BANCA INTESA

Consolidated Financial Statements

For the Year Ended 31 December 2018
and Independent Auditors' Report

Contents

Independent Auditors' Report

To the Shareholders and Board of Directors of BANCA INTESA

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of BANCA INTESA (the "Bank") and its subsidiary (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2018, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the independence requirements that are relevant to our audit of the consolidated financial statements in the Russian Federation and with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the requirements in the Russian Federation and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

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

Excepted credit losses ('ECL') for loans to customers	
Please refer to Notes 3, 9 and 25 in the consolidated financial statements.	
The key audit matter	**How the matter was addressed in our audit**
Loans to customers represent more than 59% of assets and are stated net of allowance for expected credit losses ('ECL') that is estimated on a regular basis and is sensitive to assumptions used.	We analyzed the key aspects of the Group's methodology and policies related to ECL estimate for compliance with the requirements of IFRS 9, including involvement of financial risks management specialists.
From 1 January 2018 the Group has implemented a new ECL valuation model, which requires management to apply professional judgement and to make assumptions related to the following key areas:	To analyze adequacy of professional judgement and assumptions made by the management in relation to allowance for ECL estimate, we included in our audit procedures the following:
- timely identification of significant increase in credit risk and default events related to loans to customers (allocation between stages 1, 2 and 3 in accordance with the IFRS 9);	- We tested design and operating effectiveness of controls over allocation of loans into stages. - For a sample of loans, for which a potential changes in ECL estimate may have a significant impact on the consolidated financial statements, we tested whether stages are correctly assigned by the Group by analyzing financial and non-financial information, as well as assumptions and professional judgements, applied by the Group.
- assessment of probability of default (PD) and loss given default (LGD);	- For loans to large corporate borrowers, where ECL are assessed based on internal Group's rating model, we assessed the overall adequacy of the ultimate ECL by analyzing credit ratings issued by independent rating agencies and preparing our own ECL model based on publicly available data on financial positions and defaults of Russian corporates. - For loans to customers assigned to stages 1 and 2, where ECL is assessed collectively, we tested the design and implementation of the related models, and agreed input data to supporting documents on a sample basis.
- assessment of add-on adjustment to account for different scenarios and forward-looking information;	- We assessed the overall adequacy of the add-on adjustment to account for different scenarios and forward-looking information by comparison with our own estimate, considering current economic situation and business environment of certain categories of borrowers.

- expected cash flows forecast for loans to customers classified in stage 3.	- For a sample of stage 3 loans, where ECL are assessed individually we critically assessed assumptions used by the Group to forecast future cash flows, including estimated proceeds from realisable collateral and their expected disposal terms based on our understanding and publicly available market information. We specifically focused on exposures which potentially may have the most significant impact on the consolidated financial statements.
Due to the significant volume of loans to customers, adoption of the new ECL model and the related estimation uncertainty, this area is a key audit matter.	We assessed predictive capability of the Group's methodology by comparing the estimates made as at 1 January 2018 with actual results for 2018. We also assessed whether the consolidated financial statements disclosures appropriately reflect the Group's exposure to credit risk.

Adoption of IFRS 9 'Financial instruments'

Please refer to Notes 2 and 4 in the consolidated financial statements.

The key audit matter	How the matter was addressed in our audit
The use of financial instruments is a core business of the Group and financial assets constitute a majority of Group's assets. From 1 January 2018 the Group has adopted a new accounting standard for financials instruments, IFRS 9, which provides significant changes to classification and measurement of financial assets. Due to adoption of new requirements, which provide significant changes to the effective accounting principles of financial instruments, and due to a significant impact of the new standard on the financial position and performance of the Group, this area is a key audit matter.	We analysed definition of business models used to manage financial assets by making inquiries to responsible employees, reviewing Group's internal documentation and analyzing internal business processes on selected significant financial instruments portfolios. We checked that the Group has performed proper assessment whether contractual cash flows are solely payments of principal and interest by analyzing underlying documents for a sample of financial instruments. We also checked whether the Group has correctly identified and accounted for modifications of terms of loans to customers, by means of general analysis of core procedures related to modification of loans' terms applied by the Group and analysis of underlying documents on a sample of loans to customers. We also assessed whether the consolidated financial statements provide an appropriate disclosure of key classification and measurement principles for financial instruments as well as the effects of the Group adoption of IFRS 9.

Other Information

Management is responsible for the other information. The other information comprises the Annual report for 2018, but does not include the consolidated financial statements and our auditors' report thereon.

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

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

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

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

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

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

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

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

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

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

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

— Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

— Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

— Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.

— Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

— Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

Report of findings from procedures performed in accordance with the requirements of Federal Law No. 395-1, dated 2 December 1990, *On Banks and Banking Activity*

Management is responsible for the Group's compliance with mandatory ratios and for maintaining internal control and organizing risk management systems in accordance with requirements established by the Bank of Russia.

In accordance with Article 42 of Federal Law No. 395-1, dated 2 December 1990, *On Banks and Banking Activity* (the "Federal Law"), we have performed procedures to examine:

— the Group's compliance with mandatory ratios as at 1 January 2019 established by the Bank of Russia; and

— whether the elements of the Group's internal control and organisation of its risk management systems comply with the requirements established by the Bank of Russia.

These procedures were selected based on our judgment and were limited to the analysis, inspection of documents, comparison of the Bank's internal policies, procedures and methodologies with the applicable requirements established by the Bank of Russia, and recalculations, comparisons and reconciliations of numerical data and other information.

Our findings from the procedures performed are reported below.

— Based on our procedures with respect to the Group's compliance with the mandatory ratios established by the Bank of Russia, we found that the Group's mandatory ratios as at 1 January 2019 were within the limits established by the Bank of Russia.

  We have not performed any procedures on the accounting records maintained by the Group other than those which we considered necessary to enable us to express an opinion as to whether the Group's consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with the International Financial Reporting Standards.

— Based on our procedures with respect to whether the elements of the Group's internal control and organisation of its risk management systems comply with the requirements established by the Bank of Russia, we found that:

  - as at 31 December 2018, the Bank's Internal Audit function was subordinated to, and reported to, the Board of Directors, and the Risk Management function was not subordinated to, and did not report to, divisions taking relevant risks in accordance with regulations and recommendations issued by the Bank of Russia;

  - the Bank's internal documentation, effective on 31 December 2018, establishing the procedures and methodologies for identifying and managing the Group's significant credit, operational, market, interest rate, legal, strategy, country, concentration and liquidity risks, and for stress-testing was approved by the authorised management bodies of the Bank in accordance with the regulations and recommendations issued by the Bank of Russia;

  - as at 31 December 2018, the Bank maintained a system for reporting on the Group's significant credit, operational, market, interest rate, legal, strategy, country, concentration and liquidity risks, and on the Group's capital;

- the frequency and consistency of reports prepared by the Bank's Risk Management and Internal Audit functions during 2018, which cover the Group's credit, operational, market, interest rate, legal, strategy, country, concentration and liquidity risk management, was in compliance with the Bank's internal documentation. The reports included observations made by the Bank's Risk Management and Internal Audit functions as to their assessment of the effectiveness of the Bank's procedures and methodologies, and recommendations for improvement;
- as at 31 December 2018, the Board of Directors and the Management Board of the Bank had responsibility for monitoring the Group's compliance with the risk limits and capital adequacy ratios established in the Bank's internal documentation. In order to monitor the effectiveness of the Group's risk management procedures and their consistent application during 2018 the Board of Directors and the Management Board of the Bank periodically discussed reports prepared by the Risk Management and Internal Audit functions, and considered the proposed corrective actions.

Procedures with respect to elements of the Group's internal control and organisation of its risk management systems were performed solely for the purpose of examining whether these elements, as prescribed in the Federal Law and as described above, comply with the requirements established by the Bank of Russia.

The engagement partner on the audit resulting in this independent auditors' report is:

Shevarenkov E.V.

JSC "KPMG"

Moscow, the Russian Federation

19 February 2019

(Thousands of Russian Roubles)

	Notes	2018	2017*
Assets			
Cash and cash equivalents	5	5 100 550	3 886 295
Mandatory cash balances with the Central Bank of the Russian Federation		386 641	298 979
Amounts due from credit institutions	6	9 982 367	13 654 192
Investment securities	7	4 079 778	4 130 899
Derivative financial assets	8	5 359	-
Loans to customers:		35 179 162	28 995 088
- loans to large corporate customers	*9*	*19 969 618*	*12 950 962*
- loans to small and medium corporate customers	*9*	*13 495 829*	*14 282 671*
- loans to retail customers	*9*	*1 713 715*	*1 761 455*
Net investments in finance leases	10	1 375 770	1 334 117
Property and equipment	11	714 450	1 131 217
Intangible assets	12	447 402	585 667
Deferred income tax assets	13	373 559	328 348
Other assets	14	1 999 981	748 948
Total assets		**59 645 019**	**55 093 750**
Liabilities			
Amounts due to credit institutions	15	10 467 555	5 884 650
Derivative financial liabilities	8	4	-
Amounts due to customers:		29 965 165	30 527 105
- legal entities, state and non-profit organizations	*16*	*18 010 679*	*13 700 703*
- individuals	*16*	*11 954 486*	*16 826 402*
Debt securities issued	17	3 059 954	3 186 066
Subordinated loan	17	2 828 605	2 304 839
Other liabilities	14	711 623	746 512
Total liabilities		**47 032 906**	**42 649 172**
Equity	18		
Share capital		10 820 181	10 820 181
Other capital reserves		1 803 914	1 803 914
Revaluation reserve for debt investment securities		(14 783)	22 802
Revaluation reserve for buildings		134 724	384 144
Accumulated losses		(131 923)	(586 463)
Total equity		**12 612 113**	**12 444 578**
Total equity and liabilities		**59 645 019**	**55 093 750**

* The Bank initially applied IFRS 9 at 1 January 2018. Under the transition methods chosen, comparative information is not restated. As a result of adoption of IFRS 9 the Bank changed presentation of certain captions, comparative information is re-presented accordingly (Note 2).

Signed and authorised for release on behalf of the Management Board of the Bank:

Olga Lein — Acting Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board / Head of Accounting, Planning and Control Group / Chief accountant

(Thousands of Russian Roubles)

	Notes	2018	2017
Interest income, calculated using effective interest rate method			
Loans to customers		3 458 951	3 986 434
Amounts due from credit institutions		533 701	606 401
Debt investment securities		258 378	336 723
		4 251 030	**4 929 558**
Other interest income			
Net investments in finance leases		239 050	230 026
		4 490 080	**5 159 584**
Interest expense			
Amounts due to customers		(898 276)	(1 267 902)
Debt securities issued		(301 713)	(391 791)
Amounts due to credit institutions		(247 964)	(265 796)
Subordinated loan		(165 046)	(153 585)
		(1 612 999)	**(2 079 074)**
Net interest income		**2 877 081**	**3 080 510**
Changes in allowance for credit losses on interest-bearing financial assets	19	(433 404)	(319 952)
Net interest income after allowance for credit losses for interest-bearing financial assets		**2 443 677**	**2 760 558**
Fee and commission income	20	1 932 895	1 015 654
Fee and commission expense	20	(126 919)	(145 278)
Net fee and commission income		**1 805 976**	**870 376**
Net (losses) gains from investment securities		(319)	6 139
Net gains from foreign currencies:			
- dealing		(228 142)	(161 415)
- translation differences		345 734	395 958
Net losses from other operating activities	21	(67 463)	(68 707)
Operating income		**4 299 463**	**3 802 909**
Personnel expenses	22	(1 650 260)	(1 709 822)
Other general administrative expenses	22	(1 242 159)	(1 267 204)
Depreciation and amortization	11,12	(412 266)	(439 457)
Other allowance for credit losses	14	47 099	(108 847)
Profit before income tax		**1 041 877**	**277 579**
Income tax expense	13	(172 556)	(275 508)
Profit for the year		**869 321**	**2 071**
Other comprehensive (loss) income for the year			
Items that are or may be reclassified subsequently to profit or loss:			
Revaluation reserve for debt investment securities:			
- net change in fair value		(40 993)	6 127
- net amount transferred to profit or loss		266	(5 155)
		(40 727)	**972**
Items that will not be reclassified to profit or loss:			
Revaluation of buildings		(249 420)	384 144
Total other comprehensive (loss) income for the year, net of income tax		**(290 147)**	**385 116**
Total comprehensive income for the year		**579 174**	**387 187**

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Olga Lein — Acting Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board / Head of Accounting, Planning and Control Group / Chief accountant

The accompanying Notes are an integral part of these consolidated financial statements.

(Thousands of Russian Roubles)

	Share capital	*Other capital reserves*	*Revaluation reserve for debt investment securities*	*Revaluation reserve for buildings*	*Accumulated losses*	*Total equity*
Balance as at 1 January 2017	10 820 181	1 803 914	21 830	-	(588 534)	12 057 391
Total comprehensive income						
Profit for the year	-	-	-	-	2 071	2 071
Other comprehensive income						
Items that are or may be reclassified subsequently to profit or loss:						
Revaluation of debt investment securities:						
- Net change in fair value, net of deferred tax of RUB 1 533 thousand	-	-	6 127	-	-	6 127
- Net amount transferred to profit or loss, net of deferred tax of RUB 1 289 thousand	-	-	(5 155)	-	-	(5 155)
	-	**-**	***972***	**-**	**-**	***972***
Items that will not be reclassified to profit or loss:						
Revaluation of buildings, net of deferred tax of RUB 96 036 thousand	-	-	-	384 144	-	*384 144*
Total other comprehensive income	**-**	**-**	**972**	**384 144**	**-**	**385 116**
Total comprehensive income for the year	**-**	**-**	**972**	**384 144**	**2 071**	**387 187**
Balance as at 31 December 2017 (before transition to IFRS 9)	**10 820 181**	**1 803 914**	**22 802**	**384 144**	**(586 463)**	**12 444 578**
Impact of adopting IFRS 9 as at 1 January 2018 (Note 2)	-	-	3 142	-	(414 781)	(411 639)
Recalculated balance as at 1 January 2018	**10 820 181**	**1 803 914**	**25 944**	**384 144**	**(1 001 244)**	**12 032 939**
Total comprehensive income						
Profit for the period	-	-	-	-	869 321	869 321
Other comprehensive loss						
Items that are or may be reclassified subsequently to profit or loss						
Revaluation of debt investment securities:						
- Net change in fair value, net of deferred tax of RUB 10 248 thousand	-	-	(40 993)	-	-	(40 993)
- Net amount transferred to profit or loss, net of deferred tax of RUB 67 thousand	-	-	266	-	-	226
	-	**-**	***(40 727)***	**-**	**-**	***(40 727)***
Items that will not be reclassified to profit or loss						
Revaluation of buildings, net of deferred tax of RUB 62 355 thousand	-	-	-	(249 420)	-	(249 420)
Total other comprehensive loss	**-**	**-**	**(40 727)**	**(249 420)**	**-**	**(290 147)**
Total comprehensive income for the year	**-**	**-**	**(40 727)**	**(249 420)**	**869 321**	**579 174**
Balance as at 31 December 2018	**10 820 181**	**1 803 914**	**(14 783)**	**134 724**	**(131 923)**	**12 612 113**

Signed and authorised for release on behalf of the Management Board of the Bank:

Olga Lein — Acting Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board / Head of Accounting, Planning and Control Group / Chief accountant

(Thousands of Russian Roubles)

	Note	2018	2017
Cash flows from operating activities			
Interest received		4 402 207	4 866 618
Interest paid		(1 597 981)	(2 388 949)
Fees and commissions received		912 675	1 569 628
Fees and commissions paid		(129 966)	(149 310)
Net payments for dealing in foreign currencies		(233 496)	(160 467)
Net payments for other operating activities		(5 746)	(48 044)
Personnel expenses paid		(1 665 777)	(1 704 220)
Other general administrative expenses paid		(1 251 204)	(1 180 197)
Cash flows from operating activities before changes in operating assets and liabilities		**430 712**	**805 059**
Net (increase) decrease in operating assets			
Mandatory cash balances with the Central Bank of the Russian Federation		(87 662)	(30 241)
Amounts due from credit institutions		4 285 686	(1 031 031)
Loans to customers		(5 208 888)	1 294 658
Net investments in finance leases		(43 711)	(334 484)
Other assets		156 349	130 939
Net (decrease) increase in operating liabilities			
Amounts due to credit institutions		3 711 611	(833 139)
Amounts due to customers		(1 931 517)	2 585 060
Other liabilities		(45 507)	(49 783)
Net cash provided from operating activities before income tax paid		**1 267 073**	**2 537 038**
Income tax paid		(55 486)	(79 895)
Net cash flows provided from operating activities		**1 211 587**	**2 457 143**
Cash flows from investing activities			
Purchase of property and equipment		(76 662)	(196 722)
Proceeds from sale of property and equipment		400	667
Purchase of intangible assets		(95 723)	(154 446)
Purchase of investment securities		(4 642 945)	(3 586 878)
Proceeds from sale and redemption of investment securities		4 608 540	3 034 630
Net cash flows used in investing activities		**(206 390)**	**(902 749)**
Cash flows from financing activities			
Repayment of debt securities issued	17	(130 643)	(1 686 508)
Net cash flows used in financing activities		**(130 643)**	**(1 686 508)**
Effect of exchange rates changes on cash and cash equivalents		339 701	100 176
Net increase (decrease) in cash and cash equivalents		**1 214 255**	**(31 938)**
Cash and cash equivalents as at the beginning of the year	5	3 886 295	3 918 233
Cash and cash equivalents as at the end of the year	5	**5 100 550**	**3 886 295**

Signed and authorised for release on behalf of the Management Board of the Bank:

Olga Lein — Acting Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board / Head of Accounting, Planning and Control Group / Chief accountant

(Thousands of Russian Roubles)

1. Principal activities

These consolidated financial statements include the financial statements of Banca Intesa and its subsidiary, AO "Intesa Leasing", together referred to as the "Bank" and were authorised for release on behalf of the Management Board of the Bank on 19 February 2019.

Banca Intesa is a commercial bank organized in the form of a joint-stock company under the laws of the Russian Federation.

Bank's former name, KMB Bank (Closed Joint-Stock Company), was changed following the merger on 11 January 2010 with ZAO Banca Intesa (the "incorporated Bank"), 100% Russian banking subsidiary of Intesa Sanpaolo S.p.A. (Italy).

The activities of the Bank are regulated by the Central Bank of Russia (the "CBR"). The Bank operates under General Banking License № 2216. The Bank is a member of the state deposit insurance system in the Russian Federation.

The Bank's principal business activities are corporate banking products to small, medium and large businesses and retail banking products and services, including a premium banking segment. The Bank is engaged in a program of the Corporation MSP, the Ministry of Economic Development of the Russian Federation and the CBR to support the businesses of small to medium sized companies by providing them with lending facilities.

The Bank's registered office is located at the following address: 2, Petroverigsky pereulok, Moscow, Russian Federation, 101000.

As at 31 December 2018 the Bank has 6 branches within the Russian Federation in the cities of Saint Petersburg, Nizhniy Novgorod, Ekaterinburg, Novosibirsk, Vladivostok and Rostov-on-Don (2017: 6 branches). The Bank also has 26 offices selling banking products in different cities within the Russian Federation (2017: 31 offices). 5 offices were closed during 2018 (2017: no offices) in course of network optimisation.

As at 31 December 2018, the Bank employed 1 202 people (2017: 1 384).

The Bank has a wholly owned and controlled subsidiary, AO "Intesa Leasing", former ZAO "KMB-Leasing". It is primarily engaged in the provision of finance leases to the Bank's clients and other companies.

The shareholders of the Bank as at 31 December are:

Shareholder	*2018*	*2017*
Intesa Sanpaolo S.p.A. (Italy)	46.9772%	46.9772%
Intesa Sanpaolo Holding International SA (Luxembourg)	53.0228%	53.0228%
Total	**100.0000%**	**100.0000%**

The ultimate controlling party of the Bank is Intesa Sanpaolo S.p.A. (Italy) ("ISP").

Russian business environment

The Bank's operations are primarily located in the Russian Federation. Consequently, the Bank is exposed to the economic and financial markets of the Russian Federation which display characteristics of an emerging market. The legal, tax and regulatory frameworks continue development, but are subject to varying interpretations and frequent changes which together with other legal and fiscal impediments contribute to the challenges faced by entities operating in the Russian Federation.

The conflict in Ukraine and related events has increased the perceived risks of doing business in the Russian Federation. The imposition of economic sanctions on Russian individuals and legal entities by the European Union, the United States of America, Japan, Canada, Australia and others, as well as retaliatory sanctions imposed by the Russian government, has resulted in increased economic uncertainty including more volatile equity markets, a fluctuation of the Russian Rouble, a reduction in both local and foreign direct investment inflows and a significant tightening in the availability of credit. In particular, some Russian entities may be experiencing difficulties in accessing international equity and debt markets and may become increasingly dependent on Russian state banks to finance their operations. The longer term effects of recently implemented sanctions, as well as the threat of additional future sanctions, are difficult to determine.

The consolidated financial statements reflect management's assessment of the impact of the Russian business environment on the operations and financial position of the Bank. The future business environment may differ from management's assessment.

(Thousands of Russian Roubles)

2. Basis of preparation

Statement of compliance

The accompanying consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS").

The Bank is required to maintain its records and prepare its financial statements for regulatory purposes in Russian Roubles in accordance with the Russian accounting and banking legislation and related instructions ("RAL"). These consolidated financial statements are based on the Bank's RAL books and records, as adjusted and reclassified in order to comply with IFRS.

Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that investment securities, derivative financial instruments and buildings are stated at fair value.

Functional and presentation currency

The functional currency of the Bank is the Russian Rouble ("RUB") as, being the national currency of the Russian Federation, it reflects the economic substance of the majority of underlying events and circumstances relevant to them.

The RUB is also the presentation currency for the purposes of these consolidated financial statements.

All financial information presented in RUB is rounded to the nearest thousand, except where indicated.

Changes in data presentation

As at 31 December 2018, the Bank changed presentation of settlements accounts with CCP NCC, which were reclassified from other assets to amounts due from credit institutions. The Management believes that the new presentation provides for a better view of economic substance of these accounts. Comparative data have been reclassified in order to comply with the changes in data presentation in the consolidated financial statements for 2018. The effect of these changes on consolidated statement of financial position as at 31 December 2018 is as follows:

	Before reclassification	Effect of reclassification	After reclassification
Assets			
Amounts due from credit institutions	13 528 737	125 455	13 654 192
Other assets	874 403	(125 455)	748 948

Changes in accounting policies

Accounting policies applied by the Bank in these consolidated financial statements are consistent with those, applied in the consolidated financial statements as at and for the year ended 31 December 2017, except for the effects of new standards effective on 1 January 2018 and further described below:

- IFRS 9 "*Financial Instruments*"
- IFRS 15 "*Revenue from Contracts with Customers"* was issued in May 2014, amended in April 2016 and provides a five-step single model to use when accounting for revenue arising from contracts with customers. According to IFRS 15 the revenue is recognized at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring promised goods or services to a customer. The standard is not applied to revenue related to financial instruments and leases, and as a result, the majority of the Bank's revenue, including net interest income, net income (losses) on operations with investment securities that are within the scope of other IFRS 9 *Financial Instruments*, will not be impacted. The adoption of IFRS 15 didn't have a significant impact on the financial position and performance of the Bank.

Transition to IFRS 9

In July 2014, the IASB issued the final version of IFRS 9 *"Financial Instruments"*. IFRS 9 is effective for annual periods beginning on or after 1 January 2018. In October 2017, the IASB issued *"Prepayment Features with Negative Compensation"* (Amendments to IFRS 9). The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted.

The Bank has adopted IFRS 9 *"Financial Instruments"* issued in July 2014 with a date of initial application of 1 January 2018 and early adopted amendments to IFRS 9 on the same date.

The requirements of IFRS 9 represent a significant change from IAS 39 *"Financial Instruments: Recognition and Measurement"*. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

As permitted by IFRS 9, the Bank has elected to continue to apply the hedge accounting requirements of IAS 39.

The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarized below.

(Thousands of Russian Roubles)

Classification of financial assets and liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

For an explanation of how the Bank classifies financial assets and liabilities under IFRS 9 see Note below.

Impairment of financial assets

IFRS 9 replaces the ‘incurred loss’ model in IAS 39 with an ‘expected credit loss’ model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

Under IFRS 9, credit losses are recognised earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see Note 3.

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

- Comparative periods have not been restated. Differences in the carrying amounts of financial assets and liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented as at 31 December 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented as at 31 December 2018 under IFRS 9.
- The determination of the business model within which a financial asset is held has been made on the basis of the facts and circumstances that existed at the date of initial application.
- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Bank has assumed that credit risk on the asset had not increased significantly since its initial recognition.

Analysis of impact on the consolidated financial statements

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Bank’s financial assets and liabilities as at 1 January 2018:

	Original classification under IAS 39	New classification under IFRS 9	Note	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Financial assets					
Cash and cash equivalents	Loans and receivables	Amortised cost	5	3 886 295	3 886 295
Amounts due from credit institutions	Loans and receivables	Amortised cost	6	13 528 737	13 530 353
Investment securities – debt	Available for sale	FVOCI	7	4 130 899	4 130 899
Loans to customers	Loans and receivables	Amortised cost	9	28 995 088	28 436 894
Net investments in finance leases	-	-	10	1 334 117	1 332 800
Other financial assets	Loans and receivables	Amortised cost	14	230 814	230 814
Total financial assets				**52 105 950**	**51 548 055**
Financial liabilities					
Amounts due to credit institutions	Amortised cost	Amortised cost	15	5 884 650	5 884 650
Amounts due to customers	Amortised cost	Amortised cost	16	30 527 105	30 527 105
Debt securities issued	Amortised cost	Amortised cost	17	3 186 066	3 186 066
Subordinated loan	Amortised cost	Amortised cost	17	2 304 839	2 304 839
Other financial liabilities	Amortised cost	Amortised cost	14	224 171	224 171
Allowance for loans commitments and financial guarantees issued	-	-	14, 23	247 321	203 976
Total financial liabilities				**42 374 152**	**42 330 807**

The Bank’s accounting policies on the classification of financial instruments under IFRS 9 are set out in Note 4. The application of these policies resulted in the reclassifications set out in the table above and explained below.

(Thousands of Russian Roubles)

The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018:

	IAS 39 carrying amount as at 31 December 2017 - opening balance	Reclassification to FVOCI – debt	Remeasure-ment	IFRS 9 carrying amount as at 1 January 2018 – closing balance
Financial assets				
Amortised cost				
Cash and cash equivalents	3 886 295	-	-	3 886 295
Amounts due from credit institutions	13 528 737	-	1 616	13 530 353
Loans to customers	28 995 088	-	(558 194)	28 436 894
Total amortised cost	**46 410 120**	**-**	**(556 578)**	**45 835 542**
Net investments in finance leases	1 334 117		(1 317)	1 332 800
Available-for-sale				
Investment securities	4 130 899	(4 130 899)	-	-
FVOCI – debt				
Investment securities	-	4 130 899	-	4 130 899
Total FVOCI	**4 130 899**	**-**	**-**	**4 130 899**
Provision for loans commitments and financial guarantee contracts issued	(247 321)	-	43 345	(203 976)

As a result of adoption of IFRS 9 there were no reclassification or remeasurement of financial liabilities.

The following table analyses the impact, net of tax, of transition to IFRS 9 on revaluation reserve for debt investment securities and accumulated losses. There is no impact on other components of equity.

	Revaluation reserve for debt investment securities (2017: for available-for-sale securities)	Accumulated losses
Closing balance under IAS 39 (31 December 2017)	22 802	(586 463)
Recognition of expected credit losses under IFRS 9 (including loan commitments and financial guarantee contracts)	-	(414 781)
Recognition of expected credit losses under IFRS 9 for debt investment securities at FVOCI	3 142	-
Opening balance under IFRS 9 (1 January 2018)	**25 944**	**(1 001 244)**

The following table reconciles:

- the closing impairment allowance for financial assets in accordance with IAS 39 and provisions for loan commitments and financial guarantee contracts in accordance with IAS 37 "*Provisions, Contingent Liabilities and Contingent Assets"* as at 31 December 2017; to
- the opening allowance for credit losses determined in accordance with IFRS 9 as at 1 January 2018.

The table below summarizes financial assets by measurement categories in accordance with IAS 39 and IFRS 9, and shows separately the effect of the changes in the measurement category on the loss allowance as at the date of initial application of IFRS 9, i.e. as at 1 January 2018.

	Impairment allowance and provisions		
	31 December 2017 (IAS 39/IAS 37)	Remeasu-rement	1 January 2018 (IFRS 9)
Available-for-sale debt investment securities under IAS 39 / debt investment securities at FVOCI under IFRS 9	-	(3 928)	(3 928)
Total measured at FVOCI	**-**	**(3 928)**	**(3 928)**
Loans and receivables under IAS 39 / financial assets at amortised cost under IFRS 9 (includes cash and cash equivalents, amounts due from credit institutions and loans to customers)	(4 526 089)	(556 578)	(5 082 667)
Total measured at amortised cost	**(4 526 089)**	**(556 578)**	**(5 082 667)**
Net investments in finance leases	(94 596)	(1 317)	(95 913)
Loans commitments and financial guarantee contracts issued	(247 321)	43 345	(203 976)

Change in presentation of comparative information

On adoption of IFRS 9 the Bank changed presentation of certain captions in the primary forms of the consolidated financial statements. Comparative information is reclassified to conform to changes in presentation in the current period.

The effect of main changes in presentation of the consolidated financial statements is as follows:

- "Available-for-sale securities" are presented within "Investment securities" line item in the consolidated statement of financial position;
- Interest income on net investments in finance leases is presented within "Other interest income" line item in the consolidated statement of profit and loss and other comprehensive income.
- 'Purchase of available-for-sale securities' and 'proceeds from sale and redemption of available-for-sale securities' line items are presented within 'purchase of investment securities' and 'proceeds from sale and redemption of investment securities' line items respectively in the consolidated statement of cash flows.

3. Significant accounting judgments, estimates and assumptions

When preparing the consolidated financial statements Management uses judgements, assumptions and estimates that affect accounting policy application and the amount of presented assets and liabilities, income and expenses. Actual results may differ from those estimates.

A summary of key accounting judgements most significantly affecting recognized amounts in the consolidated financial statements and estimates that may lead to a significant adjustments of carrying amounts of assets and liabilities in the next financial year include the following:

- classification of financial assets: assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding – Note 4, Assessment of the business model
- estimation of allowances for expected credit losses (ECL) on financial instruments
- estimates of fair values of buildings.

Estimation of allowances for expected credit losses (ECL) on financial instruments

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Bank's historical experience and expert credit assessment and including forward-looking information.

The objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure (adjusted where relevant for changes in prepayment expectations).

Credit risk grades

The Bank allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 2 and 3.

Each exposure is allocated to a credit risk grade at initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. The monitoring typically involves use of the following data.

Corporate exposure	Corporate and retail exposures
▪ Regularly reviewed information about the borrower, including financial statements, management accounts, budgets and projections	▪ Payment discipline and overdue status
▪ Information provided by credit rating agencies, mass media, changes in external credit ratings	▪ Renegotiated loans' terms
▪ Quoted bond and credit default swap (CDS) prices for the borrower where available	▪ Existing and expected changes in business, financial and economic environment
▪ Actual and expected significant changes in borrower's political, legal and technological environment or its operating activities	

Generating the term structure of PD

Credit risk grades are a primary input into the determination of the term structure of PD for exposures. The Bank collects performance and default information about its credit risk exposures analysed by type of product and borrower as well as by credit risk grading.

The Bank employs statistical models to analyses the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

The Bank uses expert judgment in assessment of forward-looking information. This assessment is based also on external information (see discussion below on incorporation of forward-looking information). The Bank then uses these forecasts to adjust its estimates of PDs.

Determining whether credit risk has increased significantly

The criteria for determining whether credit risk has increased significantly vary by client and include quantitative and qualitative factors.

The Bank will deem the credit risk of a particular exposure to have increased significantly since initial recognition if, based on the Bank's modelling, financial position of a client deteriorated significantly or early warning signals occurred.

Using its expert credit judgement and, where possible, relevant historical experience, the Bank may determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

The Bank considers that a credit risk significantly increased when an asset is more than 30 days past due and the overdue amount exceeds 5% threshold of total exposure on the counterparty. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower. The effect of the 5% threshold application is insignificant for the size of allowance for expected credit losses (ECL).

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value in accordance with the accounting policy set out in Note 4.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data at initial recognition and the original contractual terms.

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities') to maximize collection opportunities and minimize the risk of default. Under the Bank's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy.

For financial assets modified as part of the Bank's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Bank's ability to collect interest and principal and the Bank's previous experience of similar forbearance action. As part of this process, the Bank evaluates the borrower's payment performance against the modified contractual terms and considers various behavioral indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired / in default. A customer needs to demonstrate consistently good payment behavior over a period of time before the exposure is no longer considered to be credit-impaired/ in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to 12-month ECL.

Definition of default

The Bank considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held); or
- the borrower is past due more than 90 days on any material credit obligation to the Bank. Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than the current amount outstanding.

In assessing whether a borrower is in default, the Bank considers indicators that are:

- qualitative – e.g. breaches of covenant;
- quantitative – e.g. overdue status and non-payment on another obligation of the same issuer to the Bank; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

A loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment. In addition, a retail loan that is overdue for 90 days or more is considered impaired.

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Bank considers the following factors.

- the market's assessment of creditworthiness as reflected in the bond yields.
- the rating agencies' assessments of creditworthiness.
- the country's ability to access the capital markets for new debt issuance.
- the probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- the international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

Incorporating of forward-looking information

The Bank incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. The Bank uses expert judgment in assessment of forward-looking information. This assessment is based also on external information. External information may include economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Bank operates, such as the European Central Bank and European Banking Authority statistics.

The European Banking Authority (EBA) EU-wide stress testing exercise requires banks to use the outcome of the adverse macro-financial scenario for variables such as GDP, inflation, unemployment, asset prices and interest rates in order to estimate the potential adverse impact on profit generation and capital. The Bank as part of Intesa Sanpaolo Group uses coefficients determined for Russia by EBA to account for different scenarios and to include forward looking information by means of calculation of add-ons for PD, LGD and allowance in general.

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- probability of default (PD);
- loss given default (LGD);
- exposure at default (EAD).

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

PD estimates are estimates at a certain date, which are calculated based on statistical rating models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally compiled data comprising both quantitative and qualitative factors. Where it is available, market data may also be used to derive the PD for large corporate counterparties. If a counterparty or exposure migrates between rating classes, then this will lead to a change in the estimate of the associated PD. PDs are estimated considering the contractual maturities of exposures and estimated prepayment rates.

The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the type of counterparty and collateral and recovery costs of any collateral that is integral to the financial asset. For loans secured by retail property, LTV ratios are a key parameter in determining LGD. LGD estimates are recalibrated for different economic scenarios and, for real estate lending, to reflect possible changes in property prices. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortization. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount drawn, as well as potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts.

As described above, and for financial assets in Stage 1 and measured using 12-month PD, the Bank measures ECL considering the risk of default over the period, which does not exceed contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics that include:

- instrument type;
- credit risk grades;
- collateral type;
- collateral coverage;
- LTV ratio for retail mortgages;
- annual turnover and type of business.

The groupings are subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

For portfolios in respect of which the Bank has limited historical data the estimates provided by Intesa Sanpaolo Group (‘ISP’) are taken to calculate PD and LGD. In the model developed by ISP for Sovereign counterparties PD is determined using a two-stage process based on quantitative output (mainly, expected default frequency based on rating migration matrices for S&P, Moody’s and Fitch ratings) and a final qualitative assessment agreed with ISP Research Department. For banks PD calculation is based on matrices that describe transitions between rating classes of counterparties in the ISP portfolio. LGD calculation is based mainly on Moody’s data about defaults and recoveries.

For credit-impaired loans and net investments in finance leases the Bank estimates loan impairment based on an analysis of the future cash flows. In determining the impairment allowance management assumes a delay in obtaining proceeds from the foreclosure of collateral and discounts the estimated fair value of collateral based on the type of asset.

Revaluation of buildings

After initial recognition buildings are stated at revalued amounts that represent fair value at the date of revaluation, net of subsequent accumulated depreciation and accumulated impairment losses. The revaluation is performed on an annual basis.

As at 31 December 2017 the fair value of buildings was determined by a recognized independent appraiser firm with appropriate qualifications and experience in valuations of similar real estate property by location and type.

As at 31 December 2018 the Bank performed internal valuation of buildings.

The key valuation assumptions include selection of comparable real estate property; adjustments to fair values of comparative properties to account for differences in their condition and location as compared to the properties being revalued; projected cash flows and discount rates; allocation of part of fair value to land plot if the Bank does not have a title for long-term lease of the land plot.

4. Significant accounting policies

The following accounting policies are consistently applied in preparation of these consolidated financial statements, except for the policies, related to the Bank's adoption of IFRS 9 and IFRS 15 (Note 2), effective from 1 January 2018.

Basis of consolidation

Business combinations

Business combinations are accounted for using the acquisition method as at the date when control is transferred to the Bank.

The Bank measures goodwill at the acquisition date as the fair value of the consideration transferred (including the fair value of any previously-held equity interest in the acquiree if the business combination is achieved in stages) and the recognised amount of any non-controlling interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed. When the excess is negative, a bargain purchase gain is recognised immediately in profit or loss.

The Bank elects on transaction-by-transaction basis whether to measure non-controlling interests at fair value, or at their proportionate share of the recognised amount of the identifiable net assets of the acquiree, at the acquisition date.

Subsidiaries

Subsidiaries are investees controlled by the Bank. The Bank controls an investee when it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. In particular the Bank consolidates investees that it controls on the basis of de facto circumstances. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Acquisitions and disposals of non-controlling interests

The Bank accounts for the acquisitions and disposals of non-controlling interests as transactions with equity holders in their capacity as equity holders. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the parent.

Foreign currency transactions

Transactions in foreign currencies are translated to the functional currency of the Bank at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the reporting period. Foreign currency differences arising on retranslation are generally recognised in profit or loss.

Interest income and expense

Effective interest rate

Interest income and expense are recognised in profit or loss using the effective interest method. The "Effective interest rate" is 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; or
- the amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments other than credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not expected credit losses. For credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including expected credit losses. The accounting policy effective prior to 1 January 2018 (date of transition to IFRS 9) did not have specific provisions for calculation of effective interest rate on credit-impaired financial assets.

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

Amortised cost and gross carrying amount

The “Amortised cost” of a financial asset or liability is the amount at which the financial asset or liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any allowance for credit losses (or impairment allowance before 1 January 2018).

The “Gross carrying amount of a financial asset” measured at amortised cost is the amortised cost of a financial asset before adjusting for any expected credit loss allowance (or impairment allowance before 1 January 2018).

Calculation of interest income and expense

In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

Information on when financial assets are credit-impaired is provided further and in Note 3.

Presentation

Interest income and expense presented include interest on financial assets and liabilities measured at amortised cost calculated using the effective interest method and interest on debt instruments measured at FVOCI calculated on an effective interest basis.

Other interest income includes interest on net investment in finance leases.

Fair value measurement principles

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

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

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

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

Where the transaction price in a non-active market is different from the fair value from other observable current market transactions in the same instrument or based on a valuation technique whose variables include only data from observable markets, the Bank immediately recognises the difference between the transaction price and fair value (a “Day 1” profit) in profit or loss. In cases where data used is not observable, the difference between the transaction price and model value is only recognised in profit or loss when the inputs become observable, or when the instrument is derecognised.

If an asset or a liability measured at fair value has a bid price and an ask price, the Bank measures assets and long positions at the bid price and liabilities and short positions at the ask price.

Financial assets and liabilities (accounting policy applicable after 1 January 2018)

Classification of financial instruments

On initial recognition, a financial asset is classified as measured at:

- amortised cost or
- FVOCI or
- FVTPL.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- the 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 dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

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

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

For debt financial assets measured at FVOCI, gains and losses are recognised in other comprehensive income, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- interest revenue using the effective interest method;
- ECL and reversals; and
- foreign exchange gains and losses.

When a debt financial asset measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss.

All other financial assets are classified as measured at FVTPL.

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

Business model assessment

The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

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

For the purposes 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 other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

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

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank’s claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

For a portfolio of long-term fixed rate loans for which the Bank has the option to revise the interest rate following the change of key rate set by the CBR the borrowers have an option to either accept the revised rate or redeem the loan at par without penalty. Thus the Bank has determined that for such loans the contractual cash flows are solely payments of principal and interest because the option varies the interest rate in a way that is consideration for the time value of money, credit risk, other basic lending risks and costs associated with the principal amount outstanding. Instead, the Bank considers these loans as in essence floating rate loans.

Reclassification

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets. The Bank should reclassify financial assets if the Bank changes its business model for managing those financial assets. Such changes are expected to be very infrequent. Such changes are determined by the Bank’s senior management as a result of external or internal changes and must be significant to the Bank’s operations and demonstrable to external parties. Accordingly, a change in the Bank’s business model will occur only when the Bank either begins or ceases to perform an activity that is significant to its operations; for example, when the Bank has acquired, disposed of or terminated a business line.

Financial liabilities are not reclassified subsequent to their initial recognition.

Derecognition

Financial assets. From 1 January 2018 any cumulative gain/loss recognised in other comprehensive income in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability.

Financial liabilities. From 1 January 2018 any cumulative gain/loss recognised in other comprehensive income in respect of financial liabilities designated as at FVTPL is not recognised in profit or loss on derecognition of such financial liabilities.

Modification of financial assets and liabilities

Financial assets

If the terms of a financial asset are modified, the Bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different (referred to as ‘substantial modification’), then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and a new financial asset is recognised at fair value. Changes in cash flows on existing financial assets or financial liabilities are not considered as modification, if they result from existing contractual terms, e.g. changes in interest rates initiated by the Bank due to changes in the CBR key rate, if the loan contract entitles the Bank to do so.

The Bank assesses whether the modification is substantial based on quantitative and qualitative factors in the following order: qualitative factors, quantitative factors, combined effect of qualitative and quantitative factors. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset deemed to have expired. In making this evaluation the Bank analogizes to the guidance on the derecognition of financial liabilities.

The Bank concludes that the modification is substantial as a result of the following qualitative factors:

- change the currency of the financial asset;
- change of counterparty, unless the new counterparty is a company belonging to the same economic group of the original borrower;
- debt-equity swap;
- datium in solutum (i.e. when repayment depends on the fair value of an asset);
- clauses “pay if you can”, i.e. contractual terms that allow the borrower to repay if and when he can, without constraints. The concept of “pay if you can” does not concern situations such as delay in repayment in accordance with the contractual schedule, or moratorium for the payment of interest for a certain period of time. In fact, such agreements results in contractual conditions that can be considered as being similar, although indirectly, to a reduction of the interest rate;
- other material changes in the nature of the contract such as exposure to new risk components (returns linked to equity components or commodity, leverage, etc.).

If the cash flows of the modified asset carried at amortised cost are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, the Bank recalculates the gross carrying amount of the financial asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss. The gross carrying amount of the financial asset is recalculated as the present value of the renegotiated or modified contractual cash flows that are discounted at the financial asset's original effective interest rate. Any costs or fees incurred adjust the carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset. If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

For fixed-rate loans, where the borrower has an option to prepay the loan at par without significant penalty, the Bank treats the modification of an interest rate to a current market rate using the guidance on floating-rate financial instruments. This means that the effective interest rate is adjusted prospectively.

As part of credit risk management activities, the Bank renegotiates loans to customers in financial difficulties (referred to as “forbearance activities”). If the Bank plans to modify a financial asset in a way that would result in forgiveness of part of the existing contractual cash flows, then a portion of the asset is written off before the modification takes place. This is likely to result in the remaining contractual cash flows that are still recognised as the original financial asset at the point of modification to be similar to the new modified contractual cash flows. If based on quantitative assessment the Bank concludes that modification of financial assets modified as part of the Bank’s forbearance policy is not substantial, the Bank performs qualitative evaluation of whether the modification is substantial.

Financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability extinguished and the new financial liability with modified terms is recognised in profit or loss.

If a modification (or exchange) does not result in the derecognition of the financial liability the Bank applies accounting policy consistent with the requirements for adjusting the gross carrying amount of a financial asset when a modification does not result in the derecognition of the financial asset, i.e. the Bank recognises any adjustment to the amortised cost of the financial liability arising from such a modification (or exchange) in profit or loss at the date of the modification (or exchange).

The Bank performs a quantitative and qualitative evaluation of whether the modification is substantial considering qualitative factors, quantitative factors and combined effect of qualitative and quantitative factors. The Bank concludes that the modification is substantial as a result of the following qualitative factors:

- change the currency of the financial liability;
- change in collateral or other credit enhancement;
- inclusion of conversion option;
- change in the subordination of the financial liability.

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

Impairment

The Bank recognises loss allowances for expected credit losses (ECL) on the following financial instruments that are not measured at FVTPL:

- loans to customers;
- debt investment securities;
- net investments in financial leases;
- financial guarantee contracts issued; and
- loan commitments issued.

The Bank measures ECL allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments (other than net investments in finance leases) on which credit risk has not increased significantly since their initial recognition (see Note 3).

The Bank considers a debt security to have low credit risk when their credit risk rating is equivalent to the globally understood definition of "investment grade".

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- *financial assets that are not credit-impaired at the reporting date:* as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);
- *financial assets that are credit-impaired at the reporting date:* as the difference between the gross carrying amount and the present value of estimated future cash flows;
- *undrawn loan commitments:* as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- *financial guarantee contracts:* the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

See also Note 3.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised and ECL are measured as follows.

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.
- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired. A financial asset is 'credit-impaired' when default has occurred (Note 3).

Presentation of allowance for ECL

ECL allowances are presented in the consolidated statement of financial position as follows:

- *financial assets measured at amortised cost*: as a deduction from the gross carrying amount of the assets;
- *loan commitments and financial guarantee contracts*: generally, as a provision;
- *where a financial instrument includes both a drawn and an undrawn component, and the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component*: the Bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- *debt instruments measured at FVOCI*: no loss allowance is recognised in the consolidated statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-offs

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

Financial assets and liabilities (accounting policy applicable before 1 January 2018)

Classification (accounting policy applicable before 1 January 2018)

Financial instruments at fair value through profit or loss are financial assets or liabilities that are:

- acquired or incurred principally for the purpose of selling or repurchasing in the near term;
- part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking;
- derivative financial instruments (except for derivative that is a financial guarantee contract or a designated and effective hedging instruments) or,
- upon initial recognition, designated as at fair value through profit or loss.

The Bank may designate financial assets and liabilities at fair value through profit or loss where either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis;
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise or,
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

All trading derivatives in a net receivable position (positive fair value), as well as options purchased, are reported as assets. All trading derivatives in a net payable position (negative fair value), as well as options written, are reported as liabilities.

Management determines the appropriate classification of financial instruments in this category at the time of the initial recognition. Derivative financial instruments and financial instruments designated as at fair value through profit or loss upon initial recognition are not reclassified out of at fair value through profit or loss category.

Financial assets that would have met the definition of loans and receivables may be reclassified out of the fair value through profit or loss or available-for-sale category if the Bank has an intention and ability to hold them for the foreseeable future or until maturity. Other financial instruments may be reclassified out of at fair value through profit or loss category only in rare circumstances. Rare circumstances arise from a single event that is unusual and highly unlikely to recur in the near term.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Bank:

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

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity, other than those that:

- the Bank upon initial recognition designates as at fair value through profit or loss;
- the Bank designates as available-for-sale or,
- meet the definition of loans and receivables.

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as loans and receivables, held-to-maturity investments or financial instruments at fair value through profit or loss.

Initial recognition of financial instruments (accounting policy applicable before 1 January 2018)

Financial assets and liabilities are recognised in the consolidated statement of financial position when the Bank becomes a party to the contractual provisions of the instrument. All regular way purchases of financial assets are accounted for at the settlement date.

Subsequent measurement of financial instruments (accounting policy applicable before 1 January 2018)

A financial asset or liability is initially measured at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

Subsequent to initial recognition, financial assets, including derivatives that are assets, are measured at their fair values, without any deduction for transaction costs that may be incurred on sale or other disposal, except for:

- loans and receivables which are measured at amortised cost using the effective interest method;
- held-to-maturity investments that are measured at amortised cost using the effective interest method;
- investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured which are measured at cost.

All financial liabilities, other than those designated at fair value through profit or loss and financial liabilities that arise when a transfer of a financial asset carried at fair value does not qualify for derecognition, are measured at amortised cost.

Amortised cost (accounting policy applicable before 1 January 2018)

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Gains and losses on subsequent measurement (accounting policy applicable before 1 January 2018)

A gain or loss arising from a change in the fair value of a financial asset or liability is recognised as follows:

- a gain or loss on a financial instrument classified as at fair value through profit or loss is recognised in profit or loss;
- a gain or loss on an available-for-sale financial asset is recognised as other comprehensive income in equity (except for impairment losses and foreign exchange gains and losses on debt financial instruments available-for-sale) until the asset is derecognised, at which time the cumulative gain or loss previously recognised in equity is recognised in profit or loss. Interest in relation to an available-for-sale financial asset is recognised in profit or loss using the effective interest method.

For financial assets and liabilities carried at amortised cost, a gain or loss is recognised in profit or loss when the financial asset or liability is derecognised or impaired, and through the amortization process.

Derecognition (accounting policy applicable before 1 January 2018)

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability in the consolidated statement of financial position. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Bank enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised.

In transactions where the Bank neither retains nor transfers substantially all the risks and rewards of ownership of a financial asset, it derecognises the asset if control over the asset is lost.

In transfers where control over the asset is retained, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred assets.

If the Bank purchases its own debt, it is removed from the consolidated statement of financial position and the difference between the carrying amount of the liability and the consideration paid is included in gains or losses arising from early retirement of debt.

The Bank writes off assets deemed to be uncollectible.

Impairment of financial assets (accounting policy applicable before 1 January 2018)

The Bank assesses at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired. If any such evidence exists, the Bank determines the amount of any impairment loss.

A financial asset or group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and that event (or events) has had an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, breach of loan covenants or conditions, restructuring of a financial asset or group of financial assets that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, deterioration in the value of collateral, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers in the group, or economic conditions that correlate with defaults in the group.

In addition, for an investment in an equity security available-for-sale a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

Available-for-sale financial assets

Impairment losses on available-for-sale financial assets are recognised by transferring the cumulative loss that is recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

Financial assets carried at amortised cost

Financial assets carried at amortised cost consist principally of loans and other receivables (“loans and receivables”). The Bank reviews its loans and receivables to assess impairment on a regular basis.

The Bank first assesses whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for loans and receivables that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed loan or receivable, whether significant or not, it includes the loan or receivable in a group of loans and receivables with similar credit risk characteristics and collectively assesses them for impairment. Loans and receivables that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on a loan or receivable has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan or receivable and the present value of estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan or receivable’s original effective interest rate. Contractual cash flows and historical loss experience adjusted on the basis of relevant observable data that reflect current economic conditions provide the basis for estimating expected cash flows.

In some cases the observable data required to estimate the amount of an impairment loss on a loan or receivable may be limited or no longer fully relevant to current circumstances. This may be the case when a borrower is in financial difficulties and there is little available historical data relating to similar borrowers. In such cases, the Bank uses its experience and judgment to estimate the amount of any impairment loss.

All impairment losses in respect of loans and receivables are recognised in profit or loss and are only reversed if a subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

When a loan is uncollectable, it is written off against the related allowance for loan impairment. The Bank writes off a loan balance (and any related allowances for loan losses) when management determines that the loans are uncollectible and when all necessary steps to collect the loan are completed.

Financial assets carried at cost

Financial assets carried at cost include unquoted equity instruments included in available-for-sale financial assets that are not carried at fair value because their fair value cannot be reliably measured. If there is objective evidence that such investments are impaired, the impairment loss is calculated as the difference between the carrying amount of the investment and the present value of the estimated future cash flows discounted at the current market rate of return for a similar financial asset.

All impairment losses in respect of these investments are recognised in profit or loss and cannot be reversed.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, amounts due from the CBR (excluding mandatory cash balances with the CBR) and assets that can be converted into cash within one day and are free from contractual encumbrances. All short-term interbank placements are included in amounts due from other banks. Cash and cash equivalents are carried at amortised cost.

Mandatory cash balances with the CBR

Credit institutions are required to maintain a non-interest earning cash deposit (mandatory cash balances) with the CBR, the amount of which depends on the level of funds attracted by the credit institution. The Bank's ability to withdraw such a deposit is significantly restricted by the statutory legislation. Mandatory cash balances with the CBR are not available to finance the Bank's day-to-day operations and hence are not considered as part of cash and cash equivalents for the purposes of the consolidated statement of cash flows.

Loans to customers

In the reporting period loans to customers comprise only instruments measured at amortised cost, which are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method.

Investment securities

In the reporting period the investment securities comprise only debt securities measured at FVOCI.

Financial guarantees and loan commitments

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. Loan commitments are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value and the initial fair value is amortised over the life of the guarantee or the commitment. Subsequently, they are measured at the higher of this amortised amount and the amount of loss allowance.

In the reporting period the Bank did not issue loan commitments at a below-market interest rate that are measured at FVTPL.

The Bank recognises loss allowance for loan commitments and issued financial guarantees which are presented within other liabilities as provisions.

Repurchase and reverse repurchase agreements

Securities sold under sale and repurchase ("repo") agreements are accounted for as secured financing transactions, with the securities retained in the consolidated statement of financial position and the counterparty liability included in amounts payable under repo transactions within amounts due to credit institutions or amounts due to customers, as appropriate. The difference between the sale and repurchase prices represents interest expense and is recognised in profit or loss over the term of the repo agreement using the effective interest method.

Securities purchased under agreements to resell ("reverse repo") are recorded as amounts receivable under reverse repo transactions within due from banks or loans to customers, as appropriate. The difference between the purchase and resale prices represents interest income and is recognised in profit or loss over the term of the reverse repo agreement using the effective interest method.

If assets purchased under an agreement to resell are sold to third parties, the obligation to return securities is recorded as a trading liability and measured at fair value.

Derivative financial instruments

Derivative financial instruments include swaps, forwards, spot transactions in interest rates, foreign exchanges and any combinations of these instruments.

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Changes in the fair value of derivatives are recognised immediately in profit or loss.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to government, amounts due to credit institutions, amounts due to customers, other borrowed funds, subordinated loan and debt securities issued. After initial recognition, borrowings are subsequently measured at amortised cost using the effective interest method.

Offsetting

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

Net investments in finance leases

Lease receivables are recognized at a value equal to the net investment in the lease, starting from the date of commencement of the lease term.

Finance income is based on a pattern reflecting a constant periodic rate of return on the net investment outstanding. Initial direct costs are included in the initial measurement of the lease receivables.

When the Bank takes possession of the collateral under terminated lease contracts, it measures the assets at the lower of net realisable value and amortised historical cost of the inventory.

Operating leases

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as expenses on a straight-line basis over the lease term and included in other operating expenses.

Property and equipment

Items of property and equipment are stated at cost, excluding costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment losses, except for buildings, which are stated at revalued amounts as described below.

Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Buildings are subject to revaluation on a regular basis. The frequency of revaluation depends on the movements in the fair values of the buildings being revalued. A revaluation increase on a premise is recognised as other comprehensive income except to the extent that it reverses a previous revaluation decrease recognised in profit or loss, in which case it is recognised in profit or loss. A revaluation decrease on a premise is recognised in profit or loss except to the extent that it reverses a previous revaluation increase recognised as other comprehensive income directly in equity, in which case it is recognised in other comprehensive income.

Depreciation commences on the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and ready for use. Land is not depreciated. Depreciation is calculated on a straight-line basis (calculated by quantity of days of the corresponding month) over the estimated useful lives of the assets using the following rates:

	Annual depreciation rate	Useful life
Buildings	1.3 – 3,3%	30 – 75 years
Office and computer equipment	15 – 33%	3 – 7 years
Intangible assets	20 – 50%	2 – 5 years

The residual values of the assets, useful lives and methods are reviewed, and adjusted as appropriate, at each reporting period.

Costs related to repairs and renewals are charged when incurred and included in other operating expenses, unless they qualify for capitalisation.

The Bank accounts for capital expenditures related to acquisition of equipment subject to leasing as equipment purchased for leasing purposes. These expenditures are accumulated until the equipment is ready for use and transferred to the lessee.

Intangible assets

Intangible assets include computer software and licenses.

Intangible assets acquired separately are measured on initial recognition at cost and are subsequently stated at cost less accumulated amortization and accumulated impairment.

Intangible assets may have finite or indefinite useful lives:

- if useful live is finite amortization is charged to profit or loss on a straight-line basis over the useful economic live, not exceeding a period of 5 years. An intangible asset is assessed for impairment whenever there is an indication that the intangible asset may be impaired.
- intangible assets with an indefinite useful life are not amortised. The useful life of such assets is reviewed at each reporting period to determine whether events and circumstances continue to support an indefinite useful life assessment for such assets.

  The Bank tests intangible assets with an indefinite useful life for impairment by comparing their recoverable amounts with the corresponding carrying amounts annually, and whenever there is an indication that an intangible asset may be impaired.

Intangible assets useful life of which has ended (licenses and computer software), should be written-off twice a year, in the end of the second and the fourth quarter or based on the order of IT Department.

Repossessed collateral

Repossessed collateral represents non-financial assets obtained by the Bank in the course of settlement of overdue loans. These assets are initially recognised at fair value when obtained and can be included in property and equipment, inventories or investment property or other assets depending on their nature and the Bank's intention and are subsequently remeasured and accounted for in accordance with the accounting policies for the respective categories.

Non financial assets

Non-financial assets, other than deferred taxes, are assessed at each reporting date for any indications of impairment. The recoverable amount of non financial assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is recognised when the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

All impairment losses in respect of non financial assets are recognised in profit or loss and reversed only if there has been a change in the estimates used to determine the recoverable amount. Any impairment loss reversed is only reversed to the extent that the asset’s carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognised.

Provisions

A provision is recognised if as a result of a past event the Bank has a present legal or constructive obligation based on an existing practice, which can be estimated reliably and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation. The provision amount is determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Amortization of discount, which represents a time value of money, is recognized as a financial expense.

Contingencies and credit related commitments

Contingent liabilities are not recognised in the consolidated statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognised in the consolidated statement of financial position but disclosed when an inflow of economic benefits is probable.

In the normal course of business, the Bank enters into credit related commitments including undrawn loan commitments, guarantees and letters of credit. Guarantees are initially recognised in the consolidated statement of financial position at fair value net of associated transaction costs within other liabilities, and subsequently are measured at the higher of the amortised premium or the amount of provision for losses under the guarantee.

Provision for credit losses for guarantees and letters of credit issued is estimated in the same way as for loans to customers.

The premium received is recognised in profit or loss on a straight-line basis over the life of the guarantee.

Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issuance of new shares, other than on a business combination, are recognised as a deduction from equity, net of any tax effects.

Share premium represents the excess of contributions over the nominal value of the shares issued.

Funds provided by the Bank’s shareholders in the form of debt free financing are classified as other capital reserves.

The ability of the Bank to declare and pay dividends is subject to the rules and regulations of the Russian legislation.

Dividends in relation to ordinary shares are reflected as an appropriation of retained earnings in the period when they are declared.

Taxation

The current income tax expense is calculated in accordance with the regulations of the Russian Federation.

Income tax comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to items of other comprehensive income or transactions with shareholders recognised directly in equity, in which case it is recognised within other comprehensive income or directly within equity.

Current tax expense is the expected tax payable on the taxable profit for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affect neither accounting nor taxable profit and temporary differences related to investments in subsidiaries where the Bank is able to control the timing of the reversal of the temporary difference and it is probable that they will not reverse in the foreseeable future.

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

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

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

Fee and commission income

Fee and commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the effective interest rate.

A contract with a customer that results in a recognised financial instrument in the consolidated financial statements of the Bank 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.

The Bank earns other fee and commission income at a point in time or over the time with consideration to how performance obligation is satisfied by providing services to the customers.

Segment reporting

An operating segment is a component of the Bank that is engaged in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the Bank); whose operating results are regularly reviewed by the chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. Substantially all of the Bank's activities relate to provision of financial services mostly to corporate customers (small, medium and large business). Therefore, management concluded that the Bank has a single reportable segment.

New standards issued but not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective as at 31 December 2018, and are not applied in preparing these consolidated financial statements. Of these pronouncements, potentially the following will have an impact on the financial position and performance. The Bank plans to adopt these pronouncements when they become effective.

IFRS 16 Leases

The standard is effective for annual periods beginning on or after 1 January 2019. Early adoption is permitted for entities that apply IFRS 15 “Revenue from Contracts with Customers” at or before the date of initial application of IFRS 16.

IFRS 16 replaces existing leases guidance including IAS 17 “Leases”, IFRIC 4 “Determining whether an Arrangement contains a Lease”, SIC-15 “Operating Leases—Incentives” and SIC-27 “Evaluating the Substance of Transactions Involving the Legal Form of a Lease”.

IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. In addition, the nature of expenses related to those leases will now change as IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. There are recognition exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

The Bank plans to apply IFRS 16 initially on 1 January 2019, using the modified retrospective approach with optional practical expedients. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

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

So far, the most significant impact identified is that the Bank will recognise new assets and liabilities for its operating leases of office buildings. As at 31 December 2018, the Bank's future minimum lease payments under non-cancellable operating leases amounted to RUB 824 328 thousand, on an undiscounted basis (see Note 23).

Other standards

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

- Annual Improvements to IFRSs 2015-2017
- Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 and IAS 28).
- IFRIC 23 *“Uncertainty over Income Tax Treatments”*
- IFRS 17 *“Insurance Contracts”*.

(Thousands of Russian Roubles)

5. Cash and cash equivalents

Cash and cash equivalents as at 31 December comprise:

	2018	2017
Cash on hand	749 436	742 319
Correspondent accounts with the CBR	2 549 376	1 988 527
Correspondent accounts and overnight placements with other banks		
- rated from A- to A+	942 639	36 764
- rated from BBB- to BBB+	856 053	1 111 761
- rated from BB- to BB+	19	-
- not rated	3 027	6 924
Cash and cash equivalents	**5 100 550**	**3 886 295**

The credit rating in disclosed above using credit scale of international rating agencies Standard& Poor's and Fitch.

As at 31 December 2018, the Bank has one bank (2017: one bank), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2018 is RUB 2 549 376 thousand (2017: RUB 1 988 527 thousand).

As at 31 December 2018 cash and cash equivalents include balances with related parties totaling RUB 856 054 thousand bearing annual interest rates -0.50% for EUR, and -0.75% for other currencies. As at 31 December 2017 these balances comprise RUB 1 048 146 thousand and bear -0.50% for EUR, 0.07% for USD, -0.75% for other currencies. More information is disclosed in Note 27.

As at 31 December 2018, no cash and cash equivalents are impaired or past due.

6. Amounts due from credit institutions

Amounts due from credit institutions as at 31 December comprise:

	2018	2017
Time deposit with the CBR	-	7 005 938
Time deposits with other banks		
- rated from BBB- to BBB+	6 005 291	4 254 573
- rated from BB- to BB+	2 390 208	1 000 402
- rated B	1 593 377	1 400 883
- not rated	4 690	-
Gross amounts due from credit institutions	**9 993 566**	**13 661 796**
Less: allowance for credit losses	(11 199)	(7 604)
Net amounts due from credit institutions	**9 982 367**	**13 654 192**

The following table shows reconciliations from the opening to the closing balances of the allowance for credit losses for amounts due from credit institutions, measured at amortised cost:

	2018	2017
Balance as at 1 January	7 604	8 634
Impact of adopting IFRS 9	(1 616)	-
Net change of allowance for credit losses (Note 19)	5 211	(1 030)
Balance as at 31 December	**11 199**	**7 604**

The credit rating in disclosed above using credit scale of international rating agencies Standard& Poor's and Fitch.

As at 31 December 2018, the Bank has four banks (2017: three banks), whose balances exceed 10% of equity. The gross value of these balances as at 31 December 2018 is RUB 8 855 863 thousand (2017: RUB 11 135 397 thousand).

Amounts due from credit institutions include loans placed with related parties, which are disclosed in Note 27. The gross value of these balances as at 31 December 2018 is RUB 4 171 655 thousand (2017: RUB 2 728 577 thousand). They bear annual interest rates 2.60-3.08% for USD (2017: 1.58% for USD and 7.65% for RUB).

As at 31 December 2018, no amounts due from credit institutions are past due or credit-impaired. The allowance is measured as 12-months ECL.

(Thousands of Russian Roubles)

7. Investment securities

Investment securities as at 31 December comprise:

	2018	*2017*
Russian State bonds ("OFZ")	2 565 273	3 625 584
The CBR coupon bearing bonds ("KOBR")	1 514 505	505 315
Investment securities	**4 079 778**	**4 130 899**

As at 31 December 2018 and 2017, Russian State bonds are RUB denominated securities issued by the Ministry of Finance of the Russian Federation. Russian State bonds have maturity dates from 16 October 2019 to 29 January 2020 (2017: from 31 January 2018 to 29 January 2020), annual coupon rates from 7.4% to 8.0% (2017: from 6.2% to 10.4%) and annual yields to maturity from 7.2% to 7.7% (as at 31 December 2017: from 5.8% to 8.3%), depending on the bond issue.

As at 31 December 2018, the CBR coupon bearing bonds are RUB denominated securities with the maturity date on 13 February 2019, annual coupon rate of 7.8% and annual yield to maturity of 8.2% (2017: the maturity date on 14 February 2018, coupon rate of 7.8% and annual yield to maturity of 7.9%).

As at 31 December 2018 and 2017, the Bank has no transactions to sell securities under agreements to purchase.

As at 31 December 2018 and 2017, investment securities are eligible for pledge under refinancing from the CBR.

No investment securities are past due or credit-impaired. The allowance is measured as 12-months ECL.

The following table shows reconciliations from the opening to the closing balances of the allowance for credit losses for investment securities, measured at fair value through other comprehensive income:

	2018	*2017*
Balance as at 1 January	-	-
Impact of adopting IFRS 9	3 928	-
Net change of allowance for credit losses (Note 19)	(317)	-
Balance as at 31 December	**3 611**	**-**

8. Derivative financial instruments

The Bank enters into derivative financial instruments for trading purposes. The notional amount, recorded gross, is the amount of a derivative's underlying asset, and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts as at 31 December 2018:

	Notional amount	*Fair values*	
		Asset	*Liability*
Swap deals – domestic counterparties	1 023 816	5 359	(4)

(Thousands of Russian Roubles)

9. Loans to customers

An analysis of loans to customers as at 31 December is provided in the table below:

	2018	*2017*
Loans to customers measured at amortised cost		
- Large corporate customers	22 070 495	15 520 323
- Small and medium corporate customers	15 060 585	16 085 902
- Retail customers	1 874 490	1 907 348
Total before allowance for credit losses	**39 005 570**	**33 513 573**
Less: allowance for credit losses	(3 826 408)	(4 518 485)
Total loans to retail customers	**35 179 162**	**28 995 088**

An analysis of loans to customers measured at amortised cost by credit rating and risk grade as at 31 December 2018 is provided in the table below:

			Credit-impaired loans		Total
	Stage 1	*Stage 2*	*Stage 3*	*Upon initial recognition*	loans to customers
Large corporate customers					
Performing	18 545 240	321 313	-	-	18 866 553
Good quality	*16 509 816*	*100 756*	-	-	*16 610 572*
Average quality	*1 909 943*	*220 557*	-	-	*2 130 500*
Below average quality	*125 481*	-	-	-	*125 481*
Unlikely to pay	-	-	1 073 711	580 338	1 654 049
Doubtful	-	-	1 453 885	96 008	1 549 893
Total before allowance for credit losses	**18 545 240**	**321 313**	**2 527 596**	**676 346**	**22 070 495**
Less: allowance for credit losses	(253 237)	(12 072)	(1 739 560)	(96 008)	(2 100 877)
Total loans to large corporate customers	**18 292 003**	**309 241**	**788 036**	**580 338**	**19 969 618**
Small and medium corporate customers					
Performing	12 099 989	739 234	-	-	12 839 223
Good quality	*10 254 693*	*85 516*	-	-	*10 340 209*
Average quality	*1 836 271*	*250 600*	-	-	*2 086 871*
Below average quality	*9 025*	*403 118*	-	-	*412 143*
Unlikely to pay	-	-	175 500	-	175 500
Doubtful	-	-	2 045 862	-	2 045 862
Total before allowance for credit losses	**12 099 989**	**739 234**	**2 221 362**	**-**	**15 060 585**
Less: allowance for credit losses	(203 412)	(76 686)	(1 284 658)	-	(1 564 756)
Total loans to small and medium corporate customers	**11 896 577**	**662 548**	**936 704**	**-**	**13 495 829**
Retail customers					
Performing	1 649 791	80 846	-	-	1 730 637
Unlikely to pay	-	-	16 261	-	16 261
Doubtful	-	-	127 592	-	127 592
Total before allowance for credit losses	**1 649 791**	**80 846**	**143 853**	**-**	**1 874 490**
Less: allowance for credit losses	(38 872)	(17 433)	(104 470)	-	(160 775)
Total loans to retail customers	**1 610 919**	**63 413**	**39 383**	**-**	**1 713 715**
Total loans to customers					
Performing	32 295 020	1 141 393	-	-	33 436 413
Unlikely to pay	-	-	1 265 472	580 338	1 845 810
Doubtful	-	-	3 627 339	96 008	3 723 347
Total before allowance for credit losses	**32 295 020**	**1 141 393**	**4 892 811**	**676 346**	**39 005 570**
Less: allowance for credit losses	(495 521)	(106 191)	(3 128 688)	(96 008)	(3 826 408)
Total loans to customers	**31 799 499**	**1 035 202**	**1 764 123**	**580 338**	**35 179 162**

Expected credit losses are assessed for a 12-month period for Stage 1 exposures and for a life-time period for Stage 2 and 3.

Credit quality, disclosed in the table above, represents Bank's assessment of Borrowers' financial position and performance based on an analysis of financial and non-financial information.

(Thousands of Russian Roubles)

The information on the credit quality of loans to customers as at 31 December 2017 is provided below:

	Gross amount	Impairment allowance	Net carrying amount
Loans to corporate customers			
Large corporate customers			
Neither past due nor impaired	12 467 761	(279 616)	12 188 145
Impaired loans:	*3 052 562*	*(2 289 745)*	*762 817*
- past due less than 90 days	1 710 640	(1 111 756)	598 884
- past due more than 90 days but less than 1 year	220 186	(156 921)	63 265
- past due more than 1 year	1 121 736	(1 021 068)	100 668
Total loans to large corporate customers	**15 520 323**	**(2 569 361)**	**12 950 962**
Small and medium corporate customers			
Neither past due nor impaired	12 794 004	(164 768)	12 629 236
Past due less than 90 days but not impaired	21 138	(2 648)	18 490
Impaired loans:	*3 270 760*	*(1 635 815)*	*1 634 945*
- past due less than 90 days	317 195	(93 224)	223 971
- past due more than 90 days but less than 1 year	453 681	(180 398)	273 283
- past due more than 1 year	2 499 884	(1 362 193)	1 137 691
Total loans to small and medium corporate customers	**16 085 902**	**(1 803 231)**	**14 282 671**
Total loans to corporate customers	**31 606 225**	**(4 372 592)**	**27 233 633**
Retail customers			
Neither past due nor impaired	1 678 255	(11 828)	1 666 427
Past due less than 90 days but not impaired	35 649	(7 011)	28 638
Impaired loans:	*193 444*	*(127 054)*	*66 390*
- past due less than 90 days	34 604	(13 842)	20 762
- past due more than 90 days but less than 1 year	24 731	(18 751)	5 980
- past due more than 1 year	134 109	(94 461)	39 648
Total loans to retail customers	**1 907 348**	**(145 893)**	**1 761 455**
Total loans to customers	**33 513 573**	**(4 518 485)**	**28 995 088**

(Thousands of Russian Roubles)

Movements in the allowance for credit losses for loans to customers, measured at amortised cost as for the year ended 31 December 2018:

			Credit-impaired loans		Total
	Stage 1	***Stage 2***	***Stage 3***	***Upon initial recognition***	**loans to customers**
Large corporate customers					
Balance as at 1 January under IAS 39	246 616	33 001	2 289 744	-	2 569 361
Impact of adopting IFRS 9	(17 343)	208 376	8 249	-	199 282
Transfer to Stage 2	(275)	275	-	-	-
Transfer to Stage 3	-	(151 296)	151 296	-	-
Net remeasurement of allowance:					
- loans issued to customers	335 448	-	-	-	335 448
- loans repaid	(71 444)	(76 677)	-	-	(148 121)
- remeasurement of allowance	(239 765)	(1 607)	235 642	96 008	90 278
Unwinding of discount	-	-	(45 610)	-	(45 610)
Derecognition	-	-	(613 615)	-	(613 615)
Amounts written-off/sold	-	-	(286 146)	-	(286 146)
Balance as at 31 December 2018	**253 237**	**12 072**	**1 739 560**	**96 008**	**2 100 877**
Small and medium corporate customers					
Balance as at 1 January under IAS 39	158 288	9 127	1 635 816	-	1 803 231
Impact of adopting IFRS 9	105 286	175 505	41 945	-	322 736
Transfer to Stage 1	79 555	(79 555)	-	-	-
Transfer to Stage 2	(39 900)	39 900	-	-	-
Transfer to Stage 3	(599)	(30 218)	30 817	-	-
Net remeasurement of allowance:					
- loans issued to customers	206 947	-	-	-	206 947
- loans repaid	(50 852)	(25 577)	-	-	(76 429)
- remeasurement of allowance	(255 313)	(12 496)	247 705	-	(20 104)
Unwinding of discount	-	-	(196 023)	-	(196 023)
Amounts written-off/sold	-	-	(475 602)	-	(475 602)
Balance as at 31 December 2018	**203 412**	**76 686**	**1 284 658**	**-**	**1 564 756**
Retail customers					
Balance as at 1 January under IAS 39	16 523	2 317	127 053	-	145 893
Impact of adopting IFRS 9	35 714	(1 726)	2 188	-	36 176
Transfer to Stage 1	3 584	(2 492)	(1 092)	-	-
Transfer to Stage 2	(2 140)	2 460	(320)	-	-
Transfer to Stage 3	(323)	(3 734)	4 057	-	-
Net remeasurement of allowance	(14 486)	20 608	30 387	-	36 509
Unwinding of discount	-	-	(5 585)	-	(5 585)
Amounts written-off/sold	-	-	(52 218)	-	(52 218)
Balance as at 31 December 2018	**38 872**	**17 433**	**104 470**	**-**	**160 775**
Total loans to customers					
Balance as at 1 January under IAS 39	421 427	44 445	4 052 613	-	4 518 485
Impact of adopting IFRS 9	123 657	382 155	52 382	-	558 194
Transfer to Stage 1	83 139	(82 047)	(1 092)	-	-
Transfer to Stage 2	(42 315)	42 635	(320)	-	-
Transfer to Stage 3	(922)	(185 248)	186 170	-	-
Net remeasurement of allowance	(89 465)	(95 749)	513 734	96 008	424 528
Unwinding of discount	-	-	(247 218)	-	(247 218)
Derecognition			(613 615)		(613 615)
Amounts written-off/sold	-	-	(813 966)	-	(813 966)
Balance as at 31 December 2018	**495 521**	**106 191**	**3 128 688**	**96 008**	**3 826 408**

(Thousands of Russian Roubles)

Movements in the loan impairment allowance for the year ended 31 December 2017 is as follows:

	Large corporate customers	*Small and medium corporate customers*	*Retail customers*	*Total*
Balance as at 1 January 2017 under IAS 39	4 056 351	2 241 792	148 501	6 446 644
Net remeasurement of loss allowance	(64 961)	367 027	14 762	316 828
Unwinding of discount	(7 816)	(251 139)	(9 293)	(268 248)
Amounts written-off/sold	(1 414 213)	(554 449)	(8 077)	(1 976 739)
Balance as at 31 December 2017	**2 569 361**	**1 803 231**	**145 893**	**4 518 485**

As at 31 December 2018, the total amount of overdue outstanding payments on loans less accrued interest is RUB 3 972 552 thousand (2017: RUB 4 921 792 thousand).

Bank's credit risk exposure is further analysed in Note 25.

Concentration of loans to customers

Economic sector risk concentrations within loans to customers are as follows:

	2018		*2017*	
	Amount	*%*	*Amount*	*%*
Trading	12 195 895	31	12 636 730	38
Manufacturing	11 264 426	29	8 423 183	25
Services	10 292 683	26	9 365 348	28
Mining and quarrying	3 019 145	8	-	-
Individuals	1 874 490	5	1 907 348	6
Other	358 931	1	1 180 964	3
Total gross loans to customers	**39 005 570**	**100**	**33 513 573**	**100**

As at 31 December 2018, the Bank has twenty largest borrowers with an aggregate gross loan amount for each of them above RUB 300 259 thousand (2017: twenty largest borrowers above RUB 200 180 thousand). The total aggregate amount of these loans is RUB 17 431 254 thousand or 44.7% of the gross loan portfolio (2017: RUB 11 864 970 thousand or 35.4%), with the allowance for credit losses of RUB 1 221 317 thousand (2017: RUB 1 659 182 thousand).

Loans to customers include loans from related parties, which are disclosed in Note 27.

(Thousands of Russian Roubles)

10. Net investments in finance leases

Net investments in finance leases at 31 December 2018 comprise:

	Up to 1 year	From 1 to 5 years	Total
Gross investments in finance leases	953 988	727 796	1 681 784
Unearned future finance income on finance leases	(75 342)	(178 322)	(253 664)
	878 646	**549 474**	**1 428 120**
Less: allowance for credit losses	(28 715)	(23 635)	(52 350)
Net investments in finance leases	**849 931**	**525 839**	**1 375 770**

Net investments in finance leases at 31 December 2017 comprise:

	Up to 1 year	From 1 to 5 years	Total
Gross investments in finance leases	865 859	829 129	1 694 988
Unearned future finance income on finance leases	(77 906)	(188 369)	(266 275)
	787 953	**640 760**	**1 428 713**
Less: allowance for credit losses	(45 331)	(49 265)	(94 596)
Net investments in finance leases	**742 622**	**591 495**	**1 334 117**

The table below shows credit quality of net investments in finance leases as at 31 December 2018:

	Stage 1	*Stage 2*	*Stage 3*	Total
Performing	1 358 192	15 173	-	1 373 365
Unlikely to pay	-	-	6 894	6 894
Doubtful	-	-	47 861	47 861
	1 358 192	**15 173**	**54 755**	**1 428 120**
Less: allowance for credit losses	(20 499)	(920)	(30 931)	(52 350)
Total net investments in finance leases	**1 337 693**	**14 253**	**23 824**	**1 375 770**

Expected credit losses are assessed for a 12-month period for Stage 1 exposures and for a life-time period for Stage 2 and 3.

Movements in the allowance for credit losses for net investments in finance leases are as follows:

	2018				
	Stage 1	*Stage 2*	*Stage 3*	Total	*2017*
Balance as at 1 January	22 705	-	71 891	94 596	98 063
Impact of adopting IFRS 9	3 790	-	(2 473)	1 317	-
Transfer to Stage 1	12 135	(12 135)	-	-	-
Transfer to Stage 2	(2 190)	2 190	-	-	-
Transfer to Stage 3	(212)	(3 708)	3 920	-	-
Net remeasurement of allowance	(15 729)	14 573	5 138	3 982	4 154
Unwinding of discount	-	-	(3 172)	(3 172)	(5 494)
Amounts written-off/sold	-	-	(44 373)	(44 373)	(2 127)
Balance as at 31 December	**20 499**	**920**	**30 931**	**52 350**	**94 596**

The leased assets are effectively pledged, as the rights to the leased asset revert to the lessor in the event of default. Lease payments are due on a monthly basis. The Bank holds title to the leased property during the lease term. Risks related to the leased property such as damage caused by various reasons, theft and other are generally insured under finance lease agreements.

As at 31 December 2018, the Bank has twenty largest lessees with an aggregate gross amount for each of them above RUB 11 774 thousand (2017: twenty largest lessees above RUB 11 435 thousand). The total aggregate amount of gross investments in finance leases related to these leases is RUB 576 541 thousand or 40.4% of the total gross investments in finance leases portfolio (2017: RUB 465 057 thousand or 32.6%), with the allowance for credit losses of RUB 8 528 thousand (2017: RUB 15 687 thousand).

There is no unguaranteed residual value related to lease contracts outstanding as at 31 December 2018 and 2017.

(Thousands of Russian Roubles)

11. Property and equipment

The movements in property and equipment for the year ended 31 December are as follows:

	Buildings and improvements	*Office and computer equipment*	*Total*
Cost as at 1 January 2017	446 281	1 254 116	1 700 397
Accumulated depreciation as at 1 January 2017	(171 876)	(831 878)	(1 003 754)
Carrying amount as at 1 January 2017	**274 405**	**422 238**	**696 643**
Additions	1 458	195 264	196 722
Disposals (net of accumulated depreciation)	(6 938)	(78 210)	(85 148)
Depreciation charge for the year	(15 367)	(141 813)	(157 180)
Revaluation of buildings	480 180	-	480 180
Cost/revalued amount as at 31 December 2017	735 704	1 151 816	1 887 520
Accumulated depreciation as at 31 December 2017	(1 966)	(754 337)	(756 303)
Carrying amount as at 31 December 2017	**733 738**	**397 479**	**1 131 217**
Additions	-	76 261	76 261
Disposals (net of accumulated depreciation)	-	(2 749)	(2 749)
Depreciation charge for the year	(19 598)	(158 906)	(178 504)
Revaluation of buildings	(311 775)	-	(311 775)
Cost/revalued amount as at 31 December 2018	404 605	1 154 093	1 558 698
Accumulated depreciation as at 31 December 2018	(2 240)	(842 008)	(844 248)
Carrying amount at 31 December 2018	**402 365**	**312 085**	**714 450**

Capital expenditure commitments related to property and equipment are disclosed in Note 23.

As at 31 December 2018, an internal valuation of buildings was performed using a combination of market comparison and income capitalization approaches with 50% weight assigned to each. As at 31 December 2017, the buildings were revaluated by an independent professional valuation firm with appropriate qualifications and experience in valuations of real estate objects using income capitalization approach.

The market comparison approach comprises an analysis of sale offers for comparable buildings. The following key assumptions were made as part of market comparison approach:

- the price for one square meter is within RUB 173 - 210 thousand for comparable buildings in Moscow and RUB 70 – 109 for Nizhniy Novgorod, before adjustments for location and condition;
- sale discount of 12% and 10% for Moscow and Nizhniy Novgorod respectively.

The income capitalization approach consists of analyzing income and expenses related to the buildings and estimating fair value by capitalizing them. The base-year income is based on the expected rental income less repair and maintenance expenses for relevant buildings calculated on the basis of current market rental rates and average costs for repair and maintenance. Losses from underutilization were estimated as insignificant. Capitalization rate of 10% was used (2017: 9.5% and 11%).

Changes in the above estimates may affect the fair value of buildings. For example, decrease in capitalization rate by 100 b.p. would result in an increase of fair value of the buildings as at 31 December 2018 by RUB 19 300 thousand (increase in capitalization rate by 100 b.p. would result in a decrease in fair value of the buildings by RUB 16 200).

As at 31 December 2018, the fair value of the buildings in Moscow was decreased by RUB 199 800 thousand, which is the fair value of the underlying land plot and the title for lease of which belongs to a third party.

As at 31 December 2018, revaluation resulted in a decrease of carrying amount of buildings by RUB 311 775 thousand, which was recorded within other comprehensive loss in the amount of RUB 249 420 thousand net of income tax (2017: increased by RUB 480 180 thousand, other comprehensive income comprised RUB 384 144 thousand).

As at 31 December 2018 and 2017, the carrying amount of buildings measured at fair value, have they been measured at cost less accumulated depreciation, would be RUB 241 693 thousand and 253 558 thousand respectively.

As at 31 December 2018 and 2017, the buildings are classified to Level 3 of fair value measurement hierarchy.

In 2018 the Bank reviewed the remainder useful life of a building, located in Moscow, from 17 to 62 years. The revalued amount of this building totaled RUB 353 400 thousand as at 31 December 2018.

(Thousands of Russian Roubles)

12. Intangible assets

As at 31 December 2018 and 2017 intangible assets include licenses and computer software. The movements in intangible assets for the year ended 31 December are as follows:

	2018	*2017*
Cost as at 1 January	2 114 463	2 517 811
Accumulated amortization as at 1 January	(1 528 796)	(1 797 239)
Carrying amount as at 1 January	**585 667**	**720 572**
Additions	95 723	154 446
Disposals (net of accumulated amortization)	(226)	(7 074)
Amortization for the year	(233 762)	(282 277)
Cost as at 31 December	2 103 420	2 114 463
Accumulated amortization as at 31 December	(1 656 018)	(1 528 796)
Carrying amount as at 31 December	**447 402**	**585 667**

Capital expenditure commitments related to intangible assets are disclosed in Note 23.

13. Taxation

The corporate income tax expense for the year ended 31 December comprises:

	2018	*2017*
Current tax	42 320	73 404
Deferred tax – origination and reversal of temporary differences	130 236	202 104
Total income tax expense	**172 556**	**275 508**

The rate of tax applicable for current income and deferred taxes is 20% and is a tax rate applicable for income of Russian companies. Income on certain types of securities is subject to income tax at a rate of 15%, 10% or nil.

The effective income tax rate differs from the statutory income tax rates. A reconciliation of the income tax expense based on statutory rates with actual for the year ended 31 December is as follows:

	2018	*2017*
Profit before income tax	**1 041 877**	**277 579**
Income tax expense at the applicable tax rate	208 375	55 516
Income on government securities taxed at different rates	(14 107)	(16 393)
Prior periods adjustments	(29 962)	66 798
Non-deductible expenses	8 250	169 587
Total income tax expense	**172 556**	**275 508**
Effective tax rate	**16.56%**	**99.25%**

Temporary differences between the carrying amounts of assets for financial reporting purposes and the amounts used for taxation purposes give rise to net deferred tax assets as at 31 December 2018 and 2017.

The deductible temporary differences do not expire under the current tax legislation.

As at 31 December 2018, the Banca Intesa has the recognised tax loss carry-forward of RUB 543 347 thousand (2017: RUB 513 386 thousand), that could be utilized against the future income tax base.

As at 31 December 2018, AO “Intesa Leasing” has tax loss carry-forward of RUB 21 289 thousand (2017: no tax loss carry-forward), that could be utilized against the future income tax base.

The accumulated tax loss carry-forward not utilized in the current year can be transferred for the future years without time limitation. Starting from 1 January 2017 till 31 December 2020 the income tax base can’t be decreased by utilization of tax loss carry-forward for more than 50%.

Banca Intesa (Joint-Stock Company) and AO “Intesa Leasing” calculate net deferred tax assets and liabilities separately and cannot offset them.

(Thousands of Russian Roubles)

Movements in temporary differences during the year ended 31 December 2018 are as follows:

	1 January 2018	*Impact of adopting IFRS 9*	*Recognised in profit or loss*	*Recognised in other comprehensive income*	*31 December 2018*
Tax effect of temporary differences					
Investment securities	(5 701)	-	(64)	10 182	4 417
Loans to customers	(289 994)	111 639	(170 080)	-	(348 435)
Net investments in finance leases	61 392	263	4 654	-	66 309
Property, equipment and intangible assets	(124 230)	-	15 786	62 355	(46 089)
Subordinated loan	-	-	9 956	-	9 956
Other assets	72 850	(323)	(10 105)	-	62 422
Other liabilities	100 645	(8 669)	(31 633)	-	60 343
Tax loss carry-forward	513 386	-	51 250	-	564 636
Net deferred tax assets	**328 348**	**102 910**	**(130 236)**	**72 537**	**373 559**

Movements in temporary differences during the year ended 31 December 2017 are as follows:

	1 January 2017	*Recognised in profit or loss*	*Recognised in other comprehensive income*	*31 December 2017*
Tax effect of temporary differences				
Investment securities	(5 457)	-	(244)	(5 701)
Loans to customers	(142 431)	(147 563)	-	(289 994)
Net investments in finance leases	79 610	(18 218)	-	61 392
Property, equipment and intangible assets	(32 298)	4 104	(96 036)	(124 230)
Other assets	163 703	(90 853)	-	72 850
Other liabilities	91 140	9 505	-	100 645
Tax loss carry-forward	472 465	40 921	-	513 386
Net deferred tax assets	**626 732**	**(202 104)**	**(96 280)**	**328 348**

(Thousands of Russian Roubles)

14. Other assets and liabilities

Other assets as at 31 December comprise:

	2018	*2017*
Other financial assets		
Settlements on commission for participation in credit facilities origination	1 191 907	-
Settlements with suppliers and customers	112 822	105 359
Other financial assets before allowance for credit losses	**1 304 729**	**105 359**
Less: allowance for credit losses	(64 501)	(56 123)
Total other financial assets	**1 240 228**	**49 236**
Other non-financial assets		
Prepayments	376 758	294 227
Repossessed collateral	201 435	194 854
Construction in progress	76 871	63 043
Current income tax and other tax assets	61 046	52 296
Leasehold improvements	33 999	50 386
Other	9 644	44 906
Total other non-financial assets	**759 753**	**699 712**
Total other assets	**1 999 981**	**748 948**

As at 31 December 2018, settlements on commission for participation in credit facilities' origination are due from Intesa Sanpaolo Group member bank for participation of the Bank in 2018 in the process of setting up a credit facility to a large corporate clients by Intesa Sanpaolo group. The outstanding commission receivable comprised RUB 1 191 907 thousand including VAT and was fully paid in January 2019.

Other liabilities as at 31 December comprise:

	2018	*2017*
Other financial liabilities		
Settlements with suppliers and customers	164 161	224 171
Other non-financial liabilities		
Tax liabilities other than income tax	211 722	25 194
Provision for credit related commitments	107 133	247 321
Settlements with employees	86 528	97 187
Provision for other risks	12 015	37 670
Other	130 064	114 969
Other non-financial liabilities	**547 462**	**522 341**
Other liabilities	**711 623**	**746 512**

Movements in the allowance for credit losses for other assets and credit related commitments and other provisions for the period is as follows:

	Other assets	*Credit related commitments*	*Provisions for other risks*	*Total*
Balance as at 1 January 2017	54 713	203 931	21 252	279 896
Net charge (recovery)	49 039	43 390	16 418	108 847
Amounts written-off	(47 629)	-	-	(47 629)
Balance as at 31 December 2017	**56 123**	**247 321**	**37 670**	**341 114**
Transition to IFRS 9	-	(43 345)	-	(43 345)
Net charge (recovery)	75 399	(96 843)	(25 655)	(47 099)
Amounts written off	(67 021)	-	-	(67 021)
Balance as at 31 December 2018	**64 501**	**107 133**	**12 015**	**183 649**

The allowance for credit losses is deducted from the carrying amount of specified assets. Provisions for claims, guarantees and contractual obligations are included in other liabilities.

(Thousands of Russian Roubles)

15. Amounts due to credit institutions

Amounts due to credit institutions as at 31 December comprise:

	2018	*2017*
Time deposits and loans	9 214 290	4 914 148
Current accounts	1 253 265	970 502
Amounts due to credit institutions	**10 467 555**	**5 884 650**

As at 31 December 2018, the Bank has three banks (2017: two banks), whose balances individually exceed 10% of equity. The gross value of these balances as at 31 December 2018 is RUB 10 432 651 thousand (2017: RUB 3 033 445 thousand).

Amounts due to credit institutions include loans from related parties, which are disclosed in Note 27. The gross value of these balances as at 31 December 2018 is RUB 8 320 752 thousand (2017: RUB 964 454 thousand). These loans have annual interest rate for USD, varying from 2.79% to 3.37%, and for EUR varying from 0.09% to 1.17% (2017: 0.00% annual interest rate).

At 31 December 2018, the Bank obtained financing from credit institutions to facilitate origination of loans to customers in the amount of RUB 2 145 177 thousand (2017: RUB 1 532 849 thousand). The financing is provided under the Small and Medium Business Loan Promotion Program developed by Small and Medium Business Corporation in collaboration with the Ministry of Economic Development of the Russian Federation and the CBR.

16. Amounts due to customers

The amounts due to customers as at 31 December include the following:

	2018	*2017*
Legal entities	**17 936 494**	**13 616 591**
- current accounts	9 675 189	10 318 112
- term deposits	8 261 305	3 298 479
Individuals	**11 954 486**	**16 826 402**
- current accounts	2 405 868	1 931 215
- term deposits	9 548 618	14 895 187
State and non-profit organizations	**74 185**	**84 112**
- current accounts	50 069	47 268
- term deposits	24 116	36 844
Amounts due to customers	**29 965 165**	**30 527 105**

State and non-profit organizations exclude government-owned profit oriented organizations. Amounts received from individual entrepreneurs are classified as amounts due to legal entities.

As at 31 December 2018, the Bank has one customer (2017: one customer), whose balances exceed 10% of equity. The gross value of the balances as at 31 December 2018 is RUB 2 987 273 thousand or 10.0% of total amounts due to customers (2017: RUB 5 487 264 thousand, 18.0% of total amounts due to customers).

As at 31 December 2018, included in term deposits are deposits of individuals of RUB 9 548 618 thousand (2017: RUB 14 895 187 thousand). In accordance with the Russian Civil Code, the Bank is obliged to repay such deposits upon demand of a depositor. In case a term deposit is repaid upon demand of the depositor prior to maturity, interest on it is paid based on the interest rate for demand deposits, unless a different interest rate is specified in the agreement.

Amounts due to customers include balances of related parties, which are disclosed in Note 27.

(Thousands of Russian Roubles)

17. Debt securities issued, subordinated loan and reconciliation of changes in liabilities and cash flows from finance activities

As at 31 December 2018, the Bank has non-convertible documentary bonds totaling RUB 3 000 000 thousand (nominal amount), with a contractual maturity in October 2019, with a current annual coupon rate of 9.75% payable semi-annually (unaudited) (2017: non-convertible documentary bonds in the amount totaling RUB 130 643 thousand, with a contractual maturity in June 2018 with a current annual coupon rate of 8.25% payable semi-annually, and non-convertible documentary bonds totaling RUB 3 000 000 thousand (nominal amount), with a contractual maturity in October 2019, with a current annual coupon rate 9.75% payable semi-annually).

As at 31 December 2018 and 2017, subordinated loan is represented by the loan from Intesa Sanpaolo Bank Luxembourg. This subordinated loan is denominated in US dollars and bears fixed annual interest rate of 6.58%.In May 2018 the term of subordinated loan was changed from 7 to 10 years and the maturity date was changed from December 2022 to December 2025.

The claims of the Bank's creditors on subordinated loan shall only be satisfied after all claims of other creditors of the Bank are satisfied in full.

Reconciliation of movements of liabilities to cash flows arising from financing activities is provided below:

	Debt securities issued	Subordinated loan	Total
Balance as at 1 January 2017	4 875 106	2 426 712	**7 301 818**
Cash flows from financing activities			
Repayment of debt securities issued	(1 686 508)	-	(1 686 508)
Net cash flows used in financing activities	**(1 686 508)**	**-**	**(1 686 508)**
The effect of changes in foreign exchange rates	-	(121 873)	(121 873)
Interest expense accrued	391 791	153 585	545 376
Interest expense paid	(391 791)	(153 585)	(401 967)
Other changes	(2 532)	-	(2 532)
Balance at 31 December 2017	**3 186 066**	**2 304 839**	**5 490 905**
Cash flows from financing activities			
Repayment of debt securities issued	(130 643)	-	(130 643)
Net cash flows used in financing activities	**(130 643)**	**-**	**(130 643)**
The effect of changes in foreign exchange rates	-	473 985	473 985
Interest expense accrued	301 713	165 046	466 759
Interest expense paid	(297 095)	(165 046)	(462 141)
Other changes	(87)	49 781	49 694
Balance at 31 December 2018	**3 059 954**	**2 828 605**	**5 888 559**

18. Equity

As at 31 December 2018 and 2017, the share capital of Banca Intesa is represented by 876 128 ordinary shares with a nominal value of 12 350 RUB per share. Share capital did not change in 2018 and 2017.

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at annual and general meetings of the Bank.

As at 31 December 2018 and 2017, other capital reserves of RUB 1 803 914 thousand are represented by funds provided in June 2009 to the Bank by its shareholder Intesa Sanpaolo Holding International SA in the form of debt free financing. These funds are not repayable to the Bank's shareholder.

In accordance with Russian Accounting Legislation ("RAL"), the Bank distributes profit as dividends or transfers it to retained earnings on the basis of accounting reports prepared in accordance with RAL. The Bank's accumulated loss under RAL as at 31 December 2018 is RUB 239 563 thousand (2017: accumulated loss RUB 562 347 thousand).

During 2018 the Bank did not pay dividends for 2017.

19. Change of allowance for credit losses on interest-bearing financial assets

	2018	*2017*
Loans to large corporate customers	277 605	(64 961)
Loans to small and medium corporate customers	110 414	367 027
Loans to retail customers	36 509	14 762
Net investments in finance leases	3 982	4 154
Investment securities	(317)	-
Amounts due from credit institutions	5 211	(1 030)
Total allowance for credit losses	**433 404**	**319 952**

(Thousands of Russian Roubles)

20. Fee and commission income and expense

Analysis of fee and commission income and expense is as follows:

	2018	2017
Fee and commission income		
Participation in credit facilities' origination (note 14)	1 012 602	-
Settlement transactions	422 017	422 949
Guarantees and letters of credit issued	163 673	201 236
Remote administration of accounts	142 051	70 552
Cash transfers	64 245	88 295
Lending transactions	40 772	51 684
Consulting	-	101 835
Other	87 535	79 103
Total fee and commission income	**1 932 895**	**1 015 654**
Including income that is revenue in accordance with IFRS 15:		
- recognized over time	68 886	71 856
- recognized at a point of time when services are provided	1 769 132	814 328
	1 838 018	**886 184**
Fee and commission expense		
Settlement transactions	76 995	76 446
Services on issuance and maintenance of plastic cards	26 067	26 638
Stock exchange services	7 477	18 658
Other	16 380	23 536
Fee and commission expense	**126 919**	**145 278**
Net fee and commission income	**1 805 976**	**870 376**

Depending on the type of the service commission income when not an integral part of the effective interest rate on a financial asset or liability is recognized either at a point of time or over time according to the pattern the Bank fulfills a performance obligation under the contract:

- commission fee for settlement transactions and cash transfers is charged for the execution of payment order in accordance with tariffs depending on the type of the transaction and recognized as income at the moment of the transaction execution;
- commission fee on guarantees and letters of credit issued is paid in advance and is recognized as income over the time of the relevant guarantee or letter of credit;
- fees for asset management, custody and other management and consulting services are recognized over the time of service provision;
- success fees paid on meeting certain profitability targets are recognized after the relevant target is met;
- fees for conducting or participating in negotiations on a transaction on behalf of the third party (for example, entering into an agreement when purchasing shares or other securities; buying or selling a company; obtaining a syndicated loan) are recognized at the moment the transaction is performed by the third party;
- credit operations commission fees are charged, for example, for changing and supplementing the original terms and conditions of the a loan agreement, early repayment of a loan and preparation of information letters to borrowers and are recognized at the moment the Bank provides the relevant service.

Net commission income for 2018 comprise income of 40 772 thousand (2017: 51 684 thousand) that relate to financial assets and liabilities not measured at fair value. These amounts exclude commission fees included in the effective interest rate of relevant financial assets and liabilities.

As at 31 December 2018, receivables on commissions recognized in other assets (note 14) comprise participation in credit facilities' origination commission of RUB 1 012 602 thousand excluding VAT (2017: nil). As at 31 December 2018 and 2017, the Bank has no fee and commissions payables.

(Thousands of Russian Roubles)

21. Net losses from other operating activities

	2018	2017
Obligatory deposit insurance system contributions	(86 111)	(73 188)
Capital expenditures depreciation	(16 511)	(15 241)
Notarial and state duties expenses	(8 009)	(9 838)
Net other operating income	43 168	29 560
Net losses from other operating activities	**(67 463)**	**(68 707)**

22. Personnel and other general administrative expenses

Personnel expenses and other general administrative expenses comprise:

	2018	2017
Salaries and bonuses	1 340 828	1 380 748
Social security costs	309 432	329 074
Personnel expenses	**1 650 260**	**1 709 822**
Operating lease expense	361 931	398 600
Data processing	342 730	279 568
Legal and consultancy	259 807	262 520
Office materials	72 833	74 178
Communications	56 957	61 910
Repair and maintenance of property and equipment	34 697	26 269
Security	30 496	37 585
Charity	19 370	19 805
Insurance	14 751	15 311
Business travel and related expenses	10 367	13 816
Marketing and advertising	8 885	24 349
Operating taxes	1 905	18 398
Other	27 430	34 895
Other general administrative expenses	**1 242 159**	**1 267 204**

23. Commitments and contingencies

Legal

In the ordinary course of business, the Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial condition or the results of future operations of the Bank.

Taxation

The taxation system in the Russian Federation continues to evolve and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are sometimes contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities who have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years; however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

Starting from 1 January 2012 new transfer pricing rules came into force in Russia. They provide the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of controllable transactions if their prices deviate from the market range or profitability range. According to the provisions of transfer pricing rules, the taxpayer should sequentially apply 5 methods of market price determination prescribed by the Tax Code.

(Thousands of Russian Roubles)

Tax liabilities arising from transactions between companies are determined using actual transaction prices. It is possible with the evolution of the interpretation of the transfer pricing rules in the Russian Federation and the changes in the approach of the Russian tax authorities, that such transfer prices could be challenged. Given the short period since the current Russian transfer pricing rules became effective, the impact of any such challenge cannot be reliably estimated; however, it may be significant to the financial position and/or the overall operations of the Bank.

In addition, starting from 1 January 2015 changes aimed at regulating tax consequences of transactions with foreign companies and their activities were introduced, such as concept of beneficial ownership of income, taxation of controlled foreign companies, tax residency rules, etc. These changes may potentially impact the Bank's tax position. This legislation and practice of its application is still evolving and the impact of legislative changes should be considered based on the actual circumstances.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions. However, the interpretations of the relevant authorities could differ and the effect on the financial position, if the authorities were successful in enforcing their interpretations, could be significant.

Commitments

As at 31 December the Bank's commitments and contingencies comprise the following:

	2018	***2017***
Credit related commitments		
Guarantees issued	12 239 636	11 603 331
Undrawn credit line commitments	1 636 866	4 644 890
Undrawn overdraft loan commitments	713 209	988 473
Letters of credit	1 060 857	437 542
Credit related commitments	**15 650 568**	**17 674 236**
Allowance for credit losses for credit related commitments (Note 14)	107 133	247 321
Operating lease commitments		
Less than 1 year	278 294	339 728
From 1 to 5 years	536 668	678 632
Above 5 years	9 366	49 536
	824 328	**1 067 896**
Capital expenditure commitments		
Property and equipment	1 110	79
Intangible assets	54 707	76 975
	55 817	**77 054**

Credit related commitments represent Bank's liability to provide credit facility to the customers on demand. Guarantees and letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans.

24. Corporate governance and risk management

Corporate governance

Corporate governance framework

The Bank is established as a joint stock company in accordance with the Russian law. The supreme governing body of the Bank is the general shareholders meeting that convenes for annual or extraordinary meetings. The general shareholders meeting makes strategic decisions on the Bank's operations.

The general shareholders meeting elects the Board of Directors. The Board of Directors is responsible for overall governance of the Bank's activities.

Russian legislation and the Charter of the Bank establish the lists of decisions that are exclusively approved by the general shareholders meeting and that are approved by the Board of Directors.

As at 31 December 2018, the Board of Directors includes:

- Professor Antonio Fallico – Chairman of the Board of Directors;
- Mr. Gianluca Cugno
- Mr. Salvatore Catalano;
- Mr. Armando Selva;
- Mr. Michele Dapri;
- Mr. Christophe Velle;
- Mr. Stefano Favale;
- Mr. Andrea Mascetti;
- Mr. Alberto Mancuso.

During 2018 four members left and four new members joined the Board of Directors. There were no other changes in the composition of the Board of Directors during 2018.

General activities of the Bank are managed by the sole executive body of the Bank - the Chairman of the Management Board and the collective executive body – the Management Board of the Bank. The general shareholders meeting elects the Chairman of the Management Board. The executive bodies of the Bank are responsible for implementation of decisions of the general meeting of shareholders and the Board of Directors of the Bank. Executive bodies of the Bank report to the Board of Directors of the Bank and to the general meeting of shareholders.

As at 31 December 2018, the Management Board includes:

- Mrs. Olga Lein – Acting Chairman of the Management Board ;
- Mrs. Tatyana Pavlycheva;
- Mrs. Irina Vasina;
- Mr. Oleg Dzhus;
- Mrs. Elena Grimaylo.

During 2018 one member left the Management Board. There were no other changes in the composition of the Management Board during 2018.

Internal control policies and procedures

Internal Control System ("ICS") consists of the set of rules, functions, organizational units, resources, processes and procedures aimed at ensuring that the following activities are performed, in accordance with the principles of sound and prudent management.

The purpose of internal controls is to ensure:

- effectiveness and efficiency of financial and economic activities in banking operations and other transactions, effectiveness of asset and liability management, including the safeguarding of assets;
- proper and comprehensive risk assessment and management;
- proper business and accounting and financial reporting functions, including proper authorization, processing and recording of transactions;
- reliability, completeness, accuracy and timeliness of financial, accounting, statistical and other reporting, management information;
- reliability of IT-systems, data and systems integrity and protection;
- prevention of fraudulent or illegal activities, including misappropriation of assets;
- compliance with laws and regulations, including anti-money laundering and anti-corruption.

Internal control in the Bank is implemented via following bodies:

- the general meeting of shareholders;
- the Board of Directors and its committees, including the Audit Committee;
- the Management Board and the Chairman of the Management Board;
- the Chief Accountant;
- the Risk Management function;
- the Compliance and Financial Monitoring Department
- the Legal Department;
- the Internal Audit function.
- Unit of methodology, projects and control of management and financial reporting
- Other structural units and (or) responsible employees of the Bank, as may be determined by internal documents of the Bank in accordance with the requirements of the legislation of the Russian Federation and the Bank of Russia.

The Board of Directors is responsible for strategic supervision and control.

Bearing in mind the proposals of the Management Board, the Board of Directors establishes and approves:

- the business model, taking into account the risks to which this model exposes the Bank and the procedures for identifying and measuring these risks;
- the Bank's overall governance structure;
- the strategic guidelines which are periodically reviewed due to changes in business activities and the external context, in order to ensure their ongoing effectiveness;
- the risk appetite, risk tolerance and risk governance policies;
- the guidelines of the internal control system, ensuring that it is in line with the stated strategic choices and risk appetite, and that it is able to take account of risk evolution and interaction;
- the criteria for identifying the significant transactions to be subject to prior approval by the Risk Management function;
- the main points of the ICAAP (Internal Capital Adequacy Assessment Process), its coherence with the RAF (Risk Appetite Framework) and its prompt adaptation to significant changes in strategic policies, organizational arrangements and the business environment; taking steps to ensure the full use of the results of the ICAAP for strategic and decision-making purposes.

The Board of Directors establishes and approves:

- the Bank's organizational structure;
- the establishment of the corporate control functions, their tasks and responsibilities, the methods of coordination and collaboration, and information flows between these functions and between them and the corporate bodies;
- the risk management process, and assesses its compatibility with the strategic guidelines and risk governance policies;
- the accounting and reporting systems;
- the policies and processes for evaluating the Bank’s assets, and in particular its financial instruments, ensuring their ongoing adequacy; it also establishes the Bank’s maximum exposure limits to financial instruments or products whose valuation is uncertain or difficult;
- adoption of the internal risk measurement systems for the calculation of capital requirements. Specifically, it approves the selection of the system deemed suitable and a plan of activities for setting it up and implementing it, identifying responsibilities, specifying the timetable for implementation and the planned investment of human, financial and technological resources;
- the annual declaration of compliance with the requirements for using internal evaluation systems, taking a reasoned decision and examining all information from the validation function;
- the process for the development and validation of internal risk management systems not used for regulatory purposes, and periodically assessing their proper functioning.

The Board of Directors and the Management Board have responsibility for development, implementation and monitoring of internal control system.

The Board of Directors is responsible for strategic supervision and management. The Management Board contributes to strategic supervision functions regarding the internal control system, in line with the ISP Group Policy. The Management Board provides the Board of Directors with proposals on the appointment and removal of the managers of internal control functions.

The Management Board ensures integrated management of all business risks, evaluating the internal and external factors from which these risks may derive and their mutual interrelations. It is responsible for taking all necessary actions to ensure that the Bank and the internal control system comply with regulatory standards and requirements, monitoring their ongoing compliance. The Management Board provides the implementation of all strategic decisions; plans and manages implementation of the risk management process as well as implementation of processes relating to the praxis for the approval of new products or services; establishes the internal information flows necessary to ensure that the business units and control functions are fully apprised of and are able to manage risk factors and can verify compliance with the RAF; takes the necessary actions to ensure the ongoing comprehensiveness, adequacy, functionality and reliability of the internal control system; ensures that the risk management process is coherent with the risk appetite and risk governance policies and ensures correct, prompt and secure management of information for accounting, management and reporting purposes; ensures the comprehensiveness, adequacy, functionality and reliability of the IT systems, including supervision of the level of risk of the system, and business continuity; approves the action plan in this direction.

The Bank developed a system of standards, policies and procedures to ensure proper operations and compliance with relevant legal and regulatory requirements, including the following areas:

- requirements for appropriate segregation of duties, including the independent authorization of transactions;
- requirements for the recording, reconciliation and monitoring of transactions;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial action;
- development of contingency plans;
- training and professional development;
- ethical and business standards;
- risk mitigation, including insurance where this is effective;
- rules on protection and confidentiality of information and control over compliance with the requirements of the Federal law on the insider information and market manipulation and procedure of access to the insider information.

The CBR sets out the specific requirements for the Internal Audit function and the Internal Control function. Based on above legal requirements the Internal Control function conducts compliance activities focused primarily on regulatory risks faced by the Bank.

The main functions of the Internal Control function (Compliance division of the compliance and financial monitoring Department) include the following:

- identification of compliance risks and regulatory risks;
- monitoring of events related to regulatory risk, including probability of occurrence and quantitative assessment of its' consequences;
- monitoring of regulatory risk;
- preparation of recommendations on regulatory risk management;
- coordination and participation of design of measures to decrease regulatory risk;
- monitoring of efficiency of regulatory risk management;
- participation in preparation of internal documents on regulatory risk management, anti-corruption, compliance with corporate behavior rules, code of professional ethics and minimization of conflicts of interest;
- analysis of dynamics of clients' complaints;
- monitoring of compliance with the Russian legislation, the CBR requirements, self-regulated organizations, internal regulations, and correct accounting of securities transactions within dealer, broker, depository activity;
- maintaining the list of insiders;
- analysis of economic reasonableness of outsourcing agreements of Bank's services;
- participation in interaction with authorities, self-organized organizations, associations and financial market participants.

The main functions of the Internal Audit function include the following:

- audit and efficiency assessment of the system of internal control as a whole, fulfillment of the decisions of key management structures;
- audit of efficiency of methodology of assessment of banking risks and risk management procedures;
- audit of reliability of internal control system over automated information systems;
- audit and testing of fairness, completeness and timeliness of accounting and reporting function and the reliability (including the trustworthiness, fullness and objectivity) of the collection and submission of financial information;
- audit of applicable methods of safekeeping the Bank's property;
- assessment of economic reasonability and efficiency of operations and other deals;
- audit of internal control processes and procedures;
- audit of the Internal Control function and the Risk Management function.

Compliance with ISP Group standards is supported by periodic reviews undertaken by the Internal Audit Division (further, “the Internal Audit function”). The Internal Audit function is independent from business operations and is subordinated to and reports to the Board of Directors. The results of the Internal Audit function reviews are discussed with relevant business process managers, with summaries submitted to the Audit Committee, the Board of Directors and senior management of the Bank and the ISP Group.

Russian legislation establishes the professional qualification, business reputation and other requirements for the members of the Board of Directors, the Management Board, the Head of the Internal Audit function, Head of Compliance and financial monitoring Department (the Internal Control function) and the Risk Management function and other key management personnel. All members of the Bank’s governing and management bodies of the Bank comply with these requirements.

There is a hierarchy of requirements for the authorization of transactions depending on their size and complexity. A significant portion of operations are automated and the Bank has a system of automated controls to minimize risks.

Management believes that the Bank complies with the CBR requirements in respect of risk management and internal control systems, including requirements covering the Internal Audit function, and that risk management and internal control systems are appropriate for the scale, nature and complexity of Bank’s operations.

The Bank’s internal documentation, establishing the procedures and methodologies for identifying and managing the Bank’s significant credit, operational, market, interest rate, legal, liquidity risks, and for stress-testing was approved by the authorised management bodies of the Bank in accordance with regulations and recommendations issued by the CBR.

The Bank maintained a system for reporting on the Banks’s significant credit, operational, market, interest rate, legal, liquidity and reputational risks, and on the Bank’s capital.

The frequency and consistency of reports prepared by the Bank’s Risk management and Internal Audit functions during 2018, which cover the Banks’s credit, operational, market, interest rate, legal, liquidity and reputational risk management, was in compliance with the Bank’s internal documentation. The reports included observations made by the Bank’s Risk Management, Compliance and financial monitoring Department and Internal Audit functions as to their assessment of the effectiveness of the Bank’s procedures and methodologies, and recommendations for improvement.

The Board of Directors and the Management Board of the Bank had responsibility for monitoring the Bank’s compliance with risk limits and capital adequacy ratios as established by the Bank’s internal documentation. With the objective of monitoring effectiveness of the Bank’s risk management procedures and their consistent application during 2018 the Board of Directors and the Management Board of the Bank periodically discussed reports prepared by the risk management and Internal Audit functions, and considered proposed corrective actions.

Risk management

General information

Risk is inherent in the Bank’s activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is essential to the Bank’s continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk. Operational, business and other non-financial risks are also inherent in the Bank’s activities.

Risk management is the process of identification, measurement and monitoring of risks faced by the Bank, conducted in accordance with its particular organizational and functional structure and established for the appropriate management of the risk appetite expressed by the shareholders.

The independent risk control process does not cover business risks such as changes in the environment, technology and industry. They are monitored through the Bank’s strategic planning process.

The Bank has the Risk Management function which performs centralized risk management to preserve and enhance value for the shareholders. Risk management function is not subordinated to and does not report to divisions accepting relevant risks.

The Risk Management function is based on the following general principles:

- independence from the business lines;
- coherence at all aggregation levels through the use of consistent measuring models;
- timing in providing the data to support the decision-making and control processes;
- timely analysis and identification of potential possibilities of excess of risk thresholds along with the establishment of the corresponding measures to minimize such possibilities;
- transparency in assessment methodologies and criteria on acceptable thresholds for each risk type in accordance with the established levels of decision making process;
- segregation of duties between the Board of Directors, Chief Executive Officer, divisions and departments.

The Bank calculates mandatory ratios on a daily basis in accordance with the requirement of the CBR.

Risk management structure

There is a multilevel system established in the Bank for making decisions related to risk management. The Board of Directors performs a strategic risk management; however, tactical functions are performed by collegiate authorities and specific independent bodies responsible for managing and monitoring risks.

The Board of Directors is responsible for the overall risk management process and for approving risk strategies, principles, methodologies for identifying and managing significant risks, as well as identifying risk appetite and setting the overall risk framework for limits and monitoring capital adequacy and stress-testing.

The Management Board has the responsibility to define and monitor the risk management process within the Bank, including monitoring of risk appetite adherence, monitoring of risk limits and capital adequacy as established by the Bank's approved internal documentation. The Management Board also approved the methodologies for identifying and managing significant risks.

The Financial Risks Committee is responsible for the protection and allocation of the Bank's equity, it ensures the criteria and methods on risks' evaluation and control procedures to be compliant with ISP Group guidelines. It also manages the Bank's portfolio, regularly monitors and evaluates the structure of assets and liabilities, as well as off-balance sheet items, performs the approval of the terms of the new financial products or changes in the existing ones, performs the monitoring of established risk limits compliance (internal and external). The Financial Risks Committee ensures the decision making is performed in accordance with the Banks' policies and other internal documentation.

The Credit Committee is the superior credit approval authority in the Bank. It is responsible for the credit issuance and reapproval of lending conditions within the established limits by counterparty. It makes decisions on proposals made by business units taking into account risks evaluation on each of them. For credit exposures above certain limit the final approval has to be provided by the Credit Committee taking into consideration an opinion provided by the Credit Department of ISP Group.

The Problem Asset Committee assesses the quality of the credit portfolio and its trends, approves assets' classification, level of impairment allowance, performs an analysis of settlement strategies for impaired loans, and monitors collection process and its results.

The Risk Management function is responsible for implementing and maintaining significant and other risk management procedures, for maintenance of acceptable risk level limited by risk appetite to ensure an independent control process, including preparation of reports which include observations made as to its assessment of the effectiveness of Bank's procedures and methodologies, and recommendations for improvement. The frequency and consistency of these reports is in compliance with the Bank's internal documentation.

The Treasury Division is responsible for managing the structure of the Bank's assets and liabilities in terms of the established limits in order to minimize market risks which may arise. It is also primarily responsible for payment position and liquidity risk management.

The Internal Audit function audits annually risk management processes. It reviews risk management policies and procedures and reports its findings, including the assessment of the effectiveness of the Bank's procedures and methodologies and recommendations for improvement, to the Audit Committee. The frequency and consistency of the reports is in compliance with the internal documentation. Based on the recommendations of the Audit Committee, the Board of Directors considers proposed corrective actions.

Risk measurement and reporting systems

Risk monitoring and controlling are primarily performed based on the established limits. These limits reflect the business strategy and market environment as well as the level of the risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition, the Bank maintains the system for reporting related to the capital of the Bank, and monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risks types such as credit, operational, market, interest rate, legal, liquidity and reputational risks.

Information compiled from all business units is examined and processed in order to analyse, control and identify risks. This information is reported to the Board of Directors, the Management Board, the Financial Risks Committee and the Credit Committee. The report is prepared quarterly and includes aggregate credit exposures, credit metric forecasts, hold limit exceptions, market risk exposures, liquidity ratios and risk profile changes. The Management Board analyses risk reports and where necessary reallocates risk limits to achieve target strategic risk profile. The reports of the Risk Management function are periodically discussed by the Board of Directors and the Management Board and proposed corrective actions are considered. The Risk Management function also is involved in process of Homogeneous Credit Risk Monitoring and Risk Appetite Framework leading by the International Subsidiaries Banks Division of the ISP Group.

Risk mitigation

As part of its overall risk management process, the Bank uses derivatives and other instruments to manage exposures resulting from changes in interest rates, foreign currencies, and exposures arising from forecasted transactions.

Risk concentrations

Concentrations arise when a number of counterparties are engaged in similar business activities or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes of the same economic factors.

The Bank's policies and procedures include specific guidelines to focus on maintaining diversified portfolios. The Bank takes measures to correct the excess of the established limits of identified concentrations of credit risks accordingly.

(Thousands of Russian Roubles)

25. Analysis of financial risks

Credit risk

Credit risk is the risk of a financial loss to the Bank if a counterparty of a financial instrument fails to meet its contractual obligations.

The basic principles of credit risk management include:

- close connection between credit risk management system and strategic aims and tasks of the Bank;
- involvement of the Board of Directors and governing bodies of the Bank into credit risk management issues;
- overall identification, analysis and establishment of credit risk minimization system;
- follow-up control, regular monitoring and reporting.

The policies of the Bank within the credit procedures determine:

- procedures for review and approval of loan applications;
- methodology for the credit assessment of the borrowers (corporate and retail);
- methodology for the credit assessment of counterparties, issuers and insurance companies;
- methodology for the evaluation of collateral;
- credit documentation requirements;
- procedures for the ongoing monitoring of loans and other credit exposures.

Credit processes comprise the assessment of credit quality of counterparty and structuring the deal in terms of issued product; credit administration process and further control, including regular analysis of creditworthiness of customers, covenants check, analysis of contractual obligations, planned use of funds, etc.; management of portfolio of homogeneous credit products.

Functions of the deal's initiation and evaluation of credit risks are separated. The Underwriting Department, being an independent division, performs primary and secondary analysis of a client in terms his business, financial situation, operational market, deal structure and compliance with the Bank's and ISP Group's policy. The Credit Committee makes the decision on the loan application on the basis of submissions by the Underwriting Department.

The Bank continuously monitors the performance of individual credit exposures and regularly reassesses the creditworthiness of its customers. The review is based on the customer's most recent financial statements and other information submitted by the customer, or otherwise obtained by the Bank. Apart from planned activities, the Bank also performs additional monitoring in case of any negative signs towards clients' business and financial situation. The credit portfolio is assessed by the Risk Management function with the reports being provided to executive bodies of the Bank and to the Board of Directors.

Maximum exposure to credit risk

The maximum exposure to credit risk is generally reflected in the carrying amounts of financial assets in the consolidated statement of financial position and unrecognized credit related commitment amounts. The impact of possible netting of assets and liabilities to reduce potential credit exposure is not significant.

In accordance with the requirements of the CBR, the Bank also calculates on a daily basis mandatory maximum risk exposure ratio per borrower or group of related borrowers (N6), which regulates (mitigates) the Bank's credit risk in respect of a borrower or group of related borrowers and sets the maximum ratio of the total liabilities of a borrower (borrowers within a group of related borrowers) owed to the Bank, to the Bank's own funds (capital). As at 31 December 2018 and 2017, the maximum level of N6 ratio set by the CBR was 25.0%. The N6 ratio calculated by the Bank as at 31 December 2018 was 21.8% (2017: 18.6%) and was in compliance with limits set by the CBR.

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the consolidated statement of financial position.

The Bank provides financial guarantees and letters of credit to its customers which may require the Bank to make payments on their behalf. Such payments are further collected from customers based on the terms of financial guarantees and letters of credit. They expose the Bank to credit risk and are mitigated by the same credit risk management policies and procedures.

Analysis of sensitivity

The most significant assumptions affecting the ECL allowance relate to calculation of add-on adjustment, applied to PD, LGD and allowance in general to account for different scenarios and to include a forward looking information (Note 3).

A sensitivity analysis of allowance for credit losses on loans to customers to changes of these assumptions is presented in the table below.

	30% increase in Add-on	***30% decrease in Add-on***
Increase (decrease) in allowance for credit losses on loans to customers, measured at amortized cost		
- large corporate customers	(79 593)	79 593
- small and medium corporate customers	(84 029)	84 029
- retail customers	(16 892)	16 892
Total increase (decrease) in allowance for credit losses	**(180 514)**	**180 514**
Impact on profit before taxation and equity:		
Increase (decrease) in profit before taxation	(180 514)	180 514
Increase (decrease) in equity	(144 411)	144 411

(Thousands of Russian Roubles)

Information on quality of debt servicing on loans to customers

Information on delinquencies on loans to customers as at 31 December 2018 is presented in the table below:

			Credit-impaired loans		
	Stage 1	***Stage 2***	***Stage 3***	***Upon initial recognition***	**Total loans to customers**
Large corporate customers					
- not past due	18 545 240	321 313	688 500	580 338	20 135 391
- past due less than 30 days	-	-	29 498	-	29 498
- past due from 31 to 90 days	-	-	355 713	-	355 713
- past due from 91 to 365 days	-	-	15 121	-	15 121
- past due more than 1 year	-	-	1 438 764	96 008	1 534 772
Total before loss allowance	**18 545 240**	**321 313**	**2 527 596**	**676 346**	**22 070 495**
Allowance for credit losses	(253 237)	(12 072)	(1 739 560)	(96 008)	(2 100 877)
Total loans to large corporate customers	**18 292 003**	**309 241**	**788 036**	**580 338**	**19 969 618**
Allowance for credit losses to gross amount of loans, %	*1.37%*	*3.76%*	*68.82%*	*14.20%*	*9.52%*
Small and medium corporate customers					
- not past due	11 930 312	589 771	97 316	-	12 617 399
- past due less than 30 days	169 677	52 769	18 086	-	240 532
- past due from 31 to 90 days	-	96 694	50 705	-	147 399
- past due from 91 to 365 days	-	-	107 687	-	107 687
- past due more than 1 year	-	-	1 947 568	-	1 947 568
Total before loss allowance	**12 099 989**	**739 234**	**2 221 362**	**-**	**15 060 585**
Allowance for credit losses	(203 412)	(76 686)	(1 284 658)	-	(1 564 756)
Total loans to small and medium corporate customers	**11 896 577**	**662 548**	**936 704**	**-**	**13 495 829**
Allowance for credit losses to gross amount of loans, %	*1.68%*	*10.37%*	*57.83%*	*-*	*10.39%*
Retail customers					
- not past due	1 622 128	62 143	21 047	-	1 705 318
- past due less than 30 days	23 624	11 490	121	-	35 235
- past due from 31 to 90 days	4 039	7 213	903	-	12 155
- past due from 91 to 365 days	-	-	18 421	-	18 421
- past due more than 1 year	-	-	103 361	-	103 361
Total before loss allowance	**1 649 791**	**80 846**	**143 853**	**-**	**1 874 490**
Allowance for credit losses	(38 872)	(17 433)	(104 470)	-	(160 775)
Total loans to retail customers	**1 610 919**	**63 413**	**39 383**	**-**	**1 713 715**
Allowance for credit losses to gross amount of loans, %	*2.36%*	*21.56%*	*72.62%*	*-*	*8.58%*
Total loans to customers					
- not past due	32 097 680	973 227	806 863	580 338	34 458 108
- past due less than 30 days	193 301	64 259	47 705	-	305 265
- past due from 31 to 90 days	4 039	103 907	407 321	-	515 267
- past due from 91 to 365 days	-	-	141 229	-	141 229
- past due more than 1 year	-	-	3 489 693	96 008	3 585 701
Total before loss allowance	**32 295 020**	**1 141 393**	**4 892 811**	**676 346**	**39 005 570**
Allowance for credit losses	(495 521)	(106 191)	(3 128 688)	(96 008)	(3 826 408)
Total loans to customers	**31 799 499**	**1 035 202**	**1 764 123**	**580 338**	**35 179 162**
Allowance for credit losses to gross amount of loans, %	*1.53%*	*9.30%*	*63.94%*	*14.20%*	*9.81%*

(Thousands of Russian Roubles)

The following table provides information on the credit quality of loans to customers and net investments in finance leases as at 31 December 2017:

	Gross loans	*Impairment allowance*	*Net loans*	*Impairment allowance to gross loans, %*
Large corporate customers				
Neither past due nor impaired	**12 467 761**	**(279 616)**	**12 188 145**	**2.2**
Past due impaired loans:	**3 052 562**	**(2 289 745)**	**762 817**	**75.0**
- past due less than 90 days	1 710 640	(1 111 756)	598 884	65.0
- more than 90 days but less than 1 year	220 186	(156 921)	63 265	71.3
- past due more than 1 year	1 121 736	(1 021 068)	100 668	91.0
Total loans to large corporate customers	**15 520 323**	**(2 569 361)**	**12 950 962**	**16.6**
Small and medium corporate customers				
Neither past due nor impaired	**12 794 004**	**(164 768)**	**12 629 236**	**1.3**
Past due less than 90 days but not impaired	**21 138**	**(2 648)**	**18 490**	**12.5**
Past due impaired loans:	**3 270 760**	**(1 635 815)**	**1 634 945**	**50.0**
- less than 90 days	317 195	(93 224)	223 971	29.4
- more than 90 days but less than 1 year	453 681	(180 398)	273 283	39.8
- past due more than 1 year	2 499 884	(1 362 193)	1 137 691	54.5
Total loans to small and medium corporate customers	**16 085 902**	**(1 803 231)**	**14 282 671**	**11.2**
Retail customers				
Neither past due nor impaired	**1 678 255**	**(11 828)**	**1 666 427**	**0.7**
Past due less than 90 days but not impaired	**35 649**	**(7 011)**	**28 638**	**19.7**
Past due impaired loans:	**193 444**	**(127 054)**	**66 390**	**65.7**
- past due less than 90 days	34 604	(13 842)	20 762	40.0
- more than 90 days but less than 1 year	24 731	(18 751)	5 980	75.8
- past due more than 1 year	134 109	(94 461)	39 648	70.4
Total loans to retail customers	**1 907 348**	**(145 893)**	**1 761 455**	**7.6**
Total loans to customers	**33 513 573**	**(4 518 485)**	**28 995 088**	**13.5**
Net investments in finance leases				
Neither past due nor impaired	**1 304 753**	**(20 738)**	**1 284 015**	**1.6**
Past due less than 90 days but not impaired	**17 422**	**(1 967)**	**15 455**	**11.3**
Past due impaired loans:	**106 538**	**(71 891)**	**34 647**	**67.5**
- past due less than 90 days	16 558	(3 925)	12 633	23.7
- more than 90 days but less than 1 year	7 840	(3 902)	3 938	49.8
- past due more than 1 year	82 140	(64 064)	18 076	78.0
Total net investments in finance leases	**1 428 713**	**(94 596)**	**1 334 117**	**6.6**

(Thousands of Russian Roubles)

Analysis of collateral and other credit enhancements

The probability of loans repayment to the Bank mainly depends on creditworthiness of a client rather than on a collateral value. Nevertheless, an existence of additional repayment sources is an important part of credit risks minimization.

The Bank accepts different types of assets as collateral for loans to customers in order to minimize its' credit risks. The Bank takes collateral classified as being the 1st class (e.g. guarantees) and standard, depending on its quality and liquidity.

The Bank has procedures for monitoring the fair value of collateral, including additional collateral request when collateral's current value declines. Fair value of the collateral is reviewed within the periodicity determined in the Collateral Policy of the Bank.

During 2018, the Bank obtained certain assets by taking possession of collateral for loans to customers and net investments in finance leases. As at 31 December 2018, the carrying amount of such assets is RUB 201 435 thousand (2017: RUB 194 854 thousand), which consisted of real estate of RUB 194 882 thousand (2017: RUB 186 379 thousand) and other assets of RUB 6 553 thousand (2017: RUB 8 475 thousand). The Bank's policy is to dispose of these assets as soon as it is practicable.

The following tables provide information on collateral and other credit enhancements securing loans to customers, net of allowance for credit losses, as at 31 December 2018.

	Real estate	Motor vehicles	Equipment	Guarantees	Total secured loans	Unsecured loans	Total loans to customers
Loans to customers							
Large corporate customers							
Stage 1	777 555	665 685	968 938	282 671	2 694 849	15 597 154	18 292 003
Stage 2	216 276	-	-	-	216 276	92 965	309 241
Stage 3	746 221	-	-	-	746 221	622 153	1 368 374
	1 740 052	**665 685**	**968 938**	**282 671**	**3 657 346**	**16 312 272**	**19 969 618**
Small and medium customers							
Stage 1	9 122 657	782 209	604 078	-	10 508 944	1 387 633	11 896 577
Stage 2	543 385	30 354	34 417	-	608 156	54 392	662 548
Stage 3	842 075	43 427	22 349	-	907 851	28 853	936 704
	10 508 117	**855 990**	**660 844**	**-**	**12 024 951**	**1 470 878**	**13 495 829**
Retail customers							
Stage 1	421 656	-	-	-	421 656	1 189 263	1 610 919
Stage 2	46 151	-	-	-	46 151	17 262	63 413
Stage 3	39 383	-	-	-	39 383	-	39 383
	507 190	**-**	**-**	**-**	**507 190**	**1 206 525**	**1 713 715**
Total loans to customers	**12 755 359**	**1 521 675**	**1 629 782**	**282 671**	**16 189 487**	**18 989 675**	**35 179 162**
Net investments in finance lease							
Stage 1	4 976	599 230	731 149	-	1 335 355	2 338	1 337 693
Stage 2	-	1 712	12 541	-	14 253	-	14 253
Stage 3	-	9 696	11 476	-	21 172	2 652	23 824
Total net investments in finance leases	**4 976**	**610 638**	**755 166**	**-**	**1 370 780**	**4 990**	**1 375 770**

(Thousands of Russian Roubles)

The following tables provide information on collateral and other credit enhancements securing loans to customers, net of allowance for credit losses, as at 31 December 2017.

	Real estate	Motor vehicles	Equipment	Guarantees	Total secured loans	Unsecured loans	Total loans to customers
Loans to customers							
Large corporate customers							
Neither past due nor impaired	953 352	294 793	940 999	237 379	2 426 523	9 761 622	12 188 145
Impaired loans	624 966	-	-	-	624 966	137 851	762 817
	1 578 318	**294 793**	**940 999**	**237 379**	**3 051 489**	**9 899 473**	**12 950 962**
Small and medium customers							
Neither past due nor impaired	8 121 572	953 913	700 341	-	9 775 826	2 853 410	12 629 236
Past due but not impaired	10 638	272	253	-	11 163	7 327	18 490
Impaired loans	1 376 849	140 528	57 646	-	1 575 023	59 922	1 634 945
	9 509 059	**1 094 713**	**758 240**	**-**	**11 362 012**	**2 920 659**	**14 282 671**
Retail customers							
Neither past due nor impaired	496 763	-	-	-	496 763	1 169 664	1 666 427
Past due but not impaired	12 359	-	-	-	12 359	16 279	28 638
Impaired loans	61 991	-	-	-	61 991	4 399	66 390
	571 113	**-**	**-**	**-**	**571 113**	**1 190 342**	**1 761 455**
Total loans to customers	**11 658 490**	**1 389 506**	**1 699 239**	**237 379**	**14 984 614**	**14 010 474**	**28 995 088**
Net investments in finance lease							
Neither past due nor impaired	9 274	715 661	549 051	-	1 273 986	10 029	1 284 015
Past due but not impaired	-	8 236	7 219	-	15 455	-	15 455
Impaired loans	-	6 396	25 806	-	32 202	2 445	34 647
Total net investments in finance leases	**9 274**	**730 293**	**582 076**	**-**	**1 321 643**	**12 474**	**1 334 117**

The tables above are presented on the basis of fair value of collateral as described below excluding over collateralization.

For loans secured by multiple types of collateral, collateral that is most relevant for impairment assessment is disclosed. Guarantees and sureties received from individuals, such as shareholders of SME borrowers, are not considered for impairment assessment purposes.

For impaired, past due and other certain loans the fair value of collateral is updated with frequency defined in the Collateral Policy.

Mortgage loans to individuals are secured by the underlying housing real estate. The Bank’s policy is to issue mortgage loans with a loan-to-value ratio of a maximum of 85%.

For certain mortgage loans the Bank updates the appraised values of collateral obtained at inception of the loan to the current values considering the approximate changes in property values. The Bank may also obtain a specific individual valuation of collateral at each reporting date where there are indications of impairment. For the remaining mortgage loans the fair value of collateral was estimated at inception of the loans and was not adjusted for subsequent changes to the reporting date.

(Thousands of Russian Roubles)

Geographical concentration

The geographical concentration of assets and liabilities as at 31 December 2018 is as follows:

	Russia	OECD	CIS and other countries	Total
Assets				
Cash and cash equivalents	3 294 812	1 805 575	163	5 100 550
Mandatory cash balances with the Central Bank of the Russian Federation	386 641	-	-	386 641
Amounts due from credit institutions	4 226 249	4 171 491	1 584 627	9 982 367
Investment securities	4 079 778	-	-	4 079 778
Derivative financial assets	5 359	-	-	5 359
Loans to customers:	33 603 348	15 972	1 559 842	35 179 162
- corporate customers	18 410 145	-	1 559 473	19 969 618
- small and medium customers	13 495 829	-	-	13 495 829
- retail customers	1 697 374	15 972	369	1 713 715
Net investments in finance leases	1 375 770	-	-	1 375 770
Property and equipment	714 450	-	-	714 450
Intangible assets	447 402	-	-	447 402
Deferred income tax assets	373 559	-	-	373 559
Other assets	756 366	1 243 578	37	1 999 981
Total assets	**49 263 734**	**7 236 616**	**3 144 669**	**59 645 019**
Liabilities				
Amounts due to credit institutions	2 164 803	8 307 121	13 631	10 467 555
Derivative financial liabilities	4	-	-	4
Amounts due to customers:	26 585 067	3 217 093	163 005	29 965 165
- legal entities, state and non-profit organizations	15 754 597	2 237 354	18 728	18 010 679
- individuals	10 830 470	979 739	144 277	11 954 486
Debt securities issued	3 059 954	-	-	3 059 954
Other liabilities	655 557	4 095	51 971	711 623
Subordinated loan	-	2 828 605	-	2 828 605
Total liabilities	**32 465 385**	**14 356 914**	**228 607**	**47 032 906**
Net position	**16 816 349**	**(7 120 298)**	**2 916 062**	**12 612 113**
Credit related commitments	**12 051 163**	**114 607**	**3 484 798**	**15 650 568**

Assets, liabilities and credit related commitments are allocated based on the country in which the counterparty performs its business activities. Cash on hand and property and equipment are allocated based on the country in which they are physically held. The Bank's operations include transactions with counterparties that operate in OECD countries, primarily Italy, Luxemburg, Germany, United States and United Kingdom.

The geographical concentration of assets and liabilities as at 31 December 2017 is as follows:

	Russia	OECD	CIS and other countries	Total
Net position	12 220 563	(1 589 627)	1 813 642	12 444 578
Credit related commitments	13 555 553	86 395	4 032 288	17 674 236

(Thousands of Russian Roubles)

Liquidity risk

Liquidity risk is the risk of a potential loss arising in case the Bank is unable to meet its financial obligations as they fall due.

Liquidity risk exists when maturities of assets and liabilities do not match. The matching and/or controlled mismatching of maturities and interest rates of assets and liabilities is fundamental to liquidity management. It is unusual for financial institutions ever to be completely matched since business transacted is often of an uncertain term and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

The Bank maintains liquidity management with the objective to ensure that funds will be available at all times to honor all cash flow obligations as they become due. The liquidity policy is reviewed and approved by the Board of Directors.

The Treasury Division performs the daily liquidity management in line with the Policy on liquidity risk management established in the Bank. It performs its' activity to comply with the structured ratios and liquidity ratios of the CBR and ISP Group. When performing operating activity on liquidity management, the Treasury Division maintains the volume of liquid assets portfolio of the Bank at the required level, and uses the interbank instruments to optimize the structure of the Bank's balance.

The Risk Management function performs daily monitoring of liquidity position and performs stress-testing on a regular basis, taking into consideration possible scenarios of market conditions, both at normal and unfavorable level.

The liquidity position is also assessed and managed by the Bank, based on certain liquidity ratios calculated on a daily basis in accordance with the requirements of the CBR. As at 31 December, these ratios are as follows:

	Requirement	*2018, %*	*2017, %*
Instant Liquidity Ratio (N2)	Not less than 15%	66.1	58.7
Current Liquidity Ratio (N3)	Not less than 50%	87.2	112.4
Long-Term Liquidity Ratio (N4)	Not more than 120%	69.1	61.4

The Bank also regularly monitors Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR), established by the requirements of the Basel III.

The table below shows the structure of assets and liabilities as at 31 December 2018 in accordance with their contractual maturity.

	On demand	*Less than 1 month*	*From 1 to 3 months*	*From 3 months to 1 year*	*From 1 to 5 years*	*Over 5 years*	*Overdue or no stated maturity*	*Total*
Assets								
Cash and cash equivalents	5 100 550	-	-	-	-	-	-	5 100 550
Mandatory cash balances with the CBR	157 628	98 933	44 859	69 007	16 214	-	-	386 641
Amounts due from credit institutions	135 780	8 261 960	-	1 584 627	-	-	-	9 982 367
Investment securities	-	4 079 778	-	-	-	-	-	4 079 778
Derivative financial assets	-	5 359	-	-	-	-	-	5 359
Loans to customers	-	1 843 178	3 277 309	8 748 509	19 059 855	668 551	1 581 760	35 179 162
Net investments in finance leases	-	66 361	134 322	507 617	612 311	-	55 159	1 375 770
Property and equipment	-	-	-	-	-	-	714 450	714 450
Intangible assets	-	-	-	-	-	-	447 402	447 402
Deferred income tax assets	-	-	-	-	-	-	373 559	373 559
Other assets	-	1 270 062	225 221	209 687	95 060	-	199 951	1 999 981
Total assets	**5 393 958**	**15 626 631**	**3 681 711**	**11 119 447**	**19 783 440**	**668 551**	**3 372 281**	**59 645 019**
Liabilities								
Amounts due to credit institutions	1 253 265	-	2 384 277	24 103	6 805 910	-	-	10 467 555
Derivative financial liabilities	-	4	-	-	-	-	-	4
Amounts due to customers	12 216 378	7 667 444	3 476 599	5 348 108	1 256 636	-	-	29 965 165
incl. amounts due to individuals	2 467 896	986 185	2 750 432	4 576 902	1 173 071	-	-	11 954 486
Debt securities issued	-	-	-	3 059 954	-	-	-	3 059 954
Subordinated loan	-	-	-	-	-	2 828 605	-	2 828 605
Other liabilities	147 570	195 638	139 488	122 996	90 009	15 922	-	711 623
Total liabilities	**13 617 213**	**7 863 086**	**6 000 364**	**8 555 161**	**8 152 555**	**2 844 527**	**-**	**47 032 906**
Net position	**(8 223 25)**	**7 762 545**	**(2 318 653)**	**2 564 286**	**11 630 885**	**(2 175 976)**	**3 372 281**	**12 612 113**
Cumulative liquidity gap:								
as at 31 December 2018	**(8 223 255)**	**(460 710)**	**(2 779 363)**	**(215 077)**	**11 415 808**	**9 239 832**	**12 612 113**	
as at 31 December 2017	**(9 368 638)**	**3 622 490**	**3 319 295**	**3 576 820**	**6 590 618**	**7 680 305**	**12 444 578**	

(Thousands of Russian Roubles)

Overdue loans to customers include loans that are overdue in full and overdue payments on loans that are partially overdue.

In the Russian marketplace, many short-term credits are granted with the expectation of renewing the loans at maturity. As such, the ultimate maturity of assets may be different from the analysis presented above.

Investment securities represented by Russian State bonds (OFZ), the CBR bonds ("KOBR") are classified in the category "Less than 1 month" as they are considered to be highly liquid financial instruments.

Term deposits not withdrawn by the customers, are classified within the "On demand" category.

Debt securities are reflected by the final maturity date.

Unused vacations in the amount of RUB 31 617 thousand are classified into the category "from 3 months to 1 year" in accordance with the Bank's judgement based on historical pattern.

Mandatory cash balances with the CBR are allocated between the different maturities categories in accordance with the maturities of the liabilities to which they relate.

When necessary accumulated gap in the category "on demand" could be managed by attracting funds from ISP Group.

The maturity profile of financial liabilities and credit related commitments as at 31 December 2018 based on contractual undiscounted repayment obligations is as follows:

	On demand	*Less than 1 month*	*From 1 to 3 months*	*From 3 months to 1 year*	*From 1 to 5 years*	*Over 5 years*	*Total*	*Carrying amount*
Financial liabilities								
Amounts due to credit institutions	1 253 265	21 312	2 426 612	213 464	7 310 592	-	11 225 245	**10 467 555**
Amounts due to customers	12 216 378	7 679 802	3 512 420	5 495 721	1 317 814		30 222 135	**29 965 165**
incl. amounts due to individuals	2 467 896	988 657	2 778 706	4 708 890	1 233 418	-	12 177 567	**11 954 486**
Debt securities issued	-	-	-	3 291 720		-	3 291 720	**3 059 954**
Subordinated loan	-	15 237	30 474	137 135	731 386	3 194 799	4 109 031	**2 828 605**
Other liabilities	159 585	195 638	139 488	122 996	90 009	3 907	711 623	**711 623**
Derivative financial instruments								
- inflow	-	*(1 023 816)*	-	-	-	-	*(1 023 816)*	***(5 359)***
-outflow	-	*1 018 461*	-	-	-	-	*1 018 461*	***4***
Total financial liabilities	**13 629 228**	**7 906 634**	**6 108 994**	**9 261 036**	**9 449 801**	**3 198 706**	**49 554 399**	**47 027 547**
Credit related commitments	**15 650 568**	**-**	**-**	**-**	**-**	**-**	**15 650 568**	**15 650 568**

The maturity profile of financial liabilities and credit related commitments as at 31 December 2017 based on contractual undiscounted repayment obligations is as follows:

	On demand	*Less than 1 month*	*From 1 to 3 months*	*From 3 months to 1 year*	*From 1 to 5 years*	*Over 5 years*	*Total*	*Carrying amount*
Financial liabilities								
Amounts due to credit institutions	970 502	3 395 428	16 574	130 788	1 610 772	-	**6 124 064**	**5 884 650**
Amounts due to customers	12 392 827	3 184 606	3 544 740	10 627 981	1 250 554	-	**31 000 708**	**30 527 105**
incl. amounts due to individuals	*2 027 448*	*1 467 383*	*2 255 899*	*10 355 355*	*1 171 620*	-	***17 277 705***	***16 826 402***
Debt securities issued	-	-	-	427 766	3 291 720	-	**3 719 486**	**3 186 066**
Subordinated loan	-	12 634	25 267	113 703	2 911 254	-	**3 062 858**	**2 304 839**
Other liabilities	-	-	199 311	24 860	-	-	**224 171**	**224 171**
Total financial liabilities	**13 363 329**	**6 592 668**	**3 785 892**	**11 325 098**	**9 064 300**	**-**	**44 131 287**	**42 126 831**
Credit related commitments	**17 674 236**	**-**	**-**	**-**	**-**	**-**	**17 674 236**	**17 674 236**

The total gross inflow and outflow disclosed in the tables above is the contractual, undiscounted cash flow on the financial liability or commitment.

In accordance with the Russian Civil Code, the Bank is obliged to repay time deposits to individuals upon demand of a depositor. In the tables above these deposits are classified in accordance with their stated maturity and are disclosed by each time band.

Market risk

Market risk is the risk that the fair value of assets or future cash flows of financial instruments will diminish due to changes in the interest rates, currency rates and equity prices. Market risk includes currency risk, interest rate risk and other price risks.

Market risks arises from open positions in interest rate, currency and equity financial instruments, which are exposed to general and specific market movements.

The objective of market risk management is to manage and control market risk exposures within acceptable parameters whilst optimizing the return of risk.

Overall authority for market risk is vested in the Financial Risks Committee. Market risk limits are approved by the Board of Directors based on recommendations of the Risk Management function and the Financial Risks Committee.

The Bank manages its market risk by setting open positions and other limits in relation to financial instruments, which include acceptable level of positions (nominal and market ones), Value at Risk ("VaR"), PV100 and stop-loss limits, limits on open positions. These are monitored on a regular basis and reviewed and approved by the Management Board and the Board of Directors.

VaR – Investment securities

The Bank applies a VaR methodology to assess the market risk positions held and to estimate the potential economic loss based upon a number of parameters and assumptions for various changes in market conditions. VaR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. The VaR model used by the Bank is based upon a 99 percent confidence level and assumes a 1-day holding period.

For the purposes of interest rate risk calculations for fixed income securities the information on interest rates volatility and correlation is received from the ISP Group on a daily basis.

Although VaR is a valuable tool in measuring risk exposures, it has a number of limitations:

- the use of historical data as a basis for determining future events may not encompass all possible scenarios, particularly those that are of an extreme nature;
- a 1-day holding period assumes that all positions can be liquidated or hedged within that period. This is considered to be a realistic assumption in almost all cases but may not be the case in situations in which there is severe market illiquidity for a prolonged period;
- the use of a 99% confidence level does not take into account losses that may occur beyond this level. There is a one percent probability that the loss could exceed the VaR estimate;
- VaR is only calculated on the end-of-day balances and does not necessarily reflect exposures that may arise on positions during the trading day;
- the VaR measure is dependent upon the position and the volatility of market prices. The VaR of an unchanged position reduces if market volatility declines and vice versa.

To determine the reliability of the VaR model, actual outcomes are monitored regularly to test the validity of the assumptions and the parameters used in the VaR model. Market risk positions are also subject to regular stress tests to ensure that the Bank would withstand an extreme market event.

VaR limits have been established for available-for-sale portfolio, and exposure is calculated and monitored daily against the limits set by the Board of Directors. As at 31 December 2018, VaR for investment securities portfolio is RUB 481 thousand (2017: RUB 1 366 thousand).

(Thousands of Russian Roubles)

Interest rate risk for non-trading positions

Interest rate risk is the risk of a potential loss due to adverse changes in the market interest rates affecting the assets, liabilities and unrecognized positions sensitive to such changes.

Interest rate risk includes the following:

- Repricing Risk - the risk linked to the time differences in maturities (for fixed rate positions) and in the repricing dates (for floating rate positions);
- Yield Curve Risk - the risk linked to changes in the slope and shape of the yield curve;
- Basis Risk - the risk linked to the mismatch in the rates to be received and paid on different instruments, with similar repricing characteristics. When interest rates change, these differences can give rise to unexpected changes in the cash flows and interest margins for assets, liabilities and unrecognized positions with similar maturities or repricing frequencies.

The Bank uses the following methods to measure interest rate risk:

Fair value sensitivity measures the changes in the fair value of assets, liabilities and unrecognized positions resulting from a parallel rise in the discount curves by 100 b.p. To calculate the fair value, the discount curves which are suitable for measuring individual financial instruments are applied.

An analysis of sensitivity of the fair value as at 31 December is as follows:

Currency	***2018***	***2017***
RUB	(187 591)	(163 357)
USD	110 671	89 972
EUR	(87 134)	(2 189)
Total	**(164 054)**	**(75 574)**

A parallel fall in the discount curves by 100 b.p. would have had the equal but opposite effect on the fair value of assets, liabilities and unrecognized positions.

Sensitivity of the Interest Margin measures a one-year impact on the interest margin resulting from a parallel rise of the interest rate curves by 100 b.p. This measure highlights the effect of changes in interest rates on the portfolio being divided into current and term products excluding assumptions on future changes in the structure of assets and liabilities. Therefore, it cannot be considered as a predictor of the future levels of the interest margin.

An analysis of sensitivity of the interest margin as at 31 December is as follows.

Currency	***2018***	***2017***
RUB	66 125	33 985
USD	11 087	23 189
EUR	(2 926)	1 480
Total	**74 286**	**58 654**

The Bank is exposed to interest rate risk, principally as a result of lending at fixed interest rates, in amounts and for periods, which differ from those of term borrowings at floating interest rates. In practice, interest rates are generally fixed on a short-term horizon. To reduce the interest rate risk the Bank includes in its loan contracts a clause providing for a change in the interest rate in the event of a significant change in the market interest rates. Additionally, interest rates for long-term loans in foreign currencies are linked to LIBOR and EURIBOR.

The Board of Directors sets limits on the potential loss from interest rate risk that may be undertaken. These limits are regularly monitored.

(Thousands of Russian Roubles)

Currency risks

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates. Open currency positions limits, set by the CBR, are monitored on a daily basis The following table shows the foreign currency exposure structure of financial assets and liabilities as at 31 December 2018 and 2017:

	RUB	*USD*	*EUR*	*Other currencies*	*Total*
Assets					
Cash and cash equivalents	2 954 302	1 094 880	1 046 620	4 748	5 100 550
Mandatory cash balances with the CBR	386 641	-	-	-	386 641
Amounts due from credit institutions	2 836 814	5 560 926	1 584 627	-	9 982 367
Investment securities	4 079 778	-	-	-	4 079 778
Derivative financial assets	5 352	7	-	-	5 359
Loans to customers	22 939 548	7 916 548	4 323 066	-	35 179 162
Net investments in finance leases	1 375 770	-	-	-	1 375 770
Property and equipment	714 450	-	-	-	714 450
Intangible assets	447 402	-	-	-	447 402
Deferred income tax assets	373 559	-	-	-	373 559
Other assets	724 132	21 610	1 251 757	2 482	1 999 981
Total assets	**36 837 748**	**14 593 971**	**8 206 070**	**7 230**	**59 645 019**
Liabilities					
Amounts due to credit institutions	3 398 441	3 372 941	3 696 173	-	10 467 555
Derivative financial liabilities	4	-	-	-	4
Amounts due to customers	17 740 518	8 457 456	3 764 090	3 101	29 965 165
Debt securities issued	3 059 954	-	-	-	3 059 954
Subordinated loan	-	2 828 605	-	-	2 828 605
Other liabilities	359 421	156 679	195 523	-	711 623
Total liabilities	**24 558 338**	**14 815 681**	**7 655 786**	**3 101**	**47 032 906**
Net recognised position	**12 279 410**	**(221 710)**	**550 284**	**4 129**	**12 612 113**
Net unrecognized position	966 779	25 843	(992 622)	-	-
Cumulative currency gap	**13 246 188**	**(195 867)**	**(442 338)**	**4 129**	**12 612 113**
Credit related commitments	**4 617 258**	**10 001 252**	**1 032 058**	**-**	**15 650 568**

The exposure to currency risk as at 31 December 2017 is as follows:

	RUB	*USD*	*EUR*	*Other currencies*	*Total*
Net recognised and accumulated position	**12 014 558**	**(148 509)**	**589 567**	**(11 038)**	**12 444 578**
Credit related commitments	**5 076 124**	**11 903 545**	**511 093**	**183 474**	**17 674 236**

The Bank has loans to customers denominated in foreign currencies. Depending on the revenue sources of the borrower, the appreciation of the currencies against the RUB may adversely affect the borrowers' repayment ability and therefore increases the likelihood of future loan losses.

The following table analyses the effect of the reasonably possible movement in the currency rates against the RUB on the profit or loss and equity before income tax for the currencies to which the Bank has significant exposure as at 31 December 2018 and 2017 on its non-trading positions and foreign currency derivatives.

Currency	*2018*	*2017*
10% appreciation of USD against RUB	(19 587)	(14 851)
10% appreciation of EUR against RUB	(44 234)	58 957
Total	**(63 821)**	**44 106**

(Thousands of Russian Roubles)

Operational risk

Operational risk is the risk of direct or indirect losses arising from failures in internal processes, human errors, IT systems and technical failures or external events. This definition includes legal risk but does not include strategic and reputation risks.

For managing operational risk the Bank follows operational risk guidelines and methodology of the CBR and ISP Group in compliance with Basel recommendations as well as locally-developed methodologies and tools. The Bank, in accordance with the ISP Group's requirements and the regulatory suggestions, developed an operational risk framework consisting of operational risk policy, self-testing and the process of monitoring of key operational risk indicators in order to perform an effective operational risk management and support the Bank's business.

Operational risk management is a structured system of processes, functions, responsibilities and resources aimed at detection and monitoring, assessment, minimization and control of operational risks, as well as providing their effective prevention in accordance with the requirements of the ISP Group and external legislation. Operational risk management is directly connected with the level of corporate governance and corporate ethics of the Bank.

The calculation of operational risk level is maintained in accordance with the CBR requirements.

The Bank applies the following methods to minimize the risk:

- establishing regulations of performing all key operations in terms of internal documentation;
- accounting and documenting the operations, including the data checks in initial documentation with operation accounts;
- segregation of duties, double check principle, setting of limits on operations;
- automation of operations;
- control over the access to the information, multi-level security of data;
- taking measures on ensuring going concern when doing banking operations and deals;
- hedging of operational risks;
- minimization of risks related to personnel by means of establishing criteria on its' screening and examination, carrying out necessary events on personnel training.

The usage of the above methods leads to minimization of operational risks and allows to keep the loss from the operational risks occurrence at the level which does not influence the execution of Bank's obligations.

26. Fair value of financial instruments

Fair value hierarchy

The Bank uses the following fair value hierarchy for measuring fair values of financial instruments:

- Level 1: quoted market prices (unadjusted) in an active market for an identical instrument;
- Level 2: valuation techniques for which all significant inputs are observable, either directly or indirectly;
- Level 3: valuation techniques which use significant unobservable inputs.

The table below analyses financial instruments measured at fair value at 31 December 2018, by the level in the fair value hierarchy into which the fair value measurement is categorised.

	Level 1	***Level 2***	***Total***
Financial assets			
Derivative financial assets	-	5 359	5 359
Investment securities	4 079 778	-	4 079 778
	4 079 778	**5 359**	**4 085 137**
Financial liabilities			
Derivative financial liabilities	-	4	4

As at 31 December 2017 financial instruments measured at fair value include investment securities in the amount of RUB 4 130 899 thousand, that belong to Level 1 in the fair value hierarchy.

As at 31 December 2018, the Bank has repossessed collateral in the amount of RUB 201 435 thousand (2017: RUB 194 854 thousand) that is subsequently measured at lower of cost and fair value less cost to sell, for which fair value was determined using inputs that belong to Level 3 in the fair value hierarchy.

The estimation of fair value of repossessed collateral is based on a common valuation techniques depending on the type of collateral (market comparison, income based, cost approach). The Bank adjusts the estimated market value of similar property using the liquidity discounts. The discounts, applied by the Bank ranges from 15% to 30% for residential property in Moscow; 40% to 50% for office property and 50% to 60% for regional residential property.

The estimated fair value of financial instruments carried at amortised cost as at 31 December 2018 and 2017 approximates their carrying values.

(Thousands of Russian Roubles)

27. Related party transactions

In accordance with IAS 24 "*Related Party Disclosures*", parties are considered to be related if one party directly, or indirectly through one or more intermediaries controls, is controlled by, or is under common control with, the entity; has an interest in the entity that gives it significant influence over the entity; the party is an associate of the entity; the party is a member of the key management personnel of the entity or its parent.

Banking transactions are entered into in the normal course of business with the Bank's shareholders and key management personnel. These transactions include loans, deposits and other transactions, and are performed at market conditions.

Starting from 2005 the Bank is a member of ISP Group. ISP Group members are entities comprising a banking group which has a leading position on the Italian market and a strong international presence, mainly in Central-Eastern Europe and the Mediterranean region.

Intesa Sanpaolo Holding International SA (Luxembourg) is a parent entity of the Bank as at 31 December 2018 and 2017 owning 53.0228% of shares. Intesa Sanpaolo S.p.A. (Italy) is the ultimate controlling party of the Bank.

Transactions with foreign branches of Intesa Sanpaolo S.p.A. (Italy), which are located in different countries, are disclosed in the category named "Intesa Sanpaolo Group members".

The outstanding balances with the related parties as at 31 December 2018 and related profit or loss amounts of transactions with the related parties for 2018 are as follows:

	Intesa Sanpaolo S.p.A.	*Intesa Sanpaolo Holding International SA*	*Intesa Sanpaolo Group members*	*Key management personnel*
Cash and cash equivalents				
Correspondent accounts and overnight placements with other credit institutions	855 155	-	899	-
Amounts due from credit institutions				
Time deposits	4 171 655	-	-	-
Allowance for credit losses	(164)	-	-	-
Loans to customers				
Movements in gross carrying amount:				
- opening balance as at 1 January	-	-	-	18 773
- repayments during the year	-	-	-	(4 498)
- closing balance as at 31 December	-	-	-	14 275
Allowance for credit losses	-	-	-	(162)
Net carrying amount	-	-	-	14 113
Amounts due to credit institutions				
Current accounts	1 217 543	-	34 095	-
Term deposits	2 384 277	-	4 684 837	-
Amounts due to customers				
Current accounts	-	-	-	25 651
Term deposits	-	-	-	47 854
Subordinated loan	-	-	2 828 605	-
Other assets	-	-	1 193 516	-
Guarantees on loans and credit lines to customers and counter-guarantees				
Received by the Bank	566 810	-	-	-
Issued by the Bank	2 985 598	-	5 649 766	-
Interest income				
Amounts due from credit institutions	38 499	-	50	-
Loans to customers	-	-	-	1 786
Interest expense				
Amounts due to credit institutions	(11 315)	-	(76 424)	-
Amounts due to customers	-	-	-	(2 685)
Subordinated loan	-	-	(165 046)	-
Changes in allowance for credit losses	(164)	-	-	(74)
Net gains from foreign currencies	888	-	-	-
Fee and commission income	2 196	-	1 107 389	-
Fee and commission expense	(6 798)	-	(2 872)	-
Other general administrative expenses	-	-	(40 306)	-

As at 31 December 2018, other asses balance with Intesa Sanpaolo Group members comprises a commission and fee receivable for participation in credit facilities' origination receivable (note 14).

(Thousands of Russian Roubles)

The outstanding balances with the related parties as at 31 December 2017and related profit or loss amounts of transactions with the related parties for 2017 are as follows:

	Intesa Sanpaolo S.p.A.	*Intesa Sanpaolo Holding International SA*	*Intesa Sanpaolo Group members*	*Key management personnel*
Cash and cash equivalents				
Correspondent accounts and overnight placements with other credit institutions	749 346	-	298 800	-
Amounts due from credit institutions				
Time deposits	2 728 577	-	-	-
Loans to customers				
Movements in gross carrying amount:				
- opening balance as at 1 January	-	-	-	-
- issued during the year	-	-	-	18 861
- closing balance as at 31 December	-	-	-	18 861
Allowance for credit losses	-	-	-	(88)
Net carrying amount	-	-	-	18 773
Amounts due to credit institutions				
Current accounts	945 357	-	19 097	-
Amounts due to customers				
Current accounts	-	-	-	11 268
Term deposits	-	-	-	38 790
Subordinated loan	-	-	2 304 839	-
Other assets	-	-	1 017	-
Other liabilities	-	-	6 943	-
Guarantees on loans and credit lines to customers and counter-guarantees				
Received by the Bank	483 689	-	-	-
Issued by the Bank	3 597 340	-	3 771 661	-
Interest income				
Amounts due from credit institutions	43 148	-	420	-
Loans to customers	-	-	-	1 017
Interest expense				
Amounts due to credit institutions	(12 019)	-	-	-
Amounts due to customers	-	-	-	(2 388)
Subordinated loan	-	-	(153 585)	-
Changes in allowance for credit losses	-	-	-	(88)
Net losses from foreign currencies	(36 600)	-	-	-
Fee and commission income	1 378	-	129 380	-
Fee and commission expense	(6 414)	-	(1 493)	-
Other general administrative expenses	-	-	(37 015)	-

Remuneration of the Management Board for 2018 presented within personnel expenses totals RUB 86 167 thousand, including social contributions of RUB 7 736 thousand (2017: RUB 78 315 thousand and RUB 7 017 thousand respectively).

Remuneration of the Board of Directors for 2018 totals RUB 20 726 thousand (2017: RUB 18 862 thousand).

As at 31 December 2018, guarantees and counter-guarantees received presented in the tables above comprise of:

- Guarantees issued by Intesa Sanpaolo Group members on loans and credit lines issued by the Bank and the Bank being a beneficiary, for the total amount of RUB 282 671 thousand (31 December 2017: RUB 237 379 thousand); the guarantees have the same term as the underlying credit facilities. Commission is paid by the borrower.
- counter guarantees for guarantees issued by Intesa Sanpaolo Group members totaling RUB 284 139 thousand maturing from 1 January to 1 June 2019 and bearing commission rates from 0.15% to 0.4% (31 December 2017: RUB 246 310 thousand, maturing from 1 January 2018 to 1 June 2019, commission rates from 0.15% to 0.4%).

As at 31 December 2018, guarantees and counter-guarantees issued presented in the tables above comprise of:

- guarantees issued by the Bank to Intesa Sanpaolo Group members for the total amount of RUB 8 609 985 thousand (31 December 2017: RUB 7 112 473 thousand); these guarantees have the same term as the underlying credit facilities; commission varies from 0.3% to 1.6%.
- counter guarantees issued by the Bank for guarantees issued by Intesa Sanpaolo Group members in the amount of RUB 25 379 thousand maturing from 23 March 2019 to 31 August 2019 and bearing commission rate of 1% (31 December 2017: RUB 256 528 thousand, maturing from 15 March 2018 to 15 December 2018, commission rates vary from 1.0% to 2.0%).

(Thousands of Russian Roubles)

28. Capital adequacy

The primary objectives of the Bank's capital management are the following:

- full compliance with the capital requirements imposed by the CBR and Russian legislation;
- maintaining the Bank's ability to continue as a going concern in order to maximize shareholder value and provide economic benefits to other parties;
- ensuring that the amount of capital is sufficient for business expansion and development.

The Bank's equity management process are in line with the requirements of Directive of CBR № 4482-U "On the form and procedure of disclosure by credit organizations of information on incurred risks, procedures for assessment of risks, management of risks and capital", as well as the part of Component 2 of the Basel Committee on Banking Supervision (Basel III), establishing the requirements for the existence of own process of assessing capital adequacy in Banks:

- existence of appropriate corporate governance mechanisms;
- existence of organizational structure with clear responsibilities;
- existence of clear and effective internal control systems.

On a regular basis, the Bank develops the structured report (VPODK Report) describing the main features of the capital adequacy assessment process, the Bank's exposure to risks and the risk-based capital adequacy decision. VPODK Report also contains self-assessment of VPODK indicating direction for improvement, process weaknesses and corrective measures to be taken.

The Bank monitors its capital adequacy using, among other measures, the ratios established by the Basel Capital Accord 1988, with subsequent amendments ("Basel Capital Accord"), and the ratios established by the CBR.

The Bank has complied with all externally imposed by the CBR capital requirements as at 31 December 2018 and 2017.

The Bank manages its capital structure and makes adjustments to reflect changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payments to the shareholders, return on capital to the shareholders or issue equity securities. No changes were made in the objectives, policies and processes from the previous year.

Capital adequacy under Russian Legislation

The Bank calculates amount of capital in accordance with Provision of the CBR dated 28 December 2012 No. 395–P "*On Methodology of Calculation of Own Funds (Capital) of the Credit Organizations (Basel III)*".

As at 31 December 2018 and 2017, minimum levels of basic capital ratio (ratio N1.1), main capital ratio (ratio N1.2), own funds (capital) ratio (ratio N1.0) are 4.5%, 6.0% and 8.0%, accordingly.

As at 31 December, the Bank's CBR-defined capital adequacy ratios exceed the required statutory minimums and are as follows:

	2018	***2017***
Base capital	9 488 618	9 644 752
Additional capital	-	-
Main capital	**9 488 618**	**9 644 752**
Supplementary capital	3 260 696	2 735 855
Own funds (capital)	**12 749 314**	**12 380 607**
Risk-weighted assets (for basic and main capital ratios)	**72 587 080**	**62 119 235**
Risk-weighted assets (for own funds (capital) ratio)	**72 764 973**	**62 551 082**
Ratio N1.1 (%)	**13.1%**	**15.5%**
Ratio N1.2 (%)	**13.1%**	**15.5%**
Ratio N1.0 (%)	**17.5%**	**19.8%**

(Thousands of Russian Roubles)

Capital adequacy ratio under the Basel Capital Accord (unaudited)

The Bank applies the Basel II Framework for the purpose of capital adequacy calculation using the simplified standardized approach for credit risk measurement, the standardized measurement method for market risk and the basic indicator approach for operational risk measurement. The Bank's capital adequacy ratio as computed in accordance with the Basel Capital Accord as at 31 December is as follows:

	2018	***2017***
Share capital	10 820 181	10 820 181
Retained earnings and other capital reserves	1 671 991	1 217 451
Deductions	(447 402)	(585 667)
Tier 1 capital	**12 044 770**	**11 451 965**
Revaluation of buildings	134 724	384 144
Subordinated loan (unamortized portion)	2 828 605	2 304 839
Total capital	**15 008 099**	**14 140 948**
Risk-weighted assets	**74 277 146**	**72 084 937**
Tier 1 capital ratio	**16.2%**	**15.9%**
Total capital ratio	**20.2%**	**19.6%**

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. When calculating capital under Basel, the Bank assigns 100% risk weights to exposures of counterparties operating in jurisdictions with country risk rating below "3" in accordance with the OECD classification (including Russian Federation) or with external credit rating assigned by international credit agencies of less than "BBB". A similar treatment is adopted for unrecognized contractual commitments, with some adjustments to reflect the more contingent nature of the potential losses.

Olga Lein — Acting Chairman of the Management Board

Tatyana Pavlycheva — Member of the Management Board / Head of Accounting, Planning and Control Group / Chief accountant