial Officer, Chief Risk Officer, and Chief Operating Officer and for Security and Business Continuity Management Department, as well as for Project Management in terms of strategic

13. Branch Network

Location	Name of the branch	Regional centre	Address
Ada	**Ada, Vuka Karadžića 18**	Novi Sad	Vuka Karadžića 18
Aleksandrovac	**Aleksandrovac, 29. Novembra bb**	Niš	29. Novembra bb
Aleksinac	**Aleksinac, Knjaza Miloša 115**	Niš	Knjaza Miloša 115
Apatin	**Apatin, Petefi Šandora 2**	Novi Sad	Petefi Šandora 2
Arandjelovac	**Aranđelovac, Knjaza Miloša 192**	Kragujevac	Knjaza Miloša 192
Arilje	**Arilje, Stevana Čolovića 2**	Kragujevac	Stevana Čolovića 2
Bačka Palanka	**Bačka Palanka, Žarka Zrenjanina 80**	Novi Sad	Žarka Zrenjanina 80
Bačka Topola	**Bačka Topola, Glavna 29**	Novi Sad	Glavna 29
Bački Petrovac	**Bački Petrovac, Maršala Tita 4**	Novi Sad	Maršala Tita 4
Bajina Bašta	**Bajina Bašta, Svetosavska 19a**	Kragujevac	Svetosavska 19a
Batajnica	**Zemun, Batajnica, Majke Jugovića 1**	Beograd	Majke Jugovića 1
Bečej	**Bečej, Novosadska 2**	Novi Sad	Novosadska 2
Beočin	**Beočin, Trg Cara Lazara 8**	Novi Sad	Trg Cara Lazara 8
Beograd	**Čukarica, Požeška 128**	Beograd	Požeška 128
Beograd	**Čukarica, Požeška 45**	Beograd	Požeška 45
Beograd	**Čukarica, Trgovačka 15**	Beograd	Trgovačka 15
Beograd	**Novi Beograd, Bulevar Arsenija Čarnojevića 54**	Beograd	Bulevar Arsenija Čarnojevića 54
Beograd	**Novi Beograd, Bulevar maršala Tolbuhina 34**	Beograd	Bulevar maršala Tolbuhina 34
Beograd	**Novi Beograd, Jurija Gagarina 14**	Beograd	Jurija Gagarina 14
Beograd	**Novi Beograd, Jurija Gagarina 36b**	Beograd	Jurija Gagarina 36b
Beograd	**Novi Beograd, Milentija Popovića 7b**	Beograd	Milentija Popovića 7b
Beograd	**Novi Beograd, Milentija Popovića 7v**	Beograd	Milentija Popovića 7v
Beograd	**Novi Beograd, Milutina Milankovića 134g**	Beograd	Milutina Milankovića 134g
Beograd	**Novi Beograd, Nedeljka Gvozdenovića 24a**	Beograd	Nedeljka Gvozdenovića 24a
Beograd	**Novi Beograd, Omladinskih brigada 90**	Beograd	Omladinskih brigada 90
Beograd	**Novi Beograd, Otona Župančića 1**	Beograd	Otona Župančića 1
Beograd	**Novi Beograd, Partizanske avijacije 14**	Beograd	Partizanske avijacije 14
Beograd	**Palilula, 27. marta 23**	Beograd	27. marta 23
Beograd	**Palilula, Borča, Ivana Milutinovića 73**	Beograd	Ivana Milutinovića 73
Beograd	**Palilula, Marjane Gregoran 60**	Beograd	Marjane Gregoran 60
Beograd	**Rakovica, Miška Kranjca br. 12**	Beograd	Miška Kranjca br. 12
Beograd	**Rakovica, Vidikovački venac 80b**	Beograd	Vidikovački venac 80b
Beograd	**Rakovica, Vukasovićeva 50a**	Beograd	Vukasovićeva 50a
Beograd	**Savski Venac, Nemanjina 4**	Beograd	Nemanjina 4
Beograd	**Savski Venac, Vase Pelagića 48b**	Beograd	Vase Pelagića 48b
Beograd	**Stari Grad, Cara Dušana 50**	Beograd	Cara Dušana 50
Beograd	**Stari Grad, Džordža Vašingtona 8**	Beograd	Džordža Vašingtona 8
Beograd	**Stari Grad, Knez Mihailova 30**	Beograd	Knez Mihailova 30
Beograd	**Stari Grad, Kolarčeva 5**	Beograd	Kolarčeva 5
Beograd	**Stari Grad, Studentski trg 7**	Beograd	Studentski trg 7
Beograd	**Surčin, Vojvođanska 85**	Beograd	Vojvođanska 85
Beograd	**Voždovac, Banjica, Crnotravska 7-9**	Beograd	Crnotravska 7-9
Beograd	**Voždovac, Braće Jerković 137b**	Beograd	Braće Jerković 137b
Beograd	**Voždovac, Kumodraška 174**	Beograd	Kumodraška 174
Beograd	**Voždovac, Ustanička 69**	Beograd	Ustanička 69
Beograd	**Voždovac, Vojvode Stepe 77**	Beograd	Vojvode Stepe 77
Beograd	**Vračar, Bore Stankovića 9**	Beograd	Sarajevska 31
Beograd	**Vračar, Bulevar oslobođenja 3**	Beograd	Bulevar oslobođenja 3
Beograd	**Vračar, Južni Bulevar 84**	Beograd	Južni Bulevar 84
Beograd	**Vračar, Kneza Miloša 23**	Beograd	Kneza Miloša 23
Beograd	**Vračar, Kursulina 41**	Beograd	Kursulina 41
Beograd	**Zvezdara, Bulevar Kralja Aleksandra 330**	Beograd	Bulevar Kralja Aleksandra 330

Location	Name of the branch	Regional centre	Address
Beograd	**Zvezdara, Bulevar Kralja Aleksandra 79**	Beograd	Bulevar Kralja Aleksandra 79
Beograd	**Zvezdara, Mirijevski venac 23**	Beograd	Mirijevski venac 23
Bogatić	**Bogatić, Vojvode Stepe 35**	Kragujevac	Vojvode Stepe 35
Bor	**Bor, Đorđa Vajferta 3**	Niš	Đorđa Vajferta 3
Brus	**Brus, Kralja Petra I bb**	Niš	Kralja Petra I bb
Bujanovac	**Bujanovac, Karađorđa Petrovića 111**	Niš	Karađorđa Petrovića 111
Čačak	**Čačak, Kuželjeva 1**	Kragujevac	Kuželjeva 1
Despotovac	**Despotovac, Despota Stefana Lazarevića 50**	Niš	Despota Stefana Lazarevića 50
Gornji Milanovac	**Gornji Milanovac, Vojvode Milana 1**	Kragujevac	Vojvode Milana 1
Inđija	**Inđija, Novosadska 21**	Novi Sad	Novosadska 21
Ivanjica	**Ivanjica, Majora Ilića 1**	Kragujevac	Majora Ilića 1
Jagodina	**Jagodina, Kneza Lazara 5-6**	Niš	Kneza Lazara 5-6
Kanjiža	**Kanjiža, Glavna 3**	Novi Sad	Glavna 3
Kikinda	**Kikinda, Braće Tatića 16**	Novi Sad	Braće Tatića 16
Kladovo	**Kladovo, 22. septembra 9**	Niš	22.septembra 9
Kostolac	**Kostolac, Nikole Tesle 5-7**	Niš	Nikole Tesle 5-7
Kovačica	**Kovačica, Maršala Tita 31a**	Novi Sad	Maršala Tita 31a
Kovin	**Kovin, Cara Lazara 73**	Novi Sad	Cara Lazara 73
Kragujevac	**Kragujevac, Kralja Aleksandra I Karađorđevića 120**	Kragujevac	Kralja Aleksandra I Karađorđevića 120
Kragujevac	**Kragujevac, Kralja Petra I 19**	Kragujevac	Kralja Petra I 19
Kragujevac	**Kragujevac, Save Kovačevića 12 b**	Kragujevac	Save Kovačevića 12 b
Kraljevo	**Kraljevo, Trg Jovana Sarića 8**	Kragujevac	Trg Jovana Sarića 8
Kruševac	**Kruševac, Vece Korčagina 18**	Kragujevac	Vece Korčagina 18
Kruševac	**Kruševac, Vidovdanska 4**	Kragujevac	Vidovdanska 4
Kučevo	**Kučevo, Trg Veljka Dugoševića 2**	Niš	Trg Veljka Dugoševića 2
Kula	**Kula, Maršala Tita 242**	Novi Sad	Maršala Tita 242
Lajkovac	**Lajkovac, Vojvode Mišića 84**	Kragujevac	Vojvode Mišića 84
Lazarevac	**Lazarevac, Karađorđeva 41**	Kragujevac	Karađorđeva 41
Leskovac	**Leskovac, Trg Revolucije 7**	Niš	Trg Revolucije 7
Loznica	**Loznica, Trg Vuka Karadžića bb**	Kragujevac	Trg Vuka Karadžića bb
Ljig	**Ljig, Vojvode Mišića 12**	Kragujevac	Vojvode Mišića 12
Ljubovija	**Ljubovija, Vojvode Mišića 44**	Kragujevac	Vojvode Mišića 44
Mionica	**Mionica, Dr. Jove Aleksića bb**	Kragujevac	Dr. Jove Aleksića bb
Mladenovac	**Mladenovac, Kralja Petra I 217**	Kragujevac	Kralja Petra I 217
Negotin	**Negotin, Trg Đorđa Stanojevića 70/II**	Niš	Trg Đorđa Stanojevića 70/II
Niš	**Niš, Bulevar Nemanjića 28-32**	Niš	Bulevar Nemanjića 28-32
Niš	**Niš, Milojka Lešjanina 1**	Niš	Milojka Lešjanina 1
Niš	**Niš, Nade Tomić 8a**	Niš	Nade Tomić 8a
Niš	**Niš, Obrenovićeva 82 (Fontana)**	Niš	Obrenovićeva 82 (Fontana)
Niš	**Niš, Sinđelićev trg 18**	Niš	Sinđelićev trg 18
Niš	**Niš, Vizantijski bulevar 78**	Niš	Vizantijski bulevar 78
Novi Bečej	**Novi Bečej, Trg Oslobođenja 5**	Novi Sad	Trg Oslobođenja 5
Novi Pazar	**Novi Pazar, AVNOJ-a 6**	Kragujevac	AVNOJ-a 6
Novi Sad	**Novi Sad, Bulevar Cara Lazara 79a**	Novi Sad	Bulevar cara Lazara 79a
Novi Sad	**Novi Sad, Bulevar Jovana Dučića 1**	Novi Sad	Bulevar Jovana Dučića 1
Novi Sad	**Novi Sad, Bulevar Mihajla Pupina 4**	Novi Sad	Bulevar Mihaila Pupina 4
Novi Sad	**Novi Sad, Bulevar Oslobođenja 32 (temporary location)**	Novi Sad	Bulevar Oslobođenja 32 (temporary location)
Novi Sad	**Novi Sad, Bulevar Oslobođenja 76a**	Novi Sad	Bulevar Oslobođenja 76a
Novi Sad	**Novi Sad, Fruškogorska 10**	Novi Sad	Fruškogorska 10
Novi Sad	**Novi Sad, Rumenačka 33**	Novi Sad	Rumenačka 33
Novi Sad	**Novi Sad, Zmaj Jovina 15**	Novi Sad	Zmaj Jovina 15
Obrenovac	**Obrenovac, Miloša Obrenovića 133-135**	Kragujevac	Miloša Obrenovića 133-135

Location	Name of the branch	Regional centre	Address
Pančevo	**Pančevo, Karađorđeva 2-4**	Novi Sad	Karađorđeva 2-4
Pančevo	**Pančevo, Štrosmajerova 1**	Novi Sad	Štrosmajerova 1
Paraćin	**Paraćin, Kralja Petra I 4**	Niš	Kralja Petra I 4
Petrovac na Mlavi	**Petrovac na Mlavi, Bate Bulića 37**	Niš	Bate Bulića 37
Pirot	**Pirot, Branka Radičevića 18**	Niš	Branka Radičevića 18
Požarevac	**Požarevac, Trg Radomira Vujovića 8**	Niš	Trg Radomira Vujovića 8
Požega	**Požega, Knjaza Miloša 6**	Kragujevac	Knjaza Miloša 6
Priboj	**Priboj, Nemanjina 48-50**	Kragujevac	Nemanjina 48-50
Prijepolje	**Prijepolje, Sandžačkih brigada 39**	Kragujevac	Sandžačkih brigada 39
Prokuplje	**Prokuplje, 9. oktobra 6**	Niš	9. oktobra 6
Raška	**Raška, Miluna Ivanovića 8**	Kragujevac	Miluna Ivanovića 8
Ruma	**Ruma, Glavna 170**	Novi Sad	Glavna 170
Ruma	**Ruma, 15. maja 143**	Novi Sad	15. maja 143
Senta	**Senta, Zlatne grede 6**	Novi Sad	Zladne grede 6
Sjenica	**Sjenica, Milorada Jovanovića bb**	Kragujevac	Milorada Jovanovića bb
Smederevo	**Smederevo, Cvijićeva 3**	Niš	Cvijićeva 3
Smederevska Palanka	**Smederevska Palanka, Svetog Save 19**	Kragujevac	Svetog Save 19
Sombor	**Sombor, Venac Stepe Stepanovića 32**	Novi Sad	Venac Stepe Stepanovića 32
Srbobran	**Srbobran, Zmaj Jovina 18**	Novi Sad	Zmaj Jovina 18
Sremska Mitrovica	**Sremska Mitrovica, Kralja Petra I 6**	Novi Sad	Kralja Petra I 6
Sremska Mitrovica	**Sremska Mitrovica, Svetog Dimitrija 2**	Novi Sad	Svetog Dimitrija 2
Stara Pazova	**Stara Pazova, Ćirila i Metodija 2**	Novi Sad	Ćirila i Metodija 2
Subotica	**Subotica, Dimitrija Tucovića 2**	Novi Sad	Dimitrija Tucovića 2
Subotica	**Subotica, Štrosmajerova 6**	Novi Sad	Štrosmajerova 6
Surdulica	**Surdulica, Ulica Kralja Petra I bb**	Niš	Kralja Petra I bb
Svilajnac	**Svilajnac, Svetog Save 52**	Niš	Svetog Save 52
Šabac	**Šabac, Gospodar Jevremova 44**	Kragujevac	Gospodar Jevremova 44
Šid	**Šid, Karađorđeva 11-13**	Novi Sad	Karađorđeva 11-13
Temerin	**Temerin, Novosadska 403**	Novi Sad	Novosadska 403
Titel	**Titel, Mihajla Krestića 8a**	Novi Sad	Mihaila Krestića 8a
Topola	**Topola, Tomislava Karađorđevića 3**	Kragujevac	Tomislava Karađorđevića 3
Trstenik	**Trstenik, Cara Dušana bb**	Kragujevac	Cara Dušana bb
Ub	**Ub, Kralja Petra I 44**	Kragujevac	Kralja Petra I 44
Užice	**Užice, Dimitrija Tucovića 129**	Kragujevac	Dimitrija Tucovića 129
Valjevo	**Valjevo, Karađorđeva 71**	Kragujevac	Karađorđeva 71
Valjevo	**Valjevo, Železnička 7**	Kragujevac	Železnička 7
Velika Plana	**Velika Plana, Momira Gajića br 2**	Kragujevac	Momira Gajića br 2
Veliko Gradište	**Veliko Gradište, Kneza Lazara 35**	Niš	Kneza Lazara 35
Veternik	**Veternik, Kralja Petra I 7a**	Novi Sad	Kralja Petra I 7a
Vladičin Han	**Vladičin Han, Svetosavska 16a**	Niš	Svetosavska 16a
Vlasotince	**Vlasotince, Nemanjina 2**	Niš	Nemanjina 2
Vranje	**Vranje, Lenjinova bb**	Niš	Lenjinova bb
Vrbas	**Vrbas, Maršala Tita 66**	Novi Sad	Maršala Tita 66
Vrnjačka Banja	**Vrnjačka Banja, Kruševačka 1**	Kragujevac	Kruševačka 1
Vršac	**Vršac, Sterijina 19a**	Novi Sad	Sterijina 19a
Zaječar	**Zaječar, Nikole Pašića 70**	Niš	Nikole Pašića 70
Zemun	**Zemun, Glavna 30**	Beograd	Glavna 30
Zemun	**Zemun, Gornjogradska 38**	Beograd	Gornjogradska 38
Zlatibor	**Zlatibor, Kraljev trg bb**	Kragujevac	Kraljev trg bb
Zrenjanin	**Zrenjanin, Kralja Aleksandra I Karađorđevića bb**	Novi Sad	Kralja Aleksandra I Karađorđevića bb
Žabalj	**Žabalj, Nikole Tesle 47**	Novi Sad	Nikole Tesle 47