INTESA SANPAOLO BANK ALBANIA SH.A.

Financial Statements as at and for the year ended

31 December 2018

(with independent auditors' report thereon)

Contents

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Independent Auditors' Report

To the Shareholders of Intesa Sanpaolo Bank Albania Sh.a

Opinion

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

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2018, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

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

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

Other Information

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

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

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

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

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

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

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

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

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

Fatos Beqja
Statutory Auditor

KPMG Albania Shpk
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Twin Towers Building I, floor 13
Tirana, Albania

Tirana, 04 March 2019

Intesa Sanpaolo Bank Albania Sh.a.

Statement of financial position

(in thousands of Lek)

	Notes	31 December 2018	31 December 2017 Restated*
Assets			
Cash and cash equivalents	11	35,290,306	35,615,020
Loans and advances to banks	12	20,253,667	21,952,883
Investment securities	13	63,727,118	59,348,439
Loans and advances to customers	14	43,928,731	52,234,239
Non-current assets held for sale	15	1,132,672	610,826
Current tax assets		551,650	423,262
Property and equipment	16	2,190,495	2,185,212
Intangible assets	17	494,336	592,502
Investment property	18	545,556	575,318
Deferred tax assets	22	568,492	198,604
Inventory and other assets	19	2,666,634	6,188,449
Total Assets		**171,349,657**	**179,924,754**
Liabilities			
Due to banks	20	2,762,419	7,389,961
Due to customers	21	145,483,303	147,108,177
Deferred tax liabilities	22	138,439	148,408
Provisions	23	1,234,359	1,230,811
Other liabilities	24	1,452,227	1,664,373
Total Liabilities		**151,070,747**	**157,541,730**
Equity			
Share capital	25	5,562,518	5,562,518
Share premium	25	1,383,880	1,383,880
Reserves	26	6,031,724	6,185,491
Retained earnings		7,300,788	9,251,135
Total Equity		**20,278,910**	**22,383,024**
Total Liabilities and Equity		**171,349,657**	**179,924,754**

*See Note 7.

The notes on pages 6 to 73 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

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

	Notes	2018	2017 Restated*
Interest income		4,513,522	4,303,827
Interest expense		(819,303)	(538,258)
Net interest income	27	**3,694,219**	**3,765,569**
Fee and commission income		1,112,574	972,729
Fee and commission expense		(327,280)	(254,004)
Net fee and commission income	28	**785,294**	**718,725**
Other income	29	104,276	360,373
Other operating expenses, net	30	(44,754)	(271,841)
Operating income		**4,539,035**	**4,572,826**
Net impairment on financial assets	9(a)	(227,691)	8,054
Net impairment loss on off-balance sheet	23	21,182	(1,437)
Write down of inventory	19	(80,583)	(190,287)
Personnel expenses	31	(1,389,366)	(1,154,406)
Operating lease expenses	35	(257,610)	(202,282)
Depreciation and amortization	16,17,18	(381,086)	(315,751)
Impairment of investment property	18	(29,762)	(129,773)
Amortization of leasehold improvements	19	(26,271)	(7,863)
Other administrative expenses	32	(1,323,974)	(733,227)
Provisions for risk and expenses	23	(30,353)	(50,928)
Total expenses		**(3,725,514)**	**(2,777,900)**
Net income before taxes		**813,521**	**1,794,926**
Income tax credit/(expense)	33	30,640	(278,441)
Profit for the year		**844,161**	**1,516,485**
Other comprehensive income			
Items that are or may be reclassified subsequently to profit or loss			
Change in fair value of investment securities at FVOCI		(181,720)	-
Related tax		27,953	-
Change in fair value of investment securities Available-for-Sale		-	64,441
Related tax		-	(9,598)
Items that will not be reclassified to profit or loss			
Change in revaluation of functional properties		-	912,271
Related tax		-	(136,840)
Other comprehensive income for the year, net of tax		**(153,767)**	**830,274**
Total comprehensive income for the year, net of tax		**690,394**	**2,346,759**

*See Note 7.

The notes on pages 6 to 73 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

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

	Share capital	Share premium	Legal and regulatory reserves	Fair value reserve	Revaluation reserve	Other capital reserve	Merger Reserve	Retained earnings	Total
Balance at 1 January 2017	**5,562,518**	**1,383,880**	**1,825,623**	**1,643**	**-**	**714,555**	**-**	**10,017,655**	**19,505,874**
Profit for the year, restated*	-	-	-	-	-	-	-	1,516,485	**1,516,485**
Other comprehensive income									**-**
Change in fair value of debt investment AFS, net of income tax, restated*	-	-	-	54,843	-	-	-	-	**54,843**
Revaluation of Functional Properties, net of tax	-	-	-		775,431	-	-	-	**775,431**
Total comprehensive income for the year	**-**	**-**	**-**	**54,843**	**775,431**	**-**	**-**	**1,516,485**	**2,346,759**
Transaction with owners, recorded directly in equity									
Dividends to equity holders	-			-		-		(2,283,005)	**(2,283,005)**
Merger reserve arising on acquisition of Veneto Banka	-	-	-	-	-	-	2,813,396	-	**2,813,396**
Total contributions by and distribution to owners	**-**	**-**	**-**	**-**	**-**	**-**	**2,813,396**	**(2,283,005)**	**530,391**
Balance at 31 December 2017 as restated	**5,562,518**	**1,383,880**	**1,825,623**	**56,486**	**775,431**	**714,555**	**2,813,396**	**9,251,135**	**22,383,024**

*See Note 7.

The notes on pages 6 to 73 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.

Statement of changes in equity (continued)
For the year ended 31 December 2018
(in thousands of Lek)

	Share capital	Share premium	Legal and regulatory reserves	Fair value reserve	Revaluation reserve	Other capital reserve	Merger Reserve	Retained earnings	Total
Balance at 31 December 2017, as previously reported	**5,562,518**	**1,383,880**	**1,825,623**	**56,030**	**775,431**	**714,555**	**-**	**9,391,405**	**19,709,442**
Restatement due to merger*	-	-	-	456	-	-	2,813,396	(140,270)	**2,673,582**
Balance at 31 December 2017, as restated*	**5,562,518**	**1,383,880**	**1,825,623**	**56,486**	**775,431**	**714,555**	**2,813,396**	**9,251,135**	**22,383,024**
Adjustment on initial application of IFRS 9, net of tax (see note 10 (c))	-	-	-	-	-	-	-	(1,137,753)	**(1,137,753)**
Restated balance at 1 January 2018	**5,562,518**	**1,383,880**	**1,825,623**	**56,486**	**775,431**	**714,555**	**2,813,396**	**8,113,382**	**21,245,271**
Profit for the year	-	-	-	-	-	-	-	844,161	**844,161**
Other comprehensive income									**-**
Change in fair value of debt investment at FVOCI, net of income tax	-	-	-	(153,767)	-	-	-	-	**(153,767)**
Revaluation of Functional Properties, net of tax	-	-	-	-	-	-	-	-	**-**
Total comprehensive income for the year	**-**	**-**	**-**	**(153,767)**	**-**	**-**	**-**	**844,161**	**690,394**
Transaction with owners, recorded directly in equity									
Dividends to equity holders	-	-	-	-		-	-	(1,656,755)	**(1,656,755)**
Total contributions by and distribution to owners	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(1,656,755)**	**(1,656,755)**
Balance at 31 December 2018	**5,562,518**	**1,383,880**	**1,825,623**	**(97,281)**	**775,431**	**714,555**	**2,813,396**	**7,300,788**	**20,278,910**

*See Note 7.

The notes on pages 6 to 73 are an integral part of these financial statements.

Intesa Sanpaolo Bank Albania Sh.a.
Statement of cash flows
For the year ended 31 December
(in thousands of Lek)

	2018	2017 Restated*
Net profit for the year	**844,161**	**1,516,485**
Adjustments for:		
Depreciation and amortization	381,086	299,353
Merger reserve	-	2,813,396
Impairment loss on property and equipment	10,030	-
Changes in investment property	-	(721,489)
Impairment of investment property	29,762	146,171
Disposal of property and equipment and intangibles	59,581	1,811
Net impairment charge/(reversal) on loans and advances to customers	227,691	(8,054)
Write down of inventory	80,583	190,287
Net interest income	(3,694,219)	(3,765,569)
Net impairment (reversal)/charge on off-balance sheet items	(21,182)	1,437
Tax (credit)/expense	(30,640)	278,441
Changes in		
Loans and advances to banks	1,625,638	(4,845,915)
Loans and advances to customers	7,336,180	(9,107,129)
Due to banks	(4,627,444)	4,504,728
Due to customers	(1,626,839)	21,205,776
Non-current assets held for sale	(521,846)	(610,826)
Inventory and other assets	3,312,844	(4,019,613)
Other liabilities and provisions	(239,940)	1,756,804
Deferred tax asset	(80,929)	(8,724)
Deferred tax liability	209,317	66,897
Interest received	3,895,046	3,726,923
Interest paid	(817,436)	(610,077)
Income taxes paid	(289,081)	(476,786)
Net cash from operating activities	**6,062,363**	**12,334,327**
Cash flows from investing activities		
Acquisition of property and equipment	(217,436)	(240,323)
Acquisition of intangible assets	(140,378)	(162,139)
Net acquisitions of investments securities	(4,372,508)	(1,303,037)
Net cash used in investing activities	**(4,730,322)**	**(1,705,499)**
Cash flows from financing activities		
Dividend paid to shareholders	(1,656,755)	(2,283,005)
Net cash used in financing activities	**(1,656,755)**	**(2,283,005)**
Net (decrease)/increase in cash and cash equivalents	**(324,714)**	**8,345,823**
Cash and cash equivalents at 1 January	35,615,020	27,269,197
Effect of exchange rate fluctuations on cash and cash equivalents held	-	-
Cash and cash equivalents at 31 December	**35,290,306**	**35,615,020**

*See Note 7.

The notes on pages 6 to 73 are an integral part of these financial statements.

On behalf of the Bank, these financial statements are signed on 04 March 2019 by:

Silvio Pedrazzi
Chief Executive Officer

Julian Cela
Chief Financial Officer

Notes to the financial statements for the year ended 31 December 2018

1. Reporting entity

Intesa Sanpaolo Bank Albania Sh.a, (the “Bank”), is a company domiciled in Albania. The Bank’s registered office is at “Ismail Qemali” street, no.27, and operates through a network of 34 branches and agencies, located in different cities of Albania: Tirana, Durres, Vlora, Elbasan, Fier, Berat, Gjirokastra, Korca, Lushnja, Shkoder, Lezhe, Kavaje (2017: 32 branches and agencies).

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

On October 1rst 2018, the Bank and “Veneto Banka sh.a.” (also known as “VBA”) legally merged by incorporating VBA assets and liabilities into the Bank. Prior to the merger, the Bank and VBA were under common control of Intesa Sanpaolo SpA being the same and only shareholder since 5 December 2017 when Intesa Sanpaolo SpA acquired VBA. The Bank and VBA shareholder approved the terms and conditions of the merger on 18 September 2018.

The Bank had 641 employees as at 31 December 2018 (2017: 576).

2. Basis of accounting

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB). These financial statements were authorized for issue by Management on 31 January 2019 for approval by the Supervisory Board.

This is the first set of Bank’s annual Financial Statements in which IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers* have been applied. Changes to significant accounting policies are described in Note 6.

3. Basis of measurement

The financial statements are prepared on the amortized or historical cost basis except for financial assets at FVOCI (applicable from 1 January 2018), available-for-sale financial assets (applicable before 1 January 2018), investment properties and own used properties, which are stated at fair value.

4. Functional and presentation currency

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

5. Use of estimates and judgments

In preparing these financial statements, management has made judgements, estimates and assumptions that affect the application of the Bank’s accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively.

A. Judgements

Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the financial statements is included in the following notes.

- Applicable to 2018 only:

  -Note 8 (g) (ii): 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 SPPI on the principal amount outstanding.

5. Use of estimates and judgments (continued)

A. Judgements (continued)

-Note 9 (a): establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL.
-Note 8 (a): Management has concluded that Intesa Sanpaolo SpA's acquisition and subsequent transfer of the net assets of Veneto Banka to the Bank represent common control transaction and has restated the comparative amounts from the date after the control was acquired.

B. Assumptions and estimation uncertainties

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ended 31 December 2018 is included in the following notes.

- Applicable to 2018 only:
  - Note 9 (a): impairment of financial instruments: determining inputs into the ECL impairment model, including incorporation of forward-looking information

- Applicable to 2018 and 2017
  - Note 8 (g) (vi): determination of the fair value of financial instruments with significant unobservable inputs
  - Note 8 (f) (ii): recognition of deferred tax assets
  - Note 8 (r): recognition and measurement of contingencies: key assumption about the likelihood and magnitude of an outflow of resources
  - Note 8 (o): net realizable value of inventory: fair value measurement with significant unobservable inputs
  - Note 8 (g) (vii): impairment of financial instruments: key assumptions used in estimating recoverable cash flows

6. Changes in accounting policy

The Bank has initially adopted IFRS 9 (see A) and IFRS 15 (see B) from 1 January 2018. A number of other new standards are also effective from 1 January 2018 but they do not have a material effect on the Bank's financial statements. Due to the transition method chosen by the Bank in applying IFRS 9, comparative information throughout these financial statements has not generally been restated to reflect its requirements. The adoption of IFRS 15 did not impact the timing or amount of fee and commission income from contracts with customers and the related assets and liabilities recognised by the Bank. Accordingly, the impact on the comparative information is limited to new disclosure requirement.

The effect of initially applying these standards is mainly attributed to the following:

- an increase in impairment losses recognised on financial asset (see Note 10 (c));
- additional disclosures related to IFRS 9 (see Note 9 (a)).
- additional disclosures related to IFRS 15 (see Note 28)

Except for the changes below, the Bank has consistently applied the accounting policies as set out in Note 8 to all periods presented in these financial statements

A. IFRS 9 Financial Instruments

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement. The requirements of IFRS 9 represent a significant change from IAS 39. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

Additionally, the Bank has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures about 2018, but have not been applied to the comparative information. The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarised below. The full impact of adopting the standard is set out in Note 10 (c).

6. Changes in accounting policy (continued)

A. IFRS 9 Financial Instruments

Classification of financial assets and financial 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 previous IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. For an explanation of how the Bank classifies financial assets under IFRS 9, see note 8 (g) (ii). IFRS 9 largley retains the existing requirements in IAS 39 for the classification of financial liabilities. For an explanation of how the Bank classifies financial liabilities under IFRS 9, see note note 8 (g) (ii).

Impairment of financial assets

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

Under IFRS 9, credit losses are recognized earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see note 8 (g) (vii).

Transition

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

Comparative periods generally have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

- The determination of the business model within which a financial asset is held.
- 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.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, see Note 8 (g).

B. IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.

The Bank initially applied IFRS 15 on 1 January 2018 retrospectively in accordance with IAS 8 without any practical expedients. The timing or amount of the Bank’s fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15. The impact of IFRS 15 was limited to the new disclosure requirements (see Note 28).

7. Restatement of comparative information

As further explained in note 1 of the financial statements on 1st October 2018 the Bank merged Veneto Banka sh.a. Intesa Sanpaolo S.p.A. was the ultimate owner of both banks. The transaction represented a business combination involving entities under common control and as such it was exempt from the accounting treatment prescribed in IFRS 3 Business Combinations. As explained in Note 5, the Bank has restated its comparative financial statements to include the assets, liabilities, results of operations and cash flows of Veneto Banka sh.a from 5 December 2017 (the date of acquisition of Veneto Bank by Intesa Sanpaolo SpA).The effects on the Bank's financial position, financial performance and cash flows are set out in the following tables:

Statement of Financial Position for the year ending 31 December 2017

	As previously reported	**Merger of Veneto Banka sh.a**	**Elimination of intercompany balances**	**Restated**
Assets				
Cash and cash equivalents	22,877,864	14,667,497	(1,930,341)	35,615,020
Loans and advances to banks	20,171,066	1,781,817	-	21,952,883
Investment securities	58,533,127	815,312	-	59,348,439
Loans and advances to customers	46,557,253	5,676,986	-	52,234,239
Non-current assets held for sale	-	610,826	-	610,826
Current tax assets	389,883	33,379	-	423,262
Property and equipment	2,141,765	43,447	-	2,185,212
Intangible assets	528,695	63,807	-	592,502
Investment property	575,318	-	-	575,318
Deferred tax assets	174,247	24,357	-	198,604
Inventory and other assets	2,296,937	3,891,512	-	6,188,449
Total Assets	**154,246,155**	**27,608,940**	**(1,930,341)**	**179,924,754**
Liabilities				-
Deposit from banks	5,168,783	4,151,519	(1,930,341)	7,389,961
Deposit from customers	127,711,325	19,396,852	-	147,108,177
Current tax liabilities	-	-	-	-
Deferred tax liabilities	148,327	81	-	148,408
Provisions	468,695	762,116	-	1,230,811
Other liabilities	1,039,583	624,790	-	1,664,373
Total Liabilities	**134,536,713**	**24,935,358**	**(1,930,341)**	**157,541,730**
Equity				
Share capital	5,562,518	-	-	5,562,518
Share premium	1,383,880	-	-	1,383,880
Reserves	3,371,639	456	-	3,372,095
Merger reserve*	-	2,813,396	-	2,813,396
Retained earnings	9,391,405	(140,270)	-	9,251,135
Total Equity	**19,709,442**	**2,673,582**	**-**	**22,383,024**
Total Liabilities and Equity	**154,246,155**	**27,608,940**	**(1,930,341)**	**179,924,754**

*The Bank did not pay anything to acquire the net assets of Veneto and that the merger reserve has been used to reflect the contribution by owner equal to the net assets transferred.

7. Restatement of comparative information (continued)

Statement of Profit or Loss and Other Comprehensive Income
For the year ended 31 December 2017

	As previously reported	**Intercompany transactions**	**Veneto Banka sh.a**	**Restated**
Interest income	4,280,758	(2,647)	25,716	4,303,827
Interest expense	(522,348)	2,647	(18,557)	(538,258)
Net interest income	**3,758,410**	**-**	**7,159**	**3,765,569**
Fee and commission income	953,439	-	19,290	972,729
Fee and commission expense	(250,720)	-	(3,284)	(254,004)
Net fee and commission income	**702,719**	**-**	**16,006**	**718,725**
Other income	417,522	-	(57,149)	360,373
Other operating expenses, net	(270,161)	-	(1,680)	(271,841)
Operating income	**4,608,490**	-	**(35,664)**	**4,572,826**
Net impairment reversal on financial assets	46,003	-	(37,949)	8,054
Net impairment loss on off-balance sheet	(1,437)	-	-	(1,437)
Write down of inventory	(190,287)	-	-	(190,287)
Personnel expenses	(1,135,023)	-	(19,383)	(1,154,406)
Operating lease expenses	(159,658)	-	(42,624)	(202,282)
Depreciation and amortization	(311,101)	-	(4,650)	(315,751)
Impairment of investment property	(129,773)	-	-	(129,773)
Amortization of leasehold improvements	(7,863)	-	-	(7,863)
Other administration expenses	(733,227)	-	-	(733,227)
Provisions for risk and expenses	(50,928)	-	-	(50,928)
Total expenses	**(2,673,294)**	-	**(104,606)**	**(2,777,900)**
Net income before taxes	**1,935,196**	-	**(140,270)**	**1,794,926**
Income tax expense	(278,441)	-	-	(278,441)
Profit for the year	**1,656,755**	-	**(140,270)**	**1,516,485**
Other comprehensive income				
Items that are or may be reclassified subsequently to profit or loss				
Change in fair value of investment securities AFS, net of income tax	63,985	-	456	64,441
Related tax	(9,598)	-	-	(9,598)
Items that will not be reclassified to profit or loss				
Change in revaluation of functional properties	912,271	-	-	912,271
Related tax	(136,840)	-	-	(136,840)
Other comprehensive income for the year, net of tax	**829,818**	**-**	**456**	**830,274**
Total comprehensive income for the year, net of tax	**2,486,573**	**-**	**(139,814)**	**2,346,759**

7. Restatement of comparative information (continued)

Statement of Cash Flows
For the year ending 31 December 2017

	As previously reported	Veneto Banka sh.a	Restated
Net profit for the year	**1,656,755**	**(140,270)**	**1,516,485**
Adjustments for:			
Depreciation and amortization	294,703	4,650	299,353
Merger reserve	-	2,813,396	2,813,396
Changes in investment property	(721,489)	-	(721,489)
Impairment of investment property	146,171	-	146,171
Disposal of property and equipment	72,784	(70,973)	1,811
Net impairment reversal on loans and advances to customers	(46,003)	37,949	(8,054)
Write down of inventory	190,287		190,287
Net interest income	(3,758,410)	(7,159)	(3,765,569)
Net impairment loss on off-balance sheet items	1,437	-	1,437
Tax expense	278,441	-	278,441
Changes in			
Loans and advances to banks	(3,064,098)	(1,781,817)	(4,845,915)
Loans and advances to customers	(3,392,194)	(5,714,935)	(9,107,129)
Due to banks		(610,826)	(610,826)
Due to customers	2,283,550	2,221,178	4,504,728
Non-current assets held for sale	1,808,924	19,396,852	21,205,776
Inventory and other assets	(94,722)	(3,924,891)	(4,019,613)
Other liabilities and provisions	369,898	1,386,906	1,756,804
Deferred tax asset	15,632	(24,356)	(8,724)
Deferred tax liability	66,897	-	66,897
Interest received	3,703,854	23,069	3,726,923
Interest paid	(594,167)	(15,910)	(610,077)
Income taxes paid	(476,786)	-	(476,786)
Net cash from operating activities	**(1,258,536)**	**13,592,863**	**12,334,327**
Cash flows from investing activities			
Acquisition of property and equipment	(232,001)	(8,322)	(240,323)
Acquisition of intangible assets	(129,530)	(32,609)	(162,139)
Net acquisitions of investments securities	(488,261)	(814,776)	(1,303,037)
Net cash used in investing activities	**(849,792)**	**(855,707)**	**(1,705,499)**
Cash flows from financing activities			
Dividends paid to shareholders	(2,283,005)	-	(2,283,005)
Net cash used in financing activities	**(2,283,005)**	**-**	**(2,283,005)**
Net increase in cash and cash equivalents	**(4,391,333)**	**12,737,156**	**8,345,823**
Cash and cash equivalents at 1 January	27,269,197		27,269,197
Cash and cash equivalents at 31 December	**22,877,864**	**12,737,156**	**35,615,020**

8. Significant accounting policies

The accounting policies set out below have been consistently applied to all periods presented in these financial statements by the Bank, except for the changes explained in Note 6.

(a) Transfer of control of interest in entities under common control

In the absence of specific guidance, entities involved in common control transactions should develop an appropriate accounting policy, to be applied consistently, using the hierarchy described in IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Management has elected to account for transfers of control of interests in entities that are under the control of the shareholder that ultimately controls the Bank by using book value accounting. The assets and liabilities acquired are recognised at the carrying amounts recognised previously in the financial statements of the acquired entity. The financial statements reflect the results of the combining entities for all periods presented for which the entities were under the transferor's common control, irrespective of when the legal combination takes place, resulting in a restatement of the comparative figures in cases where common control occurred prior to the start of the current reporting period.

(b) Foreign currency

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

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

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

(c) Interest

Policy applicable from 1 January 2018

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 purchased or originated credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not ECL. For purchased or originated credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.
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 financial liability

Amortised cost and gross carrying amount

The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance (or impairment allowance before 1 January 2018). The 'gross carrying amount of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

8. Significant accounting policies (continued)

(c) Interest (continued)

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. 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. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest.

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.

For information on when financial assets are credit-impaired, see Note 8(g)(vii).

Policy applicable before 1 January 2018

Interest income and expense were recognised in profit or loss using the effective interest method. The effective interest rate was the rate that exactly discounted the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimated future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

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

(d) Fees and commissions

Fees, commission income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate (see 8 (c)).

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

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

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

8. Significant accounting policies (continued)

(e) Leases

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

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

(f) Income Tax

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

(i) Current Tax

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

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

(ii) Deferred Tax

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

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

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

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

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

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

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities

(i) Recognition and initial measurement

The Bank initially recognizes loans and advances, deposits and debt securities on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are initially recognized on the trade date on which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit and loss, transaction costs that are directly attributable to its acquisition or issue.

(ii) Classification

Financial Assets-Policy applicable from 1 January 2018

On initial recognition, the Bank classified a financial asset as measured at amortised cost , 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;

- the contractual terms of the financial asset give rise on specified dates to cash flows that are “solely payments of principal and interest” (SPPI).

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;

- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

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.

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(ii) Classification (continued)

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 its strategy for 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);

-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 stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading 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 of 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, as well as profit margin.

In assessing whether the contractual cash flows are SPPI, 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 loans);

- and features that modify consideration of the time value of money (e.g. periodical reset of interest rates).

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(ii) Classification (continued)

Reclassifications

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.

Financial Assets-Policy applicable before 1 January 2018

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

- Loans and advances;
- Held-to-maturity; and
- available for sale

See notes 8 (i), 8 (j)(i), and 8 (j)(ii).

Financial liabilities

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

See notes 8 (q).

(iii) De-recognition

Financial Assets

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

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

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

In transactions in which the Bank neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, 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 asset

Financial liabilities

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

(iv) Modification of financial assets and financial liabilities

Policy applicable from 1 January 2018

Financial assets

If the terms of a financial asset are modified, then the Bank evaluates whether the cash flows of the modified asset are substantially different.

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(iv) Modification of financial assets and financial liabilities (continued)

If the cash flows are substantially different, 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 (see (iii)) and a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

– fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and

– other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. If the Bank plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place (see below for write-off policy). This approach impacts the result of the quantitative evaluation and means that the derecognition criteria are not usually met in such cases.

If the modification of a financial asset measured at amortised cost or FVOCI does not result in derecognition of the financial asset, then the Bank first recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification.

Any costs or fees incurred and fees received as part of the modification adjust the gross 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 (see 8.g.(vii)), then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income calculated using the effective interest rate method (see 8 (c))

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 derecognised and consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument

Policy applicable before 1 January 2018

Financial assets

If the terms of a financial asset were modified, then the Bank evaluated whether the cash flows of the modified asset were substantially different. If the cash flows were substantially different, then the contractual rights to cash flows from the original financial asset were deemed to have expired. In this case, the original financial asset was derecognised (see 8.(g).(iii)) and a new financial asset was recognised at fair value
If the terms of a financial asset were modified because of financial difficulties of the borrower and the asset was not derecognised, then impairment of the asset was measured using the pre-modification interest rate (see 8.(g).(vii)).

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(iv) Modification of financial assets and financial liabilities (continued)

Policy applicable before 1 January 2018 (continued)

Financial liabilities

The Bank derecognised a financial liability when its terms were modified and the cash flows of the modified liability were substantially different. In this case, a new financial liability based on the modified terms was recognised at fair value. The difference between the carrying amount of the financial liability extinguished and consideration paid was recognised in profit or loss. Consideration paid included non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability

If the modification of a financial liability was not accounted for as derecognition, then any costs and fees incurred were recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument

(v) Off-setting

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

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

(vi) Fair value measurement

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

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

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

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

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

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

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(vii) Impairment

Policy applicable from 1 January 2018

The Bank recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments;
- financial guarantee contracts issued; and
- loan commitments issued.

The Bank measures loss 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 on which credit risk has not increased significantly since their initial recognition.

The Bank considers a debt investment security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of ‘investment grade’. The Bank does not apply the low credit risk exemption to any other financial instruments.

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. Financial instruments for which a 12-month ECL is recognised are referred to as ‘Stage 1 financial instruments’.

Life-time ECL are the ECL that result from all possible default events over the expected life of the financial instrument. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as ‘Stage 2 financial instruments’.

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 9 (a).

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 one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued)

(vii) Impairment (continued)

Credit-impaired financial assets (continued)
Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

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 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.

Presentation of allowance for ECL in the statement of financial position
Loss allowances for ECL are presented in the 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 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-off
Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. 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. This assessment is carried out at the individual asset level. Recoveries of amounts previously written off are included in 'impairment losses on financial instruments' in the statement of profit or loss and OCI.

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.

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued

(vii) Impairment (continued)

Policy applicable before 1 January 2018

Objective evidence of impairment

At each reporting date, the Bank assessed whether there was objective evidence that financial assets not carried at FVTPL were impaired. A financial asset or a group of financial assets was ‘impaired’ when objective evidence demonstrated that a loss event had occurred after the initial recognition of the asset(s) and that the loss event had an impact on the future cash flows of the asset(s) that could be estimated reliably.

Objective evidence that financial assets were impaired included:

i. significant financial difficulty of a borrower or issuer;
ii. default or delinquency by a borrower;
iii. the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
iv. indications that a borrower or issuer would enter bankruptcy;
v. the disappearance of an active market for a security; or
vi. observable data relating to a group of assets, such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlated with defaults in the group.

A loan that was renegotiated due to a deterioration in the borrower’s condition was usually considered to be impaired unless there was evidence that the risk of not receiving contractual cash flows had reduced significantly and there were no other indicators of impairment.

Individual or collective assessment

An individual measurement of impairment was based on management’s best estimate of the present value of the cash flows that were expected to be received. In estimating these cash flows, management made judgements about a debtor’s financial situation and the net realisable value of any underlying collateral. Each impaired asset was assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable were independently approved by the Credit Risk function.

The collective allowance for groups of homogeneous loans was established using statistical methods such as roll rate methodology or, for small portfolios with insufficient information, a formula approach based on historical loss rate experience. The roll rate methodology used statistical analysis of historical data on delinquency to estimate the amount of loss.

The IBNR allowance covered credit losses inherent in portfolios of loans and advances, and held-to-maturity investment securities with similar credit risk characteristics when there was objective evidence to suggest that they contained impaired items but the individual impaired items could not yet be identified.

In assessing the need for collective loss allowance, management considered factors such as credit quality, portfolio size, concentrations and economic factors. To estimate the required allowance, assumptions were made to define how inherent losses were modelled and to determine the required input parameters, based on historical experience and current economic conditions.

The accuracy of the allowance depended on the model assumptions and parameters used in determining the collective allowance. Loans that were subject to a collective IBNR provision were not considered impaired.

Measurement of impairment

Impairment losses on assets measured at amortised cost were calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset’s original effective interest rate. Impairment losses on available-for-sale assets were calculated as the difference between the carrying amount and the fair value.

8. Significant accounting policies (continued)

(g) Financial assets and financial liabilities (continued

(vii) Impairment (continued)

Policy applicable before 1 January 2018 (continued)

Reversal of impairment

For assets measured at amortised cost: If an event occurring after the impairment was recognised caused the amount of impairment loss to decrease, then the decrease in impairment loss was reversed through profit or loss.

For available-for-sale debt security: If, in a subsequent period, the fair value of an impaired debt security increased and the increase could be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss was reversed through profit or loss; otherwise, any increase in fair value was recognised through OCI.

Any subsequent recovery in the fair value of an impaired available-for-sale equity security was always recognised in OCI.

Presentation

Impairment losses were recognised in profit or loss and reflected in an allowance account against loans and receivables or held-to-maturity investment securities. Interest on the impaired assets continued to be recognised through the unwinding of the discount.

Impairment losses on available-for-sale investment securities were recognised by reclassifying the losses accumulated in the fair value reserve in equity to profit or loss. The cumulative loss that was reclassified from equity to profit or loss was the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment attributable to the application of the effective interest method were reflected as a component of interest income.

Write-off

The Bank wrote off a loan or an investment debt security, either partially or in full, and any related allowance for impairment losses, when Bank Credit determined that there was no realistic prospect of recovery.

(h) Cash and cash equivalents

‘Cash and cash equivalents’ include notes and coins on hand, balances with banks, unrestricted balances held with central banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments.

Cash and cash equivalents are carried at amortized cost in the statement of financial position.

8. Significant accounting policies (continued)

(i) Loans and advances

Policy applicable from 1 January 2018

Loans and advances captions in the statement of financial position include loans and advances measured at amortised cost. They are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method.

When the Bank purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date (reverse repo or stock borrowing), the arrangement is accounted for as a loan or advance, and the underlying asset is not recognised in the Bank's financial statements.

Policy applicable before 1 January 2018

'Loans and advances' were non-derivative financial assets with fixed or determinable payments that were not quoted in an active market and that the Bank did not intend to sell immediately or in the near term.

Loans and advances to banks were classified as loans and receivables. Loans and advances to customers included those classified as loans and receivables.

Loans and advances were initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

(j) Investment securities

Policy applicable from 1 January 2018

The "investment securities" caption in the statement of financial position includes

-debt investment securities measured at amortised cost (see g (ii)); these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;

-debt securities measured at FVOCI.

For debt securities measured at FVOCI, gains and losses are recognised in OCI, 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 debt security measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

Policy applicable before 1 January 2018

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

i. Held to Maturity

'Held-to-maturity investments' are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity, and which are not designated as at FVTPL or as available-for-sale Held-to-maturity investments are carried at amortised cost using the effective interest method, less any impairment losses (see 8 (g)(vii)). A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale, and would prevent the Bank from classifying investment securities as held-to-maturity for the current and the following two financial years. However, sales in any of the following circumstances would not trigger a reclassification.

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;

8. Significant accounting policies (continued)

(j) Investment securities (continued)

Policy applicable before 1 January 2018 (continued)

- sales or reclassifications after the Bank has collected substantially all of the asset's original principal; and
- sales or reclassifications that are attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated

ii. Available for sale

'Available-for-sale investments' are non-derivative investments that are designated as available-for-sale or are not classified as another category of financial assets. Available-for-sale investments comprise equity securities and debt securities. Unquoted equity securities whose fair value cannot be measured reliably are carried at cost. All other available-for-sale investments are measured at fair value after initial recognition.

Interest income is recognised in profit or loss using the effective interest method. Foreign exchange gains or losses on available-for-sale debt security investments are recognised in profit or loss. Impairment losses are recognised in profit or loss.

Other fair value changes, other than impairment losses, are recognised in OCI and presented in the fair value reserve within equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to profit or loss
A non-derivative financial asset may be reclassified from the available-for-sale category to the loans and receivables category if it would otherwise have met the definition of loans and receivables and if the Bank has the intention and ability to hold that financial asset for the foreseeable future or until maturity.

(k) Non-current assets held for sale

Non-current assets for which a disposal process has commenced are classified as held-for-sale if it is highly probable that they will be recovered primarily through sale rather than through continuing use. Such assets are generally measured at the lower of their carrying amount and fair value less costs to sell.

(l) Property and equipment

(i) Recognition and measurement

Equipment are measured at cost less accumulated depreciation and any accumulated impairment losses. Property are measured at revalued amounts, being the fair value at the date of revaluation less accumulated depreciation and any accumulated impairment losses (see Note 16). If significant parts of an item of property or equipment have different useful lives, then they are accounted for as separate items (major components) of property and equipment. Any gain or loss on disposal of an item of property and equipment is recognised within other income in profit or loss.

(ii) Subsequent costs

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

(iii) Depreciation

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

	2018	**2017**
• Buildings	33 years	33 years
• IT and Electrical Equipment	4 to 8 years	4 to 8 years
• Furniture	3 to 10 years	3 to 10 years
• Other non-electrical assets	5 years	5 years

8. Significant accounting policies (continued)

(m) Intangible assets

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

	2018	**2017**
• Software	5 years	5 years
• Licenses and trademarks	10 years	10 years

(n) Investment property

Investment property is initially measured at cost and subsequently at fair value, with any change therein recognised in profit or loss within other income. Any gain or loss on disposal of investment property (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in profit or loss.

When the use of a property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

(o) Inventory

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

(p) Impairment of non-financial assets

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

(q) Deposits

Deposits are the Bank's sources of debt funding.

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

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

8. Significant accounting policies (continued)

(r) Provisions

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

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

A provision for restructuring is recognised when the Bank has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

(s) 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. Subsequently, they are measured as follows:

-from 1 January 2018: at the higher of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15.

-before 1 January 2018: at the higher of the amount representing the initial fair value amortised over the life of the guarantee or the commitment and the present value of any expected payment to settle the liability when a payment under the contract has become probable.

For other loan commitments:

- from 1 January 2018: the Bank recognises a loss allowance

- before 1 January 2018: the Bank recognises a provision in accordance with IAS 37 if the contract was considered to be onerous.

Liabilities arising from financial guarantees and loan commitments are included within provisions.

(t) Employee benefits

(i) Defined contribution plans

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

(ii) Short-term benefits

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

8. Significant accounting policies (continued)

(u) New standards and interpretation not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2018. However, the Bank has not early applied the following new or amended standards in preparing these financial statements.

Of those standards that are not yet effective, IFRS 16 is expected to have a significant impact on the Bank's financial statements in the period of initial application.

IFRS 16 – Leases

The Bank is required to adopt IFRS 16 Leases from 1 January 2019. The Bank has assessed the estimated impact that the initial application of IFRS 16 will have on its financial statements, as described below. The actual impact of adopting the standard on 1 January 2019 may change because the Bank has not finalised the testing and assessment of its respective internal controls and the new accounting policies are subject to change until the Bank presents its first financial statements that include the date of initial application.

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. 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.

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

The Bank has completed an initial assessment of the potential impact on its financial statements but has not yet completed its detailed assessment.

The Bank will recognise new assets and liabilities for its operating leases of branch and office premises and for rent contracts of the vehicles. Based on the Parent company approach the Bank has excluded from treatment of IFRS 16 contract with total liability amount less than Euro 5,000 and with remaining maturity less than 12 months.

As at 31 December 2018, the Bank future minimum lease payments under non-cancellable operating leases amounted to Lek 369,362 thousand or EUR equivalent 2,990 thousand, which the Bank estimates it will recognize as lease liabilities.

Transition

The Bank plans to apply IFRS 16 initially on 1 January 2019, using a modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognized as an adjustment to the opening balances.

9. Financial Risk Management

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

a. credit risk
b. liquidity risk
c. market risk
d. operational risk

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

Risk management framework

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

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

(a) Credit Risk

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

(i) Management of credit risk

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

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

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(i) Management of credit risk (continued)

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

  According to the Bank's methodology, all exposures are classified between Performing (including Stage 1 and Stage 2) and Non- Performing exposures (Stage 3 - including Past Due, Unlikely to Pay and Doubtful). The bank classifies the performing portfolio in two clusters Stage 1 and Stage 2 based on a set of rules harmonized with the guidelines of Intesa Sanpaolo Group, driven by the signs of deterioration of the exposure as per below specifications:

Stage 1	Stage 2	Stage 3
• Performing exposures without days past due • Performing exposures with more than 30 days past due under materiality threshold (set equal to 5%)	• Performing exposures with more than 30 days past due over materiality threshold (set equal to 5%) • Forborne performing exposures • Performing exposures showing Early Warning signals (orange, red and light blue) and PCM.	• Exposures with more than 90 days past due over materiality threshold • Unlikely to Pay • Doubtful

  The Non-Performing portfolio is classified by analyzing the exposures also based on a set of rules harmonized with the guidelines of Intesa Sanpaolo Group. These rules include objective evidence being: breach of contract (such as default or delinquency in interest or principal payments); significant financial difficulty of the borrower; and other significant adverse financial information relating to the customer.

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

(ii) Maximum Exposure to Credit Risk

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

	Gross Maximum Exposure	
	31 December 2018	**31 December 2017**
Cash and cash equivalents (excluding cash on hand)	33,844,583	33,978,809
Loans and advances to banks	20,253,667	21,952,883
Investment securities	63,727,118	59,348,439
Loans and advances to customers	43,928,731	52,234,239
Sundry debtors	443,042	63,800
Total on-balance-sheet risk	**162,197,141**	**167,578,170**
Undrawn credit commitments	4,378,023	6,835,897
Letters of credit	948,692	3,028,421
Guarantees in favor of customers	4,245,210	5,431,354
Total credit related commitments	**9,571,925**	**15,295,672**
Total Credit Risk Exposure	**171,769,066**	**182,873,842**

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(ii) Maximum Exposure to Credit Risk (continued)

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

(iii) Credit Quality by class of financial assets

The following table sets out information about the credit quality of financial assets measured at amortized cost, FVOCI debt investments (2018) and available-for-sale debt assets (2017). Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

Explanation of the terms 'Stage 1', 'Stage 2' and 'Stage 3' is included in Note 8(g)(vii).

31 December 2018	Stage 1	Stage 2	Stage3	Total	31 December 2017
Loans and advances to customers					
Performing	41,106,026	2,347,997	-	**43,454,023**	**50,428,802**
Past Due	-	-	151,825	**151,825**	**212,273**
Unlikely to Pay	-	-	1,149,101	**1,149,101**	**2,728,854**
Doubtful	-	-	1,745,476	**1,745,476**	**1,056,121**
Total	**41,106,026**	**2,347,997**	**3,046,402**	**46,500,425**	**54,426,050**
Loss allowance	**663,165**	**456,354**	**1,452,175**	**2,571,694**	**2,191,811**
Carrying amount	**40,442,861**	**1,891,643**	**1,594,227**	**43,928,731**	**52,234,239**
Loans and advances to banks**					
Performing	35,069,277	3,714,468	-	**38,783,745**	**41,605,679**
Total	**35,069,277**	**3,714,468**	**-**	**38,783,745**	**41,605,679**
Loss allowance	**9,509**	**6,539**	**-**	**16,048**	**-**
Carrying amount	**35,059,768**	**3,707,929**	**-**	**38,767,697**	**41,605,679**
Investment securities at FVOCI (2017: available-for-sale)					
Performing	6,323,591	-	-	**6,323,591**	**10,238,320**
Total	**6,323,591**	**-**	**-**	**6,323,591**	**10,238,320**
Carrying amount	**6,323,591**	**-**	**-**	**6,323,591**	**10,238,320**
Loss allowance*	**4,629**	**-**	**-**	**4,629**	**-**
Investment securities at amortized cost (2017: held-to-maturity)					
Performing	55,566,406	2,110,759	-	**57,677,165**	**49,110,119**
Total	**55,566,406**	**2,110,759**	**-**	**57,677,165**	**49,110,119**
Loss allowance	**265,837**	**7,801**	**-**	**273,638**	**-**
Carrying amount	**55,300,569**	**2,102,958**	**-**	**57,403,527**	**49,110,119**

*Loss allowance for investment securities at FVOCI is recognised in other comprehensive income and not as a contra account to the carrying amount of the financial asset in the statement of financial position (see Note 8 (g) (vii) Presentation of allowance for ECL in the statement of financial position).

**Loans and advances to banks include current accounts with banks, money market placements (see Note 11) and deposits with correspondent banks (see Note 12).

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(iii) Credit Quality by class of financial assets (continued)

The following table sets out information about the overdue status of loans and advances to customers in Stages 1, 2 and 3.

	31 December 2018				31 December 2017
Loans and advances to customers	**Stage 1**	**Stage 2**	**Stage3**	**Total**	**Total**
Up to 30 days in arrears	40,653,651	1,682,259	24,748	**42,360,658**	**48,581,413**
More than 30 days in arrears	452,374	665,738	3,021,655	**4,139,767**	**5,844,637**
Total	**41,106,025**	**2,347,997**	**3,046,403**	**46,500,425**	**54,426,050**

All loans and advances to banks and investment securities fall in the overdue status of less than 30 days in arrears as of 31 December 2018 and 31 December 2017.

The following table sets out the credit quality of debt securities and loans and advances to banks based on Moody's ratings, Staging and IFRS Category:

Investments debt securities

Sovereign	31 December 2018			31 December 2017
	Stage 1	**Stage 2**	**Total**	**Total**
Rate Baa2	**3,574,631**	**2,102,958**	**5,677,589**	**6,235,718**
FOCI	*3,574,631*	-	***3,574,631***	***4,040,863***
AC	-	*2,102,958*	***2,102,958***	***2,194,855***
Rate B1	**57,512,156**	**-**	**57,512,156**	**51,102,109**
FVOCI	2,211,587	-	**2,211,587**	**4,186,845**
AC	55,300,569	-	**55,300,569**	**46,915,264**
	61,086,787	**2,102,958**	**63,189,745**	**57,337,827**

Financial Institutions				
	Stage 1	**Stage 2**	**Total**	**Total**
Rated Aaa	**537,373**	**-**	**537,373**	**2,010,612**
FVOCI	537,373	-	**537,373**	2,010,612
Total carrying amount	**61,624,160**	**2,102,958**	**63,727,118**	**59,348,439**

Loans and advances to Banks

	31 December 2018			31 December 2017
	Stage 1	**Stage 2**	**Total**	**Total**
Rated Aa1	11,672	-	**11,672**	**5,546**
Rated Aa2	24,093	-	**24,093**	**26,285**
Rated Aa3	6,944,439	-	**6,944,439**	**4,363,731**
Rated A1	38,631	-	**38,631**	**65,495**
Rated A2	-	-	**-**	**1,992,705**
Rated A3	4,887,532	17,114	**4,904,646**	**4,386,744**
Rated Baa1	16,464,970	-	**16,464,970**	**14,592,794**
Rated Baa3	4,927,241	3,690,815	**8,618,056**	**11,238,495**
Rated Ba3	1,499,513	-	**1,499,513**	**-**
Rated B1	76,677	-	**76,677**	**-**
Rated B2	185,000	-	**185,000**	**-**
Rated CAA	-	-	**-**	**1,195,573**
Non rated	-	-	**-**	**3,738,311**
	35,059,768	**3,707,929**	**38,767,697**	**41,605,679**

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(iv) Collateral held and other credit enhancements

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

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

The recovery costs are deducted from estimated future cash flows. Collateral, generally, is not held over loans and advances to financial institutions, except when securities are held as part of reverse repurchase and securities borrowing activity. Usually, collateral is not held against investment securities, and no such collateral was held at 31 December 2018 and 2017. Estimates of fair value are based on the value of collateral assessed at the time of borrowing and are updated every three years. An estimate of the undiscounted and discounted fair value of collaterals and other security enhancements held against financial assets is shown below:

	Collateral of Loans and advances to customers 31 December 2018		Collateral of Loans and advances to customers 31 December 2017	
	Undiscounted	**Discounted**	**Undiscounted**	**Discounted**
Against individually impaired				
Property	5,156,673	1,930,937	6,141,972	1,904,992
Debt securities	5,950	-	-	-
Pledges and guarantees	296,532	247	1,330	532
Other	-	-	-	-
Total	**5,459,155**	**1,931,184**	**6,143,302**	**1,905,524**
Net carrying amount		**1,258,002**		**1,551,639**

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

The table below shows the total amount of collaterals for the loans assessed under the category of collectively impaired including all the Stage 3 exposures that are lower than EUR 100 thousand.

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

	Collateral of Loans and advances to customers 31 December 2018		Collateral of Loans and advances to customers 31 December 2017	
Against Collectively Impaired	**Undiscounted**	**Discounted**	**Undiscounted**	**Discounted**
Property	76,090,868	33,216,469	79,670,147	39,319,454
Pledges and guarantees	17,393,858	1,208,001	12,013,428	5,687,801
Cash	1,621,477	1,565,114	1,624,056	1,580,973
Debt securities	2,797,132	24,647	3,259,239	1,106,704
Other	1,646,216	-	-	-
Total	**99,549,551**	**36,014,231**	**96,566,870**	**47,694,932**
Net carrying amount		**42,670,729**		**50,682,600**

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

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(iv) Collateral held and other credit enhancements (continued)

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

(v) Amounts arising from ECL

Inputs, assumptions and techniques used for estimating impairment

See accounting policy in Note 8 (g)(vii).

During 2018, the Bank complied with the "Rules on the measurement of expected credit loss pursuant to standard IFRS 9 (Impairment Policy)" issued by the Group which defines the methodological rules adopted by Intesa Sanpaolo Group on Stage Assignment and on calculation of Expected Credit Loss for the financial assets included in the following accounting categories: Amortised Cost ("AC") and Fair Value Through Other Comprehensive Income ("FVOCI") pursuant to IFRS 9 standard. The main changes introduced, refer to the shift from incurred losses to expected losses, the division of Performing Portfolio into two distinct Stages (Stage 1 for which 12-month expected loss is calculated and Stage 2 for which lifetime expected loss is calculated) and the inclusion of forward looking elements when assessing expected loss. The Non –Performing category (Stage 3 according to IFRS 9 standard) classification remains unchanged, but an Add-On on IAS 39 calculation is introduced when calculating expected loss in order to include forward looking elements. Assessments for impairment are made in accordance with the ISP Individual Assessment Handbook and ISP "Rules on the measurement of expected credit loss pursuant to standard IFRS 9 (Impairment Policy)" according to which the performing category is subject to collective assessment for impairment, while the other three categories (non-performing) can be subject to either individual or collective assessment for impairment. A significance threshold is applied all non performing categories, based on which an individual assessment for impairment is performed for all exposures exceeding the threshold. Assessment on a portfolio basis using the statistical approach for impairment, is applied to the all non performing categories not exceeding the significance threshold.

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).

The Bank uses three criteria for determining whether there has been a significant increase in credit risk:

- quantitative test based on movement in PD, for loans to banks and investment securities only;
- qualitative indicators based on forbearance and early warning signals; and
- a backstop of 30 days past due.

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(v) Amounts arising from ECL (continued)

Inputs, assumptions and techniques used for estimating impairment (continued)
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);
- the borrower is more than 90 days past due 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; or
- it is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to the borrower's inability to pay its credit obligations.

Incorporation of forward-looking information

The Bank incorporates forward-looking information into the measurement of ECL. The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between EBA (European Banking Authority) stress coefficients and credit losses. The Bank considers three economic scenarios: baseline, adverse scenario, as published by EBA, and best scenario, an internal estimate as a symmetrical reflection of adverse scenario toward baseline one.

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 8 (g)(iv).

Measurement of ECL (Expected Credit Losses)

The new framework, IFRS 9 (International Financial Reporting Standard) – Financial Instruments, is based on the estimation of expected losses, different from the incurred losses used under IAS 39. When significant deterioration of the credit quality is recognized, the new concept of Lifetime expected loss is introduced. Lifetime expected loss covers expected loss for the whole IFRS 9 specifies that if the credit risk on a financial instrument has increased significantly since initial recognition, an entity shall measure the loss allowance for that financial instrument at an amount equal to Lifetime expected credit losses and if the credit risk on such instrument has not increased significantly, 12-months expected losses should be calculated instead.

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD.
The Bank employs statistical models to analyse 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 collects performance and default information about its credit risk exposures analysed by by type of product and borrower as well as by credit risk grading. For some portfolios, information purchased from external credit reference agencies is also used.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of loss rates from defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry 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 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 and arising from amortisation. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EADs are potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts.

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(v) Amounts arising from ECL (continued)

Inputs, assumptions and techniques used for estimating impairment (continued)

Measurement of ECL (Expected Credit Losses)
Low Default Portfolio

A new category of financial instruments are considered for impairment purposes under the IFRS 9 rules, called "Low Default Portfolio". It includes securities and loans to banks, and as defined by Parent Company consists of exposures with the following parties:

- Sovereign (Central Banks, Governments, Municipalities, Public Sector Entities);
- Institutions (Banks, and other financial institutions);

Intragroup exposures are exposures with the following parties:

- Parent Company;
- Other ISP subsidiaries.

Intragroup transactions are generally classified as Stage 1 with a 12- months ECL following the staging rules for Low Default Portfolio and intragroup exposures based on parent company driven methodologies including validation. Exposures are classified to Stage 2 based on the significant increase of credit risk criterion measured by Lifetime PD comparison. This criterion for Low Default Portfolio is defined based on the specific rating and residual maturity of exposure. Thresholds are provided by Parent Company.

The criteria used to access whether the debt secuties credit quality deteriorated significantly since origination is Lifetime PDs comparison. The instrument issuer rating (counterparty rating) is used for the Lifetime PD comparison rather than rating of the single instrument (i.e. at the reporting date different instruments or tranches related to the same issuer will be assigned with the rating of the counterparty at a given date). Debt secuties purchased in tranches PD at origination is determined through First In First Out (FIFO) methodology.

Debt secuties include "Low Credit Risk Exemption" based on the assumtion that the credit risk on has not increased significantly since initial recognition if the financial instrument is determined to have low credit risk at the reporting date. Therefore, Investment grade instruments at the reporting date are classified to Stage 1. This exemption is applicable only for instruments belonging to Available For Sale (AFS) portfolio upon the IFRS 9 transition. The following criteria are approved for each stage for Bonds residual maturity of the financial instrument.

Stage 1	Stage 2	Stage 3
• Debt with no significant credit quality deterioration • Investment grade debts	• Debt with significant increase in PD since origination	• Defaulted Debt

For Stage 3 – Defaulted debt the impairment testing process for any individually securities is applied. If the fair value is less than the carrying amount or if the issuer is delinquent in its debtor obligations or defaults on payments as demonstrated by any one of the following events:

1.Default;
2.Bankruptcy proceedings;
3. Delinquency in interest or principal payments.

Where any one of these events occurs, given the gravity and the irreversibility of the confirmed situation, an impairment loss should be recorded directly. If the fair value is not more than 20% less than the carrying amount and no other impairment indicators are found, there is no need to test the securities further for impairment. The impairment test for this stage classification is performed according to the rules defined in the ISP Group accounting policy.

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

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(v) Amounts arising from ECL (continued)

Loss allowances

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, as well as collectively assessed and less significant exposures, and a collective loan loss allowance established for groups of homogeneous assets in respect of expected losses that have not been identified.

The following tables show reconciliations from the opening to the closing balance of the loss allowance by class of financial instrument. Comparative amounts for 2017 represent the allowance account for credit losses and reflect the measurement basis under IAS 39. For loans and advances to banks, investment securities at FVOCI (2017: available-for-sale) and investment securities at amortized cost (2017: held-to-maturity), no allowance for impairment has been recognized as of 31 December 2017 under IAS 39.

Movements in impairment allowance funds for:

Loans and advances to banks	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balances at 1 January 2018	**62,923**	**15,202**	**-**	**78,125**
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Financial Assets that have been derecognised	(8,579)	-	-	**(8,579)**
Net remeasurement of loss allowances	(50,589)	(12,592)	-	**(63,181)**
New financial assets originated or purchased	6,467	4,306	-	**10,773**
Foreign exchange and other movements	(713)	(377)	-	**(1,090)**
Balances at 31 December 2018	**9,509**	**6,539**	**-**	**16,048**

Investment securities at FVOCI	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balances at 1 January 2018	**27,515**	**-**	**-**	**27,515**
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Financial Assets that have been derecognised	(6,028)	-	-	**(6,028)**
Net remeasurement of loss allowances	(16,239)	-	-	**(16,239)**
New financial assets originated or purchased	544	-	-	**544**
Foreign exchange and other Movements	(1,163)	-	-	**(1,163)**
Balances at 31 December 2018	**4,629**	**-**	**-**	**4,629**

Investment securities at amortised cost	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Balances at 1 January 2018	**232,723**	**9,732**	**-**	**242,455**
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Financial Assets that have been derecognised	(70,136)	-	-	**(70,136)**
Net remeasurement of loss allowances	(39,947)	(1,648)	-	**(41,595)**
New financial assets originated or purchased	144,241	-	-	**144,241**
Foreign exchange and other movements	(1,044)	(283)	-	**(1,327)**
Balances at 31 December 2018	**265,837**	**7,801**	**-**	**273,638**

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(v) Amounts arising from ECL (continued)

Loss allowances (continued)

Loans and advances to customers	2018				2017
	Stage 1	Stage 2	Stage 3	Total	Total
Balances at 1 January	**936,079**	**488,406**	**1,665,031**	**3,089,516**	**6,576,805**
Transfer to Stage 1	215,511	(90,834)	(124,677)	**-**	**-**
Transfer to Stage 2	(13,377)	51,953	(38,576)	**-**	**-**
Transfer to Stage 3	(114,700)	(227,616)	342,316	**-**	**-**
Transfer to Non-current assets held for sale	-	-	(151,544)	**(151,544)**	**-**
Net remeasurement of loss allowances	(602,439)	30,816	(245,699)	**(817,322)**	**(3,839,060)**
New financial assets originated or puchased	267,576	220,152	607,485	**1,095,213**	**-**
Write offs	-	-	(513,464)	**(513,464)**	**(662,751)**
Foreign exchange and other movements	(25,485)	(16,523)	(88,697)	**(130,705)**	**116,817**
Balances at 31 December	**663,165**	**456,354**	**1,452,175**	**2,571,694**	**2,191,811**

The following table provides a reconciliation between:

- amounts shown in the above tables reconciling opening and closing balances of loss allowance per class of financial instrument; and
- the 'impairment losses on financial instruments' line item in the statement of profit or loss and other comprehensive income.

	Loans and advances to banks	Loans and advances to customers	Investment securities at FVOCI	Investment securities at amortized cost	Total
Net remeasurement of loss allowance	71,760	817,321	22,267	111,731	1,023,079
New financial assets originated or purchased	(10,773)	(1,095,212)	(544)	(144,241)	(1,250,770)
Balances at 31 December	**60,987**	**(277,891)**	**21,723**	**(32,510)**	**(227,691)**

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(v) Amounts arising from ECL (continued)

Credit-impaired financial assets (2017: impaired financial assets)

See accounting policy in Note 8(g)(vii). Credit-impaired loans and advances are graded Past Due, Unlikely to Pay and Doubtful in the Bank's internal credit risk grading system. The following table sets out a reconciliation of changes in the net carrying amount of credit-impaired (2017: impaired) loans and advances to customers.

	2018	2017
Credit-impaired (2017: impaired) loans and advances to customers at 1 January	1,551,638	3,049,665
Change in allowance for impairment	822,026	46,003
Classified as credit-impaired (2017: impaired) during the year	231,422	136,490
Transferred to not credit-impaired (2017: impaired) during the year	(1,318,288)	(1,805,813)
Recoveries of amounts previously written off	231,244	96,725
Other movements	76,185	28,568
Credit-impaired (2017: impaired) loans and advances to customers at 31 December	**1,594,227**	**1,551,638**

The contractual amount outstanding on financial assets that were written off during the year ended 31 December 2018 and that are still subject to enforcement activity is Lek 304 million.

(vi) Impaired financial assets – Comparative information under IAS 39

	Loans and advances to customers 2017	Loans and advances to banks 2017	Investment securities 2017
Loans with renegotiated terms			
Commercial lending	2,334,628	-	-
Mortgage lending	146,819	-	-
Consumer	43,625	-	-
Impaired amount	1,638,935	-	-
Allowance for impairment	(587,361)	-	-
Net carrying amount	**1,937,711**	**-**	**-**

	Loans and advances to customers 2017	Loans and advances to banks 2017	Investment securities 2017
Neither past due nor impaired			
Performing	50,008,805	21,952,883	59,348,439
Other categories	267,546	-	-
	50,276,351	**21,952,883**	**59,348,439**
Past due but not impaired			
30–90 days	-	-	-
91–180 days	537,452	-	-
181 days+	629,829	-	-
	1,167,281	**-**	**-**
Individually impaired			
Past Due	62,513	-	-
Unlikely to Pay	2,201,187	-	-
Doubtful	718,718	-	-
	2,982,418	**-**	**-**
Allowance for impairment			
Individual	(1,430,779)	-	-
Collective	(761,032)	-	-
Total allowance for impairment	**(2,191,811)**	**-**	**-**
Net carrying amount	**52,234,239**	**21,952,883**	**59,348,439**

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(vi) Impaired financial assets – Comparative information under IAS 39 (continued)

The financial assets in the tables below are gross of impairment allowances for ended as at 31 December 2017:

	Neither past due nor individually impaired	Past due, not individually impaired	Individually Impaired	Total
Cash and cash equivalents (excluding cash on hand)	33,978,809	-	-	**33,978,809**
Loans and advances to banks	21,952,883	-	-	**21,952,883**
Commercial lending	40,880,681	692,605	2,676,738	**44,250,024**
Mortgage lending	6,672,532	386,273	305,318	**7,364,123**
Consumer lending	2,723,138	88,403	362	**2,811,903**
Loans and advances to customers:	50,276,351	1,167,281	2,982,418	**54,426,050**
Listed financial institutions	6,771,662	-	-	**6,771,662**
Unlisted financial institutions	3,466,658	-	-	**3,466,658**
Financial Assets available-forsale:	10,238,320	-	-	**10,238,320**
Listed companies	4,267,587	-	-	**4,267,587**
Unlisted Government securities	44,842,532	-	-	**44,842,532**
Financial Assets held to maturity:	49,110,119	-	-	**49,110,119**
Investment securities	59,348,439	**-**	**-**	**59,348,439**
Total	**165,556,482**	**1,167,281**	**2,982,418**	**169,706,181**

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

	Less than 30 days	31 to 60 days	61 to 90 days	Total
Loans and advances to customers:				
Commercial lending	39,486,063	712,364	682,254	**40,880,681**
Mortgage lending	6,414,251	143,697	114,584	**6,672,532**
Consumer lending	2,632,129	73,921	17,088	**2,723,138**
Total	**48,532,443**	**929,982**	**813,926**	**50,276,351**

31 December 2017	**91 to 180 days**	**more than 180 days**	**Total**
Loans and advances to customers:			
Commercial lending	353,849	338,756	**692,605**
Mortgage lending	147,217	239,056	**386,273**
Consumer lending	36,191	52,212	**88,403**
Total	**537,257**	**630,024**	**1,167,281**

As at 31 December 2017, loans and advances to customers were the only class of financial assets resulting in non-performing categories which are not necessarily subject to individual impairment assessment.

(vii) Write-off policy

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

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(viii) Concentration of Credit Risk

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

	Net Loans and advances to customers	
Concentration by sector	**31 December 2018**	**31 December 2017**
Services	12,996,807	21,197,357
Wholesale	10,311,235	10,375,433
Construction	2,494,865	2,828,622
Manufacturing	5,201,578	5,485,134
Real Estate	726,549	393,289
Other	1,955,755	2,187,905
Corporate	**33,686,789**	**42,467,740**
Mortgage	8,166,442	7,085,187
Consumer	2,075,500	2,681,312
Retail	**10,241,942**	**9,766,499**
Carrying amount	**43,928,731**	**52,234,239**

	Loans and advances to banks	
Concentration by sector	**31 December 2018**	**31 December 2017**
Bank	20,253,667	21,952,883
Carrying amount	**20,253,667**	**21,952,883**

	Investment securities	
Concentration by sector	**31 December 2018**	**31 December 2017**
Sovereign	63,189,745	57,337,827
Bank	-	900,577
Other Financial l Institutions	537,373	1,110,035
Carrying amount	**63,727,118**	**59,348,439**

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

	31 December 2018	**Exposure In %**	**31 December 2017**	**Exposure In %**
Republic of Albania securities	57,511,936	35%	51,102,110	30%
Balances with Bank of Albania	15,330,553	9%	14,326,013	9%
Total direct Albanian Sovereign risk	**72,842,489**	**44%**	**65,428,123**	**39%**
Largest bank	16,466,776	10%	14,548,021	9%
Largest customer	1,426,673	1%	5,395,451	3%
Total largest bank and customer	**17,893,449**	**11%**	**19,943,472**	**12%**
Total on-balance-sheet risk	**90,735,938**	**55%**	**85,371,595**	**51%**

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

9. Financial Risk Management (continued)

(a) Credit Risk (continued)

(ix) Settlement risk

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

The Bank of Albania regulation "On risk management arising from the large exposures of Bank" was revised during 2014 and entered in force in March 2015. The Bank has been within the limits in accordance with Central Bank of Albania regulation up to 20 December 2018.

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

(b) Liquidity Risk

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

(i) Management of liquidity risk

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

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

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

- **Liquidity Coverage Ratio (LCR)** up to 30 days**:** aims to ensure that the Bank maintains an adequate level of unencumbered high-quality liquid assets (HQLA) to meet its short term liquidity needs under liquidity stress scenario (LCR≥100%).
- **Net Stable Funding Ratio (NSFR):** aims to guarantee an adequate liquidity position over a medium/long-term time horizon. It establishes a minimum "acceptable" amount of funding over one year horizon in relation to the needs arising from the liquidity characteristics and the residual maturities of assets and off-balances exposures (NSFR≥100%).

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

9. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

(i) Management of liquidity risk (continued)

In its Liquidity Policy, the Bank projects a LCR indicator of up to 3 months by including the estimated market effect of specific acute liquidity tensions (at bank level) combined with a widespread and general market crisis, based on assumptions provided by the Group's guidelines. (LCR up to 3 months ≥80%).

A similar, but not identical, calculation is used to measure the Bank's compliance with the liquidity limits established by the Bank of Albania, which should be above 20% for all currencies and foreign currencies and above 15% for the local currency.

(ii) Compulsory reserve

On 7 February 2018 Bank of Albania approved the decision no.14 for the change on the Compulsory Reserve requirement. These changes has entered in force during June 2018 and consist of the following:

- Decrease for the obligatory reserve requirement rate for local currency liabilities to 7.5% and 5% (previous rate applied: 10%).
- The new obligatory reserve requirement rate for foreign currency liabilities is 12.5% and 20%. Liabilities in foreign currency up to 50% of the total liabilities have a 12.5% requirement rate and for the part of above 50% of the total liabilities the requirement rate is 20% (previous rate applied: 10 %).
  All the above liquidity ratios are periodically monitored by the Bank with reference to the Group internal limits and guidelines and to the Bank of Albania requirements. During the year 2018, the bank has been within the internal and regulatory limits.

9. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

The table enclosed is only for representative purposes and shows breakdown by the earliest contractual residual maturity of financial assets and liabilities. The classification of securities portfolio in Level 1 is done based on the criteria's defined in ISBA Liquidity Risk policy. The other securities are positioned as per left maturity, since are considered as not liquid assets. Behavioral coefficients of ISP Group are applied for the drawdown percentages for off-balance-sheet categories such as committed credit lines and guarantees. The breakdown considers the cash flows in/out of the Bank for on and off-balance-sheet financial assets and liabilities, according to the earliest contractual residual maturity and not reflecting any retention history assumptions or earlier repayment. The expected cash flows differs from this representation, for example the current account from customers are expected to be stable or to be increased.

31 December 2018	Up to 1 month	1-3 months	3-12 months	1-5 years	> 5 years	Total
Assets (Cash Flow IN)	**94,855,485**	**27,637,888**	**17,092,080**	**49,102,574**	**16,915,330**	**205,603,357**
Net Cash	1,445,991	-	-	-	-	**1,445,991**
Minimum reserve requirements	-	-	-	14,993,585	-	**14,993,585**
Advances to banks	14,170,513	-	-	-	-	**14,170,513**
Investment Securities	55,425,060	8,205,840	2,926,227	7,320,997	3,235,165	**77,113,289**
Other Investment Securities	2,138,932	8,205,840	2,926,227	7,320,997	3,235,165	**23,827,161**
Loans to banks	9,751,918	9,948,950	5,255,447	-	-	**24,956,315**
Loans and advances to customers (*gross performing loans*)	11,923,071	1,277,258	5,984,179	19,466,995	10,445,000	**49,096,503**
31 December 2018						
Liabilities (Cash flow OUT)	**(93,051,713)**	**(11,860,355)**	**(28,674,589)**	**(15,869,827)**	**(710,759)**	**(150,167,243)**
Deposits from banks and customers- Current accounts	(86,635,435)	-	-	-	-	**(86,635,435)**
Current accounts with banks	*(1,526,913)*	-	-	-	-	***(1,526,913)***
Current accounts with customers	*(85,108,522)*	-	-	-	-	***(85,108,522)***
Deposits from banks	(1,244,774)	-	-	-	-	**(1,244,774)**
Deposits from customers- Time deposits	(5,171,504)	(11,860,355)	(28,674,589)	(15,869,827)	(710,759)	**(62,287,034)**
Total gap on-balance sheet	**1,803,772**	**15,777,533**	**(11,582,509)**	**33,232,747**	**16,204,571**	55,436,114
Off-Balance sheet (Cash flow in)	-	-	-	-	-	**-**
Off- Balance sheet (Cash flow out)	(290,009)	-	-	-	-	**(290,009)**
Total gap off-balance sheet	**(290,009)**	**-**	**-**	**-**	**-**	**(290,009)**
Total gap 31 December 2018	**1,513,763**	**15,777,533**	**(11,582,509)**	**33,232,747**	**16,204,571**	**55,146,105**
Cumulated gap 31 December 2018	**1,513,763**	**17,291,296**	**5,708,787**	**38,941,534**	**55,146,105**	**-**

9. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

31 December 2017	Up to 1 month	1-3 months	3-12 months	1-5 years	> 5 years	Total
Assets (Cash Flow IN)	**87,504,687**	**34,629,681**	**17,740,074**	**45,569,775**	**12,821,065**	**198,265,282**
Net Cash	1,636,632	-	-	-	-	**1,636,632**
Minimum reserve requirements	1,781,817	-	-	11,836,076	-	**13,617,893**
Advances to banks	22,586,454	-	-	-	-	**22,586,454**
Investment Securities	43,859,078	12,118,492	1,861,293	4,629,968	294,210	**62,763,041**
Other Investment Securities	93,544	12,118,492	1,861,293	4,629,968	294,210	**18,997,507**
Loans to banks	7,796,720	7,695,960	6,178,135	-	-	**21,670,815**
Loans and advances to customers (gross performing loans)	9,750,442	2,696,737	7,839,353	24,473,763	12,232,645	**56,992,940**
31 December 2017						
Liabilities (Cash flow OUT)	**(91,451,620)**	**(12,779,278)**	**(37,414,966)**	**(12,643,716)**	**(778,549)**	**(155,068,129)**
Deposits from banks and customers- Current accounts	(82,491,310)	-	-	-	-	**(82,491,310)**
Current accounts with banks	*(866,159)*	-	-	-	-	***(866,159)***
Current accounts with customers	*(81,625,151)*	-	-	-	-	***(81,625,151)***
Deposits from banks	(3,239,628)	-	(3,137,667)	-	-	**(6,377,295)**
Deposits from customers- Time deposits	(5,720,682)	(12,779,278)	(34,277,299)	(12,643,716)	(778,549)	**(66,199,524)**
Total gap on-balance sheet	**(3,946,933)**	**21,850,403**	**(19,674,892)**	**32,926,059**	**12,042,516**	**43,197,153**
Off-Balance sheet (Cash flow in)	-	-	-	-	-	**-**
Off- Balance sheet (Cash flow out)	(362,239)	-	-	-	-	**(362,239)**
Total gap off-balance sheet	**(362,239)**	**-**	**-**	**-**	**-**	**(362,239)**
Total gap 31 December 2017	**(4,309,172)**	**21,850,403**	**(19,674,892)**	**32,926,059**	**12,042,516**	**42,834,914**
Cumulated gap 31 December 2017	**(4,309,172)**	**17,541,231**	**(2,133,661)**	**30,792,398**	**42,834,914**	**-**

9. Financial Risk Management (continued)

(b) Liquidity Risk (continued)

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

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

31 December 2018	**1 Month**	**1-3 Months**	**3-12 Months**	**1-5 Years**	**>5 Years**	**Total**
Commitments	4,378,023	-	-	-		**4,378,023**
Guarantees	5,193,902	-	-	-	-	**5,193,902**
31 December 2017						
Commitments	6,835,897	-	-	-	-	**6,835,897**
Guarantees	8,459,775	-	-	-	-	**8,459,775**

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

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

	31 December 2017	**31 December 2017**
Commitments	**4,378,023**	**6,835,897**
Un-drawn credit facilities	4,378,023	6,835,897
Guarantees	**5,193,902**	**8,459,775**
Letters of credit	948,692	3,028,421
Guarantees in favor of customers	4,245,210	5,431,354

c) Market Risk

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

Management of market risks

The Bank holds its securities portfolio in accordance with IFRS 9 as either Held to Collect (HTC) or Held to collect and sell (HTCS). ISBA Security Portfolio is managed by “ISBA Financial Portfolio Policy“ which defines the below specific limits:

- Hold to collect and sell portfolio is not allowed to exceed the 55% of the sum of customer's deposits and shareholder's equity.
- Hold to collect portfolio has the maximum weighted average modified duration, 3 years.
- The security portfolio should obey the specific limits related to type of issuer limits with the following further constraints for HTC Securities: a) country of issuer must be an OECD member and b) issuer rating must be not below A-.
- The overall portfolio must comply with some pre-defined type of issuer limits, which are categorized based on the issuer type, rating and currency.

For all the investments in debt securities, classified as HTCS or HTC, issued by countries considered “at risk” according to ISP Country Risk Guidelines (i.e. countries not belonging to euro area with an internal rating lower than AA-), the approval process and authorization procedure required by the guidelines in force must be followed.

9. Financial Risk Management (continued)

c) Market Risk (continued)

(i) Exposure to Foreign Exchange rate risk

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

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

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

The Bank has been within the limits in accordance with Bank of Albania regulation during the year 2018.

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

9. Financial Risk Management (continued)

(c) Market Risk (continued)

(i) Exposure to Foreign Exchange rate risk (continued)

Assets	**LEK**	**USD**	**EUR**	**OTHER**	**TOTAL**
Cash and cash equivalents	2,643,838	5,779,559	24,667,311	2,199,598	**35,290,306**
Loans and advances to banks	6,691,714	988,279	12,573,674	-	**20,253,667**
Investment securities at FVOCI	219,756	537,373	5,566,462	-	**6,323,591**
Investment securities at amortized cost	52,820,490	2,102,957	2,480,080	-	**57,403,527**
Loans and advances to customers	14,645,471	1,481,711	27,801,487	62	**43,928,731**
Property and equipment's	2,190,495	-	-	-	**2,190,495**
Intangible assets	494,336	-	-	-	**494,336**
Investment Property	545,556	-	-	-	**545,556**
Deferred tax assets	568,492	-	-	-	**568,492**
Current tax assets	551,650	-	-	-	**551,650**
Non-current assets held for sale	77,465	10	1,055,197	-	**1,132,672**
Other assets	1,004,464	51,472	1,610,339	359	**2,666,634**
Total Assets (1)	**82,453,727**	**10,941,361**	**75,754,550**	**2,200,019**	**171,349,657**
Liabilities					
Due to Banks	2,604,904	440	152,086	4,989	**2,762,419**
Due to customers	57,813,318	10,733,389	74,760,890	2,175,706	**145,483,303**
Provisions	524,398	27,663	682,298	-	**1,234,359**
Other liabilities	893,929	25,934	531,041	1,323	**1,452,227**
Deferred tax liabilities	138,439	-	-	-	**138,439**
Net Equity	20,401,906	(411)	(122,585)	-	**20,278,910**
Total Liabilities (2)	**82,376,894**	**10,787,015**	**76,003,730**	**2,182,018**	**171,349,657**
Net FX Position at 31 December 2018 (1)-(2)	**76,833**	**154,346**	**(249,180)**	**18,001**	**-**
Off balance sheet Assets	10,984,123	3,981,142	129,140,115	81,279	**144,186,659**
Off balance sheet Liabilities	11,240,225	4,130,255	128,722,908	93,271	**144,186,659**
Net Off BSH FX Position at 31 December 2018	**(256,102)**	**(149,113)**	**417,207**	**(11,992)**	**-**
Total Net FX Position at 31 December 2018	**(179,269)**	**5,233**	**168,027**	**6,009**	**-**
Balance sheet Assets as at 31 December 2017	76,918,719	12,341,915	88,683,385	1,980,735	**179,924,754**
Balance sheet Liabilities as at 31 December 2017	76,142,554	12,352,369	89,490,263	1,939,568	**179,924,754**
Net Off BSH FX Position at 31 December 2017	**(12,501)**	**65,390**	**(21,866)**	**(31,023)**	**-**
Total Net FX Position at 31 December 2017	**763,664**	**54,936**	**(828,744)**	**10,144**	

9. Financial Risk Management (continued)

c) Market Risk (continued)

(ii) Exposure to Interest Rate risk

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

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

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

The Bank's financial assets and liabilities have mainly variable interest rate or have a re-pricing date of less than one year, except for Albanian Securities and for certain non-Albanian securities investment, which have coupon rates between 1.3 - 6.9% for USD denominated securities (2017: 0.9 - 6.9%) and between 0.4 - 5.8% for EUR denominated securities (2017: 0.5 - 5.8%)

The Bank's Regulation on Interest Rate Risk Management, "ISBA Guidelines on the governance of IRRBB" and "ISBA Rules on the measurement and control of IRRBB" have been approved by the ISBA Board of Directors on May 3rd, 2017.

These documents implements the latest regulatory provisions, recently defined in the Guidelines issued by the Parent Company, based on the EBA regulation (May 2015) on the regulatory framework provided by the Basel Committee on Banking Supervision (BCBS- April 2016) on interest rate risk in the banking book that was effective from January 2018, and the provisions of the Bank of Albania guideline "On managing interest rate risk in the banking book", approved as per decision No. 33, dated 30 April 2013. Interest rate risk generated by the Bank's assets and liabilities, as measured through shift sensitivity of Fair Value analysis of ± 100 basis points, registered at the end of December 2018 a value of ALL -659 million (for +100 basis points) compared to the end of year 2017 ALL -740 million.

9. Financial Risk Management (continued)

c) Market Risk (continued)

(ii) Exposure to Interest Rate risk (continued)

The table below shows the currency breakdown of the shift sensitivity for the year end 2018 and 2017.

Shift sensitivity 31 December 2017	**Increase in basis points**	**Total**	**Sensitivity of Profit & Loss**	**Sensitivity of Equity**
EUR	00 b.p. / -100 b.p.	(225,240)/ 111,277	(216,998)/ 105,218	(8,242)/ 6,059
USD	00 b.p. / -100 b.p.	(107,348)/ 118,124	(105,428)/ 116,178	(1,920)/ 1,946
ALL	00 b.p. / -100 b.p.	(327,223)/ 332,664	(322,341)/ 327,540	(4,882)/ 5,125
Other (GBP & CHF)	00 b.p. / -100 b.p.	1,235/ (1,269)	1,235/(1,269)	0/ 0

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

The limits on shift sensitivity of Fair Value (EVE) for shock +100bp and the NII Sensitivity for shocks +/- 50bp are part of the RAF limits for ISBA 2018.

Following the merge of Intesa Sanpaolo Bank Albania and Veneto Banka (VB) as of October 1st 2018, the Group Financial Risk Committee (GFRC - on 26 September 2018) has approved the incorporation of the VB IRRBB limits in Intesa Sanpaolo Bank Albania IRRBB limits (Shift Sensitivity of Fair Value – EVE +/-100bp and Net Interest Income Sensitivity-NII +/-50bp), by increasing ISBA Shift Sensitivity of Fair Value and Shift Sensitivity of Net Interest Income, at the levels of +/- EUR 11 million (from +/- EUR 8 million) and +/- EUR 3 million (from +/- EUR 2.5 million) respectively. The changes, due to merger, in the shift sensitivity limits by buckets and by currencies has been approved on 5 November 2018 by the Intesa Sanpaolo Bank Albania's Board of Directors.

The NII sensitivity records the NII effects generated by the market rates movement on the renewal/re-pricing of the banking book. It quantifies the short-term impact on the net interest income of a parallel, instantaneous, permanent shock of ±50 basis points to the interest rate curve. This measure highlights the effect of variations in market rates on the interest margin generated by the portfolio that is being measured, excluding potential effects deriving from the new operations and future changes in the mix of assets and liabilities. The reference time horizon is typically limited to 1 year and according to the hypothesis that the institution is able to continue its activities ("going concern" approach).
The Interest rate risk generated by the Bank's assets and liabilities, as measured through shift sensitivity of Net Interest Income analysis of ± 50 basis points, registered at 31 December 2018 a value of Lek 218 million (for +50 basis points) and a value of Lek -269 million (for -50 basis points), compared to December 2017 Lek 271 million (for +50 basis points) and a value of Lek -269 million (for -50 basis points).

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

A different method used to measure Interest Rate risk is required by the Bank of Albania, which consists of quarterly monitoring of the interest rate risk exposure towards a parallel shock of ±200 basis points of the interest rate curve. For all the financial categories of assets and liabilities divided into either fixed or floating rate, their present value is calculated and is distributed in 14 time buckets. The total present value is then multiplied accordingly with the estimated modified duration of each time bucket. The limit for this exposure is 20% of the Bank's regulatory capital. The Bank has been within the limit with the interest rate risk exposures at 31 December 2018 being 6.3% of the Bank's regulatory capital (31 December 2017: 5.5%).

The Bank has been within the limits in accordance with Bank of Albania regulation and the internal regulation during the year 2018.

9. Financial Risk Management (continued)

c) Market Risk (continued)

(ii) Exposure to Interest Rate risk (continued)

The tables below summarize the Bank’s interest bearing financial assets and liabilities with both fixed and floating interest rates, as reported to Parent company and management of the Bank. The information is not reconcilable as it is provided by management and adjusted as per below.

Based on the management of Interest Rate risk regulation, each financial instrument is mapped to the repricing gap based on contractual undiscounted cash – flows or behavioral re-pricing date. The contractual includes instruments where the Bank knows exactly when the maturity or next re – pricing takes place.

31 December 2018		**O/N**	**0-3 months**	**3-18 months**	**18 moths - 3 years**	**3 - 5 years**	**>5 years**	**Total**
Assets	**Interest rate type**							
Loans and advances to banks	Fix	18,793,707	30,071,336	5,255,447	-	-	-	**54,120,490**
	Floating	-	-	-	-	-	-	**-**
Loans and advances to customers	Fix	11,445,250	659,437	3,459,693	3,615,549	1,085,042	1,021,695	**21,286,666**
	Floating	37,782	5,860,770	20,142,929	636,721	502,526	576,274	**27,757,002**
	Fix	-	10,285,273	23,145,054	9,618,471	13,304,548	4,074,342	**60,427,688**
Investment Securities	Floating	-	4,609,943	4,058,005	47,359	38,216	4,785	**8,758,308**
Other financial assets		-	-	-	-	-	-	**-**
Total financial assets		**30,276,739**	**51,486,759**	**56,061,128**	**13,918,100**	**14,930,332**	**5,677,096**	**172,350,154**
Liabilities								
Deposits to banks	Fix	(1,526,913)	(1,100,158)	-	(144,616)	-	-	**(2,771,687)**
	Floating	-	-	-	-	-	-	**-**
Due to customers	Fix	(85,462,198)	(16,848,806)	(31,272,669)	(4,437,328)	(8,688,016)	(686,539)	**(147,395,556)**
	Floating	-	-	-	-	-	-	**-**
Total financial liabilities		**(86,989,111)**	**(17,948,964)**	**(31,272,669)**	**(4,581,944)**	**(8,688,016)**	**(686,539)**	**(150,167,243)**
Reprising gap		**(56,712,372)**	**33,537,795**	**24,788,459**	**9,336,156**	**6,242,316**	**4,990,557**	**22,182,911**

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

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

9. Financial Risk Management (continued)

c) Market Risk (continued)

(iii) Exposure to Interest Rate risk (continued)

31 December 2017		O/N	0-3 months	3-18 months	18 moths - 3 years	3 - 5 years	>5 years	Total
Assets	**Interest rate type**							
	Fix	12,867,621	38,507,787	6,178,135	-	-	-	**57,553,543**
Loans and advances to banks	Floating	-	-	-	-	-	-	**-**
Loans and advances to Customers	Fix	18,054,989	982,372	3,057,908	2,950,697	2,534,137	3,017,036	**30,597,139**
	Floating	23,327,858	531,684	1,354,486	835,270	648,515	718,502	**27,416,315**
	Fix	-	9,269,812	19,955,891	7,536,180	11,944,592	2,744,323	**51,450,798**
Investment Securities	Floating	-	5,599,688	6,775,875	125,954	51,337	27,328	**12,580,182**
Other financial assets		-	3,040,980	-	-	-	-	**3,040,980**
Total financial assets		**54,250,468**	**57,932,323**	**37,322,295**	**11,448,101**	**15,178,581**	**6,507,189**	**182,638,957**
Liabilities								
	Fix	(55,544)	(4,393,761)	(3,137,667)	(234,050)	-	-	**(7,821,022)**
Deposits to banks	Floating	-	-	-	-	-	-	**-**
	Fix	(83,756,558)	(16,706,354)	(39,078,460)	(5,504,409)	(2,010,479)	(778,549)	**(147,834,809)**
Due to customers	Floating	-	-	-	-	-	-	**-**
Total financial liabilities		**(83,812,102)**	**(21,100,115)**	**(42,216,127)**	**(5,738,459)**	**(2,010,479)**	**(778,549)**	**(155,655,831)**
Reprising gap		**(29,561,634)**	**36,832,208**	**(4,893,832)**	**5,709,642**	**13,168,102**	**5,728,640**	**26,983,126**

9. Financial Risk Management (continued)

d) Operational Risk

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

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

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

Thresholds for Bank of Albania KRI-s are defined and integrated within "ISBA KRIs Policy", approved in ISBA BOD 4 May 2018. The KRI-s are monitored on quarterly basis as per regulation BoA "On Operational Risk Management" in place, and reported in ORCO and BoD meetings.

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

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

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

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

9. Financial Risk Management (continued)

e) Capital Management

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

Implementing the current capital requirements, the Central Bank of Albania requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets and off balance sheet items, at a minimum level of 12%. During financial year 2018 the Bank achieved an adequacy ratio well above the minimum required which as at 31 December 2017 is calculated at 23.17% (2017: 18.91%).

The modified capital adequacy ratio, which represents the ratio of base capital to risk-weighted assets and off balance sheet items, is another limit set by the Central Bank of Albania at a level of 6%. Throughout the period, there were no material changes in the Bank's management of capital and all externally imposed capital requirements were complied with.

In March 2015 new regulation on Capital Adequacy Ratio entered into force. The new regulation is based on Basel II criteria and is in line with the European Directives for Financial Institutions. Regardless that the new regulation and the countercyclical measures increase the level of risk weighted assets the Capital Adequacy Ratio remained well above the minimum level required during 2018 and 2017.

Capital adequacy ratio for the year ending 31 December 2017 is calculated based on pre-merge reported statement of financial position.

	Note	31 December 2018	31 December 2017
Tier 1 capital - CET1			
Share capital	25	5,562,518	5,562,518
Share premium	25	1,383,880	1,383,880
Legal and regulatory reserves	26	1,825,623	1,825,623
Regulatory retained earnings		10,736,321	7,059,651
		19,508,342	**15,831,672**
Deductions:			
Regulatory intangible assets		(591,149)	(619,181)
Total qualifying Tier 1 capital		**18,917,193**	**15,212,491**
Risk-weighted assets:			
On and off balance sheet		72,182,375	70,887,267
Risk assets for operational risk		9,459,017	9,572,263
Total risk-weighted assets		**81,641,392**	**80,459,530**
Tier I capital to risk- weighted asset ratio		**23.17%**	**18.91%**

During 2017, the Bank of Albania issued and approved the guideline "On the internal capital adequacy assessment process" which entered in force on 31 December 2017. The purpose of this guideline is to set out the requirements for banks on drafting and implementing the Internal Capital Adequacy Assessment Process (ICAAP), as well as the expectations of the supervisor on the structure and content of the regulatory report of this process. ICAAP, which is independently realized by the bank and approved from its governing bodies by acknowledging also regulatory requirements, shall ensure the assessment of the current and future levels of capital adequacy, based on its risk profile and strategies. ICAAP has been prepared by the Bank starting from year 2013 following also the ISP Group requirement and also have been timely submitted to the regulator during May 2018.

10. Financial Assets and Financial Liabilities

(a) Fair values of financial assets and financial liabilities

		Carrying Amount					Fair Value			
31 December 2018	**Note**	**Investment securities at amortized cost**	**Investment securities at FVOCI**	**Loans and advances to banks**	**Other financial liabilities**	**Total carrying amount**	**Level 1**	**Level 2**	**Level 3**	**Total**
Loans and advances to banks	12	-	-	20,253,667	-	**20,253,667**	-	-	20,253,667	**20,253,667**
Investments securities at amortized cost	13	57,403,527	-	-	-	**57,403,527**	4,315,199	372,000	54,058,023	**58,745,222**
Investment securities at FVOCI	13	-	6,323,591	-	-	**6,323,591**	4,112,004	1,990,558	221,029	**6,323,591**
Total		**57,403,527**	**6,323,591**	**20,253,667**	**-**	**83,980,785**	**8,427,203**	**2,362,558**	**74,532,719**	**85,322,480**
Deposits from customers	21	-	-	-	145,483,303	**145,483,303**	-	-	146,483,751	**146,483,751**
Total		**-**	**-**	**-**	**145,483,303**	**145,483,303**	**-**	**-**	**146,483,751**	**146,483,751**

		Carrying Amount					Fair Value			
31 December 2017	**Note**	**Held-to-maturity (HTM)**	**Available-for-Sale (AFS)**	**Loans and advances to banks**	**Other financial liabilities**	**Total carrying amount**	**Level 1**	**Level 2**	**Level 3**	**Total**
Loans and advances to banks	12	-	-	21,952,883	-	**21,952,883**	-	-	21,952,883	**21,952,883**
HTM Investments securities	13	49,110,119	-	-	-	**49,110,119**	4,691,391	-	45,628,746	**50,320,137**
AFS Investments securities	13	-	10,238,320	-	-	**10,238,320**	6,429,954	2,486,302	1,322,064	**10,238,320**
Total		**49,110,119**	**10,238,320**	**21,952,883**	**-**	**81,301,322**	**11,121,345**	**2,486,302**	**68,903,693**	**82,511,340**
Deposits from customers	21	-	-	-	147,108,177	**147,108,177**	-	-	147,473,892	**147,473,892**
Total		**-**	**-**	**-**	**147,108,177**	**147,108,177**	**-**	**-**	**147,473,892**	**147,473,892**

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

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

10. Financial Assets and Liabilities (continued)

(b) Classification of financial assets and financial liabilities

See accounting policies in Notes 8 (g)(ii).

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments.

	Note	Amortized cost	FVOCI	Total carrying amount
31 December 2018				
Financial Assets				
Cash and cash equivalents	11	35,290,306	-	**35,290,306**
Loans and advances to banks	12	20,253,667	-	**20,253,667**
Investments securities	13	57,403,527	6,323,591	**63,727,118**
Loans and advances to customers	14	43,928,731	-	**43,928,731**
Total		**156,876,231**	**6,323,591**	**163,199,822**
Financial Liabilities				
Due to banks	20	2,762,419	-	**2,762,419**
Due to customers	21	145,483,303	-	**145,483,303**
Total		**148,245,722**	**-**	**148,245,722**

	Note	Loans and receivables	Held to Maturity	Available for sale	Other financial liability	Total carrying amount
31 December 2017						
Financial Assets						
Cash and cash equivalents	11	35,615,020	-	-	-	**35,615,020**
Loans and advances to banks	12	21,952,883	-	-	-	**21,952,883**
Investments securities	13	-	49,110,119	10,238,320	-	**59,348,439**
Loans and advances to customers	14	52,234,239	-	-	-	**52,234,239**
Total		**109,802,142**	**49,110,119**	**10,238,320**	**-**	**169,150,581**
Financial Liabilities						
Due to banks	20	-	-	-	7,389,961	**7,389,961**
Due to customers	21	-	-	-	147,108,177	**147,108,177**
Total		**-**	**-**	**-**	**154,498,138**	**154,498,138**

10. Financial Assets and Liabilities (continued)

(c) Classification of financial assets and financial liabilities on the date of initial application of IFRS 9

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

	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	Remeasurement	New carrying amount under IFRS 9
Financial assets					
Cash and cash equivalents	Loans and receivables	Amortized cost	35,615,020	(69,568)	35,545,452
Loans and advances to banks	Loans and receivables	Amortized cost	21,952,883	(8,557)	21,944,326
Loans and advances to customers	Loans and receivables	Amortized cost	52,234,239	(897,705)	51,336,534
Investment Securities debt	Available-for-sale	FVOCI	10,238,320	(27,515)	10,210,805
Investment Securities debt	Held-to-maturity	Amortized cost	49,110,119	(242,455)	48,867,664
Total financial assets			**169,150,581**	**(1,245,800)**	**167,904,781**
Financial liabilities					
Due to banks	Amortized cost	Amortized cost	7,389,961	-	7,389,961
Due to customers	Amortized cost	Amortized cost	147,108,177	-	147,108,177
Total financial assets			**154,498,138**	**-**	**154,498,138**

The effect of initially applying IFRS 9 resulted in an increase in impairment losses recognized on financial asset amounting to Lek 1,298,324 thousand, out of which Lek 52,524 thousand relate to loan commitments (see Note 23). The impairment loan increase from initial application of IFRS 9 was recognized in retained earnings, net of related deferred tax amounting to Lek 194,749 thousand. As at 31 December 2018, any corresponding reversal to the initial increase of impairment allowance resulted in derecognized deferred tax amounting to Lek 34,178 thousand.

11. Cash and cash equivalents

Cash and cash equivalents as at 31 December 2018 and 31 December 2017 are detailed as follows:

	31 December 2018	31 December 2017
Cash on hand	1,445,723	1,636,211
Current accounts with banks	13,832,185	21,864,668
Unrestricted balances with Bank of Albania	336,849	714,690
Money market placements	19,687,599	11,399,451
Less impairment loss allowance	(12,050)	-
Total	**35,290,306**	**35,615,020**

12. Loans and advances to banks

Loans and advances to banks as at 31 December 2018 and 31 December 2017 are composed as follows:

	31 December 2018	31 December 2017
Compulsory reserve with Bank of Albania	14,993,704	13,611,323
Deposits with correspondent banks	5,263,961	8,341,560
Less impairment loss allowance	(3,998)	-
Total	**20,253,667**	**21,952,883**

In accordance with the Bank of Albania requirements, the Bank at the reporting date should maintain a minimum of compulsory reserve as per percentages determined by the regulator (See note 9 (b) (ii)).

Such reserves are maintained in original currency for due to customer balances denominated in local currency. For due to customer balances denominated in foreign currency the Bank is obliged to maintained in original currency only up to 10% of the deposits included in the reserve base and the remaining part denominated in local currency.

The amount required to be deposited is calculated monthly in arrears. According to the Bank of Albania regulation 70% of this reserve in Lek is available for daily use by the Bank.

The remuneration interest rate of obligatory reserve denominated in Lek is 70% of repurchase agreements rate equal to 1.00% for 31 December 2018 (31 December 2017: 0.875%).

The remuneration interest rate of the obligatory reserve in EUR is equal to the European Central Bank base rate equal to minus 0.40% for 31 December 2018 (31 December 2017: minus 0.40%).

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

13. Investment securities

	31 December 2018	31 December 2017
Investment securities measured at FVOCI-debt instruments	6,323,591	-
Investment securities measured at amortised cost- debt instruments	57,403,527	-
Available for sale Investment securities	-	10,238,320
Held to Maturity Investment securities	-	49,110,119
Total	**63,727,118**	**59,348,439**

Investment securities measured at FVOCI as at 31 December 2018 (31 December 2017: Available for sale Investment securities) can be detailed as follows:

	31 December 2018	31 December 2017
Corporate issuers		
Bank issuers	**-**	**900,577**
Unlisted	-	-
Listed	-	900,577
Sovereign issuers		
Republic of Albania	**2,211,587**	**4,186,846**
Unlisted	2,211,587	3,466,659
Listed	-	720,187
EU member states	**3,574,631**	**4,040,862**
Listed	3,574,631	4,040,862
Other Financial Institutions	**537,373**	**1,110,035**
Listed	537,373	1,110,035
Total	**6,323,591**	**10,238,320**

Investment securities measured at amortised cost as at 31 December 2018 (31 December 2017: Held to Maturity Investment securities) can be detailed as follows:

	31 December 2018	31 December 2017
Sovereign issuers		
Republic of Albania	**55,300,570**	**46,915,264**
Unlisted	53,191,287	44,842,532
Listed	2,109,283	2,072,732
US and EU member states	**2,102,957**	**2,194,855**
Listed	2,102,957	2,194,855
Total	**57,403,527**	**49,110,119**

As at 31 December 2018, no Albanian Government securities have been pledged as collateral for repurchase agreements (2017: Lek 1,779 million) (see note 20).

14. Loans and advances to customers

Loans and advances to customers measured at amortized cost are composed as follows:

	31 December 2018	31 December 2017
Loans	35,462,579	36,714,047
Overdrafts	11,187,135	17,855,001
Deferred disbursement fees	(149,289)	(142,998)
Gross amount	**46,500,425**	**54,426,050**
Less impairment loss allowance (see Note 9 (a) (v))	(2,571,694)	(2,191,811)
Total net amount	**43,928,731**	**52,234,239**

	2018			**2017**		
	Gross carrying amount	**ECL allowance**	**Carrying amount**	**Gross carrying amount**	**Impairment allowance**	**Carrying amount**
Retail customers	**15,727,382**	**960,755**	**14,766,627**	**14,355,921**	**473,034**	**13,882,887**
Mortgage lending	12,193,829	557,035	11,636,794	10,669,270	323,533	10,345,737
Personal loans	3,516,213	400,576	3,115,637	3,644,488	140,932	3,503,556
Credit cards	17,340	3,144	14,196	42,163	8,569	33,594
Corporate customers	**30,773,043**	**1,610,939**	**29,162,104**	**40,070,129**	**1,718,777**	**38,351,352**
Investment loans	18,935,002	874,788	18,060,214	21,342,153	931,315	20,410,838
Working capital	11,838,041	736,151	11,101,890	18,727,976	787,462	17,940,514
Total	**46,500,425**	**2,571,694**	**43,928,731**	**54,426,050**	**2,191,811**	**52,234,239**

15. Non-current assets held for sale

The Bank holds under non-current assets held for sale, loans issued from VBA identified during Board of Experts due diligence as non-performing loans to be transferred back to Veneto Banca in compulsory administrative liquidation and high risk loans already classified as non performing (unlikely to pay or doubtful) which shall be transferred to the Veneto Banca in compulsory administrative liquidation, with customized guarantee from the Government of Italy, during the next retrocession windows envisaged by contract. The related loans carrying amount was determined based on the contractual indications, which set out a consideration equal to their gross value net of impairment allowance recognized only 50% of the value of those ISP Group would have had to account by complying with its own loan loss impairment policies with the price that will be payable to retransfer the corresponding exposure to the Veneto Banca in compulsory administrative liquidation.

16. Property and Equipment

Property and Equipment as at 31 December 2018 and 31 December 2017 is as follows:

	Land and Building	IT and Electrical Equipment	Furniture and Fine Art Works	Other non-Electrical Assets	Assets acquired not put into use	Total
Cost						
Balance as at 1 January 2017	**1,643,522**	**1,537,868**	**285,657**	**303,023**	**222,860**	**3,992,930**
Additions	55,540	147,996	19,804	15,404	1,579	**240,323**
Disposals	-	(179,529)	-	-	(59,550)	**(239,079)**
Effect of revaluation	(13,920)	-	-	-	-	**(13,920)**
Balance as at 31 December 2017	**1,685,142**	**1,506,335**	**305,461**	**318,427**	**164,889**	**3,980,254**
Additions	39,843	87,856	15,744	17,626	56,367	**217,436**
Disposals	-	(123,635)	(19,353)	(22,808)	-	**(165,796)**
Effect of revaluation	-	-	-	-	-	**-**
Balance as at 31 December 2018	**1,724,985**	**1,470,556**	**301,852**	**313,245**	**221,256**	**4,031,894**
Accumulated Depreciation						
Balance as at 1 January 2017	**892,411**	**1,339,714**	**248,093**	**275,561**	**-**	**2,755,779**
Depreciation for the year	33,781	91,791	7,628	10,271	-	**143,471**
Disposals	-	(178,016)	-	-	-	**(178,016)**
Effect of revaluation	(926,192)	-	-	-	-	**(926,192)**
Balance as at 31 December 2017	**-**	**1,253,489**	**255,721**	**285,832**	**-**	**1,795,042**
Depreciation for the year	57,270	104,911	16,528	13,831	-	**192,540**
Disposals	-	(117,595)	(16,844)	(21,774)	-	**(156,213)**
Impairment loss	-	10,030	-	-	-	**10,030**
Balance as at 31 December 2018	**57,270**	**1,250,835**	**255,405**	**277,889**	**-**	**1,841,399**
Carrying amount						
At 1 January 2017	**751,111**	**198,154**	**37,564**	**27,462**	**222,860**	**1,237,151**
At 31 December 2017	**1,685,142**	**252,846**	**49,740**	**32,595**	**164,889**	**2,185,212**
At 31 December 2018	**1,667,715**	**219,721**	**46,447**	**35,356**	**221,256**	**2,190,495**

17. Intangible Assets

Intangible assets as at 31 December 2018 and 31 December 2017 are as follows:

	Software and Licenses	Advances for Software	Total
Cost			
Balance as at 1 January 2017	**1,741,600**	**123,797**	**1,865,397**
Additions during period	162,139	-	**162,139**
Transfers		(38,782)	**(38,782)**
Balance as at 31 December 2017	**1,903,739**	**85,015**	**1,988,754**
Additions during period	140,378	-	**140,378**
Transfers	(144,193)	(9,209)	**(153,402)**
Balance as at 31 December 2018	**1,899,924**	**75,806**	**1,975,730**
Amortization and Impairment Losses			
Balance as at 1 January 2017	**1,240,369**	-	**1,240,369**
Amortization charge for the year	155,883	-	**155,883**
Disposals	-	-	**-**
Balance as at 31 December 2017	**1,396,252**	**-**	**1,396,252**
Amortization charge for the year	188,546	-	**188,546**
Disposals	(103,404)	-	**(103,404)**
Balance as at 31 December 2018	**1,481,394**	**-**	**1,481,394**
Carrying amount			
At 1 January 2017	**501,231**	**123,797**	**625,028**
At 31 December 2017	**507,487**	**85,015**	**592,502**
At 31 December 2018	**418,530**	**75,806**	**494,336**

18. Investment property

The Bank holds investment property as consequence of acquisitions through enforcement of security over loans and advances. As at 31 December 2018, the investment property represent a foreclosed collateral repossessed during 2017. During 2018, investment property rentals of Lek 18,056 thousand (2017: Lek 9,864 thousand) have been recognized in other income. Based on the agreement between parties the annual rent for the first year is calculated 2.8% of the historical cost. The annual rent change over the period based on the payment of instalments for purchase of the property.

	Buildings	Total
Cost		
Balance as at 1 January 2017	**-**	**-**
Additions during period	721,488	**721,488**
Disposals	-	**-**
Balance as at 31 December 2017	**721,488**	**721,488**
Additions during period	**-**	**-**
Disposals	-	**-**
Balance as at 31 December 2018	**721,488**	**721,488**
Depreciation and Impairment Losses		
Balance as at 1 January 2017	**-**	**-**
Depreciation charge for the year	16,397	**16,397**
Impairment Losses	129,773	**129,773**
Balance as at 31 December 2017	**146,170**	**146,170**
Depreciation charge for the year	-	**-**
Impairment Losses	29,762	**29,762**
Balance as at 31 December 2018	**175,932**	**175,932**
Carrying amount		
At 1 January 2017	**-**	**-**
At 31 December 2017	**575,318**	**575,318**
At 31 December 2018	**545,556**	**545,556**

19. Inventory and other assets

Other assets as at 31 December 2018 and 31 December 2017 are as follows:

	31 December 2018	31 December 2017
Inventory	1,892,768	2,478,167
Sundry debtors	443,042	63,800
Receivable from Intesa Sanpaolo Group	-	3,040,980
ATM & POS transactions	117,837	361,424
Leasehold improvements	31,407	110,037
Prepayments	47,934	57,641
Cheques for collection	4,301	3,497
Others	129,345	72,903
Total	**2,666,634**	**6,188,449**

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

	2018	2017
At beginning of the period	**2,478,167**	**2,298,654**
Additions during period	228,961	762,671
Disposals of the period	(589,308)	(363,280)
Write down to net realizable value	(80,583)	(190,287)
Effect of movements in foreign exchange	(144,469)	(29,591)
At end of the period	**1,892,768**	**2,478,167**

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

	31 December 2018	31 December 2017
At beginning of the period	**110,037**	**22,398**
Additions during period	3,103	95,502
Write off	(55,462)	-
Amortization of the period	(26,271)	(7,863)
At end of the period	**31,407**	**110,037**

20. Due to banks

Due to banks as at 31 December 2018 and 31 December 2017 are as follows:

	31 December 2018	31 December 2017
Correspondent banks		
Current accounts	**1,662,306**	**1,104,824**
Resident	3,271	851,538
Non-resident	1,659,035	253,286
Deposits	**1,100,113**	**4,712,755**
Resident	1,100,113	1,575,088
Non-resident	**-**	3,137,667
Repurchase Agreements	**-**	**1,572,382**
Total	**2,762,419**	**7,389,961**

As at 31 December 2018, no Albanian Government securities have been pledged as collateral for repurchase agreements (2017: Lek 1,779 million) (see note 13).

21. Due to customers

Due to customers as at 31 December 2018 and 31 December 2017 are composed as follows:

	31 December 2018			31 December 2017		
Current accounts	**Local Currency**	**Foreign Currency**	**Total**	**Local Currency**	**Foreign Currency**	**Total**
Retail	8,084,405	17,921,842	**26,006,247**	7,298,891	16,056,185	**23,355,076**
Corporate	10,799,571	24,580,301	**35,379,872**	11,866,510	25,456,549	**37,323,059**
	18,883,976	**42,502,143**	**61,386,119**	**19,165,401**	**41,512,734**	**60,678,135**
Deposits						
Retail	36,697,461	40,617,936	**77,315,397**	36,335,824	43,858,807	**80,194,631**
Corporate	2,231,880	4,549,907	**6,781,787**	1,565,167	4,670,244	**6,235,411**
	38,929,341	**45,167,843**	**84,097,184**	**37,900,991**	**48,529,051**	**86,430,042**
Total	**57,813,317**	**87,669,986**	**145,483,303**	**57,066,392**	**90,041,785**	**147,108,177**

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

	31 December 2018			31 December 2017		
	Local Currency	**Foreign Currency**	**Total**	**Local Currency**	**Foreign Currency**	**Total**
Current Accounts	**18,883,976**	**42,502,143**	**61,386,119**	**19,165,401**	**41,512,734**	**60,678,135**
Deposits						
On demand	3,838,216	18,325,653	**22,163,869**	3,651,809	16,553,534	**20,205,343**
One month	1,059,056	172,393	**1,231,449**	398,717	332,297	**731,014**
Three months	751,773	1,721,161	**2,472,934**	866,579	1,969,202	**2,835,781**
Six months	1,926,418	2,894,538	**4,820,956**	2,699,180	3,973,234	**6,672,414**
Nine months	432	16,684	**17,116**	767	7,317	**8,084**
Twelve months	11,366,650	18,008,943	**29,375,593**	14,370,830	20,953,013	**35,323,843**
Twenty four months	5,859,493	2,425,759	**8,285,252**	7,648,837	2,842,807	**10,491,644**
Other	14,127,303	1,602,712	**15,730,015**	8,264,272	1,897,647	**10,161,919**
	38,929,341	**45,167,843**	**84,097,184**	**37,900,991**	**48,529,051**	**86,430,042**
Total	**57,813,317**	**87,669,986**	**145,483,303**	**57,066,392**	**90,041,785**	**147,108,177**

21. Due to customers (continued)

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

2018	ALL (%)	USD (%)	EUR (%)
Current accounts and demand deposits	0.05 -2.81	0.05 - 1.90	0.002 - 0.65
Time deposits – 1 month	0.20 - 0.20	0.05 -0.05	0.002 - 0.05
Time deposits – 3 months	0.20 - 0.85	0.10 - 0.20	0.001 - 0.002
Time deposits – 6 months	0.20 - 1.05	0.10 - 0.25	0.003 - 0.005
Time deposits – 9 months	0.40 - 0.40		0.006 - 0.006
Time deposits – 12 months	0.20 - 1.50	0.20 - 0.30	0.005 - 0.01
Time deposits – 24 months	1.70 - 2.00	0.20 - 0.30	0.02 - 0.05
Time deposits – 36 months	1.80 - 2.20	0.25 - 0.90	0.05 - 0.60
Time deposits – 60 months	2.38 - 4.50	0.25 - 1.20	0.10 - 1.00
Time deposits – 84 months	3.41 - 3.60		

2017	ALL (%)	USD (%)	EUR (%)
Current accounts and demand deposits	0.01 – 2.07	0.01 – 0.53	0.002 – 0.997
Time deposits – 1 month	0.40 – 0.90	0.05 – 0.05	0.002 – 0.030
Time deposits – 3 months	0.40 – 1.20	0.10 – 0.20	0.000 – 0.050
Time deposits – 6 months	0.45 – 1.50	0.15 – 0.25	0.000 – 0.050
Time deposits – 9 months	0.40 – 1.10		0.006 – 0.070
Time deposits – 12 months	0.60 – 1.90	0.20 – 0.30	0.000 – 0.100
Time deposits – 24 months	1.15 – 2.15	0.20 – 0.30	0.020 – 0.100
Time deposits – 36 months	1.20 – 2.40		0.070 – 0.100
Time deposits – 60 months	2.38 – 2.56		
Time deposits – 84 months	3.41 – 3.60		

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

22. Deferred Tax

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

	31 December 2018			31 December 2017		
	Assets	Liabilities	Net	Assets	Liabilities	Net
Investment securities measured at FVOCI (31 December 2017: Available for sale Investment securities)	17,984	-	17,984	-	9,969	(9,969)
Allowance for expected credit losses (see note 10.c)	160,571	-	160,571	-	-	-
Investment Property	-	1,599	(1,599)	-	1,599	(1,599)
Repossessed assets	300,192	-	300,192	102,580	-	102,580
Properties	-	136,840	(136,840)	-	136,840	(136,840)
Equipment and intangible assets	89,745	-	89,745	96,024	-	96,024
Net deferred tax assets	**568,492**	**138,439**	**430,053**	**198,604**	**148,408**	**50,196**

22. Deferred Tax (continued)

Movements in temporary differences during the year are as follows:

31 December 2018	Opening balance	Recognized in profit or loss	Recognized in other comprehensive income	Closing balance
Investment securities measured at FVOCI	(9,969)	-	27,953	17,984
Allowance for expected credit losses	-	-	160,571	160,571
Investment Property	(1,599)	-	-	(1,599)
Repossessed assets	102,580	197,612	-	300,192
Properties	(136,840)	-	-	(136,840)
Equipment and intangible assets	96,024	(6,279)	-	89,745
Total	**50,196**	**191,333**	**188,524**	**430,053**
31 December 2017				
Available for sale Investment securities	(371)	-	(9,598)	**(9,969)**
Investment Property	-	(1,599)	-	**(1,599)**
Repossessed assets	-	102,580	-	**102,580**
Properties	26,748	(26,748)	(136,840)	**(136,840)**
Equipment and intangible assets	79,699	16,325	-	**96,024**
Total	**106,076**	**90,558**	**(146,438)**	**50,196**

23. Provisions

Movements in provisions during the year are as follows:

	Tax Litigation	Other Litigations	Off-Balance Sheet	Integration costs	Other Provision	Total
Balance at 1 January 2018	278,094	674,599	53,810	147,176	77,132	**1,230,811**
Adjustment on initial application of IFRS 9 related to loan commitments (see note 10.c)	-	-	52,524		-	**52,524**
Provisions made/(reversed) during the year	-	12,879	(21,182)	349,069	17,474	**358,240**
Provisions used during the year	45,446	(121,753)	-	(225,442)	(95,769)	**(397,518)**
Effect of movements in foreign exchange	-	1,915	(2,226)	(10,550)	1,163	**(9,698)**
Balance at 31 December 2018	**323,540**	**567,640**	**82,926**	**260,253**	**-**	**1,234,359**

At 31 December 2018, Lek 260,253 thousand provisions related to Veneto Banka merger integration activities are recognised net of expected recoveries of Lek 157,677 presented under other operating expenses (see note 30).

24. Other liabilities

Other liabilities as at 31 December 2018 and 31 December 2017 are composed as follows:

	31 December 2018	31 December 2017
Accrued expenses	494,163	243,147
Sundry creditors	43,931	288,836
Suspense accounts	413,091	381,407
Bank cheques issued and payments in transit	363,625	634,498
Other tax liabilities	49,379	39,567
Due to third parties	20,458	18,774
Other accrued expenses	67,580	58,144
Total	**1,452,227**	**1,664,373**

25. Share capital and share premium

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

	Number of Shares (In number)	Nominal Value (In Lek)	Total Shares Value (In Lek)
Share Capital at 31 December 2018	**15,581,282**	**357**	**5,562,517,674**

Share premium represents the amount paid from the shareholder in excess of the registered share capital. Intesa Sanpaolo S.p.A is the sole shareholder at 31 December 2018 and 31 December 2017.

On 22 February 2018 the Assembly meeting of the Shareholders approved a dividend distribution amounting to Lek 1,656,755 thousand for the fiscal year 2017. On 29 March 2017 the Assembly meeting of the Shareholders approved a dividend distribution amounting to Lek 2,283,005 thousand for the fiscal year 2016. 2018 and 2017 dividends have been fully paid at the corresponding reporting date.

26. Reserves

As at 31 December 2018 and 31 December 2017, the reserves were:

	31 December 2018	31 December 2017
Regulatory reserve (*refer to a below*)	1,130,983	1,130,983
Legal reserve (*refer to b below*)	694,640	694,640
Fair value reserve (*refer to c below*)	(97,281)	56,486
Revaluation reserve (*refer to d below*)	775,431	775,431
Other capital reserve (*refer to e below*)	714,555	714,555
Merger reserve (*refer to f below*)	2,813,396	2,813,396
Total	**6,031,724**	**6,185,491**

Nature and purpose of the reserves

a. The regulatory reserve was established according to the Central Bank of Albania regulation “On the Bank’s Regulatory Capital”, no.69, dated 18 December 2014. Banks and branches of foreign banks are required to create reserves of 1.25% to 2% of total risk-weighted assets, by appropriating one fifth of the profit after taxes and before payment of dividends, until the balance on this measure reaches at least 1.25% of total risk-weighted assets. At 31 December 2018, the regulatory reserve represented 1.39% of total risk-weighted assets (2017: 1.41%).

b. The legal reserve was established according to the provisions of the Commercial Law requiring the creation of reserves of 5% of the Bank’s net income after deduction of accumulated losses from previous years, until the balance of this reserve reaches 10% of the Bank’s share capital. At 31 December 2018, the balance represented 10% of the Bank’s share capital (2017: 10%). This threshold is not mandatory, when the existing reserves are not less than one tenth of the Bank’s share capital.

c. The Fair value reserve represent the cumulative net change in fair value of de securities at FVOCI (2017: available for sale investment securities) until the asset are derecognised or reclassified.

d. The revaluation reserve relates to the revaluation of owed used property.

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

f. As further disclosed in note 7, the merger reserve represent the contribution by owner equal to the net assets transferred considering that the Bank did not pay anything to acquire net assets of VBA.

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27. Net Interest income

Interest income	**2018**	**2017**
Loans and advances to customers	2,262,829	2,119,979
Investment securities at amortised cost	1,999,109	2,007,949
Loans and advances to banks	163,380	87,635
Investment securities at FVOCI (2017: available for sale)	88,204	88,264
Total interest income	**4,513,522**	**4,303,827**
Interest expenses		
Demand and time deposits	629,755	403,187
Deposits from banks	129,578	83,811
Current accounts of customers	59,970	51,260
Total interest expenses	**819,303**	**538,258**
Net interest income	**3,694,219**	**3,765,569**

Included within loans and advances to customers line under interest income for the year ended 31 December 2018 is a total of Lek 279,860 thousand (2017: Lek 182,362 thousand) generated impaired customers[exposures.

28. Net fee and commission income

	2018			**2017**		
	Retail Banking	**Corporate Banking**	**Total**	**Retail Banking**	**Corporate Banking**	**Total**
Collection and payment services	181,572	294,055	**475,627**	156,957	290,271	**447,228**
Active current accounts	238,034	28,568	**266,602**	191,980	22,378	**214,358**
ATMs and POSs	252,903	67,273	**320,176**	208,957	51,058	**260,015**
Guarantees given	626	20,820	**21,446**	615	18,417	**19,032**
Unused/advanced liquidated credit lines	6,146	17,196	**23,342**	12,660	10,509	**23,169**
Arrangement fees and others	3,205	2,176	**5,381**	4,410	4,517	**8,927**
Fee and commission income	**682,486**	**430,088**	**1,112,574**	**575,579**	**397,150**	**972,729**
ATMs and POSs	231,236	62,945	**294,181**	176,655	**47,753**	**224,408**
Banking services-foreign branches	128	10,589	**10,717**	**-**	8,616	**8,616**
Collection and payment services	18,722	2,469	**21,191**	11,621	3,063	**14,684**
Guarantees received	-	1,191	**1,191**	18	6,278	**6,296**
Fee and commission expenses	**250,086**	**77,194**	**327,280**	**188,294**	**65,710**	**254,004**
Net fee and commission income	**432,400**	**352,894**	**785,294**	**387,285**	**331,440**	**718,725**

Fee and commissions do not include fees received for loans and advances to customers (transaction costs), which are adjusted on initial recognition for the carrying value of these financial assets as per effective interest rate method. Fee and commission income from contracts with customers is measured based on the consideration specified in a contract with a customer. The Bank recognises revenue when it transfers control over a service to only a customer.

The Bank provides banking services only to retail and corporate customers, including account management, provision of overdraft facilities, foreign currency transactions, credit card and servicing fees. Fees for ongoing account management are charged to the customer's account on a monthly basis. The Bank sets the rates separately for retail and corporate banking customers in each jurisdiction on a regular basis. Transaction-based fees for interchange, foreign currency transactions and overdrafts are charged to the customer's account when the transaction takes place Servicing fees are charged on a monthly basis and are based on fixed rates reviewed regularly by the Bank. Revenue from account service and servicing fees is recognised over time as the services are provided Revenue related to transactions is recognised at the point in time when the transaction takes place.

29. Net other income

	2018	2017
Foreign exchange (losses)/gains	(27,092)	323,936
Other	131,368	36,437
Total	**104,276**	**360,373**

30. Other operating expenses, net

	2018	2017
Premium on deposits insurance	322,047	332,525
Loss on sale of fixed assets	72,099	6,031
(Gain)/loss on sundry net operational	(349,392)	(66,715)
Total	**44,754**	**271,841**

31. Personnel expenses

	2018	2017
Salaries	1,062,347	934,438
Personnel on secondment	98,171	92,237
Social Insurance	131,550	110,617
Training & similar	10,435	4,696
Termination indemnities and others	86,863	12,418
Total	**1,389,366**	**1,154,406**

32. Other administrative expenses

	2018	2017
Integration costs (see Note 23)	349,069	-
Software maintenance	333,121	283,607
Telephone and electricity	107,610	57,985
Advertising and publications	28,951	26,968
Maintenance and repair	80,802	53,657
Stationery	50,271	48,299
Consulting, legal and professional fees	69,387	39,758
Security	75,206	54,161
Transport and security services	52,162	29,669
Travel and business trips	10,364	9,474
Insurance	16,360	15,170
Other	150,671	114,479
Total	**1,323,974**	**733,227**

33. Income tax expenses

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

	2018	2017
Current year	160,693	368,999
Current tax expense	**160,693**	**368,999**
Origination and reversal of temporary differences	(191,333)	(90,558)
Deferred tax income	**(191,333)**	**(90,558)**
Income tax (benefit)/expense	**(30,640)**	**278,441**

Reconciliation of the income tax expense with the accounting profit for the year ended 31 December 2018 and 2017 is presented as follows:

	2018		2017	
Accounting Profit before tax		**813,521**		**1,794,926**
Income tax at domestic corporate tax rate	15.00%	122,028	15.00%	269,239
Non-deductible expenses	4.75%	38,665	5.56%	99,760
Origination and reversal of temporary differences	(23.52%)	(191,333)	(5.05%)	(90,558)
Income tax Expense	**(3.77%)**	**(30,640)**	**15.51%**	**278,441**

Non-deductible expenses are detailed as follows:

	2018	2017
Representations & Sponsorships expenses	165	199
Sundry operational losses	22,054	3,790
Operating leases expenses	4,132	3,854
Personnel expenses	9,031	6,303
Office expenses	49,565	6,868
Other provisions expenses	59,916	39,004
Litigation expenses	12,879	50,928
Losses on unrecoverable loans and overdrafts	303,573	163,261
Write down of inventory	110,346	320,060
Reversal of accruals related to prior years	-	(48,632)
Depreciation and amortization expenses	30,973	(20,839)
Changes to estimates related to prior years	(117,013)	-
Pre-merge unrecognized tax losses	-	140,270
Allowance reversals for expected credit losses	(227,853)	-
Total	**257,768**	**665,066**
At 15%	**38,665**	**99,760**

The Bank prepaid income tax in the amount of Lek 289,081 thousand were paid during 2018 (2017: Lek 476,786 thousand).

34. Commitments and contingencies

Commitments and contingencies as at 31 December 2018 and 31 December 2017 are as follows:

	31 December 2018	31 December 2017
Contingent Assets	**134,614,733**	**152,437,542**
Guarantees received from credit customers	116,320,718	139,446,251
Guarantees received from Government	1,270,000	5,200,000
Money market future dated deals	1,862,000	246,806
Forward foreign exchange contracts	1,239,005	2,096,925
Other	13,923,010	5,447,560
Contingent Liabilities	**9,571,925**	**15,295,672**
Guarantees in favor of customers	4,245,210	5,431,354
Un-drawn credit facilities	4,378,023	6,835,897
Letters of credit	948,692	3,028,421

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

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

Litigation

The Bank is defending an action related to a partial payment of a bank guarantee amounting EUR 4,830 thousand. The guarantee was issued in favor of an Albanian entity upon the request of its Parent Company Intesa Sanpaolo S.P.A. The Bank has successfully defended itself in a legal process, in which both the First Instance Court and Court of Appeal judged in favor of the Bank.

The plaintiff has appealed to the Supreme Court which has not yet issued its decision. Management does not consider that there are any legal grounds for the existing judgments in its favor to be overturned.

Nevertheless, given the complexity of the case, involving also the Italian Jurisdiction, and taking into consideration no other cases of that kind have been ever judged in the Albanian courts, some operational risks may occur. In the ordinary course of business, the Bank may be involved in other various claims and legal actions which in the opinion of management, the ultimate settlement of these matters will not have a material adverse effect on the Bank’s financial position or changes in net assets, other than those for which a provision has already been included in these financial statements.

35. Lease commitments and operating lease expenses

The Bank’s operating lease commitments as lessee as at 31 December 2018 and 31 December 2017 are as follows:

	31 December 2018	31 December 2017
Less than one year	45,274	67,061
Between one and five years	-	-
More than five years	-	-
Total	**45,274**	**67,061**

The Bank has rental agreements with renewal options for its offices in Albania. During 2018, the amount of Lek 257,610 thousand was recognized as expense in respect of lease rentals (2017: Lek 202,282 thousand). Operating lease contracts are cancellable, if notified for a period of 180 days in advance.

36. Related parties

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

Shareholders and parties related to shareholders:

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

Key management personnel and parties related to key management personnel:

- Supervisory Board members, Management Board members and other key management personnel defined as persons having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly, including any director (whether executive or otherwise) of the Bank, collectively "key management personnel", close family members of key management personnel, and companies and un-incorporated businesses controlled, or jointly controlled by key management personnel and/or their close family members.

The following transactions have taken place during the year ended 31 December 2018 and 31 December 2017:

	ISP Group companies		**Key management personnel and Other related parties**	
	31 December 2018	**31 December 2017**	**31 December 2018**	**31 December 2017**
Assets at end of year	**16,549,651**	**12,082,176**	54,199	**107,904**
Loans and advances to credit institutions	16,466,776	12,069,161	-	-
Loans and advances to customers	-	-	54,199	107,904
Other assets	82,875	13,015	-	-
Liabilities at end of year	**1,560,027**	**1,356,097**	**482,606**	**401,259**
Loans and advances from credit institutions	1,491,880	1,310,245	-	-
Customer deposits	-	-	482,606	401,259
Invoices to be received	68,147	45,852	-	-
Off balance sheet	**1,709,028**	**5,194,836**	**-**	**-**
Letter of credit/Letter of Guarantees given	497,322	501,481	-	-
Letter of credit/Letter of Guarantees received	903,347	1,120,298	-	-
Foreign currency contracts	308,359	2,332,644	-	-
Commitments given	-	1,240,413	-	-
Collaterals	-	-	-	-
Income for year ending	**127,515**	**99,022**	**3,821**	**2,974**
Interest income	89,428	55,372	3,493	2,404
Commission Income	38,087	43,650	328	570
Expenses for the year ending	**114,922**	**38,155**	**260**	**481**
Interest expense	14,200	19,507	260	481
Commission expense and others	17,458	18,648	-	-
Other Administrative Costs	83,264	**-**	-	-
Compensation of Key Managers			**163,324**	**151,866**
Net Salary			86,674	81,706
Net Bonus paid			31,750	17,905
Social & Health Insurance			5,746	4,997
Other expenses (Lecoip)			17,093	13,963
Other expenses			22,061	33,295

37. Subsequent events

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