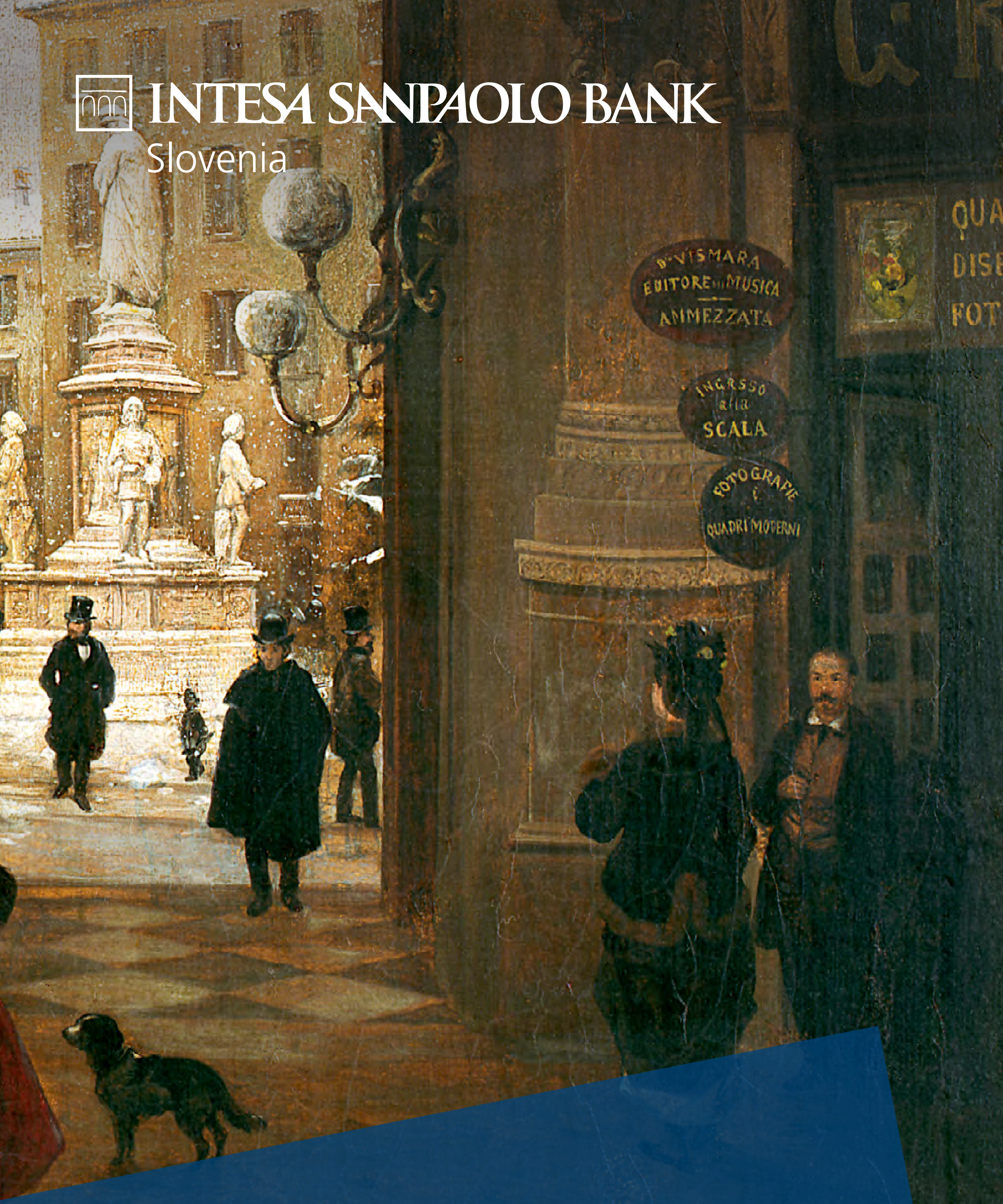
INTESA SANPAOLO BANK
Slovenia



2018 Annual Report

Bank of INTESA SANPAOLO

ANNUAL REPORT 2018

Table Of Contents

Business Report 2018

Intesa Sanpaolo Bank at a glance

In 2018, Intesa Sanpaolo Bank continued the activities designed to strengthen the name of the Bank in the wider area of Slovenia. With the strong support of our parent company Intesa Sanpaolo, the Bank provided suitable conditions for planning and implementation of changes to its business, which in times of economic growth is of strategic importance. By renaming Banka Koper to Intesa Sanpaolo Bank and by transferring majority ownership to Privredna Banka Zagreb, the Bank laid the foundations in 2017 for a further development strategy.

Throughout the entire period of its existence, Intesa Sanpaolo Bank has grown and contributed to the growth of the economy through its successful operations. The Bank is one of the first banks in Slovenia to have shifted its business to digital platforms and at the same time maintained the highest credit rating of all commercial banks in Slovenia during the financial crisis period.

The Bank's wish is to grow, develop further, and strengthen its position in the markets that are not traditionally domicile. In the Coastal-karst region, the Bank has achieved a dominant position with impressive market share. With the new strategy, the Bank wishes to outgrow the regional frameworks and establish itself as a modern and innovative bank in the all-Slovenian territory. For this reason, in 2018 the Bank adopted a new 2018–2021 Business Plan, which in its four pillars – Commercial revamp with a new light multichannel service model, Greater speed and efficiency, Engaged and empowered organization, New image position - assumes the expansion of the solid business from the regional environment to the national level. With this simpler and agile model, the Bank will be able to adapt more easily to the current market standards, to the new needs and expectations of its users, and the technological boom the Bank is witnessing.

The Plan's implementation started in the second half of 2018. Simultaneously, the renovation of the Bank's larger offices began and the plans to design some new ones were developed. One of the most important measures of the new strategy is the opening of a new business center in Ljubljana. Shifting the focus to the heart of the active Slovenian economy will bring the Bank closer to certain segments, making it easier to gain new clients and strengthen the Bank's position in other regions. Plans for the implementation of a simple multi-channel service model are also in progress. This will help the Bank will further strengthen its position in the field of digital business.

Ownership structure of Intesa Sanpaolo Bank

	Equity holding in per cent	
Shareholders	**31.12.2018**	**31.12.2017**
Privredna banka Zagreb d.d.	51.0%	51.0%
Intesa Sanpaolo S.P.A	48.1%	48.1%
Minority shareholders	0.9%	0.9%

International credit ratings

	2018	2017
Long-term	BBB-	BBB-
Short-term	F3	F3
Viability	bb+	bb
Support	2	2

In July 2018, Fitch Ratings London confirmed Intesa Sanpaolo Bank's long-term and short-term rating, an also the viability and support rating remained the same as in 2017. In April 2018 Bank's viability rating was improved by Fitch Ratings due to higher quality of assets, considerable capital buffer and good liquidity. Hence, the long-term rating is BBB-, short-term rating is F3, viability rating is bb+ and support rating is 2.

In September 2018 Fitch Ratings decreased prospects for the future from "Stable"to "Negative"which reflects the assessment that rating could decrease in the next 1-2 years. This assessment is based on changed expectations for the Parent bank of Intesa Sanpaolo Group.

Milestones in the Bank's corporate history

2018

INTESA SANPAOLO BANK

New name Intesa Sanpaolo Bank and the start of a revamp of our business activities.

Confirmation and implementation of the Bank's new development strategy.

Implementing the management of the 'My Pillar" Umbrella Pension Fund and its three sub-funds.

2017

New ownership structure of the bank within PBZ.

Transition of the most widely used payment card Activa Visa Inspire to contactless mobile payments.

New Advisory Service based on MIFID II.

2016

As the first bank in Slovenia, Banka Koper introduced the contactless mobile payments with smartphones, enabled by the mobile wallet Wave2Pay, which is based on Host Card Emulation technology.

2015

The merger by absorption of the subsidiary Finor Leasing into the Bank's organisational structure.

As the first bank in Slovenia, Banka Koper has created a brand-new cashless payment service using smartphones and QR code technology.

2014

Launch of the mobile and internet banking – Banka IN for Businesses.

2013

Launch of the mobile banking - Banka IN for Individuals.

Beginning of the Inspire debit card issuing.

2012

Establishing of entrepreneurship centers for small businesses.

2011

The first green branch and introduction of electronic signing of bank transactions.

The exclusive issue of the American Express cards.

2008

The Bank launches a new online banking solution - Banka IN.

2007

INTESA SANPAOLO

Banka Koper became a member of Intesa Sanpaolo Group.

2005

Introduction of the first smart payment card.

2002

The bank joins the Sanpaolo IMI Group - its majority shareholder.

2001

Preparations for strategic alliance with the Sanpaolo IMI, S.p.A banking group, establishment of the Open-ended Mutual Pension Fund.

1998

The developement of the i-Net Banka internet banking solution.

1997

New name and a new corporate identity for Banka Koper.

1996

The branch network expands to other Slovenian regions.

1992

Withdrawal from the LB bank system and launch of the first Slovenian payment card - Activa.

1955

Foundation of Istrska komunalna the bank.

Management overview

1. MANAGEMENT BOARD'S FOREWORD

On the wave of positive economic growth that marked both the demand and the growth of private spending, as well as export activities in the Slovenian economy, Intesa Sanpaolo Bank Slovenia succeeded in improving almost all business performance indicators in comparison with the previous year.

With the increase in operating income and the consistent lowering of operating costs, the Bank concluded the year with more than twice the net income in comparison to the previous year. The most important fact that contributed to the final result is that the Bank grew in its core activity of granting loans and collecting deposits, as it recorded growth in both areas in terms of volume and market share. In both areas, the Bank achieved even higher growth rates compared to the entire banking system. Despite the fact that the spread was down, the net performing interest income was higher in comparison to the previous year.

The general increase in salaries and private spending in the country was most visible in the increased demand for consumer and housing loans, where we recorded continuous growth each month. Lending to this customer segment increased by EUR 61.7 million or 10.7% on a yearly basis. We also achieved positive growth rates in lending to the SME (by 20.8%) and Corporate sector (by 3.4%), whereby the increase in loans to small- and medium-sized companies stood out as it rose by more than a fifth in comparison with the previous year.

In addition to increase of productivity, and to increase the total number of active customers, one of the biggest achievements is certainly the reduction of non-performing loans by almost 40% and the increase of performing loans by 8.4%, whereby we significantly improved the quality of the Bank's credit portfolio.

We were also active in the marketing of new products and services. After the withdrawal of American Express cards from the Slovenian market, whose exclusive issuer in Slovenia was Intesa Sanpaolo Bank, we immediately developed a solution for holders of this card. Thus, the Bank developed the option of payment in instalments using MasterCard, whereby the latter is possible to use with the Wave2Pay mobile wallet and not only in physical form as was the case for American Express.

In the area of supplementary pension insurance, we upgraded our range of products and offered a new form of saving in the form of life cycle investment policy through the My Pillar Umbrella Pension Fund.

Intesa Sanpaolo Bank was the first bank in the International Subsidiary Banks Division within the Intesa Sanpaolo Group and among the first banks in Slovenia to implement the advisory model in accordance with the MiFID II Directive, whose goal is to ensure a high-quality level of advisory services for the management of customer savings and investments in mutual funds that the Bank markets. With frequent marketing campaigns and emphasis on saving in mutual funds, we want to encourage our customers to consider other forms of savings, which, in comparison to classic deposits, bring potentially higher returns.

Maintaining the positive growth of operations under usual business circumstances, dictated by tough competition and favourable economic conditions, is a challenge in itself. This challenge was even bigger in the previous year for Intesa Sanpaolo Bank, since the Bank was taking important steps towards achieving its internal revamp with which it will ensure its further growth in an increasingly changing banking environment.

Thus, the Bank presented its new business strategy for growth and further development throughout the entire country, which is based on seven key initiatives that will help the Bank to become one of the most developed and prominent Slovenian banks in terms of cutting-edge digital banking solutions and customer experience.

One of the initiatives that raised the most of public attention was the Banks' decision to establish a new business centre in the capital of the country with the aim to strengthen the Bank's position in the heart of the Slovenian financial and business environment and to confirm the vision of a national innovator. We need to increase the volume of business and compete at the state level. However, we will continue to control and serve the domicile market of the Coast-Karst region as the largest banking institution and employer as well.

In parallel with preparations for the establishment of the new business centre in Ljubljana, we settled the ground for the introduction of the new business model in branches, starting with the pilot project in branches of Izola and Slovenska-Ljubljana, which be fully implemented, along with refurbishment- in branches of Koper, Maribor and Rotonda-Ljubljana in 2019. This is much more than simply a change of design and re-arrangement of the space inside the branches. The new business model changes the role of staff in our branches in the way that they are now able to dedicate more time for strengthening their relationships with customers.

From this perspective, the branches are irreplaceable and complement the role of digital banking, which is another area on the path to our transformation. Digitalisation in banking is in full swing and this is exactly the area we want to excel in. Therefore, in the second half of the year, we initiated the DIGICAL project together with our parent banking group, where the name already indicates that it addresses the connection of the digital and physical banking environment as a whole, where we will be able to provide an equally high-quality user experience through all channels.

Business practices have shown many examples of revamp strategies where the company has created new opportunities for success by changing their organisation and internal culture. Aware of the fact that changes are not always easily accepted and executed, we understand that they require careful planning and dedicated implementation coupled with the expert support of all colleagues. Teamwork, creativity and the engagement in a positive working environment will be of key importance in the realisation of the goals set as part of the revamp.

Each year, the Bank devotes particular attention to employees, as the latter, together with clients, represent key stakeholders for the further sustainable development of the Bank. Our values related to sustainable development as described in our Code of Ethics dictate our responsible behaviour within a wider society, and are founded on ethical principles and sustainability criteria of contemporary business. It is of great interest to us to diligently assess the compliance of our conduct with these principles in accordance with the ISO 26000 standard, which provides guidance on how organizations can operate in a socially responsible way.

To act sustainably means first and foremost to develop the awareness of the impact that our actions could have on a larger ecosystem than our Bank is. This is why it is important to ensure the continuous growth of our business as well as to make sure we have a positive influence on the development of the society we are part of. We are certain that, with the new strategy, we will give new momentum and new character to the Bank, at the same time we are also aware of our responsibility to leave a sustainable footprint by acting in the best interest of our stakeholders.

2. REPORT OF THE SUPERVISORY BOARD

REPORT OF THE SUPERVISORY BOARD ON THE EXAMINATION OF THE ANNUAL REPORT FOR THE FINANCIAL YEAR 2018

In accordance with the third paragraph of Article 272 and Article 546. a of the Companies Act (ZGD-1), the Management Board of Banka Intesa Sanpaolo d.d. has prepared and forwarded to the members of the Supervisory Board the following documents for review and approval:

- The Audited Annual Report for the Financial Year 2018,
- The Auditor's Report drawn up by the independent auditor KPMG Slovenija, Limited Liability Company,
- The proposal for the appropriation of profit and
- The report on the relations of the Bank with controlling company and its affiliates including the Auditor's Report drawn up by the independent auditor KPMG Slovenija, Limited Liability Company.

Pursuant to the provisions laid down in Article 282 and Article 546. a of the Companies Act, the Supervisory Board has examined the received documents and hereby presents its findings to the Annual General Meeting of Shareholders of Banka Intesa Sanpaolo d.d. (hereinafter referred to as: AGM) as follows

R E P O R T

1. The way and scope of verification of the management of the Bank during the financial year 2018

The Supervisory Board performed its duties in accordance with its principal function, i.e. supervision of the Bank's business run by the Management Board and the Bank's performance. In the course of the financial year 2018, the Supervisory Board of the Bank met five times at ordinary meetings and twelve times at extraordinary meetings in which it examined:

- strategic and operating matters in relation to the Bank's development,
- implementation of the business policy and current results posted by the Bank,
- annual and other reports of the Management Board, as well as other important issues relevant to the Bank's business;

and voted:

- on proposed business deals where due to being in excess of the limit on exposure determined for a particular customer, the Supervisory Board of the Bank has to grant its prior approval,
- on giving consent to the disclosures for the Bank for 2017, and
- on other matters of interest.

The Supervisory Board:

- gave prior approval to the budget for the financial year 2018 and to the budget for the period 2019-2021;
- monitored and assessed on a regular basis the compliance with the Bank's business policy for 2018 and the fulfilment of the goals set out within the policy framework;
- monitored the NPL reduction trends;
- gave its consent to the target values for the NPL ratios 2018 – 2020;
- adopted the annual Recovery Plan of the Parent Company for Banka Intesa Sanpaolo d.d. in part containing the measures which shall be used by the Bank to restore its own financial position in the event of a significant deterioration;
- discussed the annual plan of the Internal Audit Assignments for the year 2018 and the multiyear plan for the period 2018-2020;
- examined the annual report on the carrying out of internal control and the measures that arise from the regulations from the field of the fight against money laundering and terrorist financing, and the implementation of restrictive measures for 2017 and the semi-annual for the first half of 2018;
- examined the annual report of the Compliance and AML Department for 2017 and the action plan for 2018;
- examined and approved the annual report of the Internal Audit Department for 2017;
- verified the activities and reviewed the findings of the Internal Audit Department during the current year;

- acknowledged the receipt of the resignation notice of the member of the Supervisory Board and proposed to the AGM the composition of seven members of the Supervisory Board and election of three new members of the Supervisory Board;
- proposed to the AGM appointment of a statutory auditor for the period 2018-2020;
- appointed new members of the committees of the Supervisory Board;
- recalled three members of the Management Board;
- reduced the composition of the Management Board from seven to five members;
- appointed the new member of the Management Board to whom the term of office shall commence when the permission of the ECB will be issued;
- took note of the report on managing potential conflicts of interest situations identified with members of the Supervisory Board;
- acknowledged the ISP Group Report on remuneration;
- took note of the minutes of the committees of the Supervisory Board;
- examined and discussed the Credit and counterparty risk and risk control system report issued by the European Central Bank and monitored the follow-up to the ECB recommendations;
- examined the ICAAP Book;
- monitored the Bank's capital adequacy;
- took note of the reports of Banka Slovenije;
- adopted the Integrated Internal Control System Regulation in line with the Intesa Sanpaolo Group wide model;
- addressed other issues in accordance with powers conferred upon it under law and the Articles of Association.

In 2018, the composition of the Supervisory Board changed. The Extraordinary General Meeting of Banka Intesa Sanpaolo d.d. held on 9 May 2018 was informed that Mr Borut Bratina, PhD resigned from his position as member and deputy chairman of the Supervisory Board. On the same day Mr Alessio Cioni, Ms Andrea Pavlović and Mr Dražen Karakašić were elected. The Supervisory Board elected at its meeting held on 19 May 2018 Mr Alessio Cioni as the deputy chairman of the Supervisory Board.

The committees of the Supervisory Board, and more specifically: the Audit Committee, the Risk Committee and the Nomination Committee provided the Supervisory Board with substantive support in 2018. The Supervisory Board` s committees met regularly and discussed the topics within their respective competences and responsibilities.

The materials for the meetings were forwarded to the members of the Supervisory Board in compliance with the Rules of Procedures governing the discharging of the functions of the Supervisory Board and those functions were discharged in line with the aforementioned enactment. The Supervisory Board assesses that it had at its disposal timely and adequate data, reports and information, as well as additional clarifications and explanations when required at sessions it held, so as to be able to monitor throughout the financial year the Bank's operations with due attention, as well as the internal audit function and supervise the running of the Bank. In February 2019 the members of the Supervisory Board examined the extensive report on the performance and the results posted by the Bank in 2018, arising from the audited accounting statements.

The Supervisory Board hereby states that all its members have examined carefully the Annual Report, the Report of the Certified Auditor, Financial Statements, Notes to the Financial Statements, and other notes presented therein. Furthermore, the Supervisory Board assesses that the Annual Report of the Management Board gives a true and fair view of the business events and provide comprehensive information as to operations during the past financial year, and thus complements and expands the information already presented to the Supervisory Board in the course of the financial year. The Bank has safeguarded a high level of operational safety and effectively manages risks it is exposed to in the course of its day-to-day business. Therefore, the Supervisory Board has assessed that considering the circumstances under which the Bank conducted business, the Bank's management and performance were successful during the period under review.

Furthermore, the Supervisory Board also assessed that the work of the Internal Audit Department was well planned and effective, and supported the activities of the Management Board, Audit Committee and assisted the Supervisory Board when forming opinions and making assessments.

2. The position with regard to the Independent Auditor's Report

The Supervisory Board hereby concludes that the external auditor has expressed in the Auditor's Report an opinion in relation to the financial statements prepared by Banka Intesa Sanpaolo d.d. On this basis, the Supervisory Board hereby adopts the following

p o s i t i o n:

that the Supervisory Board has no objection to the Report of the auditor KPMG Slovenija, limited liability company.

3. Approval of the Annual Report for the financial year 2018

On the basis of the insight into operations carried out by the Bank in the course of the financial year and after due examination of the audited Annual Report and the unqualified opinion stated in the external auditor's report, the Supervisory Board hereby

a p p r o v e s a n d a d o p t s

The Annual Report of Banka Intesa Sanpaolo d.d. for the Financial Year 2018.

4. Approval of the proposal on profit appropriation

The members of the Supervisory Board have analysed the proposal regarding the appropriation of the balance-sheet profit. They have found the proposal for the adoption of the distributable profit, to be in line with the dividend policy of the Bank. After due examination of the proposal, the Supervisory Board hereby fully

a g r e e s

with the proposal of the Management Board on the appropriation of the profit.

5. Confirmation of the Report on the relations of the Bank with the controlling company and its affiliates for 2018

5.a. Position with regard to the Auditor's Report

The Supervisory Board hereby establishes that the external auditor in its report has given the following opinion regarding the Report on the relations of the Bank with the controlling company and its affiliates:

»Based on the procedures we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that the:
»Based on the procedures we have performed and the evidence we have obtained, nothing has come to our attention that causes us to believe that the:

- statements in the report on relations with affiliated companies for the financial year that ended 31 December 2018 are not accurate in all material respects;
- that the Company's execution of legal transactions stated in the Report was disproportionally high in view of circumstances that were known at the time when these transactions were performed;
- that circumstances exist that would in view of other actions mentioned in the Report indicate a significantly different assessment of the disadvantage from the one given by the management,

all by taking into account the above-mentioned criteria.«

The Supervisory Board hereby adopts the following

p o s i t i o n:

The Supervisory Board does not have any objection with regard to the Report of the audit firm KPMG Slovenija.

5.b. Statement of the Management Board of the Bank with regard to the Report on the relations of the Bank with the controlling company and its affiliates

The Management Board of Banka Intesa Sanpaolo d.d. with regard to the Report on the relations of the Bank with the controlling company and its affiliates has stated that Banka Intesa Sanpaolo d.d. in the circumstances known to it at the time when a legal transaction was carried out or abandoned, the Bank received adequate compensation and by the act of abandonment, it was not to its detriment. The Supervisory Board has no objection with regard to the Statement.

Based on the disclosures and information regarding the Bank's operations during the year under review and in-depth examination of the Report on the relations of the Bank with the controlling company and its affiliates and the unqualified opinion of the independent auditor, the Supervisory Board hereby

c o n f i r m s a n d a p p r o v e s

The Report on the relations of Banka Intesa Sanpaolo d.d. with the controlling company and its affiliates.

Koper, 19 February 2019

Chairman of the Supervisory Board
Uroš Čufer

3. BODIES OF CORPORATE GOVERNANCE

Supervisory Board

The Supervisory Board of Banka Intesa Sanpaolo d.d. is composed of seven members: the chairman as an independent expert, three are representatives of Privredna banka Zagreb d.d., and remaining three are representatives of Intesa Sanpaolo banking group.

In 2018, the composition of the Supervisory Board changed. On 9 May 2018, the Extraordinary General Shareholders Meeting of Banka Intesa Sanpaolo d.d. was informed that Mr Borut Bratina, PhD, resigned from his position as member and deputy chairman of the Supervisory Board. On the same day Mr Alessio Cioni, Ms Andrea Pavlović and Mr Dražen Karakašić were elected new members to the same body. At the meeting held on 19 May 2018 Mr Alessio Cioni was elected deputy chairman of the Supervisory Board.

Members of the Supervisory Board

As at 31 December 2018:	
Uroš Čufer	*Chairman*
Alessio Cioni	*Deputy Chairman*
Elena Breno	*Member*
Emanuele Collini	*Member*
Dražen Karakašić	*Member*
Andrea Pavlović	*Member*
Silvia Rinaldi	*Member*

Management Board

The Management Board of Banka Intesa Sanpaolo d.d. has four Members.

In 2018, the composition of the Management Board changed. Due to organisational changes number of the members of the Management Board was reduced. Term of office of three members of the Management Board, and namely: Aleksander Lozej, M.Sc., member of the Management Board responsible for the Human Resources and Organisation Department, Aleksander Milostnik, member of the Management Board responsible for financial area (but remaining at the Bank as CFO), and Rado Grdina, member of the Management Board responsible for the CCO Division terminated on 30 September 2018.

Members of the Bank's Management Board

As at 31 December 2018:	
Jozef Kausich	*President*
Irena Džaković	*Member*
Ivan Ivičić	*Member*
Drago Kavšek	*Member*

4. ECONOMIC AND BANKING ENVIRONMENT

In 2018, economic conditions in Slovenia had been improving for the fourth year in a row, however, growth was more steady than that in 2017. Construction investments by the state, municipalities and infrastructure companies, particularly in engineering structures, were significant contributing factors to the growth. High growth of activity in the service sector also had a positive impact. Unemployment continued to decrease, and an increase in salaries and social transfers was again recorded, which, together with a greater volume of consumer loans, contributed to the rise in household consumption in several segments. On the other hand, the share of the income saved by households continued to increase. The growth in exports continued with dynamics of growth being more moderate than in 2017. Apart from specific domestic factors, this is mainly due to the smaller growth in economic activity of Slovenia's main trading partners. The consequences of this are already evident in a slightly lower growth of Slovenian automotive industry and production growth slowed down also in most other industries, with the exception of technology-intensive industries. The current account surplus slowly started to decrease as the growth in goods exports eased somewhat more than the growth in goods imports.

In line with favourable economic trends, the conditions on the labour market continue to be favourable. The downward trend in the number of unemployed continues, however, the unemployment rate in the last months of the year was dropping at a steady pace. The number of unemployed persons registered at the end of December 2018 was 78,534, which is 7.7 % less than the year before. The growth in the number of persons in employment remains comparatively high, mostly on account of the growing inflow of foreign workers which is the result of companies encountering difficulties in finding suitable staff on the domestic labour market.

The annual inflation rate in 2018 stood at 1.4% (1.7% at the end of 2017). As private consumption continued to recover, the prices of goods and services rose further. The annual inflation rate is largely the result of increased prices of energy, telephone services and food.

In 2018, the fiscal position of the state continued to improve. Revenues increased primarily on account of increased tax revenues as well as social contributions, which can be attributed especially to favourable conditions on the labour market. Growth in non-tax revenues was considerably higher due to NLB dividends. Expenditure growth was significantly lower than revenue growth, the highest being in investments as a result of implementing EU projects.

Loans to the non-banking sector continued to rise in 2018. Lending activity strengthened the most in households segments as a result of improved conditions on the labour market, low interest rates and the rise in real estate prices. All forms of lending to households recorded growth with the largest increase being recorded in consumer loans. Housing loans increased at a stable rate as well. Loans to non-financial sector are still noticeably lagging behind the household segment both in growth rate and volume. The quality of banks' credit portfolio further improved. Banks continue reducing their non-performing exposures, which are rapidly decreasing in all segments of the credit portfolio.

Balance sheet liabilities show continued growth of deposits made by the non-banking sector also in 2018, despite the fact that interest rates on deposits remain at historically low levels. Deposits grew primarily in the household segment, while non-financial companies allocated the profits generated to current spending, financial restructuring and investing rather than saving. With low interest rates on deposits, the maturity of deposits continues to shorten, while the share of demand deposits is substantially on the increase.

Bank profitability has persisted for the fourth year in row. Bank profits exceeded those of the previous year on account of favourable trends in revenues, maintaining moderate operating costs and net reversal of impairments and provisions at the level of the entire banking system. The largest portion of the revenue of banks comes from net interest income. After a several-year-long downward trend in operating costs, the latter is gradually coming to an end due to the conditions banks have been facing in the most recent period (the needs for digitalisation and mandatory compliance with regulatory requirements).

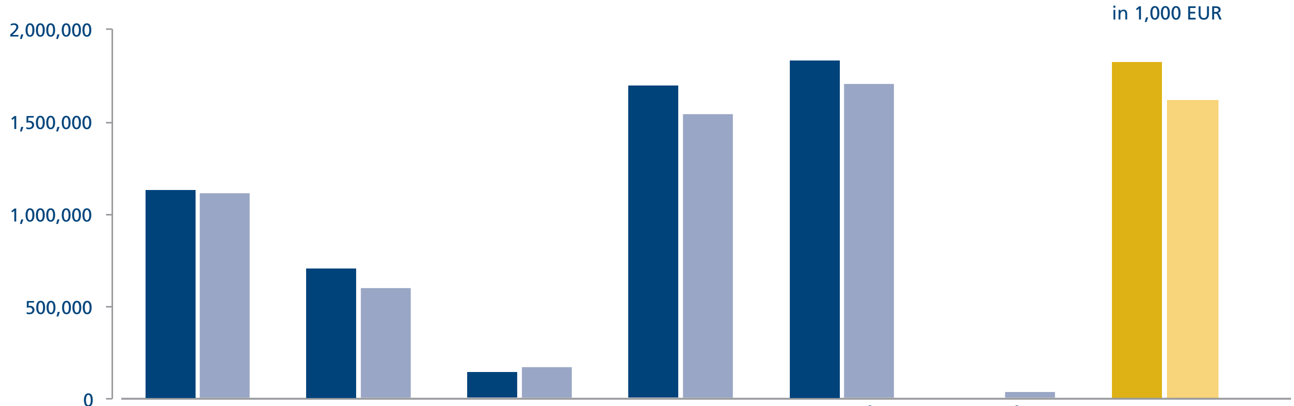
5. AN OVERVIEW OF THE BANK'S OPERATIONS IN 2018

5.1 LENDING OPERATIONS

Gross loans by Intesa Sanpaolo Bank to the non-banking sector increased by EUR 70.6 million in 2018 or 4.0% compared to 2017. The Bank's market share in lending to the non-banking sector grew by 25 basis points in 2018, thus achieving 7.9%.

In terms of currency, most loans are in domestic currency (99.9%), while long-term loans prevail in terms of maturity (92.5%). As for the maturity structure, the share of short-term loans decreased from 10.7% to 7.5%.

An overview of gross lending to the non-banking sector in thousands of euros



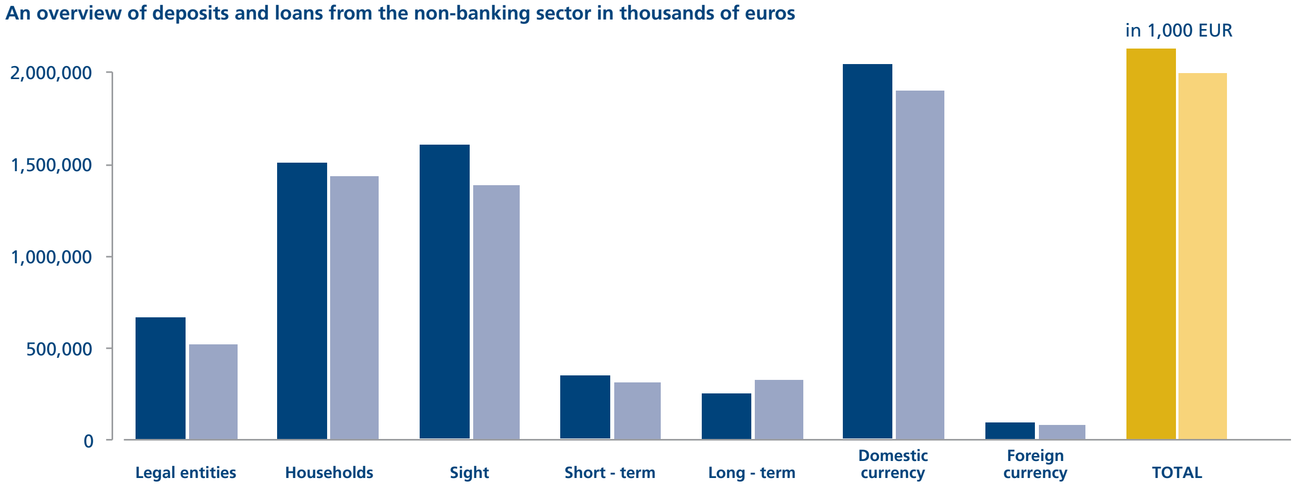
	Legal entities	Households	Short - term	Long - term	Domestic currency	Foreign currency	TOTAL
2018	1,137,443	708,392	139,125	1,706,711	1,843,329	2,507	**1,845,836**
2017	1,129,338	645,882	190,107	1,585,113	1,756,040	19,180	**1,775,220**

Loans to the corporate sector amounted to EUR 1,137.4 million or 61.6%, representing the largest portion of loans to the non-banking sector.

Lending to households (private individuals and sole proprietors) reached EUR 708.4 million or 38.4% of total lending to the non-banking sector. Lending to this customer segment increased by EUR 62.5 million or 9.7% on yearly basis. As in 2018, households mostly borrowed on a long-term basis, while borrowing in foreign currency remained on a low level. Most of long-term loans are mortgage loans. In 2018, the Bank increased its market share in the segment of private individuals and sole proprietors, which amounts to 6.8%. The market share in the segment of corporate clients also increased, from 8.4% to 8.8%.

5.2 DEPOSITS

An overview of deposits and loans from the non-banking sector in thousands of euros



	Legal entities	Households	Sight	Short - term	Long - term	Domestic currency	Foreign currency	TOTAL
2018	687,211	1,520,491	1,661,270	290,144	256,288	2,115,793	91,908	**2,207,702**
2017	512,228	1,459,268	1,418,671	265,959	286,866	1,889,969	81,527	**1,971,496**

In 2018, the Bank increased deposits and loans received from the non-banking sector by 12.0% or EUR 236.2 million, whereby the market share increased by 46 basis points to 7.6%, the market share of household deposits fell by 19 basis points and amounted to 7.8% at the end of 2018, and the market share of deposits by legal entities increased by 157 basis points, thus amounting to 7.2%.

The sight deposits account for a 75.3% share of total deposits and loans received from the non-banking sector. They are followed by short-term deposits (13.1%) and long-term deposits (11.6%). In terms of currency, deposits in domestic currency prevail with a 95.8% share. With respect to the previous year, demand deposits increased by 17.1% in 2018. Short-term deposits increased by 9.1%, while long-term deposits reduced by 10.7%.

The volume of the deposits placed by legal persons increased by 34.2% (by EUR 175.0 million) comparing with 2017. Also in 2018, the deposit structure in terms of currency was dominated by deposits denominated in euro.

Household deposits accounted for EUR 68.9 of all non-bank deposits and at the end of 2018 totalled EUR 1,520.5 million, i.e. EUR 61.2 million more year-on-year. Household deposits were mainly denominated in local currency.

5.3 OTHER SERVICES

5.3.1 Card operations

The Activa system

Some of the banks that are members of the Activa system launched the solution for mobile authentication of the card owners during online card purchases. Issuing contactless card products continued on an accelerated basis.

In the framework of the Activa system, future periods will see special attention being paid to the development of card products and services for simplifying operations.

Intesa Sanpaolo Bank

The Bank launched the possibility of payment by instalments using MasterCard card. The Bank also set up the SMS alert service for business card transactions and switched to issuing contactless cards for its entire card products portfolio.

Promotional activities focused mainly on acquiring new users of mobile banking and new owners of cards with deferred payment, both for personal and business use.

New products and services

In 2018, Intesa Sanpaolo Bank expanded and adapted its range of products and services for its clients based on their expectations, market conditions and legal requirements. The following stand out the most:

- Provision of payment by instalments using MasterCard cards,
- Provision of SMS alert for business cards,
- Redesign of the mobile banking application,
- Redesign of the Bank's website.

5.3.2 Marketing and sale of mutual investment funds

In 2018, interest rates on deposits persisted at low levels and in addition, capital markets were quite volatile. After a strong growth in January, the first correction ensued already in February. After that, markets recovered largely, but in the final quarter another downward correction followed which left most of the markets closing the year 2018 in red numbers. All this had a negative effect on investors and consequently on payments made into mutual funds. It follows from the Reports published by Slovenian asset management companies on the Securities Market Agency's website that the net outflows from Slovenian funds amounted to EUR 9.3 million in 2018. Funds held in Slovenian funds decreased by over 7% on account of negative trends in capital markets. According to the data provided by the Bank of Slovenia, mutual funds managed by foreign asset management companies also recorded net outflows of slightly less than EUR 11.3 million between January and October 2018.

Considering the above circumstances, the Bank completed 2018 with EUR 1.2 million of net payments in the foreign funds marketed by the Bank. The increase was also the result of the product called Great combination: a deposit with a better interest rate and payment in funds with lower costs.

In August 2018, the Bank discontinued marketing the funds of the Primorski skladi d.d. asset management company, therefore, as of the end of 2018, the Bank's offer now comprises the following funds:

- Eurizon Capital S. A. (14 mutual Eurizon Funds and 4 mutual Eurizon Manager Selection Funds)
- Franklin Templeton Investments S.A. (7 mutual Franklin Templeton Investment Funds).

Furthermore, the Bank also markets the funds of two Slovenian asset management companies:

- ALTA Skladi – 19 funds,
- KBM Infond – 21 funds,

The Moje finance magazine assessed the quality of the mutual funds marketed by the Bank for the 8th consecutive year. According to them, the foreign mutual funds marketed in Slovenia by the Bank won best fund awards.

In 2018, the Bank put a large emphasis on marketing saving plans, i.e. monthly payments into the mutual funds. There were a little less than 2,000 new savings plans made in 2018 thus totaling in over 4,000 saving plans provided by the Bank.

In 2018, the Bank also began offering the new service of investment counselling which involves personal recommendations at the request of a customer or at the initiative of the Bank relating to one or several transactions in financial instruments. 475 contracts on investment services were concluded in this respect in 2018.

5.3.3 Leasing

The Finor leasing Office, which is part of the SME network, specialises in the sale of financial leasing throughout Slovenia, both for natural persons and legal entities.

In 2018, 580 leasing contracts were made in the total value of EUR 23.0 million. The most (278 contracts valued at EUR 11.7 million) were made for commercial vehicles, followed by passenger cars (212 contracts valued at EUR 5.3 million), production and other equipment (75 contracts valued at EUR 4.2 million), real estate (6 contracts valued at EUR 1.0 million) and vessels (9 contracts valued at EUR 0.8 million).

Compared to 2017, the Office increased the volume of investments in 2018 by 26.3%.

5.3.4 Open-ended mutual pension funds by Intesa Sanpaolo Bank

The Bank is actively involved in the voluntary pension insurance system within the scope of the Slovenian pension system, as it established and started managing the Banka Koper d.d. open-ended mutual pension fund (OVPS) back in 2001. The fund is intended for collective and individual voluntary supplementary pension insurance.

In 2018, the Bank upgraded its offer on voluntary supplementary pension insurance. It launched to the market a new type of saving for old age in the form of a life cycle investment policy. The Bank offers such form of a life cycle investment policy through the management of the Moj Steber fund of pension funds.

The Moj Steber fund consists of three sub-funds:
- Moj Steber Dynamic, intended for insured persons aged 40 or less,
- Moj Steber Balanced, intended for insured persons aged between 40 and 55,
- Moj Steber Guaranteed, intended for insured persons aged 55 or more.

Such a form of investment policy of the fund of pension funds with various investment policies intended for different age categories is called the life-cycle investment policy and is an extended investment strategy method in developed economies. Its horizon of saving is long and is intended for acquiring additional funds for the disbursement of a supplementary pension after an insured person retires.

It provides the younger insured persons with a riskier, share-oriented investment. With the ageing of insured persons and their approaching retirement, the level of risk reduces up to the last and lowest risk level, where insured persons are, as before, again part of a guaranteed pension sub-fund and its members until they choose the supplementary pension payer or, rather, until they retire.

The performance of the Moj Steber fund of pension funds was characterised by a great uncertainty in the global capital markets in 2018 (tensions due to the trade war, Brexit, the cooling of European economies, etc.)

The value of the Moj Steber Guaranteed sub-fund unit amounted to EUR 9.57 as at 31 December 2018 and decreased by 1.58% within a year, thus falling below the guaranteed return, which amounted to 0.61% in 2018. The 5-year return rate of the Moj Steber Guaranteed sub-fund amounted to 10.8% as at 31 December 2018, while the value of unit grew by 129.4% from the establishment of the sub-fund to 31 December 2018.

As at 31 December 2018, the Moj Steber fund of pension funds disclosed total assets amounting to EUR 42.6 million, which is a 1.0% increase with respect to the end of 2017. The increase is primarily the result of somewhat higher net payments into the fund of pension funds compared to net cash outflows. Despite the fact that tax treatment does not encourage exceptional withdrawal from the second pillar compared to regular withdrawal, exceptional withdrawals (single disbursement) from the second pillar continue to prevail over regular withdrawals (supplementary pension). A positive trend in the use of the assets saved in the form of a supplementary pension – a rent – was noticed in 2018.

At the end of 2018, Moj Steber fund of pension funds included 6,411 insured persons, 5,939 of whom were included in collective voluntary supplementary pension insurance, while 574 were individually insured persons.

5.3.5 Depositary banking

Banka Intesa Sanpaolo d.d. was the first bank in Slovenia that provided depositary services for investment funds in 2004. Since then, the Bank has obtained a great deal of knowledge and experiences. The provision of depositary services is a very responsible task, since the accuracy of items in the funds' books of account need to be checked on a daily basis, along with the accuracy of net asset value and unit value calculation, conversion of payments in the funds, claims for disbursement, and investment compliance with the provisions of investment policy.

All assets of investment funds are held in accounts opened by the custodian in the name and for the account of the individual fund – the owner. The custodian is responsible for the assets and for compliance of the investment fund's operations with the provisions of the prospectus, taking over the responsibility and concern for investors.

To ensure that administrative tasks are always performed at the highest levels, the acquired knowledge and experience are upgraded also through their exchange between banks within the Intesa Sanpaolo Group. This gives the Bank a competitive edge in the market and represents added value for its customers.

In 2018, the procedures for the provision of depositary services were in line with the amendments to the Slovenian legislation, which incorporated the provisions of the EU Directive governing the method of implementation of depositary services, and new depositary contracts were harmonized and concluded with the existing customers.

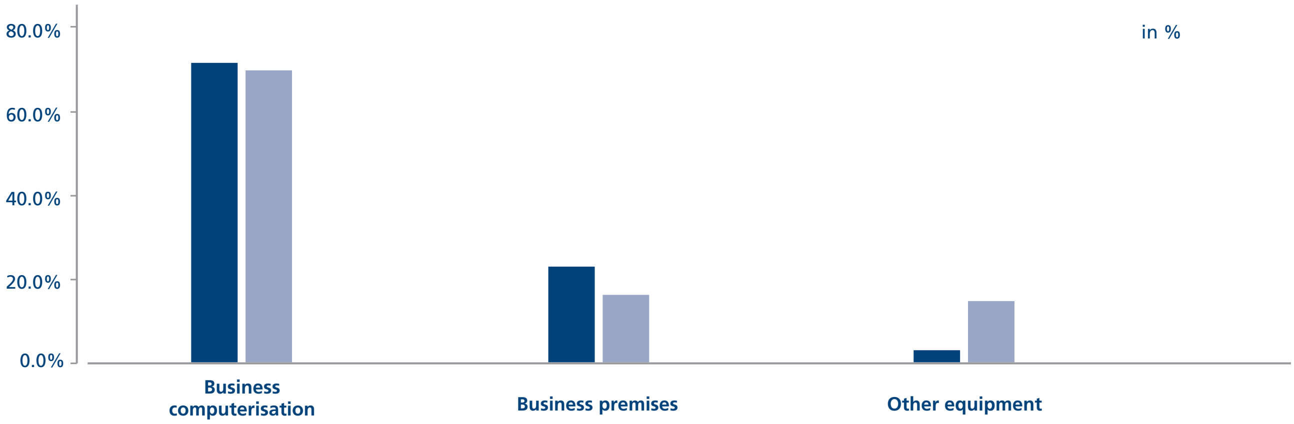
At the end of 2018, the Bank rendered depositary services for mutual funds (UCITS), pension funds and internal funds at insurance companies. At the end of the year the volume of assets under custody totalled close to EUR 0.8 billion.

6. THE BANK'S ORGANIC GROWTH AND DEVELOPMENT

6.1 CAPITAL INVESTMENTS

Also in 2018, Banka Intesa Sanpaolo d.d. continued pursuing its long-term development programme and invested EUR 1.6 million in the computerisation of business operations, commercial premises and other equipment. Bank's capital investments in 2018 were higher by 50.6 per cent or EUR 0.5 million compared to the previous year.

Structure of capital investments in 2018



	Business computerisation	Business premises	Other equipment
2018	71,5%	25,1%	3,4%
2017	68,9%	16,4%	14,7%

The majority of investments (EUR 1.1 million or 71.5%) was allocated to business computerisation. Increasingly stricter requirements regarding banking safety require yearly investments in ensuring the safety of services.

In comparison with 2017, more funds were invested in business premises. The Bank allocated EUR 0.4 million or 25.1% of total investments for renovation and rearrangement of business premises into a modern banking service and for the design of its branches pursuant to the corporate identity of the banking group, especially branches in Koper, Ljubljana and Maribor.

6.2 INFORMATION TECHNOLOGY AND TECHNOLOGICAL DEVELOPMENT

As regards business solutions in 2018, the Bank renewed its mobile banking – Banka IN and introduced additional functionalities for both legal and natural persons. The Bank continued activities in the optimisation of key business processes, namely in the areas of payment transactions(development of real-time payment services in Slovenia and within the Intesa Sanpaolo Group, completion of implementation of the »Cash management«functionality), electronic data exchange and paperless operations. In addition, the Bank started the project of renovation of branch offices and introduction of an advanced model of operations with clients and has already successfully completed it in some branch offices. The project will continue in 2019.

Pursuant to Mifid regulations the Bank implemented the »Wealth Shaper« app support for carrying out investment counselling processes. The investment counselling process includes the identification of an investor profile, an analysis of the current profile, presentation of a recommended portfolio, preparation of an offer, execution of orders and after-sale activities.

The Bank has improved the level of services and customer satisfaction, and optimised loan and credit line approvals / overdafts for certain customer segments and for certain products.

In the area of **risk management,** the Bank started implementing internal ratings for small enterprises. As regards operational risks, the Bank, it renewed the internal network and introduced additional elements of data protection, implemented a new »data centre«architecture in Slovenia pursuant to the requirements of the parent bank and provided the availability of all critical systems of the Bank in case of failure of the entire primary location.

In **regulatory affairs and compliance** in 2018, in accordance with the requirements of the EU General Data Protection (GDPR) Regulation, the Bank implemented appropriate organisational and information procedures. It also started implementing the PSD2 (Revised Payment Service Directive) project and established reporting to the regulator in accordance with regulations as well as implemented other reporting requirements.

As regards **information security,** the Bank set up additional levels of information system security in accordance with the guidelines provided by the parent bank and implemented the SWIFT security requirements. It introduced a solution to protect against advanced information attack (Advanced Threat Prevention) and started to provide support for detecting and preventing abuses in the area of online and mobile banking services.

7. ACTIVITIES IN THE FIELD OF SUSTAINABLE DEVELOPMENT

The Intesa Sanpaolo Bank Code of Ethics presents the management guidelines and key values that represent the basis for the Bank's compliant operations. As a corporate entity, the Bank must be aware that its operations extend further than simply satisfying the financial needs of its customers and have a significant impact on the wider local community. The goals and values written in the code raise the level of the employees' operating compliance and make it easier to earn the trust of stakeholders, i.e. customers, shareholders, employees, suppliers and the local community.

In accordance with the principles of the Code of Ethics and the ISO 26000 standard, the Bank performed an assessment of compliance also in 2018. While the areas of assessment in 2017 were employee relationships, indirect impact on the environment, anti-corruption, as well as financial inclusion and accessibility to financial services, in 2018 we assessed the quality and innovation regarding customer relationships, responsible management of savings, the direct impact on the environment and the local community.

By carrying out this assessment each year the Bank aims to identify any deficiencies that could represent a risk to its reputation, while also obtaining more detailed information and findings that are important for non-financial reporting. The annual assessment is performed by Bureau Veritas, an international certification company.

7.1 RESPONSIBILITY TOWARDS EMPLOYEES

7.1.1 Training programmes

Systematic training provides the basis for employee development at the Bank. In 2018, there were 11,284 hours of training realised altogether, which is an average of 20.84 hours per employee. Most, 85.5 %, of all training was in-house training. In-house lecturers carried out no less than 41% of very effective training, while the rest was provided by external lecturers and by means of e-learning tools.

The year 2018 was marked by the entry into force of the General Data Protection Directive (GDPR) of the EU, which brought about the adjustment of all processes and thus extensive staff training. The Bank also devoted special attention to employee training in relation to consumer lending.

Ensuring uninterrupted and safe operation in 2018 required constant awareness-raising of all employees about the importance of preventing money laundering and terrorist financing and the compliance of the Bank's entire operations.

An important part of educational content referred to the introduction of the new development strategy for the 2018-2021 period. The employees familiarised themselves with the new business model and innovative ways of doing business both in branches and through digital channels.

7.1.2 Development of key personnel

In key personnel development, training activities continued within the scope of the three-year Talent Management Programme for the commercial segment. The programme is consistent with the business guidelines of the Bank and designed for young employees with identified development potential in sales.

In 2018, the candidates participating in seven substantive training modules developed competencies defined by the Bank for this particular staff group.

7.1.3 Concern for and dialogue with employees

The implementation of the new business strategy entails radical changes in numerous areas of the Bank's operations and the reorganisation of work processes. The Bank complies with the principles of the Code of Ethics, and it again ensured proper communication of changes and regular informing of its employees via internal channels. In developing relations with its employees, the Bank relentlessly pursues the values of trust, equity and cooperation, thus contributing to more efficient cooperation and a more uniform working environment.

7.2 RESPONSIBILITY TOWARDS CUSTOMERS

The Bank is aware that its customers must always be the focus of their attention and that only by have an open and continuous dialogue can meet their expectations, learn about new habits and maintain excellent interpersonal relationships. The Bank listens to its customers in a variety of ways, as well as on the basis of comments and suggestions, and adapts the way it operates to the needs of specific target groups. Customers can express their comments and suggestions using the website, submit them at designated places in the branches or directly through Bank's consultants. An important overview of customer satisfaction is also got through our annual Customer Satisfaction Retail Benchmarking Survey, where the Bank consistently achieves good results.

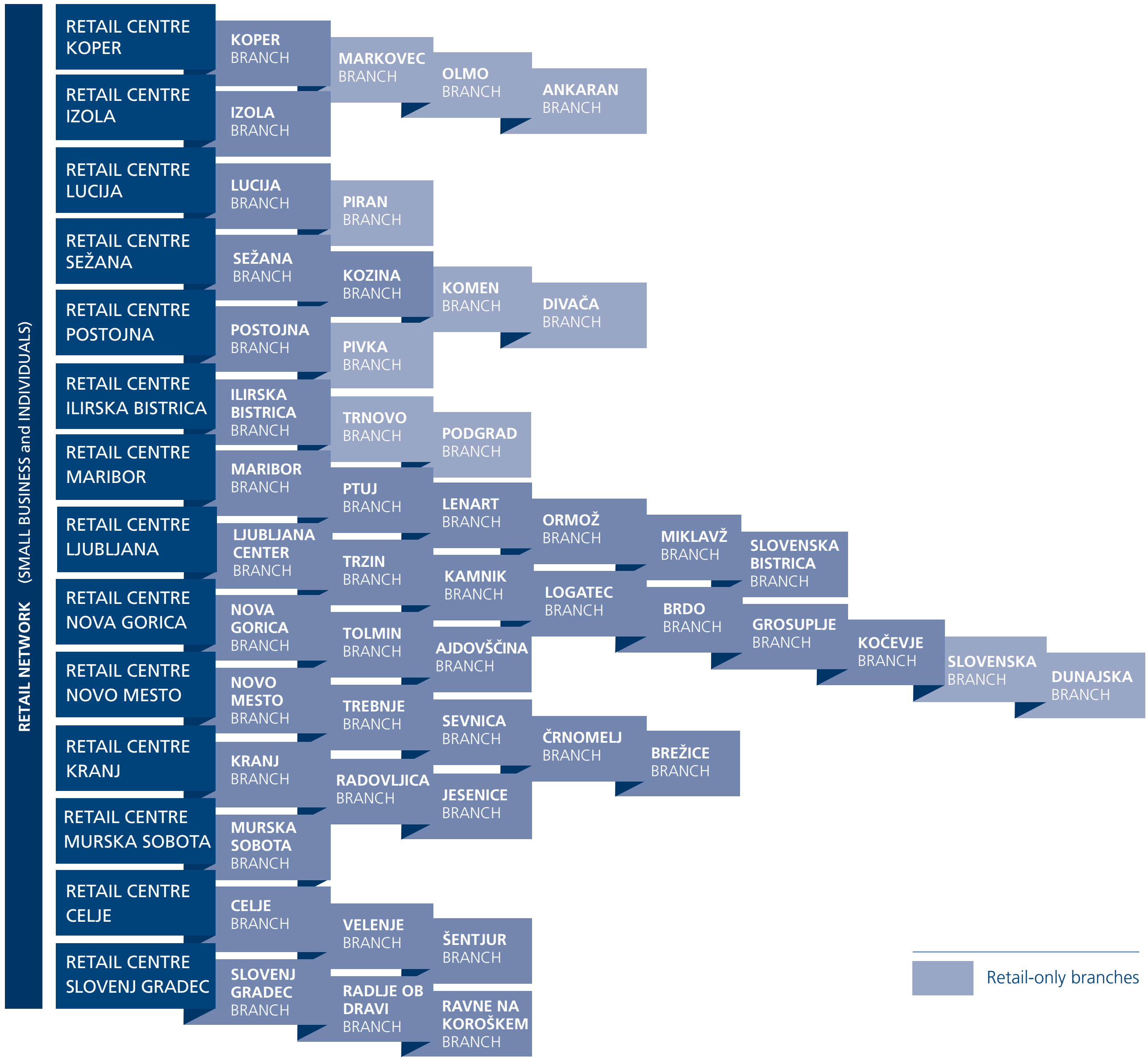
At the start of 2018, the Bank took a further step in its relationship with its customers. It presented its new 2018-2021 Business Plan where it uses simplified and more agile business model, making it easier to adapt to new customer needs and expectations, as well as the increasingly quick advances in technology. The new means of business provides customers with an even better experience than before, as the renovated branches, new approach and variety of new tools are entirely aimed at ensuring customer satisfaction. The business plan also foresees the opening of a new business centre in Ljubljana. Having its headquarters in Slovenia's central region will mean that it will be easier for the Bank to obtain new customers and consolidate its position in other regions of Slovenia.

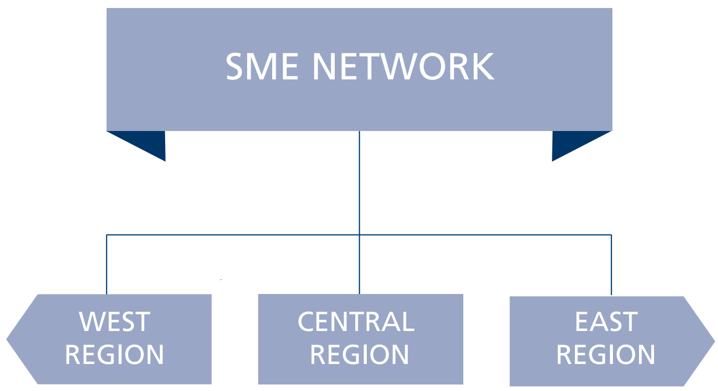
7.3 CORPORATE SOCIAL RESPONSIBILITY

One of the values of Intesa Sanpaolo Bank is also caring for the local environment in which, as a large corporate entity, it plays an important role. It places great value on the protection of historical, artistic and cultural heritage as well as good interpersonal relationships, which are nurtured by many cultural, tourism, sports societies and charities. The Bank realises its responsibility through various donations and sponsorships that represent an important source of income for voluntary organisations. To show its support of the local community the Bank have donated over EUR 50 thousands which were able to support a large number of projects and initiatives.

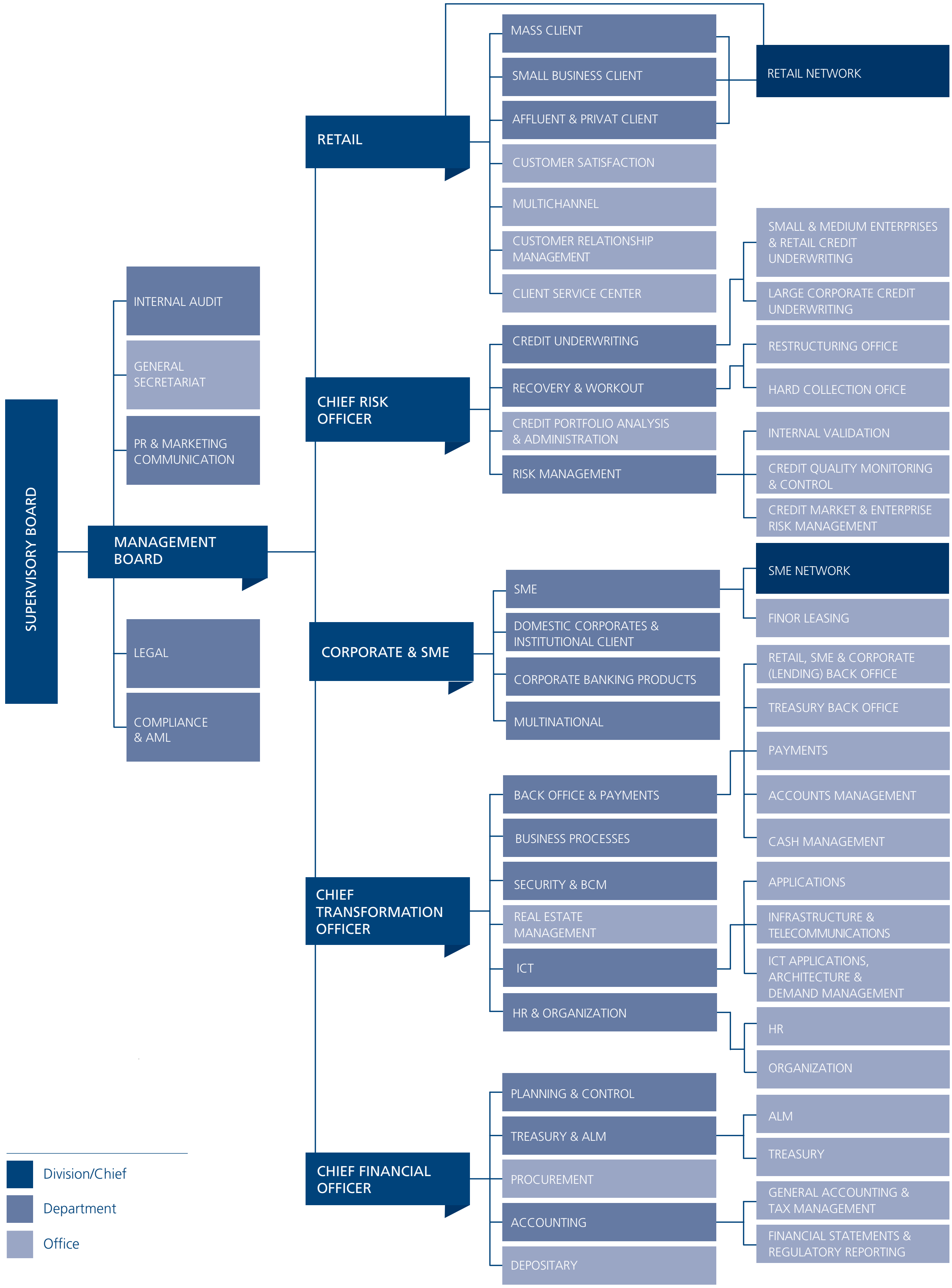
The Bank has not prepared the Non financial statement as required by the Non Financial Information Legislation availing of the exemption introduced by the local regulation, as being a subsidiary undertaking which information are included in the Consolidated non financial statement presented by Intesa Sanpaolo S.p.A.

8. TERRITORIAL CHART OF COMMERCIAL UNITS





9. INTERNAL ORGANISATION CHART



10. THE CORPORATE GOVERNANCE STATEMENT OF BANKA INTESA SANPAOLO D.D.

The corporate governance statement of Banka Intesa Sanpaolo d.d.

In accordance with the fifth paragraph of Article 70 the Companies Act – ZGD-1 (Official Gazette of the Republic of Slovenia, No. 55/2015), Banka Intesa Sanpaolo d.d., gives the following

Corporate governance statement

The corporate governance statement is an integral part of the annual report for 2018 and it is available on the website of the company http://www.intesasanpaolobank.si/.

1. The corporate governance code which Banka Intesa Sanpaolo d.d. decided to use

Banka Intesa Sanpaolo d.d. hereby declares that for governance it observes the effective legislation, regulations, other legislative and secondary legislative acts and internal rules and instructions.

The company has the two-tier system of governance under which the company is run by the management board; its operations are supervised by the supervisory board. The bodies of the company are the general meeting of shareholders, the supervisory board and the management board.

2. Deviations from corporate governance codes

Banka Intesa Sanpaolo d. d. for governance does not deviate from the regulations stated in the first point of this corporate governance statement. Banka Intesa Sanpaolo d.d. does not use any special corporate governance codes, since in that segment it is bound by the codes of the parent bank. Of very high importance for its operations also with regard to governance of the company are the following internal acts:

- Code of Ethics of Banka Intesa Sanpaolo d.d. (http://www.intesasanpaolobank.si)
- Code of Conduct in Banka Intesa Sanpaolo d.d.

3. The description of the principal characteristics of internal control and corporate governance systems in the company in connection with the financial reporting procedure.

With the aim of ensuring appropriate financial reporting procedures Banka Intesa Sanpaolo d.d. pursues the Rules of procedure on accounting and accounting policies of the group. Accounting control in the broader sense is provided through the system of internal controls. It shall encompass adequate and effective internal controls, its implementation and monitoring. Internal controls system covers all significant risks to which the bank is exposed and includes checking of administrative and accounting procedures, verification of bank´ s compliance with applicable legislation, standards, codes and internal rules and verification of information security. The descriptions of business processes including control activities for mayor areas of bank´ s business, namely landing, accepting deposits, current accounts and trading business are laid down. The processes related to financial reporting or composition of financial statements (daily and monthly closing of the general ledger) are also set out.

The principal identified risks in this area are managed with an appropriate system of authorisations, delimitation of duties, compliance with the accounting rules, documenting of all business events, the custody system, posting on the day of a business event, inbuilt control mechanisms in source applications and archiving pursuant to the laws and internal regulations. With an efficient controlling mechanism in the area of accounting reporting, the bank ensures:

- a reliable decision-making and operational support system,
- accurate, complete and timely accounting data and the resulting accounting and other reports of the Bank, and
- compliance with legal and other requirements.

In compliance with the Banking Act the independent Internal Audit Department is established. The Internal Audit Department performs the tasks of internal auditing and reports on its proceedings to the corporate bodies of the bank.

Risk management at is implemented in accordance with the banking legislation, guidelines of the parent bank and internal policies and procedures in which are laid down the principles and guidance of risk management.

The master business strategy, accepted principles of the bank´ s propensity to assume risk which include the monitoring of risk profile and of specific risks, internal policies of risk management, approved by the bank´ s Management Board and Supervisory Board lay down the objectives and the guidelines concerning the taking of risk and the methods and criteria of risk management.

4. The data on principal shareholders

The data on major direct and indirect ownership of the securities issued by Banka Intesa Sanpaolo d.d. within the meaning of achieving qualifying holding as specified in the Takeover Act.

The ownership structure of Banka Intesa Sanpaolo d.d.

Equity holding in per cent

Shareholders	31.12.2018	31.12.2017
Privredna banka Zagreb d.d.	51.0%	51.0%
Intesa Sanpaolo S.P.A.	48.1%	48.1%
Minority shareholders	0.9%	0.9%

5. The data on the holders of securities that give special controlling rights

As at 31.12.2018, no security issued by Banka Intesa Sanpaolo d.d. gives any special controlling rights.

6. The data on restrictions on voting rights

In relation to the shares issued by Banka Intesa Sanpaolo d.d., as at 31.12.2018, there are no restrictions on voting rights.

7. Information on the appointment or replacement of members of the management or supervisory bodies and amendments to articles of association

In accordance with the provisions laid down in the articles of association of Banka Intesa Sanpaolo d.d., in the text in force as of 31.12.2018, the members of the supervisory board are elected by simple majority and discharged by the general meeting of shareholders with a two-thirds vote of the represented share capital. The management board is appointed and dismissed by the supervisory board with simple majority of votes. The general meeting of shareholders decides on amendments to the articles of association with a two-thirds vote of the represented share capital.

8. Information on authorisations to the members of management

The members of management do not have any special authorisations.

9. Information on the general meeting of shareholders of Banka Intesa Sanpaolo d.d.

In accordance with the provisions of the Companies Act (ZGD-1), the general meeting of shareholders is the ultimate body of the company. The shareholders exercise their management rights in matters of the company at the general meeting of shareholders of the company, where they pass fundamental and statutory resolutions. Convening the general meeting of shareholders is regulated by the articles of association of the company in accordance with effective legislation. The general meeting of shareholders is convened by the management board on its own initiative, at the request of the supervisory board or at the request of the shareholders of the company that represent at least 5% of the share capital of the company. The management board convenes the general meeting of shareholders of the company no less than one month before the meeting. The right to attend the general meeting of shareholders of the company is granted to all the shareholders registered in the shareholder's register as shareholders of the company at the end of the fourth day prior to the general meeting of shareholders, as well as to their proxies and authorised persons, and who apply to the company to attend the meeting no later than at the end of the fourth day prior to the general meeting of shareholders.

At the general meeting of shareholders of Banka Intesa Sanpaolo d.d. held on 12.06.2018, the shareholders were notified of the annual report of the company for the financial year 2017, the opinion of the independent auditor to the annual report, the report of the supervisory board to the annual report and remuneration of the members of the management board and of the supervisory board in 2017. The shareholders passed the resolution on the distribution the accumulated profit and gave discharge to the management board and to the supervisory board.

10. The data on the composition and functioning of the management or supervisory bodies and their committees

The supervisory board

The supervisory board of Banka Intesa Sanpaolo d.d. is composed of seven members of which one is an external expert, three are representatives of Privredna banka Zagreb d.d., and remaining three are representatives of the Intesa Sanpaolo banking group.

In 2018, the composition of the Supervisory Board changed. The Extraordinary General Meeting of Banka Intesa Sanpaolo d.d. held on 9 May 2018 was informed that Mr Borut Bratina, PhD, resigned from his position as member and deputy chairman of the Supervisory Board. On the same day Mr Alessio Cioni, Ms Andrea Pavlović and Mr Dražen Karakašić were elected. The Supervisory Board elected at its meeting held on 19 May 2018 Mr Alessio Cioni as the deputy chairman of the Supervisory Board.

The members of the Supervisory board as of 31.12.2018 are:

Uroš Čufer	*Chairman*
Alessio Cioni	*Deputy chairman*
Elena Breno	*Member*
Emanuele Collini	*Member*
Dražen Karakašić	*Member*
Andrea Pavlović	*Member*
Silvia Rinaldi	*Member*

There were three committees of the supervisory board at the bank at the end of 2018: the Audit Committee, the Risk Committee and the Nomination Committee.

Audit Committee

The members of the Audit Committee as of 31.12.2018 are:

Dražen Karakašić	*Chairman*
Elena Breno	*Member*
Andrea Pavlović	*Member*

Risk Committee

The members of the Risk Committee as of 31.12.2018 are:

Andrea Pavlović	*Chairman*
Elena Breno	*Member*
Emanuele Collini	*Member*

Nomination Committee
The members of the Nomination Committee as of 31.12.2018 are:

Uroš Čufer	*Chairman*
Alessio Cioni	*Member*
Silvia Rinaldi	*Member*

Description of the diversity policy implemented concerning participation in the management and supervisory bodies

The Nomination Committee is responsible for selecting and recommending candidates for members of the Management Bodies to the Supervisory Board, or to the Bank's General Meeting of Shareholders respectively.

When selecting and recommending the candidates, the Nomination Committee shall assure the aim of achieving the diversity within the Management Body, including the appropriate representation of both genders, is being followed as much as possible.

To contribute to appropriate representation of both genders, the Nomination Committee shall take into consideration the following quotas of underrepresented genders:
- Supervisory Board: 1/5 of the total composition, but at least 1 representative of the underrepresented gender;
- Management Board: at least 1 representative of the underrepresented gender.

The management board

As at 31.12.2018 the management board of Banka Intesa Sanpaolo d.d. comprised four members.

In 2018, the composition of the Management Board changed. Due to the organisational changes in the bank the number of the members of the Management Board was reduced. The term of office of three members of the Management Board, and namely: Aleksander Lozej, M.Sc., member of the Management Board responsible for operating of the Human Resources and Organisation Department, Aleksander Milostnik, member of the Management Board responsible for financial area (but remaining as CFO), and Rado Grdina, member of the Management Board responsible for the CCO Division terminated on 30 September 2018.

Members of the Bank's Management Board as at 31 December 2018:

Jozef Kausich	*President*
Irena Džaković	*Member*
Ivan Ivičić	*Member*
Drago Kavšek	*Member*

Koper, 19 February 2019

Supervisory board of Banka Intesa Sanpaolo d.d.

Management board of Banka Intesa Sanpaolo d.d.

Financial Report 2018

Independent auditors' report on financial statements

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SI-1000 Ljubljana

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Independent Auditor's Report

To the owners of Banka Intesa Sanpaolo d.d.

Report on the Audit of Financial Statements

Opinion

We have audited the financial statements of Banka Intesa Sanpaolo d.d. ("the Bank), which comprise the statement of financial position as at 31 December 2018, the income statement and the statements of other comprehensive income, cash flows, and changes in equity 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 the International Financial Reporting Standards as adopted by the European Union ("IFRS as adopted by the EU").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs) and EU Regulation (EU) No 537/2014. Our responsibilities under those standards are further described in the *Auditor's Responsibility for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with both the International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements that are relevant to our audit of the financial statements in Slovenia, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

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

Key Audit Matters

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

KPMG

Impairment of loans to non-bank customers	
As at 31 December 2018, loans to non-bank customers amount to EUR 1,757,088 thousand (31 December 2017: EUR 1,675,027 thousand), related impairment allowance amounts to EUR 87,865 thousand (31 December 2017: EUR 100,193 thousand) and impairment loss recognized in the income statement amounts to EUR 12,031 thousand (2017: EUR 18,295 thousand). We refer to the financial statements: Note 2.4 Financial assets and liabilities, Note 2.4.7 Impairments, Note 3.3 Credit risk, Note 16 Impairments and Note 27 Loans to non-bank customers.	
Key audit matter	**How the matter was addressed in our audit**
Impairment allowances represent the Management Board's best estimate of the expected credit losses within the loans and receivables at the reporting date. We focused on this area as the determination of impairment allowances requires significant judgment from the Management Board over both the timing of recognition and the amounts of any such impairment. Additionally, as at 1 January 2018, the Bank applied the new financial instruments standard, IFRS 9 *Financial Instruments*, whose impairment requirements are based on the expected credit loss (ECL) model rather than the incurred loss model, as previously used. The new model uses a dual-measurement approach, under which the impairment allowance is measured as either 12-months expected credit losses or lifetime expected credit losses, depending on whether there has been a significant increase in credit risk since initial recognition. Following the initial application of the new standard, impairment allowances for performing exposures (Stage 1 and Stage 2 in the IFRS 9 hierarchy) and non-performing exposures (Stage 3) below EUR 0.25 million individually (together "collective impairment allowance") are determined by modelling techniques. Historical experience, identification of exposures with a significant deterioration in credit quality, forward-looking information and management judgment are incorporated into the model assumptions. The Bank is continuously recalibrating the model parameters which also requires our increased attention in the audit.	Our audit procedures in this area included, among others: – Inspecting the Bank's new ECL impairment provisioning methodology and assessing its compliance with the relevant requirements of the new standard. As part of the above, we challenged the Management Board on whether the level of the methodology's sophistication is appropriate based on an assessment of the entity-level and portfolio-level factors; – Making relevant inquiries of the Bank's risk management and information technology (IT) personnel to obtain an understanding of the provisioning process, IT applications used therein, key data sources and assumptions for data used in the ECL model. Also, assessing and testing of IT control environment for data security and access, assisted by our own IT specialists; – Testing the design, implementation and operating effectiveness of selected key controls over the approval, recording and monitoring of loans and receivables, including, but not limited to, the controls relating to the identification of loss events and default, appropriateness of classification of exposures between performing and non-performing and their segmentation into homogenous groups, calculation of days past due and calculation of the impairment allowances;

For non-performing corporate exposures exceeding EUR 0.25 million individually, the impairment assessment is based on the knowledge of each individual borrower and often on estimation of the fair value of the related collateral. Related impairment allowances are determined on an individual basis by means of a discounted cash flows analysis. For the above reasons, impairment of loans and receivables from non-bank customers was considered by us to be a significant risk in our audit, which required our increased attention. Accordingly, we considered the area to be our key audit matter.	With respect to the impairment accounting under the new standard: – Understanding the overall transition process activities and controls, including the process and controls over determining the impact as well as the underlying process activities that generated the related disclosures; – Assessing whether the definition of default and the new standard's staging criteria were consistently applied; – With the assistance of our own financial instruments specialist, evaluating the overall modelling approach of calculation of ECLs, including the calculation of main risk parameters and macroeconomic factors (probability of default (PD), loss given default (LGD) and exposure at default (EAD)); – Performing an analysis of the ECL-based impairment allowances as at the new standard's initial application date, by comparing them to those calculated at that same date in accordance with the previous standard, and assessing their reasonableness based on inquiries of the credit risk management personnel. For impairment allowances that are calculated individually: – Selecting a sample of individual exposures, with focus on those with the greatest potential impact on the financial statements due to their magnitude and risk characteristics, as well as lower value items, which we independently assessed as high-risk, such as watchlisted, loans to clients operating in higher risk industries, non-performing exposures with low provision coverage – For the sample selected, critically assessing, by reference to the underlying documentation (loan files) and through discussion with the loan officers and credit risk management personnel, the existence of any triggers for classification to Stage 2 or Stage 3;

	– For those loans where triggers for classification in Stage 3 were identified, challenging key assumptions applied in the Bank's estimates of future cash flows used in the impairment calculation, such as discount rates and collateral values, where relevant, with the assistance of our own valuation specialists; For collective impairment allowance: – Testing the underlying impairment models, assessed as significant; – Obtaining the relevant forward-looking information and macroeconomic forecasts used in the Bank's ECL assessment. Independently assessing the information by means of corroborating inquiries of the Management Board; – Challenging LGD and PD parameters, assessed as significant, by performing back-testing of historical default and by reference to historical realized losses on defaults; – For a sample of exposures, assessing the appropriateness of the staging; – For a sample of exposures tested collectively, assessing the application of the measurement models applied and checking that the impairment rates applied complied with those provided for in such models; – Critically assessing the rationale for the changes made to the model parameters in 2018, by reference to our understanding of the business, current economic trends and market practices. Critically assessing the overall reasonableness of the impairment allowances, including both the share of the gross non-performing exposure in total gross exposure and the non-performing loans provision coverage; Evaluating the accuracy and completeness of the financial statement disclosures relating to the adoption of the new standard.

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Other Information

Management is responsible for the other information. The other information comprises the Business Report included in the Annual Report, but does not include the financial statements and our auditor's report thereon. Other information was obtained before the date of issuance of the auditor's report, except for the Report from the Management board and Minutes of the Supervisory Board's meeting on the adoption of the Annual report of the Banka Intesa Sanpaolo d.d. for the year ended 31 December 2018.

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

In connection with our audit of the financial statements, our responsibility is to read the other information 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.

With respect to the Business Report, we considered whether the Business Report includes the disclosures required by the Company's Act (hereafter referred to as "the applicable legal requirements").

Based solely on the work required to be undertaken in the course of the audit of the financial statements and the procedures above, in our opinion:

- the information given in the Business Report for the financial year for which the financial statements are prepared, is consistent in all material respects with the financial statements; and
- the Business Report has been prepared in accordance with the applicable legal requirements.

In addition, in light of the knowledge and understanding of the Bank and its environment in which it operates, obtained in the course of our audit, we are required to report if we have identified material misstatements in the Business Report and other information that we obtained prior to the date of this auditors report. We have nothing to report in this respect.

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

Management is responsible for the preparation of the financial statements that give a true and fair view in accordance with the IFRS as adopted by the EU, 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 of the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

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

Auditor's Responsibility for the Audit of 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 and with EU Regulation (EU) No 537/2014 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 skepticism 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.

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

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

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Report on Other Legal and Regulatory Requirements

We were appointed by shareholders of Banka Intesa Sanpaolo d.d. on shareholders meeting dated 12 June 2018 to audit the financial statements of Banka Intesa Sanpaolo d.d. for the year ended 31 December 2018. Our total uninterrupted period of engagement is 7 years, covering the periods ending 31 December 2012 to 31 December 2018.

We confirm that:

- our audit opinion is consistent with the additional report presented to the Audit Committee of the Bank dated 13 February 2019;
- we have not provided any prohibited non-audit services (NASs) referred in Article 5 of EU Regulation (EU) No 537/2014. We also remained independent of the audited entity in conducting the audit;

For the period to which our statutory audit relates, in addition to the audit, we have not provided the any services to the Bank which are not disclosed in the Business Report or in the financial statements of the bank.

On behalf of the auditing company

KPMG SLOVENIJA,

podjetje za revidiranje, d.o.o.

Polona Repinc Kofol
Certified Auditor

Barbara Kunc
Certified Auditor
Partner

Ljubljana, 15 February 2019

KPMG Slovenija, d.o.o.
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Statement Of Management's Responsibilities

The management is responsible for preparing financial statements for each financial year that present fairly the state of affairs of the Bank as at the end of the financial year and of the profit or loss for that period.

The management confirms that suitable accounting policies have been used and applied consistently and reasonable and prudent judgments and estimates have been made in the preparation of the financial statements for the year ended 31 December 2017. The management also confirms that the financial statements have been prepared on the going concern basis and in accordance with the applicable laws and International Financial Reporting Standards, as adopted by the EU.

The management is responsible for keeping proper accounting records, for taking reasonable steps to safeguard the assets of the Bank and its subsidiaries and to prevent and detect fraud and other irregularities.

In accordance with local regulations, the tax authorities may at any time inspect the Bank's books and records within 5 years subsequent to the reported tax year and may impose additional tax assessments and penalties. The Bank's management is not aware of any circumstances, which may give rise to a potential material liability in this respect.

Koper, February 2019

Financial Statements

1. INCOME STATEMENT

(in thousands of euros)

	Notes	For the year ended 31 December	
		2018	2017
Interest income calculated using effective interest rate	4	45,683	48,634
Other interest income	4	1,139	-
Interest expenses	4	(8,234)	(8,011)
Net interest income		**38,588**	**40,623**
Dividend income	5	166	506
Fee and commission income	6	37,198	36,301
Fee and commission expenses	6	(12,057)	(11,254)
Net fee and commission income		**25,141**	**25,047**
Net gains or losses on financial assets and liabilities not measured at fair value through profit or loss	7	2,761	2,642
Net gains or losses on financial assets and liabilities held for trading	8	876	874
Gains or losses on financial assets and liabilities designated at fair value through profit or loss		-	14
Net gains or losses on non-trading financial assets mandatorily at fair value through profit or loss	9	8,469	-
Net gains or losses from hedge accounting	10	53	(157)
Net exchange differences		(228)	96
Net gains and losses on derecognition of non-financial assets	11	380	48
Other operating income	12a	1,451	3,708
Other operating expenses	12b	(3,367)	(2,967)
Administrative expenses	13	(41,527)	(41,226)
Depreciation and amortisation	14	(2,954)	(4,333)
Provisions	15	(3,738)	(612)
Impairments	16	(13,542)	(19,306)
Profit or loss from non-current assets and disposal groups classified as held for sale, not qualifying as discontinued operations	17	614	-
Total profit or loss before tax		**13,143**	**4,957**
Tax expense	18	(2,429)	(746)
Total profit or loss after tax		10,714	4,211
Net profit or loss for the financial year		**10,714**	**4,211**
Earnings per share (basic and diluted) (in EUR per share)	19	20.20	7.94

The accompanying notes on pages 49 to 125 are an integral part of the financial statements.

2. STATEMENT OF OTHER COMPREHENSIVE INCOME

(in thousands of euros)

	For the year ended 31 December	
	2018	2017
NET PROFIT OR LOSS FOR THE FINANCIAL YEAR AFTER TAX	**10,714**	**4,211**
OTHER COMPREHENSIVE INCOME AFTER TAX	**(3,149)**	**10,164**
ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS	**1,719**	**11,176**
Actuarial gains on defined benefit pensions plans	1,417	5
Revaluation of properties	-	13,792
Fair value changes of equity instruments measured at fair value through other comprehensive income	539	-
Income tax relating to items that will not be reclassified to profit or loss	(237)	(2,621)
ITEMS THAT ARE OR MAY BE RECLASSIFIED SUBSEQUENTLY TO PROFIT OR LOSS	**(4,868)**	**(1,012)**
Available-for-sale financial assets:	**-**	**(1,249)**
- fair value gain on available-for-sale securities	-	1,732
- realised gains on available-for-sale financial assets transferred to profit or loss	-	(2,981)
Debt instruments at fair value through other comprehensive income	(6,000)	-
- fair value loss on debt instrument at FVOCI	(4,830)	**-**
- realised loss on FVOCI financial assets transferred to profit or loss	(1,170)	-
Non-current assets held for sale	**(10)**	-
- transferred to profit or loss	(10)	-
Income tax relating to items that may be reclassified to profit or loss	1,142	237
TOTAL COMPREHENSIVE INCOME FOR THE FINANCIAL YEAR AFTER TAX	**7,565**	**14,375**
a) Attributable to owners of the Bank	7,565	14,375

3. STATEMENT OF FINANCIAL POSITION

(in thousands of euros)

	Notes	As at 31 December	
		2018	2017
ASSETS			
Cash, cash balances at central banks and other demand deposits at banks	20	390,660	287,084
Derivatives held for trading	21	29	60
Derivatives – hedge accounting	21	1,023	2,471
Financial assets designated at fair value through profit or loss		-	59
Non-trading financial assets mandatorily at fair value through profit or loss	23	3,019	-
Available-for-sale financial assets	22	-	318,702
Financial assets at fair value through other comprehensive income	24	314,631	-
Financial assets at amortised cost:		1,830,704	-
-debt securities	25	1,266	-
-loans to banks	26	53,623	-
-loans to non–bank costumers	27	1,757,088	-
-advances	28	18,727	-
Loans and receivables:		-	1,729,900
- loans to banks	26	-	41,142
- loans to non-bank customers	27	-	1,675,027
- advances	28	-	13,731
Fair value changes of the hedged items in portfolio hedge of interest rate risk		1,203	114
Non-current assets classified as held for sale	29	14,592	19,601
Property, plant and equipment	30	27,974	28,794
Intangible assets	32	4,071	3,518
Tax assets		-	491
- current tax assets		-	491
Other assets	33	8,580	7,357
Total assets		**2,596,486**	**2,398,151**
LIABILITIES			
Derivatives held for trading	21	-	8
Derivatives – hedge accounting	21	4,055	660
Financial liabilities measured at amortised cost:		2,289,275	2,091,860
- deposits from banks and central banks	34	15,517	10,750
- deposits from non-bank customers	35	2,207,670	1,971,496
- loans from banks and central banks	36	37,484	71,477
- loans from non-bank customers	37	32	-
- other financial liabilities	38	28,572	38,137
Fair value changes of the hedged items in portfolio hedge of interest rate risk		626	1,131
Provisions:		12,635	10,540
- provisions for liabilities and charges	39	9,737	6,272
- retirement benefit obligations	40	2,898	4,268
Tax liabilities:		2,789	3,096
- current tax liabilities		818	-
- deferred tax liabilities	41	1,971	3,096
Other liabilities	42	2,782	5,627
Total liabilities		**2,312,162**	**2,112,922**
EQUITY			
Share capital	43	22,173	22,173
Share premium	43	7,499	7,499
Accumulated other comprehensive income	44	12,447	16,023
Reserves from profit	45	230,111	229,574
Treasury shares	43	(49)	(49)
Retained earnings (including net profit for the current year)	45	12,143	10,009
Total equity		**284,324**	**285,229**
Total liabilities and equity		**2,596,486**	**2,398,151**

The accompanying notes on pages 49 to 125 are an integral part of the financial statements.

4. STATEMENT OF CHANGES IN EQUITY

(in thousands of euros)

For the year ended 31 December 2018	Notes	Share capital	Share premium	Accumulated other comprehensive income	Reserves from profit	Retained earnings or loss (including profit from the current year)	Treasury shares (equity deduction item)	Total equity
OPENING BALANCE FOR THE REPORTING PERIOD (before restatement)		**22,173**	**7,499**	**16,023**	**229,574**	**10,009**	**(49)**	**285,229**
Effects of changes in accounting policies (introduction IFRS9)		-	-	(427)	-	(4,027)	-	**(4,454)**
OPENING BALANCE FOR THE REPORTING PERIOD		**22,173**	**7,499**	**15,596**	**229,574**	**5,982**	**(49)**	**280,775**
Total comprehensive income for the year after tax		-	-	(3,149)	-	10,714	-	**7,565**
Dividends paid	45	-	-	-	-	(3,999)	-	**(3,999)**
Transfer of net profit to reserves	45	-	-	-	537	(537)	-	**-**
Loss from disposals of FVOCI shares		-	-	-	-	(17)	-	**(17)**
CLOSING BALANCE		**22,173**	**7,499**	**12,447**	**230,111**	**12,143**	**(49)**	**284,324**
DISTRIBUTABLE PROFIT		-	-	-	-	10,178	-	**10,178**

(in thousands of euros)

For the year ended 31 December 2017	Notes	Share capital	Share premium	Accumulated other comprehensive income	Reserves from profit	Retained earnings or loss (including profit from the current year)	Treasury shares (equity deduction item)	Total equity
OPENING BALANCE FOR THE REPORTING PERIOD		**22,173**	**7,499**	**5,859**	**229,362**	**25,238**	**(49)**	**290,082**
Total comprehensive income for the year after tax		-	-	10,164	-	4,211	-	**14,375**
Dividends paid	45	-	-	-	-	(19,228)	-	**(19,228)**
Transfer of net profit to reserves	45	-	-	-	212	(212)	-	**-**
CLOSING BALANCE		**22,173**	**7,499**	**16,023**	**229,574**	**10,009**	**(49)**	**285,229**
DISTRIBUTABLE PROFIT		-	-	-	-	4,000	-	**4,000**

The accompanying notes on pages 49 to 125 are an integral part of the financial statements.

5. STATEMENT OF CASH FLOWS

(in thousands of euros)

	Notes	For the year ended 31 December	
		2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES			
Total profit or loss before tax		13,143	4,957
Depreciation	14	2,954	4,333
Impairments / (reversal of impairments) of financial assets at fair value through other comprehensive income	16	(71)	-
Impairments / (reversal of impairments) of financial assets measured at amortised cost	16	12,284	18,311
Impairments of tangible assets, investment property, intangible assets and other assets	16	1,329	974
Net (gains) / losses from exchange differences		227	(96)
Net (gains) / losses from sale of tangible assets		182	(48)
Net (gains) / losses from non-current assets and disposal groups classified as held for sale, not qualifying as discontinued operations		671	-
Other adjustments to total profit or loss before tax (provisions)		3,738	612
Cash flow from operating activities before changes in operating assets and liabilities		**34,457**	**29,043**
(Increases) / decreases in operating assets (excl. cash & cash equivalents)		**(106,761)**	**35,629**
Net (increase) / decrease in financial assets held for trading		31	4
Net (increase) / decrease in financial assets mandatorily at fair value through profit or loss		17,161	-
Net (increase) / decrease in financial assets designated at fair value through profit or loss		-	77
Net (increase) / decrease in financial assets measured at fair value through other comprehensive income		2,494	-
Net (increase) / decrease in financial assets available-for-sale		-	43,106
Net (increase) / decrease of financial assets measured at amortised cost		(123,434)	(10,357)
Net (increase) / decrease in assets-derivatives - hedge accounting		359	(1,627)
Net (increase) / decrease in non-current assets and disposal groups classified as held for sale, not qualifying as discontinued operations		3,894	-
Net (increase) / decrease in other assets		(7,266)	4,426
Increases / (decreases) in operating liabilities		**201,958**	**63,249**
Net increase / (decrease) in financial liabilities held for trading		(8)	8
Net increase / (decrease) in deposits and loans measured at amortised cost		201,462	61,988
Net increase / (decrease) in liability – derivatives – hedge accounting		2,890	48
Net increase / (decrease) in other liabilities		(2,386)	1,205
Cash flow from operating activities		**129,654**	**127,921**
Income taxes (paid) / refunded		(214)	(2,073)
Net cash flow from operating activities		**129,440**	**125,848**
CASH FLOWS FROM INVESTING ACTIVITIES			
Receipts from investing activities		**183**	**1,243**
Receipts from the sale of property and equipment and investment properties		183	1,243
Cash payments on investing activities		**(2,251)**	**(4,031)**
Cash payments to acquire tangible assets, and investment properties		(815)	(4,031)
Cash payments to acquire intangible assets		(1,436)	-
Net cash flow from investing activities		**(2,068)**	**(2,788)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Cash proceeds from financing activities		**-**	**-**
Cash payments on financing activities		**(3,999)**	**(19,227)**
Dividends paid		(3,999)	(19,227)
Net cash flow from financing activities		**(3,999)**	**(19,227)**
Effects of change in exchange rates on cash and cash equivalents		1,158	(4,187)
Net increase in cash and cash equivalents		**123,373**	**103,833**
Opening balance of cash and cash equivalents	47	291,008	191,362
Closing balance of cash and cash equivalents	47	**415,539**	**291,008**

(in thousands of euros)

Operational cash flows of interest and dividends	As at 31 December	
	2018	2017
Interest paid	(9,733)	(8,543)
Interest received	48,464	49,399
Dividends received	166	506

As at 31 December 2018, the Bank did not have undrawn credit lines (2017: 100,000 thousand).

The accompanying notes on pages 49 to 125 are an integral part of the financial statements.

Notes To Financial Statements

1. GENERAL INFORMATION

Banka Intesa Sanpaolo d.d. is a public limited company with the head office at 14 Pristaniška Street, Koper/ Capodistria (hereinafter referred to as Banka Koper d.d. or the Bank). Since 2002, Banka Koper d.d. is member of the Intesa Sanpaolo Group (originally SanpaoloIMI), one of the leading banking groups in Italy. As of January 1 2007, the Sanpaolo IMI Group merged with Banca Intesa. Since July 2017, the Bank is also part of Privredna Banka Zagreb banking group, which holds 51% stake.

The Bank prepares its financial statements as at the last day of the calendar year.

The date of the Management Board statement shall be considered as the date on which the financial statements were approved.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted for the preparation of the financial statements are set out below:

2.1 BASIS OF PREPARATION

Statement of compliance

The financial statements for 2018 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.

Basis of measurement

Financial statements have been prepared on cost basis, except fort the following items, which are measured at fair value:

Financial instruments held for trading

- Financial asset at FVTPL
- Financial assets at FVOCI (applicable from 1 January 2018)
- Available for sale financial assets (applicable before 1 January 2018)
- Land and buildings
- Recognised financial assets designated as hedging items in qualifying fair value hedging relationship (which otherwise would have been measured at amortised cost)

Use of estimates and judgements

The preparation of financial statements in conformity with IFRS as adopted by the EU requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

A more detailed disclosures is shown under chapter 2.4.7 Impairment of financial assets, 2.26 Accounting estimates and judgments in applying accounting policies and 3.3 Credit risk.

Changes in accounting policies and implementation of new accounting standards

The Bank has consistently applied the accounting policies as set further on **except for implementation of accounting policies related to IFRS 9, which enter in force by 1st January 2018.** The new standard brings fundamental changes in classification and measurement of financial instruments and in calculation of credit losses.

The Bank has also initially adopted IFRS 15 from 1 January 2018. 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 recognized by the Bank. Accordingly, the impact on the comparative information is limited to new disclosure requirement.

Changes related to IFRS 9

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 existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss.

Impairment of financial assets

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

Under IFRS 9, credit losses are recognised earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see Note 3.3 Credit Risk

IFRS 9 Transition

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

- Comparative periods have not been restated. Differences in the carrying amounts of financial assets and 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.
  - The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
  - The designation of certain investments in equity instruments not held for trading as at FVOCI.

Information and details on the changes and implications resulting from the adoption of IFRS 9 are presented below.

Classification of financial assets and liabilities at the date of initial application of IFRS 9

(in thousands of euros)

Financial assets	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Cash, cash balances at central banks and other demand deposits at banks	Loans and receivables	Amortised cost	287,084	287,069
Derivatives held for trading	Held for trading	Held for trading	60	60
- derivative financial instruments	Held for trading	Held for trading	60	60
Financial assets designated at fair value through profit or loss	FVTPL designated	FVTPL mandatory	59	59
Available-for-sale financial assets				
- debt instruments	Available for sale	FVOCI	301,478	301,478
- debt instruments	Available for sale	Amortised cost	1,413	1,269
- equity instruments	Available for sale	FVOCI	13,674	13,674
- equity instruments	Available for sale	FTPL mandatory	2,137	2,137
Loans and receivables				
- loans to banks	Loans and receivables	Amortised cost	41,142	41,119
- loans to non-bank costumers	Loans and receivables	Amortised cost	1,656,149	1,651,830
- loans to non-bank costumers	Loans and receivables	FVTPL mandatory	18,878	17,984
- advances	Loans and receivables	Amortised cost	13,731	13,731
Total			**2,335,805**	**2,330,410**
Provision for off balance items			**484,706**	**484,603**

Changes in financial assets due to application of IFRS 9

(in thousands of euros)

Financial assets	Carrying amount 31 December 2017 (IAS39)	Reclassification	Remeasurement	Carrying amount 1 January 2018 (IFRS9)
Amortised cost				
Cash and cash equivalents				
Opening balance	287,084			
Remeasurement			(15)	
Closing balance				287,069
Loans and advances to banks				
Opening balance	41,142			
Remeasurement			(23)	
Closing balance				41,119
Loans and advances to costumers				
Opening balance	1,675,027			
To mandatory FVTPL		(18,878)		
Remeasurement			(4,319)	
Closing balance				1,651,830
Advances				
Opening balance	13,731			
Closing balance				13,731
Debt securities				
Opening balance	-			
From AFS		1,413		
Remeasurement: from fair value to amortised cost			(142)	
Remeasurement			(2)	
Closing balance				1,269
Total amortised cost	**2,016,984**	**(17,465)**	**(4,501)**	**1,995,018**
FVOCI				
Available for sale				
Opening balance	318,702			
To: FVOCI – debt		(301,478)		
To: FVOCI – equity		(13,674)		
To: amortised cost – debt securities		(1,413)		
To: mandatory FVTPL		(2,137)		
Closing balance				-
FVOCI – debt				
Opening balance	-			
From: AFS		301,478		
Closing balance				301,478
FVOCI - equity				
Opening balance	-			
From: AFS		13,674		
Closing balance				13,674
Total FVOCI	-	315,152	-	315,152
Mandt. FVTPL				
Financial assets held for trading	**60**			**60**
Opening and closing balance	60			60
FVTPL designated				
Opening balance	59			
To: mandatory FVTPL		(59)		
Closing balance				-
FVTPL mandatory				
Opening balance	-			
From: FVTPL designated		59		
From: AFS		2,137		
From: Loans and advances to costumers		18,878		
Remeasurement: amortised cost to fair value			(894)	
Closing balance				20,180
Total mandatory FVTPL	**-**	**21,074**	**(894)**	**20,240**
Off- balance				
Opening balance	484,706			
Remeasurement			**(103)**	
Closing balance				**484,603**

Changes in impairments due to application of IFRS 9

(in thousands of euros)

Financial assets	Impairments 31 December 2017 (IAS39)	Reclassification	Remeasurement	Impairments 1January 2018 (IFRS 9)
Impairments and provisions				
Loans and advances (IAS39)/ Financial assets at amortised cost (IFRS9)				
Cash, cash balances at central banks and other demand deposits at banks	9	-	15	24
Debt securities	-	-	2	2
Loans to banks	4	-	23	27
Loans to non-bank customers	100,193	(11,187)	4,319	93,325
Debt securities available for sale (IAS 39)/Debt securities at FVOCI (IFRS 9)	**-**	**-**	**145**	**145**
Off-balance exposures	**3,653**	**-**	**103**	**3,756**
Total	**103,859**	**(11,187)**	**4,607**	**97,279**

Changes in equity due to application of IFRS 9

(in thousands of euros)

Other comprehensive income	Impact of adopting IFRS 9 at 1 January 2018
Closing balance under IAS 39 (31 December 2017)	5,398
Reclassification of investment securities (debt) from available-for-sale to amortised cost	(115)
Reclassification of investment securities (debt and equity) from available-for-sale to mandt. FVTPL	(345)
Reclassification of investment securities (equity) from available-for- sale to FVOCI	(84)
Recognition of expected credit losses under IFRS 9 for debt financial assets at FVOCI	117
Opening balance under IFRS 9 (1 January 2018)	4,971
Impact of adopting IFRS 9 on other comprehensive income	**(427)**
Retained earnings	
Closing balance under IAS 39 (31 December 2017)	-
Reclassifications under IFRS 9	(294)
Recognition of expected credit losses under IFRS 9 (including lease receivables, loan commitments and financial guarantee contracts)	(3,733)
Opening balance under IFRS 9 (1 January 2018)	(4,027)
Impact of adopting IFRS 9 on retained earnings	**(4,027)**
Impact of adopting IFRS 9 on equity	**(4,454)**

Standards, Interpretations and amendments to published Standards as adopted by the EU that are not yet effective for annual periods beginning on 1 January 2018

The number of new Standards, amendments to Standards and Interpretations are not yet mandatorily effective for annual periods beginning on or after 1 January 2018, and have not been applied in preparing these interim consolidated financial statements. The entity / Group plans to adopt these pronouncements when they become effective. One of the standard that is effective from 1 January 2019 and will have impact on the financial statements of the Bank is IFRS 16, described below.

IFRS 16 Leases

IFRS 16 supersedes IAS 17 Leases and related interpretations. The Standard eliminates the current dual accounting model for lessees and instead requires companies to bring most leases on-balance sheet under a single model, eliminating the distinction between operating and finance leases.

Under IFRS 16, a contract is, or contains, a lease if it conveys the right to control the use of an identified asset for a period of time in exchange for consideration. For such contracts, the new model requires a lessee to recognise a right-of-use asset and a lease liability. The right-of-use asset is depreciated and the liability accrues interest. This will result in a front-loaded pattern of expense for most leases, even when the lessee pays constant annual rentals.

The new Standard introduces a number of limited scope exceptions for leases which include:
- leases with a lease term of 12 months or less and containing no purchase options, and
- leases where the underlying asset has a low value ('small-ticket' leases).

Lessor accounting, however, shall remain largely unchanged and the distinction between operating and finance leases will be retained.

The Bank will recognise in the balance sheet new assets and liabilities for its operating leases (premises and cars) in total amount of EUR 4,606 thousands. The nature and expenses related to those leases will not change a lot, because the Bank will recognise a depreciation charge for right-of-use assets and interest expense on the lease liabilities. Previously, the Bank recognised operating lease expenses on a straight-line basis over the time of the lease, and recognised assets and liabilities only to the extent that there was a timing difference between the actual lease payments and the expense recognised. Instead, the Bank will include payments due under the lease in lease liability.

No impact is expected for the Bank's finance leases.

No impact is expected for other leases in which the Bank is a lessor.

The Bank applies the practical expedient to grandfather the definition of lease on transition. This means that it will apply IFRS 16 to all contracts entered into before 1 January 2019 and identified as leases in accordance with IAS 17 and IFRIC 4.

2.2 FOREIGN CURRENCY TRANSLATION

Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates ('the functional currency'). The financial statements are presented in euros, which is the Bank's functional and presentation currency.

Recording foreign currency transactions

Foreign currency transactions are translated into the functional currency using the exchange rate prevailing at the date of transactions. Exchange rate differences resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Translation differences on non-monetary items, such as equities at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, such as equities classified as at FV through OCI, are included in the fair value reserve in equity.

Income and expenses arising on foreign currencies are translated at the exchange rate at the date of the transaction.

Gains and losses resulting from buying and selling foreign currencies for trading purposes are reported in profit or loss as net gains or losses from trading of foreign currencies.

2.3 RELATED PARTIES

For the purposes of the financial statements, related parties include all entities, that directly or indirectly, through one or more intermediaries, control or are controlled by, or are under common control with, the reporting enterprise. Related parties include parents, subsidiaries, fellow subsidiaries, associates of the reporting entity, members of the key management personnel and directors of the Banks and enterprises over which the key management personnel and directors of the reporting entity are able to exercise significant influence (participation in making financial and operating policy decisions of an enterprise).

2.4 FINANCIAL ASSETS AND LIABILITIES

2.4.1 Treatment of financial assets and liabilities in financial statements

Recognition and initial measurement

The Bank initially recognises loans and advances, deposits, on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the 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 or loss ("FVTPL"), transaction costs that are directly attributable to its acquisition or issue.

2.4.2 Classification

Financial assets – Policy applicable from 1 January 2018

On initial recognition, a financial asset is classified as measured at: amortised cost, fair value through other comprehensive income ("FVOCI") or FVTPL.
A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:
- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:
- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

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.

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

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

Assessment whether contractual cash flows are solely payments of principal and interest (SPP test)
For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:
- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

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

Financial assets at fair value through profit or loss
This category has two sub-categories: financial instruments held for trading and financial instruments designated at fair value through profit or loss at inception. Financial instruments are classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Derivatives are classified as held for trading unless they are designated as hedges.

Loans and receivables
Loans and receivables are non-derivative financial instruments with fixed or determinable payments that are not quoted in an active market, other than:
(a) those that the entity intends to sell immediately or within the short term, which are classified as held for trading and those that the entity designates at fair value through profit or loss upon initial recognition;
(b) those that the entity, upon initial recognition, designates as available for sale ; or
(c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration

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

Recognition and measurement

Date of recognition
Purchases and sales of financial instruments at fair value through profit or loss, held to maturity and available-for-sale are recognised on the trade date. Loans are recognised when the cash is advanced to the borrowers.

Value of recognition and subsequent measurement
Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit and loss.
Financial assets at fair value through profit or loss and available-for-sale financial assets are measured subsequently at fair value. Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss are presented in the income statement in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in other comprehensive income, until the financial asset is disposed of, derecognised or impaired, at which time the cumulative gain or loss previously recognised in other comprehensive income is recognised in profit or loss. However, interest calculated using the effective interest method and foreign currency gains and losses on monetary assets classified as available-for-sale are recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in profit or loss when the entity's right to receive payment is established.
Loans and receivables are carried at amortised cost.

2.4.3 De-recognition of financial instruments

The Bank derecognises 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 derecognised) and the sum of the consideration received (including any new asset obtained less any new liability assumed) and any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

From 1 January 2018 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities, but directly in retained profit or loss.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a de-recognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in income statement.

2.4.4 Modifications of financial assets and financial liabilities

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

Policy applicable from 1 January 2018
If the cash flows of the modified asset carried at amortised cost are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, the Bank recalculates the gross carrying amount of the financial asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss.

Policy applicable before 1 January 2018
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 premodification interest rate.

Financial liabilities

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

Fair value measurement principles

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

When one is 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 maximise the use of relevant observable inputs and minimise 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 on 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 on 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 for which any unobservable inputs are judged to be insignificant in relation to the measurement, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value on initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at a bid price and liabilities and short positions at an ask price.
Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Bank on the basis of the net exposure to either market or credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for the particular risk exposure. Portfolio-level adjustments – e.g. bid-ask adjustment or credit risk adjustments that reflect the measurement on the basis of the net exposure – are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of a financial liability with a demand feature (e.g. 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 recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Since the application of IFRS 13 – Fair value measurement, the inputs used to measure fair value, should be presented when classifying financial instruments in the three levels of fair value hierarchy:
- **Level 1 inputs:** Fair value measured using (unadjusted) quoted prices in active markets for identical assets or liabilities.
- **Level 2 inputs:** Fair value measured using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices from similar assets) or indirectly (i.e. derived from prices of similar instruments).
- **Level 3 inputs:** Fair value measured using inputs for the asset or liability that are not based on observable market inputs.

More detailed disclosure is shown under chapter 3.9 Fair value of assets and liabilities that are not measured at fair value.

2.4.5 Offsetting

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

2.4.6 Designated at fair value through profit or loss

At initial recognition, the Bank has designated certain financial assets as at FVTPL because this designation eliminates or significantly reduces an accounting mismatch, which would otherwise rise.
Before 1 January 2018, the Bank also designated certain financial assets as at FVTPL because the assets were managed, evaluated and reported internally on a fair value basis.

2.4.7 Impairment of financial assets

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;
- lease receivables;
- financial guarantee contracts issued; and
- loan commitments issued.

No impairment loss is recognised on equity investments.

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 (other than lease receivables) on which credit risk has not increased significantly since their initial recognition.

Loss allowances for lease receivables are always measured at an amount equal to lifetime ECL.

The Bank considers a debt security to have low credit risk when their credit risk rating is equivalent to the globally understood definition of 'investment grade', meaning government or corporate bonds with relatively low risk of default.

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

Measurement of ECL

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

Restructured financial assets

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

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

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt securities 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.

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 addition, a retail loan that is overdue for 90 days or more is considered impaired.

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

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

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; 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 realistic prospect of recovery. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

Policy applicable before 1 January 2018

Loans and other assets carried at amortised cost

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset ('a loss event') and that loss event (or events) has an impact on the estimated future cash flows.

The Bank first assess whether objective evidence of impairment exists for financial assets that are individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset it includes the asset in a group of financial assets with similar credit risk characteristic and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment.

If there is objective evidence that an impairment loss on loans and receivables or held to maturity investment has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate (in case of a variable interest rate, the last effective interest rate is taken). The carrying amount of the asset is reduced through the adjustment account and the amount of the loss is recognised in the income statement.

The calculation of present value of the estimated future cash flows of collateralised financial assets reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (on the basis of the Bank's internal classification process that considers all relevant factors).
Future cash flows for the group of individually significant financial assets that are evaluated for impairment are estimated on the basis of the contractual cash flows and historical loss experience for assets with credit risk characteristics similar to those in the group. The methodology and assumptions used for estimating future cash flows are reviewed regularly.
If the amount of the impairment subsequently decreases due to an event occurring after the write down, the reversal of loss is credited as a reduction of the adjustment account for loan impairment.

When a loan is uncollectible, it is written off against the related provision for loan impairment. In the case that the provision for loan impairment does not exist, additional provision s recognised directly in the income statement under gains less losses from financial assets and liabilities not recognised at fair value through profit or loss. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are shown as income in income statement.

Assets carried at fair value

At each reporting date the Bank assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value is considered when the investment is below its cost value. According to the Bank's accounting policies, a significant decrease is when the financial instrument's fair value decreases by more than 30% below its average initial carrying amount. A prolonged decline in the asset's fair value generally occurs when the fair value of a financial instrument has been below its average initial carrying amount for at least 24 months. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the initial carrying amount and current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from other comprehensive income and recognised in the income statement. Impairment losses on equity instruments recognised in the income statement are not reversed through the income statement but always recognised as increase in other comprehensive income. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the income statement.

2.5 DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments fall into the following categories: forward-based, swap-based and option-based, are measured initially at fair value. Subsequent to initial recognition all derivatives are measured considering changes in fair value. To determine their fair value, derivative financial assets and financial liabilities are measured using quoted prices, discounted cash flow models or pricing models, as appropriate. All derivatives are carried at their fair value as assets when favourable to the Bank, and as liabilities when unfavourable to the Bank.

Certain derivative financial instruments that provide effective economic hedges and are not qualified for hedge accounting under the specific accounting rules, are therefore accounted for as derivative financial instruments held for trading purposes.

The best evidence of the fair value of a derivative financial instrument at initial recognition is the transaction price (the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions of the same instrument (without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Bank recognises profits/losses on Day 1; if not, profits/losses are not recognised on Day 1, but if and when such evidence becomes available or when the derivative is derecognised.

De-recognition of the derivatives occurs only when through a legal transaction that transfers ownership of a financial instrument to the buyer, the seller has also transferred substantially all the risks and future rewards of ownership of the financial instrument.

2.5.1 Hedge accounting

The Bank has not adopted the hedge accounting requirements of IFRS 9, but continued to apply hedge accounting requirements of IAS 39 Financial instruments: Recognition and Measurement.
The Bank uses derivative financial instruments to manage its exposures to interest rate risk. Such derivative financial instruments are initially recognised at fair value on the date on which they are entered to and are subsequently re-measured at fair value. Derivatives are carried as financial assets when the fair value is positive and as financial liabilities when the fair value is negative.

For the purpose of hedge accounting, hedges could refer to:
- Fair value hedge – a hedge of exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment;
- Cash flow hedge – a hedge of the exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction;
- Hedge of a net investment in a foreign currency.

At the inception of a hedge relationship, the Bank formally designates and documents the hedge relationship to which the Bank wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the Bank will assess the effectiveness of changes in the hedging instrument's fair value in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are tested regularly throughout their life to determine that they actually have been highly effective throughout the financial reporting periods for which they are designated.

The Bank uses fair value hedge to cover exposure to changes in the fair value attributable to the different risk categories of assets and liabilities in the statement of financial position, or a portion of these or to cover portfolios of financial assets and liabilities.

Fair value hedge

When a derivative is designated as the hedging instrument in a hedge of the change in fair value of a recognised asset or liability or a firm commitment that could affect profit or loss, changes in the fair value of the derivative are recognised immediately in profit or loss together with changes in the fair value of the hedged item that are attributable to the hedged risk (in the same line item in the statement of profit or loss and OCI as the hedged item).

If the hedging derivative expires or is sold, terminated or exercised, or the hedge no longer meets the criteria for fair value hedge accounting, or the hedge designation is revoked, then hedge accounting is discontinued prospectively. However, if the derivative is novated to a CCP by both parties as a consequence of laws or regulations without changes in its terms except for those that are necessary for the novation, then the derivative is not considered expired or terminated.
Any adjustment up to the point of discontinuation to a hedged item for which the effective interest method is used is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

2.6 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;
- loans and advances mandatorily measured at FVTPL or designated as at FVTPL; these are measured at fair value with changes recognised immediately in profit or loss; and
- finance lease receivables.

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;
- those designated as at FVTPL; and
- finance lease 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. When the Bank chose to designate the loans and advances as measured at FVTPL, they were measured at fair value with face value changes recognised immediately in profit or loss.
Loans and advances also included finance lease receivables in which the Bank was the lessor.

2.7 SECURITIES

Policy applicable from 1 January 2018

Securities in the statement of financial position includes:
- debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;
- debt and equity investment securities mandatorily measured at FVTPL or designated as at FVTPL; these are at fair value with changes recognised immediately in profit or loss;
- debt securities measured at FVOCI; and
- equity investment securities designated as 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.
The Bank elects to present in OCI changes in the fair value of certain investments in equity instruments that are not held for trading. The election is made on an instrument-by-instrument basis on initial recognition and is irrevocable.
Gains and losses on such equity instruments are never reclassified to profit or loss and no impairment is recognised in profit or loss. Dividends are recognised in profit or loss unless they clearly represent a recovery of part of the cost of the investment, in which case they are recognised in OCI. Cumulative gains and losses recognised in OCI are transferred to retained earnings on disposal of an investment.

Policy applicable before 1 January 2018

Securities in the statement of financial position includes:
- fair value through profit or loss
- 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. Dividend income is recognised in profit or loss when the Group becomes entitled to the dividend.
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.

2.8 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.

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.

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.

2.9 FEE AND COMMISSION INCOME

Fees and commissions are generally recognised as the services are provided. Fees and commissions consist mainly of fees charged on payment services, credit cards, services and fund management on behalf of legal entities and citizens, together with commissions from guarantees. For loan commitments the bank charged the client for small administrative expenses for loan elaboration, which cover just the process costs.
Fee and commission income and expense that are integral to the effective interest rate on a financial asset or financial liability are included in the effective interest rate.

Other fee and commission income – including account servicing fees, investment management fees, sales commission, placement fees and syndication fees – is recognised as the related services are performed.
Other fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.
*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 I s the case, the Bank first applies IFRS 9 to separate and measure that part and on the residual apply IFRS 15.

2.10 NET TRADING INCOME

Net trading income' comprises gains less losses related to trading assets and liabilities, and includes all fair value changes, interest and foreign exchange differences.

2.11 INTANGIBLE ASSETS

Intangible assets encompass licences for computer software, patents, copyrights and other industrial property rights acquired, and development expenditures, are carried in the statement of financial position at cost less any accumulated amortisation and any accumulated impairment losses.
Expenditure on research and development and maintaining computer software is recognised in profit or loss as the expense is incurred. In circumstances when expenditure is directly associated with the development of computer software that will probably generate expected future economic benefits exceeding costs, expenditures are recognised as intangible assets. Directly attributable costs are capitalised as software development.

The amortisation method used to allocate the depreciable amount of an asset on a systematic basis over its useful life is the straight-line method. Amortisation begins when the asset is available for use.

The Bank reviews the amortisation period and the amortisation method for an intangible asset with a finite useful life at each financial year-end.

Intangible assets	Estimated useful lives in 2018	Estimated useful lives in 2017
Licence fees	2-4	4
Development expenditure	5	5
Computer software	4	4

The main IT system (Bančno okence) is internally developed and included within Development expenditure. For this type of intangible fixed assets the estimate useful life is 5 year.

Gains and losses arising on de-recognition should be calculated as the difference between the asset's net disposal proceeds and its carrying amount and should be recognised in the income statement. Intangible assets are assessed for impairment whenever there is an indication that the intangible asset may be impaired. The assessment for impairment is carried out at least on yearly bases.

2.12 PROPERTY, PLANT AND EQUIPMENT

Tangible fixed assets are land, buildings, manufacturing plant and equipment. Tangible fixed assets are measured at cost less depreciation, except for property, which is valued at fair value. The transition to the fair value model was implemented as of December 31, 2017 (detailed reasons and effects are shown in the chapter Change of accounting policy to evaluate functional property, investment property and artistic heritage).

The cost of an item of property, plant and equipment comprises its purchase price after deducting trade discounts, including import duties and non-refundable purchase taxes, directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating (cost of transport, installation …) and the cost of its dismantlement, removal and restoration. The cost of interest related to the acquisition of an item of property, plant and equipment is included in the cost of acquiring that item and capitalised.

The Bank measures a property, plant and equipment item acquired in exchange for a non-monetary asset or a combination of monetary and non-monetary assets at fair value.

The Bank assesses annually whether there is any indication that an asset may be impaired. If there is an indication that an asset may be impaired, the recoverable amount of the asset is determined. The recoverable amount is the higher of the fair value less costs to sell and the value in use. If the recoverable amount exceeds the carrying amount, it is an indication that the asset is not impaired.
The Bank recognises subsequent costs in the carrying amount of an item of property, plant and equipment when it is probable that future economic benefits associated with the item will flow to the Bank. The costs of day-to-day servicing (repairs and maintenance) are recognised in profit or loss as incurred.

Depreciation charges are calculated by using the straight-line method. The depreciation rates are determined to allocate the value of items of property, plant and equipment over their estimated useful lives to expenses.
Assets in the course of transfer or construction are not depreciated until they are brought into use.
The residual value and the useful life of an asset is reviewed on a regular basis and, if expectations differ from previous estimates, the change(s) is accounted for as a change in an accounting estimate.

Property, plant and equipment	Estimated useful lives in 2018	Estimated useful lives in 2017
Buildings	16.6-33	16.6-40
Other investment in intangibles	20	20
Equipment	5	5
Motor vehicles	5	5
Computers and software	4	4

Any gain or loss on disposal of an item of property, plant and equipment determined as the difference between the proceeds and the carrying amount are recognised in profit or loss, determining operating profit.

Change of accounting policy to evaluate functional property, investment property and artistic heritage

At the end of 2017, the Intesa Sanpaolo Group changed its accounting policies for evaluation of real estate and works of art in its balance sheet. The currently adopted cost criterion for the assessment of this property was replaced by revaluation model. In accordance with the Group's rules, Banka Intesa Sanpaolo d.d., as its subsidiary member, has changed its policy too.

The change in accounting policy is the result of the Group's awareness of the great historical and artistic value of its real estate and its intentions to more effectively manage real estate and cultural and historical assets, which the Group accumulated over decades from approximately 250 banks throughout the whole Italian territory. In this view, the purpose of the valuation of real estate at fair value is to be understood as a voluntary choice, with the aim to provide readers of the financial statement a more credible and relevant representation of financial information.

Considering the change in accounting policy was implemented at the end of 2017, the depreciation for 2017 was still calculated in accordance with the cost model. The revaluation of real estate was carried out in accordance with IAS 16.35, which requires the adjustment of the carrying amount of the asset to a new fair value, by using elimination approach, which states the accumulated depreciation is eliminated against the gross carrying amount of the asset. This results the fair value of the property as at December 31 2017 is equal to its cost (historical) value.
The change in accounting policy for functional properties resulted with higher net carrying amount of EUR 12,818 thousand as at 31 December 2017, compared to the net carrying amount of functional properties which would be reported in accordance with previous model.

2.13 NON-CURRENT ASSETS AND DISPOSAL GROUPS CLASSIFIED AS HELD FOR SALE

The Bank classifies a non-current asset as held for sale (or disposal groups comprising assets and liabilities) assets that are expected to be recovered primarily through sale rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale and the sale should be expected to be completed within one year from the date of classification.

Immediately before classification as held for sale, the assets (or components of a disposal group) are remeasured in accordance with the Bank's accounting policies. Thereafter, the assets (or disposal group of assets and liabilities) are measured at the lower of their carrying amount and fair value less cost to sell.
A non-current asset classified as held for sale is no longer depreciated. Impairment losses on initial classification as

held for sale and subsequent gains or losses on remeasurement are recognised in income statement. Gains are not recognised in excess of any cumulative impairment loss. Any impairment loss on a disposal group first is allocated to goodwill, and then to the remaining assets and liabilities on a pro-rata basis, except that no loss is allocated to financial assets and deferred tax assets, which continue to be measured in accordance with the Bank's accounting policies.

At reclassification back, on change of intent or if the conditions required by IFRS 5 cease to be applicable, the Bank does not restate comparative information in the balance sheet. Upon reclassification the valuation is adjusted in accordance with relevant standards, as if the reclassification had not occurred.

2.14 IMPAIRMENT OF NON-FINANCIAL ASSETS

At each reporting date, the Bank reviews the carrying amounts of its non-financial assets to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

The 'recoverable amount' of an asset or CGU is the greater of its value in use and its fair value less costs to sell. 'Value in use' is based on the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU.

An impairment loss is recognised if the carrying amount of an asset or CGU exceeds its recoverable amount. Impairment losses are recognised in profit or loss.

2.15 DEPOSITS AND RECEIVED LOANS

Deposits and received loans are initially measured at fair value minus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

2.16 ACCOUNTING FOR LEASES

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

- **The Bank as lessee**

Leases which do not transfer to the Bank substantially all the risks and rewards incidental to ownership of the leased items are operating leases. Lease payments under operating lease are recognised as an expense in profit or loss on a straight line basis over the lease term. Contingent rents are charged as expenses in the periods in which they are incurred

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership to the lessee. An item of property, plant and equipment acquired by way of finance lease is recorded as an asset and a liability at the lower of the fair value of the asset and the present value of the minimum lease payments at the commencement of the lease term, less accumulated depreciation and any impairment losses. An item of property, plant and equipment acquired under a finance lease is depreciated over the useful life of the asset. If there is no reasonable certainty that the lessee will obtain ownership of the leased asset by the end of the lease term, the leased assets shall be fully depreciated over the shorter of the lease term and its useful life.

- **The Bank as lessor**

When assets are leased under an operating lease, the Bank recognises rental income in the income statement on a straight-line basis over the period of the lease.

When assets are leased out under a finance lease, the present value of the lease payments is recognised as a receivable. Income from finance leasing transactions is apportioned systematically over the primary lease period, reflecting a constant periodic return on the lessor's net investment outstanding.

2.17 CASH AND CASH EQUIVALENTS

For the purpose of the cash flow statement, cash and cash equivalents comprise cash on hand and balances held with central banks except for obligatory reserves, securities held for trading, loans to banks and debt securities not held for trading with original maturity up to 90 days.

2.18 NON-CURRENT ASSETS AND DISPOSAL GROUPS CLASSIFIES AS HELD FOR SALE

The Bank classifies a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale and the sale should be expected to be completed within one year from the date of classification. Although the management of the Intesa Sanpaolo Group changed the classification of real estate at the end of 2017 and the sale is not completed within one year from the classification, according to the Management estimates, the sale is close to be finalised and it is expected to be closed within Q1 2019. For that reason the Management has not reclassified assets back to original classification.

Immediately before classification as held for sale, the assets (or components of a disposal group) are remeasured in accordance with the Bank's accounting policies. Thereafter, the assets (or disposal group of assets and liabilities) are measured at the lower of their carrying amount and fair value less cost to sell.

A non-current asset classified as held for sale is no longer depreciated. Impairment losses on initial classification as held for sale are included in the income statement, as well as gains and losses on subsequent measurement.

2.19 PROVISIONS

Provisions are recognised in respect of present obligations arising from past events where it is probable that outflows of resources embodying past economic benefits will be required to settle the obligation; and they can be reliably estimated.

2.20 FINANCIAL GUARANTEES

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument. Financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.
Financial guarantee liabilities are initially recognised in the financial statements at their fair value on the date the guarantee is given. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise in the income statement the fee income earned on a straight line basis over the period, and the best estimate of the expenditure required to settle any financial obligation arising as the result of the guarantees at the reporting date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the management's judgment.

2.21 INCOME TAX

Current income tax has been calculated in accordance with the local tax law and using the tax rate of 19%.
Deferred income tax is calculated for all taxable temporary differences using the tax rate of 19%. Temporary differences are differences between the carrying amount of an asset or liability in the statement of financial position and its tax base. The tax rates (and tax laws) that have been enacted by the end of the reporting date are used to determine deferred income tax. The principal temporary differences arise from the valuation of financial instruments including derivatives, the valuation of real estates and provisions for retirement benefit obligations. A deferred tax asset shall be recognised for the carry forward of unused tax losses and unused tax credits to the extent that it is probable that future taxable profit will be available against which the unused tax losses and unused tax credits can be utilised.

2.22 EMPLOYEE BENEFITS

Employee benefits include jubilee benefits, retirement indemnity bonuses and other long-service benefits. According to Slovenian legislation, employees retire after 40 years of services, when, if fulfilling certain conditions, they are entitled to a termination benefit paid out as a lump sum. Valuations of these obligations are carried out by independent qualified actuaries, by using the book reserve method.
The Bank's obligation for the current service cost of providing pension benefits and the increment in the present value of the defined benefit obligation due to the approaching beginning of the defined benefit liability (interest cost) was assessed. The increase in the benefit scheme liabilities in excess of the above two assessments shall be recognised as the actuarial gain or loss.

The defined benefit scheme liabilities are measured on an actuarial basis using the projected unit credit method, which measures actuarial liabilities in accordance with the expected wage/salary increase from the valuation date until the foreseen retirement of the employed person. The wage/salary increase comprises promotion and inflation-related rise.
Under IAS19, the calculated current scheme liabilities are discounted using the rates equivalent to the market yields at the balance-sheet date on high-quality corporate bonds that are denominated in the currency in which the benefits will be paid by the employer. Since there is no deep market in such bonds in the Republic of Slovenia, the discount rate is determined by reference to market yields on government bonds.

2.23 SHARE CAPITAL

Dividends on ordinary shares

Dividends payable to the holders of ordinary shares lower the equity in the period in which the declaration of the dividend is approved by Bank's owners.

Treasury shares

If the Bank repurchases its own equity instruments (treasury shares), the cost of the shares it has reacquired is deducted from equity. In case that the Bank subsequently sells its treasury shares, the consideration received is recognised directly in equity.

2.24 FIDUCIARY ACTIVITIES

The Bank acts as an intermediary on behalf and for account of customers who want to underwrite units of investment funds. A fee is charged for this service. These assets are not shown in the statement of financial position.

2.25 COMPARATIVE INFORMATION

The comparative information are prepared by using the same accounting policies as for the reporting period unless otherwise specified.

2.26 ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Bank makes estimates and assumptions about uncertain events, including estimates and assumptions about the future. Such accounting assumptions and estimates are regularly evaluated, and are based on historical experience and other factors such as the expected flow of future events that can be rationally assumed in the existing circumstances, but nevertheless necessarily represent sources of estimation uncertainty. The estimation of impairment losses in the Bank's credit risk portfolio and, as part of this, the estimation of the fair value of real estate collateral represents the major source of estimation uncertainty. This and other key sources of estimation uncertainty, that have a significant risk of causing a possible material adjustment to the carrying amounts of assets and liabilities within the next financial year, are described below.

Impairment losses on loans and advances

Information about judgements mode relating to classification of financial assets; assessment of business model within which the assets are held and assessment of whether the contractual terms of the financial assets are solely payments of principal and interest on the principal amount outstanding are discussed in Note 2.4.

Assumptions and estimation uncertainties related to impairment of financial instruments, assessment of whether credit risk on financial assets has increased significantly since initial recognition and incorporation of forward looking information in measurement of ECL is described in Note 3.3.

Measurement of employee benefits

For the calculation of actuarial gains and losses, the following assumptions have been used:
- The discount rate of 1.88% (2017: 1.47%), and
- Future salary increases of 2.5% p.a. for 2019 and 2.5% p.a. from 2020 onwards (2017: 1.62%).

Taxation

The Bank provides for tax liabilities in accordance with the tax laws of the Republic of Slovenia. Tax returns are subject to the approval of the tax authorities which are entitled to carry out subsequent inspections of taxpayers' records.

Litigation and claims

The Bank performs an individual assessment of all court cases and creates provisions in accordance with the assessment. The assessment of risks and proposal for provisions for legal cases is performed by the Legal Affairs Department and Finance Division, and a decision on the creation of provisions is made by the Bank's management.

As stated in Note 39, the Bank provided EUR 1,833 thousand (2017: EUR 1,779 thousand), which management estimates as sufficient. Since the estimate is made considering the specifics of each individual case, it is not practicable for management to evaluate the financial impact of changes to the assumptions based on which provisions are quantified as at the reporting date.

Fair value of property

The Bank uses the revaluation model for property. The criterion of revaluation model requires that the asset have to be amortized on the basis of new revalued value.

Changes to the accounting policies on property

In 2017 the Bank has changed the accounting criteria for the disclosure and measurement of the following classes of tangible assets:
- property (governed by IAS 16 "Property, Plant and Equipment);
- property held for investment (governed by IAS 40 "Investment property").

The amendment, applied from 2017 financial statements, has led in particular to:
- change from the cost model to revaluation after initial disclosure of property;
- change from measurement at cost to measurement at fair value for investment property.

Considering that the change in the valuation criterion occurred at the end of the 2017 amortisation for 2017 has been calculated using the preceding cost criterion; therefore, all property, has been amortised up to 31 December 2017. As of 2018, property, valued using the criterion of revaluation according to IAS 16, will continue to be amortised for the estimate useful life.

Fair value of financial instruments

If a market for a financial instrument is not active, or, if for any reason, fair value cannot be reasonably measured by market price, the Bank establishes fair value using a valuation technique (except for certain unquoted equity securities). Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent to the financial instrument.

3. RISK MANAGEMENT ORGANISATION

The risk management policies and their implementation in the Bank's operational processes are of high importance for a sound business activity. The Bank has harmonised its risk management process with the risk management framework of the Intesa Sanpaolo Group. Therefore, risk management is governed in accordance with the Group best practices, which require a strong institution-wide risk culture involving Bank's management at all levels, and an independent risk management function.

The risk management process is divided in several stages, starting with the risk identification and measurement, which allows the Bank to understand the different types of risk, to measure its potential impact and to recognise in advance possible trends that can significantly change its business environment. The second step is the management of risk, whereby the Bank has to undertake strategic decisions on the type and the level of risk to be assumed, to establish whether to mitigate, diversify or reduce risk exposure and to establish risk limits in line with the Bank's risk capacity and risk appetite. Once risk has been assumed, it shall be properly overseen, which means monitoring risk tolerance limits and reporting to the Bank's governing bodies.

The most important risks in terms of Bank's total exposure are credit risk, interest rate risk, liquidity risk and operational risk.

3.1 CORPORATE RISK MANAGEMENT AND ORGANIZATIONAL STRUCTURE

3.1.1 Corporate risk management

The following structures take part in the risk governance process:

The Supervisory Board approves the strategic directions and risk management policies and reviews the efficiency and adequacy of the overall risk management process within the Bank.

The Risk Committee is an advisory body to the Supervisory Board, which provides advice regarding the Bank's current and future propensity to assume risk and provides assistance in the supervision of senior management with respect to the implementation of the risk management strategy.

The Audit Committee is an advisory body to the Supervisory Board with responsibility to give recommendations and advice to the Board in particular on matters relating to evaluation of the adequacy and efficiency of the Bank's entire system of internal controls over financial reporting including oversight of exposure to risk.

The Management Board is responsible for the approval and implementation of risk management policies and internal controls; it establishes organisational and other conditions for the execution of risk policies and controls.

The Asset and Liability Committee (ALCO) evaluates the exposure to financial risks and give guidance about measures necessary to manage financial exposures.

Credit Risk Governance Committee defines and update credit risk strategic guidelines and credit management policies based on the constant credit portfolio monitoring.

Credit Committee is the highest permanent decision-making committee of the Bank regarding performing counterparties, whose main responsibility consists in adopting credit decisions in line with the issued strategic guidelines and credit policies.

Problem Assets Committee is the highest permanent decision-making committee of the Bank regarding risky and non-performing counterparties, whose main responsibility consists in taking the necessary measures in order to prevent and mitigate credit losses connected with risky and deteriorated assets.

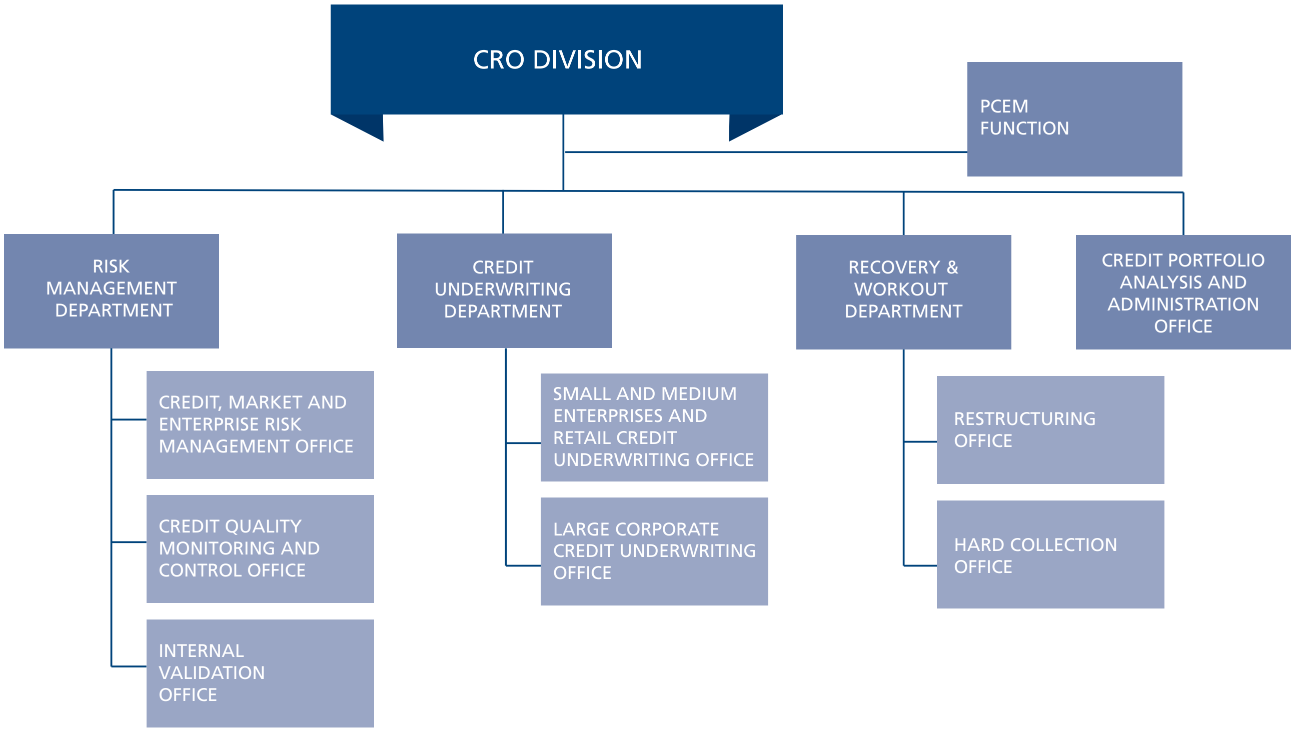
The Internal Audit Department evaluates and reviews processes, procedures, guidelines, policies and all operating activities performed by the Bank with the aim to evaluate the efficiency and effectiveness of the internal controls system and risk management system.

The Compliance and AML Department assesses and manages compliance risk in relation to domestic or international rules and internal acts, and mitigate activities that could damage the reputation of the Bank.

3.1.2. The organisational structure of Risk Division

The Risk Division (CRO area) is responsible for the risk management processes of the Bank. The person in charge of the Risk Division is a Member of the Management Board.

The organisation chart of the Risk Division:



The roles of organisational units within the Risk Division

Under the **Risk Management Department** are organized three offices, which have specific responsibilities related to second level risk control activities:

- **Credit, Market and Enterprise Risk Management Office** is responsible for risk policies, risk methodologies and reporting on risk exposures. In addition the Office monitors internal risk limits and external regulatory constraints, including the minimum capital adequacy ratios.
- **Credit Quality Monitoring and Control Office** is performing second level controls and monitoring activities over the credit portfolio, in terms of quality, composition and considerable changes.
- **The Validation Office** is in charge of evaluating the compliance of the internal systems of risk measurement and management with the regulatory requirements and their alignment with ISP Group guidelines. The Validation Office is responsible for the evaluation of the internal systems of all risk profiles (to be used for both regulatory and internal management purposes) in all the phases of the internal systems lifecycle, also supporting the Supervisory Authorities in their review activities.

  With specific regard to the credit risk, the role of Validation Office is to evaluate the adequacy and suitability of the internal rating systems, from both a design point of view (analysis of the methodological choices with regard to the regulatory requirements and internal and external best practices) and a performance point of view (back-testing analysis and periodical model monitoring). The validation analysis consists also of independent re-performance of the rating and development of alternative methodologies to be used as a benchmark.

Proactive credit exposure management contributes to the implementation of an early warning system, designed to activate the necessary measures against the identified clients by defining and agreeing with business functions the most proper action plans.

The **Credit Underwriting Department** analyses and approves loans and credit facilities to individual borrowers. There are two offices that operate within the framework of the Department: Small, Medium Enterprises and Retail Credit Underwriting Office and the Large Corporate Credit Underwriting Office.

The Recovery and Workout Department analyses and approves credit proposals for non-performing clients, participates in loan restructuring and in designing other measures in relation to borrowers with positive recovery perspective (going concern business) as much as in relation to obligors in legal enforcement status (gone concern business), seeking for the loss reduction and efficient recovery.

Credit portfolio analysis and administration office performs administrative controls in credit processes in order to verify the completeness of loan documentation before disbursement and performs credit portfolio analysis aimed at identifying negative trends and/or potential issues in the process, requiring further investigations by competent structures.

3.2 CAPITAL ADEQUACY AND OWN FUNDS (CAPITAL) MANAGEMENT

The Bank's capital includes common equity (mainly paid up capital and retained earnings). The function of the capital is to ensure long-term stability of the Bank and safeguard Bank's stakeholders.

The Bank meets the minimum capital requirement, as requested by the EU Regulation on prudential requirements for credit institutions (Capital Requirements Regulation or CRR). The CRR prescribes the minimum capital requirement, which is calculated according to the binding rules for the determination of risk- weighted assets. In addition, the CRR defines the general guidelines on the self-directed internal assessment of risk and capital requirement (Internal capital adequacy assessment process or ICAAP).

3.2.1 Compliance with the regulatory capital requirement

The regulatory capital requirement is calculated in line with CRR Regulation and is determined as a ratio between the Bank's capital and risk-weighted assets. Capital requirements have to be set aside for credit, market and operational risk. Banks have to meet the CET1 minimum capital requirement of 4.5% or higher, and the minimum own funds requirement of 8%. The Bank's capital is composed of the Common Equity Tier 1 capital and to less extent of Tier 2 capital. As of 31 December 2018, the Bank`s capital amounts to 271 million euros, whereas the CET1 ratio was 15.80%. The capital ratio was adequate and above the minimum capital requirement as defined by regulation, as well as with regard to the Pillar II framework, that is the internal assessment of capital requirement of the Bank (ICAAP) and the supervisory review process (SREP) evaluation of Pillar II.

The Bank maintains the minimum capital adequacy and the minimum amount of capital by regularly reporting the capital position to the highest governance bodies and by providing annual and strategic capital planning. A capital growth corresponding to the increase of risk capital activities was provided with proper retention of profits within the capital reserves.

(in thousands of euros)

Capital adequacy as at 31 December 2018	Risk weighted amount (unaudited)		Capital	
	2018	2017	2018	2017
Credit risk exposures of banking book				
Exposures to state and central bank	11,575	7,813	926	625
Exposures to local municipalities	16,037	12,154	1,283	972
Exposures to public sector	4,259	2,930	341	234
Exposures to development banks	-	-	-	-
Exposures to institutions	22,302	22,344	1,784	1,788
Exposures to enterprises	165,221	135,172	13,218	10,814
Exposures to equity	-	-	-	-
Exposures to retail banking	624,629	554,638	49,970	44,371
Past due exposures	13,457	27,064	1,077	2,165
Exposures to highly risk exposures	21,604	23,032	1,728	1,843
Exposures to investments funds	1,455	1,334	116	107
Exposures to other assets	-	-	-	-
Exposures to corporates-other IRB	458,087	362,435	36,647	28,995
Exposures to corporates-SME IRB	164,839	192,367	13,187	15,389
Exposures to equity IRB	20,296	17,636	1,624	1,411
Exposures to other assets IRB	59,807	62,132	4,785	4,971
Total	**1,583,568**	**1,421,051**	**126,686**	**113,685**
Credit risk weighted assets	1,583,568	1,421,051	126,686	113,685
Market risk weighted assets	368	701	29	56
Operational risk weighted assets	131,440	136,120	10,515	10,890
Total risk weighted assets	**1,715,376**	**1,557,872**	**137,230**	**124,631**
Regulatory capital				
Share capital	22,173	22,173		
Share premium	7,499	7,499		
Treasury shares	(49)	(49)		
Legal reserves	15,471	15,260		
Statutory reserves	214,055	214,054		
Treasury shares fund reserves	49	49		
Retained earnings due to transition to IFRS	1,964	6,009		
Accumulated other comprehensive income	12,447	16,023		
Less intangible assets	(4,071)	(3,517)		
Other transitional adjustments				
Unrealised gains/losses on government bonds	-	(4,594)		
Unrealised gains/losses on other shares	-	(229)		
Deferred tax assets that rely on future profitability and do not arise from temporary differences	-	-		
Requirements from prudent valuation of debt securities	(263)	(182)		
Recognised impairments for credit risk during the year	(2,494)	(3,265)		
IRB shortfall of provisions to expected losses	-	(1,549)		
Total qualifying Tier 1 capital	**266,781**	**267,682**		
IRB Excess of provisions over expected losses	**4,218**	**3,635**		
Total qualifying Tier 2 capital	**4,218**	**3,635**		
Total regulatory capital	**270,999**	**271,317**		
Capital Adequacy ratio (%)	**15.80**	**17.42**		

3.2.2 Risk Appetite Framework Limits

With the Risk Appetite Framework (RAF) limits have been established as a system of risk metrics that represent risk amounts the Bank is willing to assume. The RAF limits represent the highest level of aggregate risk representation with break down to top of the house limits, local specific risk limits and early warning indicators. Alongside the limits the Risk Appetite Framework establishes controls and procedures in case of limit breach and the roles regarding the definition and approval of RAF limits. The RAF limits also define the target amount of Available financial resources (internally assessed available capital sources) through the target AFR/ECAP ratio (Available Financial Resources/ICAAP capital charges excluding stress test).

3.3 CREDIT RISK

Credit risk is the risk of financial loss arising from a debtor's failure to repay its financial obligations. Credit risk is, by scope and strategic business orientation, the most important risk for the Bank.

The credit risk is associated with financial assets measured at amortised cost (loans and other claims). Loans & Receivables whose payments are not composed solely of principal and interest, have to be measured at fair value through profit and loss (FVTPL). The credit risk is evaluated with accurate credit analysis and corresponding credit classification of the borrower. Credit risk of derivative contracts is measured at replacement cost. The replacement cost is made up of the positive value of the deal, which represents a positive difference between the settlement price and the contractual price of the instrument, increased for the add-on, accommodating for a potential increase of positive value.

The Bank's credit risk related portfolio at the end December 2018 amounted to EUR 2.890 million of which 96% is classified as performing. Total risk portfolio includes all asset and off-balance sheet items, which are subject to credit risk according to the Bank of Slovenia methodology.

Intesa Sanpaolo Bank's credit risk related portfolio as at 31 December 2018

(in thousands of euros)

Counterparties	Total gross credit risk portfolio	Total credit risk portfolio, excluding debt securities	Share in %	Performing	Share in %	Non-performing	Share in %	Impairment losses on performing portfolio	Coverage rate of performing portfolio	Impairment losses on non performing portfolio	Coverage rate of non-performing portfolio
1	2	3	4	5	6	7	8	9	10=9/5	11	12=11/7
Central bank and government bodies	644,772	375,235	13%	375,235	13%	-	0%	77	0%	-	0%
Corporate entities	1,605,537	1,584,197	55%	1,491,420	54%	92,777	86%	13,402	1%	66,361	72%
Banks	110,255	98,022	3%	98,022	4%	-	0%	50	0%	-	0%
Private individuals	832,981	832,981	29%	818,294	29%	14,687	14%	4,336	1%	9,531	65%
Total	**3,193,545**	**2,890,435**	**100%**	**2,782,971**	**100%**	**107,464**	**100%**	**17,865**	**1%**	**75,892**	**71%**

Intesa Sanpaolo Bank's credit risk related portfolio as at 31 December 2017

(in thousands of euros)

Counterparties	Total risk portfolio	Total credit risk portfolio, excluding debt securities	Share in %	Performing	Share in %	Non-performing	Share in %	Impairment losses on performing portfolio	Coverage rate of performing portfolio	Impairment losses on non performing portfolio	Coverage rate of non-performing portfolio
1	2	3	4	5	6	7	8	9	10=9/5	11	12=11/7
Central bank and government bodies	602,002	302,267	12%	302,267	12%	-	0%	40	0%	-	0%
Corporate entities	1,489,113	1,487,633	57%	1,327,755	55%	159,878	93%	12,643	1%	84,554	53%
Banks	96,409	91,081	3%	91,081	4%	-	0%	14	0%	-	0%
Private individuals	714,040	714,040	28%	701,240	29%	12,800	7%	1,132	0%	6,582	51%
Total	**2,901,564**	**2,595,021**	**100%**	**2,422,343**	**100%**	**172,678**	**100%**	**13,829**	**1%**	**91,136**	**53%**

Analyses by type of collateral

(in thousands of euros)

	2018		2017	
	Net loans	Fair value of collateral	Net loans	Fair value of collateral
Real estate	514,552	1,645,940	506,619	1,677,185
Bank guarantees	41,263	55,199	42,212	56,017
Personal guarantees	286,448	797,616	228,396	615,254
Debt securities	19,341	49,391	9,544	22,708
Government guarantees	200,467	227,260	230,728	257,404
Other collateral	74,491	192,777	69,516	194,523
Deposits	2,236	4,865	1,828	3,911
Insurance company guarantees	106,774	136,030	103,261	126,807
Total collateralised net loans	**1,245,572**	**3,109,078**	**1,192,104**	**2,953,809**
Unsecured	512,399	-	482,923	-
Total net loans to non-bank customers*	**1,757,971**	**-**	**1,675,027**	**-**

**This amount include also the amount of net loans classified as mandatorily at FV through profit or loss*

In general loans can be secured with one or more types of collateral. The Bank's decision when collateral is acceptable depends on the obligor's credit worthiness and the type, amount and maturity of lending facilities. When accepting real estate as collateral, there is considered the value, assessed by independent evaluators, while in the exposure's life-time the value of collateral is monitored yearly and is periodically revalued at its fair value changes. For loans exceeding 3 mln EUR or 55% of the capital of the bank, there is obtained a new evaluation every 3 years. Securities and collective investment units, quoted on the market are revalued weekly, whereas movable property collateral are revalued yearly.

Credit exposure measurement

The Bank`s credit exposure includes financial assets that are debt instruments, commitment to lend, guarantee contracts issued and lease receivables. The credit exposures arising from derivative contracts are reported at replacement cost.

Maximum exposure to credit risk

(in thousands of euros)

	Maximum exposure	
	2018	2017
Credit risk exposures relating to on-balance sheet assets are as follows:		
Loans to banks	53,623	41,142
Loans to non-bank customers:*	1,755,736	1,675,725
Loans to individuals:	641,579	584,658
- overdrafts	24,652	21,897
- credit cards	13,158	16,504
- term loans	130,396	114,327
- mortgages	467,724	425,010
- finance leases	5,649	6,920
Loans to sole proprietors	48,070	48,619
Loans to corporate entities	1,066,087	1,042,448
Debt securities at amortised cost	1,266	-
Advances	18,727	13,731
Available for sale financial assets:	-	302,891
- debt securities	-	302,891
Non-trading financial assets mandatorily at fair value through profit or loss:	1,461	-
- loans and advances	1,461	-
Financial assets at fair value through other comprehensive income:	300,494	-
- debt securities	300,494	-
Other assets**	372,490	271,402
Credit risk exposures relating to off-balance sheet items are as follows:		
Guarantees and documentary letters of credit	163,846	170,918
Credit commitments and other credit related liabilities	432,145	320,790
At 31 December	**3,099,788**	**2,796,599**

**Maximum exposure of loans to non-bank customers does not include valuation of loans subject to micro hedge*
***Including balances with central bank, demand deposits and taxes and contributions*

The maximum exposure to credit risk represents the worst case scenario of credit risk exposure to the Bank at 31 December 2018 and 2017, without taking into account any collateral held or other attached credit enhancements. For off-balance-sheet assets, the exposures set out above are based on net amounts after impairments as reported in the statement of financial position.

Credit Classification

The Bank`s credit portfolio classified as performing assets have to subject to credit analysis and get assigned internal credit rating. For provisioning purposes, a PD rate equivalent to PD rate of internal rating grade S1 is assigned to unrated borrowers. In addition and according to IFRS9 reporting standards the counterpart are classified in three stages. Stage 1 are classified performing assets with unchanged or not deteriorated creditworthiness measured from the origination, while in stage 2 are classified credit assets for which the Bank recognised a significant increase of credit risk from its origination. In stage 3 are classified non-performing assets.. The criteria for recognition of significant credit risk and therefore classification in stage 2 are forbearance measures, identification and confirmation of early warning signals, rating downgrade and material due payments in arrears over 30 days.

The credit rating system arrange credit risk counterparts in 15 rating grades according to the probability of default severity. The Bank developed and implemented internal rating system for Corporate and SME clients and has been developing one for other core business segments: micro segment and private individuals. The statistical models are designed such to calculate a credit score based on debtor's financial data, behavioural data and qualitative information, which jointly make up a final score. Rating attribution process is supported with the system, which ensures required controls and is driving the process in accordance with the responsibilities and roles of functions involved in credit deliberation activity.

The obligor's classification is compliant with the European Banking Authority requirements, which has established rules for the classification of exposures to performing or non-performing categories. The non-performing obligors are further broken-down into the following categories: past due, unlikely to pay and doubtful. The work-out strategy for non-performing obligors depends on whether the Bank evaluates the borrower as going concern or gone concern, with the later expecting that the financial difficulties cannot be resolved.

Significant increase in credit risk (SICR)

The Bank considers a financial instrument to have experienced a significant increase in credit risk when one or more of the quantitative or qualitative criteria have been met. Criteria for determining a significant increase in credit risk are defined for the proper allocation of exposure in "Stage 1" or "Stage 2".

Elements that will be the main determinants which need to be considered for the purpose of assessing the "steps" between the various "stages" are the following:

- Default probability change or certain number of rating notch deterioration in relation to the moment of initial entry of the financial instrument in the financial statements. It is therefore an assessment implemented by adopting the "relative" criterion, which is configured as the main criteria;
- Eventual presence of due amount which remains overdue over 30 days. In the event of such case the credit risk of such exposure is considered "significantly increased" and is classified to Stage 2;
- Existence of "forbearance" measures;
- Qualitative information on credit quality deterioration due to which the client is included in the monitoring list;
- Certain indicators of the internal credit risk monitoring system and early warning system

Determining whether the specific factor is relevant, as well as its significance in relation to other factors, depends on the type of products and characteristics of the financial instrument. Consequently, it is not possible to define a unique set of factors that determine whether there has been a significant increase in credit risk.

Definition of default and staging criteria

Staging criteria are selected in line with IFRS9, and based on risk parameters available in the Bank. Main indicators that are used are transaction classification, Days past due, Forbearance, PCEM (watch list) Indicator and/or Early Warning System (EWS) model for Small Business, SME and Large Corporate portfolios. Considering that, Stage 3 is equal to Non-performing status of the loan, the key element in Stage assignment is recognition of increasing credit risk of a financial instrument. Significant increase of credit risk could be highlighted by quantitative and qualitative indicators as:

- Past Due days
- Forborne status
- Early warning signals and/or Proactive Credit Management watch list status of the customer

In addition, forbearance measures could represent a significant increase in credit risk since they consist of concessions towards a debtor facing or about to face difficulties in meeting its financial commitments.

Stage assignment for Loans:

Loan exposures towards Legal entities:

Condition - business condition (event) for assignment of stage	Stage
Risk class is Past Due, Unlikely to pay or Doubtful	3
DPD >30 with materiality threshold over 5% at reporting date	2
Early warning system shows significant deterioration in credit risk (PCEM flag)	2
Contract is Forborne	2
Exposures with credit deterioration: Lifetime PD Comparison (used for Sovereign, PSE, Banks – not for others segments)	2
Exposures with credit deterioration: Rating deterioration in the extent of 3 rating notches or more for low risk obligors to 1 notch or more for high risk obligors (used for Corporate and Small business segments – not for others segments)	2

Loan exposures towards Retail:

Condition - business condition (event) for assignment of stage	Stage
Risk class is Past Due, Unlikely to pay or Doubtful	3
DPD >30 with materiality threshold over 5% at reporting date	2
Early warning signals for retail exposures show significant deterioration in credit risk:	2
Contract is Forborne	2

Inclusion of forward looking element

Projection of Lifetime credit risk parameters under IFRS 9 requires inclusion of forward looking macroeconomic elements, in order to estimate future point-in-times risk drivers.

Inclusion of forward looking macroeconomic effect is based on EBA stress test coefficients. EBA stress test coefficients are used for creation of scenario for the three years, relative to the starting point of every bank. Stress test coefficient are multipliers for risk parameters: PD, LGD and LR-Loss rate. This step includes calculation of PD conditioned by EBA Stress Test coefficients. Since EBA releases only Baseline and Adverse coefficients, Best scenario coefficients have to be estimated in order to include add-on component into Lifetime PD.

Credit quality analysis

(in thousands of euros)

	2018					2017
	12 month ECL	Lifetime ECL – not credit impaired	Lifetime ECL - credit impaired	POCI	Total	Total
Loans and advances to banks at amortised cost						
Performing	53,655	-	-	-	53,655	41,146
Loss allowance	(32)	-	-	-	(32)	(4)
Carrying amount	**53,623**	**-**	**-**	**-**	**53,623**	**41,142**
Loans and advances to customers at amortised cost						
Performing	1,606,888	-	-	-	1,606,888	1,608,126
Watch list	-	136,783	-	-	136,783	-
Past due impaired	-	-	668	-	668	4,219
Unlikely to pay	-	-	40,124	7,812	47,936	89,178
Doubtful	-	-	52,678	-	52,678	73,697
Loss allowance	(8,758)	(6,741)	(72,366)	-	(87,865)	(100,193)
Carrying amount	**1,598,130**	**130,042**	**21,104**	**7,812**	**1,757,088**	**1,675,027**
Debt investment securities at amortised cost (2017: held-to-maturity/LAR)						
Performing	1,267	-	-	-	1,267	-
Loss allowance	(1)	-	-	-	(1)	-
Carrying amount	**1,266**	**-**	**-**	**-**	**1,266**	**-**
Debt investment securities at FVOCI (2017: available-for-sale)						
Performing, low risk	300,568	-	-	-	300,568	302,891
Loss allowance	(74)	-	-	-	(74)	-
Carrying amount - fair value	**300,494**	**-**	**-**	**-**	**300,494**	**302,891**
Loan commitments						
Performing	412,694	11,599	-	-	424,293	312,908
Watch list	1,462	162	-	-	1,624	1,166
Past due impaired	-	-	190	-	190	113
Unlikely to pay	-	-	519	-	519	301
Doubtful	-	-	190	-	190	82
Loss allowance	(905)	(114)	(619)	-	(1,638)	(781)
Carrying amount (provision)	**413,251**	**11,647**	**280**	**-**	**425,178**	**313,789**
Financial guarantee contracts						
Performing	147,367	2,255	-	-	149,622	166,981
Watch list	2,010	11,881	-	-	13,891	2,806
Past due impaired	-	-	-	-	-	131
Unlikely to pay	-	-	1,008	-	1,008	1,223
Doubtful	-	-	2,099	-	2,099	2,648
Loss allowance	(707)	(296)	(1,770)	-	(2,773)	(2,872)
Carrying amount (provision)	**148,670**	**13,840**	**1,337**	**-**	**163,847**	**170,917**
Loans mandt. FVTPL						
Unlikely to pay	-	-	882	-	882	-
Carrying amount (provision)	**-**	**-**	**882**	**-**	**882**	**-**

Credit quality loan analysis - summary

(in thousands of euros)

	2018					2017
	12-month ECL	Lifetime ECL not credit - impaired	Lifetime ECL credit - impaired	POCI	Total	Total
Balance exposures						
Gross carrying amount	1,962,378	136,783	94,352	7,812	2,201,325	2,119,257
Loss allowance	(8,865)	(6,741)	(72,366)	-	(87,972)	(100,197)
Net carrying amount	**1,953,513**	**130,042**	**21,986**	**7,812**	**2,113,353**	**2,019,060**
Off-balance exposure						
Gross carrying amount	563,533	25,897	4,006	-	593,436	488,359
Loss allowance	(1,612)	(410)	(2,389)	-	(4,411)	(3,653)
Net carrying amount	**561,921**	**25,487**	**1,617**	**-**	**589,025**	**484,706**

Note:
STAGE 1: 12-month ECL
STAGE 2: Lifetime ECL not credit-impaired
STAGE 3: Lifetime ECL credit-impaired

Changes in credit-impaired loans to non-bank customers

(in thousands of euros)

	2018	2017
Credit-impaired loans (Stage 3) at 31 December	**78,857**	**87,565**
Transfer to loans mandatorily FVTPL	(18,878)	-
Additional impairment due to IFRS 9	(620)	-
Credit-impaired loans (Stage 3) at 1 January	**59,359**	**87,565**
Change in allowance for impairment	(10,812)	(21,498)
Classified as credit-impaired (2017: impaired) during the year	11,136	45,798
Transferred to not credit-impaired (2017: impaired) during the year	(16,851)	(4,105)
Net repayments	(7,216)	(28,874)
Disposals	(6,773)	-
Write-offs	-	-
Other movements	72	(29)
Credit-impaired loans (Stage 3) at 31 December	**28,915**	**78,857**

Impairment provisions for credit risk

The amount of impairment provisions (credit risk allowances) for credit risk are based on the estimated amount of expected credit losses, which is calculated based on borrower's credit rating grade and collateral received in pledge. Provisions are calculated using collective or analytical approach. Credit risk losses are calculated analytically for non-performing obligors, whose total exposure at the moment of default exceeded 250,000 euros and were classified as unlikely to pay or doubtful. The analytical assessment of provisions is carried out by estimation of expected cash-flows for each obligor individually recovered from the obligor's own assets or earnings and by selling collateral. The expected cash-flows are discounted using effective interest rate.

For performing assets and non-performing assets under 250.000 euros as well as those classified as Past due, credit risk allowances are calculated using collective provisioning methodology. Collective provisions are calculated by estimating the expected loss as a result of multiplication of the probability of default (PD rate), loss given the default (LGD rate) and expected exposure at the time of default (EAD). Loss estimation parameters are updated annually.

The PD rates are estimated by measuring transition rates from performing to non-performing status by pooling obligors with internal ratings according to rating grades, while for other obligors the respective assets are pooled according to the stage assigned.

Loss Given Default rates are estimated by groups of exposures of different obligors segments secured with the same type of collateral. The recovery rate is estimated using the ratio between the net present values of recoveries, less costs, and credit exposures at default (the work-out method).

Expected credit losses for financial asset in stage 1 are calculated over one-year horizon, while expected credit losses for financial assets in stage 2 are covered with provisions calculated over the lifetime of financial asset, taking into account the possibility of default and respective losses every year till the maturity of the asset, considering the residual outstanding amount of credit receivables over time. The risk parameters (PD and LGD) are modified taking into account the forward looking view by applying estimates of macroeconomic potential trends. These are estimated with the so called macroeconomic conditioning of ECL variables by multiplying them with an add-on that is derived from best, most-likely and worst scenario. The worst and most-likely scenarios were taken as equivalent of the EBA coefficients published for the use in the EU-wide stress testing exercise, while the best scenario was calculated with internal methodology equally relying on aforementioned EBA scenarios. The ECL variables have been conditioned for the first three years with respect to the reporting date for exposures classified in stage 2 using the approach described, while the average add-on of those 3 years has been applied for the conditioning of variables over the exposure's remaining lifetime period beyond three years. The conditioning for stage 1 is performed for the first year according to time extension taken into account in the calculation of ECL.

Loans that are considered genuinely unrecoverable are written off after all available legal actions have been taken. In cases where the amount of impairment is excessive due to improvement in the economic position of the obligor, the previously recognised impairment is reversed by debiting the loan losses adjustment account and crediting the income statement.

Large exposures

In order to limit the risk of large exposure, the Bank monitors the single-name credit concentration risk. The largest allowed exposure to a single borrower and connected entities is limited by CRR Regulation and should not exceed 25 per cent of the Bank's regulatory capital. In case of exposure to banks or banking groups the maximum allowed exposure is EUR 150 million.

Financial instrument`s breakdown by country risk

(in thousands of euros)

As at 31 December 2018	Slovenia	EU	*Of which Italy*	Other Europe	Rest of world	Total
Cash, cash balances at Central Banks and other demand deposits at banks	369,064	19,546	17,321	-	2,050	390,660
Financial assets held for trading	-	29	29	-	-	29
Non-trading financial assets mandatorily at fair value through profit or loss	2,137	-	-	882	-	3,019
Financial assets at fair value through other comprehensive income	189,369	122,050	79,169	-	3,212	314,631
Financial assets at amortised cost:	1,620,809	148,262	21,268	43,868	17,765	1,830,704
- debt securities	1,266	-	-	-	-	1,266
- loans to banks	6,444	27,187	15,905	19,992	-	53,623
- loans to non-bank customers	1,600,948	119,030	5,295	23,874	13,236	1,757,088
- advances	12,151	2,045	68	2	4,529	18,727
Derivatives – hedge accounting	-	1,023	1,023	-	-	1,023
Contingent liabilities and commitments	**562,031**	**26,416**	**3,438**	**525**	**53**	**589,025**
TOTAL EXPOSURES	**2,743,410**	**317,326**	**122,248**	**45,275**	**23,080**	**3,129,091**

(in thousands of euros)

As at 31 December 2017	Slovenia	EU	Of which Italy	Other Europe	Rest of world	Total
Cash, cash balances at Central Banks and other demand deposits at banks	252,094	33,739	30,860	-	1,251	287,084
Financial assets held for trading:	10	50	50	-	-	60
Financial assets designated at fair value through profit or loss	-	59	59	-	-	59
Available for sale financial assets	173,160	142,901	131,786	-	2,641	318,702
Loans and receivables:	1,595,831	72,570	20,284	45,058	16,441	1,729,900
- loans to banks	5,978	15,164	15,164	20,000	-	41,142
- loans to non-bank customers	1,579,799	56,109	5,116	25,058	14,061	1,675,027
- advances	10,054	1,297	4	-	2,380	13,731
Derivatives – hedge accounting	-	2,471	-	-	-	2,471
Contingent liabilities and commitments	**476,509**	**7,390**	**994**	**772**	**35**	**484,706**
TOTAL EXPOSURES	**2,497,604**	**259,180**	**184,033**	**45,830**	**20,368**	**2,822,982**

3.4 ANALYSIS OF PAST DUE FINANCIAL INSTRUMENTS, COMPARATIVE INFORMATION UNDER IAS 39

Past due financial instruments relate only to loans and advances portfolio, meanwhile other financial instrument portfolios do not record delays.

Loans and advances are summarised as follows:

Loans and advances by maturity (past due)

(in thousands of euros)

	31 December 2018		31 December 2017	
	Loans and advances to customers	Loans and advances to banks	Loans and advances to customers	Loans and advances to banks
Neither past due nor impaired (stage 1 and stage 2)	1,742,044	53,655	1,604,968	41,146
Past due but not impaired (stage 3)	1,627	-	3,157	-
Impaired	102,164	-	167,095	-
Gross	**1,845,835**	**53,655**	**1,775,220**	**41,146**
Impairment losses on loans and advances	(87,865)	(32)	(100,193)	(4)
Net	**1,757,970**	**53,623**	**1,675,027**	**41,142**

Neither past due nor impaired loans are considered to be of a sound credit quality. The Bank is closely monitoring the clients with occasional delay in repayment.

Loans and advances to customers by maturity and portfolio quality

(in thousands of euros)

31 December 2018	Individuals							Total loans and advances to customers
	Overdrafts	Credit Cards	Term loans	Mortgages	Finance leases	Sole proprietors	Corporate entities	
Neither past due nor impaired (stage 1 and 2)	24,452	12,852	129,920	467,028	5,320	48,146	1,054,326	1,742,044
Not past due but impaired (stage 3)	406	74	1,016	3,500	(132)	782	43,350	48,996
Past due but not impaired (stage 1 and 2)	187	413	138	147	22	146	575	1,628
Past due and impaired (stage 3)	587	784	2,447	4,272	883	5,002	39,193	53,168
Gross	**25,632**	**14,123**	**133,521**	**474,947**	**6,093**	**54,076**	**1,137,443**	**1,845,835**
Impairment losses on loans and advances	(980)	(965)	(3,125)	(7,222)	(444)	(6,006)	(69,123)	(87,865)
Net	**24,652**	**13,158**	**130,396**	**467,725**	**5,649**	**48,070**	**1,068,320**	**1,757,970**

Loans under not past due but impaired"relate mainly to restructured loans.

Loans and advances to customers by maturity and portfolio quality

(in thousands of euros)

31 December 2017	Individuals							Total loans and advances to customers
	Overdrafts	Credit Cards	Term loans	Mortgages	Finance leases	Sole proprietors	Corporate entities	
Neither past due nor impaired	21,457	15,776	112,989	421,205	6,292	45,628	981,621	1,604,968
Not past due but impaired	312	17	620	2,439	(86)	1,324	87,013	91,639
Past due but not impaired	151	600	135	169	47	161	1,894	3,157
Past due and impaired	633	693	2,469	4,364	902	7,584	58,811	75,456
Gross	**22,553**	**17,086**	**116,213**	**428,177**	**7,155**	**54,697**	**1,129,339**	**1,775,220**
Impairment losses on loans and advances	(655)	(582)	(1,885)	(3,865)	(235)	(6,079)	(86,892)	(100,193)
Net	**21,898**	**16,504**	**114,328**	**424,312**	**6,920**	**48,618**	**1,042,447**	**1,675,027**

Ageing of past due loans and advances to customers by type of customer, product and portfolio quality

(in thousands of euros)

31 December 2018	Individuals										Total individuals
	Overdrafts		Credit cards		Term loans		Mortgages		Finance leases		
	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	127	7	312	24	123	41	131	25	19	6	815
Past due 30 - 60 days	49	3	76	10	12	34	11	59	3	5	262
Past due 60 - 90 days	9	8	25	26	3	36	4	124	-	6	241
Past due over 90 days	2	569	-	724	-	2,336	1	4,064	-	866	8,562
Total	187	587	413	784	138	2,447	147	4,272	22	883	9,880

(in thousands of euros)

31 December 2018	Sole proprietors		Corporate entities		Total
	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	128	41	411	475	1,055
Past due 30 - 60 days	15	37	113	262	427
Past due 60 - 90 days	3	23	51	263	340
Past due over 90 days	-	4,901	-	38,193	43,094
Total	146	5,002	575	39,193	44,916

Decrease of past due loans and advances in 2018 is mainly due to write-offs. Write-offs of non-performing loans amounted to EUR 11,969 thousand (2017: EUR 22,798 thousand).

Ageing of past due loans and advances to customers by type of customer, product and portfolio quality

(in thousands of euros)

31 December 2017	Individuals										Total individuals
	Overdrafts		Credit cards		Term loans		Mortgages		Finance leases		
	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	134	3	514	13	119	32	139	17	36	5	1,012
Past due 30 - 60 days	13	1	69	12	13	13	20	12	9	4	166
Past due 60 - 90 days	4	-	17	8	3	14	7	10	2	5	70
Past due over 90 days	-	629	-	660	-	2,410	3	4,325	-	888	8,915
Total	**151**	**633**	**600**	**693**	**135**	**2,469**	**169**	**4,364**	**47**	**902**	**10,163**

(in thousands of euros)

31 December 2017	Sole proprietors		Corporate entities		Total
	Not impaired	Impaired	Not impaired	Impaired	
Past due up to 30 days	96	28	1,804	350	2,278
Past due 30 - 60 days	61	34	83	579	757
Past due 60 - 90 days	4	6	7	497	514
Past due over 90 days	-	7,516	-	57,385	64,901
Total	**161**	**7,584**	**1,894**	**58,811**	**68,450**

The breakdown of the gross amount of individually impaired loans and advances by class, along with the fair value of related collateral held by the Bank as security, is as follows:

Loans and advances individually impaired

(in thousands of euros)

31 December 2018	Individuals	Sole proprietors	Corporate entities	Total
Individually impaired loans	2,354	1,570	63,369	67,294
Fair value of collateral	2,106	1,126	30,861	34,093

(in thousands of euros)

31 December 2017	Individuals	Sole proprietors	Corporate entities	Total
Individually impaired loans	2,352	1,935	125,776	130,063
Fair value of collateral	2,683	2,682	122,563	127,928

In 2018, the Bank received EUR 18,368 thousand from the sale of pledged collateral.

3.5 LIQUIDITY RISK

Liquidity risk is defined as the risk of not being able to meet payment obligations as they fall due, due to difficulties to finance liquidity needs, or convert marketable assets into cash, including potential losses incurred due to forced trades. In order to manage liquidity risk, the Bank monitors liquidity ratio levels and mandatory reserves on a daily basis in order to maintain adequate liquidity position.

The minimum liquidity to be maintained by banks is defined by the Bank of Slovenia Regulation on the minimum requirements for ensuring an adequate liquidity position (Ur. l. RS, št. 50/15, 44/16 and 79/16), establishing a minimum liquidity ratio for assets and liabilities with maturity up to one month.

The liquidity position of the Bank is monitored with two additional ratios, the LCR (Liquidity Coverage Ratio) and NSFR (Net Stable Funding Ratio). The ratios have been introduced globally as principal liquidity measures necessary to ensure a minimum short-term liquidity as well long-term balanced funding of banks. Beside the mentioned indicators, the Bank as well calculates the so-called "Stress LCR", which is meant for monitoring the Bank's liquidity position in uncertain (stress) situation. It measures the stress LCR over a 3 month period. LCR is calculated in accordance with the Delegated Act regulation (2015/61), which came into force in 2016. LCR and NSFR indicators are regularly reported to ALCO and Audit Committee.

Liquidity ratios	31.12.2018	31.12.2017	31.12.2016
LCR	216%	238%	246%
NSFR	145%	147%	139%

The LCR and NSFR ratios through the past period were stable, showing no significant movement and compliant with the regulatory limit. The regulatory limit in force in 2018 was 100% for LCR, while internal RAF limits are set at 103% for LCR and 100% for NSFR. The LCR and NSFR ratios as of 31 December 2018 are stable and high above the limits and stand at the similar level, compared to the previous year. The liquidity buffer is comprised entirely out of assets, mostly withdrawable central bank reserves and government bonds. Total expected cash inflows are capped to 75% of total expected cash outflows.

The Treasury and ALM Department manages at the operating level the liquidity with daily cash-flow planning and maintains an adequate amount of eligible assets as collateral necessary for refinancing with the ECB.
The measures aimed at managing a liquidity crisis are defined with the Contingent Liquidity Plan, establishing early warning indicators and roles and actions to be considered in adverse financial circumstances.

Maturities of assets and liabilities - Non-derivative cash flows by contractual maturities

(in thousands of euros)

As at 31 December 2018	Contractual maturity - undiscounted						
	Carrying amount	Gross nominal Inflow/(out-flow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
ASSETS							
Cash, cash balances at Central Banks and other demand deposits at banks	390,660	390,660	370,139	-	-	-	20,521
Non-trading financial assets mandatorily at fair value through profit or loss	3,019	3,019	-	-	80	803	2,136
Financial assets at fair value through other comprehensive income	314,631	314,631	215	-	52,859	178,602	82,955
Loans and receivables:*	1,830,704	1,847,375	118,457	75,765	262,920	740,198	650,035
- debt securities	1,266	1,266	-	-	-	1,266	-
- loans to banks	53,623	53,623	31,641	16,983	4,999	-	-
- loans to non-bank customers	1,757,088	1,773,759	76,665	50,206	257,921	738,932	650,035
- advances	18,727	18,727	10,151	8,576	-	-	-
Total assets	**2,539,014**	**2,555,685**	**488,811**	**75,765**	**315,859**	**919,603**	**755,647**
LIABILITIES							
Financial liabilities measured at amortised cost:	2,289,275	2,289,275	1,937,813	90,285	189,418	60,720	11,039
- deposits from banks and central banks	15,517	15,517	1,516	2,000	6,168	5,833	-
- deposits from non-bank customers	2,207,670	2,207,670	1,906,816	80,617	180,817	39,020	400
- loans from banks and central banks	37,484	37,484	3,022	781	7,195	15,847	10,639
- loans from non-bank customers	32	32	1	2	9	20	-
- other financial liabilities	28,572	28,572	19,457	8,885	230	-	-
Total liabilities	**2,289,275**	**2,289,275**	**1,930,812**	**92,285**	**194,419**	**60,720**	**11,039**
Net liquidity gap	**249,739**	**266,410**	**(1,442,001)**	**(16,520)**	**121,440**	**858,883**	**744,608**

(in thousands of euros)

As at 31 December 2017	Contractual maturity - undiscounted						
	Carrying amount	Gross nominal Inflow/(outflow)	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
Total liabilities	2,091,860	2,091,860	1,685,807	101,514	225,513	65,346	13,680
Net liquidity gap	**243,885**	**255,841**	**(1,300,767)**	**8,500**	**178,504**	**701,820**	**667,784**

**Items presented in the above table include performing items which are presented in gross amount and non-performing exposures which are presented in net amount.*

The negative net liquidity gap in the 1 month time bucket should be viewed with additional consideration of specific liquidity profile of some balance sheet items, particularly sight deposits, which balances during 2018 kept increasing. Although sight deposits can be withdrawn at any time, they are considered (for liquidity management purposes) to be largely stable. This is demonstrated by the LCR treatment of sight deposits, whereby the run-off factor is 5%, representing the percentage of sight deposits deemed volatile in one month horizon. Moreover, on the assets side the available for sale financial assets include ECB eligible bonds, which are treated as liquidity reserves entering in the 1 month maturity bucket. The stable part of sight deposits and ECB eligible bonds counterbalance the 1 month net liquidity gap. The proof of this statement is the positive LCR ratio (calculated on the base of 30 days).

Maturities of assets and liabilities - Derivative cash flows by contractual maturity

(in thousands of euros)

As at 31 December 2018	Carrying amount	Gross nominal Inflow/(outflow)	Contractual maturity Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
DERIVATIVE ASSETS							
Derivatives held for trading:							
FX Forward	-	**1**	**1**	-	-	-	-
- Inflow	-	69	69	-	-	-	-
- Outflow	-	(68)	(68)	-	-	-	-
Interest rate cap:	**29**	**36,786**	**-**	**-**	**8**	**6,305**	**30,473**
- Inflow	-	36,786	-	-	8	6,305	30,473
- Outflow	-		-	-	-	-	-
Total	**29**	**36,787**	**1**	**-**	**8**	**6,305**	**30,473**
DERIVATIVE LIABILITIES							
Derivatives held for trading:							
FX Forward	-	(1)	(1)	-	-	-	-
- Inflow	-	68	68	-	-	-	-
- Outflow	-	(69)	(69)	-	-	-	-
Total	**-**	**(1)**	**(1)**	**-**	**-**	**-**	**-**
Net liquidity gap	**-**	**36,786**	**-**	**-**	**8**	**6,305**	**30,473**

(in thousands of euros)

As at 31 December 2017	Carrying amount	Gross nominal Inflow/(outflow)	Contractual maturity Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
Total derivative held for trading liabilities	8	596	222	324	50	-	-
Net liquidity gap	**-**	**61,173**	**-**	**1**	**3**	**12,663**	**48,506**

(in thousands of euros)

As at 31 December 2018	Carrying amount	Gross nominal Inflow/ (outflow)	Contractual maturity Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
DERIVATIVE ASSETS							
Derivatives held for hedge accounting:							
IRS	1,023	1,004	(40)	(54)	(213)	(252)	1,563
- Inflow		3,088	-	-	122	688	2,278
- Outflow		(2,084)	(40)	(54)	(335)	(940)	(715)
Total	**1,023**	**1,004**	**(40)**	**(54)**	**(213)**	**(252)**	**1,563**
DERIVATIVE LIABILITIES							
Derivatives held for hedge accounting:							
IRS	4,055	(2,540)	(918)	(386)	(1,003)	(4,692)	4,459
- Inflow		13,904	103	251	308	2,241	11,001
- Outflow		(16,444)	(1,021)	(637)	(1,311)	(6,933)	(6,542)
Total	**4,055**	**(2,540)**	**(918)**	**(386)**	**(1,003)**	**(4,692)**	**4,459**
Net liquidity gap	**-**	**(1,536)**	**(958)**	**(440)**	**(1,216)**	**(4,944)**	**6,022**

(in thousands of euros)

As at 31 December 2017	Carrying amount	Gross nominal Inflow/ (outflow)	Contractual maturity Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years
Total derivative for hedge accounting liabilities	660	(669)	(439)	(197)	(164)	(1,552)	1,683
Net liquidity gap	**-**	**1,694**	**(1,056)**	**(287)**	**(1,327)**	**(3,670)**	**8,034**

Cash flows of interest rate caps, interest options and interest rate swaps represent fairly the difference between contractual price and market price of derivatives.
The increase of cash-flows from derivatives in 2018 is a result of new IRS contracts made with the aim of providing interest rate hedge on loans extended with fixed contractual interest rate.

Contractual maturities of off-balance sheet items*

(in thousands of euros)

As at 31 December 2018	Contractual maturity			
	No later than 1 year	1-5 years	Over 5 years	Total
Documentary and commercial letters of credit	-	160	-	160
Guarantees	114,505	38,617	11,310	164,432
Credit commitments	398,778	27,702		426,480
Total	**513,283**	**66,479**	**11,310**	**591,072**

(in thousands of euros)

As at 31 December 2017	Contractual maturity			
	No later than 1 year	1-5 years	Over 5 years	Total
Total	**351,972**	**114,342**	**20,065**	**486,379**

**Items presented in the above table include performing items which are presented in gross amount and non-performing exposures which are presented in net amount.*

Financial assets available to support future funding

(in thousands of euros)

As at 31 December 2018	Encumbered		Non-encumbered	
	Pledged as collateral	Other	Available as collateral	Other
Loans on demand	-	23,777	-	347,800
Equity instruments	-	-	-	16,273
Debt securities	11,175	-	290,585	-
Loans and advances other than loans on demand	-	3,140	335,429	1,491,751
Other assets	-	-	-	77,991

(in thousands of euros)

As at 31 December 2017	Encumbered		Non-encumbered	
	Pledged as collateral	Other	Available as collateral	Other
Loans on demand	-	-	-	270,281
Equity instruments	-	-	-	15,870
Debt securities	11,315	-	290,163	1,413
Loans and advances other than loans on demand	-	1,701	377,699	1,350,500
Other assets	-	-	-	79,209

Bank's liquidity reserves

(in thousands of euros)

	31.12.2018		31.12.2017	
	Gross Carrying amount	Fair value amount	Gross Carrying amount	Fair value amount
Balances with central bank	324,642	324,642	214,816	214,816
Balances with banks up to 90 days	47,039	47,039	59,395	59,395
Unencumbered debt securities issued by sovereigns	257,341	243,661	298,712	269,260
Unencumbered debt securities eligible for use as collateral with central bank	31,828	31,351	2,795	2,515
Loans to customers eligible for use as collateral with central bank	331,476	172,569	378,288	298,175
Undrawn credit lines granted by banks	-	-	100,000	100,000
Total	**992,326**	**819,262**	**1,054,006**	**944,161**

3.6 BANKING BOOK EQUITY RISK

Equity risk is defined as the risk of unexpected losses arising from positions in available-for sale equity investments (shares or equity participations).
The Bank acquired these equity investments mainly with the repossession of financial collaterals arising from lending activity. These investments are managed pursuing the target of disposal in order to recover the relative credit exposures. In fact, most of these positions were already disposed of in the previous years, therefore only a few repossessed equity positions are left in the Bank`s balance sheet.

3.7 MARKET RISK

Market risk mainly arises from trading activities. The Bank only performs trading activities with the aim to respond to the demand of its customers and these activities mostly consist of buying and selling currency and derivative contracts.

The operational risk arising from trading activities is managed on the basis of a clear division between the front and back-office operations, which assures adequate controls and segregation of functions.

The Bank has established internal market risk limits on Fixed income VaR indicator, FX VaR indicator, open position by currencies and on credit sensitivity (CR01) of Italian government bonds.

3.7.1 Derivative instruments

The Bank takes on derivative transactions only for the purpose of serving customers requests and for hedging its own exposure towards interest rate risk. Since the Bank is not willing to assume any financial risk embedded in derivative contracts (position risk or change in the fair value of a derivative due to change in the value of the underlying asset), each single transaction is fully hedged back-to-back by immediately executing an offsetting transaction with another bank. The Bank assumes only the counterparty risk in these transactions, i.e. risk of substituting the original contract with other counterparty. The counterparty credit risk for the purpose of internal credit risk monitoring is determined as an amount equal to replacement cost, which is calculated as the highest value between the positive fair value of the instrument and a percentage of the nominal amount equivalent to the counterparty credit risk. The credit counterparty risk percentage is determined with internal model and applied according to the type and maturity of derivative contract.

3.7.2 Currency Risk

When there is an open position in a particular currency, the Bank is exposed to currency risk. The open currency position in a particular foreign currency is the difference between assets and liabilities denominated in that currency. For the purpose of measuring currency risk, the Bank takes into account the overall position composed of assets and liabilities denominated in that currency, FX spot transactions and currency derivatives.
The Bank measures and monitors currency risk on a daily basis:
- as a notional open position for a particular currency, and
- as Value-at-Risk (VAR) indicator for the global currency position.

The Value-at-Risk is a statistical estimation of a maximum loss at the 99 per cent confidence level over a 1-day period. The Value-at-Risk measure is proportional to the currencies open position and to the exchange rate volatility.

The average utilisation of FX Var limit in 2018 was low at 4.36% and the average utilization of Fixed income Var limit was 56.9%.

Bank VAR by risk type

(in thousands of euros)

	12 months to 31 December 2018			12 months to 31 December 2017		
	Average	High[1]	Low[1]	Average	High[1]	Low[1]
Foreign exchange risk (trading and non-trading portfolio)	1	4	0,4	2	9	1
Debt securities risk (banking book)	953	1,902	202	400	669	231
Total VAR	**954**	**1,906**	**202**	**402**	**678**	**232**

[1]Highest and lowest 99% VaR calculated for one-day observation period for the 12-month period as indicated in the table.

Currency risk

A currency is considered "significant" if the aggregate liabilities denominated in that currency amount to 5% or more of the bank's total liabilities. Currently no currency is exceeding this threshold.

(in thousands of euros)

As at 31 December 2018	EUR	USD	Other	Total
ASSETS				
Cash and balances with central banks and other demand deposits at banks	374,092	6,872	9,696	390,660
Financial assets held for trading:	29	-	-	29
- derivative financial instruments	29	-	-	29
Non-trading financial assets mandatorily at fair value through profit or loss	3,019	-	-	3,019
Financial assets at fair value through other comprehensive income	271,483	43,148	-	314,631
Financial assets at amortised cost:	1,790,701	20,660	19,343	1,830,704
- debt securities	1,266	-	-	1,266
- loans to banks	29,766	7,855	16,002	53,623
- loans to non-bank customers	1,740,944	12,804	3,340	1,757,088
- advances	18,725	1	1	18,727
Derivatives – hedge accounting	815	208	-	1,023
Total assets	**2,440,139**	**70,888**	**29,039**	**2,540,066**
LIABILITIES				
Financial liabilities held for trading:	-	-	-	-
- derivative financial instruments		-	-	-
Financial liabilities measured at amortised cost:	2,187,672	72,267	29,336	2,289,275
- deposits from banks and central banks	15,501	-	16	15,517
- deposits from non-bank customers	2,115,762	62,714	29,194	2,207,670
- loans from banks and central banks	28,873	8,611	-	37,484
- loans from non-bank customers	32	-	-	32
- other financial liabilities	27,504	942	126	28,572
Derivatives – hedge accounting	3,947	108	-	4,055
Total liabilities	**2,191,619**	**72,375**	**29,336**	**2,293,330**
Net balance sheet position	**248,520**	**(1,487)**	**(297)**	**246,736**
Part of contingent liabilities and commitments sensitive to currency risk	**426,186**	**244**	**84**	**426,514**

(in thousands of euros)

As at 31 December 2017	EUR	USD	Other	Total
Total assets	2,243,819	68,299	26,158	2,338,276
Total liabilities	1,997,166	69,100	26,262	2,092,528
Net balance sheet position	**246,653**	**(801)**	**(104)**	**245,748**
Part of contingent liabilities and commitments sensitive to currency risk	**315,819**	**216**	**86**	**316,121**

3.7.3 Interest rate risk

The table below summarises the Bank's exposure to interest rate risk. The assets and liabilities are recorded at carrying value, while the residual maturity is presented by contractual maturity for fixed-rate positions and by next contractual re-pricing date for floating rate positions.
Since for the fixed interest rate positions it is assumed that after contractual expiring will be reinvested or refinanced according to then prevailing market conditions, they were also included in the table herein below presenting the sensitivity to interest rate risk.

Interest rate risk

(in thousands of euros)

As at 31 December 2018	Carrying amount	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years	Non-interest bearing
ASSETS							
Cash and balances with central banks and other demand deposits at banks	390,660	327,898	-	-	-	20,521	42,241
Financial assets held for trading:							
- derivative financial instruments	29	-	29	-	-	-	-
Non-trading financial assets mandatorily at fair value through profit or loss	3,019	-	-	882	-	-	2,137
Financial assets at fair value through other comprehensive income	314,631	214	-	122,089	118,944	59,247	14,137
Financial assets at amortised cost:	1,830,704	167,477	193,646	995,935	171,529	271,109	31,008
- debt securities	1,266	-	-	-	1,266	-	-
- loans to banks	53,623	31,640	16,983	5,000	-	-	-
- loans to non-bank customers	1,757,088	135,837	176,663	990,935	170,263	271,109	12,281
- advances	18,727	-	-	-	-	-	18,727
Derivatives – Hedge accounting	1,023	815	-	208	-	-	-
Total assets	**2,540,066**	**496,404**	**193,675**	**1,118,232**	**290,473**	**350,877**	**89,523**
LIABILITIES							
Financial liabilities measured at amortised cost:	2,289,275	1,922,519	101,906	196,942	38,936	400	28,572
- deposits from banks and central banks	15,517	1,516	2,000	12,001	-	-	-
- deposits from non-bank customers	2,207,670	1,906,923	80,617	180,794	38,936	400	-
- loans from banks and central banks	37,484	14,079	19,258	4,147	-	-	-
- loans from non-bank customers	32	1	31	-	-	-	-
- other financial liabilities	28,572	-	-	-	-	-	28,572
Derivatives – Hedge accounting	4,055	2,955	544	556	-	-	-
Total liabilities	**2,293,330**	**1,925,474**	**102,450**	**197,498**	**38,936**	**400**	**28,572**
Total interest repricing gap		**(1,429,070)**	**91,225**	**920,734**	**251,537**	**350,477**	

(in thousands of euros)

As at 31 December 2017	Carrying amount	Up to 1 month	1-3 months	3-12 months	1- 5 years	Over 5 years	Non-interest bearing
Total assets	2,338,276	396,728	239,078	1,138,683	165,626	300,456	97,705
Total liabilities	2,092,528	1,671,040	147,858	200,860	33,437	1,196	38,137
Total interest repricing gap		**(1,274,312)**	**91,220**	**937,823**	**132,189**	**299,260**	

The Bank measures the following sources of interest rate risk:
- Repricing risk, stemming from a different interest rate adjustment of assets and liabilities to market interest rate changes. For fixed rate contracts the interest rate can be adjusted to market rate only at maturity, while floating rate contracts are adjusted according to contract revision of the interest rate and adjustment to market reference rate;
- Basis risk arises from imperfect correlation between different types of interest rates, which are relevant market rate reference for floating rate contracts;
- Yield curve risk, refers to changes in the slope and shape of the yield curve;
- Optionality risk, refers to optionality embedded in the Group's assets, liabilities and off-balance sheet instruments.

Interest rate risk is measured from two perspectives: it is analysed through the impact of market rate change on net present value of future cash flows and, on the other hand, it is viewed through the impact of market rate changes on net interest income and therefore on the Bank's annual financial results.

Accordingly, the following data are reported to the ALCO:
- Sensitivity of net interest income to a yield curve parallel shift of +/-50 bps over a 1-year time horizon;
- Sensitivity of economic value or net present value of future cash flows to a yield curve parallel shift of +/- 100 bps and +/- 200 bps;

The measurement of Interest rate risk is further improved by using the following models:
- Sight model: Assets without contractual maturities are classified into specific time buckets based on their estimated sensitivity on changes in interest rates.
- Prepayment model based on the probability that some of the loans outstanding will be paid off earlier than originally scheduled. Consequently, the planned cash flows of the outstanding loans are modified for the level of prepayment rate.
- Excepted loss model: cash flows of outstanding loans are modified for the probability of default rate originating from credit risk.
- Fund Transfer Pricing model: the entire spread on loans above the reference rate is divided into cost of funding and commercial spread. For interest-sensitive cash flows only the spread representing cost of funding is taken.

Sensitivity of net interest income of the Bank as of 31.12.2018

(in million of euros)

		+50 b.p.			+100 b.p.			-50 b.p.			-100 b.p.		
		Sight	**Term**	**Total**	**Sight**	**Term**	**Total**	**Sight**	**Term**	**Total**	**Sight**	**Term**	**Total**
Total		**(0.13)**	**5.31**	**5.18**	**(0.29)**	**10.65**	**10.36**	**0.09**	**(4.84)**	**(4.75)**	**0.18**	**(9.24)**	**(9.06)**
Asset		**1.86**	**4.89**	**6.75**	**3.73**	**9.80**	**13.53**	**(1.86)**	**(4.42)**	**(6.28)**	**(3.73)**	**(8.37)**	**(12.10)**
Sight Loans*		1.86	-	1.86	3.73	-	3.73	(1.86)	-	(1.86)	(3.73)	-	(3.73)
Securities	FX	-	0.24	0.24	-	0.49	0.49	-	(0.24)	(0.24)	-	(0.49)	(0.49)
	FL	-	0.20	0.20	-	0.42	0.42	-	(0.12)	(0.12)	-	(0.15)	(0.15)
Loans	FX	-	0.53	0.53	-	1.06	1.06	-	(0.53)	(0.53)	-	(1.06)	(1.06)
	FL	-	3.92	3.92	-	7.83	7.83	-	(3.53)	(3.53)	-	(6.67)	(6.67)
Other Financial Assets	FX	-	-	-	-	-	-	-	-	0.00	-	-	0.00
	FL	-	-	-	-	-	-	-	-	0.00	-	-	0.00
Liabilities		**(1.99)**	**(1.25)**	**(3.24)**	**(4.02)**	**(2.48)**	**(6.50)**	**1.95**	**1.25**	**3.20**	**3.91**	**2.48**	**6.39**
Sight Deposits		(1.99)	-	(1.99)	(4.02)		(4.02)	1.95	-	1.95	3.91	-	3.91
Securities Issued	FX	-	-	-	-	-	-	-	-	0.00	-	-	0.00
	FL	-	-	-	-	-	-	-	-	0.00	-	-	0.00
Debts	FX	-	(1.07)	(1.07)	-	(2.13)	(2.13)	-	1.07	1.07	-	2.13	2.13
	FL	-	(0.18)	(0.18)	-	(0.35)	(0.35)	-	0.18	0.18	-	0.35	0.35
Other Financial Liabilities	FX	-	-	-	-	-	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-	-	-	-	-	-
Derivatives		**-**	**1.67**	**1.67**	**-**	**3.33**	**3.33**	**-**	**(1.67)**	**(1.67)**	**-**	**(3.35)**	**(3.35)**

Cash flows slotted into time buckets according to their maturity or repricing date as of 31.12.2018

(in million of euros)

		Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
Total		**416**	**471**	**(42)**	**(73)**	**28**	**6**	**26**
Asset		**2.700**	**1.995**	**172**	**148**	**249**	**86**	**50**
Sight Loans*		392	392	-	-	-	-	-
Securities	FX	235	97	56	27	55	-	-
	FL	70	70	-	-	-	-	-
Loans	FX	689	197	94	102	172	78	46
	FL	1.314	1.239	22	19	22	8	4
Other Financial Assets	FX	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-
Liabilities		**(2.260)**	**(1.912)**	**(179)**	**(137)**	**(32)**	**-**	**-**
Sight Deposits*		(1.838)	(1.514)	(160)	(134)	(30)	-	-
Securities Issued	FX	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-
Debts	FX	(375)	(351)	(19)	(3)	(2)	-	-
	FL	(47)	(47)	-	-	-	-	-
Other Financial Liabilities	FX	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-
Derivatives		**(24)**	**388**	**(35)**	**(84)**	**(189)**	**(80)**	**(24)**

**Sight loans and deposits are those available on demand*

Sensitivity of net interest income of the Bank as of 31.12.2017

(in million of euros)

	+50 b.p.			+100 b.p.			-50 b.p.			-100 b.p.		
	Sight	Term	Total	Sight	Term	Total	Sight	Term	Total	Sight	Term	Total
Total	**0.59**	**5.05**	**5.64**	**0.35**	**10.10**	**10.45**	**(1.09)**	**(4.63)**	**(5.72)**	**(2.18)**	**(8.81)**	**(10.99)**
Asset	**1.36**	**5.08**	**6.44**	**2.75**	**10.18**	**12.93**	**(1.35)**	**(4.66)**	**(6.01)**	**(2.69)**	**(8.88)**	**(11.57)**
Sight Loans	1.36	-	1.36	2.75	-	2.75	(1.35)	-	(1.35)	(2.69)	-	(2.69)
Securities	-	0.20	0.20	-	0.41	0.41	-	(0.20)	(0.20)	-	(0.41)	(0.41)
	-	0.22	0.22	-	0.45	0.45	-	(0.20)	(0.20)	-	(0.28)	(0.28)
Loans	-	0.60	0.60	-	1.20	1.20	-	(0.60)	(0.60)	-	(1.20)	(1.20)
	-	4.06	4.06	-	8.12	8.12	-	(3.66)	(3.66)	-	(6.99)	(6.99)
Other Financial Assets	-	-	-	-	-	-	-	-	-	-	-	-
	-	-	-	-	-	-	-	-	-	-	-	-
Liabilities	**(0.77)**	**(1.46)**	**(2.23)**	**(2.40)**	**(2.93)**	**(5.33)**	**0.26**	**1.46**	**1.72**	**0.51**	**2.94**	**3.45**
Sight Deposits	(0.77)	-	(0.77)	(2.40)	-	(2.40)	0.26	-	0.26	0.51	-	0.51
Securities Issued	-	-	0.00	-	-	-	-	-	-	-	-	-
	-	-	0.00	-	-	-	-	-	-	-	-	-
Debts	-	(1.14)	(1.14)	-	(2.28)	(2.28)	-	1.14	1.14	-	2.29	2.29
	-	(0.32)	(0.32)	-	(0.65)	(0.65)	-	0.32	0.32	-	0.65	0.65
Other Financial Liabilities	-	-	-	-	-	-	-	-	-	-	-	-
	-	-	-	-	-	-	-	-	-	-	-	-
Derivatives	**-**	**1.43**	**1.43**	**-**	**2.85**	**2.85**	**-**	**(1.43)**	**(1.43)**	**-**	**(2.87)**	**(2.87)**

Cash flows slotted into time buckets according to their maturity or repricing date as of 31.12.2017

(in million of euros)

		Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
Total		**416**	**522**	**(100)**	**(64)**	**35**	**5**	**18**
Asset		**2.491**	**1.938**	**88**	**132**	**208**	**75**	**50**
Sight Loans		293	293	-	-	-	-	-
Securities	FX	234	108	5	43	78	-	-
	FL	72	71	1	-	-	-	-
Loans	FX	574	224	62	68	108	66	46
	FL	1.318	1.242	20	21	22	9	4
Other Financial Assets	FX	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-
Liabilities		**(2.055)**	**(1.711)**	**(175)**	**(138)**	**(31)**	**-**	**-**
Sight Deposits		(1.581)	(1.257)	(160)	(134)	(30)	-	-
Securities Issued	FX	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-
Debts	FX	(392)	(372)	(15)	(4)	(1)	-	-
	FL	(83)	(82)	-	-	-	-	-
Other Financial Liabilities	FX	-	-	-	-	-	-	-
	FL	-	-	-	-	-	-	-
Derivatives		**(20)**	**295**	**(13)**	**(58)**	**(142)**	**(70)**	**(32)**

Due to lasting negative levels of interest rates, the Bank follows specific rules that allow adequate cash flow representation based on actual contractual interest rates and relevant yield curve shifts. The Bank is applying 0% floors on contractual interest rates for customer's sight deposits when according to shift scenario the rates drop below zero, in order to replicate actual circumstances on the market. In addition for representation of sight deposits a model, which estimates the partial and delayed changes in customer rates compared to changes in market interest rates is used. In order to control quantitatively the Bank's interest margin risk, a limit of EUR -7.5 mln has been set up for a +/- 50bp interest rates change. The impact on Bank's interest margin due to an increase of market interest rates for 50 bp according to data as of end 2018 would be positive, in the amount EUR 5.2 mln, while in case of an instantaneous 50 bp drop in interest rates, the impact would be negative EUR 4.8 mln. The largest part of the margin sensitivity arises from the floating rate loans to customer exposure class.

The impact of 100 bps interest rate parallel shift on net present value of the Bank' interest-bearing assets and liabilities, as at 31 December 2018

(in million of euros)

Currency	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**3.81**	(2.43)	2.07	4.38	1.36	1.02	(2.59)
USD	**(0.03)**	(0.03)	-	-	-	-	-
CHF	**(0.02)**	(0.02)	-	-	-	-	-
Other	**-**	-	-	-	-	-	-
Total Shift	**3.76**	**(2.48)**	**2.07**	**4.38**	**1.36**	**1.02**	**(2.59)**
Limit	**9.0**						
Utilization %	**41.76%**						

In the table is presented the interest rate risk exposure of the Bank in terms of shift sensitivity (EVE- economic value of equity), which measures the change of net present value of future cash-flows, as a result of parallel shift of market yield curve by 100 b.p. Each time-bucket shows the impact of interest rate change on net present value of cash-flows, distributed by time tenors according to residual time to the next repricing. The most significant exposure is in EUR currency, while the risk for other currencies is less material. The total exposure limit for +100 bps shift sensitivity amounts to 9.0 million EUR, while the actual exposure at reference date is 3.8 million EUR. For the EVE measure a floor assumption on market rates for negative shocks is in place. In 2018 EBA, through its Guidelines (EBA/GL/2018/02) introduced a non-constant floor that starts from a value of -100 b.p. and increases by 5 basis points per year, until eventually reaching 0% for maturities of 20 years and more. The main generators of interest rate risk are medium – long term assets with fixed interest rates (eg. housing loans, debt financial instruments), which are hedged by interest rate swaps. On liabilities side, the highest portion of shift sensitivity derives from the sight deposits, where sight deposits are slotted to time buckets up to 10 years according to the sight deposit model.

In addition to the total exposure limit, limits for specific time buckets for a +100bp change in interest rates are set:

(in million of euros)

Time bucket	Limit	Exposure
0–18 months	+/- 8.0	(2.48)
from 19 months–5 years	+/- 8.0	6.45
>5 years	+/- 8.0	(0.21)

The impact of 100 bps interest parallel rate shift on net present value of the Bank's interest-bearing assets and liabilities, as at 31 December 2017

(in million of euros)

Currency (mln EUR)	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**5.42**	(1.90)	2.93	4.01	0.63	1.21	(1.46)
USD	**(0.03)**	(0.03)	-	-	-	-	-
CHF	**(0.02)**	0.01	-	(0.02)	-	-	-
Other	**-**	-	-	-	-	-	-
Total Shift	**5.37**	**(1.92)**	**2.93**	**3.99**	**0.63**	**1.21**	**(1.46)**
Limit	**9.0**						
Utilization %	**59.67%**						

The impact of +200 bps interest parallel rate shift on net present value of the Bank's interest-bearing assets and liabilities, as at 31 December 2018

(in million of euros)

Currency (mln EUR)	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**7.66**	(4.79)	4.06	8.54	2.60	1.92	(4.68)
USD	**(0.05)**	(0.05)	-	-	-	-	-
CHF	**(0.05)**	(0.03)	-	-	(0.01)	-	-
Other	**-**	-	-	-	-	-	-
Total Shift	**7.56**	**(4.87)**	**4.06**	**8.54**	**2.59**	**1.92**	**(4.68)**
Reg,Capital (Dec. 18)	**266.8**						
15% of Reg, Capital	**2.83%**						

The impact of +200 bps interest parallel rate shift on net present value of the Bank's interest-bearing assets and liabilities, as at 31 December 2017

(in million of euros)

Currency (mln EUR)	Total	0-18m	18m-3Y	3Y-5Y	5Y-10Y	10Y-15Y	>15Y
EUR	**11.15**	(3.56)	6.10	7.79	1.19	2.24	(2.61)
USD	**(0.07)**	(0.06)	-	(0.01)	-	-	-
CHF	**(0.04)**	(0.01)	-	(0.02)	(0.01)	-	-
Other	**-**	-	-	-	-	-	-
Total Shift	**11.04**	**(3.63)**	**6.10**	**7.76**	**1.18**	**2.24**	**(2.61)**
Reg,Capital (Sept 17)	**257.1**						
15% of Reg, Capital	**4.29%**						

The 200 bp shift is a standard measure defined by Banking supervisor that treats an impact thereof on Economic value that exceeds 20% Tier I capital as outlying excessive risk exposure. As of 31.12.2018 the sensitivity reached 2.83% of Tier I capital. EBA in its Guidelines defines another threshold, the sensitivity of the Bank`s economic value to the 6 pre-defined regulatory scenarios, shall not be higher than 15% of their Tier 1 capital.

The table below summarises the effective annual interest rate for monetary financial instruments not carried at fair value through profit or loss by major currency:

The effective annual interest rate of individual financial instruments

	2018			2017		
	EUR	USD	Other	EUR	USD	Other
Assets						
Cash and balances at central banks and other demand deposits at banks	-	1.75	0.27	-	1.24	0.03
Loans and advances to banks	0.04	3.33	(0.13)	(0.02)	5.79	1.10
Loans and advances to non-bank customers	2.17	6.22	0.99	2.19	4.29	1.02
Available for sale financial assets	-	-	-	1.45	4.28	-
Financial assets at fair value through other comprehensive income	1.25	4.36	-	-	-	-
Non-trading financial assets mandatorily at fair value through profit or loss	2.98	-	-	-	-	-
Liabilities						
Deposits from banks and central banks	0.06	-	0.60	-	-	0.60
Deposits from non-bank customers	0.05	0.07	0.01	0.07	0.09	0.01
Other borrowed funds	0.39	4.30	-	1.57	3.17	-

Breakdown of financial assets and liabilities subject to trading and non-trading book

(in thousands of euros)

As at 31 December 2018	Carrying amount	Market risk measure: Trading portfolios	Market risk measure: Non-trading portfolios
Assets subject to market risk			
Cash, cash balances at central banks and other demand deposits at banks	390,660	-	390,660
Financial assets held for trading	29	29	-
Non-trading financial assets mandatorily at fair value through profit or loss	3,019	-	3,019
Financial assets at fair value through other comprehensive income	314,631		314,631
Derivatives - hedge accounting	1,023	-	1,023
Financial assets at amortized cost:	1,830,704		1,830,704
- debt securities	1,266	-	1,266
- loans to banks	53,623	-	53,623
- loans to non-bank customers	1,757,088	-	1,757,088
- advances	18,727	-	18,727
Liabilities subject to market risk			
Derivatives - hedge accounting	4,055	-	4,055
Financial liabilities measured at amortized cost:	2,289,275	-	2,289,275
- deposits from banks and central banks	15,517	-	15,517
- deposits from non-bank customers	2,207,670	-	2,207,670
- loans from banks and central banks	37,484	-	37,484
- loans from non-bank customers	32	-	32
- debt securities issued	28,572	-	28,572
Fair value changes of the hedged items in portfolio hedge of interest rate risk	626	-	626

Breakdown of financial assets and liabilities subject to trading and non-trading book

(in thousands of euros)

As at 31 December 2017	Carrying amount	Market risk measure	
		Trading portfolios	Non-trading portfolios
Assets subject to market risk			
Cash, cash balances at central banks and other demand deposits at banks	287,084	-	287,084
Financial assets held for trading	60	60	-
Financial assets designated at fair value through profit or loss	59	-	59
Available-for-sale financial assets	318,702	-	318,702
Derivatives - hedge accounting	2,471	-	2,471
Loans and receivables:	1,729,900	-	1,729,900
- loans to banks	41,142	-	41,142
- loans to non-bank customers	1,675,027	-	1,675,027
- advances	13,731	-	13,731
Liabilities subject to market risk			
Financial liabilities held for trading	8	8	-
Derivatives - hedge accounting	660	-	660
Financial liabilities measured at amortized cost:	2,091,860	-	2,091,860
- deposits from banks and central banks	10,750	-	10,750
- deposits from non-bank customers	1,971,496	-	1,971,496
- loans from banks and central banks	71,477	-	71,477
- loans from non-bank customers	-	-	-
- debt securities issued	38,137	-	38,137
Fair value changes of the hedged items in portfolio hedge of interest rate risk	1,131	-	1,131

3.8 OPERATIONAL RISK

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, systems, human behaviour or mistakes or from external events. The definition also includes legal risk, representing the risk of ineffective legal execution or defective legal documentation, as well as compliance risk, which is the risk of failure to comply with laws, rules, regulations, agreements and practices. However, the definition excludes strategic and reputational risk.

The objectives of operational risk management are to:
- Protect assets, preserve and safeguard material and intellectual Bank's assets.
- Control and proactively monitor processes to ensure that significant risks are swiftly identified.
- Comply with requirements and processes established with internal rules and external regulations.

The process of operational risk management comprises the identification, measurement or evaluation, control and monitoring of operational risk. The process of operational risk measurement and management is assisted by the risk mitigation tool developed by the parent company designed to support the carrying out of the following activities:

- Loss data collection,
- Business environment evaluation,
- Scenario analysis,
- Mitigation actions management, and
- Monitoring and reporting.

The systematic loss data collection makes it possible to perform immediate analysis of loss event causes and to adopt corrective actions. This procedure supports the compliance with general operational risk management standards.

First level operational risk management is carried out by the person directly responsible for operations in each organisational unit. The Risk Management Department, which is responsible for the operational loss data collection and the self-assessments activity with the involvement of the Level 1 organisational units, is in charge of second level operational risk management processes. The self-assessment activity is necessary to explore the level of the

Bank's exposure to operational risk and to evaluate the risk appetite measure.
The Risk Management Department assisted by the Operational Risk Group (composed of the persons responsible from the most important first-level organisational units), reports on a quarterly basis to the Management Board and proposes remedial actions.

3.9 FAIR VALUE OF ASSETS AND LIABILITIES THAT ARE NOT MEASURED AT FAIR VALUE

(in thousands of euros)

	2018					2017	
	Level 1	Level 2	Level 3	Total fair values	Total carry-ing amount	Total fair values	Total carrying amount
Financial assets							
Cash and current accounts with banks		390,660	-	**390,660**	**390,660**	**287,084**	**287,084-**
Loans to banks	-	53,330	293	**53,623**	**53,623**	**41,142**	**41,142**
Loans to non-bank customers	-	72,491	1,686,380	**1,758,871**	**1,757,088**	**1,675,921**	**1,675,027**
Financial liabilities	-						
Deposits from banks and central bank	-	8,517	7,058	**15,575**	**15,517**	**10,799**	**10,750**
Deposits from non-bank customers	-	1,951,415	256,239	**2,207,654**	**2,207,670**	**1,971,488**	**1,971,496**
Loans from banks and central banks	-	-	37,540	**37,540**	**37,484**	**70,878**	**71,477**
Loans from non-bank customers	-	-	32	**32**	**32**	**-**	**-**

Fair value of financial instruments not measured at fair value

The following methods and assumptions have been made in estimating the fair value of financial instruments:

- There are no significant differences between carrying value and fair value of cash, cash balances at central banks and other demand deposits at banks given the short maturity of such assets.
- Loans to non-bank customers are presented net of impairment allowance. The estimated fair value of these loans represents the discounted amount of the estimated future cash flows expected to be received. Expected future cash flows are discounted at current market rates. Valuation of non-performing loans includes estimation of loan receivable and collateral cash-flows. Loans to non-bank customers classified as Level 2 include short term performing loans with original maturity less than 1 year, excluding credit card receivables and overdraft loans.
- The estimated fair value of fixed-interest term deposits is based on the expected cash flows discounted using current market rates. For demand deposits and deposits with no defined maturity, the fair value is determined to be the amount payable on demand. The value of customer relationships has not been taken into account. Deposits and loans received are mainly classified as Level 2 in the fair value hierarchy, since the parameters used in valuation are market observable. Majority of loans and deposits from banks carry floating interest rates, which are linked to market and repriced regularly. As such, the management believes that their carrying values approximate their fair values.

Fair value of financial instruments

Derivatives

Accounting for derivatives at fair value is performed on the basis of observable market inputs. Derivative financial instruments subject to valuation are: interest rate swaps, interest rate caps, foreign exchange swaps, forward foreign exchange contracts. The fair value of derivatives is determined with the support of Murex, a system developed by the parent company. The system takes input data from the money market official quotations and from Reuters system. The fair value of interest rate swaps is the net present value of future cash flows, based upon spot and forward money market interest rates. The fair value of more complex derivatives such as caps is calculated by using the Black's Model with SABR volatility.

Hedge accounting

The Bank's interest rate policy course is to hedge in accordance with hedge accounting rules the interest rate risk assumed on each single large financial investments and loan clusters with similar characteristics and fixed rate remuneration (housing loans). For single large financial investments a micro fair value hedge is applied, while for housing loans the Bank engage in a macro fair value hedge. The loans eligible for hedging are chosen at the time of disbursement as having medium/long term contractual maturity and fixed rate remuneration. The identified loans are hedged with interest rate swap derivative contracts, conceding the transformation of fixed contractual rate to floating rate according to market benchmark, i.e. Euribor. The interest rate risk is hedged using the fair value method and the effectiveness of the hedging relationship is regularly measured by calculating the prospective and retrospective effectiveness tests. For the prospective test the Bank measures the relation between interest rate sensitivity of the derivative instrument and sensitivity of the hedged item. In the retrospective test the "Dollar offset method"is used, where the fair value changes of derivative instrument is compared to the fair value change of the hedged item. The ratio between the changes of value for two items has to be within 80% and 125% range.

For the macro fair value hedges two effectiveness tests are additionally carried out. The sensitivity test (first level test) is aimed at the verification that the sensitivity of the portfolio, subject to hedging and distributed by time buckets, is greater (in absolute terms) than the sensitivity of the hedging derivative instrument. The fair value capacity test (second level) is on the other hand necessary to assess the hedge effectiveness from a view of a dynamic management of the portfolio. The test verifies that the portfolio subject to hedging contains assets with sensitivity profile and expected fair value variations on hedged risk that is matching the hedging derivative.
According to the efficiency tests, as of 31 December 2018, all interest rate hedges were effective.
As of 31 December 2018 the Bank had 45 interest rate swap (IRS) contracts, 15 of which underwritten in 2018. 12 IRS contract are designated to hedge interest rates arising from fixed rate debt financial instruments, 18 for fixed rate housing loans and 15 for large individual loans.

Hedged item	Nominal amount (in mln EUR)		Number of IRS contracts	
	2018	2017	2018	2017
Fixed income bond-micro hedge	104.8	132.2	12	15
Housing loans packages-macro hedge	141.9	97.8	18	11
Individual loans-micro hedge	184.0	104.4	15	7
Total	**430.7**	**334.4**	**45**	**33**

The cumulative fair value of all Bank`s IRS contracts` as of 31 December 2018 amounted to -3.0 mln EUR.

The amounts relating to items designated as hedging instruments:

(in thousands of euros)

Interest rate risk	Nominal amount	Carrying amount	
		Assets	Liabilities
Interest rate swaps - hedge of bonds	104,826	355	959
Interest rate swaps - hedge of loans - MICRO HEDGE	184,000	40	1,900
Interest rate swaps - hedge of loans - MACRO HEDGE	141,853	628	1,196

The amount relating to items designated as hedged item:

(in thousands of euros)

Interest rate risk	Carrying amount		Accumulated amount of fair value hedge adjustments on the hedged item included in the carrying amount of the hedged item	
	Assets	Liabilities	Assets	Liabilities
Bonds	143,197	-	20	-
Loans - micro hedge	185,754	-	1,351	-
Loans - macro hedge	153,469	-	577	-

Financial instruments held at fair value through other comprehensive income

Currently, the Bank's portfolio containing fair value through other comprehensive income financial assets (FVOCI) is composed of bonds and shares. Both instruments are measured at fair value.

The fair value of level 1 bonds is derived from their quoted market prices. In case the bonds are not liquid, the fair value is determined by discounting future cash flows. The discounting rate is the yield to maturity of a liquid comparable bond. Such bonds are marked as fair value level 2.

The fair value of shares listed on the active stock market is their market value, whereas for the non-listed shares or illiquid shares, the fair value is determined using the internal valuation model. The internal valuation is carried out by applying the price multiples method. The difference between the model and market valuation when shares are quoted on illiquid market (currently only 1 such position), as at 31 December 2018 amounted to 1.2 million euros.

The basis for the calculation under the above method are the available market valuations of comparable enterprises, in connection with financial ratios and multiples of their traded shares in the valuation of non-traded or illiquid shares. A condition for the application of the method is the availability of at least two comparable enterprises with listed shares. The latter shall be comparable by industry, market capitalisation, size and geographical location.

Information on financial ratios (price multiples) for comparable enterprises shall be obtained from independent sources, such as the Ljubljana Stock Exchange, Reuters, etc.

The share value is based on the following price multiples of comparable enterprises:
- EV/S (enterprise value / sales);
- EV/EBITDA (enterprise value / EBIT + depreciation);
- P/E (price-to-earnings);
- P/BV (price / book value);

The basis for the estimation are the financial statements of the comparable enterprises:
- balance sheet (for the preceding 3 financial years);
- income statement (for the preceding 3 financial years).

The final value is computed as the average of the multiples, whereby multiples considered as inadequate, are omitted.

Breakdown of financial instruments measured at fair value by fair value hierarchy levels

(in thousands of euros)

	2018			
	Level 1	**Level 2**	**Level 3**	**Total**
Asset				
Derivatives	-	29	-	**29**
Financial assets at FVOCI:	256,092	43,386	15,153	**314,631**
- debt	245,397	40,138	14,959	**300,494**
- equities	10,695	3248	194	**14,137**
FVTPL mandatorily:	-	690	2,329	**3,019**
- equities	-	690	1,447	**2,137**
- loans and advances	-	-	882	**882**
Liabilities				
Derivatives	-	-	-	-

Breakdown of financial instruments measured at fair value by fair value hierarchy levels

(in thousands of euros)

	2017			
	Level 1	Level 2	Level 3	Total
Asset				
Derivatives	-	60	-	**60**
Available-for-sale financial assets	294,477	22,584	1,641	**318,702**
- debt	283,670	19,221	-	**302,891**
- equities*	10,807	3,363	1,641	**15,811**
FVTPL – equities	59	-	-	**59**
Liabilities				
Derivatives	-	8	-	**8**

**Fair value of investments in National Bank Resolution Fund included within Level 1 is determined by Bank of Slovenia regarding volume of assets of each bank. These investments are not quoted.*

Movement of financial instrument included in level 3

(in thousands of euros)

Financial assets	AFS Equities
As at 31 December 2016	**1,927**
Purchase/Sale	(42)
Unrealized gains/losses recorded in revaluation reserve	426
Realized gains/losses recorded in P&L	20
Transfers out of level 3	(690)
As at 31 December 2017	**1,641**

(in thousands of euros)

	Mandatorily FVTPL		FVOCI	
Financial assets	*Equities*	*Loans*	*Equities*	*Loans*
As at 31 December 2017	**-**	**-**	**-**	
Transfer from AFS	1,447	-	194	-
Transfer from loans at amortised cost	-	18,878	-	-
Impact of adopting IFRS 9	-	(894)	-	-
As at 1 January 2018	**1,447**	**17,984**	**194**	
Sale/Disposals	**-**	(19,410)	-	15,053
Unrealized gains/losses recorded in P&L	**-**	75	-	-
Unrealized gains/losses recorded in revaluation reserve	-	-	-	(47)
Realized gains/losses recorded in P&L	-	2,223	-	(47)
As at 31 December 2018	**1,447**	**882**	**194**	**14,959**

As of 31 December 2018, the Bank held in the investment portfolio 21 bonds measured at fair value (FVOCI), out of which 3 are measured with marked to model approach, due to illiquidity, while 18 were measured on market prices (level 1). As for equity portfolio all positions were valued with a marked to model approach, due to illiquidity issue or because the investments are not quoted on the stock exchange.

4. NET INTEREST INCOME

(in thousands of euros)

	2018	2017
Interest income calculated using the effective interest rate		
Investment securities (AFS)	-	3,574
Derivatives – hedge accounting	1,553	1,650
Financial assets at fair value through other comprehensive income	2,457	-
Loans and advances:	41,594	43,322
- debt securities	47	-
- to banks	303	227
- to other customers	41,242	43,085
- advances	2	10
Sight deposits within banks	76	52
Financial liabilities (negative interest rate)	3	36
Total	**45,683**	**48,634**
Other interest income	**1,139**	**-**
Interest expense		
Derivatives - hedge accounting	4,615	3,773
Financial liabilities measured at amortised cost:	2,342	3,270
- Bank deposits and borrowings	50	30
- Other customers	1,192	1,833
- Other borrowed funds	1,100	1,407
Other	1	-
Financial assets (negative interest rate)	1,276	968
- Loans to banks	1,092	954
- FVOCI securities	184	14
Total	**8,234**	**8,011**
Total	**38,588**	**40,623**

Interest income includes EUR 4,001 thousand (2017: EUR 7,267 thousand) of interest income on impaired loans.

5. DIVIDEND INCOME

(in thousands of euros)

	2018	2017
Investment securities	-	489
FVPL shares	-	17
Non-trading financial assets mandatorily FVTPL	5	-
Financial assets FVOCI	161	-
Total	**166**	**506**

6. NET FEE AND COMMISSION INCOME

(in thousands of euros)

	2018	2017
Fee and commission income		
From current bank account management	3,970	4,002
From payment services	10,688	10,432
From credit card business	8,584	8,564
From interbanking operations	4,845	4,512
From loans granted	4,627	4,537
From safe renting	123	92
From pension fund management	507	503
Depositary services	694	530
From payment systems management	1,640	1,553
From brokering of loans and insurance contract on behalf of others	300	321
Total fee and commission income from contracts with customers	**35,978**	**35,046**
From guarantees given	**1,220**	**1,255**
Total	**37,198**	**36,301**
Fee and commission expense		
For security trading	86	74
For loan brokerage on behalf of others	60	79
For custody services	242	206
For credit card processing	8,063	7,453
For payment transactions	3,345	3,013
Commitment fee for unused credit lines	261	429
Total fee and commission expense	**12,057**	**11,254**
Total	**25,141**	**25,047**

7. NET GAINS OR LOSSES ON DERECOGNITION OF FINANCIAL ASSETS AND LIABILITIES NOT MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS

(in thousands of euros)

	2018	2017
Loss/income due to sale of investment securities*	-	4,988
Net gains or losses of financial assets measured at fair value through other comprehensive income	114	-
• Gains	987	-
• Losses	(873)	-
Net gains or losses of financial assets measured at amortised cost	2,647	(2,346)
• Gains	3,159	871
- Sale	1,353	-
- Write-off in previous years	1,769	822
- Other	37	49
• Losses	(512)	(3,217)
- Sale	(32)	-
- Write-off	(480)	(2,825)
- Other	-	(392)
Total	**2,761**	**2,642**

**From released revaluation reserve due to sale of shares and maturity of bonds EUR 3,587 thousand.*

8. NET GAINS OR LOSSES ON FINANCIAL ASSETS AND LIABILITIES HELD FOR TRADING

(in thousands of euros)

	2018	2017
Trading of derivatives	(17)	(8)
- Realized	(1)	4
- Unrealized	(16)	(12)
Currency trading	893	882
Total	**876**	**874**

9. NET GAINS OR LOSSES ON NON-TRADING FINANCIAL ASSETS MANDATORILY AT FAIR VALUE THROUGH PROFIT OR LOSS

(in thousands of euros)

	2018	2017
Gains	8,471	-
- Realized	8,387	-
- Unrealized	84	-
Losses	(2)	-
- Realized	(1)	-
- Unrealized	(1)	-
Total	**8,469**	**-**

In 2018, the Bank sold the shares obtained as collateral from repossession of loans, which due to legal obstacles it was never recognized in balance sheet. The gain from this transaction amounted to EUR 6,154 thousand. The remaining amount of gain relates to sell of loans mandatorily at fair value through profit or loss.

10. NET GAINS OR LOSSES FROM HEDGE ACCOUNTING

(in thousands of euros)

	2018	2017
Net effect on derivatives used as hedging instruments	(4,777)	2,824
Net effect on hedged items*	4,830	(2,981)
Total	**53**	**(157)**

**Within correction of revaluation reserve for the hedged fair value amount of bonds for EUR 1,200 thousand (2017: EUR 606 thousand).*

Derivatives used as hedge instruments and the nature of hedged items are additionally explained in note 21 and in note 3.9. Fair value of assets and liabilities that are not measured at fair value (in paragraph hedge accounting).

11. NET GAINS AND LOSSES ON DERECOGNITION OF NON-FINANCIAL ASSETS

(in thousands of euros)

	2018	2017
Profit on sale of property and equipment	380	39
Net income realised from sale of investment property	-	9
Total	**380**	**48**

12. OTHER OPERATING INCOME/EXPENSES

12a Other operating income

(in thousands of euros)

	2018	2017
Rents	1,312	3,275
Proceeds from the sale of repossessed leased assets	139	428
Other	-	5
Total	**1,451**	**3,708**

12b Other operating expenses

(in thousands of euros)

	2018	2017
Taxes	(178)	(371)
Membership fees	(86)	(86)
Contribution to European Banking Resolution Fund	(149)	(266)
Contribution to European Deposit Guarantee Scheme	(1,978)	(1,696)
Maintenance expenses arising from leased assets	(106)	(160)
Expenses from investment property under the operating lease	-	(388)
Expenses related to services from credit card business	(193)	-
Fraud from credit card business	(131)	-
Licences	(121)	-
Other	(425)	-
Total	**(3,367)**	**(2,967)**

From rent contracts arises that the future rent revenues will amount to EUR 7,903 thousand (2017: EUR 22,580 thousand), as follows:

(in thousands of euros)

2018			2017		
Up to 1 year	**1 to 5 years**	**Over 5 years**	**Up to 1 year**	**1 to 5 years**	**Over 5 years**
2,116	3,492	2,295	2,258	9,032	11,290

13. ADMINISTRATIVE EXPENSES

(in thousands of euros)

	2018	2017
Staff cost	**29,694**	**28,494**
Salaries	20,119	19,217
Social security	3,027	3,003
Contributions to the pension scheme	1,807	1,724
Other*	4,741	4,550
Other administrative expenses	**11,833**	**12,732**
Material costs	1,717	1,895
IT costs	3,460	3,101
Rents	1,486	1,581
Professional services	1,189	1,911
Advertising and marketing	466	518
Consulting, auditing, legal and notarial fees**	287	221
Maintenance, governance and security of tangible fixed assets	994	1,079
Postal services and rent of communication lines	1,384	1,471
Insurance	322	369
Travel costs	67	55
Education, scholarships and tuition fees	183	141
Bank's supervision	278	390
Total	**41,527**	**41,226**

**Other staff costs relates to holiday incentives and accruals for bonuses.*
***Of which audit of the Bank's financial statements EUR 68 thousand (2017: EUR 67 thousand) and EUR 44 thousand (2017: EUR 45 thousand) for other audit services.*

14. DEPRECIATION AND AMORTISATION

(in thousands of euros)

	2018	2017
Amortisation	1,242	1,293
Depreciation	1,712	3,040
Total	**2,954**	**4,333**

15. PROVISIONS

(in thousands of euros)

	2018	2017
Provisions for off-balance sheet exposures	(658)	997
Provisions for legal proceedings and future contract obligations	40	(1,239)
Retirement and long service bonuses	(228)	(230)
Provisions for reorganization	(1,833)	-
Provisions for termination of employment for business reasons	(709)	(140)
Provisions for cash returns from discontinued products	(350)	-
Total	**(3,738)**	**(612)**

The movement of provisions and post-employment benefit obligations is shown in note 39 and 40.

16. IMPAIRMENTS

(in thousands of euros)

	2018	2017
Impairments of financial assets, not measured at fair value through profit and loss		
Impairments of financial assets at fair value through other comprehensive income	(71)	-
Impairments on assets measurement at amortised cost:		
- debt securities	-	-
- banks	1	17
- loans to other customers	12,031	18,295
- impairments of other assets	252	20
Impairment of non-financial assets		
Impairment on fixed assets (property)	-	974
Impairment on inventories (repossessed assets)	1,329	-
Total	**13,542**	**19,306**

17. PROFIT OR LOSS FROM NON-CURRENT ASSETS AND DISPOSAL GROUPS CLASSIFIED AS HELD FOR SALE, NOT QUALIFYING AS DISCONTINUED OPERATIONS

(in thousands of euros)

	2018	2017
Rents	1,656	-
Maintenance expenses	(431)	-
Impairment	(671)	-
Gains from sale	60	-
Total	**614**	**-**

18. TAX EXPENSE

(in thousands of euros)

	2018	2017
Current tax expense	2,537	715
Deferred tax (note 41)	(108)	31
Total	**2,429**	**746**
Profit before tax	**13,143**	**4,957**

Further information about deferred income tax is presented in note 41.
The tax on the Bank's profit before tax differs from the theoretical amount that would arise using the basic tax rate as follows:

(in thousands of euros)

	2018	2017
Prima facie tax calculated at a tax rate of 19%	2,497	942
Income form already taxed dividends	(31)	(99)
Expenses not deductible for tax purposes:		
- staff costs not assessable for tax	168	169
- impairment of financial assets measured at FVOCI	134	-
- other non-tax deductible expenses	38	41
Tax reliefs	(377)	(307)
Total income tax	**2,429**	**746**
Effective tax rate	*18,5%*	*15,0%*

For 2018 the income tax rate was 19% (2017: 19%) as prescribed by law.

In accordance with local regulations, the Financial Administration may at any time inspect the Bank's books and records within the 5 years subsequent to the reported tax year and may impose additional tax assessments and penalties. The Bank's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

Changes in income tax from items that are recognized in FVOCI

(in thousands of euros)

	31.12.2018		
	Before tax	Tax (expense) benefit	After tax
ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS	**1,956**	**(237)**	**(1,719)**
Fair value changes of equity instruments measured at fair value through other comprehensive income	539	(102)	437
Actuarial gains or losses on defined benefit pensions plans	1,417	(135)	1,282
ITEMS THAT MAY BE RECLASSIFIED TO PROFIT OR LOSS	**(6,010)**	**(1,142)**	**(4,868)**
Debt instruments at fair value through other comprehensive income:			
Valuation gains or losses taken to equity	(4,830)	918	(3,912)
Transferred to profit or loss	(1,170)	222	(948)
Non-current assets held for sale:			
Transferred to profit or loss	(10)	2	(8)
TOTAL	**(4,054)**	**905**	**(3,149)**

Changes in income tax from items that are recognized in FVOCI

(in thousands of euros)

	31.12.2017		
	Before tax	Tax (expense) benefit	After tax
ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS	**13,797**	**(2,620)**	**11,177**
Tangible assets	13,792	(2,620)	11,172
Actuarial gains (losses) on defined benefit pensions plans	5	-	5
ITEMS THAT MAY BE RECLASSIFIED TO PROFIT OR LOSS	**(1,249)**	**237**	**(1,012)**
Available-for-sale financial assets:			
Valuation gains (losses) taken to equity	1,732	(329)	1,403
Transferred to profit or loss	(2,981)	566	(2,415)
TOTAL	**12,548**	**(2,384)**	**10,164**

19. EARNINGS PER SHARE

(in thousands of euros)

	2018	2017
Net profit for the year	10,714	4,211
Weighted average number of ordinary shares in issue	530,398	530,398
Basic and diluted profit per share (in EUR per share)	**20.20**	**7.94**

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year, excluding the average number of ordinary shares purchased by the Bank and held as treasury shares (961 lots). There are no dilutive potential ordinary shares, there are no share options schemes.

20. CASH, CASH BALANCES AT CENTRAL BANKS AND OTHER DEMAND DEPOSITS AT BANKS

(in thousands of euros)

	2018	2017
Cash in hand	19,083	16,803
Balances with central banks	348,419	233,871
Other sight deposits	23,175	36,419
Gross cash, cash balances at central banks and other demand deposits at banks	**390,677**	**287,093**
Impairment	(17)	(9)
Net cash, cash balances at central banks and other demand deposits at banks	**390,660**	**287,084**
From this: mandatory reserve liability to central banks	23,777	19,055

The Bank is required to maintain a mandatory reserve with the central bank (Bank of Slovenia), relative to the volume and structure of its customer deposits. The current requirement of the Bank of Slovenia regarding the calculation of the amount to be held as mandatory reserve is 1% of time deposits and issued debt securities with maturities up to two years.

The Bank maintains sufficient liquid assets to fully comply with the central bank requirements.

21. DERIVATIVE FINANCIAL INSTRUMENTS

The majority of derivative contracts is entered into for the purpose of interest-rate risk management. A derivative instrument is entered into as an economic hedge where its terms and conditions are a mirror image of the terms and conditions of the hedged financial instruments. In addition, the Bank also uses fair value hedge accounting techniques, where interest rate swaps hedges long-term financial assets (bonds and loans) with fixed interest rate.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of these instruments and, therefore, do not indicate the Bank's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in the reference rate or index relative to their terms. The aggregate contractual or notional amount of derivative financial instruments, the extent to which instruments are favourable or unfavourable and, thus the aggregate fair values of derivative financial assets and liabilities can fluctuate significantly from time to time. The notional amount and fair values of derivative instruments held for trading and designated as hedges are set out in the following tables:

Derivative financial instruments

(in thousands of euros)

As at 31 December 2018	Notional amount	Fair value	
		Assets	Liabilities
HFT derivatives			
Foreign exchange rate			
Forwards-sale	60	-	-
Forwards-purchase	60	-	-
Interest rate			
Interest rate cap (CALL)	3	-	-
Interest rate cap (PUT)	3,960	29	-
Total held for trading derivatives		**29**	**-**
Hedging derivatives			
Interest rate swaps (IRS) – micro hedge	288,827	395	2,859
Interest rate swaps (IRS) – macro hedge	141,853	628	1,196
Total derivative for hedge accounting		**1,023**	**4,055**

(in thousands of euros)

As at 31 December 2017	Notional amount	Fair value	
		Assets	Liabilities
HFT derivatives			
Foreign exchange rate			
Forwards-sale	595	10	-
Forwards-purchase	596	-	8
Interest rate			
Interest rate cap (CALL)	4,970	50	-
Interest rate cap (PUT)	-	-	-
Total held for trading derivatives		**60**	**8**
Hedging derivatives			
Interest rate swaps (IRS) – micro hedge	236,617	1,375	516
Interest rate swaps (IRS) – macro hedge	97,796	1,096	144
Total derivative for hedge accounting		**2,471**	**660**

In financial environment of low interest rates the Bank promoted its commercial activities by lunching long term loans fix interest rates. To overcome the interest rate risk interest rate swaps were made.

22. AVAILABLE-FOR-SALE FINANCIAL ASSETS

(in thousands of euros)

	2018	2017
Government securities:		
- listed	-	298,671
Other debt securities:		
- listed	-	4,220
Equity securities:		
- listed	-	948
- unlisted	-	4,250
Investment in National Bank Resolution Fund	-	10,613
Total securities available-for-sale	**-**	**318,702**

Movement

(in thousands of euros)

	2018	2017
At beginning of the year	**318,702**	**354,615**
Additions	-	76,082
Impairment	-	-
Interest accrual	-	3,682
Expired coupons	-	(8,258)
Disposals (sale and redemption)	-	(103,740)
Gains/losses from changes in fair value	-	1,731
Exchange differences	-	(5,410)
Reclassification to FVOCI (Impact of adopting IFRS 9)	(315,152)	-
Reclassification to mandt. FVTPL (Impact of adopting IFRS 9)	(2,137)	-
Reclassification to financial assets at amortised cost (Impact of adopting IFRS 9)	(1,413)	-
At end of year	**-**	**318,702**

23. NON-TRADING FINANCIAL ASSETS MANDATORILY AT FAIR VALUE THROUGH PROFIT OR LOSS

(in thousands of euros)

	2018	2017
Equities:		
- listed	754	-
- unlisted	1,383	-
Loans and advances	882	-
Total financial assets mandatorily at fair value through profit or loss	**3,019**	**-**

Movement

(in thousands of euros)

	2018
At beginning of the year (31 December 2017)	**-**
Reclassification to mandt. FVTPL assets (Impact of adopting IFRS 9) from AFS	2,137
Reclassification to mandt. FVTPL assets (Impact of adopting IFRS 9) from FVTPL designated	59
Reclassification to mandt. FVTPL assets (Impact of adopting IFRS 9) from loans and advances	18,878
Impact of adopting IFRS 9 (loans from amortized cost to fair value)	(894)
At beginning of the year (1 January 2018)	**20,180**
Sale/ Disposals of loans	(17,177)
Valuation	75
Sale of shares	(59)
At end of year (31 December 2018)	**3,019**

24. FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

(in thousands of euros)

	2018	2017
Equities:		
- listed	89	-
- unlisted	14,048	-
Debt securities:		
Government securities:		
- listed	268,705	-
Other debt securities:		
- listed	31,863	-
Total financial assets FVOCI (Gross)	**314,705**	**-**
Impairment	(74)	-
Total financial assets FVOCI	**314,631**	**-**

The Bank adopted its own valuation model in cases where investments are not listed or measures such investments at cost less impairments.

In order to comply with the requirements of the National Bank Resolution Fund, Slovenian government bonds in the amount of EUR 11.2 million are encumbered.

Movement

(in thousands of euros)

	2018
At beginning of the year (31 December 2017)	**-**
Reclassification to FVOCI assets (Impact of adopting IFRS 9) from AFS	315,152
At beginning of the year (1 January 2018)	**315,152**
Acquisitions	130,822
Interest accrual	3,064
Paid interests	(5,361)
Disposals (sale and redemption)	(126,498)
Gains/losses from changes in fair value	(4,242)
Exchange differences	1,694
At end of year	**314,631**

Movement of impairments of assets measured at fair value through other comprehensive income

(in thousands of euros)

	STAGE 1	STAGE 2	STAGE 3	TOTAL
At the beginning of the year (1 January 2018)	**145**	**-**	**-**	**145**
Transfer to stage 1	13	(13)	-	**-**
Transfer to stage 2	(13)	13	-	**-**
Release of impairments	(71)	-	-	**(71)**
At the end of year	**74**	**-**	**-**	**74**

Note:
STAGE 1: 12-month ECL
STAGE 2: Lifetime ECL not credit-impaired
STAGE 3: Lifetime ECL credit-impaired

25. DEBT SECURITIES

(in thousands of euros)

	2018	2017
Corporate bonds	1,266	-
Total	**1,266**	**-**

Fair value of corporate bonds as at 31.12.2018 amounted to EUR 1,277 thousand.

26. LOANS TO BANKS

(in thousands of euros)

	2018	2017
Placements with other banks	53,655	41,146
Gross loans to banks	**53,655**	**41,146**
Impairment	(32)	(4)
Net loans to banks	**53,623**	**41,142**

As at 31 December 2018 no placements with other banks are shown under Pledged assets (2017: nil).

27. LOANS TO NON-BANK CUSTOMERS

(in thousands of euros)

	2018	2017
Loans to individuals:	**654,315**	**591,185**
- Overdrafts	25,632	22,552
- Credit cards	14,123	17,086
- Term loans	133,521	116,214
- Mortgages	474,947	428,177
- Financial leases	6,092	7,156
Loans to sole proprietors	**54,077**	**54,696**
Financial leases	7,609	7,959
Other loans	46,468	46,737
Loans to corporate entities	**1,136,561**	**1,129,339**
Financial leases	40,068	43,285
Other loans	1,096,493	1,086,054
Gross loans and advances	**1,844,953**	**1,775,220**
Less provision for impairment	(87,865)	(100,193)
Net loans and advances	**1,757,088**	**1,675,027**
Reclassification to financial assets mandatorily FVTPL		(18,878)
Net loans and advances	**1,757,088**	**1,656,149**

Movement in provisions for impairment losses on loans to retail and corporate as follows

(in thousands of euros)

	Loans to individuals	Sole proprietors	Corporate entities	Total
As at 31 December 2016	**8,182**	**7,105**	**89,084**	**104,371**
Provision for loan impairment	3,885	1,882	40,667	46,434
Amounts recovered during the year	(3,694)	(1,923)	(22,522)	(28,139)
Included in income statement	191	(41)	18,145	18,295
Write off	(1,151)	(985)	(20,337)	(22,473)
As at 31 December 2017	**7,222**	**6,079**	**86,892**	**100,193**

Movement in provisions for impairment losses on loans to individuals as follows:

(in thousands of euros)

As at 31 December 2017	**7,222**			
Impact of adopting IFRS9	2,218			
	STAGE 1	**STAGE 2**	**STAGE 3**	**TOTAL**
As at 1 January 2018	**2,727**	**334**	**6,379**	**9,440**
Provision for loan impairment	9,821	3,323	11,616	**24,760**
Amounts recovered during the year	(10,462)	(2,059)	(8,741)	**(21,262)**
Included in income statement	**(641)**	**1,264**	**2,875**	**3,498**
Transfer to/from stage 1	-	(1,011)	(218)	**(1,229)**
Transfer to/from stage 2	1,011	-	61	**1,072**
Transfer to/from stage 3	218	(61)	-	**157**
Write off	-	-	(202)	**(202)**
As at 31 December 2018	**3,315**	**526**	**8,895**	**12,736**

Movement in provisions for impairment losses on loans to sole proprietors as follows:

(in thousands of euros)

As at 31 December 2017	**6,079**			
Impact of adopting IFRS9	525			
	STAGE 1	**STAGE 2**	**STAGE 3**	**TOTAL**
As at 1 January 2018	**839**	**382**	**5,383**	**6,604**
Provision for loan impairment	6,620	9,851	2,615	**19,086**
Amounts recovered during the year	(6,909)	(9,589)	(811)	**(17,309)**
Included in income statement	**(289)**	**262**	**1,804**	**1,777**
Transfer to/from stage 1	-	(200)	(72)	**(272)**
Transfer to/from stage 2	200	-	88	**288**
Transfer to/from stage 3	72	(88)	-	**(16)**
Write off	-		(2,375)	**(2,375)**
As at 31 December 2018	**822**	**356**	**4,828**	**6,006**

Movement in provisions for impairment losses on loans to corporate entities as follows:

(in thousands of euros)

As at 31 December 2017	**86,892**			
Transfer to mandatorily FVTPL	(11,187)			
Impact of adopting IFRS9	1,576			
	STAGE 1	**STAGE 2**	**STAGE 3**	**TOTAL**
As at 1 January 2018	**4,798**	**6,576**	**65,907**	**77,281**
Provision for loan impairment	278,158	556,858	31,094	**866,110**
Amounts recovered during the year	(278,673)	(556,958)	(23,723)	**(859,354)**
Included in income statement	**(515)**	**(100)**	**7,371**	**6,756**
Transfer to/from stage 1	-	(307)	(32)	**(339)**
Transfer to/from stage 2	307	-	309	**616**
Transfer to/from stage 3	32	(309)	-	**(277)**
Write off	(2)	(1)	(9,390)	**(9,393)**
Sale	-	-	(4,283)	**(4,283)**
Diminution due to POCI	-	-	(1,238)	**(1,238)**
As at 31 December 2018	**4,620**	**5,859**	**58,644**	**69,123**

Note:
STAGE 1: 12-month ECL
STAGE 2: Lifetime ECL not credit-impaired
STAGE 3: Lifetime ECL credit-impaired

In 2018 the Bank continued with the non-performing reduction plan, which is also in line with Bank of Slovenia Regulation criteria for write-offs in the assessment of credit risk losses.

Customer loan portfolio by economic sector

(in thousands of euros)

	2018	2017
Non-financial entities	853,586	821,215
- transport and storage	259,578	264,762
- manufacturing	188,545	193,502
- wholesale and retail trade	138,766	119,887
- information and communication	51,294	62,895
- accommodation and service activities	38,995	34,621
- construction	28,838	31,479
- other non-financial entities	147,570	114,069
Government	20,417	62,244
Other public entities	195,315	189,828
Financial entities	66,258	55,356
Individuals	654,316	591,185
Sole proprietors	54,076	54,697
Non-profit institutions serving households	985	695
Gross loans and advances to customers	**1,844,953**	**1,775,220**
Less provision for impairment	(87,865)	(100,193)
Net loans and advances to customers	**1,757,088**	**1,675,027**

At the end of 2018 the share of loans to non-bank customers on the domestic market amounted to 91.3%, the remaining share of 6.5 related to the EU market, and 2.2% to other markets respectively.

Analysis of financial leases by residual maturity:

(in thousands of euros)

	2018	2017
Future minimum lease payment (finance lease)		
Not later than 1 year	15,436	18,899
Later than 1 year and not later than 5 years	29,457	28,804
Later than 5 years	8,876	10,697
Total	**53,769**	**58,400**
Impairment	**(5,267)**	**(4,227)**
Present value of future minimum lease payments:		
Not later than 1 year	14,038	16,966
Later than 1 year and not later than 5 years	28,301	27,693
Later than 5 years	6,163	9,514
Total	**48,502**	**54,173**

Forborne exposures as at 31.12.2018

(in thousands of euros)

	General governments	Total	Other equipment	Total
Performing exposures	-	30,681	688	**31,369**
Instruments with modifications in their terms and conditions	-	44,476	2,152	**46,628**
Refinancing	-	889	945	**1,834**
Total gross carrying amount	**-**	**76,046**	**3,785**	**79,831**
Performing	-	(1,869)	(72)	**(1,941)**
Instruments with modifications in their terms and conditions	-	(27,501)	(1,684)	**(29,185)**
Refinancing	-	(544)	(786)	**(1,330)**
Accumulated impairment, accumulated changes in fair value due to credit risk and provisions	**-**	**(29,914)**	**(2,542)**	**(32,456)**
Performing exposures	-	28,812	616	**29,428**
Instruments with modifications in their terms and conditions	-	16,975	468	**17,443**
Refinancing	-	345	159	**504**
Net carrying amount	**-**	**46,132**	**1,243**	**47,375**

In 2018 the Bank restructured loans in the amount of 28,602 thousands EUR (2017: EUR 9,322 thousands).

Forborne exposures as at 31.12.2017

(in thousands of euros)

	General governments	Total	Other equipment	Total
Performing exposures	-	6,710	585	**7,295**
Instruments with modifications in their terms and conditions	-	56,148	2,599	**58,747**
Refinancing	-	33,338	1,020	**34,358**
Total gross carrying amount	**-**	**96,196**	**4,204**	**100,400**
Performing	-	(516)	(26)	**(542)**
Instruments with modifications in their terms and conditions	-	(24,610)	(1,638)	**(26,248)**
Refinancing	-	(12,960)	(725)	**(13,685)**
Accumulated impairment, accumulated changes in fair value due to credit risk and provisions	**-**	**(38,086)**	**(2,389)**	**(40,475)**
Performing exposures	-	6,194	559	**6,753**
Instruments with modifications in their terms and conditions	-	31,538	961	**32,499**
Refinancing	-	20,378	295	**20,673**
Net carrying amount	**-**	**58,110**	**1,815**	**59,925**

Forbearance measures are concessions made to a borrower facing or about to face financial difficulties by agreeing to change agreed contractual terms and conditions, so as to make them for the borrower more favourable than those that would be granted under normal conditions. Forbearance measures are conceded in order to maximize collection and minimize the risk of default. A forborne exposure can be performing or non-performing and related to retail or corporate customers.

According to the Bank regulations, individual loan contracts are flagged as exposures with forbearance measures for the purpose of evidencing the portfolio of forborne exposures, i.e., exposures which meet the above described definition. The forborne flag is therefore an additional element for classification of credit exposures for the purpose of credit portfolio monitoring and reporting. Taking into account the internal rules for the performing and non-performing exposures classification, rules governing the forborne exposures did not have a significant impact on the Bank's income statement.

Loans and advances are further analysed as a part of the statement of financial position in the accompanying notes: Analysis of past due financial instruments 3.4, Currency Risk Note 3.7.2., Interest Rate Risk Note 3.7,3., Liquidity Risk Note 3.5., Fair value Note 3.9., and Related Party Transactions Note 49.

28. ADVANCES

(in thousands of euros)

	2018	2017
Commissions receivables	395	351
Cheques	1	1
Receivables	275	446
Claims to Europay	7,668	5,448
Claims to citizens	1,024	1,508
Claims relating to interbank settlement for Visa card	4,932	4,500
Claims due to recovery procedures	1,307	1,063
Other	4,481	1,520
Gross advances	**20,083**	**14,837**
Impairments	(1,356)	(1,106)
Net advances	**18,727**	**13,731**

Movement in provisions for impairment on other assets:

(in thousands of euros)

As at 31 December 2016	**1,376**
Additional provision for impairment	397
Amounts recovered during the year	(377)
Included in income statement	20
Write off of impairment	(290)
As at 31 December 2017	**1,106**
Additional provision for impairment	413
Amounts recovered during the year	(161)
Included in income statement	252
Write off of impairment	(2)
As at 31 December 2018	**1,356**

29. NON-CURRENT ASSETS HELD FOR SALE

(in thousands of euros)

	2018	2017
At the beginning of the year	**19,601**	**-**
Sale	(2,478)	-
Transfer to inventories	(1,416)	-
Transfer to property and equipment	(444)	-
Transfer from property and equipment	-	600
Transfer from investment property		19,001
Impairments	(671)	-
At the end of the year	**14,592**	**19,601**

30. PROPERTY, PLANT AND EQUIPMENT

(in thousands of euros)

	Land and buildings	Hardware equipment	Other equipment	Total
Movement in year 2017				
Opening net book amount	**16,430**	**747**	**1,523**	**18,700**
Additions	227	204	334	765
Disposals	-	-	(218)	(218)
Depreciation charge	(1,851)	(305)	(515)	(2,671)
Transfer to non-current assets held for sale	(600)	-	-	(600)
Closing net book amount before valuation	**14,206**	**646**	**1,124**	**15,976**
Valuation gain	13,792	-	-	13,792
Valuation loss	(974)	-	-	(974)
Closing net book amount	**27,024**	**646**	**1,124**	**28,794**
As at 31 December 2017				
Cost	29,369	5,662	10,745	45,776
Accumulated depreciation	(2,345)	(5,016)	(9,621)	(16,982)
Net book amount as at 31 December 2017	**27,024**	**646**	**1,124**	**28,794**
Movement in year 2018				
Opening net book amount	**27,024**	**646**	**1,124**	**28,794**
Additions	706	412	142	1,260
Disposals	(228)	(1)	(139)	(368)
Depreciation charge	(1,072)	(307)	(333)	(1,712)
Closing net book amount before valuation	**26,430**	**750**	**794**	**27,974**
Valuation gain	-	-	-	-
Valuation loss	-	-	-	-
Closing net book amount	**26,430**	**750**	**794**	**27,974**
As at 31 December 2018				
Cost	29,702	5,464	10,191	45,357
Accumulated depreciation	(3,272)	(4,714)	(9,397)	(17,383)
Net book amount as at 31 December 2018	**26,430**	**750**	**794**	**27,974**

In 2018 there was no property, plant and equipment pledged (2017; nil).

In addition to its own premises, the Bank hired premises at 29 locations. Future minimum lease payments under lease contracts amount to EUR 9,200 thousand, of this:

(in thousands of euros)

2018			2017		
Up to 1 year	**1 to 5 years**	**Over 5 years**	**Up to 1 year**	**1 to 5 years**	**Over 5 years**
572	3,779	4,849	560	2,240	2,800

As at 31 December 2018 properties were stated at its fair values.

31. INVESTMENT PROPERTY

(in thousands of euros)

	2018	2017
At beginning of the year	**-**	**13,985**
Depreciation	-	(369)
Transfer from property in use	-	-
Transfer to property in use	-	-
Transfer to inventory	-	-
Additions	-	3,461
Transfer from assets seized as collateral on stock	-	2,936
Disposals	-	(1,012)
Impairments	-	-
Transfer to non-current assets held for sale	-	(19,001)
At end of year	**-**	**-**

32. INTANGIBLE ASSETS

(in thousands of euros)

	Development	Licenses	Software and other	Total
Movement in year 2017				
Opening net book amount	2,801	658	608	4,067
Additions	654	18	72	744
Amortisation	(844)	(234)	(215)	(1,293)
Closing net book amount	**2,611**	**442**	**465**	**3,518**
As at 31 December 2017				
Cost	14,495	2,829	3,732	21,056
Accumulated amortisation	(11,884)	(2,387)	(3,267)	(17,538)
Net book amount as at 31 December 2017	**2,611**	**442**	**465**	**3,518**
Movement in year 2018				
Opening net book amount	2,611	442	465	3,518
Additions	1,661	128	6	1,795
Amortisation	(830)	(216)	(196)	(1,242)
Closing net book amount	**3,442**	**354**	**275**	**4,071**
As at 31 December 2018				
Cost	16,156	2,957	3,738	22,851
Accumulated amortisation	(12,714)	(2,603)	(3,463)	(18,780)
Net book amount as at 31 December 2018	**3,442**	**354**	**275**	**4,071**

The Bank has not pledged any intangible fixed assets.

The Bank does not have any intangible fixed assets in management.

In 2018, the Bank has not recognized any expenditure related to development in the income statement. All development expenditure in 2018 was capitalized as intangible fixed assets, out of which staff expenses amounted to EUR 360 thousand.

33. OTHER ASSETS

(in thousands of euros)

	2018	2017
Accruals	2,404	728
Inventory	116	4
Taxes and contributions	796	527
Repossessed assets	8,121	7,528
Prepayments and bails	5	103
Impairment on repossessed assets	(2,862)	(1,533)
Total	**8,580**	**7,357**

Repossessed assets related mainly to assets subject to leasing contracts. There are mainly real estate.

Movement in impairment

(in thousands of euros)

	2018	2017
At beginning of year	1,533	3,447
Additions	1,329	-
Diminution due to sale (included in sale effect)	-	(1,914)
At end of the year	**2,862**	**1,533**

34. DEPOSITS FROM BANKS AND CENTRAL BANKS

(in thousands of euros)

	2018	2017
Demand deposits	1,505	1,307
Term deposits	14,012	9,443
Total	**15,517**	**10,750**

35. DEPOSITS FROM NON-BANK CUSTOMERS

(in thousands of euros)

	2018	2017
Individuals		
- demand deposits	947,622	883,007
- term deposits	484,854	499,349
Sole proprietors		
- demand deposits	86,162	74,476
- term deposits	1,853	2,436
Corporate customers		
- demand deposits	627,487	461,188
- term deposits	59,692	51,040
Total	**2,207,670**	**1,971,496**

As at 31 December 2018, deposits in the amount of EUR 10,502 thousand have been pledged for covering potential credit risk on assets (2017: EUR 12,857 thousand).

36. LOANS FROM BANKS AND CENTRAL BANKS

The Bank repaid its obligations regularly. At the date of the financial statements, there are no obligations which are overdue.

(in thousands of euros)

	2018		2017	
	Short term	Long term	Short term	Long term
In local currency	-	28,872	-	58,184
In foreign currency	-	8,612	-	13,293
	-	**37,484**	**-**	**71,477**
Total	**37,484**		**71,477**	

37. LOANS FROM NON-BANK CUSTOMERS

(in thousands of euros)

	2018	2017
	Long term	Long term
Financial leases	32	-
Total	**32**	**-**

The residual maturity of the financial liability is shown in note 3.5. - Liquidity risk.

38. OTHER FINANCIAL LIABILITIES

(in thousands of euros)

	2018	2017
Unpaid commissions	140	136
Liabilities form credit card business	4,665	6,918
Not yet process payment*	9,640	20,189
Unpaid dividend	118	118
Creditors	2,258	1,137
Salaries	2,426	2,103
Deferred income	8,697	6,734
Other	628	802
Total	**28,572**	**38,137**

**The rise of unprocessed payment transactions in 2017 is a consequence of longer closure of payment systems during New Year holidays*

39. PROVISIONS FOR LIABILITIES AND CHARGES

The Bank also makes credit risk provisions for off-balance sheet items. The above credit risk provisions recorded by Banka Intesa Sanpaolo d.d. refer to contractual commitments for issued guarantees and letters of credits and irrevocable contractual commitments for granted, but undrawn loans. The same principles as for provisions for on-balance sheet items are applied.

(in thousands of euros)

	2018	2017
Provisions for restructuring	1,833	-
Provisions for legal proceedings	1,733	1,779
Provisions for off-balance sheet liabilities	4,411	3,652
Provision for redundancies	1,410	841
Provisions for cash returns from discontinued products	350	-
Total	**9,737**	**6,272**

As at 31 December 2018, the Bank was involved in several legal proceedings against it. Contingent liabilities in this respect are estimated in the amount of EUR 2,242 thousand. To this end, on the basis of its best estimation on the outcome of the legal proceedings, the Bank established provisions in the amount of EUR 1,733 thousand.

Movement in provisions:

(in thousands of euros)

	2018	2017
At beginning of year	**6,272**	**5,899**
Impact of adopting IFRS 9	103	-
At beginning of year (1 January)	**6,375**	**5,899**
Additional provision	6,823	4,508
Amounts recovered during the year	(3,313)	(4,126)
Included in income statement under provisions	3,510	382
Utilised provisions	(148)	(9)
At end of year	**9,737**	**6,272**

40. RETIREMENT BENEFIT OBLIGATIONS

(in thousands of euros)

	2018	2017
Retirement severance pay and long service bonuses	2,898	4,268
Total	**2,898**	**4,268**

Movements

(in thousands of euros)

	2018	2017
At beginning of year	**4,268**	**4,152**
Additional provisions	234	230
Amounts recovered during the year	(6)	-
Charged to income statement	228	230
Change in actuarial gains/loss	(1,416)	(5)
Utilised provisions	(182)	(109)
At end of year	**2,898**	**4,268**

41. DEFERRED INCOME TAXES

Deferred tax liabilities

(in thousands of euros)

	2018	2017
Non-current assets held for sale	-	2
Valuation of tangible fixed assets	2,621	2,621
Available-for-sale financial assets	-	1,365
Valuation and impairments of assets FVOCI	709	-
Provision for retirement benefit obligations (actuarial gains)	76	-
Total	**3,406**	**3,988**

Deferred tax assets

(in thousands of euros)

	2018	2017
Retirement and other employee benefits	360	426
Provisions for reorganization	174	-
Available-for-sale financial assets	212	331
Valuation and impairments of assets FVOCI	595	-
Loan impairments on financial and operating leasing	72	130
Other - depreciation above tax prescribed rate	22	5
Total	**1,435**	**892**
Net deferred tax	**(1,971)**	**(3,096)**

Movement in deferred taxes (offsetting of assets and liabilities)

(in thousands of euros)

	2018	2017
At beginning of year	**3,096**	**682**
Impact of adopting IFRS 9	(27)	
At beginning of year (1 January)	**3,069**	**682**
Deferred taxes charged in income statement	(108)	31
AFS financial assets (fair value measurement)	-	(237)
Valuation and impairment of FVOCI	(1,118)	-
Valuation of tangible fixed assets	-	2,620
Actuarial losses	134	-
Other	(6)	-
At end of year	**1,971**	**3,096**

Deferred taxes charged in income statement

(in thousands of euros)

	2018	2017
Retirement and other employee benefits	(8)	4
Provisions for reorganization	174	-
Impairment on FVOCI financial assets	(18)	-
Loan impairments on financial and operating leasing	(57)	(35)
Other (depreciation)	17	-
Total	**108**	**(31)**

42. OTHER LIABILITIES

(in thousands of euros)

	2018	2017
Accruals	269	1,951
Prepayments received	801	2,329
Taxes and contributions	1,712	1,347
Total	**2,782**	**5,627**

43. SHARE CAPITAL

(in thousands of euros)

	Number of shares	Ordinary shares	Share premium	Treasury shares
As at 31 December 2016	531,359	22,173	7,499	(49)
As at 31 December 2017	531,359	22,173	7,499	(49)
As at 31 December 2018	531,359	22,173	7,499	(49)

The share capital of the Bank is divided into 531,359 ordinary shares. Each share has an equal proportion in the share capital of the Bank and its participating value in the share capital as well. The proportion of each share in the share capital of the Bank is determined on the basis of the number of the issued shares.

44. ACCUMULATED OTHER COMPREHENSIVE INCOME

(in thousands of euros)

	2018	2017
Revaluation reserves:		
- Debt securities	(471)	4,386
- Equity securities	1,019	1,020
- Tangible fixed assets	11,172	11,172
Actuarial gain/losses	727	(555)
Total	**12,447**	**16,023**

Movement	Revaluation reserves
As at 31 December 2016	**5,859**
Valuation of available-for-sale securities	
Equity securities	**638**
- Fair value adjustment, net of tax	888
- Disposals	(250)
Debt securities	**(1,651)**
- Fair value adjustment, net of tax	515
- Disposals	(2,657)
- Valuation of hedge items transferred to profit or loss	491
Other comprehensive income	**11,177**
Actuarial loss	5
Effect of tax rate increase	11,172
As at 31 December 2017	**16,023**
Valuation of available-for-sale securities	
Impact of adopting IFRS 9	(427)
As at 1 January 2018	**15,596**
Equity securities	**437**
- Fair value adjustment, net of tax	420
- Disposals	17
Debt securities	**(4,860)**
- Fair value adjustment, net of tax	(3,912)
- Disposals and realised gains	24
- Valuation of hedge items transferred to profit or loss	(972)
Other comprehensive income	**1,274**
Actuarial loss	1,282
Gain from valuation of tangible fixed assets	(8)
As at 31 December 2018	**12,447**

45. RESERVES FROM PROFIT AND RETAINED EARNINGS

(in thousands of euros)

	2018	2017
Legal reserves	16,007	15,471
Statutory reserves	214,055	214,054
Retained earnings	12,143	10,009
Treasury share`s reserves	49	49
Total	**242,254**	**239,583**

(in thousands of euros)

Movement	Legal reserves	Statutory reserves	Retained earnings	Treasury shares	Total reserves
As at 31 December 2016	**15,260**	**214,053**	**25,238**	**49**	**254,600**
Net profit for the financial year	-	-	4,211	-	4,211
Dividends	-	-	(19,228)	-	(19,228)
Transfer to statutory reserves	-	1	(1)	-	-
Transfer to legal reserves	211	-	(211)	-	-
As at 31 December 2017	**15,471**	**214,054**	**10,009**	**49**	**239,583**
Impact of adopting IFRS 9	-	-	(4,027)	-	(4,027)
As at 1 January 2018	**15,471**	**214,054**	**5,982**	**49**	**235,556**
Net profit for the financial year	-	-	10,714	-	10,714
Dividends	-	-	(3,999)	-	(3,999)
Transfer to statutory reserves	-	-	-	-	-
Transfer to legal reserves	536	1	(537)	-	-
Loss from disposals of FVOCI shares	-	-	(17)	-	(17)
As at 31 December 2018	**16,007**	**214,055**	**12,143**	**49**	**242,254**

Legal reserves

In accordance with the Articles of Association of Banka Intesa Sanpaolo d.d., the Bank forms legal reserves in the amount adequate to ensure that the sum of its legal reserves and those capital reserves that shall be added to the legal reserves pursuant to the law governing the required amount of legal reserves equals twice the amount of the Bank’s share capital.

Statutory reserves

The Bank, according to its Statute, creates statutory reserves until they achieve an amount which is fifteen times that of the Bank’s registered capital stock. In each financial year, a part of the net profit that remained after any losses carried forward, legal reserves and reserves for own shares have been covered, can be allocated to statutory reserves.

46. DIVIDENDS PER SHARE

Dividends payable are not accounted for until they have been ratified by the Annual General Meeting. By the date the financial statements were authorised by the Management Board no dividends were proposed or declared. For 2017, the Bank disbursed for dividends EUR 3,999 thousand i.e. EUR 7.54 per share.

(in thousands of euros)

Distribution of the profit of the year	2018	2017
Net profit for the period	10,714	4,211
Allocation of the profit to the legal reserves (5%)	(536)	(211)
Net profit of the period available for distribution	**10,178**	**4,000**
Total net profit available for distribution at the AGM	**10,178**	**4,000**

47. CASH AND CASH EQUIVALENTS

(in thousands of euros)

	2018	2017
Cash and balances with central bank*	366,883	268,029
Loans and advances to banks	48,656	22,979
Total	**415,539**	**291,008**

**The figure Cash and balances with central bank differs from those in Statement of financial position due to mandatory reserve liability to central bank (note 20).*

48. CONTINGENT LIABILITIES AND COMMITMENTS

Capital commitments, At 31 December 2018, the Bank had no capital commitments (2017: nil).

Credit related commitments, Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, are exposed to credit risk, as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorising a third party draw funds from the Bank up to a stipulated amount under specific terms and conditions, are secured by the underlying shipments of goods to which they relate and therefore have significantly less risk, also because the Bank do not generally expect the third party to draw funds under such agreements.

With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to losses in an amount equal to the total unused commitments. However, the likely amount of losses is not easy to quantify and is considerably less than the total unused commitments since most commitments to extend credit are contingent upon customers fulfilment of specific credit standards which need to be met before the carrying out of the drawing. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

The following table indicates the contractual amounts of the Bank's off-balance sheet position by type of instrument.

(in thousands of euros)

	2018	2017
Documentary and commercial letters of credit	160	160
Guarantees	166,460	173,629
Credit commitments:	426,816	314,570
- original maturity up to 1 year	223,290	125,527
- original maturity over 1 year	203,526	189,043
	593,436	**488,359**
Provisions for off-balance sheet liabilities:		
Guarantees	(2,773)	(2,872)
Credit commitments	(1,638)	(781)
Total	**589,025**	**484,706**

Movements of provisions for off-balance sheet exposures (guarantees and credit commitments)

(in thousands of euros)

As at 31 December 2017	**3,653**			
Impact of adopting IFRS 9	103			
	STAGE 1	**STAGE 2**	**STAGE 3**	**TOTAL**
As at 1 January 2018	**1,581**	**183**	**1,992**	**3,756**
Additional impairments	1,593	604	1,362	**3,559**
Release of impairments	(1,691)	(415)	(795)	**(2,901)**
Included in income statement	(98)	189	567	**658**
Transfer from/to stage 1	-	(29)	(102)	**(131)**
Transfer from/to stage 2	29	-	(67)	**(38)**
Transfer from/to stage 3	102	67	-	**169**
Write-off	(2)	(1)	-	**(3)**
As at 31 December 2018	**1,612**	**409**	**2,390**	**4,411**

Note:
STAGE 1: 12-month ECL
STAGE 2: Lifetime ECL not credit-impaired
STAGE 3: Lifetime ECL credit-impaired

49. RELATED PARTY TRANSACTIONS

(in thousands of euros)

	Directors and employees with managerial contract		**Management board and their direct family members**		**Supervisory board members and their direct family members**		**Intesa SanPaolo Group without PBZ Group**		**PBZ Group**	
	2018	**2017**	**2018**	**2017**	**2018**	**2017**	**2018**	**2017***	**2018**	**2017***
Loans										
At beginning of the year	263	129	57	65	-	-	15,164	77,717	70,033	-
Loans issued during the year	44	181	78	-	-	-	1,204,408	1,193,012	135,570	80,178
Loan repayments during the year	(188)	(47)	(57)	(8)	-	-	(1,203,659)	(1,255,565)	(125,548)	(10,145)
At end of year	**119**	**263**	**78**	**57**	**-**	**-**	**15,913**	**15,164**	**80,055**	**70,033**
Impairment as at 31 December	-	-	-	-	-	-	-	-	-	-
Collateral received as at 31 December	381	535	88	283	-	-	-	-	-	-
Deposits										
At beginning of the year	1,425	893	1,338	2,513	-	127	55,007	116,183	-	-
Deposits received during the year	4,136	5,601	656	1,796	-	4	79,481	84,915	-	-
Deposits repaid during the year	(4,593)	(5,069)	(1,261)	(2,971)	-	(131)	(104,684)	(146,091)	-	-
At end of year	**968**	**1,425**	**733**	**1,338**	**-**	**-**	**29,804**	**55,007**	**-**	**-**
Interest expense on deposits	2	4	5	10	-	-	1,228	1,515	-	-
Interest income earned	2	3	-	1	-	-	339	204	552	168
Other revenue – fee income	2	1	2	1	-	-	96	555	27	19
Guarantees issued by the bank and commitments							9,269	5,777	1,139	527
Remuneration	**1,287**	**1,011**	**2,152**	**2,201**	**127**	**68**				

**In 2017 majority shareholder became Privredna Banka Zagreb d.d..*

There were no transactions made with companies in which the Management board, Supervisory board members and their closer family members or employees with managerial contract had significant influence.

GALLERIE D'ITALIA.
THREE MUSEUM VENUES: AN ITALIAN CULTURAL NETWORK.

Through the Gallerie d'Italia, Intesa Sanpaolo intends to share its artistic and architectural heritage with the public at large: 1,000 works of art displayed in historic palazzi in three cities creating a unique museum network.

Set in an architectural context of great value, ***Gallerie d'Italia - Piazza Scala in Milan*** displays a selection of two hundred nineteenth-century works of the Lombard school of painting, coming from the art collections of Fondazione Cariplo and Intesa Sanpaolo, along with a collection representative of twentieth-century Italian art.

Gallerie d'Italia - Palazzo Leoni Montanari in Vicenza exhibits works of eighteenth-century Veneto art and a collection of Attic and Magna Graecia pottery. Moreover, one of the most important collections of Russian icons in the West is safeguarded here.

Gallerie d'Italia - Palazzo Zevallos Stigliano in Naples houses The Martyrdom of Saint Ursula, Caravaggio's last documented painting, as well as a collection of over one hundred and twenty artworks representative of Neapolitan artistic output from the early seventeenth century to the beginning of the twentieth century.

Cover photo:

Angelo Inganni's vedute are fine works offering a valuable insight into the urban transformations that Milan experienced during the 19th century. In Piazza della Scala under the snow, seen from the Gallery, the artist depicts Teatro alla Scala before the square it faces was opened, which involved the demolition of a housing block next to the Palazzo Marino, and subsequently led to the construction of the Galleria Vittorio Emanuele II and the erection of the Leonardo da Vinci monument.

Despite the structural balance of the work, the resulting image - created with free and vibrant brushstrokes with no concern for defined outlines - seems somewhat random, almost like a snapshot of the path running between the snowy square and the Galleria.

*The work is part of the permanent collection at the **Gallerie d'Italia,** Intesa Sanpaolo's museum complex located in **Piazza Scala, Milan.** The exhibition dedicated principally to 19th century art opens with Neoclassical works and continues through to the turn of the 20th century, with a century's worth of Italian paintings depicting historical events, battles of the Risorgimento (the Italian Unification), vedute and landscapes, as well as genre paintings and masterpieces of Symbolism.*

ANGELO INGANNI
(Brescia, 1807 - 1880)
Piazza della Scala under the snow, seen from the Gallery
1874 oil on canvas, 65,5 x 55,5 cm
Intesa Sanpaolo Collection
Gallerie d'Italia - Piazza Scala, Milan

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