ANNUAL REPORT 2018

ABANKA

Your friendliest bank

Supporting knowledge

Abanka believes in the power and importance of knowledge, ideas and development. Thus, since 2018, the majority of our sponsorship activities and donations focus on supporting knowledge, from learning by the youngest generation and facilitating access to knowledge by the general public, to support for the research of top experts.

CONTENTS

The Abanka Group Annual Report 2018 is a translation of the original Abanka Group Annual Report 2018 issued in Slovene. This translation is provided for reference purpose only.

Sharing time, energy and knowledge

We can all contribute to a better today and tomorrow. Employees therefore provide assistance in a number of areas through an active corporate volunteer programme that Abanka introduced in 2018. Through charitable activities, solidarity and volunteer work, we are building a more responsible society and unselfishly improving the world around us.

FINANCIAL HIGHLIGHTS AND PERFORMANCE INDICATORS

FINANCIAL HIGHLIGHTS AND PERFORMANCE INDICATORS – THE ABANKA GROUP

STATEMENT OF FINANCIAL POSITION (EUR thousand)	31 Dec. 2018	31 Dec. 2017	31 Dec. 2016
Total assets	**3,731,542**	3,654,177	3,614,833
Total amount of deposits of the non-banking sector, measured at amortised cost	**2,934,453**	2,856,026	2,775,399
Total amount of loans to the non-banking sector (not held for trading)	**1,952,759**	1,967,460	1,806,473
Total equity	**583,407**	580,283	616,828

INCOME STATEMENT (EUR thousand)	2018	2017	2016
Net interest income	**61,075**	73,428	78,714
Net non-interest income	**64,125**	46,993	53,767
Labour costs, general and administration costs	**(65,243)**	(67,626)	(70,671)
Depreciation	**(7,804)**	(8,559)	(8,382)
Impairment and provisions (credit losses)	**21,962**	5,994	28,960
Profit or loss from ordinary operations before tax	**70,081**	47,022	83,611
Corporate income tax on ordinary operations	**(4,489)**	(5,427)	(6,097)
Profit after tax from ordinary operations	**65,592**	41,595	77,514

STATEMENT OF COMPREHENSIVE INCOME (EUR thousand)	2018	2017	2016
Other comprehensive income before tax	**(606)**	(11,273)	(11,595)
Income tax relating to components of other comprehensive income	**110**	2,112	932

INDICATORS			
	31 Dec. 2018	31 Dec. 2017	31 Dec. 2016
Common Equity Tier 1 capital ratio	**23.7%**	24.6%	26.5%
Tier 1 capital ratio	**23.7%**	24.6%	26.5%
Total capital ratio	**23.7%**	24.6%	26.5%
	2018	2017	2016
Performance (in %)			
- return on assets after tax[1]	**1.77**	1.15	2.08
- return on equity after tax[2]	**11.39**	6.96	13.14
Operational costs (in %)			
- operating expenses in gross income (CIR)	**58.34**	63.27	59.67

Note:
Financial highlights and performance indicators as at 31 December 2018 are in compliance with IFRS 9, while the comparative data for 2017 are in compliance with IAS 39. Due to the changes in accounting policies regarding the calculation of the tax on financial services, the comparative data in the income statement for 2017 were changed; see Note 1.25 of the Financial Report for further details.

Notes:

Data and performance indicators have been calculated in accordance with the Instructions for compiling the statement of financial position, the income statement and the statement of comprehensive income and for calculating the performance indicators of banks and savings banks, which the Bank of Slovenia set out.

(1) The indicator equals the ratio **profit or loss after tax/average assets**. Average assets have been calculated as the average amount of assets as at the last day of each quarter, including the amount of assets as at the last day of December of the previous year.
(2) The indicator equals the ratio **profit or loss after tax/average equity**. Average equity has been calculated as the average amount of equity as at the last day of each quarter, including the amount of equity as at the last day of December of the previous year.

LIQUIDITY	31 Mar. 2018	30 June 2018	30 Sep. 2018	31 Dec. 2018
- Liquidity coverage ratio (in %)	418%	392%	394%	430%
- Liquidity buffer (EUR thousand)	1,359,284	1,283,553	1,276,704	1,349,721
- Net liquidity outflow (EUR thousand)	324,993	327,488	324,202	313,730

FINANCIAL HIGHLIGHTS AND PERFORMANCE INDICATORS – ABANKA

STATEMENT OF FINANCIAL POSITION (EUR thousand)	31 Dec. 2018	31 Dec. 2017	31 Dec. 2016
Total assets	**3,728,713**	3,655,984	3,612,362
Total amount of deposits of the non-banking sector, measured at amortised cost	**2,935,223**	2,861,197	2,776,583
– from legal and other persons, who pursue a business activity[1]	**847,605**	879,572	850,784
– retail	**2,087,618**	1,981,625	1,925,799
Total amount of loans to the non-banking sector (not held for trading)	**1,959,283**	1,982,137	1,826,524
– to legal and other persons, who pursue a business activity[1]	**1,053,585**	1,132,563	1,011,425
– retail	**905,698**	849,574	815,099
Total equity	**583,384**	578,943	614,451
Value adjustments and provisions for credit losses[(6)]	**105,778**	176,075	-
Off-balance sheet items (B.1 to B.4)	**1,182,200**	913,098	695,525

INCOME STATEMENT (EUR thousand)	2018	2017	2016
Net interest income	**60,610**	71,915	77,573
Net non-interest income	**64,370**	46,774	52,498
Labour costs, general and administration costs	**(63,798)**	(65,424)	(68,246)
Depreciation	**(7,235)**	(7,373)	(7,185)
Impairment and provisions (credit losses)	**22,040**	8,186	29,467
Profit or loss before tax from ordinary operations	**71,212**	47,835	82,447
Corporate income tax from ordinary operations	**(4,475)**	(5,215)	(5,791)
Profit after tax from ordinary operations	**66,737**	42,620	76,656

STATEMENT OF COMPREHENSIVE INCOME (EUR thousand)	2018	2017	2016
Other comprehensive income before tax	**(608)**	(11,261)	(11,590)
Income tax relating to components of other comprehensive income	**110**	2,112	932

NUMBER OF EMPLOYEES	31 Dec. 2018	31 Dec. 2017	31 Dec. 2016
	1,010	1,047	1,147

SHARES	31 Dec. 2018	31 Dec. 2017	31 Dec. 2016
Number of shareholders	**1**	1	1
Number of shares	**15,100,000**	15,100,000	15,100,000
Proportion of par-value shares in share capital (in EUR)	**10.00**	10.00	10.00
Book value per share (in EUR)	**38.63**	38.34	40.69

Note:
Financial highlights and performance indicators as at 31 December 2018 are in compliance with IFRS 9, while the comparative data for 2017 are in compliance with IAS 39. Due to the changes in accounting policies regarding the calculation of the tax on financial services, the comparative data in the income statement for 2017 were changed; see Note 1.25 of the Financial Report for further details.

Note:
[1] non-financial corporations, public sector entities, other financial institutions, sole proprietors, foreign corporate entities and non-profit institutions serving households.

INDICATORS

	31 Dec. 2018	31 Dec. 2017	31 Dec. 2016
Common Equity Tier 1 capital ratio	**23.6%**	**24.3%**	**26.3%**
Tier 1 capital ratio	**23.6%**	**24.3%**	**26.3%**
Total capital ratio	**23.6%**	**24.3%**	**26.3%**
Quality of assets and contingent liabilities (in %)			
Non-performing (on-balance sheet and off-balance sheet) exposures / classified on-balance sheet and off-balance sheet exposures[6]	**3.06**	5.24	-
Non-performing loans and other financial assets / classified loans and other financial assets[6]	**4.37**	8.63	-
Value adjustments and provisions for credit losses / non-performing exposures[6]	**43.91**	54.96	-
Received insurance / non-performing exposures[6]	**33.05**	41.53	-
	2018	2017	2016
Performance (in %)			
– interest margin[1]	**1.64**	1.98	2.05
– financial intermediation margin[2]	**3.38**	3.27	3.44
– return on assets after tax[3]	**1.80**	1.18	2.03
– return on equity before tax[4]	**12.47**	8.02	13.95
– return on equity after tax[5]	**11.68**	7.15	12.97
Operational costs (in %)			
– operational costs/average assets	**1.92**	2.01	1.99
- operating expenses in gross income (CIR)	**56.84**	61.33	57.99

Notes:

Data and performance indicators have been calculated in accordance with the Instructions for compiling the statement of financial position, the income statement and the statement of comprehensive income and for calculating the performance indicators of banks and savings banks, which the Bank of Slovenia set out.

(1) The indicator equals the ratio **net interest income/average assets**. Average assets have been calculated as the average amount of assets over the last 13 months as at the last day of each month, including the amount of assets as at the last day of December of the previous year.

(2) The indicator equals the ratio **(net interest income+net non-interest income)/average assets**. Average assets have been calculated as the average amount of assets over the last 13 months as at the last day of each month, including the amount of assets as at the last day of December of the previous year.

(3) The indicator equals the ratio **profit or loss after tax/average assets**. Average assets have been calculated as the average amount of assets over the last 13 months as at the last day of each month, including the amount of assets as at the last day of December of the previous year.

(4) The indicator equals the ratio **profit or loss before tax/average equity**. Average equity has been calculated as the average amount of equity over the last 13 months as at the last day of each month, including the amount of equity as at the last day of December of the previous year.

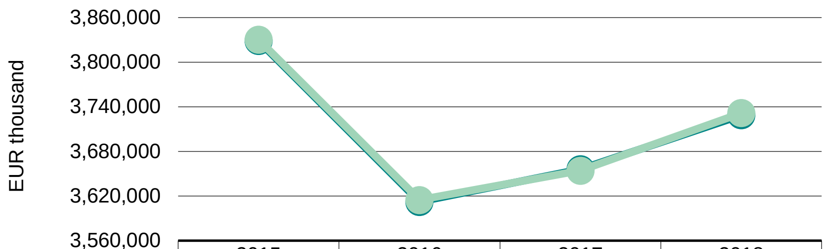
(5) The indicator equals the ratio **profit or loss after tax/average equity**. Average equity has been calculated as the average amount of equity over the last 13 months as at the last day of each month, including the amount of equity as at the last day of December of the previous year.

(6) The indicator as at 31 December 2017 is calculated based on the data as at 1 January 2018 (under the IFRS 9 standard). The indicator as at 31 December 2016 was not calculated due to the changed methodology.

LIQUIDITY

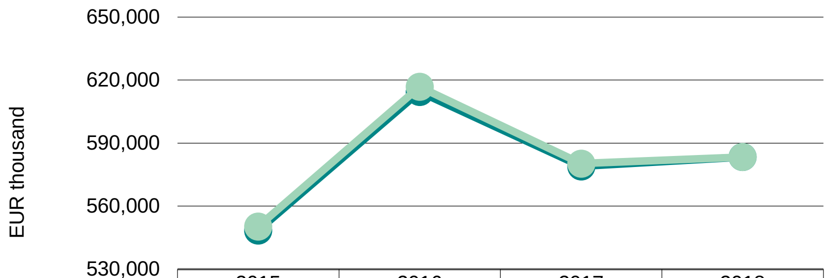
	31 Mar. 2018	30 June 2018	30 Sep. 2018	31 Dec. 2018
- Liquidity coverage ratio (in %)	414%	390%	392%	428%
- Liquidity buffer (EUR thousand)	1,359,284	1,283,553	1,276,704	1,349,721
- Net liquidity outflow (EUR thousand)	328,092	328,956	325,921	315,050

TOTAL ASSETS



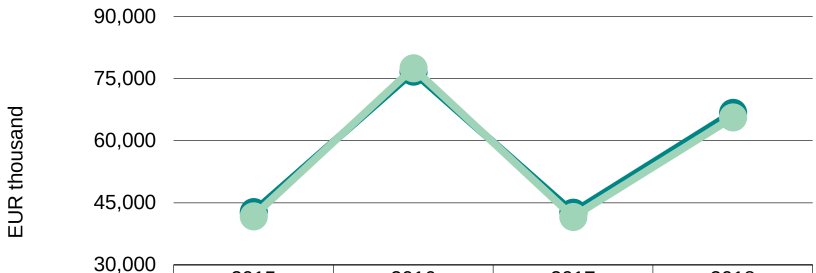
	2015	2016	2017	2018
Abanka	3,828,463	3,612,362	3,655,984	3,728,713
Abanka Group	3,830,227	3,614,833	3,654,177	3,731,542

TOTAL EQUITY



	2015	2016	2017	2018
Abanka	548,465	614,451	578,943	583,384
Abanka Group	550,379	616,828	580,283	583,407

PROFIT/LOSS AFTER TAX

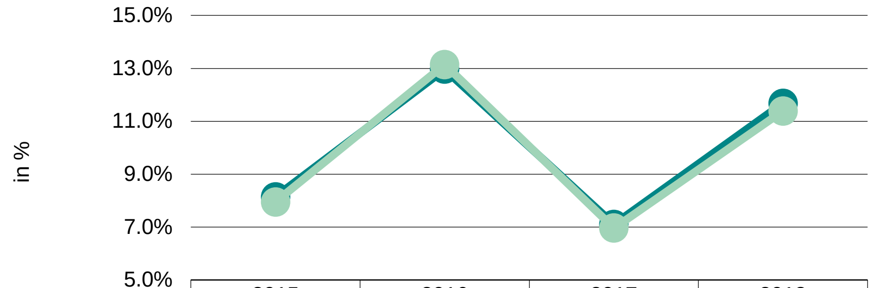


	2015	2016	2017	2018
Abanka	42,775	76,656	42,620	66,737
Abanka Group	41,722	77,514	41,595	65,592

RETURN ON AVERAGE ASSETS (net ROAA)

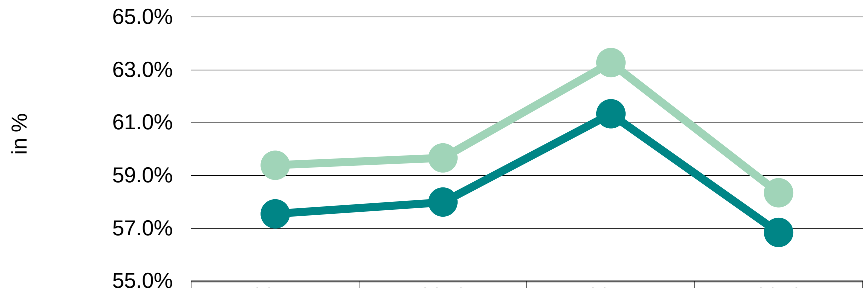
	2015	2016	2017	2018
Abanka	1.1%	2.0%	1.2%	1.8%
Abanka Group	1.0%	2.1%	1.1%	1.8%

RETURN ON AVERAGE EQUITY (net ROAE)



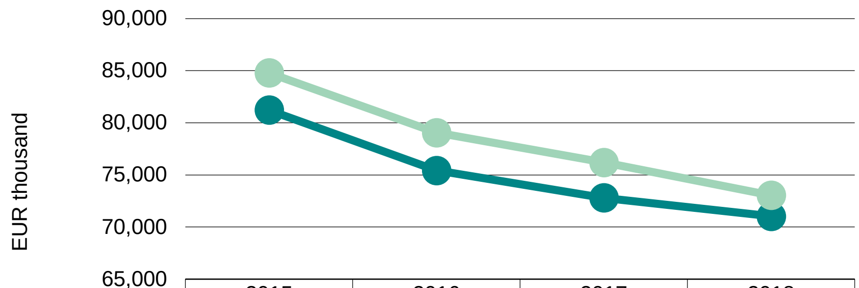
	2015	2016	2017	2018
Abanka	8.1%	13.0%	7.1%	11.7%
Abanka Group	8.0%	13.1%	7.0%	11.4%

COST TO INCOME RATIO (CIR)



	2015	2016	2017	2018
Abanka	57.6%	58.0%	61.3%	56.8%
Abanka Group	59.4%	59.7%	63.3%	58.3%

COSTS



	2015	2016	2017	2018
Abanka	81,225	75,431	72,797	71,033
Skupina Abanka	84,786	79,053	76,185	73,047

MANAGEMENT

MANAGEMENT BOARD OF THE BANK

Management Board

Matevž SLAPNIČAR
Member of the Management Board

Jože LENIČ
President of the Management Board

Matej GOLOB MATZELE
Member of the Management Board

Report of the Management Board

Dear customers, business partners and colleagues,

Abanka achieved excellent business results in 2018, generating a net profit of EUR 66.7 million. We did not rest on the laurels of the past year but we continued with the restructuring of the Bank and upgrading of business processes. A digital transformation strategy was developed and the Bank's business strategy was revised with the aim of improving customer satisfaction and creating new market opportunities, which is in line with our vision of **becoming the first bank in Slovenia according to the choice of customers, employees and investors**. Excellent performance, capital strength, high liquidity and a significant decrease in non-performing loans had an impact on the credit rating of the Bank, as in 2018 the international rating agency Moody's Investors Service upgraded Abanka's credit rating again to investment grade.

In 2018, the Bank continued with business optimisation, which was reflected in business process simplification and acceleration as well as in operating expenses, which were lower by 2.4% or EUR 1.8 million in the reporting period compared with 2017. In line with the strategy of reducing non-performing exposures, the Bank continued to actively reduce the share of non-performing loans by selling non-performing loans, thereby reducing the NPL share of the Group by 5.6 percentage points to 4.6%. The gains on the sale of non-performing loans also contributed to the good business results achieved by the Bank in 2018. Additional risk management methodologies and tools were designed, both for credit and other risks, in addition to significantly upgrading the Risk Management Strategy and the Risk Appetite.

In 2018, special attention was on the development and marketing of digital solutions. Our first tasks in the context of digitalisation focused on personal finance management, modernisation of posts, mobility of services and open banking integration. The Abaklub customer loyalty programme and the Abagarant insurance product were launched. The Abamobi mobile application and the Abanet online bank were redesigned, and a new mobile wallet Abadenarnica was designed, which stores virtual cards on a mobile phone, enabling easy and secure payment. An agile team was set up, who developed a modern, agile method of development to assist the Bank in the fulfilment of business and digital transformation objectives. All employees can participate in creating a better Abanka with their ideas through the employee-driven idea system – Aideja. The modern solutions Abanet and Abamobi are used by an increasing number of customers. In addition to the growing number of cashless transactions, the use of business cards is on the rise as increasingly more customers use the Bank's security measures, particularly the SMS notification service – Abasms.

In 2018, treasury products were actively marketed, but the highest increase in demand was seen in financial instruments for hedging against market risk, specifically for hedging against currency risks due to the high volatility in foreign exchange markets and for hedging against the interest rate risk due to the extremely low interest rates in the euro area. The management of the debt securities portfolio included in the trading and banking books demanded the Bank to continue to apply a conservative and prudent investment policy, i.e. investing in highly liquid and high investment grade securities. Abanka is recognised by domestic and foreign institutional investors as an important partner in ensuring the liquidity of the Slovene government securities.

The Bank has excellent cooperation with all customer segments. We remain the leading bank in custody services for investment and pension funds and also provide custody and administrative services for alternative investment funds. Furthermore, the Bank holds high market shares in the domestic payment system, is actively engaged in bullion trading and provides high quality and competitive insurance services, in addition to achieving good results in the sale of mutual funds. In the context of cashless operations, the Bank offers its customers a range of card services. Trade finance represents an important complementary service in financing and/or monitoring and execution of domestic and international commercial transactions. According to its customers, Abanka is an excellent partner, because it provides a comprehensive range of all trade finance products, professional execution of transactions, advice and support to customers in selecting an appropriate instrument, as well as continuous service development focused on digitalisation. Taking an individual approach and quickly tailoring a product to the customer's specific needs are of particular importance.

Abanka accomplishes its **mission of "UNITING WITH EXCELLENCE IN FINANCIAL SERVICES**" through its values. **Kindness** is Abanka's recognisable feature, because it is friendly to the customers for whom its banking services are developed, to the partners with whom its success is built, to the employees and to the environment in which it operates. In 2018, the emphasis was on **corporate volunteering** because we are aware of the problem of the socially disadvantaged in the society and are willing to help. We have shown our kindness also in helping those who need it most. Abanka performs with **excellence** in all segments, seeks better ways of doing business in general and in day-to-day operations, through service development increases customer satisfaction and contributes to the excellence of the company. The source of our success is **partnership** as it aims to build long-term relationships with its employees and partners based on respect, care, honesty, trust and cooperation. We are focused on **innovation**, understand technological development guidelines and improve our services and business processes through innovation. Furthermore, we place emphasis on **execution**, which means achieving the set objectives with excellence and in due time.

Key strategic guidelines of the Bank include:
- transformation into a performance-oriented organisation and user experience improvement,
- product range optimisation and digitalisation so as to improve user experience,
- optimisation of the number of employees and labour costs and lower outsourcing costs,
- reduction of non-performing loans and ongoing upgrading of ICAAP and ILAAP and
- improved IT efficiency and digital transformation.

Abanka's main goals in 2019 again include retail banking, the SME segment and key customers with significant non-interest income. In parallel, the aim will be that both the existing and new customers will use as many products and services provided by the Bank as possible. The existing business processes will continue to be upgraded. Furthermore, the Bank will continue to create a stimulating environment for employees, especially by maintaining a good climate and through employee engagement, and to effectively perform the lending activity and cost optimisation, as well as increase cross-selling. This will not only ensure profitable, safe and stable operations but also enhance the Bank's reputation among investors, thereby pursuing its **vision of becoming the first bank in Slovenia according to the choice of customers, employees and investors**.

In 2019, we will continue with the accelerated development of digital channels as well as with the upgrading of electronic and mobile channels so as to provide a more user-friendly experience to our customers. Acceleration of digital transformation is one of the strategic programmes of the Bank so as to continue to be and remain a technologically advanced and innovative bank as well as to design customer-tailored and easy-to-use services accessible anytime and anyplace. The aim of business digitalisation is to ensure even faster solutions and additional benefits both for the existing and new customers. Moreover, by designing new solutions and developing modern sales channels, we wish to create new sources of income, which is very important in the low interest rate environment. We believe that the success of the Bank largely depends on engaged employees and good co-worker relationships, which is also in line with our most recognisable value – kindness. Together with our employees in an open work environment, we are building a better Abanka of the future.

Abanka is an innovative commercial bank, a bank of friendly people, which focuses on customers through its wide range of banking and insurance products, as only satisfied customers contribute to long-term strong and profitable performance of the Bank. By accomplishing the set strategic objectives and having a strong capital base in addition to improving user experience, we will continue to ensure safe, stable and profitable operations throughout 2019.

We pursue our business and strategic objectives in cooperation with our customers, business partners, competent and engaged employees, as well as with the support of our owner. The Management Board thanks all colleagues for their contribution to excellent business results in 2018, to our business partners for good cooperation and to our customers for their trust.

Management Board

Matevž SLAPNIČAR	**Matej GOLOB MATZELE**	**Jože LENIČ**
Member of the Management Board	Member of the Management Board	President of the Management Board

SUPERVISORY BOARD

31 December 2018

Marko GARBAJS	• GRIFFON&ROMANO S.P.A., Director until 19 December 2018, from 20 December 2018 serves as a non-executive president of the management body • INOXPOINT, Director until 19 December 2018
Melita MALGAJ	• Slovenski državni holding, d.d., Director of Tourism and Economy Management Department
Alenka VRHOVNIK TEŽAK	• VTT, storitve z dodano vrednostjo, d.o.o., Authorised Officer and Financial Adviser until 30 September 2018, from 1 October 2018 acts as a Financial Adviser • Sodno izvedeništvo in svetovanje, Mag. Alenka Vrhovnik Težak, Sodna izvedenka za ekonomijo-finance, s.p.
Rok PIVK	• Triglav Osiguruvanje A.D., Skopje, Executive Director • Skupna pokojninska družba, d.d., Member of the Supervisory Board until 30 August 2018
Dejan KAISERSBERGER	• SIDG, d.o.o., Director of Finance, Accounting and Controlling
Varja DOLENC	• Union hoteli d.d., Ljubljana, Director of Procurement and Real Property Management
Miha KOŠAK	• Fraport Slovenija, d.o.o., Member of the Advisory Committee • Independent Consultant, independent consultant • Emona Capital LLP, London, Adviser • Elan Inventa, d.o.o., Member of the Strategy Committee • Šiaulių Bankas, Vilnius, Lithuania, Member of the Supervisory Board • The British Slovenian Chamber of Commerce, London, UK/Ljubljana, Slovenia, Member of the Management Board

Report of the Supervisory Board

As at 31 December 2018, the Supervisory Board of Abanka was composed of seven members. In 2018, the composition of the Supervisory Board changed. As at the 2017 year-end, the Supervisory Board was composed of Marko Garbajs as Chairman of the Supervisory Board, Melita Malgaj as its Vice Chairman, and Alenka Vrhovnik Težak, Rok Pivk, Dejan Kaisersberger, Peter Merc, Blaž Šterk as its members. Blaž Šterk was a Supervisory Board member until 31 December 2017, whilst Bernarda Babič started serving on the Supervisory Board as of 1 January 2018. On 20 April 2018, the Supervisory Board took note of the resignation of the Supervisory Board Member Peter Merc, who resigned as a member of the Supervisory Board of Abanka d.d. as of 10 April 2018. He served on the Supervisory Board until 9 July 2018. On 22 May 2018, the Supervisory Board took note of the resignation of the Supervisory Board Member Bernarda Babič, resigning from the office as a member of the Supervisory Board as of 5 July 2018.

At the 37th General Meeting of Shareholders held on 17 May 2018, Marko Garbajs was reappointed a member of the Supervisory Board for a four-year term of office, starting on 5 October 2018. At the 38th General Meeting of Shareholders held on 30 July 2018, Varja Dolenc was appointed a Supervisory Board Member with a four-year term of office commencing on 31 July 2018. At the 39th General Meeting of Shareholders held on 21 September 2018, Miha Košak was appointed a Supervisory Board Member with a four-year term of office starting on 22 September 2018.

As at 31 December 2018, the Supervisory Board was composed of Marko Garbajs as Chairman of the Supervisory Board, Melita Malgaj as its Vice Chairman, and Alenka Vrhovnik Težak, Rok Pivk, Dejan Kaisersberger, Varja Dolenc and Miha Košak as its members. In 2018, the members of the Supervisory Board were very careful to avoid any conflict of interest – in cases when the Supervisory Board discusses issues related to a member of the Supervisory Board and/or persons linked to the members of the Supervisory Board, the latter are regularly excluded from the discussion and voting on those issues, with the Chairman of the Supervisory Board paying special attention to the exclusion of these members. When the Chairman is excluded, the session is chaired by the Vice Chairman. Any such exclusion is entered into the minutes.

The Supervisory Board had four committees:

- As at the reporting date, the **Audit Committee** had the following composition: Dejan Kaisersberger as Chair, and Melita Malgaj, Rok Pivk and Miha Košak as members. As at the 2017 year-end, the Committee consisted of: Dejan Kaisersberger as Chair, and Melita Malgaj, Rok Pivk, Alenka Vrhovnik Težak and Blaž Šterk as members. In 2018, the composition of the Committee changed. Blaž Šterk was its member until 31 December 2017, Bernarda Babič was its member from 1 January 2018 to 5 July 2018, Alenka Vrhovnik Težak was its member until 8 October 2018, and Miha Košak has been a member of the Committee since 9 October 2018. In 2018, the Committee held eleven meetings. The main purpose of the Audit Committee is to assist the Supervisory Board in discharging its supervision duties regarding the reliability of financial statements, financial reports and other financial information that the Bank provides to its shareholders and other members of the public concerning the qualifications, effectiveness and independence of the external auditor, the operation of the internal audit function and compliance of the Bank with the applicable legal and regulatory requirements.
- As at the reporting date, **the Nomination Committee** had the following composition: Melita Malgaj as its Chair, and Marko Garbajs and Dejan Kaisersberger as its members. In 2018, the composition of the Committee did not change. Marko Garbajs was its Chair until 4 September 2018, while Melita Malgaj has been its Chair since 5 September 2018. In 2018, the Committee held eleven meetings. The main purpose of the Nomination Committee is to support the Supervisory Board in the execution of their supervisory responsibilities with respect to personnel issues involving the Management Board and the Supervisory Board membership.
- As at the reporting date, the **Remuneration Committee** had the following composition: Rok Pivk as its Chair, and Alenka Vrhovnik Težak and Varja Dolenc as its members. As at the 2017 year-end, the Committee was composed of the following members: Alenka Vrhovnik Težak served as its Chair, and Rok Pivk and Peter Merc as its members. In 2018, the Committee's composition changed. Peter Merc was its Chair until 9 July 2018, and from 10 July 2018 Rok Pivk served as its Chair, while Alenka Vrhovnik Težak was a Committee member. Melita Malgaj was its member from 10 July 2018 to 4 September 2018, while since 5 September 2018 Varja Dolenc has served as its member. In 2018, the Committee held eight meetings. The main purpose of the Committee is to support the Supervisory Board in the execution of their supervisory duties in relation to preparing decisions on remuneration, including those having an impact on the risks and risk management of the Bank.
- As at 31 December 2018, **the Risk Monitoring and Asset Liability Management Committee** had the following composition: Alenka Vrhovnik Težak served as its Chair, and Marko Garbajs, Dejan Kaisersberger and Varja Dolenc as its members. As at the 2017 year-end, the Committee was composed of the following members: Alenka Vrhovnik Težak as its Chair, and Marko Garbajs, Dejan Kaisersberger, Peter Merc and Blaž Šterk as its members. In 2018, the composition of the Committee changed. Blaž Šterk served as its member until 31 December 2017, Bernarda Babič served as a member from 1 January 2018 to 5 July 2018, while Peter Merc was a member of the Committee until 9 July 2018. On 5 September 2018, Varja Dolenc joined the Committee as its member. In 2018, the Committee held eleven meetings. The main purpose of the Committee is to support the Supervisory Board in the execution of its supervisory duties with respect to taking decisions related to the risk management function, the risk profile and the control of asset liability management in the Bank.

With the exception of these committees, the Supervisory Board has no other division of duties among its members. The Rules of Procedure of the Supervisory Board and its committees are published on Abanka’s website.

All the members submitted their signed statements of independence to the Supervisory Board in accordance with the Corporate Governance Code for Listed Companies, which are published on the website of the Bank.

The self-assessment results of the Supervisory Board and its committees in 2018 were positive and adequate. The assessment of the Supervisory Board's work included the proposed activities for the elimination of any identified deficiencies. The professional qualifications, knowledge and experience cover a broad spectrum of expertise in finance, audit, supervision and other fields. In 2018, special attention was paid to strengthening the composition of the Supervisory Board with individuals possessing direct banking knowledge and experience. The organisation and functioning of Board members as a team facilitates the ongoing monitoring and supervision of the Bank's operations as well as initiatives and guidelines for its development. The Supervisory Board's self-assessment results positively affected and encouraged its work and confirmed that the Board had properly performed its activities.

Review of the Supervisory Board's activities in 2018

The Supervisory Board oversees the management of the Bank's business operations. In accordance with the powers and obligations defined in the Banking Act, the Companies Act, the Decision on Internal Governance, the Management Body and the Adequate Internal Capital Assessment Procedure for Banks and Savings Banks and the Articles of Association of the Bank, the Supervisory Board operated pursuant to the principles of modern corporate governance and thus, through its supervisory function, contributed to the efficiency and transparency of the Bank's operations. At its sessions, the Supervisory Board took note of the Bank’s financial operations, credit portfolio, non-performing loans and risk management activities, paying a special attention to the Bank’s management of capital, credit, liquidity, interest rate and operational risks. At the Supervisory Board sessions, the members of the Supervisory Board actively participated in and encouraged discussions particularly on financial operations of Abanka and the Abanka Group. The Bank's risk appetite framework (RAF) and risk appetite statement (RAS) were redesigned. On this basis, the ICAAP and ILAAP were adjusted. The Supervisory Board approved the Annual Plan of Abanka and the Abanka Group for 2019, including the financial plans up to 2021.

In the reporting year, the Supervisory Board held thirteen sessions. All Supervisory Board members regularly attended the sessions. In its initial composition (Marko Garbajs as Chairman, Melita Malgaj as Vice Chairman, and Alenka Vrhovnik Težak, Rok Pivk, Dejan Kaisersberger, Peter Merc and Bernarda Babič as members), the Supervisory Board held five regular sessions, one extraordinary session and one meeting by correspondence. For legitimate reasons, Dejan Kaisersberger was not present at the 36th regular session held on 27 February 2018, Peter Merc was absent from the 37th regular session held on 20 April 2018, and Melita Malgaj did not attend the 39th regular session held on 21 June 2018. The Supervisory Board held its 40th regular session on 30 July 2018 in the following composition: Marko Garbajs as its Chairman, Melita Malgaj as its Vice Chairman, and Alenka Vrhovnik Težak, Dejan Kaisersberger and Rok Pivk as its members. Only Rok Pivk was absent for legitimate reasons. Following the appointment of Varja Dolenc as a Supervisory Board member, the Supervisory Board held one regular session and one extraordinary session. Following the appointment of Miha Košak as a Supervisory Board member, the Supervisory Board held three regular sessions. All the Management Board members regularly attended the sessions of the Supervisory Board. At the 44th regular session held on 18 December 2018, Matevž Slapničar, a member of the Management Board, was absent for legitimate reasons.

In line with Abanka’s commitments made to the European Commission by the Republic of Slovenia upon the approval of state aid to the Bank (*State aid SA.38522 2014/N Slovenia, Restructuring aid for Banka Celje/Abanka*), a representative of KPMG, poslovno svetovanje d.o.o. attended the Supervisory Board sessions as a Monitoring Trustee. In 2018, the Supervisory Board sessions were also attended by the representatives of the Bank of Slovenia in their role as the Joint Supervision Team (JST).

The Supervisory Board’s regular sessions lasted 39 hours and 39 minutes in total, while extraordinary sessions lasted 4 hours and 35 minutes in total, which is 4% less than in 2017 (46 hours and 2 minutes).

At its sessions in 2018, the Supervisory Board:

- approved and adopted the Audited Annual Report of Abanka for 2017, including the auditor's report by Deloitte Revizija d.o.o. and the Corporate Governance Statement for 2017;
- approved the revised Strategy of Abanka d.d. for the 2018–2020 period;
- adopted the revised Governance Policy of Abanka d.d.;
- approved the Diversity Policy of the Management Body of Abanka d.d.;
- approved the Policy on Appointment of the Management Body Members, Fit and Proper Assessment and Succession Concept in Abanka d.d.;
- took note of the resignation letter of Peter Merc, resigning as a member of the Supervisory Board as of 10 April 2018; his resignation took effect on 9 July 2018;
- took note of the resignation letter of Bernarda Babič, resigning as a member of the Supervisory Board of Abanka d.d. as of 22 May 2018; she continued to serve on the Supervisory Board until 5 July 2018;
- approved the draft agenda of the 37th General Meeting of Shareholders held on 17 May 2018, the 38th General Meeting of Shareholders held on 30 July 2018 and the 39th General Meeting of Shareholders held on 21 September 2018;
- proposed that the 37th General Meeting of Shareholders reappoint Marko Garbajs a Supervisory Board for another four-year term of office and appoint two new members of the Supervisory Board at the 38th or the 39th General Meeting of Shareholders (before the appointment of Varja Dolenc as a new Supervisory Board member at the 38th General Meeting of Shareholders held on 30 July 2018 and before the appointment of Miha Košak as a new Supervisory Board member at the 39th General Meeting of Shareholders held on 21 September 2018, the Bank performed the fit and proper assessment of both candidates for the Supervisory Board members pursuant to the Banking Act (ZBan-2));
- proposed to the General Meeting of Shareholders to appoint the audit firm Deloitte Revizija d.o.o. as auditors of Abanka's and the Abanka Group's Annual Report for a three-year period (2018–2020) at the 37th General Meeting of Shareholders;
- discussed monthly performance reports of the Bank;
- discussed reports on financial operations of Abanka and the Abanka Group in 2017 and 2018;
- discussed the report of the Compliance Office;
- discussed and decided on the remuneration policy for the Management Board members and other categories of employees whose work is of a specific nature;
- took note of the reports on the implementation of the commitments made to the European Commission and the reports of the Monitoring Trustee;
- took note of the Digital Strategy of Abanka d.d. and the new IT Strategy of the Bank;
- took note of and approved the credit limits;
- took note of the redesigned Risk Appetite Framework;
- approved the revised Risk Management Strategy and Risk Appetite;
- discussed comprehensive risk reports of Abanka and the Abanka Group;
- was briefed on the materials related to the ICAAP and ILAAP;
- took note of and discussed the largest non-performing exposures and approved the Abanka d.d.'s NPL Management Strategy for 2018–2020;
- discussed and approved as well as monitored the activities related to the sale of the NPL portfolio and the spin-off of a portion of NPLs via Ahive, d.o.o.;
- approved the revised Abanka Group Recovery Plan;
- discussed the Annual Internal Audit Report for 2017 and gave its opinion thereto, discussed internal audit reports for 2018, approved the Internal Audit Department Annual Work Plan for 2019 and the Internal Audit Department's framework strategic plan for 2020–2021;
- discussed and approved the action plan following the external quality assessment of the Internal Audit Department;
- approved the Annual Plan of Abanka and the Abanka Group for 2019, including the financial plans up to 2021;
- monitored and oversaw the implementation of IFRS 9 on an ongoing basis;
- monitored and approved the implementation of the requirements/recommendations made by the ECB;
- followed the relevant amendments to the legislation;
- was briefed on the whistleblowing system in Abanka for reporting any breach of the law and internal regulations of the Bank;
- was regularly briefed on the sales process of Abanka d.d.;
- discussed the staffing issues of the management bodies as well as the activities and procedures related to the Supervisory Board's work;
- discussed other issues related to the operations of the Bank and the Group.

Based on materials prepared by the Management Board, reports made by specialised in-house departments and its own findings, the Supervisory Board responsibly monitored the Bank's operations and the work of the Internal Audit Department, also supervising the management of the Bank. In addition, the Supervisory Board required from the Management Board to take appropriate measures and implement activities aimed at improving the performance of the Bank and reducing the risks. The Supervisory Board considers its cooperation with the Management Board good; the Management Board reported on all relevant circumstances in a timely and complete manner, provided answers to the questions received by the Supervisory Board, and duly discharged the duties imposed by the Supervisory Board. The Supervisory Board concluded that its regular and comprehensive monitoring of Abanka's operations, its guidance towards the best possible decisions in a particular situation, coupled with appropriate supervision of the Bank's governance, contributed to safe and stable operations of the Bank and excellent business results.

Annual Report for 2018

The Supervisory Board adopted the Corporate Governance Statement (including the Statement of Compliance with the Corporate Governance Code), which is an integral part of the Annual Report of Abanka for 2018.

At its session held on 16 April 2019, the Supervisory Board discussed the Annual Report of Abanka for 2018, including the audit report by Deloitte Revizija d.o.o. Cooperation with the audit firm was of high quality; the auditors responsible took part in the sessions of the Supervisory Board and the Audit Committee as well as participated in resolving any open issues. The Supervisory Board confirmed that the Annual Report is a true and fair presentation of the Bank's and the Group's position, gives a comprehensive view of operations in 2018 and thus complements the information they received during the financial year. Comparing the Annual Report with the audited financial statements for the 2018 financial year, the Supervisory Board established that the financial results presented in the Annual Report match the audit report. In its opinion, the Supervisory Board, together with the Management Board, fulfilled all their legal requirements for the 2018 financial year.

The Supervisory Board hereby establishes that the certified external auditor, in their report, issued a positive opinion of the financial statements, which present a true and fair view of the Bank's and the Group's financial position in all material aspects. The Supervisory Board has no comments on the audit report by Deloitte Revizija d.o.o. and believes the Bank's and the Group's operations in 2018 were carried out in accordance with the applicable legal requirements. Based on its insights into the Bank's operations during the year and following a careful examination of the audited Annual Report and the positive opinion issued by the certified auditor in their audit report, the Supervisory Board hereby without objections approves and adopts the Annual Report of Abanka for the 2018 financial year.

Marko GARBAJS
Chairman of the Supervisory Board

PRESENTATION OF THE GROUP AND ITS ENVIRONMENT

ABOUT THE BANK

Abanka Vipa d.d. is a bank with a long tradition in the Slovene banking sector. The origins of Abanka date back to 1955, when the bank operated as a branch of the Yugoslav Bank for Foreign Trade. In 1977, the branch was renamed Jugobanka – Temeljna banka Ljubljana. Abanka began using its current name on 1 January 1990, when it was reorganised as a public limited company. On 31 December 2002, Banka Vipa merged with Abanka. Since then, the Bank has operated under the name Abanka Vipa d.d., abbreviated to Abanka d.d. The shares of Abanka were listed on the Ljubljana Stock Exchange from October 2008 to December 2013, when on the basis of the Decision of the Bank of Slovenia on Extraordinary Measures, all qualified liabilities of the Bank on 18 December 2013 ceased in full. On 18 December 2013, the Republic of Slovenia subscribed and fully paid in all 15,000,000 shares newly issued by Abanka, and thereby became the 100% owner of the Bank. On 8 October 2014, the Republic of Slovenia paid in another 100,000 new shares. On 5 October 2015, Banka Celje d.d., established in 1864 when Celje Municipal Savings Bank was founded, was merged with Abanka Vipa d.d. in line with the commitment made to the European Commission. Since that date, the merged bank has operated under the name Abanka d.d. As at 31 December 2018, Abanka's market share in terms of total assets was 9.6%.

Abanka is a universal bank with authorisation to provide all banking and other financial services. Through its extensive network of 53 branch offices across Slovenia, e-banking, advisory services and personal approach, Abanka provides comprehensive financial services ranging from traditional banking to bancassurance services. Moreover, Abanka has gained international reputation. In interbank operations, it uses a network of correspondent banks across the globe to provide quality customer services relating to international payment transactions.

As at the 2018 year-end, the subsidiary Anepremičnine d.o.o. complemented the Bank's offer by providing trading in own real property.

9.6%

Abanka's market share as at the 2018 year-end

SERVICES OF THE BANK

As at 31 December 2018 Abanka was authorised to provide the following mutually recognised financial services under Article 5 of the Banking Act (ZBan-2):

SERVICE	LICENCE ISSUED
1. Acceptance of deposits and other repayable funds;	YES
2. Lending including, inter alia: – consumer loans, – mortgage loans, – factoring, with or without recourse, – financing of commercial transactions (including forfeiting);	 YES YES YES YES
3. Financial leasing (lease) is leasing of assets where all of the material risks and benefits derived from the property right of the leased asset are transferred to the lessee; the transfer of the property right is possible, but not required;	NO
4. Payment services;	YES
5. Issuance and administering of payment instruments (e.g. travellers' cheques and bankers' drafts insofar as this service is not covered by previous point);	YES
6. Issuance of guarantees and other commitments;	YES
7. Trading for own account or for the account of customers in: – money market instruments, – foreign exchange, including currency exchange transactions, – financial futures and options, – exchange and interest-rate instruments, – transferable securities;	YES YES YES YES YES YES
8. Participation in the issuance of securities and services related to such issues;	YES
9. Advice to companies on the capital structure, business strategy and related matters, and advice and services relating to the mergers and acquisitions of companies;	YES
10. Money intermediation on inter-bank markets;	NO
11. Investment management and advice in relation thereto;	YES
12. Safekeeping of securities and other services related to the safekeeping of securities;	YES
13. Credit reference services: collection, analysis and provision of information on creditworthiness;	YES
14. Renting of safe deposit boxes;	YES
15. Investment services and operations and ancillary investment services in accordance with the Financial Instruments Market Act.	YES

Abanka is also authorised to provide the following other financial services under Article 6 of the Banking Act (ZBan-2):

SERVICE	LICENCE ISSUED
1. Insurance brokerage in accordance with the law governing the insurance business;	YES
2. Payment system management services;	NO
3. Pension fund management in accordance with the law governing pension and disability insurance;	NO
4. Custody services in accordance with the law governing investment funds and management companies;	YES
5. Credit brokerage in consumer and other loans;	NO
6. Finance leasing brokerage and administrative services for investment funds.	YES

BANK PROFILE

Abanka is entered in the Companies Register kept by the District Court in Ljubljana under registration no. 1/02828/00.

Registered office:	Slovenska cesta 58, 1517 Ljubljana
Transaction account:	SI56 0100 0000 0500 021
SWIFT:	ABANSI2X
VAT identification number:	SI68297530
Company registration number:	5026024
Share capital:	EUR 151,000,000.00
Telephone:	(+386 1) 47 18 100
Website:	http://www.abanka.si
E-mail:	info@abanka.si
Facebook Abanka:	https://www.facebook.com/abanka.vipa/
Facebook Akeš:	https://www.facebook.com/akes.abanka/
LinkedIn Abanka:	https://www.linkedin.com/company/87740/
YouTube Abanka:	https://www.youtube.com/user/abankavipa
YouTube Akeš:	https://www.youtube.com/user/abankaakes

ABOUT THE GROUP

As at 31 December 2018, in addition to Abanka as the parent company, the Abanka Group included the **subsidiary** Anepremičnine d.o.o. with its **subsidiary** Anekretnine d.o.o. in Montenegro.

Structure as at 31 December 2018.

On 18 July 2017, Abanka d.d. signed an agreement with Banka Sparkasse d.d., Ljubljana to sell its 100% stake in its subsidiary Aleasing d.o.o., Ljubljana. The agreement stipulated that the stake would be transferred to the buyer after the fulfilment of the suspensive conditions, which inter alia included obtaining the relevant approvals of the supervisory authorities. As at the end of March 2018, Abanka d.d. as the seller and Banka Sparkasse d.d. as the buyer of Aleasing d.o.o. confirmed that all suspensive conditions required for the conclusion of the sales procedure were fulfilled. In accordance with the agreement, the stake was transferred to the buyer on 1 April 2018, which became the owner of Aleasing d.o.o., Ljubljana as of that date. As Abanka reversed the investment in equity of the subsidiary Aleasing d.o.o. in the amount of EUR 1,170 thousand, in 2018 the nominal value of Abanka's equity stake in the equity of subsidiaries fell from EUR 9,448 thousand to EUR 8,278 thousand. In 2018, the subsidiary Anepremičnine d.o.o. provided additional capital of EUR 30 thousand to its subsidiary Anekretnine d.o.o. and made an impairment of its investment in the subsidiary Anekretnine d.o.o. of EUR 40 thousand.

The following table shows the activities of the subsidiaries of the Abanka Group, the equity stake and the nominal value of the equity stake as at the reporting date compared to 31 December 2017.

Company	Activity	Equity stake 31 Dec. 2018	Equity stake 31 Dec. 2017	Nominal value of equity stakes as at 31 December 2018 (in EUR thousand)	Nominal value of equity stakes as at 31 December 2017 (in EUR thousand)
The Anepremičnine Group	real property management	100.0%	100.0%	8,278	8,278
Aleasing d.o.o.	leasing	0.0%	100.0%	0	1,170

Activities of Subsidiaries

The Anepremičnine Group

The company Anepremičnine d.o.o., which was entered in the Companies Register on 31 May 2013, was established by assuming a portion of assets from Aleasing d.o.o. to the company Anepremičnine d.o.o. On the day the demerger was entered in the Companies Register, the new company assumed a portion of the assets of the transferring company, Aleasing d.o.o., and as its successor entered all legal relations concerning the demerged assets, previously held by Aleasing d.o.o. Its core business is trading in own real property, with its headquarters in Ljubljana.

The director of the company is Gregor Žvipelj. The composition of the Supervisory Board as at the 2018 year-end was the same as at the 2017 year-end: Davorin Leskovar as its Chairman, Maja Bogdanoski as its Vice Chairman and Dejan Grum as its member.

Anepremičnine performs the full range of real property portfolio management activities, which include conducting the sales procedures, leasing and selling real properties, analysing real property development projects, construction and completion of projects, acquiring new real property portfolio in the market or via spin-offs, selling to third parties, optimising real property management and governance of subsidiaries abroad. It has an efficient real property sales and marketing system and actively participates in the brokerage of real property pledged as collateral to the bank. The company sells its non-residential property at public auctions or through invitations to submit binding or non-binding offers (tendering).

An important segment of the company's activities is the provision of support services, particularly real property appraisal both for the Bank and the Bank's customers, supervision of the eligible use of funds, marketability analysis, real property marketing, asset management for the Bank-owned real property and advisory services.

The company was established with an aim to centralise real property management at the Abanka Group level, to optimise the real property portfolio and to manage it more efficiently. The company's main task is to manage the real property portfolio in a uniform, transparent and predictable manner that will enable value maximisation and adequate profitability. If necessary, it participates in the completion of unfinished projects as an investor.

Anepremičnine is closely involved in the part of the process of real property business of the Abanka Group which relates to commercial transactions. This entails acquisition of real property within the Group, property selling, development, investment, attracting tenants, real property management, divestment and operational marketing of real property. In the reporting year, Anepremičnine developed and either sold or leased many residential and commercial real properties for its own account and made real property valuations for the real properties of the Group.

The operations of the Anepremičnine Group are geographically limited to Slovenia and Montenegro, where in Podgorica in 2014 Anepremičnine d.o.o. founded its subsidiary Anekretnine d.o.o. As at the reporting date, the subsidiary was managed by Director Slobodan Radović and had no Supervisory Board.

Aleasing d.o.o.

Aleasing, financiranje, svetovanje, trženje d.o.o. (short company name: Aleasing d.o.o.) started its operations on 11 February 2000 under the name Eurofin leasing. After Abanka became its majority owner, Eurofin leasing was renamed Aleasing on 1 April 2004. The merger by acquisition of Vogo leasing d.o.o. from Šempeter pri Gorici by Aleasing d.o.o. took place on 1 July 2009. Aleasing, as the acquiring company, entered all legal transactions in which Vogo leasing had been involved as its legal successor, operating on the Slovene market from 1990.

Until 31 March 2018, it was 100% owned by Abanka with its headquarters in Ljubljana and two business units in Celje and Šempeter pri Gorici (in 2012 the headquarters were moved from Celje to Ljubljana). In line with the commitments made to the European Commission, Abanka in 2017 completed the sale of Aleasing. The sales agreement signed with Banka Sparkasse d.d., Ljubljana entered into force on 1 April 2018. As of that date, Aleasing d.o.o. is no longer a member of the Abanka Group.

Until the date of the sale, the company was represented and managed by Director Nikolaj Fišer. The management of the company was supervised by the three-member Supervisory Board in the following composition until 31 March 2018: Davorin Leskovar as its Chairman, Jure Poljšak as its Vice Chairman and Maja Bogdanoski as its member, which was the same composition as at the 2017 year-end.

The leasing products provided by Aleasing d.o.o. complement the range of products and services provided by the Abanka Group. The company operates in a relatively narrow and highly specialised market niche; its main products are financial leasing of movable property and operating leasing of vehicles. Within the framework of its core business, the company was proactive in selling insurance services.

ABANKA'S STRATEGY

In 2018, the strategy guidelines were followed as set out in the medium-term Abanka d.d.'s Strategy for the 2016–2019 Period and the revised Strategy, approved by the Supervisory Board on 20 April 2018. Abanka d.d.'s Business Strategy for the 2018–2020 Period presents the market conditions and opportunities for Abanka, values and financial objectives, and the key projects to achieve them.

Abanka's Mission and Vision

The Abanka's mission is **UNITING WITH EXCELLENCE IN FINANCIAL SERVICES** and is known as **the BANK OF FRIENDLY PEOPLE**. Abanka accomplishes this ***mission*** through its values, core competencies and comparative advantages.

> The Abanka's mission is **UNITING WITH EXCELLENCE IN FINANCIAL SERVICES** and is known as **the BANK OF FRIENDLY PEOPLE**.

Kindness is Abanka's recognisable feature, because it is friendly to the customers for whom its banking services are developed, to the partners with whom its success is built, to the employees and to the environment in which it operates. Abanka performs with **excellence** in all segments, seeks better ways of doing business in general and in day-to-day operations, through service development increases customer satisfaction and contributes to the excellence of the company. The source of Abanka's success is **partnership** as it aims to build long-term relationships with its employees and partners based on respect, care, honesty, trust and cooperation. Abanka is focused on **innovation**, understands technological development guidelines and improves its services and business processes through innovation. Furthermore, Abanka places emphasis on **execution**, which means achieving the set objectives with excellence and in due time.

Key projects to achieve the objectives include:
- employee excellence and customer satisfaction,
- business growth,
- improved efficiency,
- risk management,
- IT and digital transformation.

Key strategic guidelines of the Bank include:
- transformation into a performance-oriented organisation and user experience improvement,
- product range optimisation and digitalisation so as to improve user experience,
- optimisation of the number of employees and labour costs and lower outsourcing costs,
- reduction of non-performing loans and ongoing upgrading of ICAAP and ILAAP and
- improved IT efficiency and digital transformation.

Abanka operates on the Slovene market, which is characterised by extremely fierce banking and non-banking competition. Its ***vision*** guides the Bank to become **THE FIRST BANK IN SLOVENIA ACCORDING TO THE CHOICE OF CUSTOMERS, EMPLOYEES AND INVESTORS.**

> **THE FIRST BANK IN SLOVENIA ACCORDING TO THE CHOICE OF CUSTOMERS, EMPLOYEES AND INVESTORS.**

ABANKA'S FINANCIAL PLAN FOR 2019

The financial plan for 2019 was prepared in autumn 2018 on the basis of the then available macroeconomic forecasts and expectations. The Annual Plan of Abanka and the Abanka Group for 2019, including the financial plans up to 2021, were approved by the Supervisory Board in December 2018.

Abanka's main goals in 2019 will again include retail banking, the SME segment and key customers with significant focus on non-interest income. The Bank will focus on the projects from the strategic programme of accelerating digital transformation, on further upgrading the existing business processes, improving risk management through the improved risk assessment/measurement, monitoring and management process, and upgrading the ICAAP. Moreover, the Bank will create a stimulating environment for its employees by maintaining a good organisational climate, through employee engagement and by promoting Abanka's values, continue to effectively perform the lending activity and cost optimisation as well as increase cross-selling, which will not only enable profitable, safe and stable operations but also enhance the Bank's reputation among investors. In parallel, measures aimed at boosting customer business will be implemented in line with the vision of becoming the first bank in Slovenia according to the choice of customers, employees and investors.

Abanka's main goals in 2019 will again include retail banking, the SME segment and key customers with significant focus on non-interest income.

MAJOR BUSINESS EVENTS IN 2018 AND AFTER THE DATE OF THE STATEMENT OF FINANCIAL POSITION

Major Business Events in 2018

Major business events in 2018 included:

- **Changes to the Supervisory Board:**
  - On 20 April 2018, the Supervisory Board took note of the resignation of the Supervisory Board member Peter Merc, who resigned as a member of the Supervisory Board of Abanka d.d. as of 10 April 2018. He served on the Supervisory Board until 9 July 2018.
  - At the 37th General Meeting of Shareholders held on 17 May 2018, Marko Garbajs was re-appointed a Supervisory Board member, starting his term of office on 5 October 2018.
  - On 22 May 2018, the Supervisory Board took note of the resignation of the Supervisory Board member Bernarda Babič, who resigned as a member of the Supervisory Board of Abanka d.d. as of 5 July 2018.
  - At the 38th General Meeting of Shareholders held on 30 July 2018, the shareholders took note of the resignation of two members of the Supervisory Board, i.e. Peter Merc as of 9 July 2018 and Bernarda Babič as of 5 July 2018. Varja Dolenc was appointed a Supervisory Board member with a four-year term of office commencing on 31 July 2018.
  - At the 39th General Meeting of Shareholders held on 21 September 2018, Miha Košak was appointed a Supervisory Board member with a four-year term of office starting on 22 September 2018.

- **Credit ratings by rating agencies:**
  - On 26 April 2018, the rating agency Fitch Ratings affirmed Abanka's Long-Term Issuer Default Rating of “BB+” with a stable outlook. Furthermore, it affirmed the Bank’s Short-Term Issuer Default Rating at “B”, Viability Rating at “bb+”, Support Rating at “5” and Support Rating Floor at “No Floor”. The Long-Term Issuer Default Rating and Viability Rating are based on the Bank’s strong capital base, high liquidity reserves, a solid structure of sources of funding, and a relatively conservative risk management policy and risk appetite. The good ratings were also affected by the improved economic situation in Slovenia, which was reflected in a high economic growth and further deleveraging of the corporate sector.
  - On 26 October 2018, the rating agency Moody’s Investors Service upgraded Abanka’s Baseline Credit Assessment from “Ba3” to “Ba1”, its Long-Term Issuer Default Rating from “Ba1” to “Baa2” and its Short-Term Issuer Default Rating from “NP” to “P-2” with a stable outlook. By being assigned these ratings, Abanka was again upgraded to investment grade.

- **Activities related to the subsidiaries of the Abanka Group:**
  - On 18 July 2017, Abanka signed an agreement with Banka Sparkasse, Ljubljana to sell its 100% stake in its subsidiary Aleasing, Ljubljana. The agreement stipulated that the stake would be transferred to the buyer after the fulfilment of the suspensive conditions, which inter alia included obtaining the relevant approvals of the supervisory authorities. As at the end of March 2018, Abanka as the seller and Banka Sparkasse as the buyer of Aleasing confirmed that all suspensive conditions required for the conclusion of the sales procedure were fulfilled. In accordance with the agreement, the stake was transferred to the buyer on 1 April 2018, which became the owner of Aleasing, Ljubljana as of that date.

- **Activities relating to the sale of the NPL portfolio:**
  - On 21 March 2018, Abanka and DDM Group, a manager of non-performing loans, signed an agreement on the sale of Abanka’s NPL portfolio, containing diversified NPLs of various companies in Slovenia, Croatia, Bosnia and Herzegovina, and Montenegro.

- **Activities relating to the sale of the Bank:**
  - On 4 July 2018, the Supervisory Board of Slovenski državni holding gave its approval to the contract of mandate for the performance of financial services in the sale of Abanka with the selected financial adviser BNP Paribas from Paris.

- **Transfer of investment and brokerage services to Nova KBM d.d.**
  - In November 2018, Abanka and Nova KBM d.d. signed an agreement on the transfer of brokerage services. The transfer date was 31 December 2018.

- **Establishment of the new company Ahive d.o.o.:**
  - At the 39th General Meeting of Shareholders held on 21 September 2018, the shareholders agreed with the spin-off by formation of the new company Ahive, upravljanje s terjatvami d.o.o., where Abanka d.d. acts as the transferring company. Furthermore, the General Meeting of Shareholders agreed with the Terms of Division of Abanka d.d. to form a new company through the spin-off of a part of assets and their transfer to the new company, which was adopted by the Management Board on 28 May 2018; in accordance with the Terms of Division, a part of assets was transferred to the newly established company Ahive d.o.o. The spin-off was entered into the Companies Register on 22 October 2018. The transfer of the shareholding in Ahive d.o.o. to the buyer DDM Invest I AG took place on 26 October 2018, thereby executing the arrangement entered into by concluding the Receivables Sale Agreement with the said buyer on 21 March 2018.

Major Business Events after the Date of the Statement of Financial Position

The following business events occurred after the reporting period:

- **Activities relating to the sale of the Bank:**
  - In 2019, activities related to the sale of Abanka d.d. continued.

- **Exclusion from membership of the Ljubljana Stock Exchange:**
  - At the request of the stock exchange member ABANKA d.d., Slovenska cesta 58, 1000 Ljubljana, with the ABALJ ticker symbol, the said stock exchange member was excluded from membership of the Ljubljana Stock Exchange as of 1 February 2019.

- **Changes to the Management Board:**
  - On 18 March 2019, the Supervisory Board adopted the agreement on mutually agreed termination of the term of office of Matevž Slapničar, Management Board Member, as of 30 June 2019.

THE ECONOMIC AND BANKING ENVIRONMENT IN 2018 AND OUTLOOK FOR 2019

The Economic Environment in 2018

The relatively favourable trend in global economic activity has continued in 2018. Given the various geopolitical tensions, among which protectionism in world trade (aggravation of relations between the USA and China) was particularly notable, the first signs of a slowdown in economic growth became visible in the second half of 2018. However, euro area forecasters estimated that they would only be temporary. According to the analysts, the dramatic decline in German car production in the third quarter of 2018, for example, was a reflection of the required transition to lighter vehicles. Nevertheless, the prevailing expectations were that China would enter a period of lower economic growth, whereas the trade between the European Union (EU) and the United Kingdom (UK) would remain more or less unaffected by Brexit at least in the medium term. During the summer months, concerns over **global trade**, the gradual normalisation of monetary policies in developed economies and volatility in financial markets led to a tightening of conditions in financing markets, particularly in certain emerging market economies. International financial markets were prudent with regard to investments in countries experiencing macroeconomic imbalances. In 2018, it was Italy that stood out in terms of negative developments. According to ECB staff estimates, the growth rate of global economic activity excluding the euro area reached 3.8 percent in 2018. Meanwhile, external demand for export from the euro area grew by 4.3 percent over 2017. The growth of the global economy also had a positive impact on **euro area** export; particularly since the current real growth in the euro area was also fuelled by intense domestic demand.[1]

The persisting positive trends in the international environment (both in the euro area and globally) in 2018 also had a positive impact on the **Slovene economy**. The value of the PMI indicator (Purchasing Managers Index) dropped to the lowest level over the past four years in December 2018. If euro area forecasters were right in saying that this trend was merely temporary, then the Slovene share of the absorption of global demand for exports from the euro area is sufficient for a continued robust growth of the Slovene economy that will be significantly higher that the euro area average[2]. However, it should also be said that Slovenia has eliminated all macroeconomic imbalances and had laid down a solid foundation for an even more competitive open market economy during the time of the crisis. Geographical diversification and product diversification of exports have therefore continued, even though the Slovene economy definitely is and will remain closely tied to the large European market and monetary system. Ever since the beginning of 2016, the surplus of Slovenian year-on-year GDP growth rate over the Eurozone average has been increasing from quarter to quarter. In the third quarter of 2018, the Slovene economy recorded a year-on-year GDP growth rate (adjusted for seasonal influences) of 5 percent, compared to the average growth rate of 1.6 percent in the euro area.[3]

As a result, the per capita GDP grew at a significantly higher rate than the euro area average (increase by around EUR 1.5 thousand per capita compared to year-end of the preceding year). Consumer confidence is also an increasingly strong driver of higher economic growth through domestic consumption. Higher economic growth has left many companies facing a shortage of skilled workers, whereas LFS unemployment dropped to only 5 percent in the third quarter of 2018. The average wage growth reached 3.4 percent by October and was even one percentage point higher year-on-year, yet the dynamic of real unit labour costs remained below the euro area average, particularly compared to other new member states; however, this did not jeopardise the cost competitiveness of export. Similarly to the previous year (12 percent year-on-year), gross investments also recorded a rapid rise in 2018, particularly investments in non-residential buildings, machinery and transport equipment. Foreign trade also remained a strong driver of economic growth. In terms of the balance of payments, Slovenia was in a strong position throughout the period and is currently even approaching imbalance (balance of payment surplus of over 7 percent). This positive formal imbalance allowed for further deleveraging and restructuring as well as for public finance consolidation through appropriate economic policies, which has all contributed to the reduction of domestic business risk factors. With external factors (prices of energy products) in decline, the inflation rate dropped towards the end of 2018 and remained below the euro area average. In the recent period, inflation has largely been the result of domestic factors that have been driving up prices on the side of demand.[4]

Preliminary estimates of the Statistical Office of the Republic of Slovenia indicate that the GDP in real terms grew by 4.5% in 2018. The value of GDP at current prices was EUR 45,948 million, which in nominal terms accounts for an increase of 6.9% over 2017. Although export growth was lower than in 2017, external demand significantly contributed to economic growth, with exports increasing by 7.2% in 2018. Domestic demand, which plays an increasingly important role, rose by 4.6%, the highest growth after 2007.[5]

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[1] Source: ECB staff macroeconomic projections for the euro area, December 2018. Frankfurt: European Central Bank.
[2] Source: Outlook 2019, December 2018. Ljubljana: Managers' Association of Slovenia.
[3] Source: Euro Area Statistics, https://www.euro-area-statistics.org/macro-economic-indicators?cr=eur&lg=sl.
[4] Source: Economic and Financial Developments, January 2019. Ljubljana: Bank of Slovenia.
Summary of Macroeconomic Developments, January 2019. Ljubljana: Bank of Slovenia.
Economic Mirror No. 1/2019, January 2019. Ljubljana: Institute of Macroeconomic Analysis and Development.
[5] Source: Statistical Office of the Republic of Slovenia, 28 February 2019, http://www.stat.si/StatWeb/News/Index/7966.

MAJOR MACROECONOMIC INDICATORS

	2015	2016	2017	2018
GDP, EUR million (current prices)	38,863	40,357	43,000	45,948*
GDP growth (%)	2.3	3.1	4.9	4.5*
GDP per capita, EUR (current prices)	18,836	19,547	20,815	22,182*
Labour productivity (GDP per employee, %)	1.0	1.1	2.1	1.5**
Unemployment (registered, %)	12.3	11.2	9.5	8.2**
Unemployment (ILO methodology, %)	9.0	8.0	6.6	5.5**
Inflation, year-end (%)	-0.4	0.5	1.7	1.4
Inflation, average (%)	-0.5	-0.1	1.4	1.7

Note: *Estimate of the Statistical Office of the Republic of Slovenia; **IMAD forecast.
Source: Slovenian Economic Mirror, No. 1/2019, January 2019. Ljubljana: Institute of Macroeconomic Analysis and Development, January 2019, and Statistical Office of the Republic of Slovenia (https://www.stat.si/StatWeb/News/Index/7875 and https://www.stat.si/StatWeb/News/Index/7966 and https://pxweb.stat.si/pxweb/Dialog/viewplus.asp?ma=H280S&ti=&path=../Database/Hitre_Repozitorij/&lang=2).

Banking Environment in 2018

The stimulating **monetary policy** in developed economies continued to foster economic growth; in the USA it was replaced by the stimulating **fiscal** policy. There are two other facts that are of relevance in the mid-term:

i) The European Central Bank (hereinafter the ECB) ended its quantitative easing programme at the end of 2018. The Governing Council of the ECB intends to continue reinvesting, in full, the principal payments from maturing securities purchased under the Asset Purchase Programme for an extended period of time past the date when it starts raising the key interest rates.

ii) The ECB left key interest rates unchanged throughout the year 2018 (valid since 16 March 2016): the interest rate on the main refinancing operations at 0.00 percent, the marginal lending facility rate at 0.25 percent and the interest rate on the deposit facility at −0.40 percent. In 2018, the ECB came very close to reaching its monetary policy target of maintaining annual inflation rates below, but close to, 2%. In terms of the structure of the target inflation rate, it was changes in energy prices that accounted for almost half of the inflation.

In view of the potential slowdown of economic growth, both of these monetary policy measures indicate that long-term low interest rates remain the most likely scenario for the future.[6]

In the light of all the above, it was expected that the pressure on cost efficiency and profitability of banks would continue. In 2018, banks invested a lot in new **business strategies and efficient management systems**. The investment activity of companies financed by banks was conducted by different decision-making standards than those applied before the big crisis. Five years after the recovery of the Slovene banking system, international financial markets confirmed their confidence in the restructured Slovene systemic banks by upgrading their credit ratings to investment grade; Abanka d.d. was among these banks even prior to the completion of the privatisation process. Showing capital adequacy and liquidity in line with Basel standards, the restructured banks have also significantly lowered the risk of long-term financing for European financial markets. Operating results show that their ambitious new business strategies and management systems have allowed them to integrate in the highly competitive domestic and foreign business environment. The Slovene banking system also achieved a further significant reduction of the share of non-performing loans in 2018, bringing it down to medium or low-risk level. The share of non-performing exposures (NPE) of banks declined to 4.2 percent or EUR 1.8 billion by November 2018, with the share of non-performing loans (NPL) dropping to 6.0 percent or EUR 1.7 billion.

In the beginning of 2018, banks successfully introduced the new financial reporting standards IFRS 9 which entails a significant upgrade the concept of managing the key risk, i.e. **credit risk**. Banks capitalised strongly on the enhanced standard and increased consumer confidence as well as domestic demand. Adapting their business models and products, they quickly

[6] Source: Monetary Policy Decisions – press release, January 2019. Frankfurt: European Central Bank;
Autumn 2018 Economic Forecast: »sustained but less dynamic growth amid high uncertainty«; November 2018. Brussels: European Commission.

responded to this demand structure. The year-on-year growth in loans to households in November was similar to that in October, amounting to 7.1 percent. The growth rate of consumer loans was 11.7 percent in November, with the year-on-year growth rate of housing loans at 4.7 percent[7], despite the fact that that housing loan growth was in decline due to fast property price increases and insufficient supply. The fact that the growth rate of loans to households is significantly higher than that of loans to non-financial corporations is characteristic of Slovenia in the post-crisis period. The net financial flow of bank loans to households was positive (loans were on the increase) even back in 2014 and kept rising sharply until 2017 (net increase in loans of EUR 643 million).[8] The deceleration of this growth in 2018 was partly the result of macroprudential measures adopted by the regulator initially with regard to housing loans and later also with regard to consumer loans. In terms of structure, long-term loans with a significant fixed-rate component prevailed. The positive net financial flow of bank loans to non-financial corporations was first detected in 2015 and remained at a modest level (net increase in loans of EUR 224 million in 2017). The growth of loans to non-financial corporations remained moderate in November 2018, reaching only 3.1 percent year-on-year.

The quality of the banks' loan portfolio continued to improve. The ratio between existing assets and deposits indicated excess capacity. Deposits of the non-banking sector increased in the low interest rate environment, showing a strong tendency of a growing share of demand deposits. The increase in the share of long-term loans resulted in increased maturity mismatches, but given the high liquidity of banks the risk remained moderate. Initial estimates show that the profitability of banks in 2018 was quite favourable, which was the result of growing interest income, good performance in non-interest activities and the continued releases of impairment and provisions. Capital adequacy was high and corresponded to the latest banking supervision standards, resulting also in low level solvency risk. The domestic economic environment remained stable despite expectations of a slowdown in economic growth, voiced particularly by domestic official institutions. Risk levels were much higher in the vicinity of the Slovene system, where risks were also much more unpredictable.[9]

Outlook for 2019

According to OECD projections, **global** economic activity is expected to remain broadly stable, but weaker than in 2018. In November, the OECD also revised the previous projections (published in May and September) for the year 2018. OECD estimates the global economic growth rate for 2018 at 3.7 percent, which is one percentage point lower than ECB projections. Global economic growth projections for both 2019 and 2020 are the same for both years at 3.5 percent. Economic growth projections for the **euro area** have also been revised slightly downwards to 1.9 and 1.8 percent for 2018 and 2019 respectively. The lower economic growth forecast for the euro area for 2020 remains unchanged at 1.6 percent. The OECD revision also applies to Slovenia’s major trading partners Germany, France and Italy. The most significant downward revision was made for the latter. In general, the OECD observes a slowdown in growth and numerous emerging difficulties or potential risk factors, which is why it has called for closer international cooperation and urged everyone to prepare to do business in much harsher times. The ECB is expected to only reach its key monetary policy goal in the second half of 2020, so the OECD expects potential very minor increases of key interest rates in this period despite the global risks of higher inflation (oil prices, tariffs). The long-term interest rates are to remain at low levels during this period, with the exception of Italy. According to the OECD, the risk of a spillover of country risk from Italy is manageable. Forecasts for Slovenia predict a growth rate of 4.4 percent (2018) and 3.6 percent (2019), followed by 2.7 percent in 2020, which is relatively low compared to the high post-crisis growth rates so far. In terms of the relative openness of its economy (volume of export and imports as a share of total GDP), **Slovenia** remains visible on the global map of OECD analysts. According to OECD estimates, the relative connectivity of the German and Chinese economies in global terms is such that a decrease of two percentage points in Chinese demand would result in a 0.15 point decrease in the German GDP. Slovenia of course also exports directly to the USA and China, but estimates of the Bank of Slovenia nevertheless predict that the impact of high tariffs in the car and steel industries would be relatively painless for the economy overall.[10]

According to forecasts of the domestic official institutions - the Institute of Macroeconomic Analysis and Development and the Bank of Slovenia - the broad-based economic growth of **Slovenia** will continue in 2019 and 2020, hovering between 4% and 3%. The slight slowdown in economic growth in 2019 will be the result of lower contributions of foreign trade and investments, however private and government consumption will have the opposite effect. At the same time, economic growth will also be affected by the gradual increase in labour costs, so no further improvements of export competitiveness are to be expected in the coming years. In addition to the agreed significant salary increase in the public sector, labour cost growth will also be affected by the inadequate quality and shortage of skilled workers on the supply side of the labour market. Nevertheless, investment activity will be ample in all segments, both in construction (housing and infrastructure investments) as well as in investments in

[7] Source: Monthly Information on Bank Operations, January 2019. Ljubljana: Bank of Slovenia.
[8] Source: Financial Accounts Statistics, own calculations, December 2018. Ljubljana: Bank of Slovenia.
[9] Source: Financial Stability Report, December 2018. Ljubljana: Bank of Slovenia.
EBA Risk Dashboard Q3-2018, december 2018. EBA, https://eba.europa.eu/risk-analysis-and-data/risk-dashboard.
[10] Source: OECD Economic Outlook, November 2018, http://www.oecd.org/eco/outlook/economic-outlook/;
Autumn 2018 Economic Forecast: »sustained but less dynamic growth amid high uncertainty«; November 2018. Brussels: European Commission.

machinery and equipment. Investments will be driven particularly by the high production capacity utilisation and the expected good business performance. IMAD estimates that the inflation rate in Slovenia will exceed 2 percent by 2020, mainly due to surging oil prices and the gradual increase in prices of services. Given the continued growth in demand and increasing cost pressures (labour, raw materials, services), the gradual rise of the inflation rate is expected to continue in the coming years. Slovenia is expected to maintain a significant, albeit slightly lower surplus in the current account balance of payments as a result of the trade balance surplus (goods, services) and the primary and secondary income deficit (7 to 6 percent of GDP). Given the expected continued relatively favourable growth of foreign demand, the Slovene economy will maintain a solid export growth rate in 2019 and 2020.[11]

Further growth of the lending activity of banks and the availability of favourable financing sources in conjunction with high levels of own funds will allow banks to continue providing loans for financing the investment cycle of companies. If the favourable macroeconomic forecasts materialise and the low or slightly increased interest rates persist, the strengthening demand for loans can be expected to continue. As releases of provisions are phased out, banks will presumably record slightly lower profit than in previous years. The development of credit risk indicators is expected to gradually turn towards higher risk.[12]

Risks that might jeopardise this outlook mainly arise from the external environment, the most prominent being the interrelated geopolitical risks and the escalation of protectionist measures. The stability of the Slovene legal and economic environment and the willingness to take on new challenges in the highly competitive international environment call for a new development strategy including a tax reform, solutions for the ageing population, halting brain drain, investing in a more extensive and affordable supply of housing as well as a shift towards generating higher added value. Domestic risks that might affect the outlook therefore primarily include the necessary structural reforms and the stronger consolidation of public finance that is absolutely essential at this point in time (after the successfully completed implementation of economic policies during the financial crisis).

[11] Source: Autumn Forecast of Economic Trends 2018, September 2018, Ljubljana: IMAD.
Forecast of macroeconomic trends in Slovenia, December 2018. Ljubljana: Bank of Slovenia.
[12] Source: Financial Stability Report, December 2018. Ljubljana: Bank of Slovenia.

FINANCIAL RESULTS OF THE GROUP AND THE BANK

In addition to Abanka as the parent bank, the consolidated financial statements of the Abanka Group for 2018 include the subsidiaries Aleasing (included profit or loss for the year until 31 March 2018) and the Anepremičnine Group.

The consolidated financial statements of the Abanka Group for 2017 include the subsidiaries Aleasing and the Anepremičnine Group, alongside Abanka as the parent bank.

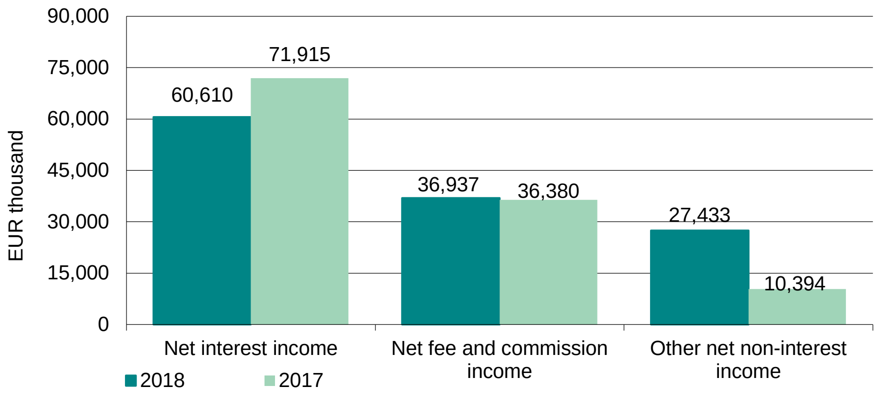
The effects of the transition to IFRS 9 are presented in detail in Note 44 of the Financial Report of the Annual Report, while only some effects compared with the 2017 year-end are presented in the Business Report. Due to the changes in accounting policies regarding the calculation of the tax on financial services, the comparative data in the income statement for 2017 were changed; see Note 1.25. of the Financial Report for further details.

Due to the immateriality of subsidiaries only data for Abanka are presented in the figures.

PERFORMANCE AS VIEWED THROUGH THE INCOME STATEMENT

In the persisting extremely low interest rate and highly competitive environment characterised by high liquidity, Abanka not only continued with its restructuring and implementing the strategic objectives but also focused on acceleration of the digital transformation, further upgrade of business processes and cost rationalisation, while achieving excellent business results.

GROSS INCOME OF ABANKA IN 2018 COMPARED TO 2017 (amounts in EUR thousand)



In the reporting year, t**he Abanka Group** recorded **net interest income** of EUR 61,075 thousand, down by 16.8% on the previous year. **Abanka's net interest income** amounted to EUR 60,610 thousand, interest income decreased by 14.4%, while interest expenses were down by 0.2%. Lower net interest income primarily resulted from lower interest income, specifically due to lower average realised interest rates on loans to non-bank customers and investments in debt securities (maturity of the DUTB bond). In the reporting year, Abanka's market share of net interest was 9.0% (vs. 11.1% in 2017), whilst interest margin was 1.64% (vs. 1.98% in 2017).

Net fee and commission income of the Abanka Group totalled EUR 36,869 thousand, up by 1.5% compared to the year before, whilst those of **Abanka** amounted to EUR 36,937 thousand. The bulk of net fee and commission income was generated by payment transactions and card operations.

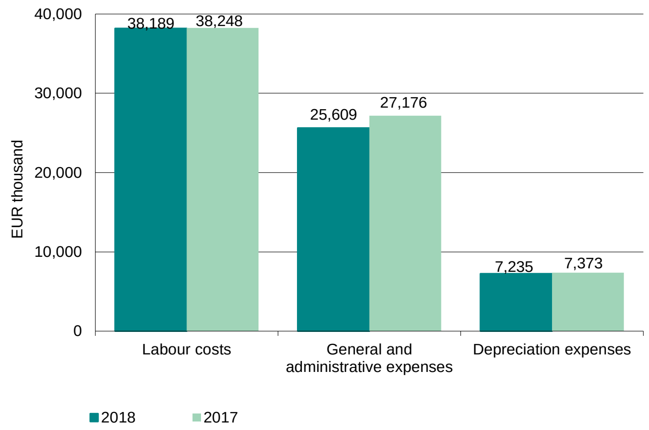
11.7%

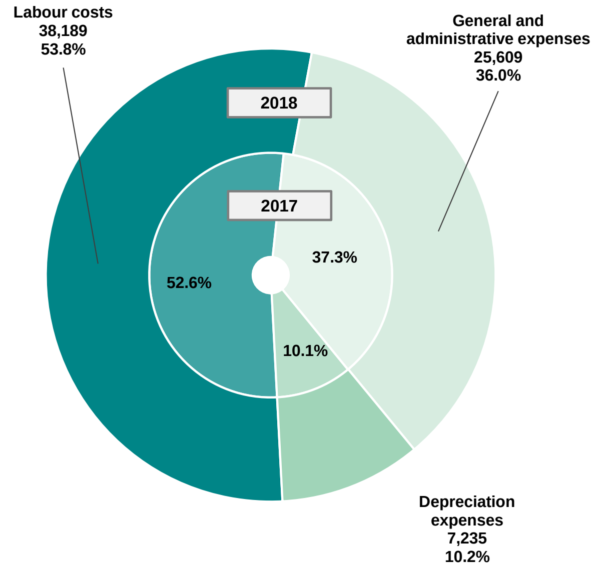
market share of Abanka in net fee and commission income in 2018 (in 2017: 11.7%)

Other net non-interest income (excluding net fee and commission income) of the Abanka Group in the reporting year amounted to EUR 27,256 thousand (vs. EUR 10,680 thousand in 2017), whereas those of **Abanka** equalled EUR 27,433 thousand, up by 63.9% compared to the year before. The increase in net other non-interest income in 2018 was primarily a result of the gains on the sale of non-performing loans.

In the reporting year, **the Abanka Group's operating expenses** amounted to EUR 73,047 thousand, down by 4.1% on the previous year. **Abanka's** operating expenses reached EUR 71,033 thousand in 2018. By streamlining costs and cutting the number of employees, the Bank managed to increase its cost-effectiveness, thereby reducing its costs by 2.4% or EUR 1,764 thousand compared to 2017. Excluding the restructuring costs, operating expenses were lower than in 2017 by 1.7% or EUR 1,201 thousand and totalled EUR 69,784 thousand.

OPERATING EXPENSES OF ABANKA IN 2018 COMPARED TO 2017 (amounts in EUR thousand)

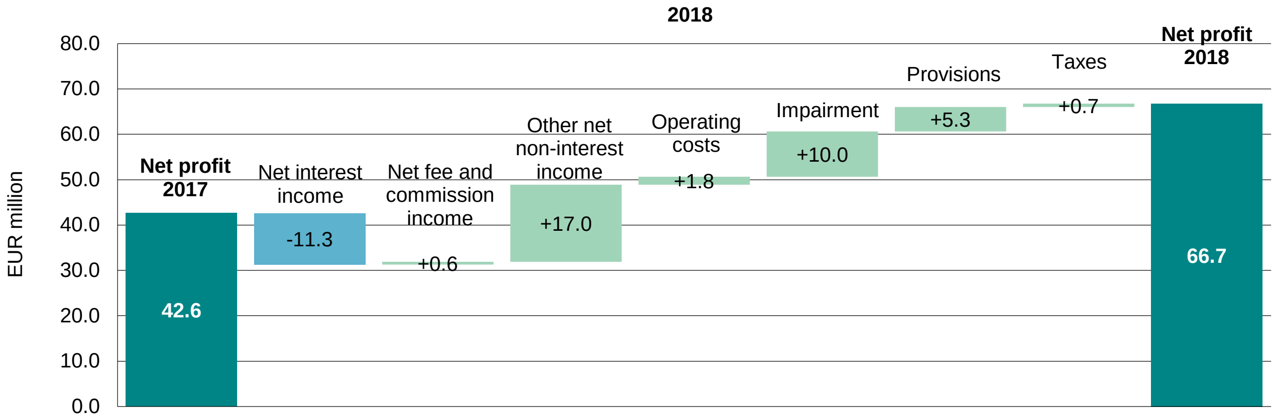




In the reporting period, the **Abanka Group cancelled net impairment and provisions** of EUR 17,928 thousand, of which **provisions were formed** in the amount of EUR 78 thousand and **impairment were cancelled** in the amount of EUR 18,006 thousand. **Abanka's net impairments and provisions cancelled** amounted to EUR 17,265 thousand (vs. EUR 1,943 thousand in 2017). In the reporting period, the Bank cancelled impairments for loans to non-bank customers of EUR 18,104 thousand and made impairments for loans to banks of EUR 19 thousand, for debt securities in the amount of EUR 251 thousand, for property, plant and equipment in the amount of EUR 283 thousand and for other financials assets in the amount of EUR 210 thousand. The Bank formed provisions for pending legal proceedings in the amount of EUR 4,460 thousand and for emlpyee benefits in the amount of EUR 32 thousand, whilst cancelling provisions in the amount of EUR 4,416 thousand for off-balance sheet liabilities. In relation to the item "gains on loans", the Bank made other provisions of EUR 4,678 thousand for certain guarantees given to the buyer of the sold NPLs.

The Abanka Group generated **profit before tax** of EUR 70,081 thousand**,** whilst **consolidated profit after tax** equalled EUR 65,592 thousand. **Abanka** alone reported EUR 71,212 thousand in **profit before tax** and a return on equity of 12.5%. In 2018, **Abanka** posted a **profit after tax** in the amount of EUR 66,737 thousand, taking into account the **corporate income tax** of EUR 4,475 thousand, which is EUR 24,117 more compared to the corresponding period of 2017 due to the abovementioned reasons. In the reporting period, **return on equity after tax** was 11.7%.

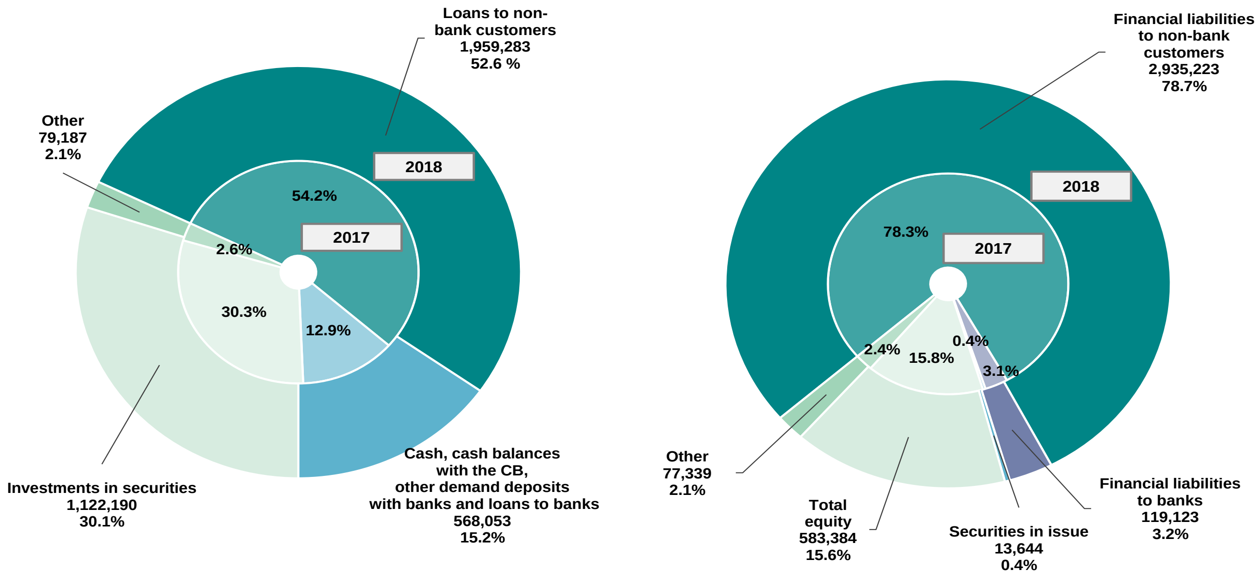
IMPACT OF INDIVIDUAL CATEGORIES OF THE INCOME STATEMENT ON THE PROFIT OF ABANKA IN 2018 COMPARED TO 2017 (amounts in EUR million)



PERFORMANCE AS VIEWED THROUGH THE STATEMENT OF FINANCIAL POSITION

Consolidated total assets as at 31 December 2018 amounted to EUR 3,731,542 thousand, up by 2.1% over the preceding year. The total assets of subsidiaries amounted to EUR 21,998 thousand (vs. EUR 64,931 thousand as at 31 December 2017) and accounted for 0.6% of consolidated total assets (vs. 1.8% as at 31 December 2017). After the elimination of inter-company transactions, the consolidated total assets of the Abanka Group were higher by EUR 2,829 thousand nominally compared to Abanka's total assets. **Total assets of Abanka** as at the reporting date amounted to EUR 3,728,713 thousand, which was 2.0% above the figure posted as at the 2017 year-end.

ASSETS AND LIABILITIES OF ABANKA AS AT 31 DECEMBER 2018 AND 31 DECEMBER 2017 (amounts in EUR thousand)

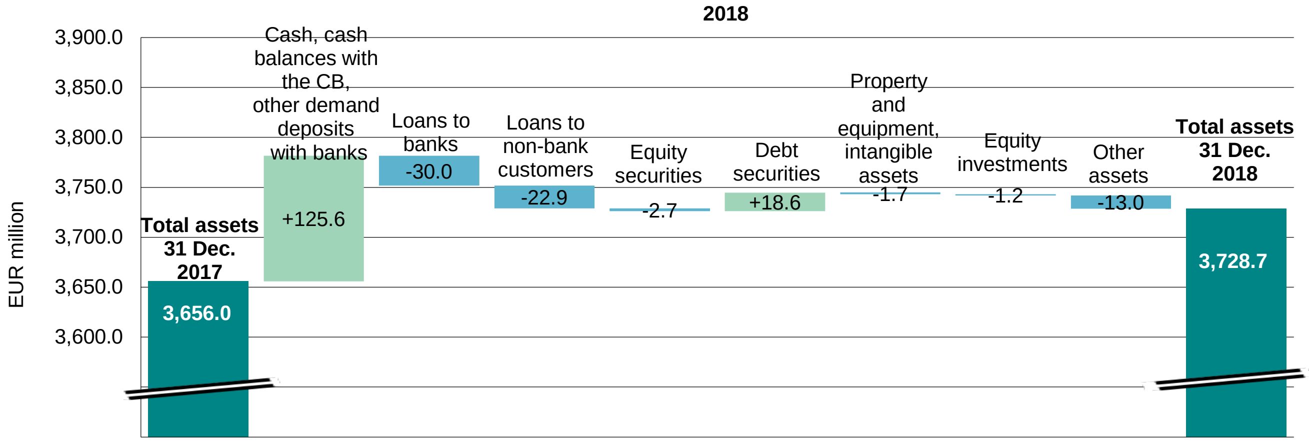


In **consolidated balance sheet assets, loans to non-bank customers** amounted to EUR 1,952,759 thousand as at the 2018 year-end and accounted for 52.3% of total assets, down by 0.7% compared with the 2017 year-end. As at the 2018 year-end, **loans to non-bank customers of Abanka** stood at EUR 1,959,283 thousand and were 1.2% or EUR 22,854 thousand lower than as at the 2017 year-end. Their share in total balance sheet assets decreased from 54.2% to 52.5%. The bulk of the decrease was a result of the NPL sale in 2018 and the impact of the transition to the new accounting standard IFRS 9 as of 1 January 2018. In total loans to the non-banking sector, retail loans accounted for the bulk with 46.2% (vs. 42.9% as at the 2017 year-end), followed by loans to large companies with 22.7% (vs. 24.6% as at the 2017 year-end) and loans to SMEs with 17.4% (vs. 16.3% as at the 2017 year-end).

Cash, cash balances with the central bank and other demand deposits with banks of the Abanka Group as at the reporting date amounted to EUR 538,234 thousand and in Abanka to EUR 537,269 thousand. **Loans to banks of the Abanka Group** and/or of **Abanka** equalled EUR 30,784 thousand. The increase in cash, cash balances with the central bank and other demand deposits as at the 2018 year-end compared with the 2017 year-end by 30.6% in the Group and by 30.5% in the Bank is primarily a result of excess liquidity in the system.

As at the reporting date, the **Abanka Group's investments in securities** amounted to EUR 1,122,190 thousand and equalled **those of Abanka**, as the subsidiary did not disclose securities operations in its balance sheets. Compared to the 2017 year-end, total investments in securities increased by 1.4% or EUR 15,875 thousand in nominal terms. As at 31 December 2018, the equities portfolio of Abanka was worth EUR 43,463 thousand, down by 5.9%, of which EUR 24,717 thousand was accounted for by the Bank Resolution Fund. The debt securities portfolio of Abanka as at the end of the reporting year totalled EUR 1,078,727 thousand and accounted for 96.1% of total securities held by the Bank. Due to the impact of the transition to IFRS 9, debt securities declined by EUR 26,892 thousand, which means an increase of EUR 45,490 thousand in 2018.

CHANGES IN ASSETS OF THE STATEMENT OF FINANCIAL POSITION OF ABANKA AS AT 31 DEC. 2018 COMPARED TO 31 DEC. 2017 (amounts in EUR million)



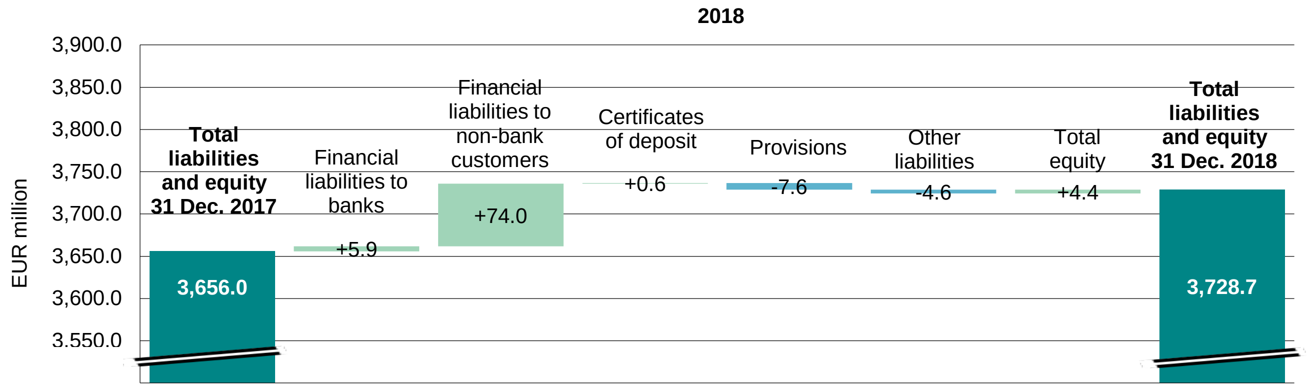
As at 31 December 2018, **consolidated balance sheet liabilities** were composed of EUR 3,148,135 thousand of total liabilities and EUR 583,407 thousand of total equity. Abanka's **balance sheet liabilities** were composed of EUR 3,145,329 thousand of total liabilities and EUR 583,384 thousand of total equity. See Section Total equity and ownership structure for more details.

The Abanka Group's deposits from non-bank customers accounted for the bulk of the Group's total liabilities and reached EUR 2,934,448 thousand as at the reporting date. Together with **loans from customers** of EUR 5 thousand they amounted to EUR 2,934,453 thousand as at the 2018 year-end. Compared with the 2017 year-end, deposits from non-bank customers grew by 2.8% or EUR 78,904 thousand nominally. As at the reporting date**, deposits from non-bank customers in Abanka** amounted to EUR 2,935,218 thousand. Together with **loans from customers** of EUR 5 thousand they reached EUR 2,935,223 thousand. Compared with the 2017 year-end, deposits from non-bank customers grew by 2.6% or EUR 74,521 thousand nominally. They accounted for 78.7% of total liabilities.

The Abanka Group's financial liabilities to banks amounted to EUR 119,123 thousand as at the 2018 year-end and equalled **those of Abanka**. Compared with 31 December 2017, they increased by 5.2%. As at the 2018 year-end, there were no financial liabilities to the central bank. Higher financial liabilities to banks resulted from lower deposits from banks by 32.6%, whilst loans from banks were up by 15.5% over the 2017 year-end.

Securities in issue of the Abanka Group equalled **those of Abanka.** As at the reporting date, they amounted to EUR 13,644 thousand, having increased by 4.8% compared to the year before. As at the reporting date, certificates of deposit equalled securities in issue.

CHANGES IN LIABILITIES OF THE STATEMENT OF FINANCIAL POSITION OF ABANKA AS AT 31 DEC. 2018 COMPARED TO 31 DEC. 2017 (amounts in EUR million)



PERFORMANCE OF THE GROUP IN 2018

Corporate Banking

In 2018, the corporate banking segment was affected by extremely low interest rates and a slight fall in corporate lending in Slovenia. The reasons for the latter primarily lie in extremely high liquidity levels in the economy, which is undoubtedly a result of the measures taken by the European Central Bank. Consequently, the levels at which banks charge transaction account balance fees to legal entities further declined. As in 2017, interest rates continued to fall in 2018, with debit interest rates declining quicker than credit interest rates. Consequently, net interest margin also decreased.

In the reporting year, a strong demand for investment loans and loans for financing working capital was seen. In addition, demand for refinancing the existing loans was observed, which caused a price pressure on the existing portfolio of the Bank. An important factor in refinancing is the fact that many companies successfully completed their restructuring, thus significantly improving their credit rating.

As a result of the favourable economic environment, exporters in particular increased sale on their target markets. Investments in the economy were focused on expanding the existing production capacities as well as on new areas of business. Good news is the fact that an increased investment cycle was seen in companies operating in the domestic environment. This mainly concerns the companies that had thus far shown restraint in expanding their existing capacities, but then it became a necessity for their business. Investments in new hardware and real property necessary for the smooth running of the production process were recorded. It is very important that a wide range of different sources of funding was available in the Slovene banking market. Funding of small and medium-sized enterprises was often provided in cooperation with the Slovene Enterprise Fund and the SID bank. Furthermore, companies increasingly used different forms of interest rate hedging.

The SME segment continues to remain the strategic segment of the Bank. However, the activities of the Bank will continue to focus also on the large corporates segment. To this end, the Bank adjusted its activities and objectives by taking into account its strategy. Additional staff were recruited to ensure quality monitoring of the customer portfolio and to further strengthen the individual approach to finding a solution. Great care is taken to ensure ongoing professional training so as to provide top-quality services. An important emphasis was devoted to retaining the existing customers, integrated customer management and upgrading mutual cooperation by increasing the number of banking products per customer. The Bank was very active in attracting new customers, mostly those who are interested in the whole range of banking products and services. In this regard, the Bank pursued the strategic guideline to establish or increase cooperation with the customers having a good credit rating, which resulted in a further improved credit portfolio.

The range of services provided to the micro-segment customers is available in major branch offices in all main branches, thus enabling customers easy access to financial services across Slovenia. Commercial activities were strengthened through cooperation with various funds and strategic partners, such as the chambers of craft and small business and the chambers of commerce and industry, the Slovene Enterprise Fund, regional agencies for development promotion and municipalities, which are aimed at promoting and facilitating the development of small businesses. Through an active and constant presence on the market, the Bank was continuously promoted, sought and exploited market opportunities, maintained good business relationships with existing micro-enterprises and entrepreneurs, as well as acquired new customers.

As in previous years, trade finance represented an important complementary service in financing and/or monitoring and execution of domestic and international commercial transactions. Backed by past positive customer experiences with regard to the importance of trade finance instruments, which provide additional protection and contribute to the successful execution of transactions, an upward trend in demand for these products has been observed for several years.

A significant factor contributing to the increase in the volume of trade finance transactions from year to year and customers choosing Abanka as an excellent partner in their execution is having a comprehensive range of all trade finance products, professional execution of transactions, providing advice and support to customers in selecting an appropriate instrument, as well as continuous service development focused on digitalisation. Taking an individual approach and adjusting the products or execution of transactions to the customer's specific needs are of particular importance. Abanka's many years of experience, including customers' experience, have been effectively exchanged at professional meetings for several years, which resulted in establishing long-term cooperation or strengthening partnerships with both the existing and new trade finance customers.

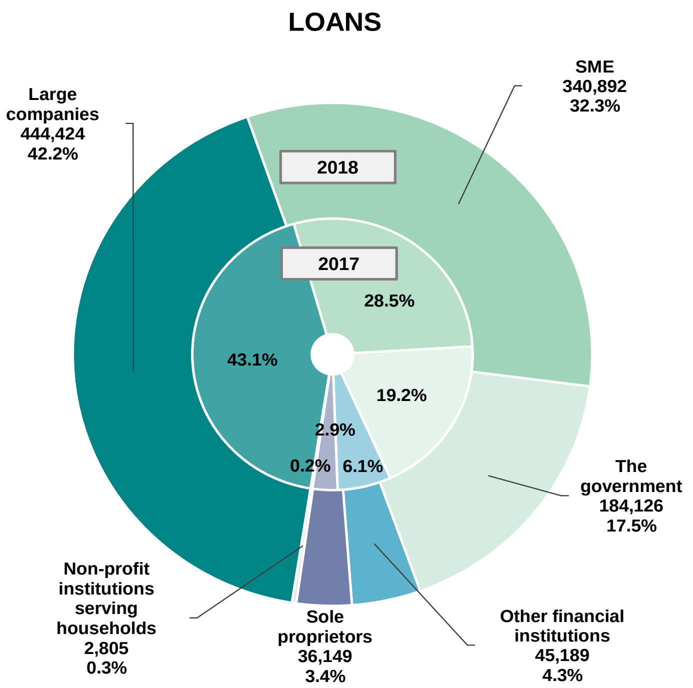
In 2018, special attention was on the development and marketing of digital solutions. The modern solutions Abanet com and Abamobi com are used by an increasing number of customers. Customers using trade finance transactions for conducting business with import letters of credit exchange data via the Abanet com online bank. In addition to the growing number of cashless transactions, the use of business cards is on the rise. In relation to the latter, increasingly more customers use the Bank's security measures, particularly the SMS notification service – Abasms. The upward trend in these products and services is expected to further increase due to the implementation of the PSD2 and instant payments. In 2018, the Abadenarnica mobile wallet was launched, which enables customers to make payments also with business cards.

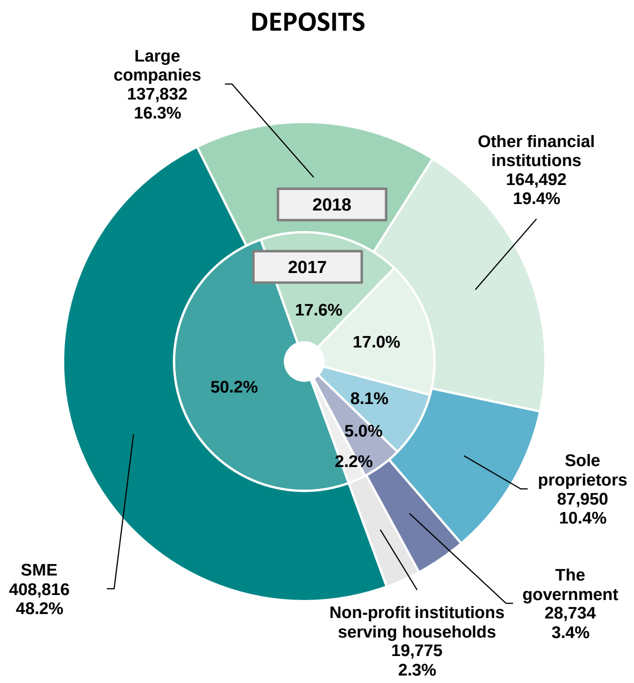
In 2018, special attention was on the development and marketing of digital solutions. The modern solutions Abanet com and Abamobi com are used by an increasing number of customers.

In order to improve user experience and focus on quality cooperation, the level of service quality will be further improved by taking into account customers' wishes and expectations with regard to both the existing and new products. Targeted campaigns are directed at increasing the volume of payment transactions, the number of points of sale equipped with Abanka's POS terminals, the number of issued business cards and the number of users of Abasms com and Abamobi com mobile services.

Customers can already see the importance of new technologies and digitalisation in their day-to-day business with the Bank. In Abanka's innovative Abasvet branch office, customers can experience the digital world in a unique and interesting manner.

LOANS AND DEPOSITS OF ABANKA BY SEGMENT AS AT 31 DECEMBER 2018 AND 31 DECEMBER 2017 (amounts in EUR thousand)





As at the 2018 year-end, **loans to corporate customers and sole proprietors of the Abanka Group** amounted to EUR 1,047,020 thousand, down by 4.6% compared with the 2017 year-end. **As at the reporting date, Abanka's loans to corporate customers and sole proprietors** reached EUR 1,053,585 thousand, having decreased by EUR 78,978 thousand or 7.0% since the end of the previous year. Approximately a quarter of the decrease was a result of the NPL sale in 2018 and the impact of the transition to the new accounting standard IFRS 9 as of 1 January 2018.

8.3%

market share of Abanka in loans to corporate customers as at the end of 2018
(as at the end of 2017: 9.0%)

Deposits from and loans from corporate customers and sole proprietors in Abanka amounted to EUR 847,605 thousand as at the 2018 year-end, down by 3.6% or EUR 31,967 thousand compared with the 2017 year-end; deposits decreased by EUR 31,472 thousand to EUR 847,600 thousand, while loans from customers were down by EUR 495 thousand to EUR 5 thousand.

8.3%

market share of Abanka in deposits from corporate customers as at the end of 2018 (as at the end of 2017: 8.9%)

Retail Banking

In addition to the sound performance of the retail banking segment in the reporting period, Abanka continued to pursue the set goals, exceeded the planned business objectives, and increased its market share.

Customers are offered a wide range of products, therefore many activities were directed towards employee training because the Bank is aware of the importance of having the relevant expertise and skills required by the complexity of individual products and processes. Adequately qualified bank employees contribute to process optimisation, a shorter time needed for the sale of services and greater customer satisfaction.

With the goal of establishing long-term cooperation with customers, in 2018 key activities were aimed at building and maintaining good customer relationships through a comprehensive range of banking products, cross-selling, expert advice, a personal customer approach (personal and private banking) and expert assistance of the Contact Centre. Moreover, branch offices were transformed into sales-/advice-oriented branch offices with a high added value.

Abanka provides a comprehensive range of financial services in one place. As a broker in the insurance market, it has provided insurance services since November 2003. In cooperation with the Triglav Group, it offers bancassurance products and investment funds.

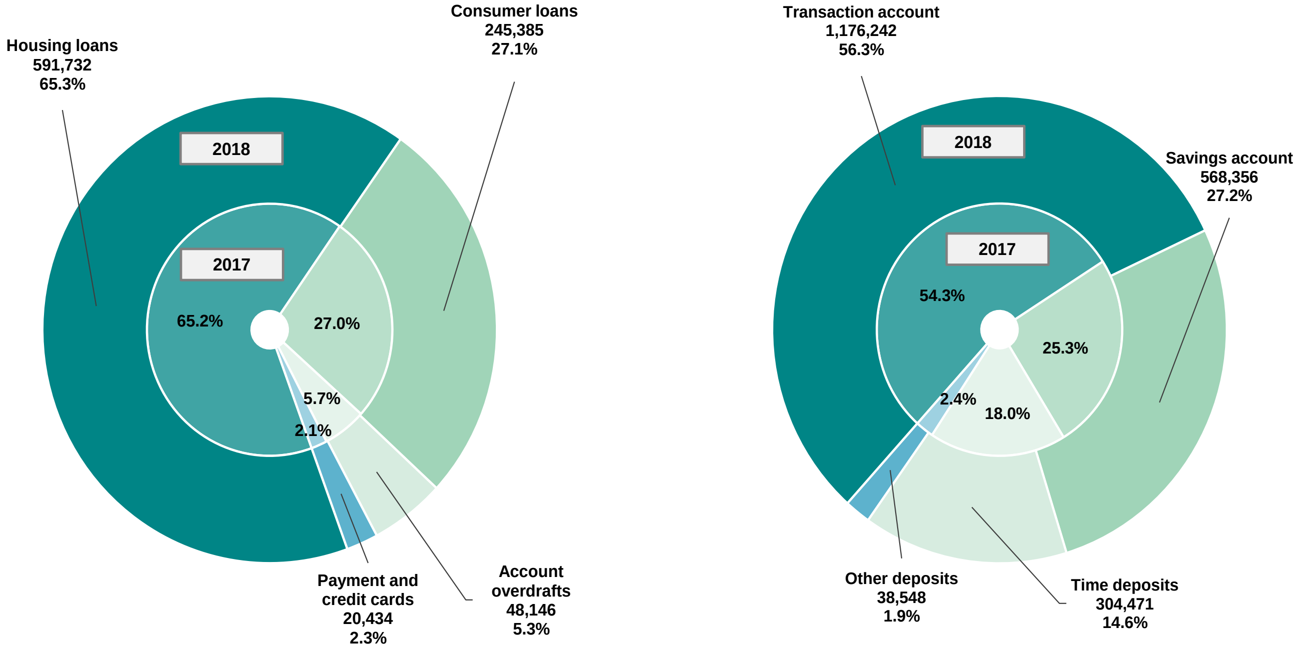
In the age of digitalisation, modern electronic and mobile products are designed; thereby effectively pursuing the business objective of the Bank to attract as many new customers with a personal account as possible. With the aim of increasing effectiveness, various different promotional channels are used to achieve greater visibility of services among potential customers. The Bank achieved good sales results, especially in the selling of Abamobi mobile bank application and the Visa Electron instalment card.

In the age of digitalisation, modern electronic and mobile products are designed; thereby effectively pursuing the business objective of the Bank to attract as many new customers with a personal account as possible.

Abanka has an extensive branch network in Slovenia; in 2018 due to the concentration of branch offices, the Ljubljanska Celje Branch Office and the Šempeter Celje Branch Office in the Celje region were closed; apart from that the Prevalje Branch Office and the Pražakova Branch Office in Ljubljana were closed. In the Central Slovenia Main Branch Office, the unique branch office Abasvet is a good example of showing the transformation from a traditional branch office into the bank of the future and keeping up with digitalisation.

Together with other business lines, retail banking strives to improve and optimise procedures and processes, which also has a positive impact on the customers, especially by ensuring a quick response and providing quality services.

RETAIL LOANS AND DEPOSITS OF ABANKA AS AT 31 DECEMBER 2018 AND 31 DECEMBER 2017 (amounts in EUR thousand)



Loans to retail customers in the Abanka Group went up by 4.2% compared with the 2017 year-end and amounted to EUR 905,739 thousand as at the 2018 year-end. **Abanka's loans to retail customers** amounted to EUR 905,698 thousand as at the 2018 year-end. Compared with 31 December 2017, they rose by 6.6% or EUR 56,124 thousand in nominal terms.

9.5%

market share of Abanka's loans to retail customers as at the end of 2018 (as at the end of 2017: 9.5%)

As at the reporting date, **Abanka's deposits from retail customers** totalled EUR 2,087,618 thousand. Compared with the 2017 year-end, they increased by 5.3% or EUR 105,993 thousand in nominal terms.

11.4%

market share of Abanka in deposits from retail customers at the 2017 year-end (as at the end of 2017: 11.5%)

Operations with Other Banks and Securities

Cash, cash balances with the central bank and other demand deposits with banks and loans to banks of the Abanka Group totalled EUR 569,018 thousand as at 31 December 2018. **Cash, cash balances with the central bank and other demand deposits with banks and loans to banks of Abanka** as at the reporting date amounted to EUR 568,053 thousand, up by 20.2% compared to the 2017 year-end.

The Abanka Group's financial liabilities to banks amounted to EUR 119,123 thousand as at the reporting date and equalled **those of Abanka.** Compared to the 2017 year-end, financial liabilities were higher by 5.2%.

The management of the debt securities portfolio included in the trading and banking books demanded the Bank to continue to apply a conservative and prudent investment policy, i.e. investing in highly liquid and high investment grade securities. The banking book portfolio was managed in accordance with the business and financial plan for 2018 as well as the liquidity situation. As at the reporting date, the value of debt securities held in the banking book was higher than originally planned for 2018, primarily as a result of additional investing of excess liquidity in securities.

As at the 2018 year-end, the value of **the Abanka Group's investments in securities** was at the same level as **those of Abanka**. Compared to the 2017 year-end, they increased by 1.4% to EUR 1,122,190 thousand. The securities portfolio included both equity and debt securities.

As at the reporting date, **securities in issue of the Abanka Group** equalled those of **Abanka**. As at the reporting date, they amounted to EUR 13,644 thousand, having increased by 4.8% compared to the year before.

Abanka remains an important primary dealer in Slovene government bond issues and participates as a market maker in MTS Slovenija as an official liquidity provider. Through different activities, it has been steadily increasing the trading volume on the primary and secondary markets of Slovene government bonds, thus becoming an important player in both the local and the international market. In the most recent international issues of government bonds and the domestic issues of RS treasury bills, Abanka played an active role as a co-lead manager and achieved a high market share in the local market. Together with other renowned foreign banking groups, Abanka was selected as a co-lead manager in charge of increasing the issue of 10-year, 17-year and 27-year bonds in the total amount of EUR 1.25 billion. In cooperation with other banks from the syndicate, the issuance was successful on both the international and the local market. This is confirmed by the fact that Abanka is recognised by domestic and foreign institutional investors as an important partner in ensuring the liquidity of the Slovene government securities.

Payment transactions

As regards domestic and cross-border payment transactions in 2018, Abanka processed 18.3 million orders through the Target payment systems and the small-value payment system (SIMP) in the total value of EUR 22,534.6 million. In terms of the number of orders, domestic and cross-border payments increased by 6.3% compared to 2017, while in terms of value they rose by 1.2%. Apart from that, the Bank internally processed 9.3 million credit payment transactions worth EUR 11,071.3 million. In the domestic payment system, the Bank increased its market share in the forwarding of payment orders to 16.4%.

Abanka is an important operator in the direct debit scheme (SEPA DD). In 2018, Abanka processed 7.0 million external direct debit transactions and 1.7 million internal direct debit transactions in the total amount of EUR 351.8 million through this payment system. The Bank's external direct debit transactions accounted for a 23.5% market share.

Card and ATM Operations

By 31 December 2018, 470,919 cards were issued, i.e. 3.4% more than as at the 2017 year-end. The bulk was accounted for by BA Maestro (59.3%), which functions as a personal account card. In the reporting period, 33.3 million transactions were recorded with the cards issued by Abanka, up by 10.3% compared to the previous year. These nominally amounted to EUR 1,607.6 million and were 7.6% above the level reported for 2017.

Abanka has an extensive network of points of sale for all types of card products, which enable transactions via Abanka-held POS terminals or through terminals of other banks. On the basis of vendor agreements, 33 million transactions with all types of cards were recorded in 2018, up by 13.4% compared to 2017. These nominally amounted to EUR 1,362.9 million and exceeded the 2017 figure by 11.5%.

Abanka has an extensive network of points of sale for all types of card products, which enable transactions via Abanka-held POS terminals or through terminals of other banks.

As at the reporting date, Abanka operated 259 ATMs. By reducing the number of bank-owned ATMs by 19 and holding a 16.4% market share, Abanka's ATM network is the third largest. Abanka's ATMs processed 9.2 million transactions of cash withdrawal worth EUR 1,009.8 million.

259

ATMs owned by Abanka as at the end of 2018

Investment Brokerage and Precious Metals

The total volume of trading generated by members of the Ljubljana Stock Exchange in 2018 was EUR 674,644 thousand. Abanka contributed EUR 24,262 thousand to total trading, thereby achieving a 3.6% market share and ranking 9th among stock exchange members. Total trading of Abanka in foreign markets amounted to EUR 12,631 thousand.

Pursuant to Article 159 of the Market in Financial Instruments Act, the Bank transferred its investment and brokerage services to Nova KBM d.d. The transfer to Nova KBM was completed on 31 December 2018.

In the reporting year, 126.51 kg (vs. 81.1 kg in 2017) in gold bars and coins totalling EUR 4,492 thousand (vs. EUR 2,986 thousand in 2017) were sold at the headquarters and 19 branch offices of Abanka. In addition, 28.03 kg (vs. 26.37 kg in 2017) in gold bars and coins totalling EUR 28,030 thousand (vs. EUR 26,372 thousand in 2017) were bought at the headquarters and 4 branch offices of Abanka.

Custody and Administrative Services

In 2018, Abanka maintained its leading market position in the segment of custody services for investment and pension funds.

A key achievement in 2018 was the adaptation of custody services for investment funds to the amended Investment Funds and Management Companies Act (ZISDU-3B) and the regulatory requirements of the Commission Delegated Regulation (EU) 2016/438, which introduced new duties and responsibilities of custodian banks, both in terms of oversight function and the safekeeping of the financial instruments of investment funds. In line with the statutory provisions, the services provided for pension funds and internal funds of insurance companies were adapted to the higher asset protection standards.

In Slovenia, Abanka has the longest tradition in the provision of administrative services for investment funds. Professional experiences accumulated through the years enable the Bank to provide administrative services also for pension funds and internal funds of insurance companies.

In addition, a comprehensive range of services is provided for alternative investment funds with broader investment policies, demand for which is increasing also in the Slovene financial market.

Abanka's range of services includes custody services under the Market in Financial Instruments Act (ZTFI), which enables the Bank to provide management services for custodial accounts for securities to domestic institutional customers.

We remain the leading bank in custody services for investment and pension funds and also provide custody and administrative services for alternative investment funds.

Total Equity and Ownership Structure

As at 31 December 2018, the **total equity of the Abanka Group** amounted to EUR 583,407 thousand, whilst **that of Abanka** equalled EUR 583,384 thousand. Compared to the 2017 year-end, the total equity of Abanka increased by 0.8% or EUR 4,441 thousand in nominal terms. Profit increased total equity by EUR 66,737 thousand, whereas dividend payments decreased total equity by EUR 42,620 thousand. Due to the transition to IFRS 9 retained profit increased by EUR 10,937 thousand, whereas accumulated other comprehensive income decreased by EUR 29,486 thousand. The total equity was also lower due to the transfer of part of receivables to the subsidiary, thereby reducing retained profit by EUR 646 thousand, and a decrease in accumulated other comprehensive income of EUR 498 thousand; total equity also increased due to to the higher retained profit in the amount of EUR 17 thousand for other changes. As at the reporting date, the Bank's total equity accounted for 15.6% of total balance sheet liabilities, while as at the 2017 year-end it was higher at 15.8%.

At the 37th General Meeting of Shareholders held on 17 May 2018, the shareholders were informed that the accumulated profit for 2017 totalled EUR 60,456,785.06 consisting of the remaining net profit for 2017 of EUR 38,357,934.65 and profit brought forward in the amount of EUR 22,098,850.41 as at the 2017 year-end. The General Meeting of Shareholders decided that a part of accumulated profit for 2017 in the amount of EUR 42,619,927.39 shall be allocated for dividend payments, whereas the remaining part of the profit amounting to EUR 17,836,857.67 shall be allocated to profit brought forward.

As at the reporting date, Abanka's **accumulated other comprehensive income** amounted to EUR 3,333 thousand (a decrease of EUR 29,984 thousand compared to 2017, of which EUR 29,486 thousand resulted from the transition to IFRS 9), **reserves from profit** equalled EUR 58,384 thousand (an increase of EUR 6,674 thousand compared to 2017) and **retained profit** totalled EUR 88,208 thousand (an increase of net profit of EUR 66,737 thousand, a decrease of EUR 42,620 thousand for dividend payments, an increase of EUR 10,937 thousand due to the transition to IFRS 9, a decrease of EUR 646 thousand resulting from the transfer of part of receivables to the subsidiary, a decrease of EUR 6,674 thousand for the allocation of net profit to reserves from profit and an increase of EUR 17 thousand for other changes).

The audited share book value was EUR 38.63 as at 31 December 2018 based on 15,100,000 shares (vs. EUR 38.34 as at 31 December 2017). It was calculated as the ratio of all capital components, including net profit for the reporting period, to the number of shares subscribed as at the reporting date.

The Bank’s share capital amounted to EUR 151,000 thousand as at the reporting date. On 18 December 2013, the Republic of Slovenia subscribed and fully paid up all 15,000,000 shares (ABKS) newly issued by Abanka, and thereby became its 100% owner, holding 15,000,000 ordinary registered no-par value shares with voting rights attached. On 25 September 2014, based on a relevant decision of the European Commission, the Government of the Republic of Slovenia was able to finally adopt its decision on measures for strengthening the stability of Abanka, which also included the second round of the capital increase of EUR 243,000 thousand. On 3 October 2014, the General Meeting of Shareholders of Abanka passed a resolution to increase the share capital through the in-kind contribution of the Republic of Slovenia in bonds totalling EUR 242,999,943.49 and through the cash contribution of EUR 56.51. In accordance with the resolution passed by the 29th General Meeting of Shareholders of Abanka on 8 October 2014, the Republic of Slovenia paid in 100,000 new shares amounting to EUR 243,000 thousand. The share capital increase of EUR 1,000,000.00 was entered in the Companies Register on 10 October 2014. The share capital of Abanka amounts to EUR 151,000,000.00 and is divided into 15,100,000 ordinary no-par value registered shares wholly owned by the Republic of Slovenia. On 5 October 2015, Banka Celje d.d., established in 1864 when Celje Municipal Savings Bank was founded, was merged with Abanka Vipa d.d. in line with the commitment made to the European Commission. After the merger of Banka Celje, the **share capital of Abanka** remained unchanged in the amount of EUR 151,000 thousand, while the share capital of Banka Celje was transferred to the **share premium of Abanka**, amounting to EUR 282,459 thousand as at the 2017 year-end, which remained unchanged in 2018. The corresponding amount per no-par value share in the share capital was EUR 10.00 as at the end of 2018.

On 16 December 2014, Banka Celje received the Decision on Extraordinary Measures of the Bank of Slovenia, based on which additional capital was provided to the Bank. The existing **share capital of Banka Celje** in the amount of EUR 16,980 thousand was therefore first reduced to EUR 0 on 16 December 2014, after which it was increased by EUR 190 million. All qualified liabilities of the bank incurred up to the issue date of the Decision and consisting of share capital and subordinated financial instruments ceased in full. After reducing it to EUR 0, the share capital was increased by EUR 50 million and share premium by EUR 140 million, while the Republic of Slovenia became the sole owner of the bank. The share capital of the bank, which amounted to EUR 50 million after the increase, was divided into 5 million new ordinary no-par value shares. The corresponding amount per no-par value share was EUR 10 and the issue value per share was EUR 38. One half of the capital increase was realised through cash contributions and the other half through the bonds of the Republic of Slovenia.

THE SHAREHOLDER OF THE BANK

31 Dec. 2018 and 31 Dec. 2017	Number of shares	Holding in %
THE REPUBLIC OF SLOVENIA	15,100,000	100.0

With regard to **transparency of financial relations between public authorities and bodies of self-governing local communities and public undertakings**, Abanka is not required to settle the operating loss and ensure the capital because in 2018 the Bank generated a profit of EUR 66,737 thousand.

Issue of shares and capital increase - Abanka

Prior to the enforcement of the 1999 Book Entry Securities Act, three issues of 3,162,362 bonds were placed amounting to EUR 13,196,302.79. Thereafter, the following capital increase operation ensued (excluding the capital increase in 2002 with 536,038 shares following the merger by acquisition of Banka Vipa d.d.): in 2001 with 337,638 shares amounting to EUR 5,752,695.52; in 2003 with 763,962 shares totalling EUR 15,206,554.58; in 2005 with 700,000 shares amounting to EUR 26,289,434.15; and in 2008 with 1,700,000 shares totalling EUR 102,000,000.00.

At the 26th General Meeting of Shareholders held on 8 April 2013, reduction of the Bank's share capital was approved, so that the share capital of the Bank, which on 8 April 2013 amounted to EUR 30,045,067.60 and was divided into 7,200,000 ordinary registered no-par value shares, was reduced through a simplified procedure by EUR 22,845,067.60; after reduction the share capital amounted to EUR 7,200,000.00. This reduction was carried out in order to cover part of the loss for 2012 in the amount of EUR 22,845,067.60 charged to the Bank's share capital. The simplified reduction of the Bank's share capital was entered in the Companies Register on 21 May 2013.

Before 17 December 2013 (i.e. the date when the Bank of Slovenia issued the relevant decision), the share capital of Abanka totalled EUR 7,200,000.00 and was divided into 7,200,000 ordinary, freely transferable, no-par value shares with the ABKN ticker symbol, of which 7,198,874 were in dematerialised (book entry) form and 1,126 in materialised form, the latter not yet submitted to KDD. The voting rights were attached to 4,676,340 shares. In January 2011, the voting rights attached to 2,513,321 shares owned by Zavarovalnica Triglav d.d., HIT d.d., SOD d.d. and Mobitel d.d. were suspended in accordance with the decision issued by the Securities Market Agency. The share issue was fully paid up.

According to the Decision of the Bank of Slovenia on Extraordinary Measures, dated 17 December 2013, as of 18 December 2013 all qualified liabilities of Abanka Vipa d.d. fully ceased, including the share capital comprising all the shares of Abanka Vipa d.d. with the ABKN ticker symbol. On the same day, respective entries were made in the Companies Register and, as a result, the above-mentioned shares were stricken off the Central Securities Depository of securities issued in dematerialised form and kept by KDD.

Simultaneously with the reduction of the share capital of Abanka Vipa d.d. to zero, on 18 December 2013, in accordance with the Decision of the Bank of Slovenia on Extraordinary Measures, dated 17 December 2013, and the Decision of the Bank of Slovenia Approving the Share Capital Increase of Abanka Vipa d.d., dated 18 December 2013, the Bank's capital share was increased to EUR 150,000,000 through the issue of 15,000,000 new ordinary registered no-par value voting shares. On the same day, respective entries were made in the Companies Register and, as a result, the above-mentioned shares were entered in the Central Securities Depository of securities issued in dematerialised form. After 18 December 2013, the share capital of Abanka Vipa d.d. was divided into 15,000,000 new shares with voting rights attached. After the subscription of new ABKS shares, the Republic of Slovenia held 15,000,000 ABKS shares, which was 100% of all issued shares of Abanka Vipa d.d. In accordance with the resolution passed by the 29th General Meeting of Shareholders on 3 October 2014, the Republic of Slovenia paid in 100,000 new shares amounting to EUR 243,000 thousand on 8 October 2014. The share capital increase of EUR 1,000,000.00 was entered in the Companies Register on 10 October 2014. After the increase, **the share capital of Abanka** amounted to EUR 151,000,000.00 and was divided into 15,100,000 ordinary no-par value registered shares wholly owned by the Republic of Slovenia.

Issue of shares and capital increase – Banka Celje

Before the capital increase in 2008, the share capital of the bank consisted of 422,123 no-par value registered shares issued in dematerialised form and entered in the Central Securities Depository of securities issued in dematerialised form. The shares included 80% ordinary shares with voting rights attached and 20% preference shares.

At the 23rd regular General Meeting of Shareholders held on 22 May 2008, the Management Board of the bank was granted the authorisation to increase the share capital by issuing new shares within the next five years. As the amount of the authorised capital may not exceed half of the share capital at the time when authorisation is given, this represented 211,061 shares. The new shares can only be issued with the approval of the Supervisory Board of the bank. In October 2008, the share capital of the bank was increased from the authorised capital by selling 86,506 shares at the total issue value of EUR 35 million. The bank sold 69,205 ordinary shares at a price of EUR 413 per share and 17,301 preference shares at a price of EUR 371 per share. After the capital increase, the share capital of the bank was divided into 508,629 no-par value shares.

No new shares were issued from the authorised capital in the following years. At the General Meeting of Shareholders held in October 2012, a resolution was passed, revoking the preferential rights of all issued preference shares and converting them into ordinary shares.

Following the capital increase through state aid on 16 December 2014, the share capital of the bank was divided into 5,000,000 ordinary registered no-par value shares issued in dematerialised form. All the shares that represented a qualified liability of the first order prior to the capital increase, i.e. all 508,629 ordinary no-par value shares, were cancelled as of the date of the capital increase. Through the capital increase the Republic of Slovenia became the sole owner of the bank.

THE BANK'S DEVELOPMENT

DEVELOPMENT AND MARKETING COMMUNICATIONS IN 2018

Corporate banking

Attracting new and retaining the existing customers was based on being well familiar with companies, understanding their business, understanding the risks to which they are exposed in the course of their operations, and on identification of their needs for obtaining financial sources and other banking products. In the reporting period, cross-marketing of all services of the Bank was promoted in cooperation with corporate banking, treasury, payment transactions and modern distribution channels. For micro- and small enterprises, special conditions for short-term and long-term financing were designed by using own funds. In the corporate lending segment, the Bank continued to cooperate with municipalities, SID Bank and the Slovene Enterprise Fund by together offering loans for businesses at favourable interest rates. For attracting new customers, a welcome package was designed, which includes price-adjusted services needed by businesses in their day-to-day operations. In upgrading the Abamobi com mobile bank and the Abanet com online bank, the range of improvements received from the users of modern channels was taken into account. Electronic and mobile channels for corporate customers were upgraded with the options to easily rename their username, import or export the business partner address book from one user to another, cancel several orders simultaneously and customise overviews, as well as a number of other improvements to facilitate business finance management. In the summer of 2018, the range of card products was expanded with a new, modern service – mobile wallet Abadenarnica, and execution of payments for business purposes was enabled on smartphones. Despite the high level of competition in card operations (acceptance of cards by merchants), the Bank managed to retain all the key customers and attract new customers by applying an appropriate marketing approach and expertise. Business process digitalisation continued by upgrading the existing lending application, enabling form autocomplete, etc.

In the summer of 2018, the range of card products was expanded with a new, modern service – mobile wallet Abadenarnica, and execution of payments for business purposes was enabled on smartphones.

In the reporting period, many business events for the business public were held, i.e. several regional educational and social events and one main event for the business public in spring 2018 in Ljubljana. Abanka's range of corporate products and services was presented at numerous conferences and business events in cooperation with different commercial and entrepreneurial organisations in Slovenia, such as: Family Business Conference, MOS (International Trade and Business Fair), SBC Academy, and many regional and local events held by regional chambers of craft and small business.

In the corporate segment, in addition to participation in various business events and memberships in various commercial and business organisations serving as a contact point for the promotion of Abanka, marketing and communication activities focused on advertising campaigns in the (business) media to raise the visibility of brands for corporate customers, such as Abamobi com, Abanet com and Abadenarnica (a mobile wallet also for corporate customers), and on various forms of direct marketing communication, which were updated according to IT developments. Furthermore, many modern (internal) communication channels of Abanka and social networks, e.g. LinkedIn, were used, while modern communication channels, e.g. e-mail and SMS, were added to traditional channels for making contact, which were followed by account managers' meetings with (potential) customers.

Retail Banking

In 2018, Abanka continued to pursue the objective of its digital transformation. The emphasis was on attracting new customers in all segments, delivering a good user experience, providing a range of quality and professional products, process and business simplification, and strengthening all distribution channels.

The development of banking services was focused on delivering a good user experience of Abanka's services. The Bank not only developed banking services that ensure a better anticipation of customer needs but also designed customer-tailored and easy-to-use services, accessible anytime and anyplace. The greatest effort was devoted to the development of digital channels and new forms of payment. The upgrading of the Abamobi mobile bank continued by adding new functionalities. In May 2018, a new version of the Abanet online bank with a new design was launched. In the middle of 2018, the Abadenarnica mobile wallet was developed. The Abadenarnica mobile wallet enables contactless payment with Abanka payment cards. It is intended for all users of smart mobile devices and Abanka Maestro and Mastercard payment cards. Apart from that, alternative forms of saving were offered to savers. Abanka maintains an excellent partnership with Zavarovalnica Triglav d.d. and Triglav Skladi d.o.o. in order to provide a wide range of insurance services and mutual funds. In 2018, a special bundled product continued to be provided, based on which customers were offered the possibility of diversifying their investment either by choosing a non-purpose deposit and investing in a selected mutual fund or by choosing a deposit with guaranteed interest payment and single premium unit-linked life insurance Fleks. To maintain customer loyalty and increase the number of users of the Abaklub loyalty programme, this service was upgraded with the option "invite a friend" and the benefits offered by several business partners of Abanka. A welcome package was prepared for all new customers, enabling them banking services at more affordable prices. The range of housing and consumer loans at affordable rates was maintained. Several processes were simplified and a series of minor improvements was made, which have an impact on service quality. The implementation of e-pen in the processes of product approval for retail customers continued, in addition to upgrading the loan application.

In the reporting period, marketing tools and digital marketing communication were upgraded, thereby consolidating Abanka's position as a technologically advanced and innovative bank of friendly people also by selecting which communication channels to use.

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Through marketing and communication campaigns in the media, the Bank raised the visibility of many service marks, particularly those relating to mobile and electronic channels and card operations. A modern and effective method of promotion, increasing the visibility and applicability was designed for two new services. Content marketing communication was again the core of marketing communication when communicating the banking services in which customers are interested before going on holidays.

Where changes in the competitive environment or the need to improve the sales results were identified, a regional approach was chosen to make customers aware of the Bank's services and bring them closer to the customers in the selected local environments.

In the reporting period, the digital marketing platform was finally integrated into the comprehensive customer relationship management support system, placing great emphasis on targeted direct marketing communication based on predictive analytics models via the channels preferred by customers (e-mail, SMS, phone calls). In this way, different target groups were addressed in an even more systematic and niche way, depending on their buying behaviour and decision-making process. Where possible, the buyer's journey and the stage in their buying decision-making process were taken into account. Moreover, the Bank remained in contact with the customer even after their buying decision by providing advice and guidance for an even better use of the product or service, thereby contributing to better engagement of the service user and boosting customer satisfaction.

Content marketing and communication on social networks were strengthened so as to address (potential) customers in a better way and obtain their contacts for further direct marketing communication.

In all marketing activities, loyal customers were informed and addressed through numerous internal communication channels.

Financial Markets

In 2018, in terms of liquidity management, the Treasury Division:
- continued with the process of upgrading, automating and centralised management of operational liquidity;
- continued the management of secondary liquidity reserves and provided for an adequate level, quality and structure of the banking book.

In the reporting period, all treasury products were actively marketed, but the highest increase in demand was seen in financial instruments for hedging against market risk. Volatility on financial markets was high in 2018, which was reflected in foreign exchange markets in particular. For this reason, customers actively used derivatives for hedging against changes in exchange rates. In 2018 interest rates remained at record-low levels, which resulted in an increasing number of customers opting for interest rate swaps (IRS) or interest rate caps for hedging against interest rate risk when taking out a loan. The interest rate cap proved to be a highly effective instrument in the period of negative rates because, in return for paying an optional premium, it provides dynamic protection, under which the customer will receive payment in the event of a rise in Euribor above the agreed interest rate without having any additional obligations arising from the interest rate cap agreement.

In the reporting period, Abanka not only strengthened cooperation with the existing customers but also acquired new customers, thereby enhancing its visibility in the sale of treasury products, which was confirmed by the extremely good attendance of corporate customers at the traditional 11th meeting with the Treasury Department, organised in October 2018 in Ljubljana.

Abanka remains an important primary dealer in Slovene government bond issues and continues actively participate as a market maker in MTS Slovenia and as an official liquidity provider, both in the domestic and foreign markets. In 2018, together with other renowned foreign banking groups, Abanka was selected as a co-lead manager in charge of increasing the issue of 10-year, 17-year and 27-year bonds in the total amount of EUR 1.25 billion.

Abanka remains an important primary dealer in Slovene government bond issues and continues actively participate as a market maker in MTS Slovenia and as an official liquidity provider, both in the domestic and foreign markets.

DEVELOPMENT AND MARKETING COMMUNICATIONS IN 2019

In retail banking, innovative solutions will be developed and optimal solutions will be provided for the users, in accordance with the digitalisation of the Bank. The product range will be expanded and new functionalities will be added to the existing products to make them simple in terms of content and availability. In 2019, the mobile bank will be upgraded with the option of submitting a quick loan approval application and an additional overdraft facility application, managing credit cards and viewing insurance, all of which will increase user satisfaction. The loyalty programme will be upgraded with the benefits provided by the Bank's business partners. The Abadenarnica mobile wallet, which enables mobile payment with Mastercard cards, will be upgraded with mobile payment using Visa cards, a new cashless payment instrument – instant payments will be added, and viewing of card balance and transactions will be enabled. A special offer for new customers will continue to be provided. A welcome package will be designed for Račun users and retired persons, enabling them banking services at affordable prices. Housing and consumer loans will continue to be provided at affordable rates (a special offer of housing and consumer loans). The range of personal accounts for existing users will be redesigned.

In corporate banking, cooperation with external business partners (SID, municipalities, etc.) will continue by together offering loans at favourable interest rates. The development of modern channels remains in the foreground. The Abamobi com mobile bank and Abanet online bank will be improved by adding new functionalities, making technological upgrades in accordance with regulatory changes (eIDAS, PSD2) and optimising user experience. In 2019, special offers for small businesses will be designed – a range of products for new customers, a special offer of loans for small business customers, etc. The existing business processes will be further upgraded. The loan application for selling and granting loans, guarantees and deposits will be upgraded with the support for approving annexes to a loan agreement, loans for commonhold owners, liquidity loans and overdraft facility for a transaction account based on receivables and with many other features designed to speed up the investment approval process.

Excellent marketing and communication results were achieved in the reporting period, therefore the set marketing activities will not only continue to be carried out but will also be updated and upgraded with new concepts by taking into account the current trends in marketing communication and the applicable business guidelines.

Advertising campaigns for raising the visibility of service marks and for sales promotion will be implemented in accordance with the set business and marketing objectives for 2019.

The main form of marketing communication will be video content, while the focus will be on a two-way communication with the customer and on personified marketing messages. In addition to advertising through the established marketing channels, most attention will be devoted to targeted direct marketing communication based on predictive analytics models via the channels preferred by customers (e-mail, SMS, phone calls). Efforts to obtain consent of customers and potential customers for direct marketing will continue in compliance with the GDPR so as to continuously expand the direct marketing database.

Great emphasis will be given to the digital forms of advertising and seeking innovative, creative digital forms and channels of marketing communication, such as social networks, content marketing, native marketing and similar.

Customer referrals and excellent reviews will be included in marketing communication, in addition to engaging customers and employees as ambassadors of Abanka's services. The marketing activities will be aimed at the existing customers as well as attracting new customers.

In 2019, active engagement of the target segments on the internet and social networks will continue, while striving to keep the indicator "Recommendation of the Bank or its products and service" (Net Promoter Score) above the average value.

> In 2019, we will keep on striving to maintain the indicator »Recommendation of the Bank or its products and service« (Net Promoter Score) above the average value.

CORPORATE GOVERNANCE STATEMENT

To achieve a high level of transparency in governance, Abanka d.d. includes a corporate governance statement in its business report in accordance with the fifth paragraph of Article 70 of the Companies Act.

Abanka d.d. implements its internal governance arrangements, including corporate governance, in accordance with the applicable legislation of the Republic of Slovenia, particularly the provisions of the Banking Act (ZBan-2) on internal governance arrangements in Section 3.4 (Governance System of a Bank) and Section 6 (Internal Governance Arrangements and Internal Capital Adequacy), the latter in the part relating to the requirements which apply to a bank or to the members of the management body, in addition to taking into account the regulations referred to in the second paragraph of Article 9 of the Banking Act (ZBan-2). Apart from that, the Bank adheres to the Decision on Internal Governance, the Management Body and the Adequate Internal Capital Assessment Procedure for Banks and Savings Banks and the relevant EBA guidelines on internal governance, on the assessment of the suitability of members of the management body and key function holders as well on remuneration policies and practices. Furthermore, the Bank seeks to follow non-mandatory recommendations from the letter of the Bank of Slovenia (ref. 38.20-0288/15-TR of 23 October 2015) to the maximum possible extent.

Abanka d.d. is a state-owned company and not a public company within the meaning of the Financial Instruments Market Act. The governance of the Bank is defined in the Articles of Association of Abanka d.d. and the Governance Policy of Abanka d.d. The governance of subsidiaries in the Abanka Group is defined in the Framework Corporate Governance Policy of the Abanka Group, which stipulates that even subsidiaries must comply with the corporate governance standards that apply to the parent company of the Abanka Group, in proportion to the characteristics, scope and complexity of their operations. The governance policies and practices of Abanka are publicly accessible on its website at http://www.abanka.si/.

In 2018, the Bank complied with the legal requirements on the governance of a bank, including the reference codes and recommendations set out in the Statement of Compliance with corporate governance codes.

Statement of Compliance with Corporate Governance Codes

The Management and Supervisory Boards declare that in their work and operations in 2018 Abanka d.d. observed the corporate governance recommendations as set out in:

- **Corporate Governance Code for Listed Companies** adopted by the Ljubljana Stock Exchange d.d., Ljubljana and the Slovenian Directors' Association on 27 October 2016. The Code is available on the website of the Ljubljana Stock Exchange at http://www.ljse.si.
- **Corporate Governance Code for Companies with Capital Assets of the State** adopted by Slovenski državni holding d.d. (hereinafter: SDH) in May 2017 and the **Recommendations and Expectations** of Slovenski državni holding d.d. adopted in March 2018. Both documents are published on the SDH's website www.sdh.si.

Individual deviations from the provisions of the codes and recommendations, including a statement of reasons and presentation of appropriate alternative practices, are disclosed below. The reasons for a different practice lie primarily in specific characteristics related to the ownership structure and industry or activities of the company.

a) <u>Corporate Governance Code for Listed Companies</u>

Code provision 6.2: Abanka is of the view that providing information to the public via its sole shareholder – the Republic of Slovenia about their investment policy is primarily at the shareholder's discretion, in line with the regulations governing capital assets of the State. No encouragement by Abanka can specifically influence its shareholder's decision to inform the public.

Code provision 12.3: The scope of topics and time frames to be respected by the Management Board in its regular reporting to the Supervisory Board are not set in the Rules of Procedure of the Supervisory Board but in a separate document – an annual calendar of meetings of the Supervisory Board and its committees, including the planned scope of topics to be discussed, which is approved by the Supervisory Board at its last session of each year for the following year. The Management Board promptly provides materials for the Supervisory Board sessions, both in writing and in electronic form (by ensuring adequate protection), while seeking to improve the quality of the materials.

Code provision 12.8: The manner of communicating with the public with respect to the decisions adopted at a Supervisory Board session is not stipulated by the Rules of Procedure of the Supervisory Board, but the manner of publishing announcements and data of the Bank is determined by the Articles of Association of Abanka d.d.

Code provision 15.3: Until 4 September 2018, the Chairman of the Supervisory Board was at the same time the Chairman of the Nomination Committee, whereas since that date he has been its member.

Code provision 27.4: Given that the Bank is wholly-owned by one shareholder, it ensured the transparency of operations by timely and appropriately informing the shareholder of the expected dates of its significant announcements.

Code provision 29.7: The Bank disclosed the remuneration of each Management Board member for 2017 by disclosing the total gross amount of the variable part of remuneration but not the gross amount broken down to the items calculated based on quantitative and qualitative criteria.

b) Corporate Governance Code for Companies with Capital Assets of the State

Code provision 6.15.1: Until 4 September 2018, the Chairman of the Supervisory Board was at the same time the Chairman of the Nomination Committee, whereas since that date he has been its member.

Code provision 8.3: The Bank disclosed the remuneration of each Management Board member for 2017 by disclosing the total gross amount of the variable part of remuneration but not the gross amount broken down to the items calculated based on quantitative and qualitative criteria.

Code provision 8.5: Given that the Bank is wholly-owned by one shareholder, it ensured the transparency of operations by timely and appropriately informing the shareholder of the expected dates of its significant announcements.

c) Recommendations and Expectations of the Slovenian Sovereign Holding

Recommendation No. 5: Attainment of quality and excellence in operations: The Bank performs a range of activities to determine, assess, manage and monitor the quality of its operations in various segments. The Code of Ethics constitutes the basis for improving the corporate culture of the Bank, thereby achieving business excellence and quality. The activities aimed at improving the quality of operations include verification of customer satisfaction (analyses on the basis of received complaints, loss events and other incidents, checking the service level among organisational units) and care for employee satisfaction (measurement of the organisational climate, management staff assessment, a Family-Friendly Enterprise certificate, concern for employee safety and health, monitoring of staff turnover, monitoring of reported infringements and irregularities, promotion and rewarding of promoters of the Bank's values and innovative ideas), professional training and acquisition of leadership skills. By ensuring adequate staffing in IT area, the quality and security of information systems is properly managed. Moreover, with their activities, the qualified internal control functions contribute to higher quality of the Bank's operations through their activities.

Main characteristics of the internal control and risk management systems in financial reporting

The Bank maintains and implements a robust internal governance system that includes an internal control system and appropriate risk management processes. The internal control system addresses all material risks in the Bank. Internal controls are established at the level of ongoing internal controls (reporting, work procedures, separation of powers and responsibilities, and automatic and manual controls) and include the verification of administrative and accounting procedures at all stages of the accounting process. They are embedded in business and support processes for carrying out core and ancillary activities of the Bank. Internal controls are also performed at the level of independent internal control functions (risk management, compliance and internal audit), which – each within its respective powers – checks or ensures compliance of the Bank with the applicable regulations, internal documents and measures adopted on their basis.

In order to provide quality, reliable and comprehensive accounting information and, consequently, correct and timely financial reporting, the Bank performs accounting control through the operation of the entire accounting function. The day-to-day security of the implementation of tasks is managed through an appropriate system of authorisations, separation of duties, compliance with accounting rules, business event documentation, the custody system, built-in control mechanisms in analytical applications and archiving in accordance with the applicable legislation and internal regulations. The Bank ensures the reliability of the support system for business operations and decision-making as well as compliance with legal and other requirements through effective implementation of primary accounting control, which is mostly carried out in analytical accounting, and secondary accounting control, which is aimed at verifying the effectiveness of primary accounting controls.

The basic risk appetite framework of Abanka consists of the Risk Management Strategy and Risk Appetite, Risk Management Limits, and ICAAP and ILAAP Rules, all revised in 2018, which provide the basis to identify, measure or assess, manage, monitor and adequately report on all material risks to which the Bank is or could be exposed in its operations.

Information required under items 3, 4, 6, 8 and 9 of paragraph 6 of Article 70 of the Companies Act

- **The structure of the company’s share capital, including all securities, as defined by the act governing takeovers**
  As at the reporting date, the share capital of Abanka amounted to EUR 151,000,000.00 and was divided into 15,100,000 ordinary no-par value registered shares wholly owned by the Republic of Slovenia. Abanka has only one class of shares without any restrictions on their transferability. Each ordinary share carries one vote at the General Meeting of Shareholders unless stipulated otherwise by the Articles of Association or the law (no voting right).

- **Significant direct or indirect ownership of securities in terms of achieving a qualifying holding as defined by the act governing takeovers**
  As at the reporting date, the Republic of Slovenia was the 100% owner of all the Bank’s shares.

- **Special controlling rights**
  None of the Bank's shareholders have special controlling rights.

- **Voting right restrictions**
  According to the Articles of Association, voting rights are not restricted to a certain holding or to a minimum number of shares. Detailed information on the exercise of voting rights is contained in Section *Functioning of the General Meeting of Shareholders, its key competencies, description of shareholders' voting rights and the manner in which they are exercised*, which is part of this statement.
  The Bank is unaware of any agreements according to which the financial rights attached to securities are through the involvement of the Bank separated from the rights attached to the holding of such securities.

- **Rules on the appointment or replacement of members of the management or supervisory bodies and amendments to the Articles of Association**
  The rules on the appointment or replacement of members of the management or supervisory bodies are presented in Section "Composition and functioning of management or supervisory bodies and their committees", which is part of this statement.
  The rules regarding amendments to the Articles of Association are disclosed in Section "Functioning of the General Meeting of Shareholders, its key competencies, description of shareholders' voting rights and the manner in which they are exercised", which is part of this statement.

- **Authorisations of the management, especially share purchase and share issuing options**
  The Management Board of the Bank is not authorised to issue or purchase shares or issue authorised capital.

Functioning of the General Meeting of Shareholders, its key competencies, description of shareholders' voting rights and the manner in which they are exercised

The General Meeting of Shareholders consists of the Bank's shareholders. The General Meeting of Shareholders decides on the following matters: distribution of the accumulated profit on the proposal of the Management and Supervisory Boards; approval of the Annual Report should the Supervisory Board fail to approve the Annual Report or should the Management and Supervisory Boards leave it to the General Meeting of Shareholders to decide on the approval of the Annual Report; the Annual Internal Audit Report, including the opinion of the Supervisory Board; adoption of and amendments to the Articles of Association; measures to increase or decrease the share capital, excluding those which, in line with the Articles of Association, fall within the competence of the Management Board; the winding-up of the Bank and status-related changes; appointment and dismissal of Supervisory Board members; a vote of no confidence in the Management Board; granting discharge to members of the Management and Supervisory Boards; appointment of the auditor; the Rules of Procedure of the General Meeting of Shareholders and other matters determined by the Articles of Association and by the law.

The General Meeting of Shareholders is convened at least once a year by the Management Board. It can also be convened by the Supervisory Board. In addition, shareholders holding a total of one-twentieth of the share capital may require that a General Meeting of Shareholders be convened.

The Management Board convenes the General Meeting of Shareholders at least thirty days prior to the General Meeting of Shareholders by publishing the notice convening the General Meeting, its agenda and draft resolutions in the manner provided by the law and the Articles of Association. The material necessary for making decisions at the General Meeting, including draft resolutions, must be available to the shareholders at the Bank’s premises from the publication of the notice convening the General Meeting.

If all shareholders of the Bank are present or represented at the General Meeting of Shareholders, the General Meeting of the Shareholders may take decisions without prejudice to the provisions of the law or the Articles of Association concerning the content, date and publication of the notice convening the General Meeting, the provisions relating to the deadlines and publication of amendments to the agenda of the General Meeting and the provisions on the majority required for the Management Board of the Bank to take a decision on the convocation of the General Meeting of Shareholders.

Only the shareholders holding ordinary shares who were entered in the Share Register no later than by the end of the fourth day before the date of the General Meeting of Shareholders and who announced their attendance to the Management Board no later than by the end of the fourth day prior to the date of the General Meeting are entitled to participate in and vote at the General Meeting of Shareholders. Shareholders may exercise their rights at the General Meeting of Shareholders in person or through a proxy.

Each ordinary share carries one vote at the General Meeting of Shareholders unless stipulated otherwise by the Articles of Association or the law (no voting right). The Bank has not issued any shares with restricted voting rights. The General Meeting of Shareholders adopts decisions by the majority of votes cast, unless otherwise stipulated by the Articles of Association or by the law. A three-quarters majority of the represented share capital is required for the General Meeting of Shareholders to adopt decisions on increasing or decreasing the capital, amendments to the Articles of Association, the denial of pre-emption rights to purchase shares in increasing the share capital, the winding-up of the Bank, status-related changes of the Bank, the dismissal of a Supervisory Board member and a vote of no confidence in the Management Board.

At the 37th General Meeting of Shareholders held on 17 May 2018, the shareholders took note the Annual Report of Abanka for 2017 and remuneration of the members of the Supervisory and Management Boards for 2017. In addition, they were briefed on the accumulated profit for 2017, which totalled EUR 60,456,785.06 consisting of the remaining net profit for 2017 of EUR 38,357,934.65 and profit brought forward in the amount of EUR 22,098,850.41 as at the 2017 year-end. The General Meeting of Shareholder decided that a part of accumulated profit for 2017 in the amount of EUR 42,619,927.39 shall be allocated to dividend payments, whereas the remaining part of the profit amounting to EUR 17,836,857.67 shall be allocated to profit brought forward. Furthermore, the General Meeting of Shareholders decided that the Bank shall pay out the dividends on 29 May 2018 according to the balance as at one business day before the payment date. The General Meeting of Shareholders granted a discharge to the Management and Supervisory Board members and adopted the Annual Internal Audit Report of Abanka d.d. for 2017, including the opinion of the Supervisory Board. Furthermore, it appointed Deloitte Revizija d.o.o. as auditors of Abanka's and the Abanka Group's Annual Report for a three-year period (2018–2020) and appointed Marko Garbajs a Supervisory Board member for a four-year term of office, starting on 5 October 2018.

At the 38th general Meeting of Shareholders held on 30 July 2018, the shareholders took note of the resignation of two members of the Supervisory Board, i.e. Peter Merc as of 9 July 2018 and Bernarda Babič as of 5 July 2018. Varja Dolenc was appointed a Supervisory Board member with a four-year term of office, commencing on 31 July 2018.

At the 39th General Meeting of Shareholders held on 21 September 2018, Miha Košak was appointed a Supervisory Board member with a four-year term of office starting on 22 September 2018. The General Meeting of Shareholders agreed with the spin-off to establish the new company Ahive, upravljanje s terjatvami d.o.o. with the short name Ahive, d.o.o., headquartered in Ljubljana, business address at Trdinova ulica 4 in Ljubljana and the share capital of EUR 7,500.00, with Abanka d.d. acting as the transferring company.

Composition and functioning of management or supervisory bodies and their committees/commissions

Abanka uses a two-tier management system. The Bank is run by the Management Board, whose work is supervised by the Supervisory Board. The governance of the Bank is based on the applicable legal regulations, the Articles of Association, internal documents, generally accepted business practices, the Corporate Governance Code for Listed Companies, the Corporate Governance Code for State-Owned Enterprises and the Recommendations and Expectations of the Slovenian Sovereign Holding (with certain exceptions and differences disclosed in the Statement of Compliance with Corporate Governance Codes).

Management Board

The Management Board runs the Bank's operations independently, for which it is fully responsible. In legal transactions, the Bank is always jointly represented by two members of the Management Board who are entitled to sign on its behalf. The Management Board is appointed and dismissed by the Supervisory Board. The Management Board has at least two and no more than five members, of whom one acts as its President. The number of Management Board members is determined by the Supervisory Board. The President and members of the Management Board are appointed for a five-year term with the possibility of reappointment. The Management Board reports to the Supervisory Board in accordance with the applicable regulations.

The composition of the Management Board in 2018 is presented in Appendix 1 of the Corporate Governance Statement.

Each member of the Management Board has one vote. The decisions of the Management Board are adopted by a majority vote of all members. Where a vote is equal, the President holds the deciding vote. By a special decision adopted unanimously, the

Management Board may authorise each of the Management Board members to take decisions on individual matters and transactions relating to the Bank's current operations at their own discretion.

If a member of the Management Board is appointed director or if their function in other companies and organisations has ended, they are required to immediately inform in writing the Bank, the Supervisory Board and the Bank of Slovenia or the European Central Bank.

A member of the Management Board is obligated to notify the Supervisory Board of the circumstances due to which a potential conflict of interest may arise with respect to the performance of the function of a Management Board member and of other circumstances that could affect the fulfilment of the conditions for the appointment as a Management Board member in line with the Banking Act, including any significant change which affects or could affect the Bank's assessment as to their suitability as a Management Board member.

The Management Board is responsible for the establishment and implementation of such an internal governance arrangement of the Bank, which will enable efficient and prudent management of the Bank based on clearly defined powers and duties as well as policies and measures for the prevention of conflicts of interest. The Management Board is fully responsible for the operations of the Bank and its risk management, including (i) the approval of strategic objectives of the Bank, adoption and regular review of the risk appetite and management strategy and internal governance arrangement; (ii) ensuring the integrity of the accounting and financial reporting systems, including financial and operational control as well as compliance with the applicable regulations and standards; (iii) monitoring of information disclosure procedures and procedures for notification of competent authorities and other stakeholders; and (iv) effective supervision of senior management. Furthermore, the Management Board regularly monitors and assesses the effectiveness of the internal governance arrangement, takes appropriate measures to eliminate any identified deficiencies, and informs and reports to the Supervisory Board.

A member of the Management Board must satisfy the statutory conditions for performing the function of a Management Board member throughout their entire term of office as well as (i) act with due diligence and in particular ensure that the Management Board acts in line with the Banking Act; (ii) act honestly, fairly and independently so as to effectively evaluate and assess senior management decisions related to the management of the Bank; (iii) act in accordance with the highest ethical standards of governance, including the prevention of conflicts of interests; and (iv) devote sufficient time to effectively perform the function of a Management Board member.

Apart from that, a member of the Management Board has to ensure that the Bank operates in accordance with the general rules and regulations governing the performance of services and transactions provided by the Bank as well as any regulations issued on the basis thereof.

The Rules of Procedure of the Management Board stipulate the methods of its work, and distribute the areas of work and tasks among its members. The Management Board assigns individual organisational units of the Bank to its members and makes them responsible for their management and co-ordination. The Management Board adopts its decisions at regular and extraordinary meetings. If needed, the Management Board convenes a meeting with select or several senior management members to share information, coordinate the operations of the Bank and discuss other important business matters.

The data on the remuneration of the Management Board members for 2018 are disclosed in *Appendix 2 of the Corporate Governance Statement*.

The Management Board may transfer certain decision-making rights to executive and other employees as well as to **collective decision-making bodies**. The number and type of bodies is determined in the rules on organisation, while the composition, scope of powers and working methods are defined by the rules of procedure of an individual body. In 2018, the Bank's committees were as follows:

- **Risk Management and Asset-Liability Committee**
  The Committee is in charge of monitoring and assessing the appropriateness of the risk management strategy, policies and methodologies, the appropriateness of the recovery plan and all ICAAP and ILAAP elements, monitoring risk exposure and taking appropriate action, capital and capital adequacy management, monitoring security in its broadest sense, discussing and approving the limit system so as to manage risks, exposure to banks, examining internal transfer prices, considering and deciding on transactions that have a material impact on the Bank's position in terms of liquidity, interest rates, currencies and capital. The Committee is composed of Management Board members and senior management representatives. The Management Board appoints the Committee Chair, Vice Chair and members as well as the persons with a standing invitation to attend the Committee meetings. As at the 2018 year-end, the Committee had nine members. Regular meetings of the Committee are convened once a month, whereas extraordinary meetings are held when necessary. The meetings can be held by correspondence.

- **Operational Risk Commission**

  The Operational Risk Commission is a working body of the Risk Management and Asset-Liability Committee in charge of the development of the operational risk management system within the Bank. The duties of the Commission include in particular: monitoring the implementation of the operational risk management policy, discussing reports on loss events and incidents and proposing the adoption of appropriate measures to the Risk Management and Asset-Liability Committee, monitoring the implementation of measures and reporting thereon, discussing all operational risk elements, making proposals to change and improve operational risk management, discussing the proposals to change business roles and performing other operational risk-related activities. The Commission is composed of representatives of various divisions and/or departments of the Bank. The Commission adopts decisions at regular meetings, which are usually held every quarter. Extraordinary meetings are convened when necessary and may be held by correspondence.
- **Credit Committee**

  With regard to asset management, the Committee decides on borrowings to customers, credit limits, accepting syndicated loan agent services, project financing and other financial services, discusses financial restructuring plans, recovery plans, investment restructuring proposals, proposals to initiate insolvency proceedings, discuses reports, monitors the execution of powers of authorised employees and the implementation of the Committee's decisions, as well as decides on other matters. The Committee is composed of two Management Board members and heads of various divisions and/or departments. The Management Board appoints the Committee Chair, Vice Chair and members as well as the persons with a standing invitation to attend the Committee meetings. At the 2018 year-end, the Committee had six members. Regular meetings of the Committee are convened once a week, whereas extraordinary meetings are held when necessary. The meetings can be held by correspondence.
- **Development Committee**

  With regard to project work, the Committee is in charge of adopting a strategic annual plan for development activities, an annual investment plan and a plan of available internal human resources for the implementation of development activities, classifying all development activities in the portfolio of development activities, supervising the implementation of development activities and initiatives relating to data management, monitoring the implementation of regulatory projects and other strategically important projects, deciding on proposals and overseeing the work of the Development Board, as well as giving initiatives and proposals to the Management Board. The Committee is composed of Management Board members and heads of various divisions and/or departments. The Management Board appoints the Committee Chair, Vice Chair and members as well as the persons with a standing invitation to attend the Committee meetings. As at the 2018 year-end, the Committee had fourteen members. Regular meetings of the Committee are convened every three months, whereas extraordinary meetings are held when necessary. The meetings can be held by correspondence.
- **Development Council**

  With regard to project work, the Council assesses proposals for capacity development and takes decisions on how to continue to implement development activities, takes decisions at all stages of the project lifecycle and development task, decides on development activities within the approved plan while monitoring the availability of human resources, monitors the implementation of projects, development tasks and other development activities, prepares a draft annual plan for development activities and possible changes, directs and controls the development of data management, as well as develops proposals for discussion at the Development Committee. The Council is composed of two Management Board members and heads of various divisions and/or departments. The Management Board appoints the Chair, Vice Chair and members as well as the persons with a standing invitation to attend the Council meetings. As at the 2018 year-end, the Council had five members. Regular meetings are convened once in two weeks but at least once a month, whereas extraordinary meetings are held when necessary. The meetings can be held by correspondence.
- **Sales and Marketing Committee**

  The Committee monitors market trends, the trends and activities of competitors on the market in terms of prices and content of products, sales channels and responsiveness, defines key performance indicators, monitors, supervises, directs and coordinates marketing activities, monitors the business results, promotes the creation of new products and approves their launch, monitors surveys on the Bank's reputation, market position and customer satisfaction, as well as adopts appropriate measures. The Committee is composed of Management Board members and heads of various divisions and/or departments. The Management Board appoints the Committee Chair, Vice Chair and members as well as the persons with a standing invitation to attend the Committee meetings. As at the 2018 year-end, the Committee had ten members. Regular meetings of the Committee are convened once a month, whereas extraordinary meetings are held when necessary. The meetings can be held by correspondence.
- **Liquidity Commission**

  The Commission designs the current liquidity, currency and interest policies of the Bank, sets interest rates on the deposits of corporate, retail and private clients and specifies other special terms and conditions regarding these deposits, as well as performs other duties within its powers. The Commission is composed of Management Board members and heads of various divisions and/or departments. The Management Board appoints the Chair, Vice Chair and members of the Commission. As at the 2018 year-end, the Commission had eleven members. Regular meetings of the Commission are usually convened once a day, whereas extraordinary meetings are held when necessary. The meetings can be held by correspondence.

- **Commission for the Treatment of High-Risk Customers in Terms of Money Laundering and Terrorist Financing Prevention**

  The Commission discusses cases of high-risk customers in order to take appropriate measures to ensure their conduct is in compliance with the applicable laws and to adopt measures for a comprehensive management of all types of risks to which the Bank is or could be exposed when dealing with such customers. The Commission is composed of representatives of various divisions and/or departments of the Bank. The Commission's meetings are held when necessary. As at the 2018 year-end, the Commission had six members.
- **Procurement Commission**

  The Procurement Commission is responsible for transparent conclusion of transactions related to the procurement of goods and services based on previously set and appropriately balanced selection criteria as well as on the basis of obtained comparable offers, which is the responsibility of the relevant departments of the Bank. The composition of the Commission is determined by the Management Board. The Commission meets when necessary and at the request of the department proposing individual purchases. As at the 2018 year-end, the Commission had three members.

Supervisory Board

The Supervisory Board oversees the management of the Bank's business operations. It consists of seven members, who are appointed and dismissed by the General Meeting of Shareholders. Two thirds of the Supervisory Board members must be independent experts. Independent persons are those who are not or have not been employed by the Slovene Government within the last 24 months since their appointment to the Supervisory Board, or who have not performed a senior or managerial function in any Slovene political party within the last 24 months. Any natural person fulfilling the relevant requirements and for whom no restrictions were stipulated in the act regulating banking, the act regulating companies and other applicable regulations may be appointed to the Supervisory Board. The members of the Supervisory Board are appointed for a four-year term with the possibility of reappointment.

The Supervisory Board is responsible for the following: deciding on the appointment and dismissal of Management Board members and their remuneration; deciding on granting loans to Management Board members, authorised officers and other persons stipulated by law; approving the agreements between Supervisory Board members and the Bank; adopting and monitoring the implementation of general remuneration policy principles; deciding on granting loans to Supervisory Board members; reviewing and providing a written opinion on the Annual Report, including the auditor's report, and on the Management Board's proposal on profit distribution to the General Meeting of Shareholders in accordance with the second paragraph of Article 282 of the Companies Act (ZGD-1); approving the Annual Report; reviewing and providing opinions on financial and other reports by the Management Board; supervising the adequacy of internal control procedures and the effectiveness of the internal audit department; proposing nominees for the Supervisory Board to the General Meeting of Shareholders; submitting proposals to the General Meeting of Shareholders for the appointment of an auditor; proposing profit distribution to the General Meeting of Shareholders together with the Management Board; providing an opinion on the annual internal audit report to the General Meeting of Shareholders; reporting on the annual audit and auditing costs of the Bank to the General Meeting of Shareholders; discussing the findings of the Bank of Slovenia or the European Central Bank (ECB) if the ECB exercises the powers and duties of the supervision over the Bank in line with the EU regulations governing banking, as well as findings of other supervisory bodies in the bank supervision procedure when they relate to the Bank, findings of the tax investigation and other supervisory bodies in the bank supervision procedure; approving the operations of the Bank if such approval is required in the Articles of Association; deciding on amendments to the Articles of Association but only to the extent so as to adjust the wording of the Articles of Association to validly adopted decisions; adopting its own Rules of Procedure; and other competencies determined by the law or the Articles of Association.

The Supervisory Board gives its approval to the Management Board's long-term capital investments in other legal entities exceeding 1% of the bank capital, which is the sum of Tier 1 and Tier 2 capital in accordance with the applicable regulations; strategic business alliances; the Bank's corporate policy; the Bank's financial plan; organisation of an internal control system; the annual work plan of the Internal Audit Department; rules of the Internal Audit Department; conclusion of any legal transaction that, in consideration of the overall exposure of the Bank, would result in the Bank's large exposure to an individual customer; conclusion of any legal transaction due to which a large exposure of the Bank to an individual customer would equal or exceed 10% or any further 5% of eligible capital of the Bank in line with the act regulating banking, which is the sum of Tier 1 and Tier 2 capital in line with the applicable regulations; conclusion of any legal transaction which would result in the Bank's exposure to the members of the Management Board and/or the Supervisory Board, authorised officers of the Bank and parties related to these persons; conclusion of any transactions with persons in a special relationship with the Bank in line with the act regulating banking; dismissal of the head of the risk management department; appointment and dismissal of the head of the internal audit department; write-off of receivables over EUR 1 million a year to an individual person or persons who are considered a group of related persons in line with the act regulating banking; raising loans, issuing bonds or subordinated debt instruments for every such assumed liability exceeding 25% of the book-value capital as well as to other matters stipulated by the law or the Articles of Association.

The Supervisory Board adopts resolutions at its sessions. The work of the Supervisory Board is performed in accordance with the Rules of Procedure of the Supervisory Board. The quorum of the Supervisory Board is constituted if a majority of members is present at a session. The decisions are adopted according to the majority of votes cast by the members present. In the event of a tie, the Chairman holds the deciding vote.

Supervisory Board Committees

The Supervisory Board forms committees as its consultative bodies. In line with the act regulating banking, the Bank set up four committees consisting of only the members of the Supervisory Board, whilst their manner of organisation and operation is governed by the applicable rules of procedure.

• **Audit Committee**

The duties of the Committee include in particular: a) monitoring the integrity of financial information provided by the Bank; b) monitoring the financial reporting process, preparing recommendations and making recommendations for ensuring its integrity and comprehensiveness; c) supervising and monitoring the effectiveness and efficiency of the internal governance system; d) assessing the drafting of the annual report; e) monitoring the statutory audit of annual and consolidated financial statements; f) cooperating with the auditor in conducting the audit of the annual report of the banking group; g) reporting to the Supervisory Board on the result of the statutory audit; h) reviewing and monitoring the independence of the auditor for the annual report of the banking group; i) participating in the identification of important audit areas and reviewing the frequency of auditing of financial statements; j) cooperating with the Internal Audit Department and monitoring its work; k) participating in the identification of important audit areas; l) being in charge of the auditor selection procedure and proposing a candidate to the Supervisory Board for auditing the annual report of the banking group; m) participating in the drafting of an agreement between the auditor and the Bank; n) monitoring the effectiveness and efficiency of the internal control system; o) monitoring or supervising the establishment of the accounting policies of the banking group; p) other duties as defined by the law, the Bank's Articles of Association, the guidelines of supervisory bodies or a Supervisory Board resolution.

• **Remuneration Committee**

The duties of the Committee include in particular: a) advising to the Supervisory Board and drafting proposals regarding general remuneration policy principles, reviewing the adequacy of the general remuneration policy principles and preparing recommendations for their implementation; b) performing professional and independent assessments of remuneration policies, practices and processes and on that basis developing incentives or recommendations to amend the existing remuneration policy as well as measures to improve the Bank's risk, capital and liquidity management; c) ensuring a regular, central and independent audit of remuneration policy and practices by the Internal Audit Department, the relevant corporate functions and other Supervisory Board committees as well as providing all the required information (reports) to the Supervisory Board; d) providing support to the Supervisory Board in establishing and implementing the remuneration system for the Management Board and other employees whose professional activities significantly affect the institution's risk profile; e) monitoring the remuneration of senior managers who perform the risk management and compliance functions; f) assessing the adequacy of the established policies and methodologies (mechanisms) of the remuneration system with respect to risk, capital and liquidity management, as well as assessing compliance with the business strategy, objectives, corporate culture, values and the long-term interest of the institution; g) assessing the achievement of performance targets and the need for ex-post risk adjustment, including the use of malus and clawback arrangements; h) reviewing various possible scenarios with a view to verifying the response of the remuneration policy and practice to external and internal events and testing the criteria used to determine the allocation and preliminary adjustments of variable remuneration on the basis of the results of realised risks; i) reviewing the suitability of an external consultant whose services are used by the Supervisory Board in determining the remuneration policies of the bank or other issues within the powers of the Committee; j) informing shareholders about remuneration policies and practices; k) actively engaging in the process of identifying employees whose work is of a specific nature; l) ensuring the participation of a member of the Risk Monitoring and Asset Liability Management Committee in the Remuneration Committee's meetings, and vice versa; m) other duties set out in the Articles of Association or a Supervisory Board resolution.

• **Nomination Committee**

The duties of the Committee include in particular: a) defining and preparing the fit and proper assessments of the candidates and members of the Management and Supervisory Boards and of the two bodies as a whole; b) making recommendations to the Supervisory Board regarding the selection of candidates for members of the Management and Supervisory Boards; c) defining the duties and conditions required for appointment to a Management Body function; d) setting a gender representation target for the gender that is underrepresented in both the Management Board and the Supervisory Board and formulating a policy on how to increase the number of representatives of the underrepresented gender in the Management Board and the Supervisory Board so as to achieve this target; e) evaluating at least once a year the structure, size, composition and performance of the Management Board and the Supervisory Board, and making recommendations regarding any changes; f) at least once a year assessing the knowledge, skills and experience of individual members of the Management Board and the Supervisory Board as well as bodies as a whole, and reporting thereon to the Supervisory Board and the Management Board; g) regularly reviewing the policy of the Management Board with regard to the selection and appointment of suitable candidates for members of senior management of the Bank and making recommendations regarding any changes; h) actively contributing to fulfilling the Bank's responsibility to adopt appropriate policies on fit and proper assessment of the members of the Management Board and the Supervisory Board; i) providing support in evaluating the work of the Management Board and preparing explanatory reasons for recalling individual members of the Management Board, when they occur; j) other duties set out in the Articles of Association or a Supervisory Board resolution.

• **Risk Monitoring and Asset Liability Management Committee**

The duties of the Committee include in particular: a) advising on the general current and future risk appetite and the risk management strategy of the Bank, b) reviewing the Bank's exposure to risks and verifying that the risk profile of the Bank is in accordance with the adopted risk appetite; c) monitoring the quality of the investment portfolio of the Bank and the adequacy of impairments and provisions formed; d) analysing the organisation and performance of risk management of the competent organisational parts of the Bank; e) reviewing the Management Board's reports on risks and asset liability management; f) reviewing and assessing the appropriateness in the drafting of documents governing risk underwriting, risk management and asset liability management; g) assessing the adequacy of the Bank's risk reporting as set out by the applicable regulations; h) monitoring the implementation of the risk management strategy and the policies for all relevant types of risks in the Bank; i) verifying that the incentives provided by the remuneration system take into account the risks, capital, liquidity, and the probability and timing of the Bank's income, with the aim of formulating prudent remuneration practices and policies; j) actively engaging in the process of identifying employees whose work is of a specific nature; k) ensuring the participation of a Committee member in the Remuneration Committee meetings, and vice versa; l) verifying that the prices of products are fully compatible with the Bank's business model and risk management strategy, and drafting corrective action proposals; m) preparing recommendations to the Supervisory Board regarding the implementation of the risk management strategy and related policies; n) other duties as defined by the law, the Bank's Articles of Association or a Supervisory Board resolution.

The composition of the Supervisory Board and its committees in 2018 is presented in Appendix 3 of the Corporate Governance Statement.

Activities of the Supervisory Board and its committees in 2018

	Number of regular sessions	Number of extraordinary sessions	Number of correspondence sessions
Supervisory Board	10	2	1
Audit Committee	11	0	0
Risk Monitoring and Asset Liability Management Committee	11	0	0
Nomination Committee	11	0	0
Remuneration Committee	8	0	0

The data on the remuneration of the Supervisory Board and its committees in 2018 are disclosed in Appendix 4 of the Corporate Governance Statement.

Diversity policy

Taking into account the diversity requirements within the management body, the Bank aims to ensure appropriate gender balance, education, professional experience and expertise, while striving for the management body to have all the relevant knowledge, experience and skills required for an effective performance of the Bank's management and supervisory functions. In October 2018, the Diversity Policy of the Management Body of Abanka d.d. was adopted, which sets (i) the criteria for management body diversity, (ii) the selection procedure of candidates for the members of the management body, and (iii) fit and proper assessment of the management body. Based on the defined elements of management body diversity, the Bank seeks to achieve the objective of effective performance of the management and supervisory functions.

The goal is to ensure such a composition of the management body, whose members:

- have different types of education acquired based on the applicable educational programmes;
- have a diverse professional profile, i.e. work experience and skills from different fields of expertise, which are necessary for an in-depth understanding of the Bank's activities and risks to which the Bank is exposed; and
- are representatives of both genders of different ages: a member of the management body is selected between a candidate who fulfils the fit and proper criteria and a candidate of the underrepresented gender, explaining the choice made. If the list of candidates of both genders of different ages is too short, the principle of diversity may be ignored in order to ensure the smooth functioning of the management body.

In periodic/annual fit and proper assessment of the management body or in the case of changed circumstances, the Nomination Committee checks the fulfilment of objectives with regard to the diversity in the composition of the management body and reports to the Supervisory Board.

The Committee assesses in particular the following:

- the diversity of the body, which ensures professional and independent participation of the body in setting the objectives, strategies and policies of risk underwriting and management;
- whether the body enjoys the trust of the shareholders, the supervisory/management body, other stakeholders and supervisory institutions;
- whether the body is a strong collegial body, in which decisions are taken jointly despite different views;
- whether the body keeps updated on innovations in governance and the fields of expertise required for performing the function in the Bank;
- whether the body undertakes training with the aim of developing and maintaining an adequate level of expert knowledge of the Bank;
- whether the body cooperates with the Supervisory Board or the Management Board in a transparent manner;
- whether the selection process of candidates for the members of the Management and Supervisory Boards is sufficiently clearly defined and implemented in accordance with the set criteria;
- whether there are members on the body who have appropriate banking knowledge and experience;
- the implementation of the succession concept;
- performance of the management body; and
- efforts to achieve an appropriate gender and age balance in both the Management Board and the Supervisory Board and the fulfilment of other requirements set out in the Diversity Policy of the Management Body of Abanka d.d.

When assessing or evaluating the management body and the committees in terms of diversity, the Nomination Committee analyses the following criteria:

- gender,
- age,
- education,
- work experience (relating to the business activity and other) and banking knowledge.

According to the analysis performed in 2018 and presented in the Joint Periodic Assessment Report, the Diversity Policy is properly implemented and taken into account in the composition of the management body. During the analysis in 2018, the Bank set up an accompanying maturity model with target values for individual content items. The target values are set for the 2019–2021 period and will be regularly monitored in the context of periodic fit and proper assessments of the management body. This system provides retrospective comparability of assessment, as well as regular monitoring of progress and improvements.

The diversity policy is publicly accessible and published in its entirety on Abanka’s website at http://www.abanka.si/.

Corporate integrity

The Bank's guiding principle is lawful, professional, ethical, safe and diligent business, which it implements by complying with the applicable regulations, standards, codes, best practices and other rules of the financial and banking sector. In order to ensure a stable governance arrangement, the management body adopted the Code of Business Ethics. The Code not only sets the standard of Abanka’s corporate culture based on its corporate values but also defines the conduct of the members of the management body and other employees in business or personal relations with the customers, co-workers, shareholders, business partners and the natural and social environment (the stakeholders).

The corporate integrity system consists of the rules of conduct, arising from the Code and defining the management of various types of risks such as the risk of unlawful operations, conduct contrary to the interests at all levels of decision-making and operation, the different types of fraud, employee harassment and mobbing, money laundering and terrorist financing, abuse of all kinds of confidential information, non-transparent and inappropriate selection of outsourcers, improper handling of consumers, market abuse, inadequate information about the performance and other.

The compliance function is integrated into the corporate integrity system so as to develop and implement the compliance programme, including the provision of advisory services and training and the identification, monitoring and assessment of risks in this area. On the basis of the self-assessment, the general annual assessment on the state of corporate integrity was made.

All employees are familiar with the Code of Business Ethics; it is published on the intranet portal and on the website of the Bank. Employees can report any detected violations to their superiors or using the internal electronic reporting system (to report infringement, loss events or incidents). The Bank ensures any employee submitting such a report that no retaliatory measures will be taken against them as a result.

Abanka d.d. is committed to further strengthen its corporate governance and raise the corporate culture.

The Corporate Governance Statement is published on Abanka's website at http://www.abanka.si/.

Ljubljana, 5 March 2019

Management Board

Jože LENIČ
President of the Management Board

Matej GOLOB MATZELE
Member of the Management Board

Matevž SLAPNIČAR
Member of the Management Board

Supervisory Board

Marko GARBAJS
Chairman of the Supervisory Board

Appendix 1: Composition of the Management Board in 2018

2018

Management Board	Function	Area of work	First appointment to the office	Termination of office	Year of birth	Education	Professional profile	Membership in supervisory bodies of non-related companies
Jože Lenič	President of the Management Board	Compliance Department	17 January 2011		1965	Master of Economic Science	Management, corporate governance, compliance, legal affairs, human resources and organisation, audit	Bank Association of Slovenia (ZBS), SB Member
		Internal Audit Department				BA in Geography and Geology		
		Legal Office						
		Personnel and Organisation Department						
		Corporate Communications Department						
		Financial Markets Division						
		Procurement and General Affairs Department						
		Coordination of work with the regulator and supervisory bodies						
		Coordination of subsidiaries						
Matej Golob Matzele	Member of the Management Board	Corporate Banking Division	28 December 2015		1972	BSc in Economics	Management, front office, development of products and services, marketing and marketing communications	Bankart d.o.o., Member of the Supervisory Board, British-Slovenian Chamber of Commerce, Member of the Supervisory Board
		Retail Banking and Small Business Division						
		Development and Marketing Department						
Matevž Slapničar	Member of the Management Board	Risk Management Division	12 June 2017		1969	Master of Economic Science	Management, risk management, IT, finance, back office	/
		Finance Division						
		Information Technology Division						
		Back Office Operations Divisions						
		Custody and Administrative Services						

Appendix 2: Remuneration of the Management Board in 2018

2018

First and last name	Function	Fixed remuneration – gross	Variable remuneration – gross	Deferred remuneration	Termination payments	Benefits	Clawback	Total gross	Total net
		1	2	3	4	5	6	1+2+3+4+5+6	
Jože Lenič	President of the Management Board	129,036.96	6,387.34	-	-	17,259.04	-	152,683.34	57,593.18
Matej Golob Matzele	Member	126,655.60	6,273.80	-	-	9,541.60	-	142,471.00	63,919.70
Matevž Slapničar	Member	126,812.51	3,659.72	-	-	9,158.18	-	139,630.41	60,488.51
Aleksander Vozel[2]		-	1,568.45	-	-	-	-	1,568.45	1,221.82
		382,505.07	**17,889.31**	**-**	**-**	**35,958.82**	**-**	**436,353.20**	**183,223.21**

1 The table does include cost reimbursement, insurance premiums (SVPI) and other rights under the agreement.
2 Management Board Member until 31 March 2017.

Appendix 3: Composition of the Supervisory Board and its Committees in 2018

2018

First and last name Function	First appointment to the office	Termination of office in 2018	Attendance of the SB sessions according to the total number of sessions in 2018	Gender	Nationality	Year of birth	Education	Professional profile	Membership in other companies (executive and non-executive posts) in 2018
Marko Garbajs									
Supervisory Board, Chairman	04 October 2014	expiry of term of office on 4 October 2018 and reappointment on 5 October 2018	100%	M	SLO	1975	MSc in Economics	Management, management of capital investments	GRIFFON&ROMANO S.P.A., Director until 19 December 2018, as of 20 December 2018 serves as a non-executive president of the management body INOXPOINT, Director until 19 December 2018
Nomination Committee, Chair until 4 September 2018, Member as of 5 September 2018	25 February 2016		100%						
Risk Monitoring and Asset Liability Management Committee, Member	13 October 2014		100%						
Melita Malgaj									
Supervisory Board, Vice Chair (since 25 February 2016)	02 October 2015		92.3 %	F	SLO	1971	BSc in Economics	Management and organisation, management of capital investments	Slovenski državni holding d.d., Director of Tourism and Economy Management Department
Nomination Committee, Member until 4 September 2018, Chair as of 5 September 2018	11 November 2015		100%						
Audit Committee, Member	11 November 2015		100%						
Remuneration Committee, Member	10 July 2018	04 September 2018	100%						
Alenka Vrhovnik Težak									
Supervisory Board, Member	08 October 2015		92.3%	F	SLO	1968	Master of Science in Business and Organisation	Management, international and strategic finance, court-appointed expert witness in economics and finance	VTT, storitve z dodano vrednostjo d.o.o., Authorised Officer and Financial Adviser until 30 September 2018, as of 1 October 2018 acts as a Financial Adviser Sodno izvedeništvo in svetovanje, Mag. Alenka Vrhovnik Težak, Sodna izvedenka za ekonomijo - finance, s.p.
Remuneration Committee, Member, Chair (as of 10 November 2017) until 9 July 208, and Member as of 10 July 2018	11 November 2015		87.5 %						
Audit Committee, Member	25 August 2016	08 October 2018	100%						
Risk Monitoring and Asset Liability Management Committee, Chair	11 November 2015		90.9%						
Rok Pivk									
Supervisory Board, Member	13 May 2016		92.3%	M	SLO	1972	BSc in Economics	Management, investment banking and treasury	Triglav Osiguruvanje A.D., Skopje, Executive Director Skupna pokojninska družba d.d., SB Member until 30 August 2018
Remuneration Committee, Member until 9 July 2018, Chair as of 10 July 2018	10 November 2017		87.5%						
Audit Committee, Member	01 June 2016		90.9%						
Dejan Kaisersberger									
Supervisory Board, Member	28 February 2017		92.3%	M	SLO	1979	BSc in Economics	Management, banking and finance, risk management	SIDG, d.o.o., Director of Finance, Accounting and Controlling
Nomination Committee, Member	31 August 2017		100%						
Audit Committee, Chair	13 March 2017		90.9%						
Risk Monitoring and Asset Liability Management Committee, Member	13 March 2017		81.8%						
Varja Dolenc									
Supervisory Board, Member	31 July 2018		100%	F	SLO	1971	BSc in Economics, MSc in International Securities, Investment and Banking	management, financial markets, front office operations, knowledge of the domestic banking environment and the internal organisation of the Bank	Union hoteli d.d., Ljubljana, Director of Procurement and Real Property Management
Remuneration Committee, Member	05 September 2018		100%						
Risk Monitoring and Asset Liability Management Committee, Member	05 September 2018		100%						
Miha Košak									
Supervisory Board, Member	22 September 2018		100%	M	SLO and UK*	1968	Master of Business Administration (MBA), Master of Arts in Economics of the European Community (MA)	international knowledge of the banking system, financial markets and investment banking, knowledge of the internal organisation of the Bank, corporate governance	Fraport Slovenija d.o.o., Member of the Advisory Committee; Independent Consultant, Independent Consultant; Emona Capital LLP, London, Adviser; Elan Inventa d.o.o., Member of the Strategy Committee; Šiaulių Bankas, Vilnius, Lithuania, Member of the Supervisory Board; The British Slovenian Chamber of Commerce, London, UK/Ljubljana, Slovenia, Member of the Management Board
Audit Committee, Member	09 October 2018		100%						
Bernarda Babič									
Supervisory Board, Member	01 January 2018	05 July 2018	100%	F	SLO	1966		financial markets, accounting, treasury, knowledge of the domestic banking environment	Slovenske železnice, d.o.o., Assistant to General Director; Terme Olimia d.d., Chair of the Supervisory Board; Telekom Slovenije, d.d., Vice Chair of the Supervisory Board
Risk Monitoring and Asset Liability Management Committee, Member	01 January 2018	05 July 2018	100%						
Audit Committee	01 January 2018	05 July 2018	100%						
Peter Merc									
Supervisory Board, Member	11 October 2017	09 July 2018	83.3 %	M	SLO	1983	PhD	Management, banking and financial law, digitisation, legal advice in IT	Lemur Legal d.o.o., Authorised Officer until 8 March 2018; Pravno, poslovno in finančno svetovanje Merc, Peter Merc, s.p.
Remuneration Committee, Member	10 November 2017	09 July 2018	75 %						
Risk Monitoring and Asset Liability Management Committee, Member	10 November 2017	09 July 2018	100%						

*citizenship of the United Kingdom of Great Britain and Northern Ireland

All members of the Supervisory Board are independent and no conflict of interest existed.

Appendix 4: Remuneration of the Supervisory Board and its Committees in 2018

2018

First and last name	Function	Basic SB payment – gross	Attendance fees for the Supervisory Board and committees – gross	Total – gross	Total – net*	Travel expenses – net
		1	2	1+2		
Bernarda Babič[1]	Member	11,552.42	4,070.00	15,622.42	11,270.97	–
Varja Dolenc[2]	Member	6,831.99	2,200.00	9,031.99	6,488.67	–
Marko Garbajs	Chairman of the Supervisory Board	31,427.08	8,140.00	39,567.08	28,696.94	–
Dejan Kaisersberger	Member	28,125.00	9,625.00	37,750.00	27,375.42	1,010.63
Miha Košak[3]	Member	3,419.35	770.00	4,189.35	2,659.22	3,771.44
Melita Malgaj	Vice Chair	25,023.85	8,305.00	33,328.85	24,159.89	–
Peter Merc[4]	Member	13,669.35	3,850.00	17,519.35	12,741.83	–
Rok Pivk	Member	23,235.89	6,886.00	30,121.89	21,827.36	3,082.82
Blaž Šterk[5]	Member	1,875.00	495.00	2,370.00	1,723.70	–
Alenka Vrhovnik Težak	Member	28,719.76	9,185.00	37,904.76	27,487.87	620.61
		173,879.69	**53,526.00**	**227,405.69**	**164,431.87**	**8,485.50**

* The amount paid to an individual's account as remuneration after income tax prepayment, which does not take into account a potential subsequent surcharge of prepayment.

SUSTAINABLE DEVELOPMENT AND CORPORATE SOCIAL RESPONSIBILITY

As the foundation of its success, Abanka identified the partnership with all its stakeholders – employees, customers, suppliers, partners and shareholders as well as a positive attitude towards the social and the natural environment. The Bank aims to build long-term relationships with all its stakeholders based on respect, care, honesty, trust and cooperation. This is a strong basis for its corporate social responsibility. As a responsible bank integrated in its environment, Abanka is aware of the many challenges facing the modern society at all levels. The shocks witnessed over the past decade strengthened the Bank's belief of not only how much interdependent we are but also that everyone should bear a part of the responsibility and contribute to the broader prosperity. Abanka therefore sees its future in the context of sustainable development, in which the economic, social and environmental aspects are integrated with the temporal aspect, which considers future generations.

Sustainable banking means carrying out banking operational and business activities, with conscious consideration for the environmental and social impacts of those activities. This means that environmental, social and governance (ESG) criteria are integrated into traditional banking. Thus far, capital market decisions were based on a two dimensional risk and return analysis. In the new era of sustainable banking, they are based on three dimensions: risk, return and impacts.

Abanka seeks to implement sustainable banking both in its internal daily operations (in terms of how it manages its branches, human capital, costs, opportunities, risk exposures, etc.) and its activities relating to external interactions with its customers and the types of projects it funds. The Bank will continue on its path of sustainability, proactively expanding it with the opportunities offered by the environment.

THE KEY CHALLENGES OF SUSTAINABLE DEVELOPMENT AND CORPORATE SOCIAL RESPONSIBILITY

The dynamic banking environment is impacted by many strong forces: specific and rising customer expectations, extremely rapid technological changes, new regulatory requirements, demographic, social, climate and other changes. Non-traditional or non-banking players are entering the traditional banking market and defining the established order anew. In the wider social environment, value and behaviour patterns are changing, with the prevailing characteristic being that trust among people and in the institutions is low. In such an environment, banks cannot be passive and operate under the existing business models. Moreover, banks should not only respond to today's challenges but should also introduce innovations in several areas and should transform themselves for the future.

Abanka carefully analyses the banking and the broader social environment and proactively responds to the necessary changes by following its vision of becoming the first bank in Slovenia according to the choice of customers, employees and investors. Customers are in the very centre of all its activities. In relation to digitalisation, Abanka has always set ambitious goals, which it has effectively pursued. In the future, the field of digitalisation will be further developed and strategically redesigned. This does not only involve responding to the challenges of fintech and big tech but changing these processes to the Bank's competitive advantages and market power. By integrating technological changes taking place at an unprecedented speed, the aim is to ensure long-term sustainability of the Bank's business model. Banks used to invest in the security and resilience of their digital systems, but did not focus much on optimising user experience (including social media). This is one of the key challenges today. The Bank is aware of the responsibility not to impair customer security (cyber security in particular) through innovative changes. Therefore, its cooperation with regulatory policy-makes is essential in order to ensure that regulations are fair for all.

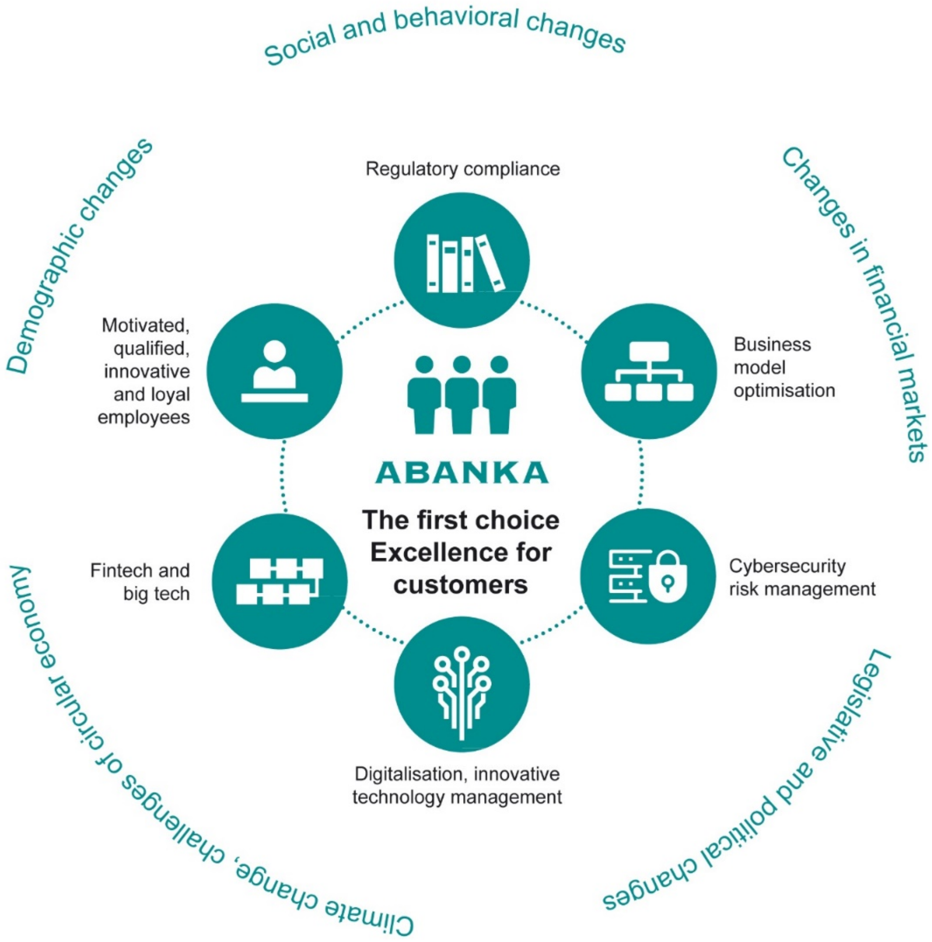
Acceleration of digital transformation is one of the Bank's strategic programmes, the aim of which is to be and to remain a technologically advanced bank with innovative solutions so as to retain the existing and attract new customers as well as to find new sources of income by adding modern sales channels.

In the context of speeding up digital transformation, the Bank focuses both on building a digital organisational culture as well as creating a collaborative and open work environment. All employees are included in the digitalisation process so as to together build a better Abanka of the future. The Bank is aware that it is vital to keep track of the changes and development trends in banking, financial markets and the business world.

We are living in a digital age where it is understandable that even the work environment is adapting to the zeitgeist. In 2018, several changes were made to adapt the work environment to the modern age. In the first half of the year, Abanka implemented a new communication tool for all employees – Skype and a new platform – Live video downloads, which allows the Management

Board to address all employees directly and live. During the live feed, employees can ask questions and immediately receive answers.

Sustainable change management in Abanka



By using a customer-focused approach, the Bank actively co-manages the following areas: regulatory compliance, digitalisation, innovative technology management, cyber risk management, fintech and big tech, and strategic management of human resources.

Abanka is aware that long-term sustainable growth in banking is only possible by radically moving away from the established way of thinking about the sale of traditional banking products and by truly focusing on the customer. The growing fintech ecosystems, which focus on the customers' user experience and which were initially perceived as a threat by banks, may also provide an opportunity to better meet and exceed customer expectations. Digital technology is only a part of the solution. The main goal is to achieve organisational agility of the Bank, which is only possible with a continuous process of innovation, excellent talent management and strategic partnerships (particularly in data collection, data analytics and cognitive technologies) in the wider ecosystem providing excellent customer solutions.

The management of sustainable challenges and risks and corporate social responsibility is based on the business strategy of Abanka and the Code of Business Ethics, which was approved by the Supervisory Board on 23 February 2017. The Code of Business Ethics sets the conduct of the members of the management body and the employees of the Bank in business or personal relations with the customers, co-workers, shareholder(s), business partners and the natural and the social environment. The management of sustainable development and corporate social responsibility is the responsibility of the Management Board, who integrates the cooperation of all areas of the Bank and the employees in accordance with their respective powers and responsibilities in order to implement the set objectives.

STAKEHOLDER RELATIONS MANAGEMENT

Respecting the legitimate expectations of everyone involved in the business processes was defined as the basis of Abanka’s ethical stance in its Code of Business Ethics.

Abanka's strategic stakeholders are:
- employees,
- customers,
- owners,
- regulators,
- suppliers,
- other interested publics (the media, the expert public, business associations, civil initiatives, etc.).

Based on two-way communication and research, key areas of interest, communication content and communication channels were defined for every stakeholder group. The focus in communication is on two-way and open communication channels. The aim is to adapt communication to every stakeholder group separately by following the principles of materiality, updatedness and transparency.

In communication, the following objectives are pursued among the stakeholders:
- consolidation of reputation and credibility of the Bank;
- awareness of the identity and competitive advantages of the Bank;
- building of confidence in the Bank;
- positioning of Abanka as the first bank in Slovenia according to the choice of customers, employees and investors.

With respect to communication, the Bank complies with the applicable law. Within the prescribed deadlines and in the prescribed manner, the Bank informs its owners and other interested publics about its performance and any significant business events.

The key stakeholders, interests, communication content and communication channels

Stakeholders	Interests, communication content	Communication channels
Employees, trade unions	Satisfied, loyal, motivated, innovative employees Talent integration Transfer of skills and experience between generations Good and open relations Good business results	• Intranet • Corporate communications e-mails • In-house newspaper “A View from the Inside” • Aideja – an idea and improvement management system • Anovičnik • Events for employees • Live – address by the Management Board • Skype – a digital communication channel • Personal interviews • Joint meetings, colleges • Annual interview, setting of objectives • Satisfaction and commitment survey
Owner	Achievement of business objectives Fair relations Long-term development of the Bank	• General Meeting of Shareholders and Supervisory Board sessions • Annual and interim reports • Other business documents
Investors	Business performance of the Bank and its reputation among financial institutions	• Reports and other business documents • Online portals
Regulators	Achievement of compliance	• Mutual information • Supervisory performance reviews • Performance reports
Customers – natural persons and legal entities	Maximum possible fulfilment of wishes and needs Building and consolidation of good business relations Achievement of common business and sustainability objectives	• Satisfaction and reputation survey • Abaklub – customer loyalty programme • Abadenarnica (a mobile wallet) • Personal communication – by telephone and via electronic, personal and group meetings • Printed matter • Electronic presentations and other presentation material • Advising • Personal interviews • Expert meetings with entrepreneurs • Receptions for business partners
Business partners, suppliers	Establishment of fair business relationships	• Personal interviews and meetings • Websites • Printed matter • Corporate gifts • Professional meetings
Expert and business publics	Formation of expert opinions and relations Strengthening of business relationships, economic growth and social welfare Prevention of unfair competition	• Website • Round tables • Expert workshops • Annual report • Membership in professional associations and interest groups
Community at large (children, the general public)	Financial literacy of children Raising awareness about the digital culture and the virtual world Historical heritage of banking in Slovenia	• Children's museum Herman's Den – the permanent exhibition • Puppet shows for children • Vesela Šola (Cici) competition • Financial school for young people • Abasvet • Facebook Abanka, Facebook Akeš • YouTube Abanka, YouTube Akeš • LinkedIn Abanka
Media	Credible information on the activities of the company Strengthening of the company reputation and prompt elimination of any communication noise	• Reports and press releases • Digital communication with the media • Up-to-date and honest answers to all questions • Monitoring and analysis of media publications

REPORTING ON SUSTAINABLE DEVELOPMENT AND CORPORATE SOCIAL RESPONSIBILITY – NON-FINANCIAL STATEMENT OR REPORT

In its Annual Report for 2018, Abanka discloses the information on its sustainable and socially responsible management in an integrated manner as in 2017. Sustainable and socially responsible management models and activities are based on the business policy of the Bank, the Code of Business Ethics and the sectoral policies of individual segments of management.

Disclosure of non-financial information in 2018 is also based on the requirements of the EU Directive on disclosure of non-financial and diversity information by certain large undertakings and groups, which were incorporated into the Slovene legal order in 2017 through the Companies Act.

The management report therefore contains the non-financial statement or report, which includes information relating to environmental, social and employee matters, respect for human rights, and anti-corruption and bribery matters.

The Bank's guiding principle is lawful, professional, ethical, safe and diligent business, which it implements by complying with the applicable regulations, standards, codes, best practices and other rules of the financial and banking sector.

Through continuous and comprehensive development, the Bank seeks both to increase business performance and to consolidate its reputation. Special attention is paid to the risks arising from corporate integrity, which include the risk of failure to respect (violation of) human rights and corruption and bribery risks.

The management body adopted the Code of Business Ethics, which not only sets the standard of Abanka’s corporate culture based on its corporate values but also defines the conduct of the members of the management body and other employees in business or personal relations with the customers, co-workers, shareholders, business partners, and the natural and the social environment (the stakeholders).

The Code is the basis for many policies and implementing regulations, which define in detail the management of risks of unlawful operations, conduct contrary to the Bank’s interests at all levels of decision-making and operation, the different types of fraud, employee harassment and mobbing, money laundering and terrorist financing, abuse of all kinds of confidential information, IT system abuse, non-transparent and inappropriate selection of outsourcers, improper handling of consumers, market abuse, inadequate information about performance and other.

In accordance with the applicable regulations, the Bank established stable internal governance, which includes: (i) a clear organisational structure with precisely defined, transparent and consistent internal relations in terms of responsibility; (ii) effective risk management processes for the risks to which the Bank is or could be exposed in its operations; (iii) adequate internal control mechanisms and (iv) appropriate remuneration policies and practices consistent with prudent and efficient risk management. Internal governance is proportionate to the nature, scope and complexity of the risks arising from the business model of the Bank and the business activities performed by the Bank.

The compliance function is integrated into the corporate integrity system so as to constantly develop and implement the compliance programme, including the provision of preventive advisory services and training as well as the identification, monitoring and assessment of risks and incidents in this area. On the basis of self-assessment, the general annual assessment on the state of corporate integrity in the Bank was made. In view of the established internal governance elements, no corporate integrity violations were reported or identified.

The Bank adequately manages any incidents relating to the (potential) infringement of internal regulations, internal documents, codes, standards, agreements or good business practices. The competent persons or functions in the Bank detect or identify an incident (i) through the disclosure made by the person who identified such circumstances in relation to them, (ii) through reporting (it can be anonymous) of employees using the internal incident reporting system or through reporting of customers using the complaint system, or (iii) through identification in internal control procedures (either in the context of business functions or internal control functions). The competent persons, bodies or functions address such events by taking appropriate action in order to prevent further occurrence and eliminate any negative consequences.

All employees are familiar with the Code of Business Ethics and other internal documents, which make up the corporate integrity system. They are published on the intranet portal, while the Code is also available on the website of the Bank. The Bank ensures any employee submitting such a report that no retaliatory measures will be taken against them as a result.

In preparing the content of non-financial information disclosure, the methodology of the GRI standard was used as the basis. When selecting the content, the Bank took into account the sustainable context, the materiality of individual areas and stakeholder engagement. The content is presented in such a way so as to ensure the balance, comparability, accuracy, clarity and reliability of the data.

The GRI reporting standard allows the Bank to expand the measurement and reporting on its sustainable and socially responsible management as needed. The Bank is committed to take long-term strategic steps in this area.

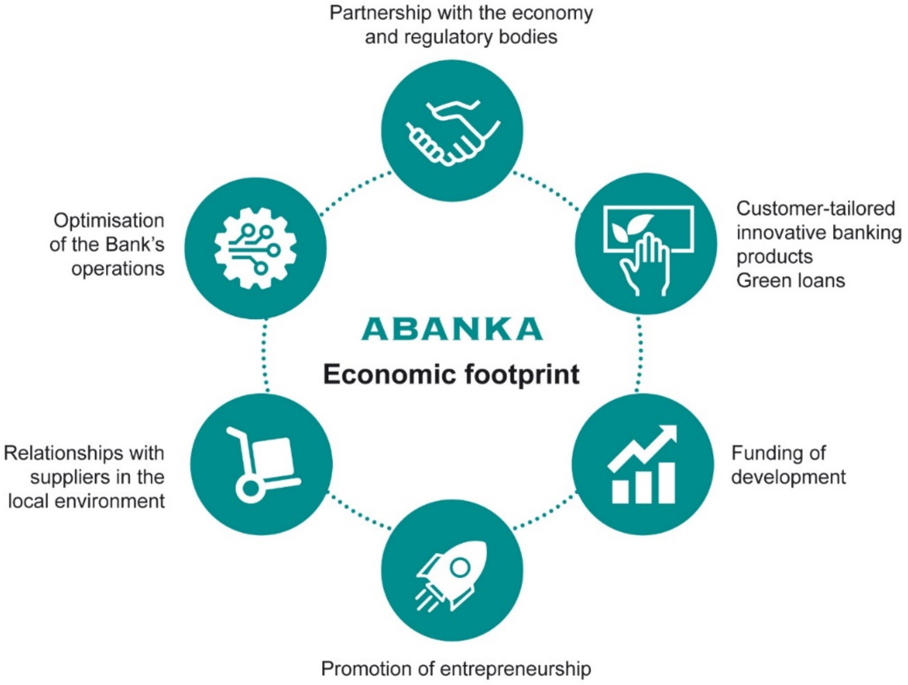
This report is transparent and accurate based on the data currently monitored within the Abanka Group. As Abanka d.d. is the parent company of the Abanka Group, the majority of non-financial disclosure relates to the Bank.

The sustainability content and the corporate social responsibility content are integrated by the Corporate Communications Department, which is also responsible for reporting on sustainable development and corporate social responsibility of Abanka. All divisions of the Bank contributed the relevant data for the report.

ECONOMIC FOOTPRINT

In accordance with its vision of becoming the first Bank in Slovenia according to the choice of customers, employees and investors, Abanka carefully manages its economic footprint in the context of sustainable development and corporate social responsibility. In its governance model, the Bank included the partnership with the economy and regulatory bodies, customer-tailored innovative banking products (among them the special offer of housing and consumer loans), funding of development, promotion of entrepreneurship, relationships with suppliers in the local environment and optimisation of the Bank's operations.

Economic footprint of Abanka



Partnership with the economy and regulatory bodies

As an active member of the Bank Association of Slovenia, Abanka contributes to the development of the banking and the financial system. The Bank is a member of the Slovene-American and the Slovene-British Chamber of Commerce, while its employees are active members of various professional associations, thereby contributing to the development of expert knowledge, integration and strengthening of the economic environment.

Customer-tailored products

The Bank strives to meet all customer expectations, which is why it not only develops banking services that ensure a better anticipation of customer needs but also designs customer-tailored and easy-to-use services, accessible anytime and anyplace. Particular attention is paid to both the promising and the vulnerable customer groups. Young people and retired persons have the possibility of using the banking products under special terms and conditions. In accordance with its focus on sustainable development, the Bank promotes environmentally friendly investments under favourable lending terms and conditions – a special offer of housing and consumer loans.

Funding of development

In relation to dedicated long-term funding sources, the Bank has cooperated with SID Bank for several years. Last year, Abanka received from SID Bank long-term sources that provide funding for a wide range of projects in accordance with the following programmes:

- funding of the development of a competitive economy and internationalisation;
- funding of the development of the knowledge-based society and innovative entrepreneurship;
- funding of the development of environmentally friendly society and production;
- funding of regional and social development.

Promotion of entrepreneurship
Abanka promotes entrepreneurship and innovative way of thinking. For this purpose, the Bank organises interactive events for various stakeholders, at which entrepreneurial ideas and projects are encouraged. Among other things, an event on the topic "The Art of Technological Balance" was organised for corporate customers, which was modelled after TEDx events.

Furthermore, a series of educational business events was co-organised for micro-enterprises and sole proprietors in Ljubljana, Celje, Maribor, Koper and Nova Gorica. The participants learned about correctly developing a financial plan, applying for tenders in practice, asset management, and the advantages of electronic and mobile banking for enterprises and entrepreneurs.

Supplier relationships
Abanka mostly cooperates with Slovene companies, which means that it stimulates the local environment. Because its business activity is dispersed throughout Slovenia, local suppliers are also considered when seeking suppliers. In 2017, the Bank gradually began to change its purchasing concept, which was realised in its internal documents. The Bank aims to centralise purchasing to the greatest extent possible and to ensure that the purchasing process is transparent and complies with the prescribed procedures. In the selection of suitable suppliers, several criteria are taken into account: in addition to the pricing conditions, the references, the business relationship, the quality of services provided, the supplier's credit rating, etc. Purchasing functions as a management system by cost type. Supervision of purchasing is centralised. The monitoring of achieved costs is performed in the framework of the cost group, based on which cost administrators report on any deviations. Purchasing and monitoring of purchasing in relation to investments in buildings and equipment are carried out by the Procurement Department, which is directly subordinated to the Management Board. The Purchasing Department thus manages the purchasing process of fixed assets and investments and is in charge of supplier management.

Abanka implements its corporate social responsibility also through cooperation with the suppliers employing people with disabilities. In 2017, the Bank transferred its mailroom services to an outsourcer, which is a social enterprise. Through this, the Bank optimised its labour costs and began to set the foundations for the renovation of the mailroom with a view to gradually transition to the digitalisation of incoming mail.

Optimisation of operations
The Bank promotes seeking the best solutions and introducing beneficial changes at all levels of its operations. Innovation is the guideline when introducing technological innovations so as to improve both its services and its business processes. In 2019, the Bank will continue with its restructuring, the optimisation of its operations and acceleration of digital transformation.

SOCIAL FOOTPRINT

In managing its social footprint, Abanka gives priority to sustainable relationships with its customers and employees. Being a socially responsible bank, its mission is to increase financial literacy and give financial advice. Benefiting from its rich 150 years of banking tradition, the Bank considerably contributes to the preservation of cultural heritage, which is closely linked to the heritage of banking in Slovenia. As a bank that considers state-of-the-art digital solutions as one of its key competitive advantages, it enables the general public to experience the digital world. Abanka's ethical attitude towards all stakeholders requires that it fosters open relationships with all segments of the interested public.

Abanka's social footprint

Corporate volunteering in Abanka

Corporate volunteering is a very effective way of integrating the company into the environment in which it operates. The Bank is aware of the problem of the socially disadvantaged in the society and is willing to help. By taking part in the volunteering programme, we do something good and useful and contribute to an even better and friendlier society. Abanka is a bank of friendly people, and by helping those who need it most, it shows its friendliest face.

In 2018, a strategic and comprehensive approach was taken to the corporate volunteering programme. In the context of the latter, Abanka's employees helped the Association of Friends of Youth Ljubljana Moste – Polje in cleaning Vila Šumica home in Kranjska Gora, cleaning their logistics premises, collecting food and hygiene products as well as gifts or packages for their Magic Winter project. In autumn, help was provided to the Local Development Foundation for Pomurje Region, which organised the #podarizvezek ("give a notebook") campaign together with the charity Helping with an Open Heart. In the campaign, all employees collected school supplies for school children from socially disadvantaged families.

Apart from that, Abanka's employees participated in the nationwide campaign Clean Up Slovenia, cleaned and painted the fence in Lipica, donated blood throughout the year across Slovenia and were given the opportunity to take part in the introductory training for volunteers held by the Slovene Philanthropy. The training costs were fully covered by Abanka.

Customer relationships

In customer relationships, the Bank aims to establish highly ethical and collaborative partnerships that meet or even exceed customer expectations. The desires and the perception of the Bank's services and its reputation among the existing and potential customers are measured each year in a special survey. Based on the results, special measures are taken.

In customer relationships, it is vital to provide timely, comprehensive and clear information about the Bank's services and operations so as to direct the customers to the best solutions tailored to their needs. The Bank consistently avoids any incomplete and therefore misleading information. It personally communicates with its customers via the range of communication channels (branch offices, online and mobile banking, info@, toll free number 080 and digital chat).

One of the very important communication channels is intended for communication of customer complaints, comments and compliments with regard to the quality of products or services. These are taken very seriously as they are an important part of the continuous improvement and development process. The Bank established a system for handling customer complaints. All employees are required to accept any customer complaint in a respectful and responsible manner, and submit it to the persons in charge in accordance with the complaint handling system. Customer complaints are handled by the Contact Centre, which is also responsible for providing information to customers.

The Bank prefers to settle any disputes out of court; if the customer is not satisfied with the Bank's final decision on the appeal or complaint or they did not receive a reply, they can file a request to the provider of out-of-court resolution of consumer disputes (ADR service provider) to initiate proceedings against the Bank's decision or action, i.e. either at the Bank Association of Slovenia or the European Centre for Dispute Resolution (ECDR).

With respect to physical and technical security, the Bank developed internal instructions and rules in compliance with the recommendations of the Bank Association of Slovenia regarding the physical security of banks and the applicable legislation. The Bank carries out regular inspections and supervision of the implementation of security, as well as training in robbery, burglary and internal and external fraud. Physical security is accompanied by fire protection, in the context of which the Bank implements the fire protection activities and measures prescribed by law.

Abanka also cares about the personal needs of customers in its premises. To this end, defibrillators (leased from and maintained by an outsourcer) were installed at two locations. Furthermore, additional measures are taken to prevent customer falls and injuries when accessing bank branches and while being inside the premises – removal of physical barriers and equipment which could pose a threat to customers' health, marking of uneven floors, etc.

Employee relationships

Human resource management in the Bank is regulated by the Human Resource Policy and other strategic human resource documents, which are together with the key human resource activities and objectives set out in greater detail in Section Employees.

In the staffing, recruitment and employee development procedures, as set out in the Human Resource Policy, everyone is given an equal opportunity, as this is the foundation for building an effective organisational culture, fostering respect for the values of the Bank and maintaining the Bank's reputation as a good employer in the social environment. Through its extensive branch network in Slovenia, the Bank provides employment opportunities for different staffing profiles in various regions across Slovenia. This means that local workers, including young generations, have the chance to find a job outside the major employment centres in Slovenia and thus stay in their local environment. Other employees work in the commercial buildings of the Bank in Ljubljana, Maribor, Nova Gorica and Celje.

The largest share (54.8%) of employees works in Central Slovenia and the lowest (9.6%) in Eastern Slovenia. The highest average age of employees is in the Celje region (48 years) and the lowest in Central Slovenia and Western Slovenia (45 years). The highest share of male employees was recorded in Central Slovenia (67.8%) and the lowest in Eastern Slovenia (10%).

Great care is taken to provide continuing development of employees and invest in their knowledge and skills, which is important from the point of view of the Bank and the individual; should the latter be without a job, they would have a competitive advantage in looking for work.

By awarding jubilee benefits, giving solidarity assistance, providing support to employees transitioning into open unemployment and awarding scholarships to the children of deceased employees, the Bank also takes care of those in a less advantageous situation.

A special emphasis is placed on employing young people, who bring fresh knowledge and skills to the Bank. To this end, in recent years, the Bank has cooperated with universities, enabled work placement to young people and casual work if necessary, and awarded company scholarships, with a view to link the needs of the Bank with promising young staff early on.

Employee structure
In recent years, no major changes have been seen in the age and gender structure of employees. The Bank has a high share of women among its employees as well as a quite high share of older employees, depending on the type of activity (particularly in the back office and the front office). The data on the average age and share of employees by gender for 2018 are presented in Section Employees.

In the context of the Human Resource Renewal Programme, various objectives were set such as: staff regeneration, intergenerational transfer of know-how and experience (intergenerational mentoring), training and learning tailored to different generations, acquisition of leadership skills for leading teams with a diverse generation structure, etc.

The employee educational structure has been improving from year to year; the share of employees with vocational education has been decreasing, while the share of employees with higher education and master's or doctor's degrees has been increasing. The educational structure of the Bank is presented in detail in Section Employees.

In the reporting period, 51 new employees were hired, of whom 37% were men and 63% were women. The average age of the new hires was 35 years. In line with the objectives of the strategic Human Resource Renewal Programme, most new hires were for front office positions, especially in Central Slovenia. The satisfaction and loyalty of employees is ensured with numerous additional measures described in Section Employees.

The Bank employs 20 disabled persons, of whom 15% are men and 85% are women. All are employed for an indefinite period, with 71% working part-time. Their average age is 51.8 years. Great care is taken that the employees with disabilities have appropriate working conditions and workload, which are consistent with the limitations of their category of disability.

Furthermore, employee incentive schemes are set up to reward and motivate the employees, which are described in greater detail in Section Employees.

In the reporting period, maternity and parental leave were used by 39 employees, while paternity leave was used by 20 employees. The right to part-time work due to child care was exercised by 30 employees.

Employee training
The Bank puts great emphasis on continuing education, professional and personal development and training of employees. Special attention was devoted to these activities, which is also reflected in the fact that the average number of training hours per employee in 2018 was 24 hours. All employees of the Bank participated in training.

The greatest attention in employee training was devoted to sales, marketing, development of leadership competencies and sales skills, and to upgrading banking and financial knowledge. Training in products, foreign language courses and learning how to use various IT tools represent a significant share of training held by the Bank. More information on employee training is presented in Section Employees.

Satisfaction measurement and organisational climate
Each year, the Bank measures organisational climate and employee engagement. In this way it identifies and monitors the factors affecting the climate, engagement and well-being of employees in the workplace. On the basis of the survey results, every year the Bank prepares and implements an action plan, which targets the areas where the results need to be improved. According to the 2018 survey results, the efforts of the Bank paid off as the general employee job satisfaction and engagement index increased compared to 2017; moreover, 10% more employees participated in the survey than in 2017.

Safety at work and recreation
In addition to the safety and health at work activities presented in Section Employees, in 2018 employees had the opportunity to participate in health promotion workshops, where they could learn how to improve their quality of life and how to more easily cope with everyday responsibilities. Regular health check-ups are scheduled for employees, care is taken that a sufficient number of employees are qualified to administer first aid and extinguish fire, ergonomic workplace arrangement is provided for employees based on their needs, and employees are encouraged to participate in sports activities in the framework of Abanka Sports Club and Mountaineering Club.

A low share of injuries at work, which has been declining in recent years, is maintained through a preventive approach. The number of injuries at work decreased in 2018 as there were only 2 injuries at work, which is one fewer than in 2017.

Internal communication

Abanka devotes a lot of attention to corporate communications. It manages the following communication tools: corporate communications e-mails, intranet sites, the in-house newspaper "A View from the Inside", Anovičnik and events for employees. In 2018, an employee satisfaction survey was conducted using internal communications tools. Based on the findings, the Bank adapted its activities to the employees' wishes and suggestions.

In internal newsletters, ecological awareness is regularly promoted by introducing a new "eco-challenge" in each issue, which encourages employees to adopt a healthy and eco-friendly lifestyle. Awareness and sustainability are the guiding principles followed when giving presents to the employees at an event organised for all employees of Abanka. They received an eco-friendly reusable shopping bag so as to promote using less plastic where this is not absolutely necessary.

Trade unions

Abanka constructively cooperates with both trade unions in the Bank and provides them with suitable conditions for their activities. By regularly meeting with the representatives of the trade unions, an ongoing dialogue is maintained and transparent information about all relevant HR topics is ensured. Furthermore, the Bank replies to all questions raised by the trade unions or individual employees of the Bank. Before the adoption of internal human resource documents, the Bank obtains the consent of the trade unions. The Bank gives an annual donation to both trade unions and takes part in giving New Year's presents to employees' children.

Abanka's clubs

The Bank's employees may join Abanka Sports Club and Abanka Mountaineering Club. Abanka provides financial support to both clubs.

The Bank remains in contact with its former employees who have retired by supporting two Abanka pensioners' associations.

Family-Friendly Enterprise

Abanka was the first among the Slovene banks to receive the Family-Friendly Enterprise certificate. The adopted measures are being consistently implemented while developing new ones, with an aim to facilitate work-life balance for employees. The relevant measures and actions are presented in detail in Section Employees.

Financial literacy and advice

Abanka has a long tradition of teaching financial literacy to children. In 2018, the Bank continued its long-term partnership with the children's museum Herman's Den, where a bank for children was created. In it, children are taught the basics of banking through fun and games.

The online advisory service offers advice to parents about money for children at different ages. In cooperation with puppeteers, the puppet shows for children entitled "Hedgehog gathers food" were again organised in 2018. Children were actively involved in the game, through which they learnt about saving. In the reporting period, the Bank actively participated in the Vesela šola and Cici Vesela šola projects and improved the digital banking literacy of secondary school students in the framework of the Autumn Financial School for Young People.

Cultural heritage

Abanka is proud of its 150-year tradition and is dedicated to the careful management of banking artefacts. Moreover, the Bank manages a rich collection of art works, especially paintings and several statues. Six buildings in which it provides its services are protected as cultural heritage (Hmeljarska 3 in Žalec, Krekov trg 6 in Celje, Braslovče 25 in Braslovče, Lapajnetova 47 in Idrija, Rozmanova 40 in Novo mesto, Partizanska 41 in Sežana). Through responsible management, the Bank contributes to the preservation of cultural heritage in several regions across Slovenia.

Development and opening up of the digital world

The Bank actively monitors technological development with the aim of not only designing advanced, digital solutions and customer-tailored products but also helping the general public in getting acquainted with the digital world through personal experience. In this way, the Bank will better know its customers, anticipate their needs and provide customer-tailored products. The aim will be to monitor new technologies in artificial intelligence, predictive buying, integration of devices into IoT (Internet of Things), augmented reality and other breakthroughs as well as to evaluate the possibility of integrating them into the services of the Bank. In 2019, the Bank will continue with the development of advanced channels and provide the option of advanced payment – development of Abamobi, Abanet and Abadenarnica.

Therefore, in 2017 the Bank created its own world – Abasvet, which contains virtual reality simulators. On Trdinova 4 in Ljubljana, anyone interested can personally experience the virtual world.

Support to the social environment and relations with the interested public

Abanka contributes to social, cultural, sports and other development through donations, sponsorships and other contributions. This is done by using transparent and documented procedures so as to prevent any personal or business conflicts of interest.

In 2018, the strategic focus of sponsorship was on corporate sponsorship of the programmes and projects under the auspices of the Scientific Research Centre of the Slovene Academy of Science and Arts (ZRC SAZU). Sponsorship of ZRC SAZU focused on the Fran.si platform and research work by Ivan Šprajc, the head of the Anthropological and Spatial Studies Research Programme, while part of the funds was allocated by ZRC SAZU to its other current projects.

In 2018, the Bank provided financial support for several projects, including the children's museum Herman's Den, the Veronika Award cultural project and sports activities (the Kladivar Celje Athletic Club, the Green Valley Marathon, skiing competitions on Rogla, the Abanka Sports Club).

Cooperation with the media is fair and transparent, and the Bank replies to the questions from the press in due time. Media publications are monitored on a daily basis and subject to an in-depth assessment. On the basis of an analysis, the Bank plans corporate communications and manages reputation risk.

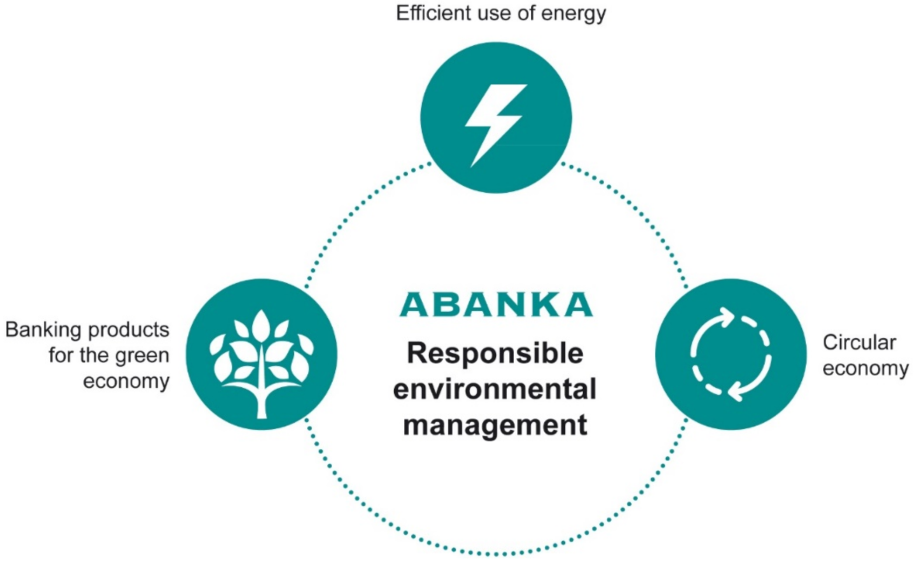
The general assessment of Abanka’s presence in the media in the year 2018 is positive.

ENVIRONMENTAL FOOTPRINT

In conducting its business operations, Abanka has an impact on the natural environment and that is why it actively manages its environmental footprint. The key elements of the impact on the natural environment and business economics include: efficient use of energy, circular economy and banking products for the green economy.

Abanka cares for the adequate protection of the natural environment with the following measures and activities:
- separate waste collection is provided for in all locations where utility service providers enable removal of separated waste;
- using a central collection point for waste electronic equipment, which is then handed over to authorised companies for further recovery; installing modern energy-efficient cooling/heating/ventilation systems in the business premises in accordance with the investment and major maintenance plan;
- using energy-efficient lighting (LED lamps).

Responsible environmental management



Efficient use of energy
With respect to an efficient use of energy, the focus is on two areas in particular: energy management of commercial buildings and the vehicle fleet.

The total floor area of the business premises for own use in Slovenia is 31,104.5 m^2, of which 29,286.5 m^2 are owned by the Bank and 1,818 m^2 are leased. In addition to these business premises, the Bank has 4,596.4 m^2 of non-core assets in its real property portfolio, for which buyers are actively sought. The geographical distribution of real properties for own use is as follows: 14,566 m^2 in Central Slovenia, 5,220 m^2 in Western Slovenia and 12,951 m^2 in Eastern Slovenia.

Renovations and major maintenance are carried out in accordance with the energy efficiency guidelines and the legal provisions relating to the construction of buildings. The Bank is installing modern systems of cooling/heating/ventilation with energy recuperation, such as LED lighting, air conditioners with a high COP, gas condensing boilers, heat pumps, heat recovery ventilation systems, energy-efficient construction/insulating materials and LED illuminated signs. Upgrades and maintenance are carried out in accordance with the investment and major maintenance plan, taking into account the estimated useful life of equipment and the economic/technical viability of replacement or upgrade.

In 2018, the cooling, heating and ventilation systems were upgraded in line with the investment and major maintenance plan, which included replacing worn-out equipment with new and energy-efficient equipment. The fitting of LED lamps to replace older bulbs continued, which significantly reduces power consumption due to higher efficiency. Energy-efficient systems will continue to be installed everywhere this is justified in terms of lower operating expenses and the level of investment in modern equipment.

In accordance with the house rules and instructions for an efficient use of energy in Abanka, all employees are required to rationally use the heating/cooling systems and to remember to switch off any electrical equipment not in use.

The Bank is gradually renewing its vehicle fleet by purchasing low CO_2 emission vehicles with a more efficient engine. Every year, a certain number of vehicles is included in the replacement plan based on a thorough analysis of the vehicle fleet and the fulfilment of the replacement criteria (consumption, costs, model year, etc.). In the reporting period, 3 cars or 6.5% of the vehicle fleet was replaced. In terms of environmental protection, the Bank is trying to reduce the number of rides of employees between locations through videoconferencing, which is available in large commercial buildings.

Circular economy

Abanka is aware of the importance of the circular economy, and therefore this concept is being gradually implemented at all levels of its operations. Separate waste collection is provided for in all locations. The Bank uses a central collection point for waste electronic equipment, which is then handed over to authorised companies for further recovery.

In large commercial buildings, special rooms for printing were arranged and the number of large printers was optimised (multiple users were connected to an individual device). These guidelines will continue to be implemented in 2019 with the aim of increasing control and consequently reducing paper consumption through controlled access to printers.

Abanka obtains quotes from the suppliers with a concern for the natural environment. When purchasing toners and cartridges, the Bank also cooperates with the suppliers offering renewable toners. The purchasing share of renewable toners at the Bank level is 10%. Through organised collection of used toners and cartridges, the Bank is trying to have a positive impact on the environment, and therefore this waste is collected in special waste separation bins. The collection is carried out by Bitea d.o.o. several times a year upon request.

Much attention is devoted to setting up a modern document management system. The introduction of e-pen in retail banking enables the processing of electronic documents. Paper documents are only provided for the needs of customers. Furthermore, instead of paper, modern document processing methods are used to transfer other documentation to the electronic archive.

In 2018, by applying these measures, paper consumption was reduced by 13%, toner consumption by 15.5% and the number of copies by 41%. In the reporting period, the volume of electronic document capture relating to lending operations increased. These types of documents account for a large share of all documents in the Bank.

Banking products for the green economy

Abanka expanded its range of products by including the products that promote a positive impact on the natural and the social environment. With a greater commitment of businesses to the green economy and of consumers to green consumption, this portfolio of banking products is expected to grow.

Management Board

Matevž SLAPNIČAR	Matej GOLOB MATZELE	Jože LENIČ
Member of the Management Board	Member of the Management Board	President of the Management Board

RISK MANAGEMENT

The operations of Abanka Group in 2018 focused on the activities relating to the redesign of risk management processes, methodologies and models. Special attention was paid to the upgrade of the risk appetite framework and recovery plan of the Group with the aim of ensuring better risk management. In the process of upgrading the risk appetite framework, the Group aligned and maximised the synergies of the previous and upgraded framework, which is defined at the main level in:

- Risk Management Strategy and Risk Appetite,
- Risk Management Limits,
- ICAAP and ILAAP Rules.

The Group established additional risk management methodologies and tools for credit and other risks, as well as made important updates and upgrades to internal risk reports. In 2018, the Group continued to comply with regulatory requirements and even took part in supervisory stress testing. The Group at all times adhered to the guidelines of the strategy to reduce non-performing exposures, thereby significantly reducing such exposures to the levels set in the strategic guidelines.

In the reporting period, the Abanka Group significantly upgraded its Risk Management Strategy and Risk Appetite and set clear risk management objectives, which are achieved by establishing appropriate procedures through key processes and a clear segregation of duties and powers. At the strategic level, the Group set the following risk management objectives:

- ensuring efficient and overall treatment of the risks which the Group encounters in the course of its business;
- setting the risk appetite of the Group and ensuring its compliance with the business model and business plans of the Group, taking into account its risk capacity and strategic analysis results;
- a timely identification and comprehensive overview of all relevant risks;
- design, maintenance and continuous upgrade of the system, which enables the Group not only to identify the deterioration of its financial situation or risk profile in due time but also to define the mitigation measures;
- clearly defined risk management duties and powers within the Group;
- conscious decisions regarding the optimisation of the risk profile and benefits.

In the reporting period, the Abanka Group significantly upgraded its Risk Management Strategy and Risk Appetite.

In order to achieve the set objectives, the Abanka Group adopted the following risk management principles:

- building and continually improving the risk-aware culture as one of the key business elements of the Group;
- clearly defined duties and powers throughout the whole risk management process in the Group;
- ensuring an effective risk management infrastructure to support business development and growth plans.

In the Risk Management Strategy and Risk Appetite, special attention was paid to the risk management policies and to the quantitative definition of risk capacity and appetite for capital and liquidity. The Group also focuses on the risk-aware culture, which is based on the awareness that its business decisions have to be aimed at not only ensuring long-term sustainable and profitable operations but also maintaining adequate capital and liquidity levels with regard to the risks taken. In doing so, the Group takes into account the bases for making business decisions, in addition to the ethical principles and interests of all stakeholders, transparency, consistency and control, unobstructed communication about risks and the relevant proposals of internal control representatives in the context of the decision-making process. The Group conducts its business in compliance with the adopted Code of Business Ethics and other applicable policies that make up the broader framework of risk management and the risk-aware culture. To this end, the Group has a robust internal arrangement in place with regard to risk-taking limits, monitoring of risk limit utilisation, control and procedures in relation to possible exceedance. Furthermore, the Group set up protocols which, particularly in the context of the loan process, direct the proposal procedures between business lines and functions responsible for risks.

The Group is aware that the business plan and business decisions have to be aimed at ensuring long-term sustainable and profitable operations, therefore exposure to risks is duly assessed, which includes stress testing. Stress testing at the Group level is an important part of the strategic planning of risk appetite, as it provides information on whether the financial position of the Group could withstand the impact of exceptional but plausible events.

Active risk management and an adequate capital level impact the credit rating of the Bank.

The Risk Management Division, an organisational unit independent from the front office, is in charge of the risk management function. It is responsible for the development and use of risk management techniques as defined by the process framework elements (identification, assessment, monitoring, reporting and management) at the Group level in the most reliable, integrated, systemic, transparent and comprehensible manner. Moreover, it is responsible for improving risk management so as to ensure long-term stability and safety of the Group's operations within the scope of the key risk appetite indicators set out in the risk management strategy.

The activities of the Risk Management Division in 2018 and the achieved results are presented in detail below. In 2019, its focus will be on further development of the internal capital and liquidity adequacy assessment processes (ICAAP and ILAAP) and on synchronisation of processes with risk management framework development. Apart from that, the Division will focus on upgrading the methodologies and data for assessing credit risk parameters and exposure to individual types of risks, additional assessment of the models used, establishment and upgrading of software support and tools for effective risk management, an efficient and controlled loan process, and further reduction of the share of non-performing exposures. Additional attention will be paid to various types of preventive action so as to prevent the emergence of new non-performing exposures.

CREDIT RISK

Credit risk is the most important risk in the Abanka Group and represents a risk that a debtor or counterparty will cause a loss for the Group by failing to discharge an obligation. In addition to default risk, credit risk also includes concentration risk, the risk of less effective credit protection than expected (residual risk), country risk, dilution risk of purchased receivables, risk associated with foreign currency loans, participation risk, credit rating risk and shadow banking risk. The Group identified the following risks as material risks: default risk, counterparty risk, concentration risk, credit rating risk and residual risk.

The main objectives of credit risk management in the Abanka Group is to achieve and maintain the quality and diversification of the credit portfolio, that provides for stable and sound operations. To achieve these objectives, procedures for credit risk exposure monitoring and loss prevention were set up.

The main objectives of credit risk management in the Abanka Group is to achieve and maintain the quality and diversification of the credit portfolio, that provides for stable and sound operations.

The Abanka Group established the credit risk management process, which includes: credit risk identification, measurement/assessment, monitoring, management and reporting procedures. In credit risk management, various credit risk mitigation tools are used, such as: the limit system, credit protection, master netting agreements, financial covenants and other contractual provisions in credit agreements (e.g. contractual (financial) obligations).

Exposure to credit risk depends on the following three credit risk components:
- a debtor’s probability of default reflected in their credit rating,
- the loss or recovery rate in case of default,
- the exposure at default (including the conversion factor in the case of an off-balance-sheet exposure).

The Group uses expected and unexpected loss as a credit risk measure. To this end, the credit portfolio risk assessment, amount and quality of collateral and exposure maturity are taken into account as well as the risk characteristics of various types of exposures. In credit risk assessment, the volume and concentration of assets are taken into account in addition to asset quality.

In 2018, the Abanka Group continued to upgrade its credit risk management process and develop the necessary application software. On 1 January 2018, the transition and compliance of the Bank’s accounting with the provisions of the new international accounting standard for classification, measurement and impairment of financial instruments and general hedging against risks (IFRS 9) was carried out. Apart from that, the Group evaluated the methods/models for the assessment of credit parameters to calculate impairment and provisions.

The Abanka Group continued to upgrade the process for the early warning system for increased credit risk – EWS by linking the EWS with the SISBIZ information system for legal entities (the Central Credit Register of the Bank of Slovenia) and by upgrading the EWS system for entrepreneurs and retail customers.

Special emphasis was put on decreasing non-performing loans and on the recovery process and credit protection management.

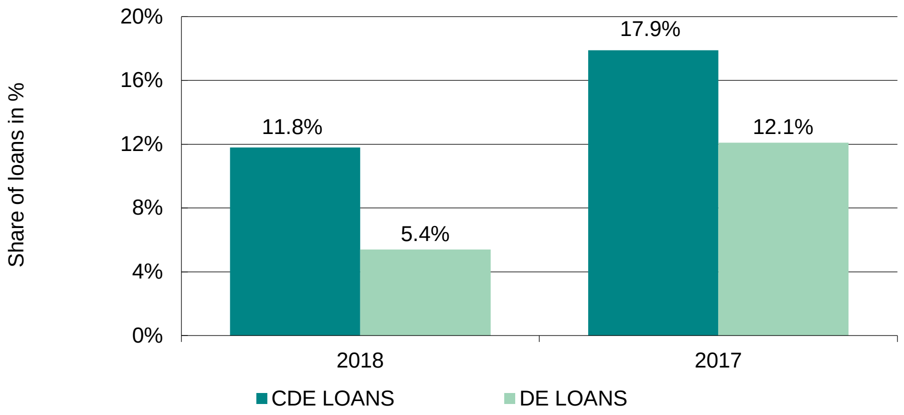
In the area of credit protection, Real Property Valuation Methodology Pledged as Collateral for Exposures of Abanka d.d. (hereinafter: the Methodology) was updated. In accordance with the revised Methodology, collaterals are monitored and their current value is set based on appropriate records by applying different valuation techniques depending on the type of real property, the type of previous valuation, the value of real property and the value of investment. The Abanka Group also devoted considerable emphasis on upgrading application software on the basis of user and regulatory requirements (new requirements relating to collateral, integration with other application software), while taking into account the need to ensure an adequate data basis for reporting to supervisory institutions. Additional activities were also carried out in connection with the preparation of reports on credit protection.

In 2018, the Abanka Group continued with a more proactive approach to reducing the share of non-performing loans, which was reflected in the sale of a NPL and substantial decrease of the NPL share.

In 2018, the shares of C, D and E loans in the Group's credit portfolio, excluding exposures to banks, decreased compared to the previous year. The share of non-performing loans decreased mainly due to the implementation of new accounting standard IFRS 9 and the sale of the portfolio of non-performing loans. The reasons for reducing the share of non-performing loans were also continued activities related to the collection of non-performing loans, the restructuring of corporate loans which have a business model and a sufficient cash flow for future loan repayment, the implementation of activities connected to the early warning system for increased credit risk (EWS) and a selective approach in the approval of new loans to companies for financing their ordinary course of business or investments.

Trends in the shares of CDE and DE loans in the Group's credit portfolio, excluding exposures to banks, are presented in the graph below.

TRENDS IN THE SHARES OF CDE LOANS, AND DE LOANS (EXCLUDING BANKS) IN THE ABANKA GROUP



The volume and share of non-performing loans are discussed in greater detail in Risk Management, Section 2.1.10. of Financial Report.

The Abanka Group began to update the recovery plan with a view to ensuring a more robust recovery framework.

In 2019, the Abanka Group will focus on further development of credit parameter assessment methodologies and continue to ensure the quality of the data for the assessment of the said parameters based on the evaluation results. The Group will upgrade the technological support for the calculation of expected losses from credit risk by implementing the modules that will allow for greater integration as well as better quality control of calculations and simulations.

Apart from that, the Group will continue to upgrade the EWS process, the credit-scoring system for corporate and retail customers, the ICAAP, the credit portfolio monitoring information system and the credit risk reporting system. Great emphasis will be devoted to the activities aimed at reducing non-performing exposures (collection, collection of collateral, sale of receivables, write-offs, implementation and monitoring of EWS measures). An important part of the tasks will be devoted to a further update of the recovery plan.

OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. The definition additionally includes model risk, conduct risk, outsourcing risk, compliance risk, legal risk and cyber risk, but excludes business risk and reputational risk. However, the realisation of operational risk may, as a consequence, impair the Group's reputation.

The Group regularly identifies and assesses the operational risk exposure and lists preventive and corrective measures of operational risk incidents. The system of reporting the occurrence of operational risk incidents in the Abanka Group involves all employes and enables a quick reaction in the event of difficulties, as the Management Board and senior management are involved in such reporting if necessary. In addition, Security Officer and Information System Security Officer play an active role in incident management. The occurrence and frequency of operational risk incidents – financial, non-financial and contingent – are quarterly discussed by the Operational Risk Commission, responsible for the development of the operational risk management system, and the Risk Management and Asset-Liability Committee, which is a collective decision-making body, responsible for monitoring, directing and controlling operational risk management. The Risk Management and Asset-Liability Committee is promptly informed of all significant operational risks and major losses. It monitors the operational risk exposure and takes the necessary risk management measures, monitors their implementation and discusses operational risk profiles (assessed, realised, targeted).

According to the results of operational risk incident analyses, external factors, a higher number of reported incidents from past years and losses resulting from human error were the main sources of losses arising from operational risk. Action plans were prepared for all significant operational risk incidents, aimed at their prevention or reducing the likelihood of their occurrence, including the persons in charge and the deadlines. Implementation of measures is regularly monitored.

In the reporting year, special attention was paid to effective business continuity management. To this end, the Group developed new application software, defined maximum allowed torerable periode of downtime for all systems and maximum accetable data loss, and ensured the preparation of business continuity plans and recovery plans among business lines and the Information Technology Division. Continuity business plans were updated for all critical and sensitive business functions.

In the context of **the internal capital adequacy assessment process (ICAAP)**, a new **Operational Risk Assessment Methodology** was developed and implemented. In this Methodology, the calculation of adequate capital for operational risk is based on all seven basic types of operational risk, which – in terms of content – are consistent with the following event-type categories referred to in Regulation (EU) No 575/2013 on prudential requirements for credit institutions:

1. internal fraud,
2. external fraud,
3. employment practices and workplace safety,
4. clients, products and business practices,
5. damage to physical assets,
6. business disruption and system failures,
7. execution, delivery and process management.

In the context of the internal capital adequacy assessment process (ICAAP), a new Operational Risk Assessment Methodology was developed and implemented.

In accordance with the new methodology, the Group assessed the initial and remaining potential operational risk by taking into account and without taking into account the internal control environment.

In 2018, the incident management system was upgraded and an operational risk incident management application was developed, which enables more effective management, analysis and reporting.

The Group closely monitors its outsourcers to identify a possible increased risk that results from such cooperation and affects business continuity.

In 2019, the Group will continue to upgrade the operational risk management system, placing great emphasis on establishing appropriate procedures for minimising and limiting the loss arising from operational risk of individual organisational units and the Group as a whole. Measures to reduce the frequency and severity of operational risk incidents will be planned and implemented. Furthermore, the business continuity management system will be upgraded, the organisational culture will be strengthened in combination with effective operational risk management, and education of all employees will continue.

MARKET RISK

Market risk is the risk of loss due to the unfavourable movement of market prices. It is caused by an adverse movement of risk factors, including interest rates, exchange rates, credit spreads, the prices of shares, commodity/gold prices and other important factors. The Group separately monitors its market risk exposure to financial instruments according to its trading and banking books.

The main purpose of market risk management is to achieve a balance between the return and the acceptable risk level, taking into account the Group's risk appetite and risk capacity, macroeconomic environment factors, abiding by legal restrictions and the corporate policy in force. In the Group, trading units generating risk are operationally and organisationally separated from the risk management units and other support services.

In 2018, the Group continued its policy of limited trading in financial instruments. Trading in equity financial instruments did not occur, whilst trading in debt financial instruments for own account was mainly limited to primary dealing in the government bonds of the Republic of Slovenia and active maintenance of this bond market. Trading in derivatives was limited to foreign exchange and interest rate financial instruments requested by customers (mostly corporates) for the purpose of hedging against interest rate and currency risks.

The banking book portfolio includes both equity and debt securities, which are not held for trading. The banking book equity portfolio includes only the strategic positions of the Group and positions obtained from collateral foreclosure or debt-to-equity swaps. The size of the debt securities portfolio of the banking book, serving as an asset and liability management tool, increased by EUR 19 million compared to the end of 2017, amounting to EUR 1,079 million as at the 2018 year-end.

To measure market risks, the Group applies Value at Risk (VaR): a quantitative measure used for assessing potential loss in the value of a position caused by adverse risk factor changes over a given future period at a given level of confidence in normal market conditions. The Group calculates VaR for debt financial instruments based on a historical simulation at a 95% to 99% confidence level and with a 10-day holding period. At a 99% confidence level, with a 10-day holding period and under the assumption of normal market conditions, the Group could not have incurred more than EUR 21 thousand of loss from trading in debt financial instruments as at the 2018 year-end.

A limit system is the basic tool for effective market risk management, which arises from the Group’s appetite to bear market risk. The Group has established a limit system, including credit and position limits, stop loss limits, market rate compliance limits, VaR limits and limits per single authorised person. In setting limits in the trading and banking books of financial instruments, the Abanka follows the principles of prudence and increased portfolio diversification to minimise exposure to credit and market risks.

In the reporting period, trading in derivatives was based on the back-to-back trading policy. Trading in derivatives with other companies was mostly performed only to hedge positions against interest and currency risks. There was not trading in more complex derivatives.

The Group plans to maintain a low appetite for market risk in the future through restrictive limit systems for high liquidity of the trading portfolio, debt financial instruments of high credit quality and effective portfolio diversification. A potential threat is the possibility that portfolios will deteriorate and expand due to the possible realisation of collaterals in lending operations or due to potential debt-to-equity swaps, which will increase the market risk exposure. A potential increased exposure of the Group to market risk can also be caused by a counterparty’s failure to meet its obligations from transactions in derivatives, which the Group is closing with high-street European banks.

The Group plans to maintain a low appetite for market risk in the future.

INTEREST RATE RISK

Interest rate risk is the risk arising from the exposure to unfavourable changes in levels of market interest rates. Fluctuations in the levels of prevailing market interest rates have an impact on the value of financial instruments and the future cash flows. As a consequence of these changes, interest margins and profits change as well.

For interest rate risk management, an effective interest rate risk management process is in place, which keeps risks at an acceptable level. Interest rate risk is identified, measured, managed, controlled and monitored in line with the Risk Management Strategy and Risk Appetite, the objectives of the interest rate risk management policy, and the ICAAP and ILAAP Rules. In terms of organisation, interest rate risk limitation and control are separated from operational interest rate risk management and the fulfilment of requirements.

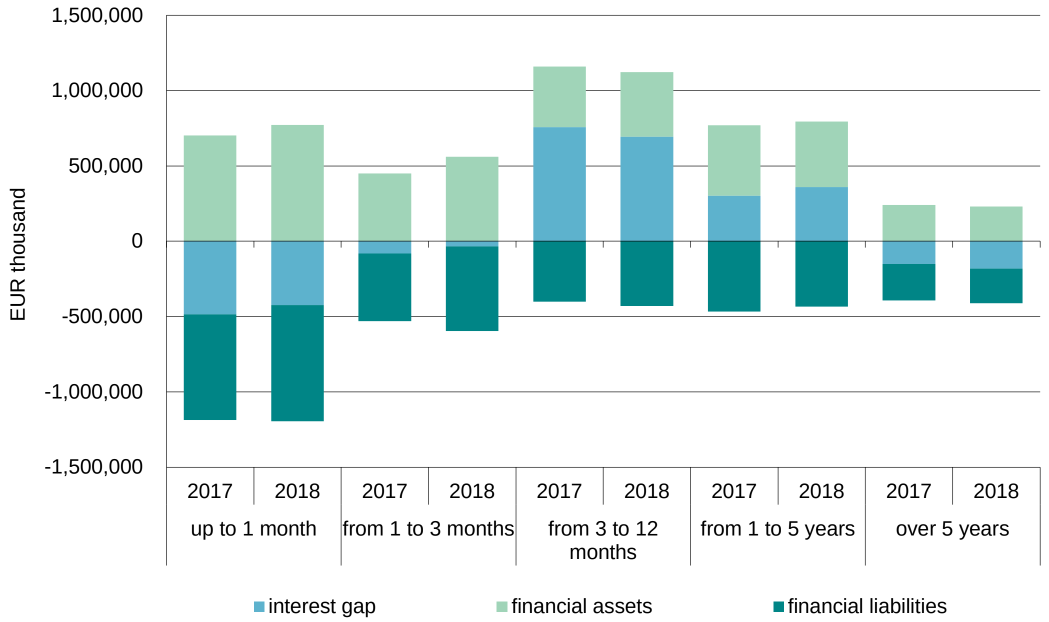
The interest rate risk arising from trading is monitored within the framework of monitoring market risks, whereas the interest rate risk arising from the banking book is measured through interest rate gaps and regular balance sheet interest rate sensitivity analyses. Interest rate gaps show the difference between the cash flows of interest-sensitive assets and liabilities by different time buckets. An interest rate sensitivity analysis, which takes into account various scenarios and forecasts, measures the impact of potential changes in interest rates and other factors on the economic value of equity and on net interest income of the Bank. The basis risk, arising from various types of reference interest rates, is also taken into account when interest rate risk is measured. In the current extremely low interest rate environment, interest rate risk continues to be carefully monitored and managed. Stress testing is regularly performed for measuring the impact of yield curve changes on interest rate risk. The extent of interest rate risk is restricted by the established limit system.

The Abanka Group continuously adjusts its interest rate policy to the conditions in domestic and international markets as well as balances its interest rate position. In the reporting year, the Group developed a loan prepayment model (early repayment of loans), carried out the model validation process and began to implement the prepayment model in the regular processes of the Bank. The model was first implemented in the internal transfer pricing system. The prepayment model has been gradually implemented in the interest rate risk exposure monitoring process, by taking into account interest rate gap calculation with regard to prepayments.

The Abanka Group continuously adjusts its interest rate policy to the conditions in domestic and international markets as well as balances its interest rate position.

The graph below shows interest gaps by time bucket in Abanka at the 2018 year-end compared with the 2017 year-end, taking into account prepayments in 2018.

INTEREST RATE GAPS IN ABANKA



In the framework of the banking book interest rate management in 2019, the Bank will continue to strive for a balance of interest gaps by time bucket, paying more attention to longer maturity time buckets, thereby reducing the sensitivity of the economic value of equity. In addition, a special focus will continue to be on balancing the net interest income sensitivity. The interest rate risk identification and measurement methodology will be upgraded to include the prepayment model in the calculation of sensitivity of the economic value of equity and net interest income as well as to harmonise the methodology with the updated EBA Guidelines on Technical Aspects of the Management of Interest Rate Risk Arising from Non-Trading Activities. The Group will further develop the econometric models for non-maturing items and upgrade the technological infrastructure for interest rate risk identification and management.

LIQUIDITY RISK AND THE ILAAP PROCESS

Liquidity risk is the risk of loss that includes the risk of failing to provide liquidity sources, market liquidity risk and asset encumbrance risk. The risk of failing to provide liquidity sources is the risk that the Group might not be able to meet its payment obligations when due and/or that as a consequence of its inability to provide sufficient funding to meet payment obligations by the due date it might be forced to provide the required funding at costs significantly above the average market costs. Market liquidity risk is the risk of loss arising from the impossibility to sell or replace positions (in financial instruments) in a short period of time without this bearing a significant impact on the market price, due to either insufficient market depth, market imbalances or other reasons. Liquidity risk also includes asset encumbrance risk, which arises from the encumbrance of the Group's assets and means an increase in the risk of providing liquidity sources and market liquidity risk due to fewer possibilities of providing liquidity sources and disposing of assets.

The Abanka Group has developed its own methodology for identifying, measuring, managing and monitoring liquidity risk, which enables it to match the actual and potential sources of liquidity with the actual and potential uses of such liquid assets over certain time periods.

The Group implements the internal liquidity adequacy assessment process (hereinafter: ILAAP), which includes the assessment of liquidity requirements and the assessment of available liquidity. The Group regularly checks its liquidity adequacy, both within the framework of the ordinary course of business and in the context of the business plan for the future planning period. The verification of liquidity adequacy includes liquidity stress testing, which is also carried out within the framework of the ordinary course of business and in the context of developing the business plan for the future planning period. The Group discloses its liquidity adequacy by using selected ratios, whose values are properly calibrated, both in the risk management strategy and in other documents of the Group, such as the business plan, the recovery plan, the plan to restore sufficient liquidity and others. The ILAAP process includes the assessment of adequate funding of the Group and the appropriateness of the liquidity risk management system. The assessment of adequate funding is particularly significant in planning procedures, where the funding policy for the current planning period is developed. Apart from that, adequate funding is disclosed in the current operations, in the context of which decisions on the sources of funding are adopted, both in terms of actual circumstances and potential corrective measures to achieve the planned status. In the ILAAP process, the Group revises methodologies, particularly in relation to stress testing, and establishes an effective liquidity adequacy planning system, both in the context of regular planning and as part of verifying the impact of business decisions on current and future liquidity adequacy.

The liquidity risk management process consists of:
- planning and monitoring future cash flows, which include day-to-day funding to ensure that requirements are met, as well as structural assets and liabilities management;
- maintaining an adequate liquidity buffer that can be easily liquidated as protection against any unforeseen cash flow trends;
- monitoring and calculating balance sheet liquidity ratios and indicators against the Group's internal and regulatory requirements;
- monitoring the diversity of sources of funding and the profile of debt maturities;
- execution of liquidity management scenarios based on the normal course of operations and the liquidity stress situation (stress scenarios).

For the purpose of liquidity risk hedging and its mitigation, the Group established an internal limit system, which includes quantitatively measurable risks and material liquidity risk factors. The Group also uses other tools to reduce exposure to liquidity risk, which are of a qualitative nature. In setting the limits, the Group takes into account the regulatory requirements and the results of internal stress scenarios. The limit setting and liquidity risk monitoring are, in terms of organisation, separated from daily operational liquidity management.

For the purpose of liquidity management in a stress situation, three groups of stress scenarios at different degrees of severity and duration of a liquidity stress situation are analysed. The idiosyncratic scenario is adapted to own liquidity position, the market scenario is linked to a significant macroeconomic event, a sudden change of risk in the financial system or tightening conditions in several markets simultaneously, while the combined scenario is defined as a combination of idiosyncratic and market scenarios. Moreover, in order to hedge liquidity risk, the Group established procedures for the early identification of a liquidity shortage by monitoring liquidity ratios and other indicators, based on which the Group is able to identify any liquidity problems in due time. An action plan taking into account the source and severity of a stress situation was developed in order to take appropriate action to restore normal liquidity levels in the event of a liquidity shortage.

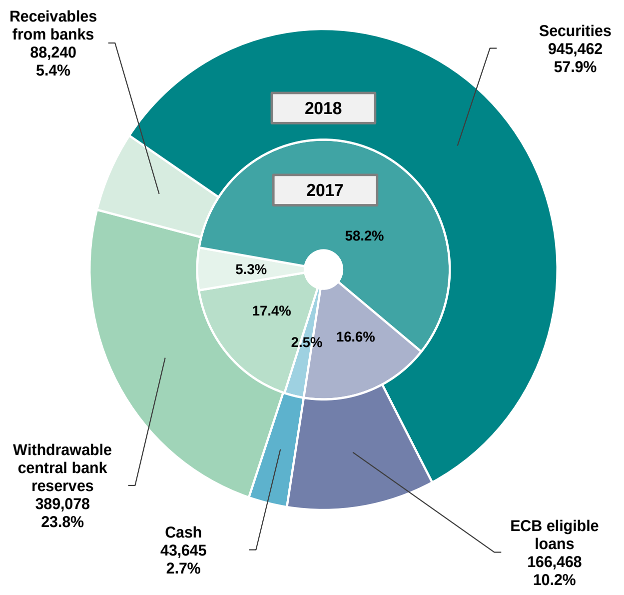
In the reporting period, the Group maintained adequate liquidity levels and a high liquidity buffer. The risks arising from the persisting environment of low or negative interest rates, and consequently a high share of demand deposits in the structure of sources of funding, remained in the foreground. In contrast, conditions in the markets create excess liquidity. The Group holds a high proportion of free assets eligible as collateral for central bank operations and thus a potential source of liquidity at the ECB. In addition to the above, the declining dependence on wholesale funding and a proper emphasis on ensuring a sufficient level of secondary liquidity ensured appropriate liquidity risk management.

In the reporting period, the Group maintained adequate liquidity levels and a high liquidity buffer.

In 2018, the Group revised the definition of stress scenario assumptions and stress scenario implementation methodology for liquidity risk. With regard to the development of econometric models, the models of utilisation of individual off-balance sheet items were redesigned and a loan prepayment model was developed, which is gradually implemented in the liquidity risk exposure monitoring process by including prepayments in the liquidity gap calculation. Furthermore, the Group recalibrated its appetite and liquidity limit system as well as the critical values for the recovery plan and the contingency plan for the re-establishment of appropriate liquidity, and harmonised them. In the framework of the liquidity test carried out for five consecutive working days in 2018, the Bank provided the relevant data on liquidity for reporting to the ECB in line with the requirements of the ECB.

Abanka's internal liquidity buffer structure is shown below.

INTERNAL LIQUIDITY BUFFER STRUCTURE IN ABANKA



In the persisting low interest rate environment and related risks in 2019, the Group will maintain adequate liquidity levels and liquidity buffer as well as ensure compliance with regulatory requirements on liquidity risk management through prudent asset liability management in relation to the current market conditions and through prudent secondary liquidity management. In 2019 in the context of ILAAP, the Group will further upgrade its liquidity risk identification and management methodology. Moreover, statistical models for predicting the trends by financial instrument type will continue to be developed and the developed models will be implemented in regular processes. Application software for liquidity risk management and the ILAAP will be further improved. The Group will adapt the ILAAP to regulatory guidelines and strategic objectives, continue to prepare regular analyses for early detection of potential vulnerabilities, ensure quality reporting to the management and supervisory bodies of the Bank, and upgrade regulatory reporting.

THE ICAAP PROCESS

The Group regularly implements its Internal Capital Adequacy Assessment Process (hereinafter: ICAAP). The ICAAP and risk appetite framework are closely linked, which is adequately reflected not only in the risk management limits at the level of the Group and portfolios but also in integration with the business strategy, the business plan and the recovery plan.

In 2018 in the context of ICAAP, the Group identified material risks and determined their treatment methods. It regularly checked its exposure to the identified risks and examined the emergence of possible new types of risks, with a view to ensuring an adequate capital level and quality. Risk assessment monitoring allows timely identification of key changes in the risk profile and provides the basis for taking the necessary measures. The Group revised the content of reports, optimised the reporting flows and upgraded the escalation processes.

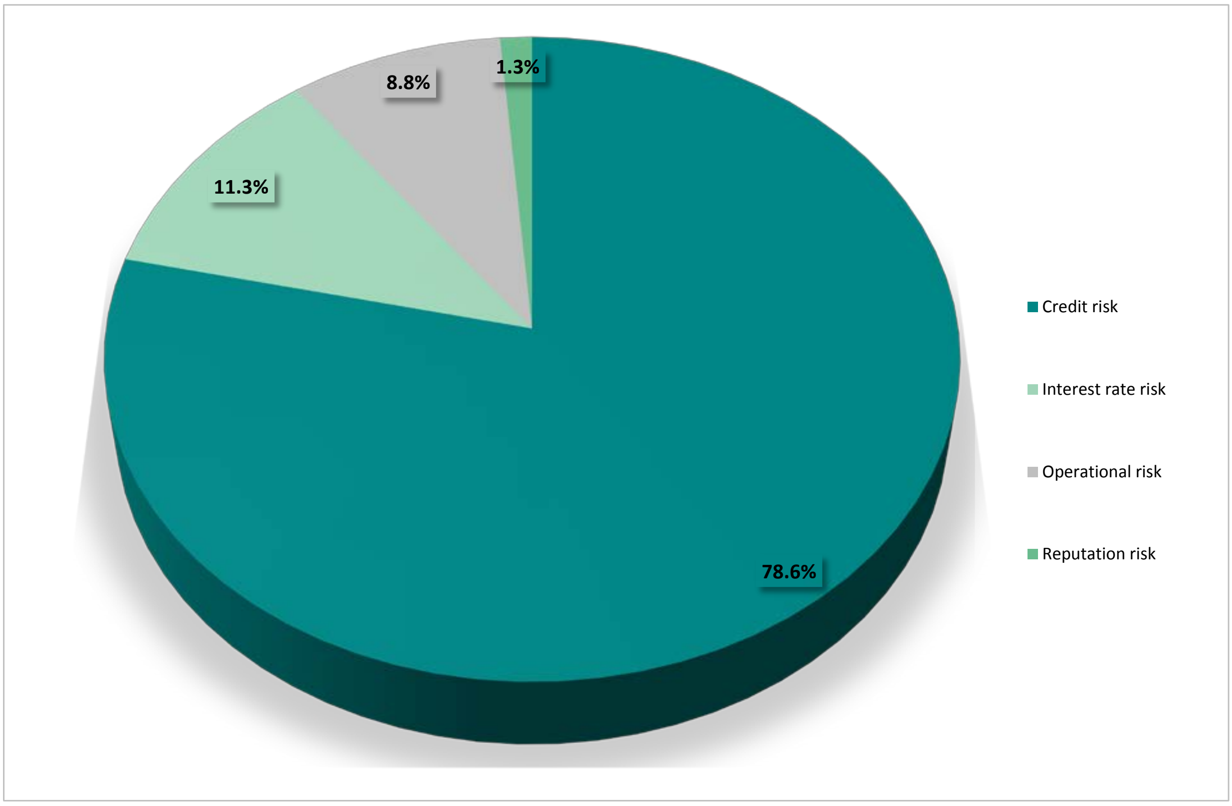
In the reporting period, the Group upgraded its internal capital requirement assessment matrices for material risks in order to increase the clarity of internal capital requirement assessments and keep them up-to-date as well as to implement the ICAAP and ILAAP Guides.

In the ICAAP process, the Group places great emphasis on regular stress testing, which is performed to identify the vulnerability of the Group in the event of less likely, but still possible, changes of various risk factors.

The internal capital adequacy assessment process is defined by two variables. The first variable is the risks to which the Group is exposed, going beyond the first pillar of capital requirements; the second variable is the capital held by the Group for covering risks and potential losses arising from such risks. A comparison of the assessed internal capital requirements and the assessed internal capital indicates the Group's ability to cover all the risks to which it is exposed.

As at the 2018 year-end, the internal assessment of capital requirements was structured as follows:

INTERNAL ASSESSMENT OF CAPITAL REQUIREMENTS



Note:
Operational risk includes: employee cyber risk, third-party cyber risk, compliance risk, conduct risk, model risk, legal risk and outsourcing risk.

STATEMENT OF THE MANAGEMENT BOARD AND THE SUPERVISORY BOARD ON THE ADEQUACY OF RISK MANAGEMENT IN ABANKA AND THE ABANKA GROUP

The Management Board is responsible to set up an appropriate risk management system and a financial and internal control system in Abanka and the Abanka Group.

The Supervisory Board together with the Audit Committee, the Risk Monitoring and Asset Liability Management Committee and the Remuneration Committee monitors the implementation of the Risk Management Strategy. Through its supervision, it contributes to the establishment and implementation of not only an adequate and stable risk management system but also an appropriate internal control system in Abanka and the Abanka Group.

Both the Management Board and the Supervisory Board assess that based on their risk profile and the adopted business strategy Abanka and the Abanka Group have an appropriate risk management system, which enables the implementation of the adopted Risk Management Strategy.

Ljubljana, 5 March 2019

Management Board

Jože LENIČ
President of the Management Board

Matej GOLOB MATZELE
Member of the Management Board

Matevž SLAPNIČAR
Member of the Management Board

Supervisory Board

Marko GARBAJS
Chairman of the Supervisory Board

STATEMENT OF THE MANAGEMENT BOARD AND THE SUPERVISORY BOARD ON THE RISKS OF ABANKA AND THE ABANKA GROUP

A concise statement of the management and supervisory bodies on risks in accordance with Article 435(1)f of Regulation (EU) No 575/2013 (CRR) succinctly describes the bank's or the group's overall risk profile associated with the business strategy, business models and risk tolerance.

Abanka and the Abanka Group achieve strategic objectives based on the pre-defined risk appetite. The aim of the risk appetite is to manage both the acceptable profitability and the capital and liquidity adequacy of Abanka and the Abanka Group within the limits laid down by the management body of Abanka and the Abanka Group, which are in line with the applicable regulations, commitments made to the European Commission and good banking practices.

In line with the above, the following guidelines will be observed:
- focusing on the domestic market;
- strengthening the SME and retail business;
- investing in less risky debtors (defined by the internal credit rating scale) and limiting the exposures associated with a very high risk;
- focusing on decreasing the share of non-performing exposures;
- pursuing credit portfolio diversification at the exposure level of individual borrowers, groups of related parties and industries;
- acquiring collateral of appropriate form, size and quality;
- maintaining an adequate level of liquidity reserves and liquidity ratios as defined in the applicable risk management strategy and risk appetite;
- ensuring stable and diversified sources of funding.

The Abanka Group establishes and manages the framework and processes of comprehensive risk management by taking into account the Group's business model and risk profile. The risk management strategy defines not only the key risk appetite elements but also the processes and mechanisms to ensure that the Bank's risk-taking always complies with its target and sustainable risk tolerance. To ensure that the risk profile complies with the defined risk appetite and adopted risk policies, the Bank maintains the appropriate separation of powers and duties, clear and efficient processes, focuses on and raises awareness about the importance of risk identification and management, as well as uses various risk management tools and techniques.

Among other things, the risk appetite is limited so as to ensure adequate capital and liquidity levels also in extraordinary circumstances. Setting the risk appetite limits represents an important part of the decision-making process. Regular risk monitoring and reporting enables Abanka and the Abanka Group to take timely action at pre-set limits before reaching the upper tolerance limit. Risk management involves the entire senior management, who participates in all relevant meetings and committees where decisions on risk management are taken. Within the framework of the Supervisory Board, the Risk Monitoring and Asset Liability Management Committee is set up, whose work particularly focuses on risk management.

Abanka and the Abanka Group monitor and assess all the risks on the basis of a risk catalogue (part of the Risk Management Strategy and the Risk Appetite), which includes the definitions, scope, persons in charge and designation of (im)materiality. Special emphasis is put on careful management of all material risks, including: credit risk, market risk, operational risk, interest rate risk, liquidity risk, reputational risk, compliance risk and business risk.

The Management Board set and the Supervisory Board approved the risk appetite, defined by key indicators determining the acceptable risk level to ensure capital and liquidity adequacy. The risk appetite of Abanka and the Abanka Group is moderate, which means that a more conservative credit risk management policy will be followed in the context of internal processes and business decisions. With regard to material risks, Abanka and the Abanka Group pay special attention to credit and liquidity risks. Credit risk taking is moderate and complies within the specified permissible quality and diversification of the credit portfolio. To ensure the quality of the portfolio, the risk management function is actively involved in the loan process for approving new loans; furthermore, the Group places great emphasis on the activities to further reduce the share of non-performing exposures and to prevent the emergence of new non-performing exposures. Liquidity risk taking is low, because Abanka and the Abanka Group aim to ensure a secure liquidity position and an adequate liquidity buffer, both under normal and stressed conditions. A special emphasis is placed on regular monitoring of exposure to liquidity risk and having appropriately diversified sources of funding by focusing on the primary sources of liquidity. Abanka and the Abanka Group maintain a moderate exposure to interest rate risk and a low exposure to currency risk. The non-financial risk appetite, which includes broad operational risks, is low. Abanka and the Abanka Group monitor realised operational risks and assess potential operational risks. Exposure to operational risks is managed by appropriately adjusting internal controls, increasing the risk awareness culture and upgrading internal processes. In the context of risk control, business risk is also thoroughly managed.

The appropriateness of the risk profile of Abanka and the Abanka Group is monitored based on six key risk measures (indicators), which define the risk appetite with respect to the following values:

- total capital ratio – over 18.3%,
- Common Equity Tier 1 (CET1) ratio – over 14.8%,
- weighted probability of default of new exposures – under 3%,
- liquidity coverage ratio (LCR) – over 150%,
- net stable funding ratio (NSFR) – over 110% and
- survival period under liquidity stress conditions – over 3 months.

To provide a comprehensive presentation of the Bank's risk profile, the key indicators are presented in the Business Report (Section *Financial Highlights and Performance Indicators*) and the Financial Report (Sections *Risk Management* and *Capital Management*). More information on risk management is disclosed under Section *Disclosures* in line with Pillar 3 of Basel standards. The risk profile of Abanka and the Abanka Group is within the risk appetite limits set by the management body.

Abanka and the Abanka Group have clearly defined risk appetite limits through the risk appetite, limit systems (regional and sectoral limits, portfolio credit limits, individual credit limits, limits for trading and transactions with financial instruments of the banking book, limits for liquidity, currency and interest rate risk management, and others) and additional indicators by individual risk types. In line with the implementation of the Group's strategy and the commitments made to the European Commission, risk-adjusted pricing is used for loans.

Risk assessment is conducted in the context of both the internal capital adequacy assessment process (ICAAP) and the internal liquidity adequacy assessment process (ILAAP). Within these processes, the assessments of the required capital and liquidity levels are performed and reported to the Bank's bodies (The Risk Management and Asset-Liability Committee, the Management Board, the Supervisory Board and its Committee).

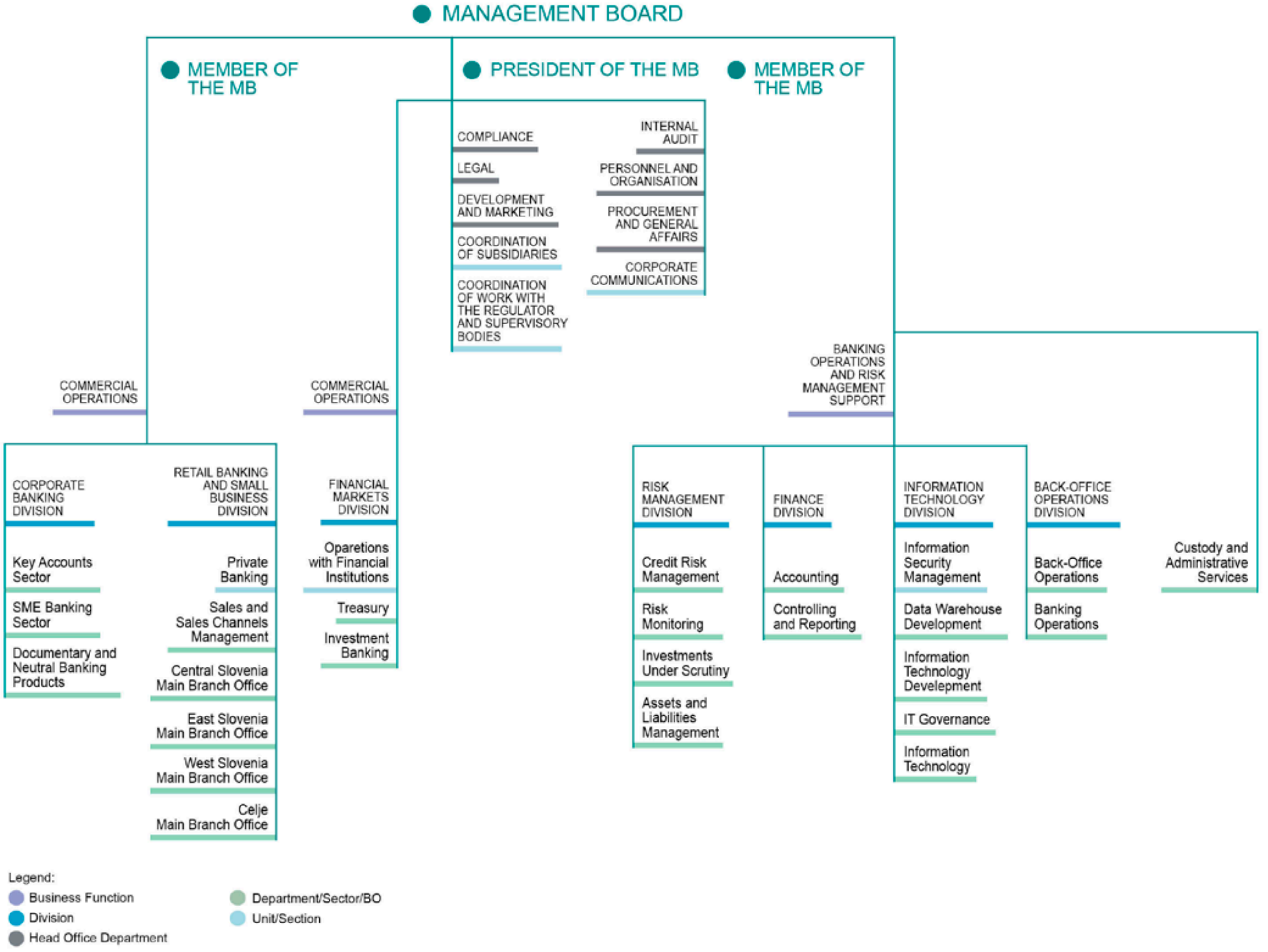
The risk management systems in Abanka and the Abanka Group are appropriate and consistent with both the Business Strategy and the Risk Management Strategy, which is based on the defined key risk management indicators.

Ljubljana, 5 March 2019

Management Board	**Supervisory Board**
Jože LENIČ President of the Management Board	**Marko GARBAJS** Chairman of the Supervisory Board
Matej GOLOB MATZELE Member of the Management Board	
Matevž SLAPNIČAR Member of the Management Board	

ORGANISATION AND PROCESSES

ORGANISATIONAL CHART AS AT 31 DECEMBER 2018



Optimisation of the Bank's organisational structure was continued in 2018 based on the guidelines set in the Bank's strategy.

The goal is to set up and maintain an efficient organisational structure adapted to the planned volumes of business not only in the front office but also in the back office and management. Optimisation and upgrading of the organisational structure continued with the aim of including additional functions, centralisation and ensuring a more efficient execution of individual functions.

Finding **new solutions in process and organisational structures** enables the vital parts of the Bank to be less burdened with administrative barriers that create bottlenecks in sales activities, as well as facilitates rapid adaptation to the needs of the market, the establishment of a lean organisational structure and the implementation of the strategy focused on digitalisation.

The goal is to set up and maintain an efficient organisational structure adapted to the planned volumes of business not only in the front office but also in the back office and management.

PROJECTS AND DEVELOPMENT ACTIVITIES PLANNED FOR 2019

In 2019, the highest priority will be given to projects aimed at ensuring compliance of the Bank with the regulatory requirements imposed by:

- General Data Protection Regulation (GDPR) and the future new Personal Data Protection Act (ZVOP-2);
- PSD2 (Payment Service Directive) and its incorporation into the Payment Services, Services of Issuing Electronic Money and Payment Systems Act (ZPlaSS-1);
- requirements to revise reporting in the context of the single credit register (Anacredit).

We will continue with the projects and development activities aimed at implementing the strategic initiative to use digitalisation in order to improve customer experience by digitalising the points of contact for interaction with customers and to optimise the product range. To speed up the launch of strategic products, from drafting a proposal to customer use, in 2018 the first i.e. agile team for mobile channels was established, who will continue to apply agile approaches also in 2019.

> To speed up the launch of strategic products, from drafting a proposal to customer use, in 2018 the first i.e. agile team for mobile channels was established.

Apart from the above development activities, we will continue to develop the digital platform, which will provide the technical conditions for the digital transformation of Abanka.

Development activities will be implemented within the limits of the funds available for investment in intangible fixed assets and available human resources, with the goal of effectively implementing the strategic objectives and adjusting to market conditions.

EMPLOYEES

HUMAN RESOURCE POLICY AND STRATEGIC HUMAN RESOURCE HIGHLIGHTS

Efficient, motivated and engaged employees are crucial to achieving the strategic and business objectives of the Bank.

The operations of the Bank are based on good interpersonal relationships, which are strengthened with the values for which the Bank stands. New employees are recruited in accordance with the principle of equal opportunity. All employees enjoy optimal working conditions and social security, have the possibility of personal and professional development, and are presented with work-related challenges through which they harmonise their personal goals with the objectives and needs of the Bank. By using transparent and open communication, the Bank creates the basis for trust and a work environment that contributes to employee satisfaction, offers a pleasant working atmosphere and encourages employee engagement and commitment.

> New employees are recruited in accordance with the principle of equal opportunity. All employees enjoy optimal working conditions and social security, have the possibility of personal and professional development, and are presented with work-related challenges.

In 2018, many human resource activities were related to the strategic guidelines of the Bank, which included the implementation of the commitments arising from the restructuring plan. In addition to the Human Resource Policy as the main document regulating human resource management, the Bank implements the Human Resource Renewal Programme, the Human Resource Optimisation Programme and the Digital Culture Programme.

The strategic highlights of the **Human Resource Policy** are aimed at increasing productivity and performance of the Bank, retaining key staff and attracting the best workers from the external labour market, increasing employee engagement and performance, and enhancing the visibility of the Bank in the banking and wider environment. The Human Resource Policy activities are divided into the following four sets: staffing levels and procedures, development and training, motivation and salary policy, organisational culture and values.

On the basis of the **Human Resource Optimisation Programme**, the Bank optimises its staffing structure by reducing the number of employees, restructuring the existing posts and ensuring such staffing and employee profiles that adjust to the changes in the market and the competitive environment.

Through the **Human Resource Renewal Programme**, the Bank promptly adapts to the future challenges on the labour market. In 2018, the implementation of qualitative changes to the staffing structure continued by primarily focusing on strengthening the sales channels of the Bank, both in terms of number and specialisation. The Human Resource Renewal Programme also defines other activities aimed at staff regeneration, enhancing intergenerational cooperation, building a pool of potential promising staff, cooperation with universities, awarding scholarships for jobs in demand and maintaining the reputation of the Bank by presenting Abanka at various HR events and employment fairs. In 2018, nine scholarships for jobs in demand were awarded, seven for graduate studies and two for post-graduate studies. Moreover, work placement and gaining new knowledge and experience in the Bank was provided to pupils and students. Abanka was promoted as a good employer at the Career Fair in Ljubljana. Moreover, the Bank actively participated in HR Hackathon.

An additional set of activities carried out in the context of the digital transformation process is defined in the **Abanka's Digital Culture Project**, which was developed with a view to creating a cooperative work environment, introducing new and modern forms of work in order to ensure that employees have an appropriate set of skills in the digital era, and applying new digital approaches to recruitment and employment.

Other disclosures about the human capital of the Abanka Group and Abanka in 2018 are shown in the table below:

	The Abanka Group	Abanka
Total employees as at 31 December 2018	1,022	1,010
Average number of employees during the year	1,056	1,038
New recruits in 2018	51	51
Employees leaving in 2018	88	88
Employees – permanent work contract	998	987
Employees – fixed-term work contract	24	23
Employees with disabilities	20	20

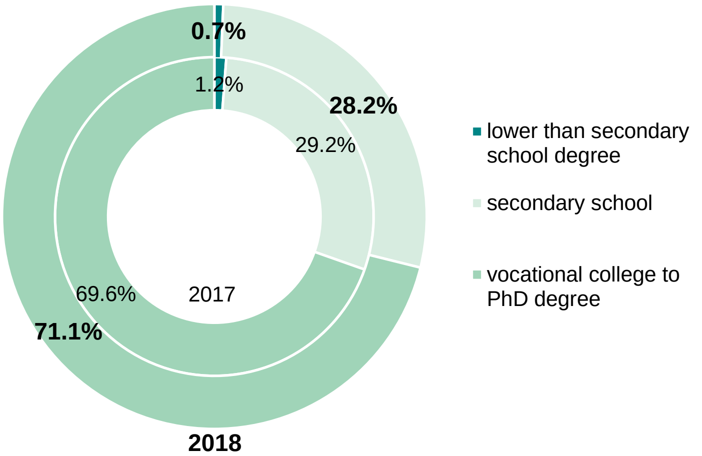
1,010

employees of Abanka as at the 2018 year-end

Of the total number of employees, 76% were women and 24% were men. Most employees were aged between 40 and 49 years with the average age of 45.5 years. The employees of the Bank perform their work in different regions as Abanka is present across Slovenia through its extensive branch office network.

Almost 72% of the Bank's employees have university or higher education (level VI or higher). The educational structure has been improving from year to year.

EMPLOYEE EDUCATIONAL STRUCTURE IN ABANKA IN 2018 AND 2017



EMPLOYEE EDUCATION AND TRAINING

Investment in education and training of employees is an investment for the future success of the Bank. Education and training needs arise not only from individual needs relating to the professional and personal development of employees but also from business needs relating to the business strategy of the Bank. **In 2018, all employees attended at least one training course**.

Education and training needs arise not only from individual needs relating to the professional and personal development of employees but also from business needs relating to the business strategy of the Bank.

The key activities in education and training in 2018 were aimed at the acquisition of relevant know-how and skills required by business priorities, which employees obtained through **in-house and external training**.

External training was provided by recognised external experts, whereas in-house training was based on the transfer of know-how and skills among co-workers. In the context of in-house training, the frequently used method is **mentoring**, particularly for employees who are assuming new duties or greater responsibility.

In the spirit of digital transformation, the Bank continues to increase the proportion of e-learning. The Bank established its own **e-platform**, where a library of e-material primarily prepared by in-house trainers is being built.

The average number of training hours per employee was 24 hours.

As in previous years, **work study** of the employees who participated in an internal call was co-financed in 2018. The employees of the Bank regularly participate in various forms of training to obtain different types of certificates, licenses or qualifications.

In 2018, the greatest attention in employee training was devoted to upgrading professional banking and financial knowledge, sales, marketing, developing leadership competencies and sales skills, and acquiring the knowledge required by the applicable legislation. Training in products, foreign language courses, learning how to use various IT tools and acquiring the knowledge of business analytics represent a significant share of training held by the Bank. Many training courses are dedicated to the targeted training of key staff.

The development of leadership competencies was focused on different types of leadership training and coaching and soft leadership skills and communications. Much attention was paid to the unification of the organisational culture and mutual communication, therefore leaders and employees are offered a diverse range of team-building exercises, even such that support corporate social responsibility.

EMPLOYEE DEVELOPMENT

Abanka constantly develops and upgrades its employee development activities. Different tools and approaches are used in employee development, including various motivational mechanisms. Furthermore, the ever-increasing intergenerational differences are taken into account.

In 2018, the Bank operationalised and actively monitored the key staff retention programme in a small focus group and developed the starting points for the retention programme for the remaining key promising staff in the Bank. Key staff management provides an opportunity for employees to build a successful career and for the Bank to retain key, tacit knowledge gained through work experience.

Coordinated succession mapping for key posts enables the Bank greater efficiency and safety in terms of the transfer and retention of key know-how within the Bank; moreover, a substitution system in the event of absence of key employees was established.

One of the tools that the Bank has used for many years, and that allows management by objectives is the **annual interview**, which is, traditionally, held with a very high percentage of employees. The purpose of the annual interview is to maintain appropriate communication between leaders and employees, review the realised objectives and set new ones, prepare a development plan for the employee and discuss a possible career change.

One of the tools that the Bank has used
for many years, and that allows management
by objectives is the annual interview.

In 2018, the measures having a significant impact on the organisational culture of the Bank continued to be implemented, among them systematic training for leaders in order to upgrade their leadership competencies. In its care for the ongoing development of leadership skills, in 2018 the Bank continued to perform the **360-degree feedback** for the selected management level with the aim of reviewing the possibilities for further development of the competences of individual leaders.

EMPLOYEE MOTIVATION AND REMUNERATION

Employee motivation and remuneration are not only an important factor in ensuring the success and competitiveness of the Bank but also an important factor in ensuring satisfaction and commitment of employees. An effective and transparent remuneration system is key in stimulating the employees to perform better. Employees' salaries are subject to collective agreements and internal regulations. The Bank established appropriate remuneration schemes for all employee categories.

An effective and transparent remuneration
system is key in stimulating the employees
to perform better.

In past years, the Bank upgraded **the employee promotion and remuneration system with an aim** to simplify the promotion criteria in the manner that is close to the current needs and existing practices of the Bank and that is primarily based on employees' performance and quality of work. A special emphasis was given to variable remuneration focused on the sales staff as part of a broad systematic approach to improving sales efficiency.

As project work is an increasing form of work in the Bank and because it involves specific workload of employees who work on a project in addition to their regular duties, the **project remuneration concept** was formalised; the most engaged and effective project team members receive bonuses for effectively completing the projects.

Apart from that, the Bank:
- pays **supplemental voluntary pension insurance** premiums for its employees;
- awards **solidarity assistance** to those employees who are entitled to it;
- ensures **accident insurance** for the employees on the posts with increased risk exposure as defined in the Safety Statement and Risk Assessment;
- rewards employees – **jubilarians** who have continuously worked in the Bank for 10, 20, 30 or 40 years;
- each year selects **the best front office employees, the best colleagues and ambassadors of Abanka's values**;
- in 2018 implemented **the employment ambassador concept** with a view to including employees in the recruitment process;
- has **a scholarship system for the children of deceased employees** in the context of implementing Family-Friendly Enterprise measures;
- implements measures for mitigating the consequences of losing a job for the employees who lost their job;
- enables the employees to actively spend their free time by being members of **the sports club and the mountaineering society**.

By rewarding the jubilarians and giving recognition to those employees who deserve it, **commitment and loyalty to the Bank** are built in particular.

ORGANISATIONAL CULTURE AND PRESENCE OF THE BANK

Every year, **the organisational culture and employee engagement** are measured within the Bank so as to enable the employees to improve the working conditions and interpersonal relationships in the workplace with their suggestions and opinions. According to the 2018 survey results, the general employee job satisfaction and engagement index increased compared to 2017. On the basis of the survey results, every year the Bank prepares and implements an action plan, which targets the areas where the results need to be improved.

In the reporting period, the Bank paid great attention to the activities aimed at raising the innovation and digital culture in the Bank, as in early 2018 a**n idea and improvement management system** was implemented and application support for innovation management was provided. In the context of its digital transformation, the Bank developed a plan of activities relating to the **training of employees in digitalisation** and computer tools, the implementation of tools that will not only enable an easier and faster transfer of information among the employees but that will also contribute to the development of **a cooperative work environment and culture** in the Bank.

The Bank strives to have an ongoing constructive dialogue with employee representatives. **Two trade unions** were active in Abanka in the reporting year – Abanka Workers' Union and Banka Celje Workers' Union.

In relation to the prevention of mobbing and any other harassment at the workplace, the Bank established appropriate rules and appointed **Anti-Mobbing Officers**, who provide advice or information in confidence to all employees.

The development of the organisational culture is affected by the implementation of the **Family-Friendly Enterprise Certificate** measures, the aim of which is to facilitate work-life balance for employees. The upgrade of Family-Friendly Enterprise certificate measures continued in 2018.

Special attention is devoted to the **safety and health of employees**. Employees are regularly referred to preventive and periodical health checks as well as to different training courses in health and safety at work. The goal is to prevent injuries at work and reduce the amount of sick leave through employee training and a preventive approach. In 2018, in the context of health promotion, various in-house training courses were organised for the employees.

POLICY ON FIT AND PROPER ASSESSMENT OF MANAGEMENT AND SUPERVISORY BOARD MEMBERS AND POLICY ON FIT AND PROPER ASSESSMENT OF KEY FUNCTION HOLDERS

In accordance with the Banking Act and the related regulations and guidelines issued by the European Banking Authority (hereinafter: EBA), the Bank formulated two policies: the Policy on Fit and Proper Assessment of Management and Supervisory Board Members and the Policy on Fit and Proper Assessment of Key Function Holders.

The Policy on Fit and Proper Assessment of Management and Supervisory Board Members was established so as to define the qualities required by the person who is a candidate for performing the function of a Management Board or Supervisory Board member and the qualities required by the person who already performs the function of a Management Board or Supervisory Board member. In defining the necessary qualities of a Management Board or Supervisory Board member, the Bank adheres to the fit and proper principle. In addition, the Policy defines the procedures and activities for recruiting the members of both bodies as well as induction and training of the members of both bodies. With respect to the relevant criteria, the diversity of the required knowledge and experience in the context of the management body will be considered, including an appropriate gender balance, each member's contribution to the diversity, expertise and delegation within the management body.

Criteria for a fit and proper assessment

A fit and proper assessment of a member is made based on the following criteria defined in the Policy:
- the scope and nature of work experience required to perform a managerial and supervisory function,
- reputation,
- ethical integrity and
- the ability for constructive cooperation in governance and supervision.

In the assessment of experience, a wide range of knowledge (theoretical and practical), skills and experience is taken into account, including the nature and complexity of the function for which a member is a candidate or to which they have been appointed. In line with the Policy, at least university education and five years of work experience in a managerial function are required, in addition to knowing at least one foreign language. A study programme will be deemed appropriate if, in terms of content, it is related to banking and finance, economics, administrative sciences, financial regulations, or mathematical and statistical knowledge (the conditions for the performance of an individual function).

With respect to the criteria regarding the ability for constructive cooperation in governance, the diversity of the required knowledge and experience in the context of the management body will be considered, including appropriate representation of both genders, while also taking into account each member's contribution to the diversity, complementary expertise and delegation of duties within the management body.

The Policy defines the key guidelines for the appointment and assessment of suitability of candidates or members of the management body, both in terms of professional competence, knowledge, skills, experience and the conditions required for the performance of the functions as well as in terms of time devoted to the function, including the definition of personal characteristics (reputation). These criteria will also be considered in the appointment of members of Supervisory Board committees.

In making a fit and proper assessment of the Management Board and the Supervisory Board as bodies, the Nomination Committee assesses in particular:
- the diversity of the body, which ensures professional and independent participation of the body in setting the objectives, strategies and policies of taking risks and risk management;
- whether the body enjoys the trust of the shareholders, the supervisory/management body, other stakeholders and supervisory institutions;
- whether the body is a strong collegial body, in which decisions are taken jointly despite different views;
- whether the body keeps updated on innovations in governance and the fields of expertise required for performing the function in the Bank;
- whether the body undertakes training with the aim of developing and maintaining an adequate level of expert knowledge of the Bank;
- whether the body cooperates with the Supervisory Board and/or the Management Board in a transparent manner;
- whether the selection process of candidates for the members of the Management and Supervisory Boards is sufficiently clearly defined and implemented in accordance with the set criteria;
- whether there are members on the board who have appropriate banking knowledge and experience;

- the implementation of the succession concept;
- performance of the management body;
- efforts to achieve an appropriate gender balance in the Management Board or the Supervisory Board and to meet other requirements set out in the Diversity Policy.

With the aim of being familiar with and understanding the manner of work, the contents, the organisation and key strategic areas that the Bank manages in its operations, the Policy also defines the method and time of induction of new members. Apart from that, an annual training plan is adopted.

Considering the abovementioned criteria, the composition of both the Supervisory Board and the Management Board of the Bank is evident from the information published on the Bank's website.

The Nomination Committee, which was set up as a working body of the Supervisory Board, once a year or upon any substantial change in circumstances prepares a fit and proper assessment of the Management Board and Supervisory Board members as well as of the Management Board and Supervisory Board as the bodies of the Bank. This is a documented fit and proper assessment of every candidate for a Management Board or Supervisory Board member or the members already performing these functions, which includes reputation, experience and management. The assessment is made based on the predetermined procedures and criteria in line with the Policy on Fit and Proper Assessment of Management and Supervisory Board Members. When making a periodical assessment, on the basis of the knowledge and experience matrix of the existing members, the Bank defines the staffing profile, which is used in the recruitment of new Supervisory Board members and as the basis for developing a training plan for the Supervisory Board members.

In line with the law and the implementation of this Policy, the Supervisory Board of the Bank discussed and approved the fit and proper assessments also in December 2018.

The Policy on Fit and Proper Assessment of Key Function Holders in the Abanka Group was established so as to define the qualities required by the person who is a candidate for holding a key function in the Abanka Group and the qualities required by the person who already holds a key function in the Abanka Group. The key function holders are those employees whose work tasks and activities have a material impact on the operations and reputation of the Bank. These posts are defined in greater detail in the Policy. In defining the necessary qualities of the employee, the Bank adheres to the fit and proper principle.

The employee fit and proper assessment, which is a documented assessment of suitability of every candidate, is made during the selection process of a new employee or in the process of verifying compliance with the conditions of this Policy of existing employee due to changed circumstances or potential reappointment to the same or other key function. The fit and proper assessment of key function holders is made based on predetermined procedures and criteria in accordance with this Policy.

At least once a year, a periodic report is produced and presented to both the Nomination Committee and the Supervisory Board of the Bank on the implementation of this Policy. In line with the law and the implementation of this Policy, the Supervisory Board of the Bank discussed the report on the execution of the Policy on Fit and Proper Assessment of Key Function Holders in the Abanka Group also at the end of 2018.

REMUNERATION POLICY

Since the end of 2011, Abanka has regulated remuneration pursuant to the applicable legislation (the Banking Act (ZBan-2) and the regulations arising from this Act, the EBA Guidelines, Abanka's Remuneration Policy). As the Bank is subject to the special legislation for the companies in which the Republic of Slovenia, directly or indirectly, holds a majority stake and due to the commitments made to the European Commission under the restructuring plan, remuneration is also regulated in line with this legislation.

The bodies in charge of the formulation, implementation and control of the remuneration policy are the Management Board, the Remuneration Committee, the Risk Monitoring and Asset Liability Management Committee as the professional bodies of the Supervisory Board, and the Supervisory Board. Furthermore, independent control functions within the Bank participate in the development, control and assessment of adequacy of the remuneration policy. Once a year, the Bank reports on the implementation of the remuneration policy to the Remuneration Committee and the Supervisory Board as part of a periodic report; such a report was given also at the end of 2018.

The remuneration policy is designed for all employees and defines different employee groups, including the employee group based on the significance of their impact on the risk profile of the Bank in accordance with the criteria laid down in the EU regulations or in accordance with the criteria of the Bank. This group consists of the employees whose work is of a specific nature.

The remuneration policy of the Bank is based on the balance between remuneration and prudent risk-taking. The Bank ensures that through appropriate ratios between the fixed and the variable remuneration component of the employees whose work is of a specific nature, whereby the total remuneration of an employee may not significantly depend on the variable component. The remuneration policy and the relevant internal rules of the Bank regulate the ratios between the fixed and the variable component of managers' salaries, the mode of payment of the managers' variable remuneration component, and the period of deferred and retained variable remuneration of managers.

Employee remuneration is determined based on the assessment of adhering to the guidelines set in the business strategy and the risk management strategy, the corporate values, the risk appetite and long-term interests of the Bank.

In line with the remuneration policy, the employees whose work is of a specific nature are those employees whose work tasks and activities could have a material impact on the Bank’s risk profile.

The employees whose work is of a specific nature are defined based on qualitative and quantitative criteria of the remuneration policy.

The remuneration policy of Abanka is in compliance with its mission, business strategy, risk management strategy, corporate culture, values and the set goals. The remuneration policy and practice are strictly focused on the fulfilment of the Bank's business strategy objectives and adjusted to the risk profile of the Bank and its risk-taking ability.

Remuneration on the basis of manager employment agreements is linked to the fulfilment of objectives and criteria in compliance with the Bank's strategy and business plan. The amount of variable remuneration for the employees whose work is of a specific nature also depends on their contribution to achieving high professional and ethical standards of the Bank and a positive attitude towards the internal controls, based on which a strong organisational culture is built. The amount of variable remuneration can increase by achieving and exceeding concrete business and financial goals. Such a remuneration policy provides performance incentives, while simultaneously containing corrective measures in the case of critical deviations from the set goals. Appropriately set decision-taking processes and implemented business policies prevent any generation of improper risks in the business operations of the Bank.

INFORMATION TECHNOLOGY

The Information Technology Division is in charge of the development and management of the Bank's information system. Its role is to develop IT solutions and manage highly available, integrated, safe and user-friendly IT services at minimum cost and with maximum reliability. Moreover, the Information Technology Division is also in charge of ensuring security of the IT system.

The core of Abanka's information system is principally developed and maintained in-house, whereas the sub-systems that do not interact directly with the core are developed externally or already developed solutions are purchased. External development is actively managed and attention is paid that the IT solutions are compliant with the concepts, technologies and standards of the Bank.

In own software solution development, a great deal of effort was put in the activities connected with the support of the International Financial Reporting Standard (IFRS) 9, which became effective on 1 January 2018. To this end, some parts of software as well as support for the operational implementation of procedures and processes required upgrades.

In 2018, software solutions were focused on the development and introduction of modern IT concepts. Applications continued to be developed in the AIDO framework (the online Abanka integrated work environment); thus, the single customer view (SCV) system was further developed, the EWS application was upgraded to incorporate retail customers, while further upgrades were made to NKAPO, CEZ+ and several other applications. In the second half of 2018, all applications developed in the Java/JavaEE environment were reprogrammed and adapted to a later version and a new version of the IBM WAS application server (from version 8.5 to 9).

Furthermore, the Bank continued to introduce software solution development processes based on the continuous development/integration concept. The implementation of the application programming interface management (API management) system continued. The latter is already used by the Abaklub mobile application, and in 2018 it began to be used by the applications for opening an account, GDPR and subscribing to e-statements. Moreover, API is prepared to be integrated into Bankart for instant payments.

An important part of the development capacity was directed towards the projects focusing on the acceleration of digital transformation. Activities are underway in various areas. The online banking services for retail and corporate customers were upgraded, and the system for opening a transaction account online was upgraded with video identification, which is not yet in production. In the second half of 2018, intensive preparations were underway for the PSD2 project and the related project Digital Platform, which will set up the technical basis for open banking. The latter was officially approved at the end of December.

An important part of the development capacity was directed towards the projects focusing on the acceleration of digital transformation. Activities are underway in various areas.

In **outsourced software development** in 2018, the Division took part in the transfer of data in the context of selling investment brokerage services to a new owner. A considerable part of the resources was engaged on the project GDPR Implementation. A new solution for money laundering prevention was designed. The CRM system was deployed, accompanied by training and a user guide. Many tasks were related to the coordination of outsourcers for the development of upgrades adapted to a later version of the application server. The asset-liability management software is in the process of being implemented, but its completion has been delayed into 2019. In parallel, the existing software was upgraded, thereby ensuring smooth system functioning and asset-liability management during the implementation of new software. Part of the resources involved in the development of software for electronic and mobile banking for retail customers became part of the Agile Team, who employs agile methods to change the manner of work. A lot of time was devoted to participating in the implementation of audit recommendations. The solutions for legal aid, sending of statements by e-mail and periodic annual interviews were implemented. In the reporting period, the activities related to the digitalisation of incoming mail were carried out, which will continue in 2019.

In 2018, the greater part of resources allocated to the development of the **banking data warehouse** (BDW) was devoted to the activities related to the implementation of IFRS 9, the asset-liability management application and Basel interest-rate risk standards. Furthermore, the team was strongly involved in the AnaCredit project. The team also had to participate in various other projects of the Bank, especially by providing the necessary data from the data warehouse. Apart from that, various amendments to reporting were made due to the methodological changes (matrix reporting, the blacklist, LCR, NSFR, FINREP, CRM reports, guarantees, controlling DM, credit exposure) and development tasks/reports were implemented in the BI tool Business Objects. A relatively large part of development and maintenance work was required on the central systems of analytical accounting.

In **IT management**, the reporting year was marked by the activities relating to the consolidation and optimisation of the solutions and technologies used in Abanka. In accordance with the business needs and the consequent increase in data quantities, the data storage systems and databases were adapted. Obsolete central computer equipment and some of the peripheral equipment of end-users were replaced. The required adaptations and upgrades of the wired and wireless networks were made. The Division also participated in other projects undertaken by the Bank and its subsidiaries by providing IT support for new business applications and solutions and cooperating in the development of new security solutions. In addition, both the system and application software of servers, workstations and communication equipment were regularly updated. As every year, in 2018 the business continuity tests were performed.

In **technical support,** the focus was on internal user assistance requests, data processing, system operation control and installation of hardware and software.

In **information system protection and security** in 2018, Abanka analysed information technology and cyber risks, participated in the planning, development and implementation of new information systems and in making changes to the existing ones, as well as took part in incident management and IT audits and inspections. Great emphasis is put on cyber security, security checks and testing vulnerability using penetration tests.

In December 2018, the Management Board adopted the IT Strategy, which sets out the main development guidelines of the Bank for the coming two years. The main strategic initiative focuses on building a digital platform consisting of an integration platform and a central identity management system, which will separate the core systems from the applications intended for the customers as well as provide support for the PSD2 standard and development of API economy systems.

PROCUREMENT AND GENERAL AFFAIRS DEPARTMENT

By centrally managing and controlling the purchasing process, fixed assets and investments, the Procurement and General Affairs Department complies with the strategy of the Bank and achieves the set objectives.

The Department is strongly connected and intertwined with the business segments of the Bank; most of all, the Department aims to provide appropriate and rational support at the Bank level.

Its role is reflected in particular in the implementation of a cost-effective and rational purchasing process, responsible planning and management of fixed assets of the Bank, transparency of procedures, clearly defined purchasing rules, a comprehensive overview of costs and investments, and in careful selection of quality and reliable suppliers.

In 2018, key activities were related to fixed assets management, effective implementation of the purchasing process, cost and investment optimisation, maintenance of commercial buildings, optimisation of processes within the Department, regular monitoring of the relevant legislation, and coordination of development and project work.

The Bank pursues the goal of cost-effectiveness also in the management of real properties owned by the Bank and optimisation of business premises occupancy. Particular attention was paid to optimising the utilisation of business premises and to selling non-core assets. With respect to the latter, the Department cooperates with the subsidiary Anepremičnine.

Protection of property also represents an important part of activities. In 2018, technical and mechanical security systems were further upgraded and redesigned in order to ensure high standards of protection of property and people in the Bank. The best practice of regular employee training in security continued.

Taking into account the regulatory changes in personal data protection and the GDPR, the Department was strongly involved in making adjustments to archiving, especially with regard to electronic documents.

INTERNAL AUDIT

The internal audit control function as the third line of defence is performed by the Internal Audit Department (hereinafter: IAD), which is functionally and organisationally separated from other units and is directly subordinated to the Management Board of the Bank. The IAD regularly reports on its work, audit findings and the implementation of recommendations also to the Audit Committee and the Supervisory Board. The Internal Audit Department operates in accordance with the Banking Act, the International Standards for the Professional Practice of Internal Auditing, the Code of Professional Ethics for Internal Auditors and the Code of Internal Auditing Principles. The work of the IAD as a whole is regulated by the Rules on the Internal Audit Department, which are adopted by the Management Board with the approval of the Supervisory Board. The operating procedures of the internal audit activity are defined in greater detail in the Manual on Internal Auditing.

The IAD provides to the management body, the Audit Committee and senior management an independent assessment of the quality and efficiency of internal management, including the risk management and internal control systems and processes, and thereby contributes not only to improving the performance and achievement of the Bank's objectives but also to strengthening risk management and internal governance. The IAD carries out its mission by performing internal audits of riskier areas and providing advisory services in line with the IAD's annual plan and the strategic work plan. Both plans are based on the risk analysis and regulatory requirements and are approved by the Management Board with the consent of the Supervisory Board. In 2018, the IAD concentrated on regulatory mandatory and riskier areas: appropriate separation of powers and duties, risk management development activities connected to the internal processes for determining sufficient capital and liquidity levels, drawing up of the Bank's recovery plans and strategy, the money laundering monitoring and prevention system, personal data protection, corporate lending, implementation of regulatory requirements for leveraged transactions, non-performing loan management, the human resource function and compliance of remuneration with the remuneration policy.

In addition to internal auditing and advisory services, the IAD's employees devoted a considerable amount of their time to the monitoring of the implementation of recommendations made in audits. In 2018, the IAD was subject to an external quality assessment, which confirmed the IAD's general compliance with the International Standards for the Professional Practice of Internal Auditing, its independence and objectivity.

As at 31 December 2018, the IAD employed 8 internal auditors including the IAD Director. The internal auditors have adequate knowledge of the field and the banking processes and hold the following titles and/or licences: certified internal auditor, auditor, certified information systems auditor, certified auditor, FACCA[13] and CISA[14]. Being aware of the importance of internal audit in its governance system, the Bank not only invests in employee training and acquiring additional licenses of internal audit employees but also actively seeks new recruits.

[13] FACCA stands for Fellow Chartered and Certified Accountant.
[14] CISA stands for Certified Information Systems Auditor.

SENIOR MANAGEMENT

MANAGEMENT BOARD	Jože Lenič	President of the Management Board
	Matej Golob Matzele	Member of the Management Board
	Matevž Slapničar	Member of the Management Board
Coord. of work with the regulator and supervisory bodies	Mitja Mavko	The authorised Representative of the Management Board
Coordination of subsidiaries	Davorin Leskovar	The authorised Representative of the Management Board
Procurement and General Affairs	Davorin Leskovar	In charge of Procurement and General Affairs
Compliance	Bojan Salobir	Director of the Compliance
Internal Audit	Tatjana Kirn Volk	Director of the Internal Audit
Custody and Administrative Services	Klavdija Markič	Director of the Custody and Administrative Services
Legal	Tomaž Marinček	Director of the Legal
Personnel and Organisation	Mateja Sedej	Director of the Personnel and Organisation
Development and Marketing	Jasna Kajtazović	Director of the Development and Marketing
Development and Marketing	Tomaž Poznič	Director of the Development and Marketing (replacement during absence)
CORPORATE BANKING DIVISION	Blaž Stiplovšek	Division Executive Director
	Aleš Zupančič	Assistant Executive Director
	Barbara Jagodič	Director of the Key Accounts Sector
	Tina Možina	Director of the SME Banking Sector
	Nataša Velunšek Golčer	Director of the Documentary and Neutral Banking Products
RETAIL BANKING AND SMALL BUSINESS DIVISION	Nataša Damjanovič	Division Executive Director
	Simon Ličen	Director of Sales and Sales Channels Management
	Bojan Stanković	Director of the Central Slovenia Main Branch Office
	Alenka Kikec	Director of the Celje Main Branch Office
	Nastja Colja	Director of the West Slovenia Main Branch Office
	Urška Travner	Director of the East Slovenia Main Branch Office
FINANCIAL MARKETS DIVISION	Boštjan Herič	Division Executive Director
	Jure Gedrih	Director of the Treasury
	Blaž Angel	Director of the Investment Banking
RISK MANAGEMENT DIVISION	Boštjan Rupar	Division Executive Director
	Jure Poljšak	Director of Credit Risk Management
	Matej Jovan	Director of Risk Monitoring
	Simon Svet	Director of the Investments Under Scrutiny
	Tatjana Štuler Štavt	Director of the Assets and Liabilities Management
FINANCE DIVISION	Alenka Plut	Division Executive Director
	Irena Rojc	Director of the Accounting
	Silva Matko Gosak	Director of the Controlling and Reporting
INFORMATION TECHNOLOGY DIVISION	Matej Jereb	Division Executive Director
	Vojko Božiček	Assistant Executive Director and in charge of Information Technology Development
	Marko Zabukovec	Director of the Data Warehouse Development
	Davor Hvala	Director of the IT Governance
	Ivan Turk	Director of the Information Technology
BACK-OFFICE OPERATIONS DIVISION	Nada Mertik	Division Executive Director
	Mojca Žlak	Director of the Back-Office Operations
	Marija Kordiš	Director of the Banking Operations

Senior management organisational chart as at 31 December 2018.

BRANCH NETWORK

Regional and branch offices of Abanka

CENTRAL SLOVENIA MAIN BRANCH OFFICE

Slovenska Branch Office	Slovenska 50	Ljubljana
Šiška Branch Office	Celovška 106	Ljubljana
Bežigrad Branch Office	Dunajska 48	Ljubljana
Njegoševa Branch Office	Njegoševa 8	Ljubljana
Smelt Branch Office	Dunajska 160	Ljubljana
Vič Branch Office	Tržaška 87	Ljubljana
Šmartinska Branch Office	Šmartinska 102–104	Ljubljana
Logatec Branch Office	Tržaška 50a	Logatec
Domžale Branch Office	Ulica Nikola Tesla 19	Domžale
Novo mesto Branch Office	Rozmanova 40	Novo mesto
Novo mesto Mercator center Branch Office	Ljubljanska c. 47	Novo mesto
Trnovo Branch Office	Ziherlova 4	Ljubljana
Kranj Branch Office	Nazorjeva 1	Kranj
Jesenice Branch Office	Maršala Tita 39a	Jesenice
Tržič Branch Office	Cankarjeva 1a	Tržič
Abasvet Branch Office	Trdinova 4	Ljubljana

EAST SLOVENIA MAIN BRANCH OFFICE

Glavni trg Branch Office	Glavni trg 18	Maribor
Cankarjeva Branch Office	Cankarjeva 6b	Maribor
Tabor Branch Office	Kardeljeva 61	Maribor
Murska Sobota Branch Office	Kocljeva 16	Murska Sobota
Ptuj Branch Office	Osojnikova 9	Ptuj
Slovenj Gradec Branch Office	Ronkova 4a	Slovenj Gradec
Tezno Branch Office	Prvomajska 26	Maribor
Slovenske Konjice Branch Office	Oplotniška 1A	Slovenske Konjice
Zreče Branch Office	Cesta na Roglo 13B	Zreče
Rogaška Slatina Branch Office	Kidričeva 5	Rogaška Slatina
Podčetrtek Branch Office	Zdraviliška cesta 27C	Podčetrtek
Rogatec Branch Office	Ulica ceste 10	Rogatec

WEST SLOVENIA MAIN BRANCH OFFICE

Koper Branch Office	Ferrarska 12	Koper
Izola Branch Office	Sončno nabrežje 6	Izola
Sežana Branch Office	Partizanska 41	Sežana
Erjavčeva Branch Office	Erjavčeva 2	Nova Gorica
Šempeter Branch Office	C. Prekomorskih brigad 2c	Šempeter pri Gorici
Kidričeva Branch Office	Kidričeva 18	Nova Gorica
Ajdovščina Branch Office	Goriška 25a	Ajdovščina
Idrija Branch Office	Lapajnetova 47	Idrija
Tolmin Branch Office	Mestni trg 5	Tolmin
Kobarid Branch Office	Markova 16	Kobarid
Postojna Branch Office	Titov trg 1	Postojna

CELJE MAIN BRANCH OFFICE

Aškerčeva Branch Office	Aškerčeva 10	Celje
Vojnik Branch Office	Celjska cesta 29	Vojnik
CMH Branch Office	Krekov trg 6	Celje
Citycenter Branch Office	Mariborska cesta 100	Celje
TUŠ Celje Branch Office	Mariborska cesta 128	Celje
Žalec Branch Office	Savinjska cesta 20	Žalec
Mozirje Branch Office	Na trgu 53	Mozirje
Polzela Branch Office	Malteška cesta 38	Polzela
Šentjur Branch Office	Mestni trg 8	Šentjur
Laško Branch Office	Valvasorjev trg 5	Laško
Radeče Branch Office	Ulica OF 4A	Radeče
Šmarje Branch Office	Aškerčev trg 13	Šmarje pri Jelšah
Miklošičeva Branch Office	Miklošičeva 1	Celje
Velenje Branch Office	Kersnikova 1	Velenje

Branch network overview as at 31 December 2018.

Table: GRI content index

Indicator	Page
Organisational profile	
102-1 Name of the organisation	21
102-2 Activities, services	20
102-3 Location of headquarters	21
102-4 Location of operations	103, 104
102-5 Ownership and legal form	19, 42, 43
102-6 Markets served	19, 21
102-7 Scale of the organisation	21
102-8 Information on employees	91
102-10 Significant changes to the organisation	25, 26
102-13 Membership of associations	68
Strategy	
102-14 Management Board Statement	12, 13
102-15 Key impacts, strategy, risks and opportunities	23, 62
Ethics and integrity	
102-16 Values, principles, standards and norms of behaviour	66, 67
102-17 Mechanisms for advice and concerns about ethics	66, 67
Governance	
102-18 Governance structure	59, 89
102-19 Delegating authority	59, 89
102-22 Composition of the highest governance body	59
102-23 Chair of the highest governance body	59
102-24 Nominating and selecting the highest governance body	95, 96
102-26 Role of highest governance body in setting purpose, values and strategy	48
102-27 Collective knowledge of highest governance body	59
102-28 Evaluating the highest governance body's performance	50, 101
102-29 Identifying and managing economic, environmental and social impacts	62, 63
102-30 Effectiveness of risk management processes	77, 78, 83, 84, 85
102-35 Remuneration policy	59, 96
Stakeholder engagement	
102-40 List of stakeholder groups	64
102-42 Identifying and selecting stakeholders	64, 65
102-43 Approach to stakeholder engagement	44, 45, 46, 47, 65, 70, 71
102-44 Key topics and concerns raised	47, 65, 70
Reporting practice	
102-45 Entities included in the consolidated financial statements	21
102-46 Defining report content and topic boundaries	66, 67
102-47 List of material topics	65
102-50 Reporting period	66
102-51 Date of most recent report	66
102-52 Reporting cycle	66
102-53 Contact point for questions regarding the report	67
102-54 Claims of reporting in accordance with the GRI Standards	106
102-55 GRI content index	105, 106
Economic performance	
201-1 Financial results	31
Market presence	
202-1 Proportion of senior management hired from the local community	59

Indicator	Page
Indirect economic impacts	
203-2 Significant indirect economic impacts	68
204-1 Cooperation with local suppliers	69
Materials	
301-1 Materials used	75
301-2 Recycled input materials used	75, 76
Energy	
302-1 Energy consumption within the organisation	75, 76
Employment	
401-1 Employees	91
401-2 Standard benefits provided to full-time employees	93, 94
402-1 Management/labour relations in terms of notification	65, 71
Occupational health and safety	
403-1 Employee health and safety	72, 94
403-4 Cooperation with trade unions	73, 94
Training and education	
404-1 Scope of employee training	72, 92, 93
404-2 Training programmes	72, 92, 93
404-3 Career development	93
Diversity and equal opportunity	
405-1 Diversity of governance bodies and employees	59
Non-discrimination	
406-1 Non-discrimination	94
Security practices	
410-1 Security practices	71, 99
Local communities	
413-1 Relations with local communities	70, 71, 73, 74
Customer health and safety	
416-1 Impacts of the organisation on customer health and safety	71
Marketing and labelling	
417-1 Product and service information for the protection of customer interests	44, 45, 46, 47, 70, 71, 73, 74
Socioeconomic compliance	
419-1 Compliance with laws and regulations in the social and economic area	66, 67

This report has been prepared in accordance with the GRI Standards: Core.

FINANCIAL REPORT

Moving forward with ideas

Innovation is one of Abanka's core values, and it received new impetus in 2018, when we introduced the Aideja system, in which employees propose new ideas to improve work at the Bank. Very successful: in only a few months, we collected more than 200 ideas, some of which have already been implemented.

STATEMENT OF MANAGEMENT'S RESPONSIBILITIES

The Management Board of the Bank has approved the financial statements of ABANKA d.d. and the consolidated financial statements of the ABANKA GROUP for the year ended 31 December 2018 (pages 111 to 124 of the Annual Report), the applied accounting policies, and the notes to the financial statements (pages 125 to 270 of the Annual Report).

The Management Board is responsible for preparing the Annual Report, which gives a true and fair representation of the financial position of the Bank and the Group as at 31 December 2018, and the results of their operations for the year then ended.

The Management Board confirms that accepted accounting policies have been used on a consistent basis, and that the accounting estimates have been made in compliance with the principles of prudence and good management. The Management Board also confirms that the financial statements with the accompanying notes have been prepared on the assumption of a going concern for the Bank and the Group and in compliance with the relevant legislation and International Financial Reporting Standards, as adopted by the EU.

The Management Board is also responsible for the proper management of accounting, taking appropriate measures to protect the Group's assets, as well as for preventing and discovering fraud and other irregularities or illegal acts.

In the year ended 31 December 2018, Abanka d.d. did not start any related party transactions under unusual market conditions.

Ljubljana, 22 March 2019

Management Board

Matevž SLAPNIČAR	**Matej GOLOB MATZELE**	**Jože LENIČ**
Member of the Management Board	Member of the Management Board	President of the Management Board

FINANCIAL STATEMENTS

INDEX TO THE FINANCIAL STATEMENTS

NOTE PAGE

NOTE	PAGE

(All amounts in EUR thousand unless otherwise stated)

INCOME STATEMENT OF ABANKA D.D.

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	**2**		**3**	**4**
1	Interest income	6	67,167	78,488
2	Interest expenses	6	(6,557)	(6,573)
3	**Net interest income (1+2)**		**60,610**	**71,915**
4	Dividend income	7	1,435	1,588
5	Fee and commission income	8	53,227	50,757
6	Fee and commission expenses	8	(16,290)	(14,377)
7	**Net fee and commission income (5+6)**		**36,937**	**36,380**
8	Net gains on financial assets and liabilities not measured at fair value through profit or loss	9	18,229	10,626
9	Net gains on financial assets and liabilities held for trading	10	3,199	2,360
10	Net gains on non-trading financial assets mandatorily at fair value through profit or loss	11	4,345	/
11	Net losses on financial assets and liabilities designated at fair value through profit or loss		(410)	(45)
12	Exchange differences		(628)	415
13	Net losses on derecognition of non-financial assets		(79)	(270)
14	Net other operating expenses	12	(916)	(4,283)
15	Administrative expenses	13	(63,798)	(65,424)
16	Depreciation and amortisation	14	(7,235)	(7,373)
17	Net losses on modification of financial assets		(52)	/
18	Provisions	15	(76)	(5,409)
19	Impairment	16	17,341	7,352
20	Total profit from non-current assets held for sale		2,310	3
21	TOTAL PROFIT BEFORE TAX FROM CONTINUING OPERATIONS (3+4+7 to 20)		71,212	47,835
22	Tax expense related to profit from continuing operations	17	(4,475)	(5,215)
23	TOTAL PROFIT AFTER TAX FROM CONTINUING OPERATIONS (21+22)		66,737	42,620
24	**NET PROFIT for the financial year (23)**		**66,737**	**42,620**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

Matevž SLAPNIČAR
Member of the Management Board

Matej GOLOB MATZELE
Member of the Management Board

Jože LENIČ
President of the Management Board

The notes on pages 125 to 270 are an integral part of these financial statements.

(All amounts in EUR thousand unless otherwise stated)

STATEMENT OF COMPREHENSIVE INCOME OF ABANKA D.D.

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	2		3	4
1	**NET PROFIT FOR THE FINANCIAL YEAR AFTER TAX**		**66,737**	**42,620**
2	**OTHER COMPREHENSIVE LOSS AFTER TAX (3+4)**		**(498)**	**(9,149)**
3	**ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS (3.1 + 3.2 + 3.3)**		**205**	**(147)**
3.1	Actuarial losses on defined benefit pension plans	34	(31)	(147)
3.2	Fair value changes of equity instruments measured at fair value through other comprehensive income		291	/
3.3	Income tax relating to items that will not be reclassified to profit or loss	36	(55)	/
4	**ITEMS THAT MAY BE RECLASSIFIED TO PROFIT OR LOSS (4.1 + 4.2 + 4.3)**		**(703)**	**(9,002)**
4.1	Debt instruments at fair value through other comprehensive income (4.1.1 + 4.1.2)		(868)	/
4.1.1	Net valuation losses taken to equity		(978)	/
4.1.2	Net losses transferred to profit or loss		110	/
4.2	Available-for-sale financial assets (IAS 39) (4.2.1 + 4.2.2)		/	(11,114)
4.2.1	Net valuation losses taken to equity		/	(6,822)
4.2.2	Net gains transferred to profit or loss		/	(4,292)
4.3	Income tax relating to items that may be reclassified to profit or loss	36	165	2,112
5	**TOTAL COMPREHENSIVE INCOME FOR THE FINANCIAL YEAR AFTER TAX (1+2)**		**66,239**	**33,471**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

Matevž SLAPNIČAR
Member of the Management Board

Matej GOLOB MATZELE
Member of the Management Board

Jože LENIČ
President of the Management Board

The notes on pages 125 to 270 are an integral part of these financial statements.

(All amounts in EUR thousand unless otherwise stated)

STATEMENT OF FINANCIAL POSITION OF ABANKA D.D.

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT As at 31 December 2018	As at 1 January 2018*	As at 31 December 2017
1	**2**		**3**	**4**	**5**
1	Cash, cash balances with the central bank and other demand deposits with banks	18	537,269	411,665	411,665
2	Financial assets held for trading	19	3,837	3,048	3,048
3	Non-trading financial assets mandatorily at fair value through profit or loss	20	36,587	41,580	/
4	Financial assets at fair value through other comprehensive income	21	163,466	173,619	/
5	Available-for-sale financial assets (IAS 39)	22	/	/	1,090,690
6	Financial assets at amortised cost		2,924,518	2,925,180	/
	– debt securities	23	946,334	890,409	/
	– loans to banks	23	30,784	60,732	/
	– loans to non-bank customers	23	1,934,862	1,950,326	/
	– other financial assets	23	12,538	23,713	/
7	Loans and receivables (IAS 39)		/	/	2,066,543
	– loans to banks	24	/	/	60,745
	– loans to non-bank customers	24	/	/	1,982,137
	– other financial assets	24	/	/	23,661
8	Held-to-maturity investments (IAS 39)	25	/	/	15,408
9	Investments in subsidiaries	27	8,278	9,448	9,448
10	Tangible assets		33,033	36,412	36,412
	– property and equipment	26	32,832	36,228	36,228
	– investment property	26	201	184	184
11	Intangible assets	26	8,930	7,254	7,254
12	Tax assets		10,225	12,436	12,408
	– current tax assets	35	–	3,323	3,323
	– deferred tax assets	35	10,225	9,113	9,085
13	Other assets	28	2,082	2,303	2,302
14	Non-current assets held for sale	26	488	806	806
15	**TOTAL ASSETS (from 1 to 14)**		**3,728,713**	**3,623,751**	**3,655,984**

* The financial statements as at 1 January 2018 are not audited and are presented only as additional information about the effects of the transition to IFRS 9, which are presented in more detail in Section 44.

(All amounts in EUR thousand unless otherwise stated)

STATEMENT OF FINANCIAL POSITION OF ABANKA D.D. (continued)

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT As at 31 December 2018	As at 1 January 2018*	As at 31 December 2017
1	**2**		**3**	**4**	**5**
16	Financial liabilities held for trading	19	3,044	2,492	2,492
17	Financial liabilities designated at fair value through profit or loss		2,281	1,871	/
18	Financial liabilities at amortised cost		3,089,588	3,013,637	3,013,637
	– deposits from banks and the central bank	30	16,335	24,243	24,243
	– deposits from non-bank customers	31	2,935,218	2,860,697	2,860,697
	– loans from banks and the central bank	30	102,788	89,011	89,011
	– loans from non-bank customers		5	500	500
	– debt securities issued	32	13,644	13,021	13,021
	– other financial liabilities	33	21,598	26,165	26,165
19	Provisions	34	46,059	43,374	53,676
20	Tax liabilities		2,732	1,263	5,960
	– current tax liabilities	35	1,897	304	–
	– deferred tax liabilities	35	835	959	5,960
21	Other liabilities		1,625	1,366	1,276
22	TOTAL LIABILITIES (from 16 to 21)		3,145,329	3,064,003	3,077,041
23	Share capital	36	151,000	151,000	151,000
24	Share premium	36	282,459	282,459	282,459
25	Accumulated other comprehensive income	36	3,333	3,831	33,317
26	Reserves from profit	36	58,384	51,710	51,710
27	Retained earnings (including income from the current year)		88,208	70,748	60,457
28	TOTAL EQUITY (from 23 to 27)		583,384	559,748	578,943
29	**TOTAL LIABILITIES AND EQUITY (22+28)**		**3,728,713**	**3,623,751**	**3,655,984**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

Matevž SLAPNIČAR
Member of the Management Board

Matej GOLOB MATZELE
Member of the Management Board

Jože LENIČ
President of the Management Board

The notes on pages 125 to 270 are an integral part of these financial statements.

(All amounts in EUR thousand unless otherwise stated)

STATEMENT OF CHANGES IN EQUITY OF ABANKA D.D. FOR THE REPORTING PERIOD ENDED 31 DECEMBER 2018

Item No.	ITEM DESCRIPTION	Share capital	Share premium	Accumulated other comprehensive income	Reserves from profit	Retained earnings (including income from the current year)	Total Equity (from 3 to 7)
1	2	3	4	5	6	7	8
1	**OPENING BALANCE FOR THE REPORTING PERIOD** (before adjustments)	**151,000**	**282,459**	**33,317**	**51,710**	**60,457**	**578,943**
2	Transition to IFRS 9 (Note 44)	–	–	(29,486)	–	10,937	**(18,549)**
3	Transition to IFRS 9 - correction (spin-off)	–	–	–	–	(646)	**(646)**
4	**OPENING BALANCE FOR THE REPORTING PERIOD (1+2+3)**	**151,000**	**282,459**	**3,831**	**51,710**	**70,748**	**559,748**
5	**Comprehensive income for the financial year after tax**	**–**	**–**	**(498)**	**–**	**66,737**	**66,239**
6	Dividends (Note 37)	–	–	–	–	(42,620)	**(42,620)**
7	Transfer of net profit to reserves from profit	–	–	–	6,674	(6,674)	**–**
8	Other	–	–	–	–	17	**17**
9	**CLOSING BALANCE FOR THE REPORTING PERIOD (4+5+6+7+8)**	**151,000**	**282,459**	**3,333**	**58,384**	**88,208**	**583,384**
10	**DISTRIBUTABLE PROFIT FOR THE FINANCIAL YEAR**	**–**	**–**	**–**	**–**	**88,208**	**88,208**

STATEMENT OF CHANGES IN EQUITY OF ABANKA D.D. FOR THE REPORTING PERIOD ENDED 31 DECEMBER 2017

Item No.	ITEM DESCRIPTION	Share capital	Share premium	Accumulated other comprehensive income	Reserves from profit	Retained earnings (including income from the current year)	Total Equity (from 3 to 7)
1	2	3	4	5	6	7	8
1	**OPENING BALANCE FOR THE REPORTING PERIOD**	**151,000**	**282,459**	**42,466**	**47,448**	**91,078**	**614,451**
2	**Comprehensive income for the financial year after tax**	**–**	**–**	**(9,149)**	**–**	**42,620**	**33,471**
3	Dividends	–	–	–	–	(68,991)	**(68,991)**
4	Transfer of net profit to reserves from profit	–	–	–	4,262	(4,262)	**–**
5	Other	–	–	–	–	12	**12**
6	**CLOSING BALANCE FOR THE REPORTING PERIOD (1+2+3+4+5)**	**151,000**	**282,459**	**33,317**	**51,710**	**60,457**	**578,943**
7	**DISTRIBUTABLE PROFIT FOR THE FINANCIAL YEAR**	**–**	**–**	**–**	**–**	**60,457**	**60,457**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

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Member of the Management Board

Jože LENIČ
President of the Management Board

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(All amounts in EUR thousand unless otherwise stated)

CASH FLOW STATEMENT OF ABANKA D.D.

Desig-nation	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	2		3	4
A	**CASH FLOWS FROM OPERATING ACTIVITIES**			
a)	Total profit before tax		71,212	47,835
	Depreciation and amortisation	14	7,235	7,373
	Impairments of investments in debt securities measured at fair value through other comprehensive income	16	113	/
	(Reversal of impairments) of loans and other financial assets measured at amortised cost	16	(17,875)	(6,823)
	(Reversal of impairments) of investments in subsidiaries	16	–	(529)
	Impairments of tangible assets (including investment property)	16	283	–
	Net losses/(gains) from exchange differences		628	(415)
	Net losses from sale of tangible assets		78	101
	Net losses from sale of intangible assets		1	163
	Other (gains) from investing activities	38	(10,941)	(802)
	Net (gains) from sale of investment in a subsidiary	27	(307)	–
	Other adjustments to total profit or loss before tax	38	(3,858)	5,473
	Cash flows from operating activities before changes in operating assets and liabilities		**46,569**	**52,376**
b)	**Decreases in operating assets (excluding cash & cash equivalents)**		**66,682**	**4,186**
	Net (increase)/decrease in financial assets held for trading		(781)	2,169
	Net decrease in non-trading financial assets mandatorily at fair value through profit or loss		9,339	/
	Net decrease in financial assets measured at fair value through other comprehensive income		10,211	/
	Net decrease in financial assets designated at fair value through profit or loss		–	2,412
	Net decrease in financial assets available for sale (IAS 39)		/	154,896
	Net decrease/(increase) in loans and other financial assets measured at amortised cost		46,625	(155,407)
	Net decrease in non-current assets held for sale		1,086	–
	Net decrease in other assets		202	116
c)	**Increases in operating liabilities**		**69,506**	**95,624**
	Net increase/(decrease) in financial liabilities held for trading		552	(2,435)
	Net increase in received deposits and loans measured at amortised cost		68,072	105,952
	Net increase/(decrease) in debt securities issued measured at amortised cost		623	(8,026)
	Net increase in other liabilities		259	133
d)	**Cash flows from operating activities (a+b+c)**		**182,757**	**152,186**
e)	**Income taxes (paid)**		**(659)**	**(11,969)**
f)	**Net cash flows from operating activities (d+e)**		**182,098**	**140,217**

(All amounts in EUR thousand unless otherwise stated)

CASH FLOW STATEMENT OF ABANKA D.D. (continued)

Designation	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	2		3	4
B	**CASH FLOWS FROM INVESTING ACTIVITIES**			
a)	**Receipts from investing activities**		**232,297**	**17,579**
	Receipts from the sale of tangible assets		74	154
	Receipts from the disposal of a subsidiary	27	1,477	–
	Receipts from the disposal and maturity of investments in debt securities measured at amortised cost		224,749	–
	Receipts from the sale of financial assets held to maturity (IAS 39)		/	17,422
	Receipts from non-current assets held for sale		5,997	3
b)	**Cash payments on investing activities**		**(277,243)**	**(4,630)**
	(Cash payments to acquire tangible assets)		(1,785)	(1,807)
	(Cash payments to acquire intangible assets)		(5,130)	(2,823)
	(Cash payments to acquire debt securities measured at amortised cost)		(270,328)	–
c)	**Net cash flows from investing activities (a+b)**		**(44,946)**	**12,949**
C	**CASH FLOWS FROM FINANCING ACTIVITIES**			
a)	**Cash proceeds from financing activities**		**–**	**–**
b)	**Cash payments on financing activities**		**(42,620)**	**(68,991)**
	(Dividends paid)	37	(42,620)	(68,991)
c)	**Net cash flows from financing activities (a+b)**		**(42,620)**	**(68,991)**
D	Effects of change in exchange rates on cash and cash equivalents		2,564	(10,028)
E	**Net increase in cash and cash equivalents (Af+Bc+Cc)**		**94,532**	**84,175**
F	**Opening balance of cash and cash equivalents**		**459,907**	**385,760**
G	**Closing balance of cash and cash equivalents (D+E+F)**	**38**	**557,003**	**459,907**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

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Jože LENIČ
President of the Management Board

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(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED INCOME STATEMENT OF THE ABANKA GROUP

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	**2**		**3**	**4**
1	Interest income	6	67,638	80,006
2	Interest expenses	6	(6,563)	(6,578)
3	**Net interest income (1+2)**		**61,075**	**73,428**
4	Dividend income	7	1,435	1,588
5	Fee and commission income	8	53,212	50,742
6	Fee and commission expenses	8	(16,343)	(14,429)
7	**Net fee and commission income (5+6)**		**36,869**	**36,313**
8	Net gains on financial assets and liabilities not measured at fair value through profit or loss	9	18,229	9,742
9	Net gains on financial assets and liabilities held for trading	10	3,199	2,360
10	Net gains on non-trading financial assets mandatorily at fair value through profit or loss	11	4,345	/
11	Net losses on financial assets and liabilities designated at fair value through profit or loss		(410)	(45)
12	Exchange differences		(628)	415
13	Net losses on derecognition of non-financial assets		(57)	(189)
14	Net other operating income/(expenses)	12	307	(3,356)
15	Administrative expenses	13	(65,243)	(67,626)
16	Depreciation and amortisation	14	(7,804)	(8,559)
17	Net losses on modification of financial assets		(52)	/
18	Provisions	15	(78)	(5,412)
19	Impairment	16	18,006	8,198
20	Total profit from non-current assets held for sale		888	165
21	TOTAL PROFIT BEFORE TAX FROM CONTINUING OPERATIONS (3+4+7 to 20)		70,081	47,022
22	Tax expense related to profit from continuing operations	17	(4,489)	(5,427)
23	TOTAL PROFIT AFTER TAX FROM CONTINUING OPERATIONS (21+22)		65,592	41,595
24	**NET PROFIT for the financial year (23)**		**65,592**	**41,595**

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(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME OF THE ABANKA GROUP

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	**2**		**3**	**4**
1	**NET PROFIT FOR THE FINANCIAL YEAR AFTER TAX**		**65,592**	**41,595**
2	**OTHER COMPREHENSIVE LOSS AFTER TAX (3+4)**		**(496)**	**(9,161)**
3	**ITEMS THAT WILL NOT BE RECLASSIFIED TO PROFIT OR LOSS (3.1 + 3.2 + 3.3)**		**207**	**(159)**
3.1	Actuarial losses on defined benefit pension plans	34	(29)	(159)
3.2	Fair value changes of equity instruments measured at fair value through other comprehensive income		291	/
3.3	Income tax relating to items that will not be reclassified to profit or loss	36	(55)	/
4	**ITEMS THAT MAY BE RECLASSIFIED TO PROFIT OR LOSS (4.1 + 4.2 + 4.3)**		**(703)**	**(9,002)**
4.1	Debt instruments at fair value through other comprehensive income (4.1.1 + 4.1.2)		(868)	/
4.1.1	Net valuation losses taken to equity		(978)	/
4.1.2	Net losses transferred to profit or loss		110	/
4.2	Available-for-sale financial assets (IAS 39) (4.2.1 + 4.2.2)		/	(11,114)
4.2.1	Net valuation losses taken to equity		/	(6,822)
4.2.2	Net gains transferred to profit or loss		/	(4,292)
4.3	Income tax relating to items that may be reclassified to profit or loss	36	165	2,112
5	**TOTAL COMPREHENSIVE INCOME FOR THE FINANCIAL YEAR AFTER TAX (1+2)**		**65,096**	**32,434**

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(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION OF THE ABANKA GROUP

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT As at 31 December 2018	As at 1 January 2018*	As at 31 December 2017
1	**2**		**3**	**4**	**5**
1	Cash, cash balances with the central bank and other demand deposits with banks	18	538,234	412,168	412,168
2	Financial assets held for trading	19	3,837	3,048	3,048
3	Non-trading financial assets mandatorily at fair value through profit or loss	20	36,587	41,580	/
4	Financial assets at fair value through other comprehensive income	21	163,466	173,619	/
5	Available-for-sale financial assets (IAS 39)	22	/	/	1,090,690
6	Financial assets at amortised cost		2,918,162	2,910,591	/
	– debt securities	23	946,334	890,409	/
	– loans to banks	23	30,784	60,732	/
	– loans to non-bank customers	23	1,928,338	1,935,481	/
	– other financial assets	23	12,706	23,969	/
7	Loans and receivables (IAS 39)		/	/	2,052,122
	– loans to banks	24	/	/	60,745
	– loans to non-bank customers	24	/	/	1,967,460
	– other financial assets	24	/	/	23,917
8	Held-to-maturity investments (IAS 39)	25	/	/	15,408
9	Tangible assets		37,496	45,985	45,985
	– property and equipment	26	33,072	38,963	38,963
	– investment property	26	4,424	7,022	7,022
10	Intangible assets	26	9,074	7,427	7,427
11	Tax assets		10,225	12,324	12,296
	– current tax assets	35	–	3,164	3,164
	– deferred tax assets	35	10,225	9,160	9,132
12	Other assets	28	9,459	13,963	13,962
13	Non-current assets held for sale	26	5,002	1,071	1,071
14	**TOTAL ASSETS (from 1 to 13)**		**3,731,542**	**3,621,776**	**3,654,177**

* The financial statements as at 1 January 2018 are not audited and are presented only as additional information about the effects of the transition to IFRS 9, which are presented in more detail in Section 44.

(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION OF THE ABANKA GROUP (continued)

Item No.	ITEM DESCRIPTION	NOTE	AMOUNT As at 31 December 2018	As at 1 January 2018*	As at 31 December 2017
1	2		3	4	5
15	Financial liabilities held for trading	19	3,044	2,492	2,492
16	Financial liabilities designated at fair value through profit or loss		2,281	1,871	/
17	Financial liabilities at amortised cost		3,089,052	3,008,973	3,008,973
	– deposits from banks and the central bank	30	16,335	24,243	24,243
	– deposits from non-bank customers	31	2,934,448	2,855,544	2,855,544
	– loans from banks and the central bank	30	102,788	89,011	89,011
	– loans from non-bank customers		5	482	482
	– debt securities issued	32	13,644	13,021	13,021
	– other financial liabilities	33	21,832	26,672	26,672
18	Provisions	34	46,109	43,500	53,796
19	Tax liabilities		2,550	1,263	5,960
	– current tax liabilities	35	1,715	304	–
	– deferred tax liabilities	35	835	959	5,960
20	Other liabilities		5,099	2,763	2,673
21	TOTAL LIABILITIES (from 15 to 20)		3,148,135	3,060,862	3,073,894
22	Share capital	36	151,000	151,000	151,000
23	Share premium	36	282,459	282,459	282,459
24	Accumulated other comprehensive income	36	3,332	3,798	33,284
25	Reserves from profit	36	58,401	51,760	51,760
26	Retained earnings (including income from the current year)		88,215	71,897	61,780
27	TOTAL EQUITY (from 22 to 26)		583,407	560,914	580,283
28	**TOTAL LIABILITIES AND EQUITY (21+27)**		**3,731,542**	**3,621,776**	**3,654,177**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

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Jože LENIČ
President of the Management Board

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(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY OF THE ABANKA GROUP FOR THE REPORTING PERIOD ENDED 31 DECEMBER 2018

Item No.	ITEM DESCRIPTION	Share capital	Share premium	Accumu-lated other comprehen-sive income	Reserves from profit	Retained earnings (including income from the current year)	Total Equity (from 3 to 7)
1	2	3	4	5	6	7	8
1	**OPENING BALANCE FOR THE REPORTING PERIOD** (before adjustments)	**151,000**	**282,459**	**33,284**	**51,760**	**61,780**	**580,283**
2	Transition to IFRS 9 (Note 44)	–	–	(29,486)	–	10,763	**(18,723)**
3	Transition to IFRS 9 - correction (spin-off)	–	–	–	–	(646)	**(646)**
4	**OPENING BALANCE FOR THE REPORTING PERIOD (1+2+3)**	**151,000**	**282,459**	**3,798**	**51,760**	**71,897**	**560,914**
5	**Comprehensive income for the financial year after tax**	**–**	**–**	**(496)**	**–**	**65,592**	**65,096**
6	Dividends (Note 37)	–	–	–	–	(42,620)	**(42,620)**
7	Transfer of net profit to reserves from profit	–	–	–	6,684	(6,684)	**–**
8	Other	–	–	30	(43)	30	**17**
9	**CLOSING BALANCE FOR THE REPORTING PERIOD (4+5+6+7+8)**	**151,000**	**282,459**	**3,332**	**58,401**	**88,215**	**583,407**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY OF THE ABANKA GROUP FOR THE REPORTING PERIOD ENDED 31 DECEMBER 2017

Item No.	ITEM DESCRIPTION	Share capital	Share premium	Accumu-lated other comprehen-sive income	Reserves from profit	Retained earnings (including income from the current year)	Total Equity (from 3 to 7)
1	2	3	4	5	6	7	8
1	**OPENING BALANCE FOR THE REPORTING PERIOD**	**151,000**	**282,459**	**42,445**	**47,468**	**93,456**	**616,828**
2	**Comprehensive income for the financial year after tax**	**–**	**–**	**(9,161)**	**–**	**41,595**	**32,434**
3	Dividends	–	–	–	–	(68,991)	**(68,991)**
4	Transfer of net profit to reserves from profit	–	–	–	4,292	(4,292)	**–**
5	Other	–	–	–	–	12	**12**
6	**CLOSING BALANCE FOR THE REPORTING PERIOD (1+2+3+4+5)**	**151,000**	**282,459**	**33,284**	**51,760**	**61,780**	**580,283**

These financial statements were approved for issue by the Management Board on 22 March 2019.

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(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED CASH FLOW STATEMENT OF THE ABANKA GROUP

Designation	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	2		3	4
A	**CASH FLOWS FROM OPERATING ACTIVITIES**			
a)	Total profit before tax		70,081	47,022
	Depreciation and amortisation	14	7,804	8,559
	Impairments of investments in debt securities measured at fair value through other comprehensive income	16	113	/
	(Reversal of impairments) of loans and other financial assets measured at amortised cost	16	(17,797)	(4,635)
	(Reversal of impairments) of tangible assets (including investment property) and other assets	16	(460)	(3,563)
	Net losses/(gains) from exchange differences		628	(415)
	Net losses from sale of tangible assets		56	20
	Net losses from sale of intangible assets		1	163
	Other (gains) from investing activities	38	(10,941)	(964)
	Net losses from sale of investment in a subsidiary	27	1,115	–
	Other adjustments to total profit or loss before tax	38	(3,856)	5,482
	Cash flows from operating activities before changes in operating assets and liabilities		**46,744**	**51,669**
b)	**Decreases in operating assets (excluding cash & cash equivalents)**		**60,714**	**6,238**
	Net (increase)/decrease in financial assets held for trading		(781)	2,169
	Net decrease in non-trading financial assets mandatorily at fair value through profit or loss		9,339	/
	Net decrease in financial assets measured at fair value through other comprehensive income		10,211	/
	Net decrease in financial assets designated at fair value through profit or loss		–	2,412
	Net decrease in financial assets available for sale (IAS 39)		/	154,896
	Net decrease/(increase) in loans and other financial assets measured at amortised cost		38,562	(158,435)
	Net (increase) in non-current assets held for sale		(2,725)	(559)
	Net decrease in other assets		6,108	5,755
c)	**Increases in operating liabilities**		**75,710**	**92,391**
	Net increase/(decrease) in financial liabilities held for trading		552	(2,435)
	Net increase in received deposits and loans measured at amortised cost		72,199	101,884
	Net increase/(decrease) in debt securities issued measured at amortised cost		623	(8,026)
	Net increase in other liabilities		2,336	968
d)	**Cash flows from operating activities (a+b+c)**		**183,168**	**150,298**
e)	**Income taxes (paid)**		**(1,038)**	**(12,027)**
f)	**Net cash flows from operating activities (d+e)**		**182,130**	**138,271**

(All amounts in EUR thousand unless otherwise stated)

CONSOLIDATED CASH FLOW STATEMENT OF THE ABANKA GROUP (continued)

Desig-nation	ITEM DESCRIPTION	NOTE	AMOUNT Year ended 31 December 2018	2017
1	2		3	4
B	**CASH FLOWS FROM INVESTING ACTIVITIES**			
a)	**Receipts from investing activities**		**233,525**	**21,422**
	Receipts from the sale of tangible assets		1,037	2,854
	Receipts from the disposal of a subsidiary	27	1,477	–
	Receipts from the disposal and maturity of investments in debt securities measured at amortised cost		224,749	–
	Receipts from the sale of financial assets held to maturity (IAS 39)		/	17,422
	Receipts from non-current assets held for sale		6,262	1,146
b)	**Cash payments on investing activities**		**(278,041)**	**(6,042)**
	(Cash payments to acquire tangible assets)		(2,556)	(3,211)
	(Cash payments to acquire intangible assets)		(5,157)	(2,831)
	(Cash payments to acquire debt securities measured at amortised cost)		(270,328)	–
c)	**Net cash flows from investing activities (a+b)**		**(44,516)**	**15,380**
C	**CASH FLOWS FROM FINANCING ACTIVITIES**			
a)	**Cash proceeds from financing activities**		**–**	**–**
b)	**Cash payments on financing activities**		**(42,620)**	**(68,991)**
	(Dividends paid)	37	(42,620)	(68,991)
c)	**Net cash flows from financing activities (a+b)**		**(42,620)**	**(68,991)**
D	Effects of change in exchange rates on cash and cash equivalents		2,564	(10,028)
E	**Net increase in cash and cash equivalents (Af+Bc+Cc)**		**94,994**	**84,660**
F	**Opening balance of cash and cash equivalents**		**460,410**	**385,778**
G	**Closing balance of cash and cash equivalents (D+E+F)**	**38**	**557,968**	**460,410**

These financial statements were approved for issue by the Management Board on 22 March 2019.

Management Board

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The notes on pages 125 to 270 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Separate and consolidated financial statements were compiled in accordance with the basic accounting policies defined hereinafter.

Reporting entity

Abanka d.d. is headquartered in Slovenia. The consolidated financial statements of the Bank as at and for the year ended 31 December 2018 comprise the Bank and its subsidiary (together referred to as the "Group" and individually as "Group entities"). The Group is primarily involved in corporate, retail and investment banking.

1.1 Basis of preparation

(a) Basis of preparation

Accepted accounting policies have been used on a consistent basis, and the accounting estimates have been made in compliance with the principles of prudence and good management. The accounting policies used in the preparation of the financial statements for 2018 are the same as those used in the preparation of the Annual Report for 2017, except for the change in the accounting policy regarding the recognition of tax on financial services (Note 1.25 Comparative data) and accounting standards and other changes effective from 1 January 2018 and approved by the European Union. Upon the transition to IFRS 9, comparative data were not adjusted (Note 1.25 Comparative data), and the balance as at 1 January 2018 is presented in the statement of financial position for information purposes only. The Management Board confirms that the financial statements and the accompanying notes have been prepared on the assumption of a going concern for the Bank and the Group for the period of assessment, being twelve months from the date of approval of these financial statements and in compliance with the relevant legislation and International Financial Reporting Standards, as adopted by the European Union.

These statutory financial statements are prepared for the purpose of compliance with legal requirements. The Bank is legally required to obtain an independent audit of these financial statements. The scope of that audit is limited to an audit of general purpose statutory financial statements to fulfil the legal requirement for audit of statutory financial statements. The audit scope comprehends the statutory financial statements taken as a whole and does not provide assurance on any individual line item, account or transaction. The audited financial statements are not intended for use by any party for the purposes of decision making concerning any ownership, financing or any other specific transactions relating to the Bank. Accordingly, users of the audited statutory financial statements should not rely exclusively on the financial statements and should undertake other procedures before making decisions.

(b) Statement of compliance

The financial statements of the Bank and the consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union (hereinafter: EU).

The scope of information and notes included in the Group's Annual Report and the breakdown of financial statements are also prescribed in the Companies Act and in the Regulation on the Books of Account and Annual Reports of Banks and Savings Banks issued by the Bank of Slovenia.

(c) Basis of measurement

The financial statements of the Bank and the consolidated financial statements have been prepared on the historical cost basis, except for the following material items in the statement of financial position measured at fair value:

- financial assets held for trading;
- financial assets mandatorily at fair value through profit or loss;
- financial assets at fair value through other comprehensive income (2017: available-for-sale financial assets).

(d) Functional and presentation currency

The financial statements of the Bank and the consolidated financial statements are presented in euros, which is the Bank's functional currency. All financial information presented in euros has been rounded to the nearest thousand unless otherwise stated. Due to rounding, minor differences may occur.

NOTES TO THE FINANCIAL STATEMENTS (continued)

(e) Use of estimates and judgements

The preparation of the financial statements in conformity with IFRS as adopted by the EU requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information on critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is included in Note 3 Critical accounting estimates, judgments and sources of uncertainty in applying accounting policies.

(f) Standards, interpretations and amendments effective for the financial year beginning on 1 January 2018

Among the standards effective on 1 January 2018, IFRS 9 – Financial Instruments is the most significant for the Group in terms of financial statements. More about the standard itself and the transition impact is presented in Note 44 IFRS 9 – Financial Instruments (with the transition impact).

On 1 January, the IFRS 15 “Revenue from Contracts with Customers”, adopted by the EU on 22 September 2016 (including Clarifications to IFRS 15 adopted by the EU on 31 October 2017), also became applicable. The Standard introduces a new income recognition framework that specifies the time and amount of revenue recognised. It replaces IAS 18 “Revenue”, IAS 11 “Construction Contracts” and related Interpretations. The Group first applied IFRS 15 as at 1 January 2018. The timing and amount of recognition of fee and commission income falling within the scope of IFRS 15 did not change due to the introduction of this standard. The effect of IFRS 15 is limited to certain additional disclosures, as shown in Note 1.9.

Other standards, interpretations and amendments effective for the financial year beginning on 1 January 2018 are as follows:

- Amendments to IFRS 4 “Insurance Contracts” – Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts - adopted by the EU on 3 November 2017 (effective for annual periods beginning on or after 1 January 2018 or when IFRS 9 Financial Instruments is applied first time);
- Amendments to IFRS 2 “Share-based Payment” – Classification and Measurement of Share-based Payment Transactions - adopted by the EU on 26 February 2018 (effective for annual periods beginning on or after 1 January 2018);
- Amendments to various standards “Improvements to IFRSs (cycle 2014-2016)” resulting from the annual improvement project of IFRS (IFRS 1, IFRS 12 and IAS 28) primarily with a view to removing inconsistencies and clarifying wording - adopted by the EU on 7 February 2018 (amendments to IFRS 1 and IAS 28 are to be applied for annual periods beginning on or after 1 January 2018);
- Amendments to IAS 40 “Investment Property” – Transfers of Investment Property - adopted by the EU on 14 March 2018 (effective for annual periods beginning on or after 1 January 2018);
- IFRIC 22 “Foreign Currency Transactions and Advance Consideration” - adopted by the EU on 28 March 2018 (effective for annual periods beginning on or after 1 January 2018).

The adoption of these new standards, amendments to the existing standards and new interpretations did not lead to significant changes in the Group's financial statements (with the exception of the aforementioned IFRS 9, where the effects are shown in greater detail).

(g) Standards, interpretations and amendments not yet effective for the financial year beginning on 1 January 2018

The Group decided not to early apply the following published standards and interpretations approved by the EU but not yet effective for the financial year beginning on 1 January 2018:

- IFRS 16 “Leases” - adopted by the EU on 31 October 2017 (effective for annual periods beginning on or after 1 January 2019);

In 2018, the Bank examined the existing lease agreements and determined which leases will be disclosed under IFRS 16 as of 1 January 2019. Accounting policies were also adapted to the new standard, and an impact assessment was carried out, which represents an increase in the Bank’s total assets by EUR 2.8 million.

NOTES TO THE FINANCIAL STATEMENTS
(continued)

- Amendments to IFRS 9 “Financial Instruments” – Prepayment Features with Negative Compensation - adopted by the EU on 22 March 2018 (effective for annual periods beginning on or after 1 January 2019);
- IFRIC 23 “Uncertainty over Income Tax Treatments” - adopted by the EU on 23 October 2018 (effective for annual periods beginning on or after 1 January 2019).

The Group estimates that the introduction of these new standards, amendments to the existing standards and new interpretations will not have a material impact on the Group's financial statements.

(h) New standards and amendments to the existing standards issued by International Accounting Standards Board (IASB) but not yet adopted by the EU

- IFRS 17 “Insurance Contracts” (effective for annual periods beginning on or after 1 January 2021);
- Amendments to IAS 28 “Investments in Associates and Joint Ventures” – Long-term Interests in Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2019);
- Amendments to various standards “Improvements to IFRSs (cycle 2015-2017)” resulting from the annual improvement project of IFRS (IFRS 3, IFRS 11, IAS 12 and IAS 23) primarily with a view to removing inconsistencies and clarifying wording (effective for annual periods beginning on or after 1 January 2019);
- Amendments to IAS 19 “Employee Benefits” – Plan Amendment, Curtailment or Settlement (effective for annual periods beginning on or after 1 January 2019);
- Amendments to References to the Conceptual Framework in IFRS Standards (effective for annual periods beginning on or after 1 January 2020);
- Amendments to IFRS 3 “Business Combinations” – Definition of a Business (effective for annual periods beginning on or after 1 January 2020);
- Amendments to IAS 1 “Presentation of Financial Statements” and IAS 8 “Accounting Policies, Changes in Accounting Estimates and Errors” – Definition of Material (effective for annual periods beginning on or after 1 January 2020);

The Group anticipates that the adoption of these new standards and amendments to the existing standards will have no material impact on the Group's financial statements in the period of initial application.

- Hedge accounting (part of IFRS 9) for a portfolio of financial assets and liabilities whose principles have not been adopted by the EU remains unregulated. The Group estimates that the application of hedge accounting to a portfolio of financial assets or liabilities pursuant to IAS 39 “Financial Instruments: Recognition and Measurement” would not significantly impact the financial statements, if applied as at the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1.2 Consolidation

Subsidiaries

Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date on which control ceases.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated in the consolidated financial statements. Unrealised losses are also eliminated unless the transaction provides evidence of the impairment of the asset transferred.

In the separate financial statements of the Bank, investments in subsidiaries are measured at cost.

1.3 Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Management Board of the Bank.

In accordance with IFRS 8, the Group voluntarily reports on the following business segments: retail banking, corporate banking and financial markets. Additional information is disclosed in Note 5 Segment Analyses.

1.4 Foreign currency translation

The functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The functional and presentation currency of the Bank and its subsidiaries in Slovenia and Montenegro is the euro.

(a) Transactions and balances

Foreign currency transactions are translated into the respective functional currency of the operation, using the spot exchange rates as at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into the functional currency at the ECB reference rate as at that date. Foreign exchange gains and losses on monetary items are the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the spot exchange rate as at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the spot exchange rate as at the date that fair value was determined. Foreign currency differences arising from retranslation are recognised in profit or loss, except for differences arising from the retranslation of equity instruments measured at fair value through other comprehensive income that are recognised directly in other comprehensive income. Non-monetary assets and liabilities that are measured in terms of the historical cost in a foreign currency are translated using the exchange rate as at the date of the transaction.

(b) Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into euros at spot exchange rates at the reporting date. The income and expenses of foreign operations are translated into euros at spot exchange rates as at the dates of the transactions.

Foreign currency differences on the translation of foreign operations are recognised in other comprehensive income in the translation reserve, which is part of the accumulated other comprehensive income. However, if the operation is not wholly owned, the relevant proportional share of the difference is instead allocated to the non-controlling interest. When a foreign operation is disposed of, the relevant amount in the translation reserve is transferred to profit or loss upon disposal. When the Group disposes of only part of its interest in a subsidiary that includes a foreign operation, whilst retaining control, the relevant proportion of the cumulative amount is reattributed to non-controlling interests. When the Group disposes of only part of its investment in an associate that includes a foreign operation, whilst retaining significant influence, the relevant proportion of the cumulative amount is reclassified to profit or loss.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Foreign exchange gains or losses arising from a monetary item receivable from or payable to a foreign operation, the settlement of which is neither planned nor likely to occur in the foreseeable future and which in substance is considered to form part of the net investment in the foreign operation, are recognised in other comprehensive income in the translation reserve, which is part of the accumulated other comprehensive income.

1.5 Financial assets and financial liabilities

Explained below are the accounting policies used for 2018 in accordance with IFRS 9. The accounting policies used for 2017 (IAS 39) are presented in the financial statements for 2017, which are included in the Annual Report for 2017. In 2017, financial assets and financial liabilities were classified into the following categories:
- financial assets and liabilities measured at fair value through profit or loss,
- loans and receivables,
- held-to-maturity investments,
- available-for-sale financial assets.

Recognition and measurement at recognition
The Group initially recognises loans and receivables, given deposits and debt securities issued on the date that they originate. Regular purchases and sales of other financial assets are recognised on the trade date at which the Group commits to purchasing and selling the asset.

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

Financial liabilities are initially recognised at fair value less costs incurred.

Classification and measurement of financial assets
Classification and measurement of financial instruments in the financial statements is determined by the selected business model in which financial assets are managed and by the characteristics of contractual cash flows. At initial recognition, each financial asset is classified into one of the following business models:
1. the model whose objective is to hold the financial asset to collect the contractual cash flows (measurement at amortised cost),
2. the model whose objective is achieved by collecting contractual cash flows and selling financial assets (measurement at fair value through other comprehensive income – FVTOCI),
3. other models (measurement at fair value through profit or loss – FVTPL and at fair value through other comprehensive income – FVTOCI).

The Group assesses the purpose of a business model in the context of which a financial asset is classified on a portfolio basis, as this is the way the business is managed and information submitted to the management. In defining a business model, the Group takes into account the following information:
- policies and objectives for the portfolio of financial assets and the implementation of these policies in practice;
- the frequency, volume and timing of sales in prior periods, the reasons for these sales and expectations about future sales activity;
- how the performance of the business model and the financial assets held within that business model are evaluated and reported to the management of the Bank;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and particularly the way those risks are managed;
- the method of setting the variable component of the remuneration of the manager responsible for these transactions (e.g. whether the remuneration is based on the fair value of the assets managed or the contractual cash flows collected) on the basis of the remuneration criteria laid down in the internal rules of the Group.

Loans and debt securities not intended to regulate operational, current liquidity but to collect contractual cash flows are classified into the business model whose objective is to hold the financial asset to collect the contractual cash flows (valued at amortised cost).

Debt securities held in the banking book, which are intended to regulate operational, current liquidity and are, as a rule, more liquid and less exposed to credit risk, are classified into the business model whose objective is achieved by both collecting

NOTES TO THE FINANCIAL STATEMENTS (continued)

contractual cash flows and selling financial assets (valued at fair value through other comprehensive income). The Group chose the irrevocable option of valuation of equity instruments not held for trading at fair value through other comprehensive income, where only dividend income is recognised in profit or loss in the following cases:
- equity securities that are complementary to the principal activity of the Bank (of strategic nature for the Bank) and
- equity securities that support the principal activity of the Bank (of infrastructure nature for the Bank) and were under IAS 39 classified as available-for-sale financial assets.

All financial assets not classified as measured at amortised cost or at fair value through other comprehensive income are measured at fair value through profit or loss. The Group measures at fair value through profit or loss those instruments that do not pass the SPPI test as well as the following financial assets:
- instruments obtained for hedging of other positions;
- structured products;
- securities held for trading;
- equity securities for which the option of irrevocable election of measurement at fair value through other comprehensive income is not selected at initial recognition.

Financial assets held for trading and those whose performance is measured on the basis of fair value are measured at fair value through profit or loss because their purpose is neither to collect contractual cash flows nor to collect contractual cash flows and sell financial assets.

In accordance with IFRS 9, where the host contract falls within the scope of IFRS 9, embedded derivatives will not be separated from the host contract but will be assessed in their entirety for the purpose of classification in accordance with IFRS 9.

The assessment whether the contractual cash flows meet the solely payments of principal and interest (SPPI) criterion (the SPPI test)
The Group performs the SPPI test for the debt instruments in a hold-to-collect or hold-to-collect or sell business model. For this purpose, the principal is the fair value of the financial asset on initial recognition. Interest is consideration for the time value of money, credit risk relating to the outstanding principal, other basic lending risks and costs (liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows meet the solely payments of principal and interest criterion, the Group assesses the contractual features of a financial instrument. This includes the judgement whether a financial asset contains the contractual terms that may change the time and amount of contractual cash flows in a way that this criterion would no longer be fulfilled. To this end, the following is taken into account:
- potential events that may change the time and amount of contractual cash flows;
- the possibility of early repayment or extension of repayment;
- the conditions that limit the Group in respect of the cash flows of certain assets (e.g. the subordination of payments);
- the features that change the perception of the time value of money (e.g. interest rates are periodically reset).

Derecognition of a financial asset
The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred, when the terms of an existing financial asset measured at amortised cost are changed which significantly affect the cash flows of the modified financial asset or with the write-off. If the Group, in its debt collection process, based on available information and past experience, assesses that the balance sheet exposure will not be repaid and, in accordance with IFRS 9, the conditions for derecognition of that exposure from the statement of financial position have been fulfilled, the Group writes it off from the statement of financial position and keeps it on off-balance-sheet records in the amount due until the legal basis for concluding the collection process has been obtained.

Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset in the statement of financial position. Upon the derecognition of a financial asset, the difference between the carrying amount of the asset and the sum of the consideration received and the cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

NOTES TO THE FINANCIAL STATEMENTS (continued)

As of 1 January 2018, total profit or loss for equity securities for which the irrevocable option to classify them into assets measured at fair value through other comprehensive income was chosen is not recognised in profit or loss upon derecognition.

Modification of terms of an existing financial asset
When the cash flows of a modified financial asset measured at amortised cost are not substantially different, such modification will not result in derecognition. The Group recalculates the gross carrying amount of the financial asset by discounting the modified cash flows using the original effective interest rate. The resulting difference is then recognised in profit or loss as net gain or loss on modification of financial assets. If terms are modified due to the counterparty's financial difficulties, the resulting profit or loss is recognised as impairment loss.

Restructured loans
Restructured loans are defined in Section 2 Risk Management.

Financial liabilities
Financial liabilities include financial liabilities held for trading and financial liabilities measured at amortised cost.

Financial liabilities held for trading include liabilities arising from the valuation of forward sale of securities, and are measured at fair value.

Among financial liabilities designated at fair value through profit or loss, the Group presents the valuation of the undrawn portion of non-trading loans mandatorily measured at fair value through profit or loss.

Financial liabilities measured at amortised cost are deposits and loans from banks (including the central bank) and non-bank customers, liabilities arising from debt securities issued, and other financial liabilities.

Financial liabilities measured at amortised cost are recognised in the amount of proceeds received net of any direct transaction costs. After they are initially recognised, the liabilities are measured at amortised cost, and any difference between net proceeds and the redemption value is recognised in profit or loss using the effective interest method.

A financial liability is derecognised when the obligation is discharged, cancelled or expires. The difference between the carrying amount of a financial liability that is cancelled or transferred to another party and the compensation paid is recognised in profit or loss.

1.6 Offsetting financial instruments

Financial assets and liabilities are offset, and the net amount is 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 realise the asset and settle the liability simultaneously. The ISDA (International Swaps and Derivatives Association) and similar master netting arrangements do not meet the criteria for offsetting in the statement of financial position. This is because they create for the parties to the agreement a right of set-off of recognised amounts that is enforceable only following an event of default, insolvency or bankruptcy of the Group or the counterparties or following other predetermined events. In addition, the Group and its counterparties do not intend to settle on a net basis or to realise the assets and settle the liabilities simultaneously.

1.7 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received).

All derivatives of the Group are classified as held-for-trading (Note 19). Changes in the fair value of derivative instruments are recognised immediately in the income statement.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Past due receivables from derivatives held for trading remain recorded under the same item of financial assets (derivatives) and are not reclassified under other receivables. When objective evidence of the possible impairment of derivative financial assets due to credit risk exists, the Group assesses the impairment loss and recognises it in the valuation of the derivative.

1.8 Interest income and expenses

Interest income and expenses for all interest-bearing financial instruments are recognised within “interest income” and “interest expenses” in the income statement, using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, except in case of credit-impaired financial assets, the Group estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. For credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using the estimated future cash flows, which take into account credit risk.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the interest rate used to discount the future cash flows for the purpose of measuring the impairment loss.

Interest income is calculated by applying the effective interest rate on the gross carrying amount of the asset when it does not refer to a credit-impaired asset. For financial assets whose credit risk deteriorated since initial recognition, interest income is calculated by applying the effective interest rate on the amortised cost of the asset. When the asset is no longer credit-impaired, interest income is again calculated on the basis of the gross value.

For purchased or originated credit-impaired (POCI) assets, interest income is calculated by applying a credit-adjusted effective interest rate on the amortised cost of the financial asset. The calculation of interest income does not change even if the credit risk of the asset has improved.

The definition of an increase in credit risk is presented in Note 1.11.

1.9 Fee and commission income and expenses

Income is recognised when control is transferred to the customer and the execution obligation is fulfilled. The transfer of control can take place at a particular moment or gradually over a certain period. Fees and commissions received are generally recognised on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct cost) and recognised as an adjustment to the effective interest rate on the loan. Loan syndication fees are recognised as revenue over the life of the loan, and if the Group has retained no part of the loan package for itself or has retained a part at the same effective interest rate as the other participants. Commissions and fees arising from negotiating or participating in the negotiation of a transaction for a third party (e.g. the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses) are recognised upon completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis. Asset management fees related to investment funds are recognised rateably over the period in which the service is provided. The same principle is applied for custody services that are continuously provided over an extended period of time. Performance-linked fees or fee components are recognised when the performance criteria are fulfilled. Transaction-related income is recognised at the moment a transaction is executed.

Fees and commissions paid that are mostly related to payment transactions are recognised as the Group’s expenses as they arise.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1.10 Dividend income

Dividends are recognised in the income statement when the entity's right to receive payment is established.

1.11 Impairment of financial assets

Explained below are the accounting policies used for 2018 in accordance with IFRS 9. The accounting policies used for 2017 (IAS 39) are presented in the financial statements for 2017, which are included in the Annual Report for 2017 and briefly summarised in Section 2.1.2.1.

Expected credit loss is recognised for the following financial instruments not measured at fair value through profit or loss:
- loans to banks,
- loans to non-bank customers,
- debt securities,
- lease receivables and
- off-balance sheet exposures from credit commitments and financial guarantee contracts.

Equity securities are not subject to impairment.

Except in the case of POCI assets, as presented in detail below, expected credit loss is measured as the amount of:
- possible losses expected within 12 months after the reporting date (hereinafter: stage 1) or
- all possible losses expected in the full lifetime of a financial asset (hereinafter: stage 2 or stage 3).

The measurement of all possible losses expected in the full lifetime of a financial asset is required in the event of a significant increase in credit risk of a financial asset since initial recognition. For other financial assets, impairment loss is measured on the basis of possible losses expected within 12 months after the reporting date. Significant increase in credit risk is defined in Section 2.1.2.2.

Expected credit loss is a probability-weighted estimate of credit losses and is measured as the present value of the difference between the contractual cash flows and the expected cash flows by taking into account future macroeconomic scenarios and discounted at the financial asset's effective interest rate.

For undrawn loan commitments, expected credit loss is the present value of the difference between the contractual cash flows if the loan is drawn down and expected cash flows.
For a financial guarantee, expected credit loss is the present value of expected payments to the guarantee holder less any amounts that the Group expects to replace.

Expected credit loss is measured on the basis of individual or collective assessment for portfolios of assets with similar credit risk characteristics, as explained in more detail in Section 2. The measurement of credit losses is based on expected cash flows by applying the asset's original effective interest rate, irrespective of whether it is measured on the basis of individual or collective assessment of credit losses.

For more information on credit loss measurement see Section 2.1.2.2.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Credit-impaired financial assets
At each reporting date, it is assessed whether financial assets measured at amortised cost and debt instruments measured at fair value through other comprehensive income are credit-impaired. A financial asset is credit-impaired when one or more events have occurred that have a negative impact on the asset's estimated future cash flows. Evidence that a financial asset is credit-impaired includes the following:

- significant financial difficulties of the borrower;
- an actual breach of contract (default or being past due for 90 days or more);
- restructuring of financial assets for economic or legal reasons relating to the borrower's financial difficulty, granting the borrower a concession that would not otherwise be considered;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for that financial asset because of financial difficulties;
- the purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses.

Purchased or originated credit-impaired (POCI) assets
POCI financial assets are treated differently because the asset is credit-impaired at initial recognition. For these assets, expected credit loss is recognised since initial recognition as impairment loss and any changes are recognised in profit or loss. Any favourable changes (an increase in value) for such assets are an impairment gain.

Presentation of expected credit losses in the statement of financial position:

- financial assets measured at amortised cost: as a decrease in gross carrying amount of the asset,
- undrawn loan commitments and financial guarantees: as provisions,
- debt instruments measured at fair value through other comprehensive income: expected credit loss as a loss allowance is not recognised in the statement of financial position, because the carrying amount of these assets is their fair value. However, this value adjustment is disclosed and included in accumulated other comprehensive income.

1.12 Property and equipment, investment property, intangible assets and non-current assets held for sale

Land and buildings mainly comprise investments in branches and offices. All property and equipment is stated at the historical cost less depreciation and impairment loss. The historical cost includes expenditure that is directly attributable to the acquisition of the items.

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

Investment property includes land and buildings leased out under an operating lease. Investment property is valued at the historical cost upon initial recognition. Subsequent valuation is made using the historical cost model, as made for property and equipment. The same accounting treatment that applies to property and equipment is applied to investment property.

The Group includes licences and software among its intangible assets. Intangible assets are valued at historical cost upon initial recognition. Subsequent valuation is made using the historical cost model. All intangible assets have finite useful lives. In line with the historical cost model, intangible assets are recorded at the historical cost less amortisation and the accumulated impairment loss.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

Land is not depreciated. Depreciation of other assets is calculated using the straight-line method to allocate their cost less their residual values over their estimated useful lives as follows:

	2018	2017
Buildings (including investments in third-party property and equipment)	2–10%	2–6%
Equipment	14–20%	14–20%
Computers	10–50%	10–50%
Intangible assets	9–50%	9–50%

The residual values and useful lives of assets are reviewed at least once a year or as needed and adjusted accordingly. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Property and equipment are reviewed for impairment at least once a year. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on the disposal of property and equipment are determined by comparing proceeds with carrying amount and are included in gains and losses upon the de-recognition of assets other than those held for sale in the income statement.

Non-current assets classified as held for sale are measured at the lower of the carrying amount and fair value less costs to sell. Non-current assets are classified as held for sale if their carrying amount is to be recovered through a sales transaction rather than through continued use. This condition is regarded as being met only when the sale is highly probable and the asset is available for immediate sale in its present condition, subject to terms that are usual and customary for the sale of such assets. Management must be committed to the sale and must actively market the property for sale at a price that is reasonable in relation to the current fair value. The sale should be expected to qualify for recognition as a completed sale within one year of the date of classification.

The property and equipment received by the Group following foreclosure due to unpaid past-due receivables are disclosed as inventory. If such property and equipment are leased by the Group under an operating lease, they are recognised as investment property.

1.13 Impairment of investments in subsidiaries

In line with IAS 36, when assessing the impairment of investments in subsidiaries, the Group reviews not only objective evidence of impairment, but also any indication that an investment in a subsidiary may be impaired. In addition to indications from external and internal sources of information, the Group takes into account other indications of possible impairment, such as underperformance, or the decision of a company's management to wind up the company.

If there is objective evidence or an indication that an investment in a subsidiary may be impaired, according to IAS 36 the Group calculates the impairment amount as being the difference between the carrying amount of the investment and its recoverable amount. The recoverable amount is that which is found to be higher following a comparison of an investment's:
- fair value less costs to sell; or
- value in use, which equals the present value of the future cash flows expected to arise from this investment, discounted at the current market rate of return on a similar financial asset.

If any of these amounts exceeds the carrying value, the financial asset is not impaired, and the other amount need not be assessed. If expected future cash flows cannot be estimated to calculate the value in use, the Group calculates the necessary impairments using the net asset value method (the asset accumulation method), or as the difference between the carrying amount of a financial asset and the equity book value of the company into which the Group has invested, and does so by reference to its proportional share in equity.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1.14 Leases

A group company is the lessor

A lease is classified as a finance lease if it transfers all the substantial risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer all the substantial risks and rewards incidental to ownership.

When assets are held subject to a finance lease, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is treated as unearned finance income. Lease income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return.

Lease income from operating leases is recognised in income on a straight-line basis over the lease term. Costs, including depreciation, incurred in earning the lease income are recognised as costs. Initial direct costs incurred by lessors in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised as costs over the lease term on the same basis as the lease income.

A group company is the lessee

The leases entered into by the Group are primarily operating leases. The Group rents business premises, computers and other equipment, cars and locations for cash machines. The total payments made under operating leases are charged to administrative expenses. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as a cost in the period in which termination takes place.

1.15 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents include cash in hand and non-restricted balances with the central bank, demand deposits with banks, loans to other banks and ECB eligible debt securities with less than three months maturity from the date of acquisition.

1.16 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; when it is more likely than not that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as an interest expense.

1.17 Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer 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. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was given. Subsequent to initial recognition, the Group’s liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise the fee income earned on a straight line basis over the life of the guarantee and provision for expected credit losses in accordance with IFRS 9, which presents the best estimate of the expenditure required to settle any financial obligation existing as at the statement of financial position date. These estimates are determined based on the experience of similar transactions and a history of past losses.

Any increase in the liability relating to guarantees is recorded in the income statement under provision expenses.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1.18 Employee benefits

The Group provides benefits to employees as a legal obligation, including jubilee benefits and retirement bonuses. Employee benefits are included in provision expenses for employee benefits and provisions for employee benefits. The Group sets aside such provisions based on actuarial calculations. The major assumptions used in these calculations are the following: the discount rate, the number of employees eligible for benefits, the rate of labour turnover and the average annual salary growth.

Employees retire once they meet the requirements of the old-age pension scheme and achieve the required years of service in accordance with the relevant Slovene legislation. At that time (if they meet certain conditions) they become eligible for full retirement benefits. Furthermore, pursuant to the collective agreement, employees are also entitled to jubilee payments.

Defined contributions to state social security are deducted each month from the payroll, expensed as incurred and included in administrative expenses.

1.19 Taxation

Taxation is provided for in the financial statements in accordance with the Slovene legislation currently in force. The charge for taxation in the income statement for the year comprises current tax and changes in deferred tax. Current tax is calculated on the basis of the taxable profit for the year using the tax rates in effect at the statement of financial position date.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax basis of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the statement of financial position date, and are expected to apply when the related deferred income tax asset is realised, or the deferred income tax liability is settled.

The Group has created deferred taxes on the temporary differences arising from the impairment of tangible and intangible assets, from different depreciation rates for accounting and tax purposes, from the revaluation and impairment of debt and equity securities measured at fair value through other comprehensive income (2017: available-for-sale securities), from the impairment of equity securities measured at fair value through profit or loss – created before transition to IFRS 9 in available-for-sale category, from the impairment of debt securities measured at amortised cost, from provisions created for employee benefits, from restructuring provisions, from the impairment of loans and receivables in subsidiaries and from tax losses carried forward.

The Group fully recognises deferred taxes for the above-mentioned temporary differences, while deferred taxes for tax loss are formed by taking into account other recorded deferred tax assets to the extent that it is probable that future taxable profits will be available, against which they can be utilised in the foreseeable future period (a three-year period). Current income tax payable on profits, based on the applicable tax law in each jurisdiction, is recognised as an expense in the period in which profits arise.

Deferred tax related to the fair value remeasurement of financial assets measured at fair value through other comprehensive income (2017: available-for-sale investments), which is charged or credited directly to other comprehensive income, is also credited or charged directly to other comprehensive income and subsequently (upon derecognition or impairment) recognised in the income statement, together with the deferred gain or loss.

1.20 Share capital

(a) Share issue costs
Incremental costs directly attributable to the issue of new shares or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds.

(b) Dividends on ordinary shares
Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Bank's shareholders.

1.21 Transactions in the name and for the account of third parties

In compliance with the Slovene legislation, Note 41 includes fees charged to customers for the acceptance, transmission and execution of orders, custody of financial instruments, itemised assets and liabilities per customer account which the Group uses to account for customers' financial assets arising from brokered transactions.

NOTES TO THE FINANCIAL STATEMENTS (continued)

1.22 Sale and repurchase agreements

Securities sold subject to repurchase agreements (“repos”) are classified in the financial statements as financial assets held for trading, financial assets at fair value through other comprehensive income or financial assets at amortised cost, even though the transferee has the right by contract or custom to sell or re-pledge them as collateral. The counterparty financial liability is included in loans from banks and the central bank or loans from non-bank customers. Securities purchased under agreements to resell (“reverse repos”) are recorded as loans to banks or non-bank customers, as appropriate. The difference between the sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Securities lent to counterparties are also retained in the financial statements.

1.23 Precious metals

The Group carries precious metals among other assets. Although precious metals are not considered to be financial assets, they are recognised, measured and derecognised in compliance with IAS 39. This means that the stock of precious metals held for trading is measured at fair value through profit or loss. Gains and losses from the valuation and sales are recognised in net other operating income or expenses.

1.24 Information in the notes to the financial statements

Disclosures in the notes to the financial statements are presented for the Bank and for the Group separately. In the cases of completely identical information for the Bank and the Group, only information for the Group is presented. Notes 2, 3, 4 and 5 are prepared on a consolidated basis, as there are no significant differences between the Bank and the Group.

1.25 Comparative data

- *IFRS 9*

In comparison with the presentation of the financial statements for the year ended 31 December 2017, the presentation of the income statement, the statement of financial position and the cash flow statement changed due to the adjustments following the introduction of IFRS 9 and the changes prescribed by the Bank of Slovenia. In accordance with the provisions of the transition to IFRS 9, the Bank has chosen the option of not restating comparative data in the financial statements for 2018, therefore financial statements for 2017 are presented in accordance with IAS 39 and for 2018 in accordance with IFRS 9. More on the transition impact is presented in Note 44 IFRS 9 - Financial instruments (with the transition impact).

- *Tax on financial services (TFS)*

In 2018 the Group began to recognise tax on financial services as income reduction (under the net principle), which was recognised as other operating expense until then. Consequently, the comparative data in the income statement for 2017 changed for the following items: interest income, fee and commission income and net other operating income/(expenses). Interest income (from loans to non-bank customers) decreased by EUR 321 thousand and fee and commission income by EUR 4,292 thousand, whilst net other operating expenses fell by EUR 4,613 thousand. The net operating profit remains unchanged.

- *Pledged assets*

Due to the change in the regulator’s position on the definition of encumbered assets (encumbered assets also include assets not directly related to specific sources of funding or off-balance-sheet liabilities), the comparative data in the disclosure of pledged assets for 2017 were adjusted (expanded), as originally only loans to banks of EUR 8,847 thousand were reported (Note 29).

NOTES TO THE FINANCIAL STATEMENTS (continued)

2 RISK MANAGEMENT

In its operations, the Group is exposed to the following financial risks:
- credit risk,
- market risk,
- interest rate risk and
- liquidity risk.

In addition, the Group is exposed to other types of risks, such as: capital management, operational risk, business risk, reputational risk and compliance risk. The ability to manage and appropriately control risks has a direct impact on the long-term stability and performance of the Group, which is therefore paying heightened attention to the risk management function, including risk identification, measurement or assessment, control, monitoring and risk reporting procedures.

Individual types of financial risks in the Group, capital management and operational risk management are described in this Section. In addition to these, the Group's operations may also be affected by other risks that are not yet recognised as significant by the Group, or which are insignificant at present but could grow in significance in the future. Risk management is disclosed only on a consolidated basis, as there are no significant differences between the Bank and the Group in the treatment of individual risks.

The Group is most exposed to credit risk, which remained the most important systemic risk in the banking system in 2018, even though it gradually stabilised with the resolution of non-performing loans. Credit risk is analyzed in greater detail under Chapter 2.1.

A risk management system in the Group

The Management Board is responsible for the establishment and monitoring of the Group's risk management system. For this purpose, the Management Board has set up special committees, such as the Risk Management and Asset-Liability Committee, the Credit Committee and the Asset Liability Management Committee, which are responsible for the development and monitoring of risk management policies. The management body of the Bank approves the strategic objectives and strategy as well as related risk management policies. The Audit Committee and the Risk Monitoring and Asset Liability Management Committee as special bodies of the Supervisory Board supervise how the Management Board ensures compliance with the Group's risk management policies and procedures and review the adequacy of the risk management system in relation to the actual risks to which the Group is exposed. In this type of supervision, the Audit Committee cooperates with the Internal Audit Department of the Bank, which performs regular and extraordinary audits of internal controls and procedures related to risk management and reports its findings to the Audit Committee of the Group. The risk management function is independent from operational functions.

The Abanka Group is a systemically important bank, included in the supervision performed by the European Central Bank (ECB) via the Single Supervisory Mechanism (SSM). The ECB assesses the overall viability of an institution in line with the guidelines on common procedures and methodologies for the supervisory review and evaluation process.

2.1 Credit risk

Credit risk is the risk that a debtor or counterparty will cause a financial loss for the Group by failing to discharge an obligation. This risk represents the potential unwillingness or inability of the debtor to fully meet its contractual obligations within the agreed period and/or amount and arises mainly from loans to banks and loans to non-bank customers and investments in debt securities, as well as loan commitments and derivatives. In addition to default risk and counterparty risk, credit risk includes the following significant risks: concentration risk, residual risk and credit rating risk.

Concentration risk is the risk of a loss arising from being overexposed to a single individual, groups of related parties and parties connected by common risk factors, such as the same economic sector, geographical area or transactions of the same type. Concentration risk also arises from using credit protection.

Residual risk is the risk of less effective credit protection than expected.

Credit rating risk refers to the risk of loss due to the downgrading of a customer or receivable.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Credit risk arises in all areas of banking involving risk-bearing balance sheet asset items and risk-bearing off-balance sheet items. Credit risk is the most important risk in the Group's operations and, therefore, is given high priority by the management.

2.1.1 The credit risk management process

The main objective of credit risk management in the Group is to achieve and maintain the quality and diversification of the credit portfolio. Careful and prudent management of the credit portfolio includes the minimization of credit risk in achieving the planned credit risk management objectives, which are defined in the Risk Management Strategy and Risk Appetite.

The credit risk management process includes the identification, measurement, control and monitoring of credit risk, including reporting credit risks to which the Group is or might be exposed in its operations.

Credit risk is managed at the level of individual transactions and debtors, as well as at the level of the overall credit portfolio.

The Group has an established **structure and organisation of appropriate functions for credit risk management**. The Management Board and senior management are responsible for efficient credit risk management. The Management Board transferred some of its competencies in this area to senior management and collective decision-making bodies as follows: The Risk Management and Asset-Liability Committee, the Credit Committee and The Asset Liability Management Committee. Within the scope of its powers, the Loan Recovery and Restructuring Department not only processes problem loans but is also closely involved in their recovery in collaboration with experts from other departments. The credit risk management function is coordinated at the Group level so as to provide compliance and maximise standardisation in all subsidiaries.

The Group clearly delimited competencies and tasks between commercial divisions and the Risk Management Division, which is organisationally independent of the front-end units (where credit risk is assumed). Furthermore, competencies and tasks are also clearly delimited between commercial units and the back office, including management.

The Group established the **internal control system**, which includes:
- protection of confidential information;
- operational procedures in processes, operating instructions and rules;
- physical controls;
- Internal and external audits;
- compliance with the applicable legislation and internal documents;
- IT support development and security and its use in the credit risk management process;
- human resource policy;
- public data disclosure policy.

The purpose of internal controls in credit risk management is to effectively carry out tasks in accordance with the credit risk management policy and the internal control system policy of the efficient use of funds and their protection against loss due to negligence, abuse, misadministration, default, fraud and other errors, compliance with primary and secondary legislation and instructions by the Management Board and senior management of the Bank, the provision and maintenance of timely, comprehensive and reliable data and information and their fair disclosure in internal and external reports.

The extent and features of internal reporting on credit risk allow an appropriate flow of information up and down-stream, as well as between organisational units. This enables timely decision-making at all managerial levels of the Group with regard to measures for mitigating credit risk and for monitoring the results of these measures. There is an established practice of producing periodic and, when appropriate, extraordinary reports on assumed credit risk. The Risk Management and Asset-Liability Committee, the Management Board, the Risk Monitoring and Asset Liability Management Committee and the Supervisory Board discuss and review at least quarterly comprehensive risk reports focusing primarily on credit risk.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.1.1 Credit risk measurement

a) Loans

The Group's exposure to credit risk depends on the following three credit risk components: exposure amount, a debtor's default probability reflected in its credit rating, and the recovery ratio on defaulted obligations, which is dependent on collateral and debt collection. The listed credit risk components are further defined below in Chapter 2.1.2.2.

The Group has set up its own internal methodologies for measuring credit risk, which serve as the basis for the process of classifying borrowers and exposures into credit rating categories: A, B, C, D and E.

Credit rating A denotes the lowest credit risk and is assigned to borrowers with the highest creditworthiness, those who are assessed as being able to regularly settle their liabilities when they fall due. Credit rating B is assigned to borrowers whose financial position is somewhat weaker, yet the Group does not expect any significant difficulties in them being able to service their obligations. Credit rating C is assigned to borrowers who are either undercapitalised or who lack sufficient long-term sources of funds to finance long-term investments, whose cash flows have been ascertained to be insufficient for the regular settlement of all due liabilities. However, their past-due liabilities to the Group do not exceed 90 days and no material credit-related economic losses with these borrowers are foreseen. Credit rating D is assigned to borrowers to whom the Group's exposures are treated as non-performing, who are insolvent or undergoing rehabilitation or compulsory settlement and for whom the Group consider that they are unlikely to pay their credit obligations in full, but it can be reasonably expected that their loans will be repaid, at least in part. Credit rating E denotes the highest credit risk and is also assigned to borrowers to whom the Group's exposures are treated as non-performing, but the Group considers that the borrowers are highly unlikely to pay their credit obligations or does not expect any repayment at all.

Companies are ranked in ten credit classes (credit grades A and B have three credit sub-grades, credit grade C has two).The assignment of credit ratings to customers and exposures is based on quantitative and qualitative criteria, such as an assessment of the borrowers' financial position, the ability to provide sufficient cash flow for future debt servicing, the borrower's loan servicing track record, and the quality and amount of credit protection. Country risk is also taken into account when assigning credit ratings to foreign borrowers.

The Group also performs its own credit risk analyses of foreign banks and countries, taking into account inter alia credit ratings and credit reports by credit rating agencies, as well as export credit agencies' ratings in the case of country credit risk analyses.

Prior to credit approval, all debtors must be classified into the appropriate rating category. Throughout the duration of the legal relationship underlying credit exposure, the Group monitors the borrower's operations and the quality of credit protection. The Group also regularly evaluates the level of expected credit losses and creates the necessary impairments and provisions in accordance with the International Financial Reporting Standards.

b) Debt securities

Credit risk arising from investments in debt securities is managed by a limit system in accordance with provisions of the Banking Act, which is based on internal and external ratings (Fitch Ratings and Moody's Investors Service) of securities and their issuers. The limit system ensures investments mostly in debt securities of high credit quality. Investing in debt securities issued by foreign issuers without an external credit rating, investments in subordinated and structured debt financial instruments are not allowed.

c) Loan commitments and contingent liabilities

Loan commitments and contingent liabilities represent guarantees, letters of credit and undrawn portions of granted loans, overdrafts and credit lines. The primary purpose of these instruments is to ensure that funds are available to a customer when required. Guarantees and standby letters of credit, which are written undertakings by the Group to pay in the event of the customer's default on its obligations to a third party, potentially carry the same credit risk for the Group as loans. Loan commitments and contingent liabilities represent potential credit risk for the Group. The same methodology as for loans is used to measure the credit risk arising from these instruments.

d) Derivatives

In case of derivative instruments, which are traded over-the-counter (OTC); the Group is exposed to counterparty credit risk, i.e. the risk that the counterparty may not fulfil their underlying contractual payment obligations. Counterparty credit risk from

NOTES TO THE FINANCIAL STATEMENTS (continued)

positions in derivatives equals the credit exposure value of these transactions. The exposure on a specific transaction is calculated as the sum of the current market value of the transaction and potential credit exposure.

The Group avoids transactions involving counterparties with lower credit ratings. For transactions that involve counterparties with such a credit rating, the Group insists on adequate collateral.

2.1.1.2 Credit risk mitigation

a) Credit limits

The Group mitigates credit risk by setting and monitoring credit limits at the level of individual borrowers and groups of related parties, and concentration limits that ensure the diversification of the Group's portfolio. Structural limits are also established for industries, geographical regions, the homogeneous groups of debtors with similar characteristics (funding with financial leverage), and for specific products. The system of credit limits is also the basic tool for the successful management of the credit risk arising from positions in debt securities, derivatives, REPO and reverse transactions. Credit risk exposure limits ensure that the Group’s credit portfolio is adequately diversified. The Group has also set limits on the weighted-average probability of default (wPD), which are designed to measure the quality of newly approved transactions, and limits of credit risk-weighted assets (RWA).

Credit limits are set and monitored according to internal methodologies. The Risk Management Division proposes credit limits, taking into account the limits prescribed by law. Credit limits are approved by the Risk Management and Asset-Liability Committee, the Credit Committee or by duly authorised employees, depending on the type of credit limit. Exposure limits (so-called gross limits and limits after exemptions) are set for every exposure to an individual customer or a group of related parties whose gross direct or indirect exposure equals or exceeds 10% (and every further 5%) of the capital of the Bank or Group or is very likely to reach or exceed 10% (and every further 5%) of the capital of the Bank or Group in the near future. Limits on exposure to individuals in a special relationship with the Bank and limits on the weighted-average probability of default are subject to a previous approval by the Supervisory Board.

The Group complies with regulatory requirements on the maximum exposure to individual customers or a group of related parties (after taking into account impairments and provisions as well as regulatory exemptions and the effect of eligible credit protection) which is set at 25% of the Group's regulatory capital.

b) Credit protection (collateral and guarantees)

In addition to the risk limit system, the Group also requires credit protection in order to reduce credit risk. The types of funded and unfunded credit protection accepted by the Group as well as the procedures for assessing and monitoring the adequacy and value of credit collateral are defined in the rules on collateral and real property valuation methodology. The most common forms of credit protection are real-estate collateral and bank guarantees.

As funded credit protection, the Group primarily accepts collateral in the form of real property, other physical collateral, receivables, cash on deposit held by a credit institution, and securities. As unfunded credit protection, the Group mainly accepts joint and several guarantees from corporate and retail customers, guarantees of the Republic of Slovenia, and guarantees issued by insurance companies and banks.

In granting credit, most important for the Group is a borrower's creditworthiness, enabling the settlement of all obligations, whilst accepted credit protection serves as a secondary source of loan repayment. The quality of collateral and the loan-to-value ratio required by the Group depend on a borrower’s credit rating and loan maturity. Credit protection instruments (CRM techniques) mitigate credit risk losses, improve the recovery of past-due receivables and decrease capital requirements on the condition they are compliant with minimum requirements in terms of their adequacy defined in banking regulation.

The Group mitigates credit risk by applying credit protection, but this may simultaneously trigger or increase other risks (such as legal risk, operational risk, liquidity risk or market risk); therefore, the Group pays due attention to residual risk in applying credit protection. This risk arises, for example, when the property provided as collateral is overvalued or when the liquidation of the collateral in reasonable time is either problematic or implausible.

c) Master netting agreements

The Group further reduces its exposure to credit risk by entering into master netting agreements that cover repurchase transactions, OTC derivatives contracts and other capital market instruments. These transactions can be carried out only with the counterparties who have concluded master netting agreements with the Group. These arrangements are usually settled on a gross basis, but in the case of a default they are settled on a net basis.

d) Financial covenants and other contractual provisions in credit agreements

The Group additionally mitigates credit risk exposure by including financial covenants and other contractual provisions in credit agreements. Financial covenants consist of a set of financial categories or financial ratios that a borrower must maintain at an agreed level throughout the term of the loan. They most often refer to the funding structure and income statement.

2.1.1.3 Credit risk management in extreme circumstances

The Group performs activities to reduce credit risk and mitigate the impact of extreme situations on its operations.

In a difficult economic and financial situation, the Group adapts its credit policy and takes measures based on stricter credit standards.

The framework for conducting stress tests in the Group is based on the policy of conducting stress testing, which was adopted in 2018. The preparation and implementation of stress tests requires a number of different interconnected analytical steps. Regardless of the scope of application and the type of stress test, and following the ECB solvency analysis framework, the Group uses a uniform, modular system for the implementation of stress tests, which includes:

- the first pillar (scenario design) consists of the design of macrofinancial scenarios and idiosyncratic events, which are the basis for conducting stress tests;
- the second pillar (satellite models) consists of the modules used to translate the scenarios defined in the first pillar into variables affecting the valuation of the bank balance sheet components;
- the third pillar (dynamic statement of financial position) takes into account the calculated profit/loss derived from the satellite models in calculating the Group's solvency position.

The Group performs stress tests for various purposes:

- capital adequacy assessment,
- liquidity adequacy assessment,
- design of the recovery plan,
- preparation of the risk appetite and
- design of the business plan.

Irrespective of the scope of application, the Group's capital/liquidity position is assessed in the context of the baseline and the stress scenario:

- the baseline scenario is a mild scenario whose assumptions reflect the continuation of the current direction and conditions of the Group's operations and is not necessarily the same as the planned forecast;
- the stress scenario is a scenario of extreme circumstances, which are unlikely but possible and represent a scenario whose assumptions contain important changes in the factors affecting the Group's capital or liquidity adequacy in the direction of deterioration.

Stress scenarios include three types of scenarios in a way to capture:

- system-wide events, conditioned by the economic situation and/or the situation on the market,
- idiosyncratic - Group-specific events and
- combinations of system-wide events and idiosyncratic events.

The following objectives are key in the implementation of the stress testing programme for the Group's internal needs:

- to capture the impact of severely adverse but possible scenarios on the financial position of the Group,
- to support business decisions in the Group,
- to assess the robustness of the capital models of the Group (validation) and
- to provide for transparent communication about the risks within and outside the Group.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.2 Impairment and provisioning methodologies

The impairment and provisioning methodology was amended on 1 January 2018 with the introduction of IFRS 9. Before 1 January 2018, the impairment and provisioning methodology was developed on the basis of IAS 39.

2.1.2.1 Impairment and provisioning methodologies – IAS 39

In accordance with the International Financial Reporting Standards, the Group regularly assessed whether there was objective evidence of financial asset impairment or possible losses from off-the-balance-sheet commitments and contingencies. Where there was objective evidence of impairment or possible losses, the Group created impairments of financial assets or provisions for off-the-balance-sheet commitments and contingencies on the basis of an individual or collective assessment. For the purpose of assessing the credit risk losses, the Group individually assessed its significant exposures to corporate customers where there was objective evidence of impairment or the possibility of a loss.

Individual impairments of financial assets were calculated as the difference between the carrying amount and recoverable amount. The latter was calculated by discounting estimated future cash flows, which included cash flows from the foreclosure of collateral, if certain required conditions were met.

For the purpose of calculating collective impairments, homogenous groups of debtors were formed according to similar credit risk characteristics that reflect the debtor's ability to meet its contractual obligations. The Group estimated the impairments and provisions for any homogenous groups of exposures on the basis of available historical default data and credit losses.

2.1.2.2 Impairment and provisioning methodologies – MSRP 9

The estimate of expected credit losses reflects an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes (credit losses in the event of different scenarios). All reasonable and supportable information, including forward-looking information, is considered in such an estimate.

Types of financial instruments subject to impairment

Impairment requirements apply to the following financial instruments not measured at fair value through profit or loss:
- financial assets measured at amortised cost,
- financial assets (debt financial instruments) measured at fair value through other comprehensive income,
- lease receivables and
- off-balance sheet exposures from loan commitments and financial guarantee contracts (including service guarantees).

Definition of default

In accordance with IFRS 9, the Group defined that a financial asset is in default when the following applies:
- unlikely to pay, the Group assessed that the debtor is unlikely to pay their credit obligations in full without realisation of collateral (loans to D- and E-rated debtors according to the internal credit rating);
- the debtor is over 90 days past due with the payment of a significant obligation.

This default definition is consistent with the definition of default that will be used for regulatory reporting purposes.

In assessing whether the debtor is in default, the Group takes into account the following factors:
- qualitative: e.g. breach of loan commitments;
- quantitative: e.g. the status of past-due and defaulted other obligations of the same debtor; and
- on the basis of the data obtained from internal and external sources.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Classification of financial instruments into stages by risk

The Group makes a distinction in the recognition of loss between 12-month expected credit losses and full lifetime expected credit losses. In view of the above, the Group classifies financial assets subject to impairment into the following four stages:

- stage 1: an ECL estimate on the basis of possible losses expected within 12 months. A financial asset is reclassified into Stage 1 when approved and remains there until the increased credit risk is identified;
- stage 2: an ECL estimate on the basis of full lifetime expected credit losses of a non-impaired financial asset. A financial asset is reclassified into stage 2 once an increased credit risk has been identified and remains there until the occurrence of a default event;
- stage 3: an ECL estimate on the basis of full lifetime expected credit losses of an impaired financial asset a financial asset is reclassified into stage 3 when there is objective evidence of impairment or when a default event has occurred (i.e. non-performing exposures pursuant to Article 178 of the CRR);
- POCI within stage 3: purchased or originated credit-impaired financial assets (POCI).

Inputs in the calculation of expected credit losses

Key variables used in the calculation of expected credit losses are as follows:

- probability of default (PD),
- loss given default (LGD),
- exposure at default (EAD), including credit conversion factor (CCF).

These parameters are derived from internally developed statistical models, publicly available data and other historical information, used in regulatory models, taking into account the characteristics relating to the segments of exposure to corporate entities, the retail customers and the state. They are adjusted to forward-looking information as described below.

<u>Probability of default</u> is the probability of a non-payment event, calculated on the basis of statistical models.
These models are based on internally collected data, which include both qualitative and quantitative factors, and in some cases even publicly available data (in the case of exposures to central governments, banks and debt securities). In the event that the exposure or customer moves between different rating grades, this leads to a change in the estimated PD. The estimated PD is adjusted to various macroeconomic scenarios.

<u>Loss given default:</u> The Group estimates LGD on the basis of internally developed statistical models, publicly available data and other historical information. The data are primarily collected from the portfolio of customers in default, where the repayment of past-due outstanding exposures is observed from the time of the occurrence of default. In some cases (e.g. securities), these data are also based on other data used in regulatory models. The estimated LGD is adjusted to various macroeconomic scenarios.

<u>Exposure at default</u> is the expected exposure upon the occurrence of an event of default. The Group estimates EAD for each future month. The starting point is the current exposure of the Group, which is monitored based on the estimated changes in exposure. In the case of transactions with a contractual amortisation schedule, the exposure is estimated on the basis of the amortisation plan adjusted for any advance payments and potential late payments (hereinafter: the late payment scenario). In the case of transactions without a predefined amortisation schedule, EAD of the drawn portion of the exposure is equal to the drawn amount up to maturity of the transaction including future interest. At the time of maturity of the transaction, the late payment scenario is taken into account. EAD for the off-balance sheet portion of the exposure is equal to the off-balance sheet amount as at the date of credit loss calculation up to the transaction maturity date. At the time of maturity, the late payment scenario is taken into account. The off-balance sheet portion is multiplied by the conversion factor estimated on the basis of historical data or the regulatory set conversion factor when the Group does not have enough available historical data on actual drawn amounts.

Methods for assessing expected credit losses

The Group creates impairments of financial assets or provisions for off-balance sheet commitments and contingencies on the basis of:

- individual assessment or
- collective assessment.

NOTES TO THE FINANCIAL STATEMENTS (continued)

Individual assessment of expected credit losses is normally used in the case of significant exposures with deteriorated credit quality (non-performing exposures), depending on the specific amount of gross exposure. Individual assessments of expected credit losses are made on the basis of projected future cash flows, taking into account all relevant information about the debtor's financial position and ability to pay.

For the purpose of **collective** assessment of expected credit losses, the credit portfolio is divided into exposure classes according to the following types of debtors:
- central government,
- corporates,
- sole proprietors,
- retail customers,
- banks.

Credit risk parameters used to calculate expected credit losses are typically designed in the form of models and vary depending on the type of debtor; that is PD for retail customers, LGD for corporates and CCF depending on the type of financial instrument. Models are based on historical data and take into account future prospects.

Measuring expected credit losses
An expected credit loss is measured as follows:
- financial assets not impaired as at the reporting date: the difference between the present value of contractual cash flows and the present value of expected cash flows;
- financial assets impaired as at the reporting date: the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: the present value of the difference between the contractual cash flows if the loan is drawn down and the expected cash flows;
- financial guarantees: the present value of expected payments to the guarantee holder less any amounts that the Group expects to replace.

The estimation of expected credit losses is complex and requires significant judgements of the management as well as estimates and assumptions, particularly in the following areas:
- assessment of a significant increase in credit risk since initial recognition and
- inclusion of forward-looking information in the measurement of expected credit risk losses.

Significant increase in credit risk
The Group classifies financial instruments into stages at initial recognition and on the reporting date based on the following criteria that may reflect a significant increase in credit risk:
- the credit rating or changes in the credit rating as a result of early identification of an increased credit risk (the Early Warning System);
- the debtor has been added to the watch list;
- change in the repayment terms of the financial asset because of the debtor's failure to pay their debt under the initially agreed terms and conditions (restructuring of the financial asset);
- a significant loan obligation is over 30 days past due.

Forward-looking information
IFRS 9 is based on the concept of expected losses, based on which expected credit loss is adjusted to macroeconomic forecasts, thus ensuring that future events are taken into account. Where there is a non-linear link between various macroeconomic forecasts and the associated credit risk losses, more than one macroeconomic scenario should be included in the measurement of expected credit losses. In such a case, the expected credit loss will be calculated as the probability-weighted estimate of expected credit losses over the life of the financial instrument on the basis of pre-calculated macroeconomic scenarios.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

For the purposes of calculating the expected loss, three scenarios are calculated which cover significant non-linearities between macroeconomic forecasts and the associated credit losses:

- the baseline scenario, which is based on the forecasts of economic trends of the Institute of Macroeconomic Analysis and Development of the Republic of Slovenia (IMAD) and which has also been used in the preparation of the Business Plan;
- the optimistic (upside) scenario, which assumes a more favourable economic environment in the future than that forecast in the baseline scenario;
- the pessimistic (downside) scenario, which assumes a deteriorating economic environment compared to the one used in the baseline scenario.

The methodology for calculating macroeconomic scenarios allows the Group to use more than three scenarios for the purposes of calculating the ECL in the event of increased volatility in the economy or one-off events. In the second half of 2018, the economy in the key partners of Slovenia (Germany, Italy) began to cool down and, at the same time, an increasing number of warnings indicated the deterioration of the economic environment. Thus, according to the index values calculated by the Munich Institute for Economic Research (IFO), the mood in the European economy deteriorated in the last quarter. Uncertainty associated with the UK exit from the EU (Brexit) is increasing, too. The Bank of England analyses show a very high negative impact of Brexit on the economic environment in the EU. On 19 December 2018, the Bank of Slovenia published its macroeconomic trend forecasts for Slovenia for the next three years, which are typically lower than the forecasts of IMAD from September 2018.

For the above reasons, the Group decided to prepare a fourth scenario for calculating the expected credit loss for 2019, so that it now has two pessimistic scenarios:

- The pessimistic scenario 1, which assumes a deteriorating economic environment compared to the one used in the baseline scenario.
- The pessimistic scenario 2, which takes into account the Bank of Slovenia's macroeconomic forecasts (December 2018) and complements the previous pessimistic scenario based on the IMAD's Autumn Forecasts with the newest macroeconomic projections.

Both optimistic and pessimistic scenarios are designed to meet each of the following requirements:

- The scenario should be based on events that are most relevant for the Group, taking into account the Group’s business and financing models.
- The scenario should be based on events that are highly probable, and not on extreme events that present a risk of collapse of the Group.

The table below shows the macroeconomic variables forecasts that are needed to calculate the expected credit losses across all four scenarios.

FORCASTS OF MACROECONOMIC VARIABLES INCLUDED IN ECLs MEASUREMENT IN SCENARIOS

Year	2019	2020	2021	2022
GDP growth				
– Base scenario	3.67%	3.45%	2.98%	2.88%
– Upside scenario	5.09%	4.86%	4.40%	3.82%
– Downside scenario 1	(0.24%)	(0.47%)	(0.93%)	0.27%
– Downside scenario 2	(0.54%)	(0.87%)	(0.93%)	0.27%
Unemployment rates				
– Base scenario	4.85%	4.42%	4.16%	5.12%
– Upside scenario	4.59%	3.86%	3.30%	4.55%
– Downside scenario 1	5.59%	5.66%	5.83%	6.24%
– Downside scenario 2	5.61%	5.77%	5.98%	6.34%

The table below shows the impact of changes in macroeconomic variables on the level of the average probability of default, the average loss given default and the average expected loss.

NOTES TO THE FINANCIAL STATEMENTS (continued)

IMPACT OF CHANGES INMACROECONOMIC VARIABLES ON THE LEVEL OF THE PROBABILITY OF DEFAULT, LOSS GIVEN DEFAULT AND EXPECTED CREDIT LOSS

	Change of macroeconomic indicator as expected (v %)
GDP growth	
– Base scenario	–
– Upside scenario	1.30
– Downside scenario	(3.67)
Unemployment rates	
– Base scenario	–
– Upside scenario	(0.56)
– Downside scenario	1.24

SCENARIO	Average PD	Average LGD	ECL (in thousand EUR)
Base scenario	4.63%	52.87%	55,153
Upside scenario	4.55%	46.48%	45,617
Downside scenario	4.76%	62.78%	70,200

Note:
The average change in any individual macroeconomic variable for the optimistic or the pessimistic scenario is calculated as the average of changes in the individual macroeconomic variable by optimistic or pessimistic scenario against the expected scenario in the 2019–2022 period.

The average probability of default and the average loss given default for each scenario are calculated based on the average probability of default and/or average loss given default, weighted with the average exposure at default.

The sensitivity analysis is based on the portfolio of loans and guarantees, where the expected loss is calculated collectively.

The sensitivity analysis of credit parameters to the change in macroeconomic indicators shows that in the optimistic scenario, with an increase in GDP growth by 1.3 percentage point and a decline in the unemployment rate by 0.6 percentage point, the average probability of default was lower by 0.1 percentage point, the average loss given default by 6.4 percentage points and the expected loss by EUR 9.5 million. In the pessimistic scenario, with a decrease in GDP growth by 3.7 percentage points and an increase in the unemployment rate by 1.2 percentage points, the average probability of default was higher by 0.1 percentage point, the average loss given default by 9.9 percentage points and the expected loss by EUR 15 million.

2.1.3 Maximum exposure to credit risk

The following table shows the maximum exposure to credit risk from the balance sheet items and off-balance sheet items, without taking collateral or other credit protection into account.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

MAXIMUM EXPOSURE TO CREDIT RISK WITHOUT TAKING INTO ACCOUNT THE EFFECTS OF LOAN COLLATERAL AND OTHER REDUCTIONS

	As at 31 December	Note	Maximum exposure 2018	2017
	Credit risk exposures:			
1	Cash balances with the central bank and other demand deposits with banks	2.1.4. a)	494,590	373,455
2	Financial assets at fair value through other comprehensive income	2.1.4. b)	132,393	
	Available-for-sale financial assets	2.1.4. b)		1,044,721
3	Financial assets at amortised cost		2,918,162	2,052,123
	– debt securities	2.1.4. c)	946,334	–
	– loans to banks	2.1.4. d)	30,784	60,745
	– loans to non-bank customers		1,928,338	1,967,461
	– loans and receivables to retail customers	2.1.4. e)	905,739	869,445
	– loans and receivables to corporate entities	2.1.4. f)	1,022,599	1,098,016
	– other financial assets	2.1.4. g)	12,706	23,917
	Held-to-maturity investments	2.1.4. c)		15,408
	Total credit risk exposure - relating to on-balance sheet assets		**3,545,145**	**3,485,707**
	Credit risk exposures relating to commitments and contingencies			
	– financial guarantees	2.1.4. h)	48,411	34,676
	– other commitments and contingencies	2.1.4. i)	635,567	570,716
	Total credit risk exposure - relating to off-balance sheet assets		**683,978**	**605,392**
	Total credit risk exposure		**4,229,123**	**4,091,099**

The exposure arising from balance sheet assets and commitments and contingencies shown above is based on carrying values as shown in the statement of financial position and in commitments and contingencies. Balance sheet assets are disclosed at their carrying amount after impairment, and off-balance sheet items are disclosed at nominal value.

Financial assets measured at fair value through other comprehensive income include only debt financial instruments.

Non-trading financial assets mandatorily at fair value through profit or loss (both used and unused) are excluded from the table. As at 31 December 2018 the amount was EUR 25.6 million.

Lease receivables are included in loans to non-bank customers and are not specifically dealt with due to low exposure.

2.1.4 The balance of loans and loan commitments by credit rating grade and risk group

The gross exposure to credit risk and impairments or provisions made by credit rating grade and risk group are shown below with regard to the type of financial assets and the type of loan commitments.

a) Cash balances with the central bank and other demand deposits with banks

The balances with the central bank and demand deposits with banks mainly consist of cash balances with the central bank, which are classified into stage 1.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

b) Financial assets at fair value through other comprehensive income

FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Financial assets at fair value through other comprehensive income						
Credit rating "A"	122,111	–	–	–	122,111	992,614
Credit rating "B"	10,404	–	–	–	10,404	52,107
Credit rating "C"	–	–	–	–	–	–
Credit rating "D"	–	–	–	–	–	–
Credit rating "E"	–	–	–	–	–	–
Total gross amount	**132,515**	**–**	**–**	**–**	**132,515**	**1,044,721**
Less: total impairment	(122)	–	–	–	(122)	–
Total net amount	**132,393**	**–**	**–**	**–**	**132,393**	**1,044,721**

Note:
For 2017, available-for-sale financial assets are shown in accordance with IAS 39.

c) Debt securities, measured at amortised cost

DEBT SECURITIES, MEASURED AT AMORTISED COST

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Debt securities, measured at amortised cost						
Credit rating "A"	918,624	–	–	–	918,624	15,408
Credit rating "B"	27,986	–	–	–	27,986	–
Credit rating "C"	–	–	–	–	–	–
Credit rating "D"	–	–	–	–	–	–
Credit rating "E"	–	–	–	–	–	–
Total gross amount	**946,610**	**–**	**–**	**–**	**946,610**	**15,408**
Less: total impairment	(276)	–	–	–	(276)	–
Total net amount	**946,334**	**–**	**–**	**–**	**946,334**	**15,408**

Note:
For 2017, financial assets held to maturity are shown in accordance with IAS 39.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

d) Loans to banks, measured at amortised cost

LOANS TO BANKS, MEASURED AT AMORTISED COST

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Loans to banks						
Credit rating "A"	21,302	–	–	–	21,302	43,995
Credit rating "B"	9,514	–	–	–	9,514	16,750
Credit rating "C"	–	–	–	–	–	–
Credit rating "D"	–	–	–	–	–	–
Credit rating "E"	–	–	–	–	–	–
Total gross amount	**30,816**	**–**	**–**	**–**	**30,816**	**60,745**
Less: total impairment	(32)	–	–	–	(32)	–
Total net amount	**30,784**	**–**	**–**	**–**	**30,784**	**60,745**

e) Loans to retail customers, measured at amortised cost

LOANS TO RETAIL CUSTOMERS, MEASURED AT AMORTISED COST

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Loans to corporate entities						
Credit rating "A"	889,271	837	2,771	–	892,879	843,515
Credit rating "B"	4,005	1,297	697	–	5,999	13,300
Credit rating "C"	182	6,385	1,359	–	7,926	12,463
Credit rating "D"	–	–	2,945	–	2,945	4,564
Credit rating "E"	–	–	7,909	–	7,909	11,816
Total gross amount	**893,458**	**8,519**	**15,681**	**–**	**917,658**	**885,658**
Less: total impairment	(1,128)	(2,541)	(8,250)	–	(11,919)	(16,213)
Total net amount	**892,330**	**5,978**	**7,431**	**–**	**905,739**	**869,445**

f) Loans to corporate entities, measured at amortised cost

LOANS TO CORPORATE ENTITIES, MEASURED AT AMORTISED COST

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Loans to retail costumers						
Credit rating "A"	516,162	32	105	–	516,299	540,754
Credit rating "B"	367,282	22,513	10	–	389,805	395,514
Credit rating "C"	64,045	57,387	1	–	121,433	115,469
Credit rating "D"	–	–	22,242	14,310	36,552	168,068
Credit rating "E"	–	–	18,231	491	18,722	78,961
Total gross amount	**947,489**	**79,932**	**40,589**	**14,801**	**1,082,811**	**1,298,766**
Less: total impairment	(16,462)	(21,900)	(25,974)	4,124	(60,212)	(200,750)
Total net amount	**931,027**	**58,032**	**14,615**	**18,925**	**1,022,599**	**1,098,016**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

g) Other financial assets

Other financial assets include mainly cash withdrawals at ATMs and receivables from the sale of securities classified into Stage 1.

h) Financial guarantees

FINANCIAL GUARANTEES

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Financial guarantees						
Credit rating "A"	22,715	–	–	–	22,715	16,518
Credit rating "B"	17,286	619	–	–	17,905	16,053
Credit rating "C"	1,630	2,227	–	–	3,857	2,461
Credit rating "D"	–	–	5,875	–	5,875	6,294
Credit rating "E"	–	–	19	–	19	88
Total gross amount	**41,631**	**2,846**	**5,894**	**–**	**50,371**	**41,414**
Less: total impairment	(211)	(236)	(1,513)		(1,960)	(6,738)
Total net amount	**41,420**	**2,610**	**4,381**	**–**	**48,411**	**34,676**

i) Other commitments and contingencies

OTHER COMMITMENTS AND CONTINGENCIES

As at 31 December	2018					2017
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total	Total
Other commitments and contingencies						
Credit rating "A"	438,987	28	–	–	439,015	392,509
Credit rating "B"	131,400	17,638	–	–	149,038	137,217
Credit rating "C"	19,318	26,639	–	–	45,957	41,613
Credit rating "D"	–	–	1,743	–	1,743	5,586
Credit rating "E"	–	–	12,777	–	12,777	16,690
Total gross amount	**589,705**	**44,305**	**14,520**	**–**	**648,530**	**593,615**
Less: total impairment	(1,658)	(1,188)	(10,117)	–	(12,963)	(22,899)
Total net amount	**588,047**	**43,117**	**4,403**	**–**	**635,567**	**570,716**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.5 Credit risk exposure by industry sector and geographical area

The following table shows the credit risk exposure of financial assets by industry sector and geographical area.

CREDIT RISK EXPOSURE OF FINANCIAL ASSETS ACCORDING TO INDUSTRY SECTOR AND GEOGRAPHICAL AREA

		2018						2017	
	As at 31 December	Loans to banks measured at amortised cost	Loans to non-bank customers measured at amortised cost	Debt securities, measured at amortised cost	Financial assets at fair value through other comprehensive income	Other financial assets	Financial guarantees and other commitments and contingencies	On-balance sheet exposure	Off-balance sheet exposure
	Concentration by industry sector								
1	Manufacturing	–	297,498	40,874	–	47	139,866	337,342	121,818
2	Construction	–	34,044	5,597	–	42	78,184	33,103	72,176
3	Trade	–	105,016	2,053	–	640	170,024	167,676	117,320
4	Financial and insurance activities	30,784	48,874	208,218	12,373	505,484	42,559	732,862	37,501
5	Professional, scientific and technical activities	–	32,038	–	–	35	33,425	42,977	31,652
6	Public administration and defence	–	34,884	660,333	120,020	829	4,447	783,637	15,903
7	Other	–	470,245	29,259	–	200	95,673	518,573	94,564
8	Retail customers	–	905,739	–	–	19	119,800	869,537	114,458
	– covered by mortgages	–	453,805	–	–	–	2,031	446,217	3,598
	– not covered by mortgages	–	451,934	–	–	19	117,769	423,320	110,860
	Total	**30,784**	**1,928,338**	**946,334**	**132,393**	**507,296**	**683,978**	**3,485,707**	**605,392**
	Geographical concentration								
1	Slovenia	5,001	1,915,285	352,920	38,283	431,801	678,087	2,663,824	598,977
2	Other EU countries	23,297	5,936	537,725	85,056	43,284	5,240	709,471	662
3	Europe (without the EU member	–	1,032	13,412	–	22,845	584	25,655	5,684
4	Other coutries	2,486	6,085	42,277	9,054	9,366	67	86,757	69
	Total	**30,784**	**1,928,338**	**946,334**	**132,393**	**507,296**	**683,978**	**3,485,707**	**605,392**

Note:
Non-trading financial assets mandatorily at fair value through profit or loss are are excluded from the table.
Other financial assets include "Cash, cash balances with the central bank and other demand deposits wih banks" and "Other financial assets".

The Group's exposure by geographical areas is based on the domicile or head office of the debtor or counterparty.

In 2018, the entire portfolio exposed to credit risk increased by 3.4% and amounted to EUR 4,229.1 million as at the 2018 year-end (2017: EUR 4,091.1 million). The balance sheet exposure increased by 1.7% in 2018, and off-balance sheet exposure by 13%. The largest absolute increase was in financial and insurance activities, in public administration, defence and manufacturing. Exposures to retail customers also increased.

The Group operates mainly in the territory of the Republic of Slovenia. The largest exposure to the rest of the world is reported to customers from other EU Member States, primarily from France, the Netherlands, Luxembourg, Belgium, Germany, Austria and the Czech Republic, all of which are predominantly from debt securities.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.6 Loans to non-bank customers by past due status

Presented below is gross exposure to non-bank customers and their impairments by maturity bucket.

LOANS TO NON-BANK CUSTOMERS BY PAST DUE STATUS

As at 31 December	2018		2017	
	Gross carrying amount	Loss allowance	Gross carrying amount	Loss allowance
Non past-due	1,943,434	(48,857)	2,034,651	(133,173)
Past due up to 30 days	19,822	(2,598)	27,390	(3,586)
Past due 31 to 60 days	9,137	(2,855)	14,348	(1,662)
Past due 61 to 90 days	3,102	(1,117)	6,555	(2,817)
Over 90 days past due	24,974	(16,704)	101,480	(75,725)
Total	**2,000,469**	**(72,131)**	**2,184,424**	**(216,963)**

Note:
Non-trading financial assets mandatorily at fair value through profit or loss are excluded from the table.

Past due loans are loans where the debtor has failed to make a payment when contractually due in part or in the total amount. Past due loans include the total amount of exposure under a single loan agreement and not just the instalment not paid when contractually due. Exposures from other loan agreements to the same debtor not in arrears are not included among past due loans.

In the report concerned, only loans to non-bank customers are presented by maturity bucket because others exposures are not past due or do not include significant amounts past due.

In the reporting period, past due loans to non-bank customers declined by 61.9% to EUR 57 million as at the 2018 year-end (vs. EUR 149.8 million in 2017). Loans past due over 90 days decreased the most, primarily as a result of the sale of non-performing portfolio.

2.1.7. Movements in loss allowance and provisions

The following table shows the movement in impairments and provisions between stages and by class of assets.

a) Impairments of cash and cash balances with the central bank and demand deposits with banks
Cash and cash balances with the central bank and demand deposits with banks are risk-free items that are not impaired.

b) Impairments of financial assets (debt securities), measured at fair value through other comprehensive income
Impairments of financial assets (debt financial instruments), measured at fair value through other comprehensive income, amounted to EUR 122 thousand at the end of 2018 and were fully classified in stage 1.

c) Impairments of debt securities at amortised cost
Impairments of debt securities at amortised cost amounted to EUR 276 thousand at the end of 2018 and were fully classified in stage 1.

d) Impairments of loans to banks at amortised cost
Impairments of loans to banks at amortised cost amounted to EUR 32 thousand at the end of 2018 and were fully classified in stage 1.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

e) Impairments of loans and receivables to retail customers at amortised cost

MOVEMENTS IN LOSS ALLOWANCE – LOANS AND RECEIVABLES TO RETAIL CUSTOMERS AT AMORTISED COST

	2018				
Year	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total
Loss allowance as at 1. January	**944**	**4,481**	**10,640**	**–**	**16,065**
New financial assets originated or purchased (increase)	233	134	3	–	370
Transfers between stages due to change in credit risk	2,174	(1,720)	(454)	–	–
transfer to Stage 1	2,181	(1,939)	(242)	–	–
transfer to Stage 2	(3)	791	(788)	–	–
transfer to Stage 3	(4)	(572)	576	–	–
transfer to Stage 3 - POCI	–	–	–	–	–
Financial assets that have been derecognised or recovered (decrease)	(965)	(554)	(2,137)	–	(3,656)
Write-offs	–	–	(2,383)	–	(2,383)
sale	–	–	(1,310)	–	(1,310)
other write-offs	–	–	(1,073)	–	(1,073)
Changes due to modifications that did not result in derecognition	–	72	–	–	72
Changes in models/risk parameters	–	–	–	–	–
Net increases/(decreases) due to change in credit risk	(1,216)	214	2,589	–	1,587
Other changes	(42)	(86)	(8)	–	(136)
revolving loans and overdraft	(44)	(94)	(12)	–	(150)
foreign exchange and other	2	8	4	–	14
Loss allowance as at 31 December	**1,128**	**2,541**	**8,250**	**–**	**11,919**

In 2018, impairments of loans to retail customers decreased by EUR 4.1 million, mainly due to repayments and write-offs of receivables. The credit risk reduction was also affected by the re-calculation of credit parameters, which was the result of new forecasts of the macroeconomic environment. This affected the reversal of impairments for loans to retail customers in the amount of EUR 0.1 million. The impact of new macroeconomic environment forecasts on the level of impairments is included in the item "Net increases/(decreases) due to changes in credit risk".

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

f) Impairments of loans and receivables to corporate entities at amortised cost

MOVEMENTS IN LOSS ALLOWANCE – LOANS AND RECEIVABLES TO CORPORATE ENTITIES AT AMORTISED COST

	2018				
Year	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total
Loss allowance as at 1. January	**11,055**	**30,477**	**77,524**	**(585)**	**118,471**
New financial assets originated or purchased (increase)	10,552	2,462	360	(2)	13,372
Transfers between stages due to change in credit risk	4,778	(5,511)	733	–	–
transfer to Stage 1	5,456	(5,456)	–	–	–
transfer to Stage 2	(631)	736	(105)	–	–
transfer to Stage 3	(47)	(791)	838	–	–
transfer to Stage 3 - POCI	–	–	–	–	–
Financial assets that have been derecognised or recovered (decrease)	(8,105)	(9,152)	(9,069)	(4,012)	(30,338)
Write-offs	–	(6)	(44,087)	(909)	(45,002)
sale	–	(6)	(42,614)	(909)	(43,529)
other write-offs	–	–	(1,473)	–	(1,473)
Changes due to modifications that did not result in derecognition	–	5	–	–	5
Changes in models/risk parameters	–	–	–	–	–
Net increases/(decreases) due to change in credit risk	(2,301)	5,005	(30)	1,384	4,058
Other changes	483	(1,380)	543	–	(354)
revolving loans and overdraft	483	(1,381)	543	–	(355)
foreign exchange and other	–	1	–	–	1
Loss allowance as at 31 December	**16,462**	**21,900**	**25,974**	**(4,124)**	**60,212**

Impairments of loans to corporate entities in 2018 decreased by EUR 58.3 million, primarily from the sale and repayment of receivables. The reduction of impairments was also affected by the re-calculation of credit parameters, which was the result of new macroeconomic forecasts. This affected the reversal of impairments for loans to corporate customers in the amount of EUR 2.75 million. The impact of new macroeconomic environment forecasts on the level of impairment is included in the item "Net increases/(decreases) due to changes in credit risk".

g) Impairments of other financial assets at amortised cost

As at 31 December 2018, impairments of other financial assets amounted to EUR 0.5 million. As much as 92.8% of the gross value of other financial assets was classified into stage 1.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

h) Provisions of financial guarantees

MOVEMENTS IN PROVISIONS – FINANCIAL GUARANTEES

	2018				
Year	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total
Provisions as at 1. January	**243**	**862**	**2,157**	**–**	**3,262**
New financial assets originated or purchased (increase)	173	–	871	–	1,044
Transfers between stages due to change in credit risk	4	22	(26)	–	–
transfer to Stage 1	39	(11)	(28)	–	–
transfer to Stage 2	(35)	35	–	–	–
transfer to Stage 3	–	(2)	2	–	–
transfer to Stage 3 - POCI	–	–	–	–	–
Financial assets that have been derecognised or recovered (decrease)	–	–	(77)	–	(77)
Write-offs	–	–	–	–	–
sale	–	–	–	–	–
other write-offs	–	–	–	–	–
Changes due to modifications that did not result in derecognition	–	–	–	–	–
Changes in models/risk parameters	–	–	–	–	–
Net increases/(decreases) due to change in credit risk	(209)	(648)	(1,412)	–	(2,269)
Other changes	–	–	–	–	–
revolving loans and overdraft	–	–	–	–	–
foreign exchange and other	–	–	–	–	–
Provisions as at 31 December	**211**	**236**	**1,513**	**–**	**1,960**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

i) Provisions for other loan commitments

MOVEMENTS IN PROVISIONS – OTHER LOAN COMITTMENTS

	2018				
Year	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Stage 3 - POCI Lifetime ECL	Total
Provisions as at 1. January	**928**	**1,475**	**13,670**	**–**	**16,073**
New financial assets originated or purchased (increase)	633	52	381	–	1,066
Transfers between stages due to change in credit risk	678	(669)	(9)	–	–
transfer to Stage 1	830	(816)	(14)	–	–
transfer to Stage 2	(151)	153	(2)	–	–
transfer to Stage 3	(1)	(6)	7	–	–
transfer to Stage 3 - POCI	–	–	–	–	–
Financial assets that have been derecognised or recovered (decrease)	(337)	(61)	(1,091)	–	(1,489)
Write-offs	–	–	–	–	–
sale	–	–	–	–	–
other write-offs	–	–	–	–	–
Changes due to modifications that did not result in derecognition	–	–	–	–	–
Changes in models/risk parameters	–	–	–	–	–
Net increases/(decreases) due to change in credit risk	(386)	609	(2,836)	–	(2,613)
Other changes	142	(218)	2	–	(74)
revolving loans and overdraft	142	(217)	2	–	(73)
foreign exchange and other	–	(1)	–	–	(1)
Provisions as at 31 December	**1,658**	**1,188**	**10,117**	**–**	**12,963**

j) Impact of significant changes in gross financial assets on impairments and provisions in 2018

In 2018, the volume of impairments and provisions was largely influenced by the sale of portfolio of non-performing loans.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.8. Modified financial assets

The table below shows financial assets for loans to non-bank customers which, in 2018, experienced changes in contractual cash flows, their amortised cost before the change in the cash flows, the net gain/loss on the change in the cash flows and the gross carrying amount of financial assets, which, from the initial recognition when the value adjustment for the loss of the criteria was still measured by the amount equal to the expected credit losses over the entire life (stage 2), were classified into stage 1, where the value adjustment for loss was equal to the expected credit losses in a 12-month period.

MODIFIED FINANCIAL ASSETS

	2018
Financial assets (with loss allowance based on lifetime ECL) modified during the period Stage 2, 3 (lifetime ECL)	
– Amortised cost before modification	799
– Net modification gain/(loss)	(52)
Financial assets for which loss allowance has changed in the period from Stage 2 (lifetime ECL) to Stage 1 (12-month ECL)	
– Gross carrying amount	–

2.1.9. Restructured loans

Restructured loans are loans resulting from a debtor's incapacity to repay debt in accordance with the originally agreed contractual terms due to financial difficulties of the debtor (i.e. troubled loans), whereby the Group has taken actions or measures which it would not have taken had the economic and financial position of the debtor been normal. Restructuring measures may entail a loss for the Group, as they consist of concessions towards a debtor.

Loans can be restructured in two ways:
- by modifying the terms and conditions of the original loan contract with an annex;
- by total or partial refinancing of a troubled debt contract.

Restructuring actions may include:
- extending the term of the loan or declaring a moratorium on the repayment of debt;
- decreasing the claimed amount following a contractually agreed write-off or equity restructuring;
- debt to equity swap;
- repossession of other assets (exp. property, plant and equipment, securities) including realising collateral for partial or full debt recovery;
- a reduction in the interest rate to a level below market conditions, i.e. a level that could at the same time from the same institution be granted to other debtors who are not yet in a situation of default,
- reduction in the interest rate to a level which is not below the market conditions, i.e. a level that could at the same time from the same institution be granted to other debtors who are not yet in a situation of default;
- other similar actions.

Restructuring measures are divided into short-term and long-term. Most solutions comprise a combination of different restructuring measures that sometimes relate to a different time period with a combination of short-term and long-term options.

The Group must determine the leading measure for each restructured loan. This is the measure that most affects the net present value of the restructured loan.

In the Group, all loan restructuring decisions exceeding a certain threshold are supported by a documented analysis of alternative solutions with their economic effects (that may arise from the realisation of collaterals, sales of loans, loan agreement terminations or any other foreseeable action). After restructuring, loans cease to be accounted for as restructured when all the terms and conditions (exit criteria) are met, as required by the standards set by the European Banking Authority on the treatment of restructured and non-performing exposures.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

The Group assesses whether the restructuring of an exposure to a defaulter is reasonable, which also applies to exposures included in compulsory settlements. When restructuring of the exposure to the debtor in question is reasonable, the Group forms an appropriate restructuring plan and monitors its execution and effects. When restructuring an exposure to a company is not reasonable without the restructuring of that entire company, the latter is obliged to submit to the Group its business plan including operational, equity and financial restructuring measures. When the Group decides that it is no longer reasonable to continue restructuring an exposure, an approximate loan recovery plan is made.

RESTRUCTURED LOANS

							Total restructured loans
	Loans to retail customers			Loans to corporates			
As at 31 December 2018	Loans without mortgage collateral	Collateralised mortgage loans		Loans without mortgage collateral	Collateralised mortgage loans		
Gross loans	1,394	4,961	**6,355**	5,000	92,188	**97,188**	**103,543**
– performing loans	1,324	1,596	**2,920**	475	11,001	**11,476**	**14,396**
– non-performing loans (NPLs)	70	3,365	**3,435**	4,525	81,187	**85,712**	**89,147**
Less: total impairments	(413)	(1,869)	**(2,282)**	(2,865)	(33,987)	**(36,852)**	**(39,134)**
– impairments of performing loans	(392)	(596)	**(988)**	(62)	(4,722)	**(4,784)**	**(5,772)**
– impairments of non-performing loans (NPLs)	(21)	(1,273)	**(1,294)**	(2,803)	(29,265)	**(32,068)**	**(33,362)**
Net loans	**981**	**3,092**	**4,073**	**2,135**	**58,201**	**60,336**	**64,409**

Share of restructured **gross loans** in **total gross loans** to non-bank customers	**5.18%**
Share of restructured **net loans** in total **net loans** to non-bank customers	**3.34%**

							Total restructured loans
	Loans to retail customers			Loans to corporates			
As at 31 December 2017	Loans without mortgage collateral	Collateralised mortgage loans		Loans without mortgage collateral	Collateralised mortgage loans		
Gross loans	2,952	5,743	**8,695**	20,949	203,312	**224,261**	**232,956**
– performing loans	2,738	2,420	**5,158**	9,738	18,671	**28,409**	**33,567**
– non-performing loans (NPLs)	214	3,323	**3,537**	11,211	184,641	**195,852**	**199,389**
Less: total impairments	(584)	(1,873)	**(2,457)**	(12,474)	(123,522)	**(135,996)**	**(138,453)**
– impairments of performing loans	(527)	(473)	**(1,000)**	(3,152)	(6,063)	**(9,215)**	**(10,215)**
– impairments of non-performing loans (NPLs)	(57)	(1,400)	**(1,457)**	(9,322)	(117,459)	**(126,781)**	**(128,238)**
Net loans	**2,368**	**3,870**	**6,238**	**8,475**	**79,790**	**88,265**	**94,503**

Share of restructured **gross loans** in **total gross loans** to non-bank customers	**10.66%**
Share of restructured **net loans** in total **net loans** to non-bank customers	**4.80%**

Note:
Loans include non-trading financial assets mandatorily at fair value through profit or loss.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

In 2018, gross forborne loans fell by EUR 129.4 million, of which performing forborne loans declined by EUR 19.2 million and non-performing forborne loans decreased by EUR 110.2 million. Due to the reduction in gross forborne loans, the share of gross forborne loans in total gross loans to non-bank customers decreased by 5.5 percentage points. The reduction in gross forborne loans was the result of the sale of the portfolio of non-performing loans, regular and early repayments, and the effect of purchased or originated credit-impaired financial assets[1] in forborne non-performing loans.

2.1.10. Non-performing loans

All default loans and impaired loans which fulfil at least one of the following conditions are treated as non-performing loans:

- the debtor is past due more than 90 days on any material credit obligation to the Group;
- the Group considers that the debtor is unlikely to pay its credit obligations to the Group in full without recourse by the Group to actions such as realising security (loans to D- and E-rated debtors according to internal credit rating methodology).

For loans to retail customers, the Group uses the definition of default at the level of individual exposure.

Loans are classified as non-performing for their entire amount and without taking into account the existence of any collateral.

NON-PERFORMING LOANS

Stanje 31. december 2018	Loans to non-bank customers	Loans to banks	Other Financial assets	Total loans and other Financial assets
Non-performing loans	118,616	–	956	**119,572**
Share of NPLs in total loans	5.80%	–	0.19%	**4.63%**
Coverage of NPLs with total impairments	78.33%	–	50.09%	**78.14%**

Stanje 31. december 2017	Loans to non-bank customers	Loans to banks	Other Financial assets	Total loans and other Financial assets
Non-performing loans	267,234	–	2,125	**269,359**
Share of NPLs in total loans	12.23%	–	0.53%	**10.19%**
Coverage of NPLs with total impairments	81.19%	–	28.11%	**80.77%**

Note:
Loans include non-trading financial assets mandatorily at fair value through profit or loss
Other financial assets include cash balances with the central bank, demand deposits with banks and other financial assets.

In 2018, the amount of non-performing loans decreased to EUR 119.6 million. (2017: EUR 269.4 million), so that the share of non-performing loans stood at 4.6% (2017: 10.2%). The decline in non-performing loans was mainly due to the effect of the purchased or originated credit-impaired assets in and the sale of the portfolio of non-performing loans. The reduction in non-performing loans was also influenced by repayments, write-offs, recoveries (realisation of collaterals) and the reclassification of debtors into higher rating classes thanks to the improvement of their financial position. In order to reduce non-performing loans, the Group carries out recovery proceedings, writes off the receivables which were justifiably deemed unrecoverable in the recovery process (as explained in Note 1.5), implements a process for the early detection of increased credit risk and has a selective approach to granting new loans (the base criterion for the approval of a new loan is a sufficient cash flow to repay the loan or the calculated credit rating with respect to loan approval for retail customers).

[1] As of 1 January 2018, IFRS 9 became effective, which had a significant impact on the gross value of non-performing loans and their impairments. In accordance with the Instructions for the introduction of the Decision on Reporting of Monetary and Financial Institutions, resulting from IFRS 9 and Annex V of the amended Commission Implementing Regulation (EU) No. 680/2014, the purchased or originated credit-impaired financial assets (POCI loans) are disclosed at net value or the difference to the fair value is taken into account in the gross value of loans. The difference to the fair value of POCI loans therefore reduces the gross value of non-performing loans and impairments.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.11. Loan collateral

The value of collateral and credit risk concentration by type of collateral accepted by the Group is shown in the table below.

VALUE OF COLLATERAL BY COLLATERAL TYPE

As at 31 December		2018		2017	
	Type of collateral	**Amount**	**Structure**	**Amount**	**Structure**
1	Deposits from banks	11,216	0.3%	14,993	0.4%
2	Irrevocable guarantees of Republic of Slovenia	224,495	6.1%	297,305	8.0%
3	Financial guarantees excluded irrevocable guarantees of Republic of Slovenia	304,706	8.3%	–	–
4	Securities and equities	137,190	3.7%	130,557	3.5%
5	Real estate	2,324,238	63.0%	2,428,636	65.5%
6	Other real collateral	115,138	3.1%	–	–
7	Insurance company	388,084	10.5%	344,347	9.3%
8	Other collateral	184,824	5.0%	492,314	13.3%
	Total amount of collateral	**3,689,891**	100.0%	**3,708,152**	100.0%

Note:
The table includes eligible collaterals. These are collaterals that the Group observes under the IFRS when calculating the impairment or fair value of financial assets or provisions for off-balance sheet commitments.

The largest share in the structure was real property collateral, as their share is 63%. An important share in the structure was insurance with irrevocable guarantees of the Republic of Slovenia, financial guarantees, except for irrevocable guarantees of the Republic of Slovenia, securities and equity shares and insurance with the insurance company, since they represented almost 30% in the structure.

The table below shows gross exposure (not impaired and impaired presented separately) and its impairments and provisions by loan-to-value ratio. Impaired exposures are exposures that have deteriorated credit quality, including purchased or originated credit impaired assets. These are non-performing exposures that the Group classifies for the purpose of estimating the expected credit losses to stage 3.

MORTGAGE-SECURED EXPOSURES BY LOAN LTV RATIO

Non-impaired exposures secured by commercial and residential real properties

As at December		2018	
	LTV	**Gross carrying amount**	**Loss allowance**
1	less than 50%	280,629	(10,407)
2	from 50 to 70%	297,869	(7,228)
3	from 50 to 70%	196,637	(3,550)
4	from 50 to 70%	48,330	(1,314)
5	more than 100%	272,613	(11,838)
	Total	**1,096,077**	**(34,337)**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

Impaired exposures secured by commercial and residential real properties

As at December		2018	
	LTV	Gross carrying amount	Loss allowance
1	less than 50%	12,067	(4,072)
2	from 50 to 70%	13,766	(4,519)
3	from 50 to 70%	7,800	(1,390)
4	from 50 to 70%	43,988	(2,585)
5	more than 100%	21,113	(3,429)
	Total	**98,735**	**(15,995)**

2.1.12. Assets seized for debt repayment

As at the 2018 year-end, the value of assets received for the recovery of collateral claims decreased by 13.1% compared to the 2017 year-end, mainly due to the decline in investment property. Other assets decreased due to the transfer of land and commercial properties to non-current assets held for sale.

ASSETS SEIZED FOR DEBT REPAYMENT

As at 31 December 2018	Carrying amount 2018	2017
Non-current assets held for sale	4,376	265
Property and equipment	148	96
Investment properties	3,434	5,843
Equity and debt securities	199	233
Other	6,049	9,907
Total	**14,206**	**16,344**

The assets obtained in recovery procedures are sold off by the Group at the earliest possible date and certain investment properties are leased out.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

ADDITIONAL DISCLOSURES OF IMPAIRMENT OF FINANCIAL ASSETS – COMPARATIVE INFORMATION FOR 2017 IN ACCORDANCE WITH IAS 39

2.1.13. Loans to non-bank customers and loans to banks

The following tables show loans by their overdue status, impairments and fair value of collateral.

LOANS TO NON-BANK CUSTOMERS AND LOANS TO BANKS

As at 31 December 2017	Loans to non-bank customers	Loans to banks	Total loans
Neither past due nor impaired loans	1,887,892	60,745	**1,948,637**
Past due but not impaired loans	40,805	–	**40,805**
Impaired loans	255,726	–	**255,726**
– individually imapired loans	218,245	–	**218,245**
– collectively imapired loans	37,481	–	**37,481**
Gross loans	**2,184,423**	**60,745**	**2,245,168**
Less: total impairments	(216,963)	–	**(216,963)**
– individual impairments	(148,777)	–	**(148,777)**
– collective impairments	(68,186)	–	**(68,186)**
Net loans	**1,967,460**	**60,745**	**2,028,205**
Fair value of collateral	**2,415,434**	**–**	**2,415,434**
– of which fair value of collateral for individually impaired loans	192,745	–	**192,745**

Note:
This excludes other financial assets.

Among **impaired loans**, the Group classifies individually and collectively impaired loans with objective evidence for impairment. These include defaulted exposures, i.e. exposures to debtors or derived from transactions, respectively, with internal credit ratings D and E as well as those that are more than 90 days[2] past due, excluding those outstanding exposures that are not subject to impairment. Among **non-impaired loans,** the Group classifies loans that are not subject to impairment (secured by best quality collateral, risk-free items and other loans not impaired according to internal methodology), and collectively impaired loans without objective evidence for impairment (with credit ratings A, B and C, which are not more than 90 days past due).

The fair value of collateral shows the value of deposits, residential and commercial real property and securities and does not take into account any haircuts. Residential and commercial real property is evaluated by independent external appraisers. For valuation purposes, properties' sales agreement values or the adjusted generalised market values published by the Surveying and Mapping Authority of the Republic of Slovenia are also used (this only applies to residential properties with a value of less than EUR 500 thousand). Marketable securities are designated at their market value or by using valuation models. Exceptionally, book value of securities is applied when their fair value cannot be reliably estimated. Deposits pledged as collateral are carried at their book value.

[2] For corporate customers and sole proprietors defaults on exposures are established per debtor, whereas for retail customers per exposure.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.14. Loans neither past due nor impaired

LOANS NEITHER PAST DUE NOR IMPAIRED

As at 31 December 2017

Internal credit rating	Loans and receivables to retail customers: Over-drafts	Credit cards	Housing loans	Consumer loans		Loans and receivables to corporate customers: Large corpo-rates	SMEs	Other		Total loans to non-bank customers	Loans to banks	Total loans
A	38,476	17,525	540,682	237,594	834,277	229,954	297,694	12,136	539,784	**1,374,061**	**43,995**	**1,418,056**
B	–	–	–	20	20	155,934	215,081	18,100	389,115	**389,135**	**16,750**	**405,885**
C	446	1	3,761	2,133	6,341	62,905	42,412	5,049	110,366	**116,707**	–	**116,707**
D	–	–	–	–	-	7,985	1	–	7,986	**7,986**	–	**7,986**
E	–	–	–	–	-	3	–	–	3	3	–	**3**
Total	**38,922**	**17,526**	**544,443**	**239,747**	**840,638**	**456,781**	**555,188**	**35,285**	**1,047,254**	**1,887,892**	**60,745**	**1,948,637**
Fair value of collateral	–	–	955,722	70,169	1,025,891	534,877	515,318	63	1,050,258	**2,076,149**	**–**	**2,076,149**

Note:
This excludes other financial assets.

2.1.15. Loans past due but not impaired

LOAN PAST DUE BUT NOT IMPAIRED

As at 31 December 2017

	Loans and receivables to retail customers: Overdrafts	Credit cards	Housing loans	Consumer loans		Loans and receivables to corporate customers: Large corporates	SMEs	Other		Total loans to non-bank customers
Past due up to 30 days	9,418	154	712	3,872	**14,156**	220	7,859	2,483	**10,562**	**24,718**
Past due 31 to 60 days	265	68	7,131	4,058	**11,522**	251	900	198	**1,349**	**12,871**
Past due 61 to 90 days	114	49	1,771	1,028	**2,962**	–	122	63	**185**	**3,147**
Past due over 90 days	–	–	–	–	**–**	–	69	–	**69**	**69**
Total	**9,797**	**271**	**9,614**	**8,958**	**28,640**	**471**	**8,950**	**2,744**	**12,165**	**40,805**
Fair value of collateral	–	–	22,111	3,057	**25,168**	–	10,030	4,437	**14,467**	**39,635**

Note:
This excludes other financial assets.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.1.16. Individually impaired loans

INDIVIDUALLY IMPAIRED LOANS

As at 31 December 2017	Loans and receivables to retail customers			Loans and receivables to corporate entities				Loans to banks	Total loans
	Consumer loans	Housing loans		Large corporates	SMEs	Other			
Individually impaired loans	2,212	174	**2,386**	95,515	116,117	4,227	**215,859**	**–**	**218,245**
Fair value of collateral	–	–	**–**	80,856	109,182	2,707	**192,745**	**–**	**192,745**

Note:
This excludes other financial assets.

2.1.17. Movements in provisions for impairment

The following table shows movements in provisions for impairment of loans to non-bank customers are as follows (Note 20 in the Annual report 2017.

MOVEMENTS IN PROVISIONS FOR IMPAIMENT OF LOANS TO NON-BANK CUSTOMERS ARE AS FOLLOWS:

		Abanka			Group		
	Note	**Corporate entities**	**Retail custo-mers**	**Total**	**Corporate entities**	**Retail custo-mers**	**Total**
As at 1 January 2017		**219,398**	**18,590**	**237,988**	**225,160**	**22,918**	**248,078**
Other adjustments		–	–	–	(2,134)	(1,346)	(3,480)
Provision for impairment	16	(2,996)	(4,019)	(7,015)	(871)	(4,108)	(4,979)
Transfer to off-balance sheet records, write-offs, sales, debt to equity		(21,315)	(922)	(22,237)	(21,327)	(1,179)	(22,506)
Exchange differences		(78)	(72)	(150)	(78)	(72)	(150)
As at 31 December 2017		**195,009**	**13,577**	**208,586**	**200,750**	**16,213**	**216,963**

All loans were written down to their recoverable amounts.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.2 Market risk

Market risk is the uncertainty that an adverse change in risk factors, including interest rates, exchange rates, credit spreads, prices of financial instruments, commodity prices and other relevant parameters, may unfavourably affect the value of a financial instrument and/or consequently lead to a loss.

The Group monitors its market risk exposure in its trading and banking books. Market risks primarily arise from activities performed in treasury and the investment banking departments. The trading book positions include mainly positions in equity and debt instruments that the Group intends to sell at a profit in the short term. Part of the trading book also consists of financial derivatives that the Group sells to its customers to hedge against interest rate and foreign exchange risk. These positions are closed according to the Group's back-to-back policy. In the reporting period, the trading book on average stood at EUR 0.6 million and decreased by 0.2 million compared to the 2017 average trading volume. The average trading volume in debt securities increased. The banking book positions include positions in debt instruments, foreign exchange instruments and financial derivatives held for asset and liability management purposes of the Group, equity instruments (acquired through collateral foreclosures and/or debt to equity swaps) and strategic positions. On average, in 2018 the banking book amounted to EUR 1,104 million and decreased by 153 million compared to 2017 average, mainly from debt financial instruments.

2.2.1 Market risk management process

The market risk management strategy is based on the Group's market risk-bearing capacity, the existing and expected market conditions, realised and projected financial data, regulations in force and the existing risk management systems. In the reporting period, the Group traded in debt financial instruments on a limited scale, while trading in equity financial instruments for own account was not allowed. The Group's trading in derivative financial instruments is based on a policy of back-to-back trading and the involvement of counterparties with higher credit ratings. Such trades are concluded mostly to hedge against financial risks.

The purpose of **the market risk management process** is to minimise losses from positions in trading and banking books. Simultaneously, it takes into account business policies, balance sheet structure, capital adequacy and opportunities in capital markets. The Group aspires to achieve the most favourable ratio between generated return and assumed risk and it manages market risk pursuant to the Market Risk Policy of the Group.

The market risk management process comprises:
- procedures of market risk identification, measurement/assessment, monitoring, control, and
- internal reporting on market risk.

Identification procedures are used to define existing and potential risks that arise from trading and banking book positions. Risks and a risk management process must be defined before launching new services or entering new markets. Every year, the Group develops the policy on the management of debt securities in the banking book, which includes the purpose, objectives and limitations of management, as well as potential risks and their management method, which is approved by the Risk Management and Asset-Liability Committee and/or the Management Board. The Group also prepares the investment and trading policy, which defines the target annual volume and structure of trading (the trading book) and operations (banking book) with financial instruments, clients and a financial impact assessment of performing this activity.

The system of limits for trading in financial instruments allows market risk appetite to be kept at low levels. This system also requires investing in highly liquid positions whilst maintaining an adequate risk diversification. The Risk Management Department sets a limit system primarily based on the Group's market risk appetite and capital adequacy. The limit system includes credit and position limits, stop loss limits, market rates compliance limits and limits per single authorised person.

The Group has also established a system of limits for debt financial instruments in the banking book through which it implements its policy of investing in bonds of high credit quality pledgeable as collateral to the European Central Bank, while following the goal of credit diversification and maximum loss limitation.

The structure and organisation of appropriate functions for market risk management is the responsibility of the Management Board and senior management.

NOTES TO THE FINANCIAL STATEMENTS (continued)

The competencies and responsibilities are clearly delimited between trading units, the back office, the middle office and the Risk Monitoring Department, which is organisationally independent of the units that assume market risk.

The extent and features of internal reporting: The Risk Monitoring Department is responsible for the daily calculating of exposures from financial instruments in trading and in the banking book and reporting to the Management Board, senior management and trading units. Quarterly reports on market risk exposure, the utilisation of limits, are presented to the Management Board. The Supervisory Board discusses and reviews a report on the Group's exposure to various types of risks, including market risk, on at least a quarterly basis.

2.2.1.1 Market risk measurement techniques

Market risk measurement techniques comprise risk analyses and validation. This includes assessing the possible frequency of a potential event and the size of its consequences. Market risk is regularly measured by:
- the Value-at-Risk method (i.e. VaR);
- stress testing;
- sensitivity analysis and
- calculating market risk capital requirements, using the standardised approach.

The Group is aware of the limitations of the VaR method in cases of extreme market conditions, which is why the Group performs stress testing as a supplement to VaR. Stress testing assesses potential impacts of extraordinary, yet plausible, events in financial markets on the value of financial instruments. The Group designs stress test scenarios for interest rate-sensitive financial instruments in the trading book, for financial instruments sensitive to price developments in the capital markets and for debt securities in the banking book, by taking into account the forecasts of macroeconomic indicators and the forecasts of interest rate and credit spread movements.

Market risk is also measured with sensitivity analyses to determine the impact of changes in different risk factors and their influence on the Group's profit and equity levels.

2.2.1.2 Market risk mitigation

An adequate limit system, in line with the conservative market risk policy, is the basic tool of effective risk management. For the purpose of **hedging and reducing market risk,** a risk weighted assets limit, a system of trading limits and a system of limits on the banking book operations with debt financial instruments are in place. The market risk regime is implemented on a daily basis through systems of limits and clear guidelines on responsibilities and competencies in assuming risk.

For the main part of trading in derivative financial instruments, exposures to position risk, interest rate risk and currency risk are reduced by pursuing a back-to-back policy. Market risks are hedged by counter-transactions.

2.2.1.3 VaR of debt securities

Value-at-risk assessment (VaR assessment) is a quantitative measure used for assessing potential loss in the value of positions caused by adverse risk factor changes over a given future period at a given confidence level. The Group calculates value-at-risk (VaR) by applying the historical simulation approach. The model assumes the following:
- a 10-day holding period – meaning that within 10 days all the positions included in the calculation can be liquidated, i.e. sold off. This assumption does not necessarily always hold true for all positions, i.e. not in a period of general illiquidity of financial markets. Expanding the daily VaR to a longer period is based on a static portfolio assumption;
- a 1-year observation period – meaning that the latest year should sufficiently reflect the market situation changes which influence the business of the Group. In fact, historical data do not necessarily represent a good indicator of potential future risk factors. This is especially true in periods of extreme market conditions;
- a 99% level of confidence – meaning that on any one day of one hundred trading days the Group would suffer a loss from trading activity exceeding the calculated value. The amount of such excessive losses cannot be measured with VaR.

Measuring VaR shows that the Group's potential loss on one day out of one hundred trading days will at least be equal to the calculated VaR on an individual trading day, under the assumption that positions can be sold over the following 10-day period.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

In 2018 Slovenia witnessed stable macroeconomic conditions and high volatility of major global stock indices. The yield-to-maturity on the Slovene ten-year government bond was 0.99% as at the year-end. The annual growth of stock indices on the Ljubljana Stock Exchange was over 4%.

The Group's market risk appetite remained low. VaR went down due to less volatile bond markets. The Group's market risk exposure was carefully managed through a system of exposure limits.

The following table presents the VaR value of debt securities.

VaR OF DEBT SECURITIES

2018	As at 31 December	Average	Maximum	Minimum
VaR of debt securities	**3,897**	4,333	5,971	3,861

2017	As at 31 December	Average	Maximum	Minimum
VaR of debt securities	5,098	3,594	5,098	2,251

In 2018, most of the potential loss, using a value-at-risk model, resulted from a debt securities portfolio of the banking book**.** At the end of the reported year, the Group estimated with 99% probability that it would lose no more than EUR 3.9 million over the following ten days.

2.2.1.4 Sensitivity analyses

The Group uses sensitivity analyses to measure the impact of changes in various factors on market risk.

The sensitivity analysis of equity securities portfolio reflects the impact of changes in risk factors on the value of the position, while showing the impact of changes in profit or loss and equity. The methodology for determining potential changes in risk factors is based on expectations concerning their movement in the next calendar year. When defining the expected changes in the equity indices, the Group uses internal assessments made by analysts, based on the trend in stock market indices.

The table below shows the sensitivity analysis of equity securities.

SENSITIVITY ANALYSES OF EQUITY SECURITES

(Note 19 and 22)

As at 31 December 2018

Equity securities	Carrying amount	Effect on result of income statement	Effect on equity
Equity securities, held for trading (measured at fair value through profit or loss)	224	56	–
Equity securities, at fair value through other comprehensive income	15,304	–	3,826
Total	**15,528**	**56**	**3,826**

As at 31 December 2017

Equity securities	Carrying amount	Effect on result of income statement	Effect on equity
Equity securites held for trading	217	54	–
Avaliable-for-sale equity securites	17,776	–	4,444
Total	**17,993**	**54**	**4,444**

NOTES TO THE FINANCIAL STATEMENTS (continued)

Taking into account a 25% lower value of equity securities portfolio, as at the reporting date, 3,826 thousand lower equity would be disclosed but the impact on total loss would be minimal. Due to a decrease in equity securities resulting from lower share prices, the decrease would have been lower by 14% compared to 31 December 2017.

The impact of interest rate changes on net interest income and economic value of capital based on the sensitivity analysis is shown in Section 2.2.3.2.

2.2.2 Foreign exchange risk

Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

2.2.2.1 Foreign exchange risk management process

The foreign exchange risk strategy focuses on risk exposure in accordance with set limits and the Group's risk capacity in view of its income and capital adequacy. Foreign exchange risk is identified, measured, controlled and monitored in line with the Group's established foreign exchange risk management policy. **The foreign exchange risk management process** is based on the procedures for identifying, measuring, monitoring and managing foreign exchange risk and includes internal reporting.

The structure and organisation of appropriate functions for foreign exchange risk management are set out in the relevant policy. The adequacy of the strategy, policies and limit system of foreign exchange risk management is monitored by the Risk Management and Asset-Liability Committee. The implementation of the relevant policy is monitored and controlled by the Risk Management and Asset-Liability Committee; foreign exchange risk management is the responsibility of the Assets and Liabilities Management Department, whereas the Treasury Department and other divisions are in charge of the operationalisation of policies and guidelines.

The extent and features of internal reporting: it is an established practice to produce daily reports on foreign exchange exposures, including daily calculations of maximum potential losses arising from net foreign exchange positions. Regular monthly reports on foreign exchange exposures are also produced for the Risk Management and Assets-Liability Committee. The Supervisory Board quarterly discusses and reviews a report on a Group's exposure to various types of risks, including foreign exchange risk.

The foreign exchange measurement system covers the daily monitoring of net foreign exchange positions per currency and currency groups, as well as the daily calculation of maximum loss limits associated with foreign exchange risk by using the Value-at-Risk method. Foreign exchange risk is measured and assessed in accordance with internal methodology. This defines the stress testing used by the Group to evaluate potential losses resulting from foreign exchange rate fluctuations.

The Group **hedges and reduces foreign exchange rate risk,** since fluctuations in the prevailing foreign currency exchange rates have an impact on its financial position and cash flows. In 2018, the gaps between foreign currency inflows and outflows, which mostly arose from payment transactions, were managed by arbitrage. These exposures associated with financial instruments in foreign currencies were low and well within the set limits.

The following table presents the Group's foreign exchange risk exposure and includes the Group's financial instruments at their carrying amounts by currency.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

CONCENTRATION OF CURRENCY RISK: ON- AND OFF-BALANCE SHEET FINANCIAL INSTRUMENTS

As at 31 December 2018

		EUR	USD	CHF	Other	Total
	Financial assets					
1	Cash, cash balances with the central bank and other demand deposits with banks	482,984	14,019	18,533	22,698	**538,234**
2	Financial assets held for trading	3,138	565	–	134	**3,837**
3	Non-trading financial assets mandatorily at fair value through profit or loss	36,587	–	–	–	**36,587**
4	Financial assets at fair value through other comprehensive income	149,248	14,218	–	–	**163,466**
5	Financial assets at amortised cost	2,861,849	47,963	8,345	7	**2,918,164**
	– debt securities	916,118	30,216	–	–	**946,334**
	– loans to banks	19,566	11,219	–	–	**30,785**
	– loans to non-bank customers	1,913,479	6,515	8,345	–	**1,928,339**
	– other financial assets	12,686	13	–	7	**12,706**
	Total financial assets	**3,533,806**	**76,765**	**26,878**	**22,839**	**3,660,288**
	Financial liabilities					
1	Financial liabilities held for trading	2,395	490	–	159	**3,044**
2	Financial liabilities designated at fair value through profit or loss	2,282	–	–	–	**2,282**
3	Financial liabilities at amortised cost	2,966,870	75,357	27,150	19,675	**3,089,052**
	– deposits from banks and the central bank	7,315	5,025	1,619	2,376	**16,335**
	– deposits from non-bank customers	2,821,718	70,024	25,515	17,190	**2,934,447**
	– loans from banks and the central bank	102,788	–	–	–	**102,788**
	– loans from non-bank customers	5	–	–	–	**5**
	– debt securities issued	13,644	–	–	–	**13,644**
	– other financial liabilities	21,400	308	16	109	**21,833**
	Total financial liabilities	**2,971,547**	**75,847**	**27,150**	**19,834**	**3,094,378**
	Net on-balance sheet position	**562,259**	**918**	**(272)**	**3,005**	**565,910**
	Loan commitments	**423,904**	**2,774**	**–**	**4,564**	**431,242**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

CONCENTRATION OF CURRENCY RISK: ON- AND OFF- BALANCE SHEET FINANCIAL INSTRUMENTS

As at 31 December 2017

		EUR	USD	CHF	Other	Total
	Financial assets					
1	Cash, cash balances with the central bank and other demand deposits with banks	360,516	10,765	12,820	28,066	**412,167**
2	Financial assets held for trading	2,674	239	–	135	**3,048**
3	Financial assets, designated at fair value through profit or loss	–	–	–	–	**–**
4	Avaliable-for-sale financial assets	1,052,805	37,883	–	2	**1,090,690**
5	Loans	1,994,049	44,785	9,505	3,783	**2,052,122**
	– loans to banks	15,134	41,839	–	3,772	**60,745**
	– loans to non-bank customers	1,955,020	2,935	9,505	–	**1,967,460**
	– other financial assets	23,895	11	–	11	**23,917**
6	Held-to-maturity investments	15,408	–	–	–	**15,408**
	Total financial assets	**3,425,452**	**93,672**	**22,325**	**31,986**	**3,573,435**
	Financial liabilities					
1	Financial liabilities held for trading	2,123	250	–	119	**2,492**
2	Financial liabilities at amortised cost	2,877,474	76,915	22,624	31,960	**3,008,973**
	– deposits from banks and the central bank	7,827	12,042	1,609	2,765	**24,243**
	– deposits from non-bank customers	2,741,641	63,822	20,960	29,120	**2,855,543**
	– loans from banks and the central bank	89,011	–	–	–	**89,011**
	– loans from non-bank customers	483	–	–	–	**483**
	– debt securities issued	13,021	–	–	–	**13,021**
	– other financial liabilities	25,491	1,051	55	75	**26,672**
	Total financial liabilities	**2,879,597**	**77,165**	**22,624**	**32,079**	**3,011,465**
	Net on-balance sheet position	**545,855**	**16,507**	**(299)**	**(93)**	**561,970**
	Loan commitments	**359,682**	**1,143**	**–**	**5,213**	**366,038**

2.2.2.2 Value-at-risk (VaR) of net foreign exchange position

The table below shows Value-at-Risk (VaR) of net foreign exchange positions. Calculations are based on a historical simulation in a 1-year period, at a 99% confidence level and with a 10-day holding period.

VAR OF NET FOREIGN EXCHANGE POSITION

2018	As at 31. December	Average	Maximum	Minimum
foreign currencies risk	**24**	22	46	7

2017	As at 31. December	Average	Maximum	Minimum
foreign currencies risk	**26**	17	92	5

The Group's exposure to foreign exchange risk was minimal. As at 31 December 2018, the Group estimated with 99% probability that it would lose no more than EUR 24 thousand over the following ten days.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.2.3 Interest rate risk

Interest rate risk is the risk arising from the exposure of the Group's financial position to unfavourable changes in interest rate levels in the market. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on fair value risk and cash flow risk. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate due to changes in market interest rates. As a consequence of these changes, interest margins and the Group's income also change.

Interest rate risk management is defined by the adopted risk appetite framework, which includes the strategy, policies and risk appetite, the limit system and risk management processes.

Identification and measurement of interest rate risk is defined by the adopted Methodology for interest rate risk identification and measurement based on the general Basel standards for interest rate risk management in the banking book and EBA guidelines on interest rate risk management arising from non-trading activities. With this methodology, the Group defines a set of methods for identifying and measuring interest rate risk, assumptions for identifying and measuring interest rate risk and the scenarios for measuring the interest rate sensitivity of the Group.

In 2018, the Group developed a prepayment model, distinguishing between interest and liquidity prepayments. The results of the prepayment model are included in interest rate risk measurement.

2.2.3.1 Interest rate risk management process

The Group performs an efficient **interest rate risk management process,** which ensures that the risk remains at an acceptable level. Interest rate risk is identified, assessed and monitored or controlled in line with the established risk appetite framework. The interest rate risk management process includes interest rate risk management procedures at efficient internal reporting.

In accordance with the risk appetite framework, the Group has limited the extent of interest rate risk by setting up a limit system and by defining the amount of required internal capital. The Group monitors interest risk through assets and liabilities management in terms of their maturity, amount and interest rate setting method and through the application of derivative financial instruments.

In the context of separating the roles and responsibilities in the interest rate risk management process, the Risk Management and Asset-Liability Committee is responsible for the adequacy of the strategy, policy and limit system and for monitoring and supervising the implementation of the adopted policy. The Asset and Liability Management Department is responsible for the management of interest rate risk, while the operational implementation of policies is carried out by commercial departments and the Financial Markets Division.

The interest rate risk in the banking book is measured, monitored and reported on a monthly basis. The level of exposure to interest rate risk is monthly discussed by the Risk Management and Asset-Liability Committee, whilst quarterly Risk reports are submitted to the Supervisory Board. As required by its **internal reporting**, the Group monitors interest rate risk arising from trading in the framework of global market risk control and uses the Value-at-Risk method, stress testing, and sensitivity analysis to measure it.

Interest rate risk, arising from mismatches in the banking book, **is measured** by means of gap analysis. Gap analysis comprises aggregating cash flows into different maturity buckets, categorised by the earlier of contractual re-pricing or maturity dates. The Group classifies non-maturity items in accordance with internal assumptions and models. With regard to non-maturity deposits, which include demand deposits and savings accounts, the Group additionally determines the share of core non-maturity deposits, with respect to which there is a low probability of changes in interest rates even in the event of significant changes in market interest rates. The core non-maturity deposits are evenly distributed to time buckets up to a maximum of 10 years, while non-core deposits are assumed to have immediate maturity.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

The Group takes on exposure to the effects of interest rate fluctuations. It is therefore important for the Group to measure its interest rate sensitivity and manage its assets and liabilities in accordance therewith. The Group regularly calculates the effect of interest rate changes on the economic value of equity and net interest income. Several stress scenarios were designed for the measurement of interest rate sensitivity, in which the Group takes into account its risk profile, including the definition of the parameters used in the ICAAP, historical data on individual scenario variables and regulatory prescribed scenarios. Stress testing is used for determining the interest rate position of the Bank, interest rate risk management and ensuring compliance with the defined risk appetite.

The Group's exposure to interest rate risk was reduced by closing out interest rate positions by individual time buckets. The following table summarises the Group's exposure to interest rate risk. It includes the Group's financial instruments at carrying amounts categorised by the earlier of contractual re-pricing or maturity dates.

In 2018, the Group developed a prepayment model. The results of the prepayment model were included in the measurement of interest rate risk concentration. Prepayments are taken into account for loans to corporate entities and retail customers. The table below shows the impact of prepayments on the level of open interest rate gaps for 2018.

CONCENTRATION OF INTEREST RATE RISK

As at 31. December 2018

		Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
	Interest-sensitive assets						
1	Cash, cash balances with the central bank and other demand deposits with banks	494,641	–	–	–	–	**494,641**
2	Non-trading financial assets mandatorily at fair value through profit or loss	–	21,817	–	–	132	**21,949**
3	Financial assets at fair value through other comprehensive income	1,000	38,915	9,750	74,430	2,000	**126,095**
4	Financial assets at amortised cost	276,063	500,978	1,113,107	720,213	228,252	**2,838,613**
	– debt securities	10,000	95,188	73,946	559,888	165,389	**904,411**
	– loans to banks	25,299	–	–	5,451	–	**30,750**
	– loans to non-bank customers	240,764	405,790	1,039,161	154,874	62,863	**1,903,452**
	Total interest-sensitive assets	**771,704**	**561,710**	**1,122,857**	**794,643**	**230,384**	**3,481,298**
	Interest-sensitive liabilities						
1	Financial liabilities at amortised cost	1,195,928	595,150	428,882	433,737	411,717	**3,065,414**
	– deposits from banks and the central bank	16,330	–	–	–	–	**16,330**
	– deposits from non-bank customers	1,177,419	560,143	370,969	412,453	410,692	**2,931,676**
	– loans from banks and the central bank	1,079	35,003	57,895	7,944	948	**102,869**
	– debt securities issued	–	–	–	13,246	–	**13,246**
	– other financial liabilities	1,100	4	18	94	77	**1,293**
	Total interest-sensitive liabilities	**1,195,928**	**595,150**	**428,882**	**433,737**	**411,717**	**3,065,414**
	Interest rate sensitivity gap	**(424,224)**	**(33,440)**	**693,975**	**360,906**	**(181,333)**	
	Interest rate sensitivity gap excluding prepayments	(437,226)	(50,236)	699,910	355,120	(151,684)	

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

CONCENTRATION OF INTEREST RATE RISK

A at 31. December 2017

		Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
	Interest-sensitive assets						
1	Cash, cash balances with the central bank and other demand deposits with banks	373,455	–	–	–	–	**373,455**
2	Available-for-sale financial assets	19,257	35,392	82,178	645,184	177,514	**959,525**
3	Loans	309,355	409,557	1,076,765	114,190	64,442	**1,974,309**
	– loans to banks	58,348	3,258	–	2,348	–	**63,954**
	– loans to non-bank customers	251,007	406,299	1,076,765	111,842	64,442	**1,910,355**
4	Held-to-maturity investments	–	5,000	–	10,000	–	**15,000**
	Total interest-sensitive assets	**702,067**	**449,949**	**1,158,943**	**769,374**	**241,956**	**3,322,289**
	Interest-sensitive liabilities						
1	Financial liabilities designated at fair value through profit or loss						
2	Financial liabilities at amortised cost	1,186,834	530,473	401,627	467,198	393,677	**2,979,809**
	– deposits from banks and the central bank	23,739	500	–	–	–	**24,239**
	– deposits from non-bank customers	1,158,864	486,516	369,620	446,516	390,663	**2,852,179**
	– loans from banks and the central bank	2,848	43,453	31,989	7,944	2,934	**89,168**
	– debt securities issued	–	–	–	12,642	–	**12,642**
	– other financial liabilities	1,383	4	18	96	80	**1,581**
	Total interest-sensitive liabilities	**1,186,834**	**530,473**	**401,627**	**467,198**	**393,677**	**2,979,809**
	Interest rate sensitivity gap	**(484,767)**	**(80,524)**	**757,316**	**302,176**	**(151,721)**	

Note:
Foreign exchange derivatives are not included.

The tables include the following:
- debt securities at face value (not at market value or amortised cost);
- loans after taking into account impairments in relation to the first re-defining of interest rates or contractual maturity;
- principal amounts of loans and deposit (excluding interest, outstanding commissions and initial recognition costs).

2.2.3.2 Interest rate sensitivity analyses

The impact of interest rate changes on net interest income and the economic value of capital arising from the presented existing interest sensitivity gaps is shown in the table below.

The economic value of equity is calculated as a sum of discounted cash flow of individual interest-sensitive assets and interest-sensitive liabilities of the banking book. The defined scenarios of yield curve movements are used to calculate a new economic value and, consequently, the effect of interest rate fluctuations on the economic value of equity.

The impact of interest rate changes on interest income is calculated for a 1-year period. Interest rate changes have an impact on the interest income and expense dependant on a flexible interest rate over a period when the latter is not yet defined (i.e. from the date the interest rate is redefined). The calculation is based on the static balance sheet, which includes reinvesting and refinancing.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

INTEREST RATE SENSITIVITY ANALYSES

	As at 31 December 2018		As at 31 December 2017	
	Effect on interest rate income	Effect on the economic value of equity	Effect on interest rate income	Effect on the economic value of equity
+200 basis points	(5,150)	(8,158)	(5,003)	(7,177)
+50 basis points	(1,823)	(2,009)	(2,079)	(1,697)
–50 basis points	(2,150)	2,006	(2,093)	1,638
–200 basis points	(10,227)	7,955	(9,890)	6,089

If a market interest rate **increase** of 200 basis points was taken into account, the economic value of equity in the reporting period would decrease by EUR 8,158 thousand based on the data, while net interest income would fall by EUR 5,150 thousand. If a market interest rate **decrease** of 200 basis points was taken into account, the economic value of equity would increase by EUR 7,955 thousand based on the data. The Group also assesses the impact on the economic value of capital in such a way that, when making downward adjustments to interest rates, it is considered that the interest rates used for discounting are not negative. When the interest rates are shifted by 200 basis points, taking into account that discount rates are not negative, the economic value of capital would be reduced by EUR 3,064 thousand, while the economic value of capital decreased by EUR 3,962 thousand at a downward movement of 50 basis points.

According to the data as at the 2018 year-end, if market interest rates increased by 200 basis points, net interest income would be reduced by EUR 5,150 thousand over a one-year period, which is the result of interest expenses arising from non-core non-maturity deposits for which immediate maturity is assumed. If market interest rates decreased by 200 basis points, net interest income would be reduced by EUR 10,227 thousand over a one-year period. The reduction in net interest income in the event of a decrease in interest rates is a consequence of the assumption that, when interest rates fall, the interest rate for retail customers and corporate entities cannot be negative.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.2.3.3 Interest rates by currency

The Group monitors interest rates by currency for financial instruments. Average interest rates are shown in the following table.

AVERAGE INTEREST RATES BY CURRENCY FOR FINANCIAL INSTRUMENTS

		2018			2017		
		EUR	USD	CHF	EUR	USD	CHF
	Financial assets						
1	Cash, cash balances with the central bank and other demand deposits with banks	(0.32%)	1.54%	0.00%	(0.33%)	0.00%	0.00%
2	Non-trading financial assets mandatorily at fair value through profit or loss	3.21%	–	–	–	–	–
3	Financial assets at fair value through other comprehensive income	0.39%	2.44%	–	–	–	–
	Available-for-sale financial assets				1.03%	2.51%	–
4	Financial assets at amortised cost	1.89%	3.12%	1.38%	2.26%	1.99%	1.41%
	– debt securities	0.96%	3.23%	–	–	–	–
	– loans to banks	(0.23%)	1.86%	–	(0.12%)	2.00%	–
	– loans to non-bank customers	2.34%	4.83%	1.38%	2.29%	1.82%	1.41%
	Held-to-maturity investments				4.53%	–	–
	Financial liabilities						
1	Financial liabilities at amortised cost	0.12%	0.08%	(0.05%)	0.15%	0.10%	(0.06%)
	– deposits from banks and the central bank	(0.41%)	0.81%	(1.01%)	(0.41%)	0.42%	(1.01%)
	– deposits from non-bank customers	0.08%	0.03%	0.01%	0.10%	0.03%	0.01%
	– loans from banks and the central bank	0.71%	–	–	0.73%	–	–
	– debt securities issued	5.95%	–	–	5.95%	–	–
	– other financial liabilities	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

2.3 Liquidity risk

Liquidity risk is the risk that includes the risk of failing to provide liquidity sources, market liquidity risk and asset encumbrance risk.

The risk of failing to provide liquidity sources is the risk that the Group might not be able to meet its payment obligations when due, and/or that as a consequence of its inability to provide sufficient funding to meet payment obligations by the due date, the Group might be forced to provide the required funding at costs significantly above usual.

Market liquidity risk is the risk of loss arising from the impossibility of selling or replacing positions (in financial instruments) in a short period of time without this bearing a significant impact on the market price, due to insufficient market depth, market imbalances or other reasons.

The asset encumbrance risk is the risk arising from the encumbrance of the Group's assets and means an increase in the risk of providing liquidity sources and market liquidity risk due to fewer possibilities of providing liquidity sources and disposing of assets. Any decrease in the value of encumbered assets as a result of market factors and the related demand for additional coverage further increases this risk.

2.3.1 Liquidity risk management process

The liquidity risk management strategy is based on prudent and stable operations, and includes the careful management of assets and liabilities (both on and off-balance sheet) as well as a balanced borrowing strategy, which enables the Group to meet its financial obligations as they fall due.

NOTES TO THE FINANCIAL STATEMENTS (continued)

The Group provides for the appropriate volume and structure of the liquidity buffer, taking into account the risk related to procuring liquidity sources, market liquidity risk and asset encumbrance risk.

The liquidity risk management process follows the adopted risk appetite framework, which involves the strategy, policies and risk appetite, the limit system and risk management processes. The Group identifies, measures and monitors or controls liquidity risk in line with the adopted risk appetite framework. The liquidity risk management process includes the liquidity risk management procedures at efficient internal reporting.

The liquidity risk management process consists of:

- integrated planning and monitoring future cash flows, which include day-to-day funding, with a view to ensuring that requirements are met and sources are replenished as they mature;
- intraday cash flow planning and monitoring;
- maintaining an appropriate volume of the liquidity buffer, i.e. a portfolio of highly liquid assets that can be easily liquidated and serve as protection against unforeseen cash flow developments;
- assessing market liquidity risk;
- monitoring and calculating liquidity indicators in line with the requirements of the Bank and regulatory requirements;
- monitoring the diversity of financing sources and the profile of outstanding liabilities;
- running liquidity management scenarios for the normal course of business and for extraordinary liquidity requirements (stress scenarios);
- monitoring the liquidity position of the banking system and the national economy;
- adopting adequate liquidity policies in view of the given circumstances; and
- establishing an adequate relationship between the costs, benefits and risks involved in providing liquidity.

The structure and organisation of appropriate functions for liquidity risk management are set out in the relevant policy. The adequacy of the strategy, policies and limit system of liquidity risk management is monitored by the Risk Management and Asset-Liability Committee. The implementation of the relevant policy is controlled by the Risk Management and Asset-Liability Committee and the Liquidity Commission, liquidity risk management lies within the competence of the Treasury Department and the Assets and Liabilities Management Department, whilst the Financial markets division and other divisions are in charge of the operationalisation of policies and guidelines.

Internal reporting takes the form of cash flow measurement and projections for the next day, week and month, as these are key periods for operational liquidity management. Furthermore, liquidity measurements for longer periods are carried out to monitor liquidity exposure in those periods, and to manage stress liquidity situation. The starting point for those projections is the contractual maturity of financial liabilities, the expected recovery date of financial assets, the anticipated early repayment of loans and the assessment of the expected movement of unstable sources. Liquidity risk exposure is followed and controlled by the Liquidity Committee on a daily basis and by the Risk Management and Asset-Liability Committee on a monthly basis. The Supervisory Board discusses a quarterly report on the Group's exposure to various types of risks, including liquidity risk.

2.3.1.1 Liquidity risk measurement

The procedures for **measuring liquidity risk** include quality and quantity assessments for risk measurement. The Group has developed its own methods for establishing, measuring, managing and monitoring liquidity, which enable matching of the actual and potential liquid funds to the actual and potential use of such funds over certain time periods. The Group evaluates the adequacy of liquid assets and their availability. When an assessment of liquidity is made, the Group primarily takes into account the possibility of obtaining liquidity in the short run on the basis of these funds. The Group also monitors the distribution of costs, benefits and risks involved in providing liquidity. An internal methodology has been developed for this purpose, which covers important assets and liability items, off-balance items and all liquidity maintenance costs. This methodology is regularly upgraded by the Group.

The Group also regularly upgrades its methodology for assessing expected cash flows. The discrepancy between the expected and contractual cash flows is evaluated using assumptions, which are based on historical data and model estimates. The Group regularly verifies the adequacy and accuracy of these assumptions.

NOTES TO THE FINANCIAL STATEMENTS (continued)

The Group implements the internal liquidity adequacy assessment process (ILAAP). The key aim of the ILAAP process is ensuring that the Group has sufficient short-term and mid-term liquidity available both under normal and stress conditions. The ILAAP process includes the assessment of liquidity requirements and the assessment of available liquidity. The Group regularly checks its liquidity adequacy, both within the framework of the ordinary course of business and in the context of the business plan for the future planning period. The verification of liquidity adequacy also includes liquidity stress testing for pre-defined stress situations of varying severity.

2.3.1.2 Liquidity risk mitigation

With the aim **of hedging and reducing liquidity risk**, the Group implements prudent assets and liabilities management, which is the foundation of stable operations; therefore, the following objectives are pursued:

- the ability to fulfil all obligations related to balance-sheet and off-balance-sheet outflows in the short term;
- minimizing the costs of maintaining liquidity;
- foreseeing the occurrence of extraordinary liquidity conditions and implementing the adopted action plan for re-establishing appropriate liquidity in the event that such extraordinary conditions materialise.

In order to reduce the liquidity risk, the Group established a limit system, which includes compliance with regulatory requirements and internally defined limits as well as monitoring of target structural liquidity indicators.

For the purpose of liquidity risk hedging, the Group applies a methodology for identifying and measuring liquidity risk and maintains an action plan for the re-establishment of appropriate liquidity. The Group is hedged against liquidity risk by virtue of diligent and effective liquidity buffer management and the availability of adequate sources of funding, which are kept as diverse as possible. The Group also adequately addresses liquidity risk in its Recovery Plan.

In order to monitor the effectiveness of hedging and minimise liquidity risk, the Group regularly assesses its risk capacity in accordance with the established methodology.

2.3.1.3 Liquidity management scenarios in extreme situations

The Group prepares various **liquidity scenarios in extreme situations** with the aim of identifying potential weaknesses and vulnerabilities in its liquidity position. These scenarios assume worsened liquidity conditions due to a weaker financial position of the Group and a diminished reputation domestically and internationally. Moreover, the Group prepares scenarios assuming extreme liquidity situations in domestic and foreign financial markets, reduced confidence in the banking system, and a decline in economic activity.

The Group prepares various liquidity management scenarios also including liquidity risk mitigation measures and uses these scenarios as the basis for testing the assumptions used in decision-making on liquidity-related issues. Based on these scenarios, the Group determines the most appropriate measures for ensuring adequate liquidity, taking into account:

- the baseline scenario: a scenario whose assumptions reflect the continuation of the current direction and conditions of a Group's operations and for which it can be assumed with certainty that they will affect the Group's liquidity in the normal course of business;
- a liquidity stress scenario, in which a liquidity stress situation is unlikely but probable, is a liquidity management scenario, with liquidity, whose assumptions contain important changes in the factors that influence the liquidity of the Group towards the deterioration.

Liquidity stress scenarios are divided into three main groups:

- the scenario adapted to own liquidity position or the idiosyncratic scenario;
- the market scenario is associated with a significant macroeconomic event, a sudden risk change in the financial system or with simultaneous worsening conditions in several markets at the same time;
- the combined scenario, which is based on the combination of the idiosyncratic and market scenarios.

Liquidity stress scenarios are performed for two levels of severity, where the intensity of the liquidity stress situation changes over time. The Group regularly verifies the adequacy and accuracy of the assumptions used in scenarios.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

In 2018, the Group upgraded the definition of assumptions of stress scenarios and the methodology for implementing stress scenarios for liquidity risk. With regard to the development of econometric models, the Group redesigned the models of utilisation of individual off-balance sheet items and developed the loan prepayment model, in which distinction is made between liquidity and interest prepayments. In addition, a recalibration of the risk appetite was carried out together with the limit system for liquidity and critical values for the recovery plan and the contingency plan for the re-establishment of appropriate liquidity, bringing them into line.

Based on the results of liquidity stress tests, the Group determines the overall size and composition of the liquidity buffer.

2.3.1.4 Contingency plan

In order to hedge liquidity risk, procedures are defined for minimising the occurrence of crisis situations that would prevent the Group from duly and promptly discharging its obligations. Early identifying of potential crisis situations is carried out during the daily monitoring of the Group's liquidity position.

The contingency plan for the re-establishment of appropriate liquidity is a catalogue of processes aimed at the early detection of liquidity deficits based on the monitoring of liquidity indicators and other indicators used by the Group to identify potential liquidity issues in due time. The plan also includes a list of situations deemed as examples of liquidity deficits, with the aim of restoring a normal liquidity position of the Group.

2.3.2 Liquidity ratios and structural liquidity indicators

Liquidity ratios determine the ratio of financial assets to financial liabilities according to residual maturity. For this purpose, the following prescribed ratios are calculated and monitored:

- liquidity coverage ratio (LCR), the purpose of which is to provide liquidity in the short term by determining the required volume of highly liquid assets for settling liabilities in times of extraordinary liquidity conditions;
- net stable funding ratio (NSFR), the purpose of which is to provide medium and long-term stable financing for banks' operations by determining the appropriate structure of assets and liabilities relative to maturity;
- the liquidity ratio with a residual maturity of assets and liabilities of up to 30 days (LR1) and the liquidity ratio with a residual maturity of assets and liabilities of up to 180 days (LR2).

The Group calculates the LCR every month and the NSFR on a quarterly basis as at last day of the month as at the last day of the month, and the LR1 and LR2 ratios on a daily basis.

As at the 2018 year-end, all ratios were at high levels and above the limit.

The Group measures liquidity risk also with the survival period indicator, which measures the number of days the Group can survive in a liquidity stress situation. The defined risk appetite value of this indicator may not be less than three months. The survival period of the Group significantly exceeds the predetermined risk appetite of the Group.

LIQUIDITY RATIOS

	Average 2018	As at 31 December 2018	Average 2017	As at 31 December 2017
Liquidity coverage ratio (LCR)	4.14	4.30	4.92	4.43
Net stable funding ratio (NSFR)	1.69	1.74	1.57	1.56
Liquditiy ratio (Maturity up to 30 days)	1.48	1.47	1.57	1.56

The Group also monitored the liquidity situation by continuously calculating structural liquidity indicators. Cash and cash equivalents, reserves held at the central bank, receivables due from banks, securities and loans eligible as collateral for Eurosystem refinancing constitute the Group's liquidity buffer.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

STRUCTURAL LIQUIDITY INDICATORS (%)

	Average 2018	As at 31 December 2018	Average 2017	As at 31 December 2017
Liquidity buffer/total assets	43.5	43.8	43.6	42.4
Liquidity buffer/short-term deposits of the non-banking sector	256.3	252.7	266.2	256.6
Loans to non-banking sector/deposits of the non-banking sector	67.2	66.5	65.4	68.6

2.3.3 Funding approach

The Group keeps its funding sources at an adequate level and appropriately diversifies them by currency, lender/creditor, banking product, and maturity.

2.3.4 Non-derivative cash flows from liabilities based on contractual maturity

The following table shows non-derivative cash flows according to their remaining contractual maturity as at the date of the statement of financial position. On-balance sheet items disclosed in the maturity table represent undiscounted cash flows including future payments. Off-balance sheet items are included in the time bucket containing the earliest date on which loan commitments could be drawn down (according to IFRS7 amendments: B11C(b)), or on which financial guarantees could be called (according to IFRS7 amendments: B11C(c)).

Foreign currency cash flows are converted into euros using the spot exchange rate as at the date of the statement of financial position.

NON-DERIVATIVE CASH FLOWS BASED ON CONTRACTUAL MATURITY

	As at 31 December 2018	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
	Financial liabilities						
1	Financial liabilities designated at fair value through profit or loss	2,282	–	–	–	–	**2,282**
2	Financial liabilities at amortised cost	2,512,954	75,196	320,964	158,563	37,283	**3,104,960**
	– deposits from banks and the central bank	16,334	–	–	–	–	**16,334**
	– deposits from non-bank customers	2,474,069	72,219	308,965	86,952	2,911	**2,945,115**
	– loans from banks and the central bank	894	2,978	11,823	56,922	34,373	**106,990**
	– loans from non-bank customers	–	–	5	–	–	**5**
	– debt securities issued	–	–	170	14,689	–	**14,859**
	– other financial liabilities	21,656	–	–	–	–	**21,656**
	Total financial liabilities	**2,515,235**	**75,196**	**320,964**	**158,563**	**37,283**	**3,107,241**
	Loan commitments and financial guarantees	**479,653**	–	–	–	–	**479,653**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

	As at 31 December 2017	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
	Financial liabilities						
1	Financial liabilities at amortised cost	2,359,148	109,108	317,391	189,459	33,867	**3,008,973**
	– deposits from banks and the central bank	23,741	502	–	–	–	**24,243**
	– deposits from non-bank customers	2,307,894	103,826	306,862	133,537	3,425	**2,855,544**
	– loans from banks and the central bank	860	4,770	10,388	43,034	29,959	**89,011**
	– loans from non-bank customers	–	–	–	–	483	**482**
	– debt securities issued	–	–	141	12,880	–	**13,021**
	– other financial liabilities	26,654	10	–	8	–	**26,672**
	Total financial liabilities	**2,359,149**	**109,108**	**317,391**	**189,459**	**33,867**	**3,008,973**
	Loan commitments and financial guarantees	**414,695**	–	–	–	–	**414,695**

The largest part of liquidity reserves held by the Group in 2018 to meet balance sheet and off-balance sheet obligations was composed of debt securities, whilst the second largest liquidity reserve item as at the reporting date was cash and cash equivalents. The Group did not have any commitments and contingencies that would exceed the contractually determined amount of obligations.

2.3.5 Cash flows of financial instruments based on expected maturity

The following table shows on- and off-balance cash flows according to their expected maturity as at the date of the statement of financial position including anticipated interests.

Expected cash flows from on-balance sheet items for individually assessed large loans include expected cash flows instead of contractually agreed ones. Demand deposits and saving accounts are classified into different time buckets according to an internal methodology. They are divided into stable and unstable sources, using a statistical method based on a multi-annual time series. Stable sources are subsequently classified into different long-term time buckets. Expected cash flows from off-balance sheet items are classified into different time buckets according to an internal methodology based on historical data.

The Group takes measures to maintain an appropriate liquidity position. These measures include maintaining the appropriate volume and quality of the liquidity buffer, activities for raising long-term funds, maturity matching of assets and liabilities and ongoing adjustments of the interest rate policy.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

CASH FLOWS OF FINANCIAL INSTRUMENTS BASED ON EXPECTED MATURITY

	As at 31 December 2018	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
	Financial assets						
1	Cash, cash balances with the central bank and other demand deposits with banks	476,480	–	–	61,800	–	**538,281**
2	Financial assets held for trading	442	9	139	1,852	1,396	**3,837**
3	Non-trading financial assets mandatorily at fair value through profit or loss	53	322	2,037	33,029	132	**35,573**
4	Financial assets at fair value through other comprehensive income	1,467	40,607	11,358	80,156	29,902	**163,489**
5	Financial assets at amortised cost	147,777	167,985	406,057	1,645,466	820,906	**3,188,191**
	– debt securities	16,288	100,268	83,812	601,950	170,742	**973,059**
	– loans to banks	19,699	(2)	1,119	9,447	511	**30,774**
	– loans to non-bank customers	99,256	67,720	321,127	1,034,069	649,653	**2,171,824**
	– other financial assets	12,534	–	–	–	–	**12,534**
	Total financial assets	**626,219**	**208,923**	**419,591**	**1,822,303**	**852,336**	**3,929,371**
	Financial liabilities						
1	Financial liabilities held for trading	427	45	125	1,616	827	**3,041**
2	Financial liabilities designated at fair value through profit or loss	2,282	–	–	–	–	**2,282**
3	Financial liabilities at amortised cost	244,592	117,787	491,749	1,070,878	1,179,955	**3,104,960**
	– deposits from banks and the central bank	16,334	–	–	–	–	**16,334**
	– deposits from non-bank customers	206,841	114,790	479,664	998,809	1,145,010	**2,945,115**
	– loans from banks and the central bank	894	2,978	11,823	56,922	34,373	**106,990**
	– loans from non-bank customers	–	–	5	–	–	**5**
	– debt securities issued	–	–	170	14,689	–	**14,859**
	– other financial liabilities	20,522	19	86	458	572	**21,656**
4	Capital	–	–	–	–	583,407	**583,407**
	Total financial liabilities	**247,300**	**117,832**	**491,874**	**1,072,494**	**1,764,189**	**3,693,689**
	Net liquidity gap	**378,919**	**91,090**	**(72,283)**	**749,809**	**(911,853)**	**235,682**
	Loan commitments and financial guarantees	**65,312**	**15,607**	**40,105**	**–**	**–**	**121,024**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

CASH FLOWS OF FINANCIAL INSTRUMENTS BASED ON EXPECTED MATURITY

	As at 31 December 2017	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
	Financial assets						
1	Cash, cash balances with the central bank and other demand deposits with banks	378,721	–	–	33,447	–	**412,168**
2	Financial assets held for trading	145	152	78	2,321	351	**3,047**
3	Financial assets designated at fair value through profit or loss	–	–	–	–	–	**–**
4	Available-for-sale financial assets	25,604	42,147	93,849	719,023	212,747	**1,093,370**
5	Loans and receivables	173,000	69,566	315,940	1,075,496	645,983	**2,279,985**
	– loans to banks	48,242	3,265	1,131	10,897	517	**64,052**
	– loans to non-bank customers	101,097	66,301	314,809	1,064,598	645,466	**2,192,271**
	– other financial assets	23,661	–	–	–	–	**23,661**
6	Held-to-maturity investments	219	5,419	–	10,875	–	**16,513**
	Total financial assets	**577,689**	**117,284**	**409,867**	**1,841,162**	**859,081**	**3,805,083**
	Financial liabilities						
1	Financial liabilities held for trading	150	149	72	2,065	56	**2,492**
2	Financial liabilities at amortised cost	550,241	146,055	456,622	924,322	949,173	**3,026,413**
	– deposits from banks and the central bank	23,741	502	–	–	–	**24,243**
	– deposits from non-bank customers	499,536	140,530	445,515	864,064	916,912	**2,866,557**
	– loans from banks and the central bank	902	5,000	10,889	45,107	31,403	**93,300**
	– loans from non-bank customers	–	–	–	–	483	**483**
	– debt securities issued	–	–	162	14,843	–	**15,005**
	– other financial liabilities	26,062	22	56	309	375	**26,825**
3	Capital	–	–	–	–	580,283	**580,283**
	Total financial liabilities	**550,391**	**146,204**	**456,694**	**926,387**	**1,529,511**	**3,609,187**
	Net liquidity gap	**27,298**	**(28,920)**	**(46,827)**	**914,775**	**(670,430)**	**195,896**
	Loan commitments and financial guarantees	**44,985**	**15,641**	**46,980**	**–**	**–**	**107,606**

2.3.6 Derivative cash flows

2.3.6.1 Derivatives settled on a net basis

The Group's derivatives that are settled on a net basis include:
- foreign exchange derivatives: over-the-counter (OTC) currency options and
- interest rate derivatives: interest rate swaps and interest rate options.

The following table shows an analysis of the Group's derivative financial instruments with negative fair value, which are settled on a net basis, arranged in groups according to maturity on the basis of the outstanding contractual maturity on the date of the statement of financial position. The amounts disclosed in the table are the contractual undiscounted cash flows.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

DERIVATIVE FINANCIAL INSTRUMENTS WITH A NEGATIVE FAIR VALUE SETTLED ON A NET BASIS

As at 31 December 2018	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
Derivatives held for trading						
– foreign exchange derivatives	–	–	–	–	–	**–**
– interest rate derivatives	(11)	(320)	(166)	(368)	(11)	**(876)**
Total	**(11)**	**(320)**	**(166)**	**(368)**	**(11)**	**(876)**

As at 31 December 2017	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
Derivatives held for trading						
– foreign exchange derivatives	–	–	–	–	–	**–**
– interest rate derivatives	(14)	(323)	(84)	(164)	–	**(585)**
Total	**(14)**	**(323)**	**(84)**	**(164)**	**–**	**(585)**

2.3.6.2 Derivatives settled on a gross basis

The Group's derivatives that are settled on a gross basis include foreign exchange derivatives:
- currency forwards
- currency swaps.

The following table shows an analysis of the Group's derivative financial instruments with a negative fair value settled on a gross basis and arranged in logical groups according to maturity on the basis of the outstanding contractually determined maturity on the date of the statement of financial position. Items shown in the table represent the contractually determined undiscounted cash flows.

DERIVATIVE FINANCIAL INSTRUMENTS WITH A NEGATIVE FAIR VALUE SETTLED ON A GROSS BASIS

As at 31 December 2018	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
Derivatives held for trading						
– foreign exchange derivatives						
– inflows	10,828	2,095	23,495	682	–	**37,100**
– outflows	11,277	2,091	23,770	716	–	**37,854**
Total inflows	**10,828**	**2,095**	**23,495**	**682**	**–**	**37,100**
Total outflows	**11,277**	**2,091**	**23,770**	**716**	**–**	**37,854**

As at 31 December 2017	Up to 1 month	From 1 to 3 months	From 3 to 12 months	From 1 to 5 years	Over 5 years	Total
Derivatives held for trading						
– foreign exchange derivatives						
– inflows	23,545	5,063	4,554	–	–	**33,162**
– outflows	23,667	5,206	4,603	–	–	**33,476**
Total inflows	**23,545**	**5,063**	**4,554**	–	–	**33,162**
Total outflows	**23,667**	**5,206**	**4,603**	–	–	**33,476**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.3.7 Commitments and contingencies

Items referring to potential obligations are presented off-balance sheet. The triggering events for these obligations have not occurred and these facilities are not yet due. Those obligations, for which trigger events have already occurred are presented in the statement of financial position.

a) Loan commitments

The following table shows a summary of the contractually determined values of loan commitments (overdrafts and credit lines, granted undrawn loans, revolving loans) that oblige the Group to provide loans to customers.

b) Guarantees and other financial facilities

The following table also includes guarantees and other financial facilities, arranged according to contractually determined maturity dates.

COMMITMENTS AND CONTINGENCIES

(Note 39)

As at 31 December 2018	Up to 1 year	From 1 to 5 years	Over 5 years	Total
Loan commitments	320,559	17,861	92,822	**431,242**
Guarantees and other financial facilities	167,552	69,337	20,618	**257,507**
– financial guarantees	28,137	18,440	1,834	**48,411**
– performance guarantees	137,658	48,670	17,453	**203,781**
– derivatives	586	1,852	1,172	**3,610**
– other	1,171	375	159	**1,705**
Total	**488,111**	**87,198**	**113,440**	**688,749**

As at 31 December 2017	Up to 1 year	From 1 to 5 years	Over 5 years	Total
Loan commitments	272,060	37,274	56,704	**366,038**
Guarantees and other financial facilities	155,159	65,415	18,779	**239,353**
– financial guarantees	20,911	13,073	1,868	**35,852**
– performance guarantees	133,612	50,021	16,777	**200,410**
– derivatives	360	2,321	134	**2,815**
– other	276	–	–	**276**
Total	**427,219**	**102,689**	**75,483**	**605,391**

Commitments and contingencies are reduced by the provisions for guarantees and commitments, and by the other provisions.

Commitments and contingencies are carried at nominal value; the only exception is derivative financial instruments carried at market value. The counterparty credit risk exposure amounting to EUR 8,940 thousand at the end of 2018 (at the end of 2017: EUR 4,386 thousand) was the sum of the market value (current exposure) and the potential exposure of derivative financial instruments.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.4 Capital management

Capital management comprises monitoring the level of capital, capital adequacy ratios, drafting guidelines for achieving the planned capital adequacy ratios and following the implementation of measures aimed at keeping at least minimum capital adequacy ratios in compliance with the respective business policy of the Group.

The management and supervisory bodies regularly monitor and assess the effectiveness of the capital management system. The Group calculates its regulatory capital and capital adequacy at least quarterly.

The Group's capital must be at least equal the total sum of minimum capital requirements at all times set out in Article 92 of Regulation (EU) No 575/2013, the requirements for the maintenance of capital buffers referred to in Article 128 of Directive (EU) No 2013/36 and the requirements for the provision of adequate internal capital referred to in Article 97 of Directive (EU) No 2013/36.

2.4.1 Regulatory capital and capital adequacy

The regulatory capital of the Group is calculated on the basis of the Group's consolidated financial statements in accordance with the Part Two of Regulation (EU) No 575/2013. The Group's regulatory capital calculation takes into account capital components, prudential filters and deductible items. In calculating the capital adequacy and capital requirements of the Group, the Part Three of Regulation (EU) No 575/2013 is applied.

Regulatory capital includes Tier 1 capital and Tier 2 capital. The Tier 1 capital of the Group consists of the sum of the Common Equity Tier 1 capital and Additional Tier 1 capital of the Group. The Regulation (EU) No. 575/2013 stipulates the application of three ratios:
- a Common Equity Tier 1 capital ratio of at least 4.5%,
- a Tier 1 capital ratio of at least 6% and
- a total capital ratio of at least 8%.

Disclosures related to own funds are laid down in Article 437 of Regulation (EU) No 575/2013 and, with regard to disclosure of own funds set out in the implementing technical standards contained in Commission Implementing Regulation (EU) No 1423/2013.

The following table shows regulatory capital components and capital adequacy ratios.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

REGULATORY CAPITAL AND CAPITAL ADEQUACY

As at 31 December	2018	2017
Paid up capital instruments	151,000	151,000
Share premium	282,459	282,459
Previous years retained earnings	19,190	24,478
Profit or loss eligible	–	–
Accumulated other comprehensive income	3,332	33,283
Other reserves	51,727	47,468
Adjustments to CET1 capital due to prudential filters	(209)	(1,096)
(-) Other intangible assets	(9,073)	(7,427)
(-) Deferred tax assets thar rely on future profitability and do not arise from temporary differences	(8,641)	(7,055)
(-) Excess of deduction from AT1 items over AT1 capital	–	(1,485)
(-) Other transitional adjustments to CET1 capital	–	(17,997)
(-) CET1 capital elements or deductions - other	–	–
Common Equity Tier 1 capital (CET1)	**489,785**	**503,628**
Additional Tier 1 capital (AT1)	**–**	**–**
Tier 1 capital (T1)	**489,785**	**503,628**
Tier 2 capital (T2)	**–**	**–**
Total regulatory capital (for solvency purposes)	**489,785**	**503,628**
Risk weighted exposure amounts for credit risk	1,835,763	1,805,377
Risk exposure amount for position and foreign-exchange risk	590	518
Risk exposure amounts for operational risk	230,369	244,228
Risk exposure amount for credit valuation adjustment	2,160	417
Settlement/delivery risk exposure amount	–	–
Total risk exposure amount	**2,068,883**	**2,050,540**
Common Equity Tier 1 capital ratio	**23.67%**	**24.56%**
Tier 1 capital ratio	**23.67%**	**24.56%**
Total capital ratio	**23.67%**	**24.56%**

The regulatory capital of the Group amounted to EUR 489,785 thousand as at 31 December 2018, which represents a year-on-year decrease of EUR 13,843 thousand. As at the reporting date, the total risk exposure amount stood at EUR 2,068,883 thousand, or EUR 18,343 thousand higher compared to 31 December 2017. The total capital ratio, i.e. capital adequacy, reached 23.67%, which was almost a percentage points lower than at the 2017 year-end. In 2018, regulatory capital was comprised solely of Common Equity Tier 1 capital. As a result, all three prescribed ratios were the same.

In accordance with Article 492(1) of Regulation (EU) No 575/2013, the following own funds requirements shall apply during the period from 1 January 2015 on: a Common Equity Tier 1 capital ratio of a level reaching or exceeding 4.5%; a Tier 1 capital ratio of a level reaching or exceeding 6%; and a total capital ratio of a level reaching or exceeding 8%. As at 31 December 2018, Common Equity Tier 1 capital surplus amounted to EUR 396,686 thousand, Tier 1 capital surplus to EUR 365,652 thousand and total regulatory capital surplus to EUR 324,275 thousand.

As at the reporting date, non-consolidated total capital ratio, Tier 1 capital ratio and Common Equity Tier 1 capital ratio stood at 23.62%.

2.4.1.1. Full harmonisation of own funds items disclosures with audited financial statements

Disclosures related to reconciliation of own funds items to audited financial statements are laid down in Article 437(1)(a) of Regulation (EU) No 575/2013. The disclosure of the elements of own funds according to Article 437(1)(f) of Regulation (EU) No 575/2013, is not relevant, as own funds are calculated on the basis of Regulation (EU) No 575/2013.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

In the first column, the amounts of individual items from the statement of financial position are shown. In the second column the amounts of regulatory capital items calculated on the basis of Regulation (EU) No. 575/2013. In the third column, references to individual items from the disclosure template are shown (the table in Section 2.4.1.3).

RECONCILIATION OF OWN FUNDS ITEMS TO AUDITED FINANCIAL STATEMENTS

As at 31 December 2018	Consolidated audited financial statements items	Own funds items	Own funds disclosure template reference
Assets			
Intangible assets	9,074	(9,073)	8
Tax assets	10,225	(8,641)	
– tax assets	–	–	
– deferred tax assets	10,225	(8,641)	
– deferred tax assets that rely on future profitability and do not arise from temporary differences	8,641	(8,641)	10
– deferred tax assets that rely on future profitability and arise from temporary differences	1,584	–	
Adjustments to CET1 capital due to prudential filters	–	(209)	7
Liabilities			
Equity			
Share capital	151,000	151,000	1
– capital instruments eligible as CET 1 capital	151,000	151,000	1
Share premium	282,459	282,459	1
Accumulated other comprehensive income	3,332	3,332	3
Reserves from profit	58,401	51,727	3
Retained earnings (including profit from the current year)	88,215	19,190	
– retained profit	29,307	19,190	3
– net profit in the financial year	58,908	–	
Total equity	**583,407**	**489,785**	

2.4.1.2. Main features of Common Equity Tier 1 instruments

Disclosures related to the main features of the Common Equity Tier 1 instruments are laid down in Article 437(1)(b)(c) of Regulation (EU) No 575/2013.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

CAPITAL INSTRUMENTS' MAIN FEATURES TEMPLATE

1	Issuer	Abanka d.d.
2	Unique identifier	ISIN SI0021116510
3	Governing law (s) of the instrument	Companies Act (ZGD-1)
	Regulatory treatment	Regulation (EU) No 575/2013
4	Transitional CRR rules	Common Equity Tier 1 capital
5	Post-transitional CRR rules	Common Equity Tier 1 capital
6	Eligible at solo/(sub-)consolidated/ solo&(sub-)consolidated	solo and (sub-) consolidated
7	Instrument type	Common Equity Tier 1 capital
8	Amount recognised in regulatory capital	EUR 781 million
9	Nominal amount of instrument	"N/A"
9a	Issue price	EUR 348 million in December 2013 (Abanka Vipa d.d.), EUR 243 million in October 2014 (Abanka Vipa d.d.), EUR 190 million in December 2014 (Banka Celje)
9b	Redemption price	EUR 348 million in December 2013, EUR 243 million in October 2014, EUR 190 million in December 2014
10	Accounting classification	shareholders' equity
11	Original date of issuance	on 19 December 2013 (15 million shares), on 21 October 2014 (100 thousand shares), on 16 December 2014 (5 million shares)
12	Perpetual or dated	perpetual
13	Original maturity date	no maturity
14	Issuer call subject to prior supervisory approval	no
15	Optional call date, contingent call dates and redemption amount	"N/A"
16	Subsequent call dates, if applicable	"N/A"
	Coupons / dividends	"N/A"
17	Fixed or floating dividend/coupon	"N/A"
18	Coupon rate and any related index	"N/A"
19	Existence of a dividend stopper	no
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	mandatory
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	mandatory
21	Existence of step up or other incentive to redeem	"N/A"
22	Noncumulative or cumulative	"N/A"
23	Convertible or non-convertible	"N/A"
24	If convertible, conversion trigger(s)	"N/A"
25	If convertible, fully or partially	"N/A"
26	If convertible, conversion rate	"N/A"
27	If convertible, mandatory or optional conversion	"N/A"
28	If convertible, specify instrument type convertible into	"N/A"
29	If convertible, specify issuer of instrument it converts into	"N/A"
30	Write-down features	"N/A"
31	If write-down, write-down trigger(s)	"N/A"
32	If write-down, full or partial	"N/A"
33	If write-down, permanent or temporary	"N/A"
34	If temporary write-down, description of write-up mechanism	"N/A"
35	Position in subordination hierarchy in liquidation	all other obligations
36	Non-compliant transitioned features	no
37	If yes, specify non-compliant features	"N/A"

Note:
"N/A" the question is not applicable.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.4.1.3. Disclosure of own funds – the nature and amounts of specific capital items

The disclosures of information related to own funds are laid down in Commission Implementing Regulation (EU) No 1423/2013 (Annex IV).

The disclosures of the nature and amounts of special items of own funds and of restrictions applied to the instruments, prudential filters and deductions used in the calculation of own funds are defined in Article 437(1)(d) and (e) of Regulation (EU) No 575/2013.

OWN FUNDS DISCLOSURE TEMPLATE

Own funds disclosure template		Amount at disclosure date as at 31 December 2018	Regulation (EU) No 575/2013 article reference
Common Equity Tier 1 capital: instruments and reserves			
1	Capital instruments and the related share premium accounts	433,459	26(1), 27, 28, 29
	of which: Instrument type 1		26(3), EBA list
	of which: Instrument type 2		26(3), EBA list
	of which: Instrument type 3		26(3), EBA list
2	Retained earnings	19,190	26(1)(c)
3	Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under the applicable accounting standards)	55,059	26(1)
3a	Funds for general banking risk		26(1)(f)
4	Amount of qualifying items referred to in Article 484 (3) and the related share premium accounts subject to phase out from CET1		486(2)
5	Minority Interests (amount allowed in consolidated CET1)		84, 479, 480
5a	Independently reviewed interim profits net of any foreseeable charge or dividend		26(2)
6	**Common Equity Tier 1 (CET1) capital before regulatory adjustments**	**507,708**	
Common Equity Tier 1(CET1) capital: regulatory adjustments			
7	Additional value adjustments (negative amount)	(209)	34, 105
8	Intangible assets (net of related tax liability) (negative amount)	(9,073)	36(1)(b), 37, 472(4)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) are met) (negative amount)	(8,641)	36(1)(c), 38, 472(5)
11	Fair value reserves related to gains or losses on cash flow hedges		33(a)
12	Negative amounts resulting from the calculation of expected loss amounts		36(1)(d), 40, 159, 472(6)
13	Any increase in equity that results from securitised assets (negative amount)		32(1)
14	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing		33(b)
15	Defined-benefit pension fund assets (negative amount)		36(1)(e), 41, 472(7)

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

Own funds disclosure template		Amount at disclosure date as at 31 December 2018	Regulation (EU) No 575/2013 article reference
16	Direct and indirect holdings by an institution of own CET1 instruments (negative amount)		36(1)(f), 42, 472(8)
17	Holdings of the CET1 instruments of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution (negative amount)		36(1)(g), 44, 472(9)
18	Direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution does not have a significant investment in those entities (amount above the 10% threshold and net of eligible short positions) (negative amount)		36(1)(h), 43, 45, 46, 49(2) in (3), 79, 472(10)
19	Direct, indirect and synthetic holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)		36(1)(i), 43, 45, 47, 48(1)(b), 49(1) do (3), 79, 470, 472(11)
20a	Exposure amount of the following items which qualify for a RW of 1250%, where the institution opts for the deduction alternative		36(1)(k)
20b	of which: qualifying holdings outside the financial sector (negative amount)		36(1)(k)(i), 89 do 91
20c	of which: securitisation positions (negative amount)		36(1)(k)(ii), 243(1)(b), 244(1)(b), 258
20d	of which: free deliveries (negative amount)		36(1)(k)(iii), 379(3)
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability where the conditions in 38 (3) are met) (negative amount)		36(1)(c), 38, 48(1)(a), 470, 472(5)
22	Amount exceeding the 15% threshold (negative amount)		48(1)
23	of which: direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities		36(1)(i), 48(1)(b), 470, 472(11)
25	of which: deferred tax assets arising from temporary differences		36(1)(c), 38, 48(1)(a), 470, 472(5)
25a	Losses for the current financial year (negative amount)		36(1)(a), 472(3)
25b	Foreseeable tax charges relating to CET1 items (negative amount)		36(1)(l)
27	Qualifying AT1 deductions that exceed the AT1 capital of the institution (negative amount)		36(1)(j)
28	**Total regulatory adjustments to Common equity Tier 1 (CET1)**	**(17,923)**	
29	**Common Equity Tier 1 (CET1) capital**	**489,785**	
44	**Additional Tier 1 (AT1) capital**		
45	**Tier 1 capital (T1 = CET1 + AT1)**	**489,785**	
58	**Tier 2 (T2) capital**		
59	**Total capital (TC = T1 + T2)**	**489,785**	
60	**Total risk weighted assets**	**2,068,883**	

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

Own funds disclosure template		Amount at disclosure date as at 31 December 2018	Regulation (EU) No 575/2013 article reference
Capital ratios and buffers			
61	Common Equity Tier 1 (as a percentage of risk exposure amount)	23.67%	92(2)(a), 465
62	Tier 1 (as a percentage of risk exposure amount)	23.67%	92(2)(b), 465
63	Total capital (as a percentage of risk exposure amount)	23.67%	92(2)(c)
64	Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus systemically important institution buffer expressed as a percentage of risk exposure amount)	1.89%	128, 129 and 130 (Directive 2013/36/EU)
65	of which: capital conservation buffer requirement	1.88%	
66	of which: countercyclical buffer requirement	0.02%	
67	of which: systemic risk buffer requirement		
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer		131 (Directive 2013/36/EU)
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	23.67%	128 (Directive 2013/36/EU)
Amounts below the thresholds for deduction (before risk weighting)			
72	Direct and indirect holdings of the capital of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	13,165	36(1)(h), 45, 46, 472(10), 56(c), 59, 60, 475(4), 66(c), 69, 70, 477(4)
73	Direct and indirect holdings by the institution of the CET 1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)		36(1)(i), 45, 48, 470, 472(11)
75	Deferred tax assets arising from temporary differences (amount below 10% threshold, net of related tax liability where the conditions in Article 38 (3) are met)	1,584	36(1)(c), 38, 48, 470, 472(5)

Note:
Other items are not included in the template because the Group does not have them. The Group doesn't have Additional Tier 1 instruments and regulatory adjustments, Tier 2 instruments and regulatory adjustments, applicable caps on the inclusion of provisions in Tier 2 and capital instruments subject to phase-out arrangements.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.4.2 Capital requirements

The disclosures relating to capital requirements are laid down in Article 438 of Regulation (EU) No 575/2013. In addition, disclosure requirements are defined in Chapter 4.6 of the Guidelines on disclosure requirements under Part Eight of Regulation (EU) No 575/2013.

The following table EU OV1 provides an overview of the risk-weighted exposure amounts.

The total credit risk-weighted exposure amount of the Group is calculated by applying the standardised approach.
The total market risk exposure amount is calculated by multiplying the own funds requirement for market risk by 12.5. The Group applies the standardised approach to calculate the capital requirement for market risk. In this context, the own funds requirement is calculated for position and foreign-exchange risk.

The total operational risk exposure amount is calculated by multiplying the own funds requirement for operational risk by 12.5. The Group applies the basic indicator approach to calculate the own funds requirement for operational risk. Therefore, the own funds requirement for operational risk is equal to 15% of the average annual gross income over the previous three years.

The total risk exposure amount for credit valuation adjustment is calculated by multiplying the own funds requirement for credit valuation adjustment by 12.5. The Group applies the standardised approach to calculate the own funds requirement for credit valuation adjustment. Credit valuation adjustment or CVA means an adjustment to the mid-market valuation of the portfolio of transactions with a counterparty for all OTC derivative instruments.

The total settlement risk exposure amount is calculated by multiplying the own funds requirement for settlement risk by 12.5. This calculation is made in the case of transactions in which debt instruments, equities, foreign currencies and commodities are unsettled after their due delivery, for which an institution has to calculate the price difference to which it is exposed.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

EU OV1 – OVERVIEW OF RWAs

As at 31 December			2018	2017	2018
			RWAs		Minimum capital require-ments
	1	Credit risk (excluding CCR)	1,824,484	1,796,382	145,959
Article 438 (c) (d)	2	Of which the standardised approach	1,824,484	1,796,382	145,959
Article 438 (c) (d)	3	Of which the foundation IRB (FIRB) approach	–	–	–
Article 438 (c) (d)	4	Of which the advanced IRB (AIRB) approach	–	–	–
Article 438 (d)	5	Of which equity IRB under the simple risk-weighted approach or the IMA	–	–	–
Article 438 (c) (d) Article 107	6	CCR	9,480	4,220	758
Article 438 (c) (d)	7	Of which mark to market	7,319	3,714	586
Article 438 (c) (d)	8	Of which original exposure	–	–	–
	9	Of which the standardised approach	–	89	–
	10	Of which internal model method (IMM)	–	–	–
Article 438 (c) (d)	11	Of which risk exposure amount for contributions to the default fund of a CCP	–	–	–
	12	Of which CVA	2,161	417	173
Article 438 (e)	13	Settlement risk	–	–	–
Article 449 (o) (i)	14	Securitisation exposures in the banking book (after the cap)	–	–	–
	15	Of which IRB approach	–	–	–
	16	Of which IRB supervisory formula approach (SFA)	–	–	–
	17	Of which internal assessment approach (IAA)	–	–	–
	18	Of which standardised approach	–	–	–
Article 438 (e)	19	Market risk	590	518	47
	20	Of which the standardised approach	590	518	47
	21	Of which IMA	–	–	–
Article 438 (e)	22	Large exposures	–	–	–
Article 438 (f)	23	Operational risk	230,369	244,228	18,430
	24	Of which basic indicator approach	230,369	244,228	18,430
	25	Of which standardised approach	–	–	–
	26	Of which advanced measurement approach	–	–	–
Article 437 (2), Article 48 and Article 60	27	Amounts below the thresholds for deduction (subject to 250% risk weight)	3,960	5,192	317
Article 500	28	Floor adjustment	–	–	–
	29	**Total**	**2,068,883**	**2,050,540**	**165,511**

Compared with the previous year, in 2018 the total risk exposure amount increased by 1% or EUR 18,343 thousand, within which credit risk and operational risk exposures increased the most in absolute terms. Other categories of exposure in 2018 did not show significant differences over the previous year. In 2018, the total amount not to be deducted from Common Equity Tier 1 items equalled the amount of deferred tax assets that rely on future profitability and arise from temporary differences, because it was lower than 10% of Common Equity Tier 1 items. In 2018, the amount of investments in the capital instruments of insurance undertakings, reinsurance undertakings or an insurance holding company did not represent a significant investment.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

RISK WEIGHTED EXPOSURE AMOUNTS FOR CREDIT RISK

As at 31 December	2018	2017	2018
	Risk exposure amount		Capital require-ments
Standardised approach	**1,835,763**	**1,805,377**	**146,861**
Exposure classes excluding securitization positions	**1,835,763**	**1,805,377**	**146,861**
Exposures to central governments or central banks	27,382	15,758	2,191
Exposures to regional governments or local authorities	9,899	10,891	792
Exposures to public sector intities	8,189	14,715	655
Exposures to institutions	15,645	18,362	1,252
Exposures to corporates	734,318	701,383	58,745
Retail exposures	721,667	693,634	57,733
Exposures secured by mortgages on immovable property	117,396	117,560	9,392
Exposures in default	66,416	73,723	5,313
Exposures associated w ith particularly high risk	23,352	20,910	1,868
Exposures in the form of covered bonds	9,367	7,028	749
Exposures to institutions and corporates w ith a short-term credit assessment	29,695	42,552	2,376
Exposures in the form of units or shares in collective investment undertakings (CIUs)	8,232	5,876	659
Equity exposures	15,106	17,540	1,208
Other items	49,098	65,445	3,928

Compared with the previous year, in 2018 the credit risk-weighted exposure amount increased by 2% or EUR 30,386 thousand, within which corporate exposures and retail exposures increased the most in absolute terms.

Disclosures relating to the own funds requirements for market risk are laid down in Article 445 of Regulation (EU) No 575/2013. In addition, disclosure requirements are defined in Chapter 4.13 of the Guidelines on disclosure requirements under Part Eight of Regulation (EU) No 575/2013.

The following table EU MR1 provides an overview of the risk-weighted exposure to market risk.

The total market risk exposure amount is calculated by multiplying the own funds requirement for market risk by 12.5. The Group applies the standardised approach to calculate the own funds requirement for market risk. In this context, the own funds requirement is calculated for position risk and foreign-exchange risk.

EU-MR 1 - RISK EXPOSURE AMOUNT FOR POSITION AND FOREIGN-EXCHANGE RISK

As at 31 December		2018	2017	2018
		RWAs		Capital require-ments
	Outright products	**590**	**518**	**47**
1	Interest rate risk (general and specific)	142	83	11
2	Equity risk (general and specific)	448	435	36
3	Foreign-exchange risk	–	–	–
4	Commodity risk	–	–	–
	Options	**–**	**–**	**–**
5	Simplified approach	–	–	–
6	Delta-plus method	–	–	–
7	Scenario approach	–	–	–
8	**Securitisation (specific risk)**	–	–	**–**
9	**Total**	**590**	**518**	**47**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.4.3 Leverage ratio

The disclosures of information regarding the leverage ratio are laid down in Article 451 of the Regulation (EU) No 575/2013 and the Commission Implementing Regulation 200/2016.

2.4.3.1 Reconciliation of accounting assets and the leverage ratio total exposure measure

The disclosures of information regarding a reconciliation of accounting assets and the leverage ratio total exposure measure are laid down in Article 451(1)(b) of Regulation (EU) 575/2013.

TABLE LRSum – SUMMARY RECONCILIATION OF ACCOUNTING ASSETS AND THE LEVERAGE RATIO TOTAL EXPOSURE MEASURE

As at 31 December		2018	2017
1	Total assets as per published financial statements	3,731,543	3,654,147
2	Adjustment for entities w hich are consolidated for accounting purposes but are outside the scope of regulatory consolidation	–	–
3	(Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting framew ork but excluded from the leverage ratio exposure measure in accordance w ith Article 429(13) of Regulation (EU) No 575/2013 "CRR")	–	–
4	Adjustments for derivative financial instruments	5,330	1,601
5	Adjustments for securities financing transactions "SFTs"		–
6	Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	299,871	274,317
EU-6a	(Adjustment for intragroup exposures excluded from the leverage ratio exposure measure in accordance w ith Article 429 (7) of Regulation (EU) No 575/2013)	–	–
EU-6b	(Adjustment for exposures excluded from the leverage ratio exposure measure in accordance w ith Article 429 (14) of Regulation (EU) No 575/2013)	–	–
7	Other adjustments	(17,714)	(13,070)
8	**Total leverage ratio exposure**	**4,019,030**	**3,916,995**

2.4.3.2 Breakdown of the leverage ratio total exposure measure

The disclosures of information regarding a breakdown of the leverage ratio total exposure measure are laid down in Article 451(1)(a)(b)(c) of Regulation (EU) 575/2013.

The breakdown of the leverage ratio total exposure measure in terms of exposure, capital measure, specified choice of the definition of the capital measure and fiduciary assets in the statement of financial position is shown in the table below.

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(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

TEMPLATE LRCom - LEVERAGE RATIO TOTAL COMMON DISCLOSURE

	As at 31 December	2018	2017
On-balance sheet exposures (excluding derivatives and SFTs)			
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	3,727,933	3,648,103
2	(Asset amounts deducted in determining Tier 1 capital)	(17,714)	(13,070)
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2)**	**3,710,219**	**3,635,033**
Derivative exposures			
4	Replacement cost associated with *all* derivatives transactions (ie net of eligible cash variation margin)	3,610	2,785
5	Add-on amounts for PFE associated with *all* derivatives transactions (mark-to-market method)	5,330	1,601
EU-5a	Exposure determined under Original Exposure Method	–	–
6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework	–	–
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	–	–
8	(Exempted CCP leg of client-cleared trade exposures)	–	–
9	Adjusted effective notional amount of written credit derivatives	–	–
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)	–	–
11	**Total derivative exposures (sum of lines 4 to 10)**	**8,940**	**4,386**
Securities financing transaction exposures			
12	Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	–	–
13	(Netted amounts of cash payables and cash receivables of gross SFT assets)	–	–
14	Counterparty credit risk exposure for SFT assets	–	**3,259**
EU-14a	Derogation for SFTs: Counterparty credit risk exposure in accordance with Article 429b (4) and 222 of Regulation (EU) No 575/2013	–	–
15	Agent transaction exposures	–	–
EU-15a	(Exempted CCP leg of client-cleared SFT exposure)	–	–
16	**Total securities financing transaction exposures (sum of lines 12 to 15a)**	**–**	**3,259**
Other off-balance sheet exposures			
17	Off-balance sheet exposures at gross notional amount	687,420	602,576
18	(Adjustments for conversion to credit equivalent amounts)	(387,549)	(328,259)
19	**Other off-balance sheet exposures (sum of lines 17 to 18)**	**299,871**	**274,317**
Exempted exposures in accordance with CRR Article 429 (7) and (14) (on and off balance sheet)			
EU-19a	(Exemption of intragroup exposures (solo basis) in accordance with Article 429(7) of Regulation (EU) No 575/2013 (on and off balance sheet))		
EU-19b	(Exposures exempted in accordance with Article 429 (14) of Regulation (EU) No 575/2013 (on and off balance sheet))		
Capital and total exposures			
20	**Tier 1 capital**	**489,785**	**503,628**
21	**Total leverage ratio exposures (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)**	**4,019,030**	**3,916,995**
Leverage ratio			
22	**Leverage ratio**	**12.19%**	**12.86%**
Choice on transitional arrangements and amount of derecognised fiduciary items			
EU-23	Choice on transitional arrangements for the definition of the capital measure		the definition of Tier 1 capital in accordance with Article 499 (1) (b) of Regulation (EU) No 575/2013
EU-24	Amount of derecognised fiduciary items in accordance with Article 429(11) of Regulation (EU) NO 575/2013		

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

TEMPLATE LRSpl - SPLIT-UP OF ON BALANCE SHEET EXPOSURES (EXCLUDING DERIVATIVES, SFTS AND EXEMPTED EXPOSURES)

As at 31 December		2018	2017
EU-1	Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:	3,727,933	3,648,103
EU-2	Trading book exposures	228	233
EU-3	Banking book exposures, of which:	3,727,705	3,647,870
EU-4	Covered bonds	89,462	67,000
EU-5	Exposures treated as sovereigns	1,228,236	1,363,274
EU-6	Exposures to regional governments, MDB, international organisations and PSE NOT treated as sovereigns	215,517	74,658
EU-7	Institutions	57,537	72,467
EU-8	Secured by mortgages of immovable properties	264,587	266,447
EU-9	Retail exposures	935,543	903,171
EU-10	Corporate	623,655	565,315
EU-11	Exposures in default	63,006	68,571
EU-12	Other exposures (eg equity, securitisations, and other non-credit obligation assets)	250,162	266,967

2.4.3.3 Disclosure of qualitative information on risk of excessive leverage

The disclosures of information regarding the processes used to manage the risk of excessive leverage are laid down in Article 451(1)(d) of Regulation (EU) 575/2013.

The process of excessive leverage risk management is performed in accordance with the adopted policy on excessive leverage risk management. It includes regular monitoring of the movement of the leverage ratio, which is within the competence of the Risk Management and Asset-Liability Committee. Considering the structure of the statement of financial position and the level of the leverage ratio, the Group assessed that the risk of excessive leverage was low. Such an assessment was made on the basis of achieving the tolerance value of the leverage ratio as set out in the Risk Management Strategy and Risk Appetite as well as achieving the warning and limit values under the Recovery Plan.

2.4.3.4 Disclosure of qualitative information on risk of the factors impacting the leverage ratio

The disclosures of information regarding the factors that had an impact on the leverage ratio during the period to which the disclosed leverage ratio refers are laid down in Article 451(1)(e) of Regulation (EU) 575/2013.

The leverage ratio is calculated as a Tier 1 measure of the Group divided by the total exposure measure of the Group.

KEY INFORMATION REGARDING LEVERAGE RATIO

As at 31 December	2018	2017
Tier 1 capital	489,785	503,628
Total leverage ratio exposures	4,019,030	3,916,995
Leverage Ratio	12.19%	12.86%

Tier 1 capital of the Group amounted to EUR 489,785 thousand as at 31 December 2018, which represents a year-on-year decrease of EUR 13,843 thousand. As at the reporting date, the total leverage ratio exposures of the Group stood at EUR 4,019,030 thousand, or EUR 102,035 thousand more compared to 31 December 2017. The leverage ratio of the Group, reached 12.19%, which was 0.5 percentage points lower than at the 2017 year-end.

NOTES TO THE FINANCIAL STATEMENTS (continued)

In 2018, the bulk of Tier 1 measure was accounted for by:
- capital instruments and related share premium accounts,
- retained earnings,
- accumulated other comprehensive income and other reserves.

Due to higher Common Equity Tier 1 items and lower reductions from Common Equity Tier 1 items, the Tier 1 measure improved in 2018 compared to 2017, positively impacting the level of the leverage ratio.

In the reporting period, the bulk of leverage ratio total exposure measure was accounted for by:
- exposures to central governments
- retail exposures,
- exposures to corporates.

Due to higher amounts of exposures to regional governments and public sector entities and lower amounts of exposures to central governments, the leverage ratio total exposure measure decreased in 2018 compared to 2017, which had a positive impact on the level of the leverage ratio.

2.4.4 Capital buffers

The disclosures of information regarding capital buffers are laid down in Article 440 of Regulation (EU) 575/2013 and the Commission Delegated Regulation (EU) 2015/1555.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

GEOGRAPHICAL DISTRIBUTION OF CREDIT EXPOSURES RELEVANT FOR THE CALCULATION OF THE COUNTERCYCLICAL CAPITAL BUFFER AS AT 31 DECEMBER 2018

	General credit exposures		Trading book exposure		Own funds requirements				
Country	Exposure value for SA	Exposure value IRB	Sum of long and short position of trading book	Value of trading book exposure for internal models	Of which: General credit exposures	Of which: Trading book exposures	Total	Own funds requirement weights	Countercyclical capital buffer rate
United Arab Emirates	1				0		0	0.00%	0.00%
Afghanistan	0				0		0	0.00%	0.00%
Albania	1				0		0	0.00%	0.00%
Argentina	0				0		0	0.00%	0.00%
Austria	25,276				934		934	0.66%	0.00%
Australia	4,685				75		75	0.05%	0.00%
Bosnia and Herzegovina	423				25		25	0.02%	0.00%
Belgium	17,275				352		352	0.25%	0.00%
Bulgaria	16				1		1	0.00%	0.00%
Brazil	1				0		0	0.00%	0.00%
Belarus	0				0		0	0.00%	0.00%
Canada	4,286				334		334	0.24%	0.00%
Switzerland	20,976				344		344	0.24%	0.00%
Chile	0				0		0	0.00%	0.00%
China	4				0		0	0.00%	0.00%
Czech Republic	8,535				672		672	0.47%	1.00%
Germany	23,266				697		697	0.49%	0.00%
Denmark	3,590				57		57	0.04%	0.00%
Egypt	15				1		1	0.00%	0.00%
Spain	61				3		3	0.00%	0.00%
Finland	11,686				93		93	0.07%	0.00%
France	29,881				1,116		1,116	0.79%	0.00%
United Kingdom	31,519				1,357		1,357	0.96%	1.00%
Greece	0				0		0	0.00%	0.00%
Hong Kong	0				0		0	0.00%	1.88%
Croatia	5,988				181		181	0.13%	0.00%
Hungary	132				11		11	0.01%	0.00%
Indonesia	1				0		0	0.00%	0.00%
Ireland	8				0		0	0.00%	0.00%
India	0				0		0	0.00%	0.00%
Iran	0				0		0	0.00%	0.00%
Italy	2,126				95		95	0.07%	0.00%
Island of Jersey	0				0		0	0.00%	0.00%
Jamaica	0				0		0	0.00%	0.00%
Japan	843				13		13	0.01%	0.00%
South Korea	0				0		0	0.00%	0.00%
Kazakhstan	0				0		0	0.00%	0.00%
Liechtenstein	5				0		0	0.00%	0.00%
Sri Lanka	0				0		0	0.00%	0.00%
Lithuania	0				0		0	0.00%	0.50%
Luxembourg	2				0		0	0.00%	0.00%

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

Country	General credit exposures		Trading book exposure		Own funds requirements				
	Exposure value for SA	Exposure value IRB	Sum of long and short position of trading book	Value of trading book exposure for internal models	Of which: General credit exposures	Of which: Trading book exposures	Total	Own funds requirement weights	Countercyclical capital buffer rate
Latvia	0				0		0	0.00%	0.00%
Libya	0				0		0	0.00%	0.00%
Moldavia	2				0		0	0.00%	0.00%
Montenegro	5				0		0	0.00%	0.00%
Madagascar	0				0		0	0.00%	0.00%
Macedonia	38				2		2	0.00%	0.00%
Mexico	0				0		0	0.00%	0.00%
Nigeria	0				0		0	0.00%	0.00%
Netherlands	38,136				2,021		2,021	1.42%	0.00%
Norway	14,430				124		124	0.09%	2.00%
Nepal	0				0		0	0.00%	0.00%
Philippines	2				0		0	0.00%	0.00%
Pakistan	0				0		0	0.00%	0.00%
Poland	1,124				45		45	0.03%	0.00%
Palestine	0				0		0	0.00%	0.00%
Portugal	96				6		6	0.00%	0.00%
Paraguay	0				0		0	0.00%	0.00%
Romania	2				0		0	0.00%	0.00%
Serbia	4,892				57		57	0.04%	0.00%
Russian Federation	9				1		1	0.00%	0.00%
Sweden	11,029				94		94	0.07%	2.00%
Slovenia	2,190,988		224		129,832	36	129,868	91.40%	0.00%
Slovakia	715				57		57	0.04%	1.25%
Thailand	0				0		0	0.00%	0.00%
Tunisia	0				0		0	0.00%	0.00%
Turkey	2				0		0	0.00%	0.00%
Ukraine	8				0		0	0.00%	0.00%
United States of America	45,705				3,445		3,445	2.42%	0.00%
Uzbekistan	0				0		0	0.00%	0.00%
Venezuela	1				0		0	0.00%	0.00%
Kosovo	20				1		1	0.00%	0.00%
South Africa	0				0		0	0.00%	0.00%
	2,497,808	**–**	**224**	**–**	**142,047**	**36**	**142,083**		

Note:
Exposures to securitisation positions are not included in the table as the Group has none.

AMOUNT OF INSTITUTION-SPECIFIC COUNTERCYCLICAL CAPITAL BUFFER

As at 31 December	2018
Total risk exposure amount	2,068,883
Institution specific conuntercyclical buffer rate	0.018%
Institution specific conuntercyclical buffer requirement	365

NOTES TO THE FINANCIAL STATEMENTS (continued)

2.4.5 Indicators of global systemic importance

The disclosures of information regarding the indicators of global systemic importance are laid down in Article 441 of Regulation (EU) 575/2013 and the Commission Implementing Regulation (EU) 2016/818.

Institutions identified as G-SIIs disclose the values of the indicators of global systemic importance on an annual basis. Abanka d.d. is not defined as a G-SII bank.

2.4.6 Internal capital adequacy assessment process

The internal capital adequacy assessment process is defined by two variables. The first variable represents the risks to which the Group is exposed, going beyond the first pillar of capital requirements, while the second variable is the capital held by the Group for covering risks and potential losses arising from such risks. A comparison of the internal assessment of capital requirements and the internal assessment of capital indicates the Group's ability to cover all risks to which it is exposed.

Within the framework of the Internal Capital Adequacy Assessment Process (ICAAP), the Group upgraded existing methods for calculating the internal assessments of capital requirements; continued to regularly monitor its risk profile and evaluated risk-bearing capacity; set up and performed stress tests; and calculated the amount of its internal assessment of capital and internal assessment of capital requirements for all important types of risks. The findings of the ICAAP process are included in risk reports, which are communicated to the members of the Risk Management and Asset-Liability Committee, consisting of senior management of the Bank, the Management Board members, the members of the The Risk Monitoring and Asset Liability Management Committee and the Supervisory Board members.

As at 31 December 2018, the consolidated total capital ratio, Common Equity Tier 1 ratio and Additional Tier 1 capital ratio were at 23.67% (non-consolidated 23.62%). In accordance with Regulation (EU) No 575/2013, the following own funds requirements shall apply in the period from 1 January 2015 on: a Common Equity Tier 1 capital ratio at 4.5% or higher; a Tier 1 capital ratio at 6% or higher; and a total capital ratio at 8% or higher. As at 31 December 2018, the Group's capital adequacy ratios were above the legally required levels. As at the 2018 year-end, the overall capital requirement (OCR) was 13.64% on a consolidated basis, consisting of:
- 11.75% of total SREP capital requirement (TSCR), comprising 8% Pillar 1 requirement and 3.75% Pillar 2 requirement, and
- 1.89% of combined buffer requirement (1.875% – capital conservation buffer and 0.018% – countercyclical capital buffer).

Since 2017, when the overall capital requirement stood at 13.25%, it increased to 13.64% in 2018 due to the statutory prescribed gradual incorporation of the capital conservation buffer and the reduction of Pillar 2 capital requirement.

As of March 1, 2019, the Group must achieve a total capital requirement of 14.52 percent. The increase in the requirement compared to 2018 is the consequence of the prescribed growth of the capital conservation buffer (reaching the full legal value of 2.5% in 2019); andadditional buffer for other systemically important banks in the amount of 0.25%).

2.5 Operational risk management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

In the basic operational risk classification, the Group derives from the following seven categories that are in line with the CRR requirements:
- internal fraud,
- external fraud,
- employment practices and workplace safety,
- clients, products and business practices,
- damage to physical assets,
- business disruption and systems failures,
- execution, delivery and process management.

NOTES TO THE FINANCIAL STATEMENTS (continued)

In the context of this classification, the Group also monitors the following sub-categories of operational risk:
- conduct risk,
- outsourcing risk,
- model risk,
- compliance risk,
- legal risk and
- cyber risk.

The definition excludes business risk and reputational risk. However, the realisation of operational risk may, as a consequence, impair the Group's reputation.

2.5.1 Operational risk management process

The strategy, policy, framework, system and processes for managing operational risk are defined by the following documents: Risk Management Strategy and Risk Appetite, Risk Management Limits, and ICAAP and ILAAP Rules.

In 2018, the Group continued with the activities formulated in the above-mentioned strategy, which was updated in 2018 to include current amendments. In addition, the accompanying internal instructions, which refer to all operational risk management steps and to the Group's risk capacity and risk appetite, were brought in line with the strategy requirements. In 2018, the Group implemented a new methodology for operational risk assessment in the Abanka Group.

The objective of the operational risk management process is to establish procedures for reducing risk and limiting the occurrence of losses from operational risk. Measures to reduce the frequency and severity of operational incidents will be planned and implemented.

The operational risk management process includes:
- procedures of operational risk identification, measurement/assessment, monitoring (controlling) and mitigation;
- operational risk internal reporting.

The Group regularly identifies and quantitatively assesses operational risk exposure and lists preventive and corrective measures of operational risk incidents. The system of operational risk internal reporting in the Group involves all employees and enables a quick reaction in the event of difficulties, as the Management Board and senior management are involved in such reporting. If necessary, after each incident additional measures are taken and the project holders and deadlines are set in order to mitigate the consequences or prevent or reduce possible reoccurrence with an aim to improve operational risk management. Risk Management Department monitors the implementation of measures and reports to the Operational Risk Commission and to the Risk Management and Asset-Liability Committee.

The structure and organisation of appropriate operational risk management in the Group involves employees at all levels with different responsibilities and duties. Operational risk management and risk mitigation measures are decentralised and take place in all organisational units. The Risk Management Department is in charge of coordinating the operational risk management function.

Working within the Group are the Operational Risk Commission, which is responsible for the development of the operational risk management system, and the Risk Management and Asset-Liability Committee, which is a collective decision-making body responsible for directing and controlling operational risk management. The latter includes all senior managers and is chaired by a member of the Management Board.

For the purpose of **operational risk internal reporting**, the Group uses an application developed in-house for reporting operational risk incidents, which allows for regular / non-anonymous and anonymous reporting of such incidents. In the context of incident reporting, the Group also collects information on operational risk sub-categories.

The Risk Management Department is responsible for the preparation of summary quarterly reports on loss events, which are discussed by the Operational Risk Commission and the Risk Management and Asset-Liability Committee. The Committee discusses major loss events in greater detail, takes appropriate measures as they occur and monitors implementation of these measures. It also discusses other reports on operational risk and its management and investigates all operational risk profiles

NOTES TO THE FINANCIAL STATEMENTS (continued)

(assessed, realised) by organisational units and at the Group level. Moreover, the Management Board and senior management are promptly informed of all major loss events. At least quarterly, the Supervisory Board discusses the risk exposure report.

2.5.1.1 Operational risk measurement

Characteristic of the **operational risk measurement system** is the identification and assessment and/or measurement of operational risk in accordance with the Methodology for operational risk assessment in the Abanka Group. Risk measurement is based on the **operational risk exposure assessment by individual organisational units** using a standardised form and the list of sub-categories derived from the seven event types of operational risk. Each sub-category is assessed with the probability of occurrence and severity of the consequences in case of occurrence. The assessment uses a quantitative approach and a frequency and effect method. Key controls are also identified for each operational risk sub-category.

In parallel, exposure to operational risk is measured by reporting individual operational risk incidents into the centralised database of incidents. The financial impact is measured/assessed for each reported incident.

2.5.1.2. Operational risk mitigation

The Group carries out activities within the framework of **operational risk hedging and reduction**, which are based on the identification, measurement, assessment, monitoring and internal reporting on operational risk. In addition, the Group performs activities to mitigate the consequences of occurred loss events. The implementation of these activities is the responsibility of individual organisational units. An analysis of the loss events which occurred during the last year was performed, indicating that the external factor was the main source of losses arising from operational risks. Therefore, the Group is continuously introducing measures for constant risk mitigation.

Actions are prepared **for the financially highest ranked operational risk sub-categories**, aimed at their prevention or reducing the likelihood of their occurrence, including the persons in charge and the deadlines.

For **each reported incident**, actions are also prepared to most effectively deal with the consequences and, where appropriate, measures for future avoidance to similar incidents.

In order to appropriately manage and reduce operational risk, the Group has **developed business continuity plans and disaster recovery plans** for all important processes and systems, which are updated, upgraded and tested at least once a year. The plans also include the Recovery Time (RTO) and Recovery Point Objective (RPO) parameters, and ensure effective coordination of these between the IT and organisational units.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3 CRITICAL ACCOUNTING ESTIMATES, JUDGEMENTS AND SOURCES OF UNCERTAINTY IN APPLYING ACCOUNTING POLICIES

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable given the circumstances.

Critical judgements in applying accounting policies

Described below are the management's critical judgements in applying the accounting policies that most significantly affect the amounts reported in the financial statements:

- the definition of business models for the classification and measurement of financial assets, as explained in more detail in Note 1.5 Financial assets and financial liabilities.
- a significant increase in credit risk: As explained in Section 2, expected credit loss is measured as the amount of possible losses expected within 12 months after the reporting date for financial assets classified into stage 1 or as the amount of all possible losses expected in the full lifetime of a financial asset for financial assets classified into stage 2 and stage 3. An asset is reclassified into stage 2 when there is a significant increase in credit risk; however, IFRS 9 does not define what constitutes a significant increase in credit risk and therefore judgement is needed. In using judgement to determine whether there has been a significant increase in credit risk, both qualitative and quantitative forward-looking information is used, as explained in more detail in Section 2.
- the definition of segments with similar credit risk characteristics: When expected credit loss is measured on the basis of collective assessment, financial assets are classified into individual segments based on similar credit risk characteristics by using judgement. Classification into individual segments is described in detail in Section 2.
- assessment models and the assumptions used: The Group uses the corresponding valuation models in the valuation of financial assets at fair value and estimation of expected credit losses. Judgement is needed to determine which models are appropriate for a particular financial asset or group of financial assets as well as the definition of the relevant assumptions used in these models. The fair value of financial assets is further defined in Note 4, while the expected credit loss estimate is described in detail in Section 2.

Critical estimates and sources of uncertainty

Described below are the critical estimates, which the management used in the accounting policies and which most significantly affect the amounts reported in the financial statements:

- the selection of the appropriate number of macroeconomic scenarios and used weights as well as forward-looking information relevant for each scenario: Expected credit loss is estimated by using reasonable and supportable forward-looking information, which is based on assumptions about future developments of various economic indicators and the interaction among these indicators. See Section 2 for further information, including a sensitivity analysis.
- probability of default: Probability of default is one of the main parameters in the measurement of expected credit loss, the value of which depends on historical data, assumptions and expectations about future conditions. See Section 2 for further information, including a sensitivity analysis.
- loss given default is estimated loss arising from default. It is determined on the basis of the difference between contractual cash flows due and those that the Group expects to receive, taking into account collateral. See Section 2 for further information, including a sensitivity analysis.
- fair value measurement: Fair value is estimated by using market observable data to the extent available. When these data (level 1) are not available, the fair value of financial assets is estimated using valuation models. Fair value measurement of financial assets is described in detail in Note 4.

NOTES TO THE FINANCIAL STATEMENTS (continued)

4 FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

Financial instruments carried at fair value

Fair value is defined as the price achieved on the sale of an asset or paid to transfer a liability in an orderly transaction in the principal (or, if not existent, in the most advantageous) market under current market conditions between participants at the measurement date. Such a definition of price requires the market participants to be independent and unrelated, informed and capable, willing and not forced to enter into a transaction.

When measuring fair value, it is assumed that an asset or liability is exchanged in an orderly transaction between market participants under current market conditions at the measurement date, whether or not the price can be directly observed or estimated by applying other valuation techniques.

Fair value hierarchy

In line with IFRS 13, the Group categorises financial instruments into three fair value levels based on the nature of inputs used to determine fair value. Higher levels contain financial instruments whose fair value was measured by using directly observable inputs (directly observable prices). Financial instruments, for which the fair value was also measured by using unobservable inputs, are categorised into lower fair value levels. The level of inputs having the strongest impact on determining the fair value of a financial instrument is taken into consideration. In cases where several types of inputs impact the determination of fair value, the lowest level in the hierarchy of inputs is used.

- Level 1: The Group categorises financial instruments, for which the fair value was measured through direct price observation at markets for identical financial instruments, to which the Group had access at the measurement date, into fair value Level 1. Debt instruments must meet the detailed liquidity criteria stipulated in internal acts, while equity instruments listed on the Ljubljana Stock Exchange are required to comply with the liquidity rules determined by the Ljubljana Stock Exchange.

- Level 2: The Group categorises financial instruments, for which the fair value was measured through direct price observation at markets for similar financial instruments, into fair value Level 2. The Group categorises debt instruments into fair value level 2 if the fair value was measured using the direct observation of quoted prices by third parties (e.g. BGN, BVAL, etc.). In addition, the Group categorises into fair value level 2 those financial instruments whose fair value was measured using inputs which make it impossible to categorise a financial instrument into fair value Level 1, whilst the inputs are accessible at the market and indirectly indicate the market conditions, or are derived from observable market prices or from observable quoted prices for equal financial instruments from market participants or third parties, provided orderly transaction pricing and a binding quote of a third party.

- Level 3: The Group categorises financial instruments, for which the fair value was measured using unobservable inputs, into fair value Level 3. Unobservable inputs comprise assumptions and anticipations. In using this valuation technique, the Group forms assumptions and anticipations in compliance with other market participants. In addition, the Group categorises into fair value Level 3 the financial instruments whose fair value was measured by using insufficient or unknown inputs in applying the selected valuation technique and those financial instruments whose fair value was measured on the basis of third party quoted prices that do not indicate an orderly transaction or a binding quote of a third party. Equity securities and equity holdings for which the fair value was measured using internal valuation methods are also classified into fair value level 3.

Valuation techniques for financial instruments measured at fair value

Valuation techniques used in the measurement of fair value encourage maximising the use of relevant observable inputs and minimising the use of unobservable inputs. The markets where inputs for the valuation of financial instruments can be observed include organised exchange markets, dealer markets, brokered markets and principal-to-principal markets.

NOTES TO THE FINANCIAL STATEMENTS (continued)

The Group measures the fair value of financial instruments by using directly observable market prices for identical assets or liabilities, accessible to the Group at the measurement date. As a rule, in such cases the Group makes use of closing market prices on the valuation cut-off date. The Group may further use quoted prices provided by market participants or third parties to measure the fair value of financial instruments, provided that inputs stem from orderly transaction pricing and constitute a binding quote of a third party. In case of several quotations, the Group may use the most favourable quotation.

If directly observable market prices for identical assets or liabilities are not available and, at the same, there are no quoted prices available from market participants or third parties (provided orderly transaction pricing, and a binding quote of a third party, or when the Group estimates that there is no active market for a financial instrument), a market approach or an income approach valuation technique is used to determine fair value.

The fair value of equity securities for which there is no active market, or no market price is available, is mainly determined using a yield-based valuation technique, namely the discounted cash flow method. When a sufficient number of similar listed companies exists, the Group uses a market-based valuation method, namely the method of similar listed companies.

The valuation of debt securities is based on a market-based valuation method using the method of similar companies.

Valuation of derivatives is based on discounting the expected future cash flows estimated on the basis of market information, such as interest rates and exchange rates. The Group applies the Garman-Kohlhagen model for the valuation of European-style currency options, and the Barone-Adesi and Whaley model for American currency options valuation. The Blacks model is used for the valuation of interest options.

When measuring the fair value of loans given, the Group uses the income approach with the net present value method or transaction prices for purchased credit impaired assets.

Internal environment for valuations

The Group has created an internal environment for the proper implementation of the valuation activity. The valuation of financial instruments that are measured at fair value is carried out by an organisational unit that is completely independent of the assets and liabilities management unit. The valuation of financial instruments received as collateral for the Group's investments is carried out by the organisational unit that is not the owner of claims collateralised with financial instruments subject to valuation.

Valuation models, modes of application and types of inputs are defined in the internal rules of the Group, which also hereby restricts any subjective judgement in fair value measurement. On a daily basis, the Group performs independent verification of recorded exchange rates and prices used in the valuation of financial instruments.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

VALUATION METHODOLOGY FOR FINANCIAL INSTRUMENTS MEASURED AT FAIR VALUE

As at 31 December 2018	Quoted prices in active markets (level 1)	Valuation techniques based on observable market data (level 2)	Valuation techniques incorporating information other than observable market data (level 3)	Total
Financial assets measured at fair value				
Financial assets held for trading	–	3,613	224	**3,837**
– shares	–	–	224	**224**
– derivatives	–	3,609	–	**3,609**
– other	–	4	–	**4**
Non-trading financial assets mandatorily at fair value through profit or loss	11,963	–	24,624	**36,587**
– shares and equity holdings	11,963	–	203	**12,166**
– loans and other financial assets	–	–	24,421	**24,421**
Financial assets at fair value through other comprehensive income	97,701	59,409	6,356	**163,466**
– shares and equity holdings	–	–	6,356	**6,356**
– debt securities	97,701	34,692	–	**132,393**
– Bank Resolution Fund	–	24,717	–	**24,717**
Total financial assets	**109,664**	**63,022**	**31,204**	**203,890**

Financial liabilities measured at fair value				
Financial liabilities held for trading	–	3,044	–	**3,044**
– derivatives	–	3,041	–	**3,041**
– spot transactions	–	3	–	**3**
Financial liabilities designated at fair value through profit or loss	–	–	2,281	**2,281**
Total financial liabilities	**–**	**3,044**	**2,281**	**5,325**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

As at 31 December 2017	Quoted prices in active markets (level 1)	Valuation techniques based on observable market data (level 2)	Valuation techniques incorporating information other than observable market data (level 3)	Total
Financial assets measured at fair value				
Financial assets held for trading	–	2,831	217	**3,048**
– shares	–	–	217	**217**
– derivatives	–	2,815	–	**2,815**
– other	–	16	–	**16**
Financial assets designated at fair value through profit or loss	–	–	–	**–**
– unit linked investments	–	–	–	**–**
Available-for-sale financial assets	316,628	767,766	6,296	**1,090,690**
– debt securities	301,691	743,030	–	**1,044,721**
– shares	14,937	2	2,837	**17,776**
– equity holdings	–	–	3,459	**3,459**
– Bank Resolution Fund	–	24,734	–	**24,734**
Total financial assets	**316,628**	**770,597**	**6,513**	**1,093,738**

Financial liabilities measured at fair value				
Financial liabilities held for trading	–	2,492	–	**2,492**
– derivatives	–	2,469	–	**2,469**
– spot transactions	–	23	–	**23**
Total financial liabilities	**–**	**2,492**	**–**	**2,492**

FAIR VALUE TRANSFERS OF FINANCIAL INSTRUMENTS

In 2018 and 2017 there were no significant transfers between the levels of fair value.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

FINANCIAL ASSETS AND LIABILITIES MEASURED AT FAIR VALUE AT LEVEL 3 OF THE FAIR VALUE HIERARCHY

	Financial assets held for trading	Available-for-sale financial assets	Non-trading financial assets mandatorily at fair value through profit or loss	Financial assets at fair value through other comprehensive income	Total
	Shares	Equity holdings			
As at 31 December 2017	**217**	**6,296**	**/**	**/**	**6,513**
Transition to IFRS 9	–	(6,296)	26,641	6,058	**26,403**
As at 1 January 2018	**217**	**/**	**26,641**	**6,058**	**32,916**
Total gains	7	/	4,743	324	**5,074**
– in profit or loss	7	/	4,743	–	**4,750**
– in other comprehensive income	–	/	–	324	**324**
Change in balance that is not the result of transfers between levels or valuation (repayments and similar)	–	/	(6,760)	(26)	**(6,786)**
As at 31 December 2018	**224**	**/**	**24,624**	**6,356**	**31,204**
Gains in profit or loss for financial instruments held as at 31 December 2018	**7**	**/**	**4,759**	**–**	**4,766**

	Financial assets held for trading	Available-for-sale financial assets	Total
	Shares	Equity holdings	
As at 1 January 2017	**170**	**5,397**	**5,567**
Total gains/(losses)	52	1,373	**1,425**
– in profit or loss	–	(53)	**(53)**
– in other comprehensive income	52	1,426	**1,478**
Sales, redemptions, settlements, other	(5)	(474)	**(479)**
As at 31 December 2017	**217**	**6,296**	**6,513**
Gains/(losses) in profit or loss for financial instruments held as at 31 December 2017	**–**	**489**	**489**

	Financial liabilities designated at fair value through profit or loss	Total
As at 31 December 2017	**/**	**/**
Transition to IFRS 9	1,871	**1,871**
As at 1 January 2018	**1,871**	**1,871**
Total gains	410	**410**
– in profit or loss	410	**410**
As at 31 December 2018	**2,281**	**2,281**
Gains in profit or loss for financial instruments held as at 31 December 2018	**410**	**410**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

Financial instruments not measured at fair value

The following table summarises the carrying amounts and fair values of those financial assets and liabilities not measured at their fair value in the Group's statement of financial position.

FINANCIAL INSTRUMENTS NOT MEASURED AT FAIR VALUE

As at 31 December 2018	Carrying value	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets					
Cash, cash balances with the central bank and other demand deposits with banks	538,234	538,234	–	–	538,234
Financial assets at amortised cost	2,918,162	189,497	819,933	1,985,370	2,994,800
– debt securities	946,334	189,497	776,602	–	966,099
– loans to banks	30,784	–	30,625	–	30,625
– loans to non-bank customers	1,928,338	–	–	1,985,370	1,985,370
– corporate entities	1,022,599	–	–	1,034,028	1,034,028
– retail customers	905,739	–	–	951,342	951,342
– other financial assets	12,706	–	12,706	–	12,706
Financial liabilities					
Financial liabilities at amortised cost	3,089,052	–	3,032,464	–	3,032,464
– deposits from banks and the central bank	16,335	–	15,670	–	15,670
– deposits from non-bank customers	2,934,448	–	2,889,209	–	2,889,209
– corporate entities	846,831	–	830,131	–	830,131
– retail customers	2,087,617	–	2,059,078	–	2,059,078
– loans from banks and the central bank	102,788	–	105,748	–	105,748
– loans from non-bank customers	5	–	5	–	5
– debt securities issued	13,644	–	13,644	–	13,644
– other financial liabilities	21,832	–	21,832	–	21,832

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

As at 31 December 2017	Carrying value	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets					
Cash, cash balances with the central bank and other demand deposits with banks	412,168	412,168	–	–	412,168
Loans and receivables	2,052,122	–	84,557	2,090,605	2,175,162
– loans to banks	60,745	–	60,640	–	60,640
– loans to non-bank customers	1,967,460	–	–	2,090,605	2,090,605
– corporate entities	1,098,015	–	–	1,137,003	1,137,003
– retail customers	869,445	–	–	953,602	953,602
– other financial assets	23,917	–	23,917	–	23,917
Held-to-maturity investments	15,408	16,562	–	–	16,562
Financial liabilities					
Financial liabilities measured at amortised cost	3,008,973	–	2,971,869	–	2,971,869
– deposits from banks and the central bank	24,243	–	24,244	–	24,244
– deposits from non-bank customers	2,855,544	–	2,815,709	–	2,815,709
– corporate entities	873,919	–	862,357	–	862,357
– retail customers	1,981,625	–	1,953,352	–	1,953,352
– loans from banks and the central bank	89,011	–	91,741	–	91,741
– loans from non-bank customers	482	–	482	–	482
– debt securities issued	13,021	–	13,021	–	13,021
– other financial liabilities	26,672	–	26,672	–	26,672

The following summarises major methods and assumptions used in estimating the fair values of financial instruments carried at other than fair value in the financial statements.

- Loans to banks and to non-bank customers
  Estimating the fair value of loans is based on the income approach valuation technique by applying the discounted cash flow method. It takes into account the sum of the individual contractual future cash flows (principal and interest), which are discounted with the rates of return on risk-free interest rates for each currency, increased by the level of credit spreads applicable to the industry with a rating of BBB. The calculation takes into account the residual maturity of each cash flow. The discount factor is linearly interpolated as a function of residual maturity in days.

- Debt securities at amortised cost
  The fair value of debt securities measured at amortised cost is determined on the basis of direct observation of market prices for identical financial instruments available to the Group on the day of valuation. If these debt securities also meet the liquidity criteria stipulated in the Bank's internal acts, they are classified into fair value level 1; if not, they are classified into fair value level 2, provided that the fair value was based on the direct observation of quoted prices provided by third parties (e.g. Bloomberg Generic (BGN), Bloomberg Valuation (BVAL)).

- Deposits and loans from banks, the central bank and non-bank customers
  Estimating the fair value of loans is based on the income approach valuation technique by applying the discounted cash flow method. It takes into account the sum of the individual contractual future cash flows (principal and interest), which are discounted with the rates of return on risk-free interest rates for each currency. The calculation takes into account the residual maturity of each cash flow. The discount factor is linearly interpolated as a function of residual maturity in days.

NOTES TO THE FINANCIAL STATEMENTS (continued)

5 SEGMENT ANALYSES

(a) By business segment

The Group provides services in three business segments:

- Retail banking – incorporating personal accounts (of residents and non-residents), savings accounts, domestic and foreign currency fixed-term deposits, annuity and dedicated savings, online banking, mobile banking, AbaSMS mobile service, loans, account overdrafts, insurance services, funds, payment cards, Abacent, gold bullion, safe deposit boxes, MoneyGram, “design your own card” (Oblikuj si kartico!), payment transactions and payment instruments, e-account;
- Corporate banking – incorporating transaction accounts, account overdrafts, loans and deposits with different terms, payment cards, certificates of deposit, documentary operations, guarantees, letters of credit, payment transactions and payment instruments, Abatočka, cash management, Abakredit, e-account, online banking, mobile banking, on-line payment service, AbaSMS mobile service; and
- Financial markets – incorporating trading with financial instruments, liquidity management, investment banking and inter-bank operations.

The “Other” segment includes the activities of the Group that relate to custody and administrative services, activities of subsidiaries (leasing and other activities) and the impact of inter-company transactions in the consolidated statements.

The results by business segment are affected by the opportunity interest rate system. The system is based on alternative/opportunity interest rates, which are determined for all material interest-bearing assets and liabilities items at a contract level. Opportunity interest rates are the basis for calculating opportunity interest margins, both for the individual segments of assets as the difference between earned income and opportunity income as well as for the individual segments of liabilities as the difference between opportunity expenses and incurred expenses. Positive or negative opportunity interest margins are the basis for determining positive and negative contributions to the performance results of individual business segments. Maturity transformation as the difference between opportunity income and expenses is disclosed in the “other” segment (as the result of asset-liability maturity mismatch).

The results of the business segments are also affected by the transactions between the business segments for the purpose of intra-company accounting of income effects. These transactions are made on the basis of an agreed and harmonised set of instruments to account for the transfer of various effects (internal transfers/allocation of indirect costs by business segment, debiting overheads to commercial segments, internal transfers of income effects among business segments).

Liabilities, interest expenses and other non-interest expenses from financing were allocated to those business segments that generated them.

Assets and liabilities by business segment represent a majority of the statement of financial position assets and liabilities, but they exclude tax receivables that are disclosed at the group level and not allocated to business segments.

Business segments are reported to the Management Board of the Bank.

For comparability purposes, business segments for 2017 were adjusted for the effects of the tax on financial services by individual segments in the items external net income and segment result.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

PRIMARY SEGMENT INFORMATION OF THE GROUP

As at 31 December 2018	**Retail banking** (retail customers and sole proprietors)	**Corporate banking**	**Financial markets**	**Other[3]**	**Total**
External net income[1]	48,495	38,822	9,253	2,809	99,379
Revenues from other segments	–	–	–	–	–
Segment result	(335)	53,807	(71)	16,680	70,081
Operating profit					70,081
Profit before tax					70,081
Income tax					(4,489)
Net profit for the year					**65,592**
Segment assets	940,292	1,049,908	1,644,517	96,825	3,731,542
Investments in subsidiaries	–	–	8,278	(8,278)	–
Unallocated assets					–
Total assets					**3,731,542**
Segment liabilities	2,178,971	743,879	185,494	39,791	3,148,135
Unallocated liabilities					–
Total liabilities					**3,148,135**
Other segment items					
Capital expenditure[2]	341	17	4	7,351	7,713
Depreciation and amortisation	1,393	200	26	6,185	7,804
Net impairment and provision	1,381	20,930	(266)	(4,117)	17,928
[1]Including					
– interest income	29,993	25,588	11,586	471	67,638
– interest expenses	(1,970)	(465)	(4,109)	(19)	(6,563)
– dividend income	–	–	1,435	–	1,435
– fee and commission income	26,948	20,641	1,134	4,489	53,212
– fee and commission expenses	(6,476)	(6,942)	(793)	(2,132)	(16,343)

[2] Capital expenditure relates to the purchases of tangible and intangible assets in the current business year.
[3] The result of the “Other” segment is largely represented by maturity transformation, which is not divided among profit segments.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

As at 31 December 2017	Retail banking (retail customers and sole proprietors)	Corporate banking	Financial markets	Other[3]	Total
External net income[1]	46,751	43,509	17,980	3,089	111,329
Revenues from other segments	–	–	–	–	–
Segment result	(859)	23,759	5,766	18,356	47,022
Operating profit					47,022
Profit before tax					47,022
Income tax					(5,427)
Net profit for the year					**41,595**
Segment assets	903,841	1,154,442	1,546,373	49,521	3,654,177
Investments in subsidiaries	–	–	9,448	(9,448)	–
Unallocated assets					–
Total assets					**3,654,177**
Segment liabilities	2,056,566	788,788	199,869	28,671	3,073,894
Unallocated liabilities					–
Total liabilities					**3,073,894**
Other segment items					
Capital expenditure[2]	24	956	7	5,055	6,042
Depreciation and amortisation	2,082	342	51	6,084	8,559
Net impairment and provision	3,374	4,827	529	(5,944)	2,786
[1]Including					
– interest income	29,621	30,014	18,853	1,518	80,006
– interest expenses	(2,849)	(485)	(3,219)	(25)	(6,578)
– dividend income	–	–	1,588	–	1,588
– fee and commission income	27,669	20,065	1,358	1,650	50,742
– fee and commission expenses	(7,690)	(6,085)	(600)	(54)	(14,429)

[2] Capital expenditure relates to the purchases of tangible and intangible assets in the current business year.
[3] The result of the “Other” segment is largely represented by maturity transformation, which is not divided among profit segments.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

(b) Geographical concentration

In the course of its business, the Group also assumes country risk as part of credit risk. In order to manage country risk, the Bank produced a set of rules and methodology stipulating the procedure for setting and monitoring exposure limits to foreign countries and the procedure for determining and monitoring the risk of foreign countries. In line with the methodology, the risk of a foreign country is determined on a quarterly basis using the credit ratings obtained by external credit rating institutions, and annually using key macroeconomic indicators. Foreign countries are classified into four categories in terms of their location and into ten internal credit rating grades, which serves as the basis for setting exposure limits for foreign countries in accordance with the rules. In this way, adequate diversification of investments is ensured, thus achieving an optimal return with an acceptable risk.

GEOGRAPHICAL CONCENTRATIONS OF NON-CURRENT ASSETS AND REVENUES

	Group	
As at 31 December 2018	**Total non-current non-financial assets**	**Revenues**
Slovenia	69,699	116,744
Other European Union countries	–	4,093
Europe (without the EU member states)	–	1,076
Other countries	–	371
	69,699	**122,284**

	Group	
As at 31 December 2017	**Total non-current non-financial assets**	**Revenues**
Slovenia	55,786	125,822
Other European Union countries	–	4,805
Europe (without the EU member states)	–	1,495
Other countries	–	214
	55,786	**132,336**

Revenues consist of interest income, fee and commission income and dividend income.

The Group operates principally in Slovenia, where it is based. Inter-bank exposures account for more than 50% of all international transactions, whilst the rest are transactions with foreign companies and at the level of the central government.

Comparative data for 2017 were adjusted (decreased) by EUR 4,613 thousand due to the changed accounting policy regarding the recognition of tax on financial services (Note 1.25 Comparative data).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

ADDITIONAL DISCLOSURE IN ACCORDANCE WITH THE COUNTRY-BY-COUNTRY REPORTING REQUIREMENT PURSUANT TO ARTICLE 89 OF DIRECTIVE 2013/36/EU (CRD IV)

INFORMATION FOR THE FINANCIAL YEAR 2018 ON A CONSOLIDATED BASIS BY EU MEMBER STATE AND BY THIRD COUNTRY

States	Name(s) and nature of activities	Turnover*	Profit before tax	Tax on profit	Number of employees on a full time equivalent basis
EU Member States:					
Slovenia	ABANKA d.d. (bank), ALEASING d.o.o. (leasing)**, ANEPREMIČNINE d.o.o. (real property management)	122,210	70,046	(4,489)	1,009.08
Third countries:					
Montenegro	Anekretnine d.o.o. (real property management)	75	35	–	0.50
TOTAL ABANKA GROUP		**122,285**	**70,081**	**(4,489)**	**1,009.58**

* including interest income, fee and commission income and dividend income by country in which an individual member company of the Abanka Group is registered
** until 31 March 2018 (sale of subsidiary Aleasing)

In 2018 and 2017, the Group did not receive any public subsidies.

INFORMATION FOR THE FINANCIAL YEAR 2017 ON A CONSOLIDATED BASIS BY EU MEMBER STATE AND BY THIRD COUNTRY

States	Name(s) and nature of activities	Turnover*	Profit before tax	Tax on profit	Number of employees on a full time equivalent basis
EU Member States:					
Slovenia	ABANKA d.d. (bank), ALEASING d.o.o. (leasing), ANEPREMIČNINE d.o.o. (real property management)	132,258	46,970	(5,427)	1,075.93
Third countries:					
Montenegro	Anekretnine d.o.o. (real property management)	78	52	–	0.50
TOTAL ABANKA GROUP		**132,336**	**47,022**	**(5,427)**	**1,076.43**

***** including interest income, fee and commission income and dividend income by country in which an individual member company of the Abanka Group is registered

Comparative data for 2017 were adjusted (decreased) by EUR 4,613 thousand due to the changed accounting policy regarding the recognition of tax on financial services (Note 1.25 Comparative data).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

6 NET INTEREST INCOME

	Abanka		Group	
	2018	2017 (adjusted)	2018	2017 (adjusted)
Interest income				
Financial assets at amortised cost (IFRS 9)	63,834	/	64,305	/
– debt securities	9,526	/	9,526	/
– loans to banks	282	/	282	/
– loans to non-bank customers	54,026	/	54,497	/
Loans (IAS 39)	/	60,085	/	61,603
– to banks	/	515	/	515
– to non-bank customers	/	59,570	/	61,088
Financial assets held for trading	411	318	411	318
Non-trading financial assets mandatorily at fair value through profit or loss (IFRS 9)	1,544	/	1,544	/
Financial assets at fair value through other comprehensive income (IFRS 9)	920	/	920	/
Available-for-sale securities (IAS 39)	/	16,983	/	16,983
Held-to-maturity investments (IAS 39)	/	799	/	799
Other assets	458	303	458	303
	67,167	**78,488**	**67,638**	**80,006**
Interest expenses				
Deposits	2,642	3,627	2,642	3,627
– from banks	168	135	168	135
– from non-bank customers	2,474	3,492	2,474	3,492
Debt securities issued	770	769	770	769
Financial liabilities held for trading	315	263	315	263
Loans from banks and the central bank	770	756	776	756
Other liabilities	2,060	1,158	2,060	1,163
	6,557	**6,573**	**6,563**	**6,578**
Net interest income	**60,610**	**71,915**	**61,075**	**73,428**

Net interest income in 2018 was lower due to lower average realised interest rates on loans to non-bank customers and investments in debt securities (maturity of the DUTB bonds).

Comparative data for 2017 were adjusted (decreased) in the item loans to non-bank customers by EUR 321 thousand due to the changed accounting policy regarding the recognition of tax on financial services (Note 1.25 Comparative data).

7 DIVIDEND INCOME

	Group	
	2018	2017
Held-for-trading securities	10	9
Non-trading securities mandatorily at fair value through profit or loss (IFRS 9)	1,162	/
Securities at fair value through other comprehensive income (IFRS 9)	263	/
Available-for-sale securities (IAS 39)	/	1,579
	1,435	**1,588**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

8 NET FEE AND COMMISSION INCOME

BREAKDOWN BY TYPE OF TRANSACTION

	Abanka		Group	
	2018	2017 (adjusted)	2018	2017 (adjusted)
Fee and commission income				
Payment transactions	18,341	17,776	18,341	17,776
Transaction account management	6,653	6,112	6,645	6,101
Card and ATM operations	20,131	18,478	20,131	18,478
Lending operations and guarantees granted	3,844	3,989	3,837	3,982
Other services	4,258	4,402	4,258	4,405
	53,227	**50,757**	**53,212**	**50,742**
Fee and commission expenses				
Payment transactions	2,247	2,310	2,257	2,312
Card and ATM operations	13,183	11,349	13,183	11,349
Other services	860	718	903	768
	16,290	**14,377**	**16,343**	**14,429**
Net fee and commission income	**36,937**	**36,380**	**36,869**	**36,313**

Comparative data for 2017 were adjusted (decreased) due to the changed accounting policy for the recognition of tax on financial services in the following items of fee and commission income: payment transactions (EUR 1,660 thousand), transaction account management (EUR 550 thousand), card and ATM transactions (EUR 1,623 thousand), lending operations and guarantees granted (EUR 392 thousand) and other services (EUR 67 thousand) (Note 1.25 Comparative data).

9 NET GAINS/LOSSES ON FINANCIAL ASSETS AND LIABILITIES NOT MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS

	Abanka		Group	
	2018	2017	2018	2017
Net gains from financial assets and liabilities at amortised cost (IFRS 9)	18,593	/	18,593	/
Net losses from financial assets and liabilities at amortised cost (IFRS 9)	(364)	/	(364)	/
Net realised gains from available-for-sale financial assets (IAS 39)	/	2,512	/	2,512
Realised losses from loans and other financial assets and liabilities (IAS 39)	/	(3)	/	(3)
Realised gains from loans and other financial assets and liabilities (IAS 39)	/	8,117	/	7,233
	18,229	**10,626**	**18,229**	**9,742**

Net gains realised in 2018 primarily resulted from the gains on the sale of the NPL package.

In 2017, the Bank sold a part of its DUTB bonds, thereby generating a profit of EUR 1,922 thousand within the item net gains from available-for-sale financial assets.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

10 NET GAINS/LOSSES ON FINANCIAL ASSETS AND LIABILITIES HELD FOR TRADING

	Group	
	2018	2017
Foreign exchange transaction gains	1,993	1,197
Net gains from derivatives	597	597
Realised gains/(losses) from trading with:	597	514
– debt securities	597	519
– shares and equity holdings	–	(5)
Unrealised gains from securities held for trading	12	52
	3,199	**2,360**

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

	Group
	2018
Realised gains from equity securities and equity holdings	440
Unrealised losses from equity securities and equity holdings	(951)
Realised gains from loans	97
Unrealised gains from loans	4,759
	4,345

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

12 NET OTHER OPERATING INCOME/EXPENSES

	Abanka		Group	
	2018	2017 (adjusted)	2018	2017 adjusted)
Other operating income				
– income from non-banking services	3	2	3	2
– income from sale of vehicles, real property and other	–	–	1,181	1,402
– other operating income	2,343	992	3,190	1,738
	2,346	**994**	**4,374**	**3,142**
Other operating expenses				
– taxes, contributions and other duties	(36)	(384)	(52)	(442)
– membership fees and similar	(123)	(130)	(129)	(137)
– Single Resolution Fund (SRF)	(682)	(1,117)	(682)	(1,117)
– Deposit Guarantee Fund	(1,641)	(1,524)	(1,641)	(1,524)
– expenses from sale of real property	–	–	(620)	(1,130)
– other operating expenses	(780)	(2,122)	(943)	(2,148)
	(3,262)	**(5,277)**	**(4,067)**	**(6,498)**
Net other operating (expenses)/income	**(916)**	**(4,283)**	**307**	**(3,356)**

Comparative data for 2017 were adjusted (decreased) in the item other operating expenses (eliminated item financial services tax) by EUR 4,613 thousand due to the changed accounting policy regarding the recognition of tax on financial services (Note 1.25 Comparative data).

Other operating income in 2018 also includes realised income from the transfer of brokerage services to Nova KBM d.d. as at the transfer date of 31 December 2018.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

13 ADMINISTRATIVE EXPENSES

	Abanka		Group	
	2018	2017	2018	2017
Staff costs	38,189	38,248	38,878	39,386
– gross salaries	32,505	32,593	33,084	33,554
– social security costs	2,005	2,018	2,042	2,079
– pension costs	3,679	3,581	3,752	3,691
– provisions for employee benefits[1] (Note 34)	–	56	–	62
Professional services	15,397	16,047	15,881	16,652
Advertising and marketing	1,961	1,952	1,983	2,008
Other administrative expenses	1,974	2,201	2,019	2,274
IT and software costs	4,557	5,287	4,557	5,287
Rent payable	1,262	1,107	1,294	1,202
Other costs	458	582	631	817
	63,798	**65,424**	**65,243**	**67,626**

[1] In 2018, expenses for provisions for employee benefits are presented within provisions for employee benefits.

	Abanka		Group	
Amount spent[1] for the auditor of the annual report:	2018	2017	2018	2017
– auditing of the annual report[2]	124	98	135	119
– other assurance services	7	–	7	–
– other non-auditing services	191	51	191	81
– tax advisory services	–	–	–	1
	322	**149**	**333**	**201**

[1] Include amounts paid in each reporting year.
[2] Compared to the previous year, the amount spent for auditing of the annual report was higher due to payment of the review of the transition to IFRS 9 and the different dynamics of payments.

Within the administrative expenses in 2018, EUR 678 thousand referred to the restructuring costs of the Bank (2017: EUR 1,080 thousand) and EUR 578 thousand to the restructuring costs of the Group (2017: EUR 627 thousand).

14 DEPRECIATION AND AMORTISATION

		Abanka		Group	
	Note	2018	2017	2018	2017
Property and equipment	26	3,793	3,979	4,018	4,808
Investment property	26	22	17	336	331
Intangible assets	26	3,420	3,377	3,450	3,420
		7,235	**7,373**	**7,804**	**8,559**

Within the depreciation and amortisation costs in 2018, EUR 571 thousand referred to costs of restructuring (2017: EUR 732 thousand).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

In 2018, the Bank changed the depreciation rate for investments in third-party property and equipment from 3% to 10%. As a result, depreciation expenses in 2018 were higher by EUR 115 thousand. Other depreciation rates did not change in 2018 (there were no changes in depreciation rates in 2017).

15 PROVISIONS

		Abanka		Group	
	Note	2018	2017	2018	2017
Restructuring provisions	34	–	3,673	–	3,673
Provisions for legal proceedings	34, 39	4,460	3,112	4,460	3,112
Provisions for employee benefits	13, 34	32	–	34	–
Other provisions	34	–	(13)	–	(13)
Provisions for guarantees and commitments	34	(4,416)	(1,363)	(4,416)	(1,360)
Net additional provisions		**76**	**5,409**	**78**	**5,412**

A significant part of the income from released provisions for guarantees and commitments of the Group in 2018 relates to service guarantees that were either realised or expired in 2018.

16 IMPAIRMENT

		Abanka		Group	
	Note	2018	2017	2018	2017
Impairment/(reversal of impairment) of financial assets:					
– debt securities at fair value through other comprehensive income (IFRS 9)		113	/	113	/
– loans and receivables at amortised cost (IFRS 9)		(17,875)	/	(17,797)	/
– loans to banks		19	/	19	/
– loans to non-bank customers	2.1.7	(18,104)	/	(18,046)	/
– other financial assets		210	/	230	/
– debt securities at amortised cost (IFRS 9)		138	/	138	/
– loans to non-bank customers (IAS 39)	23	/	(7,015)	/	(4,979)
– other financial assets (IAS 39)		/	192	/	344
Impairment of investments in subsidiaries	27	–	(529)	–	–
Impairment/(reversal of impairment) of non-financial assets:		283	–	(460)	(3,563)
– property and equipment	26	283	–	283	–
– investment property	26	–	–	(172)	(884)
– other non-financial assets		–	–	(571)	(2,679)
		(17,341)	**(7,352)**	**(18,006)**	**(8,198)**

The reversal of impairments for loans to non-bank customers in 2018 was primarily a result of an improved financial position of the companies subject to the financial restructuring process, more optimistic expectations of the Bank regarding future individual loan repayments, regular loan repayment and income from debt collection.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

17 INCOME TAX

	Note	Abanka		Group	
		2018	2017	2018	2017
Current tax		(5,602)	(4,625)	(5,616)	(4,814)
Deferred tax	35	1,127	(590)	1,127	(613)
		(4,475)	**(5,215)**	**(4,489)**	**(5,427)**

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the basic tax rate of the parent as follows:

	Abanka		Group	
	2018	2017	2018	2017
Profit before tax	71,212	47,835	70,081	47,022
Tax calculated at the prescribed tax rate of 19%	(13,530)	(9,089)	(13,315)	(8,934)
19% of tax-exempted income	2,143	878	2,526	1,527
19% of non-deductible expenses	(1,894)	(781)	(2,018)	(1,233)
Tax reliefs and tax loss covering	7,375	5,009	7,375	5,213
	(5,906)	**(3,983)**	**(5,432)**	**(3,427)**
Tax from the transition to IFRS 9, booked to retained earnings	304	–	304	–
Tax from previous years	–	(642)	–	(642)
Effect of not recognised deferred taxes on the tax loss of the current year	–	–	(485)	(741)
Net deferred tax credit/(charge)	1,127	(590)	1,127	(613)
Effect of tax rate differences between states	–	–	(3)	(4)
Total	**(4,475)**	**(5,215)**	**(4,489)**	**(5,427)**

In accordance with local regulations, the tax authorities may at any time inspect the Bank's books and records covering the period of five years subsequent to the reported tax year and may impose additional tax assessments and penalties. In 2015, a tax inspection was initiated, the subject of which was the corporate income tax for the period 1 January 2009 to 31 December 2014. In December 2017, based on the received report on the tax audit findings, tax expenses in the amount of EUR 642 thousand and default interest expenses in the amount of EUR 338 thousand were recognised, while tax losses were reduced by EUR 5,805 thousand. In January 2018, the Bank received a decision on the completion of the tax inspection of corporate income tax, which imposed the tax liability, as established in the report. The procedure is completed.

By completing this procedure, the Bank excluded the tax risk of the uncertain result of tax disputes with the tax authority, as it has no open tax audits.

The effective income tax rate of the Bank for 2018 was 5.80% (2017: 9.56%). The effective income tax rate of the Group for 2018 was 5.89% (2017: 10.17%).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

18 CASH, CASH BALANCES WITH THE CENTRAL BANK AND OTHER DEMAND DEPOSITS WITH BANKS

	Abanka		Group	
	2018	2017	2018	2017
Cash in hand	43,645	38,713	43,645	38,713
Settlement account and obligatory reserve	416,387	296,383	416,387	296,383
Demand deposits with banks	77,237	76,569	78,202	77,072
Total cash, cash balances with the central bank and other demand deposits with banks	**537,269**	**411,665**	**538,234**	**412,168**
Included in cash and cash equivalents (Note 38)	537,269	411,665	538,234	412,168

The balance in the settlement account increased by EUR 120,004 thousand compared to balance as at 31 December 2017, mainly as a result of surplus system liquidity and negative interest rates in the market.

An interest rate analysis of cash, cash balances with the central bank and other demand deposits with banks is disclosed in Note 2.2.3.3. Fair value is disclosed in Note 4.

19 FINANCIAL ASSETS AND LIABILITIES HELD FOR TRADING

	Group	
	2018	2017
Shares	224	217
Derivatives	3,609	2,815
Other	4	16
Total financial assets held for trading	**3,837**	**3,048**
Current	814	593
Non-current	3,023	2,455

An interest rate analysis of financial assets and liabilities held for trading is disclosed in Note 2.2.3.3. Additional information about fair value is disclosed in Note 4.

Derivative financial instruments
The Group uses the following derivative instruments for economic hedging purposes:

Currency forwards represent an obligation to buy or sell a certain amount of a currency in accordance with the provisions of the forward contract.

Foreign currency and interest rate futures are contractual rights and obligations to receive or pay a net amount based on changes in currency rates or interest rates, or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk is negligible, as futures contracts are collateralised by cash or marketable securities, and changes in the futures' contract value are settled daily with the exchange.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted interest rate and the current market rate, based on a notional principal amount.

An **interest rate cap** is an interest rate option in which the buyer has the right (but no obligation) to call upon the issuer (seller) of the option to pay the difference between the strike price and the actual interest rate as at the relevant maturity dates. The purpose of the interest rate cap is to provide a hedge against rising interest rates, for which the buyer pays a premium in advance.

An **interest rate floor** is an interest rate option in which the buyer has the right (but no obligation) to call upon the issuer (seller) of the option to pay the difference between the strike price and the actual interest rate as at the relevant maturity dates. The purpose of the interest rate floor is to provide a hedge against falling interest rates, for which the buyer pays a premium in advance.

An **interest rate collar** is an interest rate option: a combination of purchasing an interest rate cap and selling an interest rate floor.

Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates. No exchange of principal takes place, except for certain currency swaps. The Group's credit risk is the potential cost of replacing the swap contracts if the counterparties fail to perform their obligations. This risk is monitored on an on-going basis with reference to the current fair value, a proportion of the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

Foreign currency options are contractual agreements under which the seller (issuer) grants the buyer (owner) the right, but not the obligation, to buy (call option) or to sell (put option) foreign currency on or by a specified date or within a specified period in accordance with the provisions of the contract (amount, price in a specified amount at a pre-determined rate). The buyer of the option pays and the seller receives a premium to compensate for the currency risk assumed. The Group negotiates foreign currency options with its customers (OTC market). The Group is exposed to credit risk only if it purchases such options and up to their carrying amount that is equal to their fair value.

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised in the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate the Group's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in foreign exchange rates relative to their terms. The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities can fluctuate significantly over time. The fair values of derivative instruments held by the Group are set out as follows.

DERIVATIVES HELD FOR TRADING

	Group		
	Notional contract amount	Fair values	
As at 31 December 2018		Assets	Liabilities
Derivatives held for trading			
Foreign exchange derivatives (OTC):			
– currency forwards	35,774	578	598
– currency swaps	39,139	29	20
Interest rate derivatives (OTC):			
– interest rate swaps	293,215	1,422	843
– OTC interest rate options	104,713	1,580	1,580
Total derivative assets/liabilities held for trading		**3,609**	**3,041**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

As at 31 December 2018, financial liabilities held for trading also included (besides derivatives) spot transactions in the amount of EUR 3 thousand (2017: EUR 23 thousand).

	Group		
	Notional contract amount	Fair values	
As at 31 December 2017		Assets	Liabilities
Derivatives held for trading			
Foreign exchange derivatives (OTC):			
– currency forwards	30,926	358	341
– currency swaps	18,344	–	5
Interest rate derivatives (OTC):			
– interest rate swaps	138,026	431	97
– OTC interest rate options	77,884	2,026	2,026
Total derivative assets/liabilities held for trading		**2,815**	**2,469**

20 NON-TRADING FINANCIAL ASSETS MANDATORILY AT FAIR VALUE THROUGH PROFIT OR LOSS (IFRS 9)

	Group
	2018
Shares and equity holdings	12,166
Loans	24,421
Total non-trading financial assets mandatorily at fair value through profit or loss	**36,587**
Current	14,642
Non-current	21,945

Additional information about fair value is disclosed in Note 4.

21 FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME (IFRS 9)

	Group
	2018
Debt securities	132,393
Shares	3,143
Equity holdings*	3,213
Bank Resolution Fund	24,717
Total financial assets at fair value through other comprehensive income	**163,466**
Current	52,597
Non-current	110,869

* investments in limited liability companies

Additional information about fair value is disclosed in Note 4.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

	Group
	2018
Gross debt securities	132,515
Loss allowance	(122)
Net debt securities	**132,393**

MOVEMENTS IN EQUITY SECURITIES ARE AS FOLLOWS:

	Group
	2018
As at 1 January	**30,791**
Derecognition	(26)
Valuation	308
As at 31 December	**31,073**

Derecognition of a part of one minor investment was a result of the issuer's rules regarding the maintenance of ownership relations.

22 AVAILABLE-FOR-SALE FINANCIAL ASSETS (IAS 39)

	Group
	2017
Debt securities	**1,044,721**
Treasury bills	28,034
Other debt securities	1,016,687
Shares and equity holdings	**21,235**
Equity holdings	3,459
Shares	17,776
Bank Resolution Fund	**24,734**
Total available-for-sale financial assets	**1,090,690**
Current	154,621
Non-current	936,069

23 FINANCIAL ASSETS AT AMORTISED COST (IFRS 9)

	Abanka	Group
	2018	2018
Debt securities (23 a.)	946,334	946,334
Loans to banks (23 b.)	30,784	30,784
Loans to non-bank customers (23 c.)	1,934,862	1,928,338
Other financial assets (23 d.)	12,538	12,706
	2,924,518	**2,918,162**

Fair value is disclosed in Note 4.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

a. Debt securities

	Group
	2018
Gross debt securities	946,610
Loss allowance	(276)
Net debt securities	**946,334**
Current	194,053
Non-current	752,281

b. Loans to banks

	Group
	2018
Gross loans to banks	30,816
Loss allowance	(32)
Net loans to banks	**30,784**
Current	20,857
Non-current	9,927
Included in cash and cash equivalents (Note 38)	19,734

c. Loans to non-bank customers

	Abanka	Group
	2018	2018
Loans to corporate entities	1,084,350	1,082,811
Loans to retail customers	917,558	917,658
Gross loans to non-bank customers	**2,001,908**	**2,000,469**
Loss allowance	(67,046)	(72,131)
Net loans to non-bank customers	**1,934,862**	**1,928,338**
Current	248,081	239,851
Non-current	1,686,781	1,688,487

Receivables for interest are recognised together with the underlying financial instrument.

Compared to 31 December 2017 (Note 24 b.), gross loans to corporate entities decreased primarily due to the sale of the NPL portfolio and the transition to IFRS 9 (adjustment of credit-impaired financial assets, i.e. POCI, to fair value and reclassification of part of loans into mandatorily measured at fair value).

The Group accepted listed securities at a fair value of EUR 11,595 thousand (2017: EUR 16,712 thousand) as collateral for loans, which it is permitted to sell or re-pledge.

The table of movements in loss allowance is presented in Section 2.1.7 Movements in loss allowance and provisions.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

MOVEMENTS IN LOANS TEMPORARILY WRITTEN OFF AND HELD IN OFF-BALANCE-SHEET RECORDS ARE AS FOLLOWS:

	Group		
	Corporate entities	Retail customers	Total
As at 1 January 2018	**222,128**	**7,570**	**229,698**
Increase	1,636	823	2,459
Decrease due to final write-offs – completion of the collection process	(2,847)	(868)	(3,715)
Decrease due to repayments, sale, debt to equity	(156,135)	(266)	(156,401)
As at 31 December 2018	**64,782**	**7,259**	**72,041**

In 2018, temporarily written-off loans held in off-balance-sheet records decreased by EUR 148,070 thousand due to the sale of the NPL portfolio.

Loans assessed (as described in Note 1.5) as unrecoverable by the Group were removed from the statement of financial position, but are kept in the off-balance-sheet records until the legal basis for the completion of the collection process has been obtained.

Loans to banks and non-bank customers are further analysed in the following notes: Credit risk (Note 2.1), Foreign exchange risk (Note 2.2.2), Interest rate risk (Note 2.2.3), Liquidity risk (Note 2.3), Fair value (Note 4) and Related-party transactions (Note 42).

Loans to non-bank customers also include finance lease receivables as disclosed in Note 40 Leases.

d. Other financial assets

	Abanka	Group
	2018	2018
Gross other financial assets, of which:	12,846	13,185
– receivables from customers	11	337
– receivables from card and ATM operations	5,512	5,512
– receivables from settlements	1,795	1,795
– other receivables	5,528	5,541
Loss allowance	(308)	(479)
Net other financial assets	**12,538**	**12,706**
Current	11,999	12,155
Non-current	539	551

24 LOANS AND RECEIVABLES (IAS 39)

	Abanka	Group
	2017	2017
Loans to banks (24 a.)	60,745	60,745
Loans to non-bank customers (24 b.)	1,982,137	1,967,460
Other financial assets (24 c.)	23,661	23,917
	2,066,543	**2,052,122**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

a. Loans to banks

	Group
	2017
Placements with other banks	–
Loans and deposits to other banks	60,745
Gross loans to banks	**60,745**
Loss allowance	–
Net loans to banks	**60,745**
Current	49,965
Non-current	10,780
Included in cash and cash equivalents (Note 38)	48,242

b. Loans to non-bank customers

	Abanka	Group
	2017	2017
Loans to corporate entities	1,327,572	1,298,765
Loans to retail customers	863,151	885,658
Gross loans to non-bank customers	**2,190,723**	**2,184,423**
Loss allowance	(208,586)	(216,963)
Net loans to non-bank customers	**1,982,137**	**1,967,460**
Current	488,785	446,289
Non-current	1,493,352	1,521,171

MOVEMENTS IN LOANS TEMPORARILY WRITTEN OFF AND HELD IN OFF-BALANCE-SHEET RECORDS ARE AS FOLLOWS:

	Group		
	Corporate entities	Retail customers	Total
As at 1 January 2017	**244,850**	**10,855**	**255,705**
Increase	26,910	1,145	28,055
Decrease due to final write-offs – completion of the collection process	(40,209)	(3,992)	(44,201)
Decrease due to repayments, sale, debt to equity	(9,423)	(438)	(9,861)
As at 31 December 2017	**222,128**	**7,570**	**229,698**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

c. Other financial assets

	Abanka	Group
	2017	2017
Receivables from customers	13	254
Receivables from card and ATM operations	6,035	6,035
Receivables from settlements	10,467	10,467
Other receivables	7,146	7,161
Total other financial assets	**23,661**	**23,917**
Current	23,132	23,395
Non-current	529	522

25 HELD-TO-MATURITY INVESTMENTS (IAS 39)

	Group
	2017
Debt securities – at amortised cost	**15,408**
Current	5,161
Non-current	10,247

In 2017, the Group did not reclassify any financial assets out of held-to-maturity investments.
Debt securities had fixed interest rates.

An interest rate analysis of held-to-maturity investments is additionally disclosed in Note 2.2.3.3. Fair value is disclosed in Note 4.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

26 PROPERTY AND EQUIPMENT, INVESTMENT PROPERTY, INTANGIBLE ASSETS AND NON-CURRENT ASSETS HELD FOR SALE – ABANKA

	Land and buildings	Computers	Other equipment	Assets under construction	**Total property and equipment**	**Investment property**	**Intangible assets**	**Non-current assets held for sale**
Cost								
As at 1 January 2017	**76,758**	**29,494**	**19,060**	**608**	**125,920**	**513**	**40,037**	**1,975**
Additions	493	1,176	608	(470)	1,807	–	2,823	–
Transfer between groups	(104)	–	–	–	(104)	104	–	–
Disposals	(115)	(5,274)	(624)	–	(6,013)	–	(5,760)	–
As at 31 December 2017	**77,032**	**25,396**	**19,044**	**138**	**121,610**	**617**	**37,100**	**1,975**
Depreciation								
As at 1 January 2017	**45,494**	**26,438**	**15,290**	**–**	**87,222**	**348**	**32,005**	**1,169**
Depreciation and amortisation (Note 14)	1,756	1,599	624	–	3,979	17	3,377	–
Transfer between groups	(68)	–	–	–	(68)	68	–	–
Disposals	(24)	(5,118)	(609)	–	(5,751)	–	(5,536)	–
As at 31 December 2017	**47,158**	**22,919**	**15,305**	**–**	**85,382**	**433**	**29,846**	**1,169**
Net book amount as at 31 December 2017	**29,874**	**2,477**	**3,739**	**138**	**36,228**	**184**	**7,254**	**806**
Cost								
As at 1 January 2018	**77,032**	**25,396**	**19,044**	**138**	**121,610**	**617**	**37,100**	**1,975**
Additions	512	833	347	93	1,785	–	5,130	–
Transfer between groups	(4,752)	–	–	–	(4,752)	147	–	4,605
Disposals	(404)	(3,167)	(1,698)	–	(5,269)	–	(4,604)	(5,134)
Impairment (Note 16)	(333)	–	–	–	(333)	–	–	–
As at 31 December 2018	**72,055**	**23,062**	**17,693**	**231**	**113,041**	**764**	**37,626**	**1,446**
Depreciation								
As at 1 January 2018	**47,158**	**22,919**	**15,305**	**–**	**85,382**	**433**	**29,846**	**1,169**
Depreciation and amortisation (Note 14)	1,852	1,433	508	–	3,793	22	3,420	–
Transfer between groups	(4,072)	–	–	–	(4,072)	108	–	3,964
Disposals	(163)	(3,030)	(1,651)	–	(4,844)	–	(4,570)	(4,175)
Impairment (Note 16)	(50)	–	–	–	(50)	–	–	–
As at 31 December 2018	**44,725**	**21,322**	**14,162**	**–**	**80,209**	**563**	**28,696**	**958**
Net book amount as at 31 December 2018	**27,330**	**1,740**	**3,531**	**231**	**32,832**	**201**	**8,930**	**488**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

PROPERTY AND EQUIPMENT, INVESTMENT PROPERTY, INTANGIBLE ASSETS AND NON-CURRENT ASSETS HELD FOR SALE – THE GROUP

	Land and buildings	Computers	Other equipment	Assets under construction	**Total property and equipment**	**Investment property**	**Intangible assets**	**Non-current assets held for sale**
Cost								
As at 1 January 2017	**77,293**	**29,494**	**23,111**	**608**	**130,506**	**9,735**	**40,581**	**2,142**
Additions	493	1,176	1,463	(470)	2,662	549	2,831	–
Disposals	(116)	(5,274)	(1,331)	–	(6,721)	(2,377)	(5,761)	(1,143)
Impairment (Note 16)	–	–	–	–	–	884	–	–
Transfer between groups	–	–	–	–	–	(576)	–	520
Transfer from inventories	–	–	–	–	–	–	–	721
As at 31 December 2017	**77,670**	**25,396**	**23,243**	**138**	**126,447**	**8,215**	**37,651**	**2,240**
Depreciation								
As at 1 January 2017	**45,763**	**26,438**	**16,575**	**–**	**88,776**	**1,035**	**32,341**	**1,169**
Depreciation and amortisation (Note 14)	1,774	1,599	1,435	–	4,808	331	3,420	–
Disposals	(25)	(5,118)	(957)	–	(6,100)	(117)	(5,537)	–
Transfer between groups	–	–	–	–	–	(56)	–	–
As at 31 December 2017	**47,512**	**22,919**	**17,053**	**–**	**87,484**	**1,193**	**30,224**	**1,169**
Net book amount as at 31 December 2017	**30,158**	**2,477**	**6,190**	**138**	**38,963**	**7,022**	**7,427**	**1,071**
Cost								
As at 1 January 2018	**77,670**	**25,396**	**23,243**	**138**	**126,447**	**8,215**	**37,651**	**2,240**
Additions	512	833	943	93	2,381	175	5,157	–
Disposals	(404)	(3,167)	(1,932)	–	(5,503)	(981)	(4,609)	(5,399)
Impairment (Note 16)	(333)	–	–	–	(333)	172	–	–
Disposal of subsidiary	(212)	–	(4,500)	–	(4,712)	–	(324)	–
Transfer between groups	(4,605)	–	–	–	(4,605)	(205)	–	4,791
Transfer from inventories	–	–	–	–	–	212	–	4,328
Transfer to inventories	–	–	–	–	–	(1,843)	–	–
As at 31 December 2018	**72,628**	**23,062**	**17,754**	**231**	**113,675**	**5,745**	**37,875**	**5,960**
Depreciation								
As at 1 January 2018	**47,512**	**22,919**	**17,053**	**–**	**87,484**	**1,193**	**30,224**	**1,169**
Depreciation and amortisation (Note 14)	1,871	1,433	714	–	4,018	336	3,450	–
Disposals	(163)	(3,030)	(1,772)	–	(4,965)	(72)	(4,575)	(4,175)
Impairment (Note 16)	(50)	–	–	–	(50)	–	–	–
Disposal of subsidiary	(140)	–	(1,780)	–	(1,920)	–	(298)	–
Transfer between groups	(3,964)	–	–	–	(3,964)	(19)	–	3,964
Transfer to inventories	–	–	–	–	–	(117)	–	–
As at 31 December 2018	**45,066**	**21,322**	**14,215**	**–**	**80,603**	**1,321**	**28,801**	**958**
Net book amount as at 31 December 2018	**27,562**	**1,740**	**3,539**	**231**	**33,072**	**4,424**	**9,074**	**5,002**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

All investment property generates income and expenses. There was EUR 46 thousand of rental income from investment property (2017: EUR 37 thousand) and EUR 23 thousand of direct expenses recognised in the income statement of the Bank in 2018 (2017: EUR 17 thousand). In 2018, the Bank's income from other operating leases totalled EUR 68 thousand (2017: EUR 83 thousand).

The Group recognised EUR 674 thousand of rental income from investment property (2017: EUR 638 thousand) and EUR 337 thousand of direct expenses in the consolidated income statement in 2018 (2017: EUR 332 thousand). In 2018, the Group's income from other operating leases totalled EUR 266 thousand (2017: EUR 986 thousand). As at 31 December 2018, the fair value of investment property approximates the carrying amount. The Group holds a building right on one of the investment properties. The assets are free of encumbrance.

27 INVESTMENTS IN SUBSIDIARIES

	Abanka	
	2018	**2017**
Subsidiaries		
As at 1 January	**9,448**	**4,483**
Additions	–	4,436
Disposals	(1,170)	–
Impairment (Note 16)	–	529
As at 31 December	**8,278**	**9,448**

SUBSIDIARIES

2018 Name	Carrying amount of investment	Assets	Liabilities	Equity	Revenues	Net profit	% Interest held
Anepremičnine Group (Slovenia)	8,278	22,013	12,607	9,406	6,807	213	100

2018 Name	Country of incorporation	Assets	Liabilities	Equity	Revenues	Net profit/ (loss)	% Interest held
Anepremičnine Group							
Anepremičnine d.o.o.	Slovenia	18,974	9,537	9,437	6,791	197	100
Anekretnine d.o.o.	Montenegro	4,782	4,773	9	75	(24)	100

In 2018, the subsidiary Anepremičnine d.o.o. increased the share capital of its subsidiary Anekretnine d.o.o. in an amount of EUR 30 thousand. In the same year, the subsidiary Anepremičnine d.o.o. made an impairment of its equity stake in its subsidiary Anekretnine d.o.o. in the amount of EUR 40 thousand.

In 2018, the subsidiary Anepremičnine sold a part of due receivables from finance lease contracts.

In 2018, the Bank transferred a part of its NPL portfolio in the amount of EUR 4,096 thousand to the newly established subsidiary Ahive d.o.o. in accordance with the draft terms of division, which were adopted by the Management Board on 28 May 2018 and approved by the General Meeting of Shareholders of Abanka on 21 September 2018; the spin-off was entered into the Companies Register on 22 October 2018. The balance sheet date was 31 December 2017. When a new subsidiary was established, the NPL portfolio was transferred to non-current assets held for sale. The transfer of the shareholding in Ahive d.o.o. to the buyer DDM Invest I AG took place on 26 October 2018, thereby executing the arrangement entered into by concluding the Receivables Sale Agreement with the said buyer on 21 March 2018.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

2017 Name	Carrying amount of investment	Assets	Liabilities	Equity	Revenues	Net profit	% Interest held
Aleasing d.o.o. (Slovenia)	1,170	36,769	34,292	2,477	3,975	449	100
Anepremičnine Group (Slovenia)	8,278	28,891	19,700	9,191	12,856	122	100

2017 Name	Country of incorporation	Assets	Liabilities	Equity	Revenues	Net profit/ (loss)	% Interest held
Anepremičnine Group							
Anepremičnine d.o.o.	Slovenia	28,185	18,948	9,237	12,869	162	100
Anekretnine d.o.o.	Montenegro	4,318	4,315	3	78	(40)	100

On 18 July 2017, Abanka d.d. signed an agreement with Banka Sparkasse d.d., Ljubljana to sell its 100% stake in its subsidiary Aleasing d.o.o., Ljubljana. The Agreement stipulates that the stake will be transferred to the buyer after the fulfilment of the suspensive conditions, which inter alia included obtaining the relevant approvals of the supervisory authorities. At the end of March 2018, Abanka d.d. as seller and Banka Sparkasse d.d. as buyer of Aleasing d.o.o. confirmed, that all suspensive conditions, required for the conclusion of the sales procedure, were fulfilled. In accordance with the agreement on sale, as of 1 April 2018 the equity stake was held by the buyer who as of that date became the owner of Aleasing d.o.o., Ljubljana.

In both agreements on the sale of the subsidiaries Afaktor d.o.o. and Aleasing d.o.o., the Bank committed to the buyer that within a certain period after the sale it would settle all potential contingent liabilities which might arise from certain business events incurred before the closing of the sale of Afaktor and Aleasing.

Due to the immateriality in the financial statements, the subsidiary Aleasing was not reclassified into non-current assets held for sale category. In the consolidated statement of financial position, the assets of the subsidiary Aleasing as at 31 March 2018 amounted to EUR 38,984 thousand, which accounted for 1.04% of consolidated assets, and its liabilities totalled EUR 36,392 thousand, which accounted for 1.14% of consolidated liabilities. In the consolidated income statement, the net profit of Aleasing equalled EUR 115 thousand, accounting for 0.46% of consolidated net profit, its income totalled EUR 1,021 thousand (1.29% of total consolidated income) and its expenses amounted to EUR 906 thousand (1.70% of total consolidated expenses).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

ANALYSIS OF ASSETS AND LIABILITIES OVER WHICH CONTROL WAS LOST

2018	Aleasing d.o.o.
Demand deposits with banks	1,360
Financial assets at amortised cost	34,381
– loans to banks	13
– loans to non-bank customers	34,211
– other financial assets	157
Property and equipment	2,792
Intangible assets	26
Tax assets	85
Other assets	340
Total assets	**38,984**
Financial liabilities measured at amortised cost	35,406
– loans from banks	35,048
– other financial liabilities	358
Provisions	75
Tax liabilities	15
Other liabilities	896
Total liabilities	**36,392**
Net assets disposed of	**2,592**

GAIN/(LOSS) ON DISPOSAL OF A SUBSIDIARY

2018	Abanka	Group
Consideration received	1,477	1,477
Carrying amount of the investment in subsidiary	1,170	–
Net assets disposed of	–	(2,592)
Gain/(loss) on disposal	**307**	**(1,115)**

NET CASH INFLOW ON DISPOSAL OF A SUBSIDIARY

2018	Group
Consideration received in cash and cash equivalents	1,477
Less: cash and cash equivalent balances disposed of	(1,360)
Net cash inflow on disposal	**117**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

28 OTHER ASSETS

	Abanka		Group	
	2018	2017	2018	2017
Inventories of material and small tools	10	9	10	9
Other inventories (real properties)	148	96	6,775	10,737
Precious metals	1,118	1,304	1,118	1,304
Deferred costs	433	516	442	524
Prepaid taxes	17	12	583	625
Prepayments	356	365	531	763
Total other assets (current)	**2,082**	**2,302**	**9,459**	**13,962**

29 PLEDGED ASSETS

	Group	
	2018	2017
Loans to banks	7,697	8,847
Financial assets at amortised cost	17,985	/
Financial assets at fair value through other comprehensive income	4,320	/
Available-for-sale financial assets	/	23,593
Obligatory reserve	27,309	26,366
Financial assets of the Bank pledged for Bank's liabilities	16,491	15,447
Other financial assets	89	55
Total pledged assets	**73,891**	**74,308**

Assets are pledged as collateral for Eurosystem (ECB) claims, claims from VISA and Mastercard card transactions, claims by counterparties arising from derivatives, to provide liquid assets of the Bank Resolution Fund (pursuant to the Bank Resolution Authority and Fund Act – ZOSRB), to ensure obligatory reserves on the cash account with the Bank of Slovenia and for collateral paid to clearing systems (SEPA IKP, SEPA EKP, SEPA IDD CORE and SEPA IDD B2B) and KDD.

Due to the amended definition of encumbered assets, the comparative data for 2017 were adjusted, as originally only loans to banks in the amount of EUR 8,847 thousand were reported.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

30 DEPOSITS AND LOANS FROM BANKS AND THE CENTRAL BANK

All deposits from banks had remaining maturities up to 12 months and fixed interest rates in 2018 (EUR 16,335 thousand) and 2017 (EUR 24,243 thousand).

LOANS FROM BANKS AND THE CENTRAL BANK

	Group	
	2018	2017
Loans from banks	102,788	89,011
Loans from the central bank	–	–
Total loans from banks and the central bank	**102,788**	**89,011**
Current	1,293	16,143
Non-current	101,495	72,868

Fixed and variable interest rate loans from banks and the central bank accounted for 10.6% (2017: 14.5%) and 89.4% (2017: 85.5%) of the total, respectively.

An interest rate analysis of deposits and loans from banks and the central bank is additionally disclosed in Note 2.2.3.3. Fair value is disclosed in Note 4.

Deposits and loans from banks and the central bank are further analysed as part of the statement of financial position in the following notes: Foreign exchange risk (Note 2.2.2), Interest rate risk (Note 2.2.3), Liquidity risk (Note 2.3), Fair value (Note 4) and Related-party transactions (Note 42).

31 DEPOSITS FROM NON-BANK CUSTOMERS

	Abanka		Group	
	2018	2017	2018	2017
Deposits from corporate entities	847,601	879,072	846,831	873,919
Deposits from retail customers	2,087,617	1,981,625	2,087,617	1,981,625
Total deposits from non-bank customers	**2,935,218**	**2,860,697**	**2,934,448**	**2,855,544**
Current	2,847,236	2,726,423	2,846,466	2,721,270
Non-current	87,982	134,274	87,982	134,274

Fixed and variable interest rate deposits from non-bank customers accounted for 79.6% (2017: 81.3%) and 20.4% (2017: 18.7%) of the total, respectively.

Bank deposits provided as collateral for loans granted in 2018 totalled EUR 11,216 thousand (2017: EUR 14,993 thousand).

An interest rate analysis of deposits from non-bank customers is additionally disclosed in Note 2.2.3.3. Fair value is disclosed in Note 4.

Deposits from non-bank customers are further analysed as part of the statement of financial position in the following notes: Foreign exchange risk (Note 2.2.2), Interest rate risk (Note 2.2.3), Liquidity risk (Note 2.3), Fair value (Note 4) and Related-party transactions (Note 42).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

32 DEBT SECURITIES ISSUED

	Interest rate on 31 December	Group	
		2018	2017
Certificates of deposit (falling due: 2019 to 2020)	5.95%	13,644	13,021
Other securities issued		–	–
Total debt securities issued		**13,644**	**13,021**
Current		397	379
Non-current		13,247	12,642

33 OTHER FINANCIAL LIABILITIES

	Abanka		Group	
	2018	2017	2018	2017
Liabilities from card operations	1,300	875	1,300	875
Liabilities to suppliers	1,673	1,298	1,756	1,680
Liabilities for unexecuted payments	1,780	4,243	1,780	4,243
Liabilities for salaries	2,879	3,008	2,921	3,107
Accrued costs	6,098	4,426	6,127	4,443
Other financial liabilities	7,868	12,315	7,948	12,324
Total other financial liabilities	**21,598**	**26,165**	**21,832**	**26,672**
Current	21,445	26,024	21,665	26,621
Non-current	153	141	167	51

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

34 PROVISIONS

ABANKA

	Restructuring provisions	Provisions for legal proceedings	Provisions for employee benefits	Provisions for guarantees and commitments	Other provisions	Total
As at 1 January 2017	**4,382**	**9,932**	**5,307**	**31,008**	**163**	**50,792**
Additional/(released) provisions through profit or loss (Note 13 and 15)	3,673	3,112	56	(1,363)	(13)	5,465
Additional provisions through equity – actuarial losses	/	/	135	/	/	135
Utilised during the year	(1,815)	(673)	(77)	(1)	(150)	(2,716)
As at 31 December 2017	**6,240**	**12,371**	**5,421**	**29,644**	**–**	**53,676**
Transition to IFRS 9 (Note 44)	/	/	/	(10,303)	/	(10,303)
As at 1 January 2018	**6,240**	**12,371**	**5,421**	**19,341**	**–**	**43,373**
Additional/(released) provisions through profit or loss (Note 15)	–	4,460	32	(4,416)	4,678	4,754
Additional provisions through equity – actuarial losses	/	/	29	/	/	29
Utilised during the year	(1,808)	(168)	(110)	(2)	(9)	(2,097)
As at 31 December 2018	**4,432**	**16,663**	**5,372**	**14,923**	**4,669**	**46,059**

GROUP

	Restructuring provisions	Provisions for legal proceedings	Provisions for employee benefits	Provisions for guarantees and commitments	Other provisions	Total
As at 1 January 2017	**4,382**	**9,932**	**5,416**	**30,998**	**163**	**50,891**
Additional/(released) provisions through profit or loss (Note 13 and 15)	3,673	3,112	62	(1,360)	(13)	5,474
Additional provisions through equity – actuarial losses	/	/	147	/	/	147
Utilised during the year	(1,815)	(673)	(77)	(1)	(150)	(2,716)
As at 31 December 2017	**6,240**	**12,371**	**5,548**	**29,637**	**–**	**53,796**
Transition to IFRS 9 (Note 44)	/	/	/	(10,296)	/	(10,296)
As at 1 January 2018	**6,240**	**12,371**	**5,548**	**19,341**	**–**	**43,500**
Sale of subsidiary Aleasing (Note 27)	–	–	(75)	–	–	(75)
Additional/(released) provisions through profit or loss (Note 15)	–	4,460	34	(4,416)	4,678	4,756
Additional provisions through equity – actuarial losses	/	/	27	/	/	27
Utilised during the year	(1,808)	(168)	(112)	(2)	(9)	(2,099)
As at 31 December 2018	**4,432**	**16,663**	**5,422**	**14,923**	**4,669**	**46,109**

NOTES TO THE FINANCIAL STATEMENTS (continued)

Provisions for retirement benefits and jubilee payments were set aside by the Group as at 31 December 2018. The calculation is based on the following key assumptions:
- a discount rate of 1.89% (2017: 1.31%),
- a staff fluctuation rate of 2.97% (2017: 2.83%),
- average salary growth: 2.39% per annum (2017: 1.58%).

Employees are also entitled to jubilee payments for every decade of service in the Group.

In 2018, the Bank sold the NPL portfolio and formed provisions for certain guarantees given to the buyer in the amount of EUR 4,678 thousand (other provisions).

35 DEFERRED INCOME TAX

Deferred income tax is calculated on all temporary differences under the liability method using effective tax rates according to the tax rate valid in the year the elimination of temporary differences is projected, i.e. 19% or up to the amount recoverable against future profits.

The tax base reduction due to unused tax losses is permitted to a maximum of 50% of the tax base for the current period. In 2018, the tax loss from previous years amounting to EUR 34,948 thousand was used in the corporate tax return of the Bank.

As at 31 December 2018, the unused tax losses for which deferred tax assets were not recognised in the statement of financial position amounted to EUR 720,814 thousand for the Bank and EUR 728,956 thousand for the Group. Total tax loss of the Bank amounted to EUR 766,288 thousand (2017: EUR 801,236 thousand), while for the Group it equaled EUR 774,430 thousand (2017: EUR 812,846 thousand). In accordance with the Slovene Corporate Income Tax Act, the tax losses can be carried forward indefinitely.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

MOVEMENTS IN THE DEFERRED INCOME TAX ACCOUNT ARE AS FOLLOWS:

	Abanka				Group			
	2017	Transition to IFRS 9	Movement	2018	2017	Transition to IFRS 9	Movement	2018
Deferred income tax assets								
Impairment of equity investments	709	/	(709)	–	709	/	(709)	–
Impairment of property and equipment, investment property and intangible assets	93	/	–	93	93	/	–	93
Provisions for employee benefits	635	/	(10)	625	635	/	(10)	625
Restructuring provisions	593	/	(172)	421	593	/	(172)	421
Impairments on loans and receivables (sale of subsidiary Aleasing in 2018)	–	/	–	–	47	/	(47)	–
Impairment of equity securities at fair value through profit or loss (before transition to IFRS 9: available for sale)	–	/	393	393	–	/	393	393
Impairments of debt securities at amortised cost (IFRS 9)	/	28	24	52	/	28	24	52
Tax losses carried forward	7,055	/	1,586	8,641	7,055	/	1,586	8,641
	9,085	**28**	**1,112**	**10,225**	**9,132**	**28**	**1,065**	**10,225**
Deferred income tax liabilities								
Debt securities at fair value through other comprehensive income (IFRS 9)	/	861	(131)	730	/	861	(131)	730
Different depreciation rates for accounting and tax purposes	98	/	6	104	98	/	6	104
Available-for-sale securities (IAS 39)	5,862	(5,862)	/	/	5,862	(5,862)	/	/
	5,960	**(5,001)**	**(125)**	**834**	**5,960**	**(5,001)**	**(125)**	**834**

INCLUDED IN THE INCOME STATEMENT:

		Abanka		Group	
	Note	2018	2017	2018	2017
Impairment of equity securities at fair value through profit or loss (IFRS 9)		393	/	393	/
Available-for-sale securities (IAS 39)		/	(269)	/	(269)
Impairment of debt securities at amortised cost (IFRS 9)		24	/	24	/
Impairment of debt securities at fair value through other comprehensive income (IFRS 9)		21	/	21	/
Impairment of equity investments		(709)	(101)	(709)	(101)
Different depreciation rates for accounting and tax purposes		(6)	(10)	(6)	(10)
Provisions for employee benefits		(10)	(3)	(10)	(3)
Restructuring provisions		(172)	177	(172)	177
Impairment on loans and receivables		–	–	–	(23)
Tax losses carried forward		1,586	(384)	1,586	(384)
	17	**1,127**	**(590)**	**1,127**	**(613)**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

INCLUDED IN EQUITY:

	Group	
	2018	**2017**
Securities at fair value through other comprehensive income - unrealised gains (IFRS 9)	430	/
Securities at fair value through other comprehensive income - unrealised losses (IFRS 9)	(320)	/
Available-for-sale securities – unrealised gains (IAS 39)	/	3,147
Available-for-sale securities – unrealised losses (IAS 39)	/	(1,035)
	110	**2,112**

36 SHARE CAPITAL, SHARE PREMIUM, ACCUMULATED OTHER COMPREHENSIVE INCOME AND RESERVES FROM PROFIT

2018	Share
The Republic of Slovenia	100%

2017	Share
The Republic of Slovenia	100%

The amounts of the share capital and share premium are equal for the Bank and the Group.

As at 31 December 2018, accumulated other comprehensive income of the Bank amounted to EUR 3,333 thousand arising from the valuation of financial assets, measured at fair value through other comprehensive income of EUR 3,689 thousand and actuarial losses on provisions for retirement benefits of EUR 356 thousand.

As at 31 December 2017, accumulated other comprehensive income of the Bank amounted to EUR 33,317 thousand arising from the valuation of financial assets available for sale of EUR 33,642 thousand and actuarial losses on provisions for retirement benefits of EUR 325 thousand.

As at 31 December 2018, accumulated other comprehensive income of the Group to the amount of EUR 3,332 thousand refers to the valuation of financial assets, measured at fair value through other comprehensive income, which totalled EUR 3,689 thousand and actuarial losses on provisions for retirement benefits to the amount of EUR 357 thousand.

As at 31 December 2017, accumulated other comprehensive income of the Group to the amount of EUR 33,284 thousand refers to the valuation of available-for-sale financial assets, which totalled EUR 33,642 thousand and actuarial losses on provisions for retirement benefits to the amount of EUR 358 thousand.

Share premium consists of payments exceeding the nominal amounts of paid-in shares (paid-in surplus) in the amount of EUR 277,296 thousand and amounts from the simplified share capital reduction through the withdrawal of shares (Banka Celje) in the amount of EUR 5,163 thousand.

Reserves from profit include legal reserves, statutory reserves and other reserves from profit. In the past, the Group created legal reserves in accordance with the Companies Act.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

RESERVES FROM PROFIT

	Abanka		Group	
	2018	2017	2018	2017
Legal reserves	16,213	16,213	16,230	16,263
Statutory reserves	22,879	16,205	22,879	16,205
Other reserves from profit	19,292	19,292	19,292	19,292
Total reserves from profit	**58,384**	**51,710**	**58,401**	**51,760**

Share premium, legal and statutory reserves may be used for covering loss after tax for the year, if it cannot be covered from retained earnings or other reserves from profit.

37 PROPOSED TREATMENT OF DISTRIBUTABLE PROFIT

	Abanka	
	2018	2017
Net profit from the current year	66,737	42,620
Distribution of net profit from the current year:		
– for statutory reserves	(6,674)	(4,262)
– for other reserves from profit	–	–
Retained earnings	28,145	22,099
Distributable profit	**88,208**	**60,457**
– for dividend payments	66,737	42,620
– distributable profit - unappropriated	21,471	17,837

The Bank paid out dividends for 2017 to the sole shareholder, i.e. the Republic of Slovenia, in the amount of EUR 42,620 thousand on 29 May 2018.

The allocation of distributable profit is subject to a decision by the Bank's Annual General Meeting.

38 CASH FLOW STATEMENT

The indirect method was used to prepare the cash flow statement.

CASH AND CASH EQUIVALENTS

	Abanka		Group	
	2018	2017	2018	2017
Cash, cash balances with the central bank and other demand deposits with banks (Notes 1.15 and 18)	537,269	411,665	538,234	412,168
Loans to banks (Notes 1.15, 23 and 24)	19,734	48,242	19,734	48,242
	557,003	**459,907**	**557,968**	**460,410**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

CASH FLOWS FROM INTEREST AND DIVIDENDS

	Abanka		Group	
	2018	2017	2018	2017
Interest paid	5,591	7,604	5,591	7,604
Interest received	87,539	91,621	88,366	94,063
Dividends received	1,435	1,588	1,435	1,588

OTHER ITEMS IN THE CASH FLOW STATEMENT

In 2018, other gains from investing activities of the Bank and the Group totalling EUR 10,941 thousand related to debt securities measured at amortised cost (EUR 8,938 thousand) and non-current assets held for sale (EUR 2,003 thousand).

In 2017, other gains from investing activities of the Bank totalling EUR 802 thousand and of the Group totalling EUR 964 thousand related to held-to-maturity investments (EUR 799 thousand) and non-current assets held for sale (the Bank EUR 3 thousand, the Group EUR 165 thousand).

Other adjustments to total profit or loss before tax relate to net provisions, gains from non-trading financial assets mandatorily at fair value through profit or loss, losses on financial assets and liabilities designated at fair value through profit or loss and realised losses on loans at amortised cost.

NOTES TO THE FINANCIAL STATEMENTS (continued)

39 COMMITMENTS AND CONTINGENCIES

a) *Legal proceedings*

As at 31 December 2018, the Group and the Bank were involved as defendants in several judicial proceedings and other disputes. The total amount of pecuniary claims filed against the Bank on the reporting date stood at EUR 21,712 thousand excluding default interest (as at 31 December 2017: EUR 23,227 thousand) and against the Group EUR 22,226 thousand (as at 31 December 2017: EUR 23,630 thousand). Based on the assessment of the likely outcome of disputes, respective provisions were made (Note 34).

In the field of intellectual property rights, the Bank is involved in several disputes brought against it by ABANCA CORPORACION BANCARIA S.A. from Spain, who is seeking the annulment of two international brands ABANKA no. 860 632 and no. 860 561. Proceedings have been initiated in Spain, Austria, France, the United Kingdom, Germany, Switzerland, Croatia, Portugal and Hungary, with the claimant opposing the use of the abovementioned brands in these countries. Proceedings are at various stages and are pending; the Bank is pursuing legal remedies in order to protect its interests. The proceedings in Switzerland, Spain and Germany have been concluded, with the court ruling in favour of Abanca Corporacion Bancaria S.A.

b) *Credit-related commitments*

The primary purpose of these instruments is to ensure that funds are available to customers upon request. Guarantees and standby letters of credit (which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet their obligations to third parties) carry the same credit risk as loans, documentary and commercial letters of credit (which are written undertakings by the Group on behalf of a customer authorising a third party to draw drafts on the Group up to a stipulated amount under specific terms and conditions) are collateralised by the underlying shipments of goods to which they relate, or cash deposits, and therefore carry less risk than direct borrowing. Cash requirements under guarantees and standby letters of credit are considerably lower than the amount of the commitment, because the Group does not generally expect the third party to draw the funds under the agreement.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to a loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, since most commitments to extend credit are contingent upon customers maintaining specific credit standards.

Whilst there is some credit risk associated with the remainder of commitments, the risk is viewed as modest, since it results from the possibility of unused portions of loan authorisations being drawn by the customer and, secondly, from these drawings subsequently not being repaid when due. The Group monitors the term to maturity of credit commitments, because long-term commitments generally involve greater credit risk than short-term ones. The total outstanding contractual amount of credit commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments may expire or terminate without being funded.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

The following table indicates the contractual amounts of the Bank's and the Group's guarantees and commitments to extend credit to customers.

GUARANTEES AND COMMITMENTS

		Abanka		Group	
	Note	2018	2017	2018	2017
Service guarantees		215,422	217,364	215,014	216,922
Financial guarantees		50,371	41,415	50,371	41,415
Letters of credit		34	40	34	40
Loan commitments		436,056	374,909	435,251	373,601
Derivatives		3,610	2,815	3,610	2,815
Other		1,673	236	1,673	236
		707,166	**636,779**	**705,953**	**635,029**
Provisions for guarantees and commitments and other provisions:	34, 44				
– provisions for guarantees and commitments		(14,923)	(29,644)	(14,923)	(29,637)
– provisions for undrawn portion of loans measured at fair value		(2,281)	/	(2,281)	/
		689,962	**607,135**	**688,749**	**605,392**

40 LEASES

	Group	
	2018	2017
Gross investment in finance leases, receivable:	**7,691**	**49,598**
– no later than 1 year	5,763	22,350
– later than 1 year and no later than 5 years	1,809	26,746
– later than 5 years	119	502
Unearned future finance income on finance leases	293	4,658
Net investment in finance leases:	**7,398**	**44,940**
– no later than 1 year	5,649	20,406
– later than 1 year and no later than 5 years	1,633	24,049
– later than 5 years	116	485

Regardless of the Note 1.24, the amount of finance lease receivables relates only to the receivables of subsidiaries.

Compared to the 2017 year-end, receivables from finance lease were lower primarily due to the sale of the subsidiary Aleasing, whose gross receivables from finance lease amounted to EUR 37,308 thousand or EUR 33,115 thousand in net receivables from finance lease as at 31 December 2017.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

	Abanka		Group	
	2018	2017	2018	2017
Investment in operating leases, receivable:	**53**	**67**	**2,271**	**7,219**
– no later than 1 year	14	14	347	1,708
– later than 1 year and no later than 5 years	39	53	1,370	4,624
– later than 5 years	–	–	554	887

	Group	
	2018	2017
Operating lease liabilities:	**2,256**	**403**
– no later than 1 year	478	135
– later than 1 year and no later than 5 years	1,455	268
– later than 5 years	323	–

	Abanka		Group	
	2018	2017	2018	2017
Finance lease liabilities:	**4**	**607**	**4**	**589**
– no later than 1 year	4	71	4	57
– later than 1 year and no later than 5 years	–	234	–	230
– later than 5 years	–	302	–	302

Compared to the 2017 year-end, operating lease liabilities were higher mainly due to new lease agreements and the extension of the lease agreements that expired in 2018.

Compared to the 2017 year-end, finance lease liabilities were lower primarily due to the early acquisition of the real property held by the Bank under a finance lease.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

41 TRANSACTIONS IN THE NAME AND FOR THE ACCOUNT OF THIRD PARTIES

Pursuant to the Regulation on the Books of Account and Annual Reports of Banks and Savings Banks issued by the Bank of Slovenia, the Bank discloses transactions in the name and for the account of third parties.

	Abanka	
	2018	2017
Assets	**3,439,760**	**4,260,212**
Claims of settlement and transaction accounts for customer assets	**3,270,770**	**4,167,875**
- from financial instruments	3,270,452	4,167,157
– investment services and transactions (Financial Instruments Market Act - ZTFI)	27,624	815,015
– reception, transmission and execution of orders	27,624	815,015
– custody operations (Investment Trusts and Management Companies Act - ZISDU)	3,242,828	3,352,142
- against the CSCC (Central Securities Clearing Corporation) or the bank's clearing account for sold financial instruments	–	182
- against other settlement systems and institutions for sold financial instruments (buyers)	318	514
- against the brokerage for purchased financial instruments and net receivables from the CSCC (ZISDU)	–	22
Customers' cash	**1,034**	**4,940**
- in the settlement account for customer assets	9	1,163
- in banks' transaction accounts (ZTFI)	–	1,244
- in banks' transaction accounts (ZISDU)	1,025	2,533
Other transactions authorised by the customer	**167,956**	**87,397**
Liabilities	**3,439,760**	**4,260,212**
Liabilities of settlement and transaction accounts for customer assets	**3,271,804**	**4,172,633**
- to customers from cash and financial instruments	3,270,714	4,169,785
– investment services and transactions (ZTFI)	27,620	817,561
– reception, transmission and execution of orders	27,620	817,561
– custody operations (ZISDU)	3,243,094	3,352,224
- to the CSCC (Central Securities Clearing Corporation) or the bank's clearing account for purchased financial instruments	–	22
- to other settlement systems and institutions for purchased financial instruments (sellers)	1,077	2,767
- to the bank or the bank's settlement account for commission, fees, etc.	13	59
- to the brokerage for sold financial instruments and income from transactions in the name and for the account of third parties (ZISDU)	–	–
Other transactions authorised by the customer	**167,956**	**87,579**

In line with the signed agreement between Abanka and Nova KBM d.d., Abanka transferred its investment and brokerage services to Nova KBM d.d., which was reflected in the reduction of receivables from the acceptance, transmission and execution of orders in the amount of EUR 787,391 thousand. The remaining amount of EUR 27,624 thousand is accounted for by receivables from financial instruments held with custodian banks abroad, the transfer of which will be executed after the legal options to transfer the portfolio have been determined.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

	Abanka	
	2018	**2017**
Income from fees and commissions related to (ancillary) investment services and transactions for customers	**2,530**	**2,906**
Reception, transmission and execution of orders	589	994
Custody and related services	1,699	1,707
Maintenance of customers' dematerialised securities accounts	236	194
Advice to undertakings on capital structure, business strategy and related matters and advice and services relating to mergers and acquisitions of undertakings	6	11

Expenses from fees and commissions related to (ancillary) investment services and transactions for customers	**371**	**332**
Fees and commissions in connection with the CSCC (Central Securities Clearing Corporation) and similar organisations	293	254
- from investment banking operations (ZTFI)	293	254
Fees and commissions in connection with the stock exchange and similar organisations	19	17
Other transactions	59	61

42 RELATED-PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise a significant influence over the other party in making financial or operational decisions.

Related parties of the Bank include: subsidiaries, key management personnel (the Management Board of the Bank, executive directors of the Bank, members of the Supervisory Board of the Bank, all of these persons' close family members) and other related companies (individual companies in which key management personnel have significant influence).

Related parties of the Group include: associates, key management personnel (the Management Board of the Bank, executive directors of the Bank, members of the Supervisory Board of the Bank, directors of subsidiaries, all of these persons' close family members) and other related companies (individual companies in which key management personnel have significant influence).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

A number of banking transactions were entered into with related parties in the normal course of business. The volume of transactions involving related parties for the year-end and related expenses and income for the year are as follows:

TRANSACTIONS WITH RELATED PARTIES OF THE BANK

Type of related party	Subsidiaries		Key management personnel		Other related companies	
	2018	2017	2018	2017	2018	2017
Financial assets						
Loans	8,832	50,940	243	237	–	–
Equity securities						
– investments in subsidiaries	8,278	9,448	–	–	–	–
Financial liabilities						
Deposits	769	5,153	1,056	817	7	–
Loans from non-bank customers	–	18	–	–	–	–
Other financial liabilities	–	59	–	–	–	–
Off-balance sheet records						
Nominal amount of loan commitments and financial guarantees issued	1,213	1,750	51	41	–	–
Comfort letters	–	–	–	–	–	–
Allowances for impairment losses on financial assets	–	239	–	–	–	–
Provisions for guarantees and commitments	–	6	–	–	–	–

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

Type of related party	Subsidiaries		Key management personnel		Other related companies	
	2018	2017	2018	2017	2018	2017
Interest income	449	1,311	4	6	–	–
Interest expenses	–	–	2	5	–	–
Dividend income	–	–	–	–	–	–
Fee and commission income	6	7	3	2	–	–
Fee and commission expenses	–	–	–	–	–	–
Net gains on financial assets held for trading	–	–	–	–	–	–
Net gains on hedge accounting	–	–	–	–	–	–
Net gains on financial assets and liabilities designated at fair value through profit or loss	–	–	–	–	–	–
Net gains on derecognition of investments in subsidiaries	307	–	–	–	–	–
Net other operating income	81	104	–	–	–	–
Administrative expenses	330	840	–	–	–	–
Income from the reversal of impairment of financial assets	60	139	–	–	–	–
Income from the reversal of impairment of investments in subsidiaries	–	529	–	–	–	–
Income on provisions for guarantees and commitments	–	4	–	–	–	–

In terms of transactions that have an impact on profit or loss, related parties include all parties that meet the definition of related parties in the reporting period.

TRANSACTIONS WITH RELATED PARTIES OF THE GROUP

Type of related party	Key management personnel		Other related companies	
	2018	2017	2018	2017
Financial assets				
Loans	245	240	–	–
Financial liabilities				
Deposits	1,155	956	7	–
Loans from non-bank customers	–	–	–	–
Debt securities issued	–	–	–	–
Other financial liabilities	–	–	–	–
Off-balance sheet records				
Nominal amount of loan commitments and financial guarantees issued	53	44	–	–
Comfort letters	–	–	–	–
Allowances for impairment losses on financial assets	–	–	–	–
Provisions for guarantees and commitments	–	–	–	–

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

Type of related party	Associates		Key management personnel		Other related companies	
	2018	2017	2018	2017	2018	2017
Interest income	–	–	4	6	–	–
Interest expenses	–	–	2	5	–	–
Dividend income	–	–	–	–	–	–
Fee and commission income	–	–	3	3	–	–
Fee and commission expenses	–	–	–	–	–	–
Net gains on financial assets held for trading	–	–	–	–	–	–
Net gains on hedge accounting	–	–	–	–	–	–
Net gains on financial assets and liabilities designated at fair value through profit or loss	–	–	–	–	–	–
Net other operating income	–	–	–	–	–	–
Administrative expenses	–	–	–	–	–	–
Income from the reversal of impairment of financial assets	–	–	–	–	–	–
Income on provisions for guarantees and commitments	–	–	–	–	–	–

In terms of transactions that have an impact on profit or loss, related parties include all parties that meet the definition of related parties in the reporting period.

As at 31 December 2018, the Bank's financial assets, measured at amortised cost included debt securities of the Republic of Slovenia in the amount of EUR 350,344 thousand, while the Bank's financial assets, measured at fair value through other comprehensive income included debt securities of the Republic of Slovenia in the amount of EUR 29,550 thousand. In 2018, net interest income from these transactions totalled EUR 7,076 thousand, net gains from trading with debt securities EUR 402 thousand and fee and commission income EUR 71 thousand. As at 31 December 2018, the Bank did not have deposits of the Ministry of Finance. Interest expenses from these deposits totalled EUR 6 thousand in 2018.

As at 31 December 2017, the Bank's available-for-sale financial assets included debt securities of the Republic of Slovenia in the amount of EUR 318,189 thousand, while the Bank's held-to-maturity financial assets included debt securities of the Republic of Slovenia in the amount of EUR 15,562 thousand. As at 31 December 2017, purchased receivables from the state amounted to EUR 470 thousand. Interest income from these transactions totalled EUR 8,167 thousand in 2017. In 2017, net gains from trading with debt securities reached EUR 166 thousand. As at 31 December 2017, deposits of the Ministry of Finance amounted to EUR 10,009 thousand, with interest expenses from these deposits totalling EUR 75 thousand in 2017.

The Bank has also contractual relations with state-related companies.

Individually significant transactions with state-related companies include given and received long-term loans and deposits. As at 31 December 2018, individually significant given long-term loans totalled EUR 211,248 thousand (3 contracts), received long-term loans EUR 68,718 thousand (5 contracts) and received deposits EUR 40,168 thousand (1 contract).

As at 31 December 2018, the remaining (individually insignificant) given long-term loans totalled EUR 39,605 thousand, received long-term loans EUR 32,211 thousand and received deposits EUR 26,943 thousand.

Individually significant transactions with state-related companies include given and received long-term loans and deposits. As at 31 December 2017, there was no individually significant debt securities available for sale, individually significant given long-term loans totalled EUR 248,600 thousand (4 contracts), received long-term loans EUR 58,261 thousand (4 contracts), received deposits EUR 40,026 thousand (1 contract) and given deposits EUR 10,264 thousand (1 contract).

As at 31 December 2017, the remaining (individually insignificant) debt securities available for sale totalled EUR 23,293 thousand, given loans EUR 55,598 thousand, received long-term loans EUR 43,480 thousand, received deposits EUR 38,719 thousand and given deposits EUR 6,348 thousand.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

In 2018, interest income from transactions with state-related companies amounted to EUR 2,307 thousand (2017: EUR 8,738 thousand) and interest expenses totalled EUR 1,677 thousand (2017: EUR 1,511 thousand).

DISCLOSURE ON RELATED PARTIES BASED ON OTHER REGULATIONS

LOANS AND REPAYMENTS OF THE MANAGEMENT BOARD, MEMBERS OF THE SUPERVISORY BOARD AND MANAGEMENT PERSONNEL OF THE BANK

	Members of the Management Board of Abanka		Members of the Supervisory Board		Management personnel of the Bank	
	2018	2017	2018	2017	2018	2017
Loan balance as at 31 December	–	1	–	–	1,188	1,089
Average interest rate						
– reference IR	/	/	/	/	*6M Euribor spread 1.96%*	*6M Euribor spread 2.04%*
– nominal IR	/	7.90%	/	/	4.56%	4.69%
Repayments in the year	3	5	–	–	271	303

The balance of loans includes all loans that were previously granted by the Bank to those Management Board members, the Supervisory Board members and management personnel of the Bank, who performed these functions as at 31 December 2018 or 31 December 2017, regardless of whether the persons concerned had also been performing these functions at the time of loan approval.

The average interest rate is calculated on the basis of the balance of loans and other interest-bearing exposures and the applicable contractual interest rates as at 31 December 2018 or 31 December 2017.

BREAKDOWN OF PAYMENTS TO THE MANAGEMENT AND SUPERVISORY BOARD MEMBERS, MANAGEMENT PERSONNEL AND DIRECTORS OF SUBSIDIARIES

PAYMENTS TO THE MANAGEMENT BOARD MEMBERS FROM 1 JANUARY TO 31 DECEMBER 2018

	Jože Lenič	Matej Golob Matzele	Matevž Slapničar	Aleksander Vozel[5]	Total in EUR
Fixed part of the salary (gross)	129,036.96	126,655.60	126,812.51	–	382,505.07
Variable part of the salary (gross)	6,387.34	6,273.80	3,659.72	1,568.45	17,889.31
Profit sharing	–	–	–	–	–
Options and other remuneration	–	–	–	–	–
Reimbursements[1]	913.93	887.86	995.62	–	2,797.41
Insurance premiums[2]	1,973.28	2,537.16	2,537.16	–	7,047.60
Benefits[3]	17,259.04	9,541.60	9,158.18	–	35,958.82
Fees and commissions	–	–	–	–	–
Other additional payments	–	–	–	–	–
Total payments	**155,570.55**	**145,896.02**	**143,163.19**	**1,568.45**	**446,198.21**
Total net payments	**58,507.11**	**64,807.56**	**61,484.13**	**1,221.82**	**186,020.62**
Other rights under the contract[4]	**8,203.06**	**9,591.06**	**9,254.22**	**–**	**27,048.34**

[1] meal allowance
[2] voluntary supplemental pension insurance premium
[3] company car, liability insurance, voluntary pension insurance and other insurance
[4] medical examinations, education, other insurance and membership fees
[5] Member of the Managment Board until 31 March 2017

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

As at 31 December 2018, Matej Golob Matzele, a member of the Management Board, was also a member of the supervisory board of an unrelated company, i.e. Bankart d.o.o., Ljubljana, whereas no Management Board member was a member of the supervisory board of any related company.

PAYMENTS TO THE MANAGEMENT BOARD MEMBERS FROM 1 JANUARY TO 31 DECEMBER 2017

	Jože Lenič	Matej Golob Matzele	Matevž Slapničar[5]	Aleksander Vozel[6]	Total in EUR
Fixed part of the salary (gross)	129,045.45	126,774.69	60,380.73	41,106.50	357,307.37
Variable part of the salary (gross)	19,162.01	28,586.41[7]	–	18,821.41	66,569.83
Profit sharing	–	–	–	–	–
Options and other remuneration	–	–	–	–	–
Reimbursements	839.94	856.88	565.25	197.22	2,459.29
Insurance premiums[1]	1,677.31	2,123.70	1,201.31	345.34	5,347.66
Benefits[2]	13,465.21	3,404.67	3,580.19	1,680.90	22,130.97
Fees and commissions	–	–	–	–	–
Other additional payments[3]	–	–	–	50,229.36	50,229.36
Total payments	**164,189.92**	**161,746.35**	**65,727.48**	**112,380.73**	**504,044.48**
Total net payments	**66,537.58**	**78,881.79**	**28,879.13**	**61,078.90**	**235,377.40**
Other rights under the contract[4]	**8,538.72**	**9,886.84**	**6,615.37**	**2,396.64**	**27,437.57**

[1] voluntary supplemental pension insurance premium
[2] company car, liability insurance, voluntary pension insurance and other insurance
[3] compensation for invocation of non-compete clause and unused leave
[4] medical examinations, education, other insurance and membership fees
[5] term of office from 12 June 2017
[6] term of office until 31 March 2017
[7] payment of EUR 18,821.41 to a Management Board member for 2016; payment of a deferred part of variable remuneration in the amount of EUR 9,765 to Executive Director for 2015

PAYMENTS TO DIRECTORS OF DIRECT SUBSIDIARIES FROM 1 JANUARY TO 31 DECEMBER 2018

	Nikolaj Fišer (Aleasing d.o.o.)[4]	Gregor Žvipelj (Anepremičnine d.o.o.)	Total in EUR
Fixed part of the salary (gross)	18,135.00	73,849.09	91,984.09
Variable part of the salary (gross)	–	10,155.60	10,155.60
Reimbursements	228.08	1,339.64	1,567.72
Insurance premiums[1]	704.76	2,537.12	3,241.88
Benefits[2]	1,648.14	1,991.06	3,639.20
Total payments	**20,715.98**	**89,872.51**	**110,588.49**
Total net payments	**9,669.39**	**49,122.00**	**58,791.39**
Other rights under the contract[3]	**–**	**680.00**	**680.00**

[1] voluntary supplemental pension insurance premium
[2] company car, life insurance and liability insurance
[3] education
[4] payments until 31 March 2018 (sale of subsidiary Aleasing)

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

PAYMENTS TO DIRECTORS OF DIRECT SUBSIDIARIES FROM 1 JANUARY TO 31 DECEMBER 2017

	Nikolaj Fišer (Aleasing d.o.o.)	Gregor Žvipelj (Anepremičnine d.o.o.)	Total in EUR
Fixed part of the salary (gross)	73,838.86	73,838.85	147,677.71
Variable part of the salary (gross)	7,254.00	–	7,254.00
Reimbursements	982.55	1,346.80	2,329.35
Insurance premiums[1]	2,707.68	1,836.06	4,543.74
Benefits[2]	2,613.40	2,392.50	5,005.90
Total payments	**87,396.49**	**79,414.21**	**166,810.70**
Total net payments	**45,002.12**	**43,420.29**	**88,422.41**
Other rights under the contract[3]	**2,984.91**	**248.98**	**3,233.89**

[1] voluntary supplemental pension insurance premium
[2] company car, life insurance, accident insurance and liability insurance
[3] education

PAYMENTS TO DIRECTORS OF INDIRECT SUBSIDIARIES FROM 1 JANUARY TO 31 DECEMBER 2018

	Slobodan Radović (Anekretnine d.o.o., Montenegro)
Fixed part of the salary (gross)	4,029.72
Variable part of the salary (gross)	–
Total payments	**4,029.72**
Total net payments	**2,700.00**
Other rights under the contract	**–**

PAYMENTS TO DIRECTORS OF INDIRECT SUBSIDIARIES FROM 1 JANUARY TO 31 DECEMBER 2017

	Slobodan Radović (Anekretnine d.o.o., Montenegro)
Fixed part of the salary (gross)	4,029.72
Variable part of the salary (gross)	–
Total payments	**4,029.72**
Total net payments	**2,700.00**
Other rights under the contract	**–**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

PROVISIONS, ACCRUED COSTS AND DEFERRED REMUNERATION FOR THE BANK'S MANAGEMENT BOARD AND DIRECTORS OF SUBSIDIARIES

	Abanka		Group	
	2018	2017	2018	2017
Provisions for retirement benefits and jubilee payments	80	101	85	118
Accrued costs for unused leave	26	16	31	30
Deferred part of the variable remuneration	18	57	28	64
	124	**174**	**144**	**212**

TOTAL EARNINGS RECEIVED BY MANAGEMENT PERSONNEL

	Abanka		Group	
	2018	2017	2018	2017
Salaries	3,199	3,374	3,304	3,479
Retirement, severance and jubilee payments	3	83	3	83
	3,202	**3,457**	**3,307**	**3,562**

PROVISIONS, ACCRUED COSTS AND DEFERRED REMUNERATION FOR MANAGEMENT PERSONNEL

	Abanka		Group	
	2018	2017	2018	2017
Provisions for retirement benefits and jubilee payments	833	943	849	960
Accrued costs for unused leave	120	127	128	136
Deferred part of the variable remuneration	–	–	–	–
	953	**1,070**	**977**	**1,096**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

PAYMENTS TO MEMBERS OF THE SUPERVISORY BOARD FROM 1 JANUARY TO 31 DECEMBER 2018

	Service remuneration	Attendance fees	Reimbursements	Total in EUR (gross)	Total in EUR (net)	Other benefits[6]
Bernarda Babič[1]	11,552.42	4,070.00	–	15,622.42	11,270.97	334.54
Varja Dolenc[2]	6,831.99	2,200.00	–	9,031.99	6,488.67	2,149.50
Marko Garbajs	31,427.08	8,140.00	–	39,567.08	28,696.94	1,352.07
Dejan Kaisersberger	28,125.00	9,625.00	1,389.63	39,139.63	28,386.05	294.50
Miha Košak[3]	3,419.35	770.00	5,725.15	9,914.50	6,430.66	294.50
Melita Malgaj	25,023.85	8,305.00	–	33,328.85	24,159.89	902.30
Peter Merc[4]	13,669.35	3,850.00	–	17,519.35	12,741.83	–
Rok Pivk	23,235.89	6,886.00	4,238.74	34,360.63	24,910.18	902.30
Blaž Šterk[5]	1,875.00	495.00	–	2,370.00	1,723.70	–
Alenka Vrhovnik Težak	28,719.76	9,185.00	853.32	38,758.08	28,108.48	2,385.33
	173,879.69	**53,526.00**	**12,206.84**	**239,612.53**	**172,917.37**	**8,615.04**

[1] Member of the Supervisory Board until 5 July 2018
[2] Member of the Supervisory Board since 31 July 2018
[3] Member of the Supervisory Board since 22 September 2018
[4] Member of the Supervisory Board until 9 July 2018
[5] Member of the Supervisory Board until 31 December 2017
[6] liability insurance and education

PAYMENTS TO MEMBERS OF THE SUPERVISORY BOARD FROM 1 JANUARY TO 31 DECEMBER 2017

	Service remuneration	Attendance fees	Reimbursements	Total in EUR (gross)	Total in EUR (net)	Other benefits[5]
Marko Garbajs	37,171.88	8,481.00	–	45,652.88	33,112.21	2,871.90
Dejan Kaisersberger[1]	18,179.72	5,676.00	3,153.02	27,008.74	19,552.24	1,927.89
Vid Leskovec[2]	16,088.71	5,401.00	–	21,489.71	15,629.49	1,111.46
Melita Malgaj	24,000.00	7,557.00	–	31,557.00	22,860.29	2,000.62
Peter Merc[3]	2,534.27	275.00	–	2,809.27	1,951.95	889.16
Rok Pivk	22,500.00	6,743.00	1,476.48	30,719.48	22,251.06	3,425.31
Blaž Šterk	24,791.33	6,226.00	–	31,017.33	22,558.91	1,666.09
Alenka Vrhovnik Težak	28,234.38	7,986.00	923.20	37,143.58	26,923.43	3,483.66
Bernarda Babič[4]	–	–	–	–	–	958.81
	173,500.29	**48,345.00**	**5,552.70**	**227,397.99**	**164,839.58**	**18,334.90**

[1] Member of the Supervisory Board since 28 February 2017
[2] Member of the Supervisory Board until 18 August 2017
[3] Member of the Supervisory Board since 11 October 2017
[4] Member of the Supervisory Board since 1 January 2018
[5] liability insurance and education

NOTES TO THE FINANCIAL STATEMENTS (continued)

43 EVENTS AFTER THE REPORTING DATE

No material events occurred after the reporting date that would require additional disclosures or corrections of the presented financial statements.

44 IFRS 9 – FINANCIAL INSTRUMENTS (WITH THE TRANSITION IMPACT)

On 1 January 2018, IFRS 9 became effective and, therefore, the Bank amended its accounting policies in accordance with the requirements, as described in Notes 1 and 3.

Changes in accounting policies were mostly applied retrospectively, except in the following cases:
- the Group used the exception that allows comparative information from prior periods not to be restated in accordance with IAS 8 due to the effects of classification and measurement (including impairments). The differences in the carrying amount of financial assets resulting from the introduction of IFRS 9 are recognised in retained earnings as at 1 January 2018 (Notes 44.1.1 and 44.1.2).
- In view of the facts and circumstances existing at the date of the first application, the following assessments were made:
  - the definition of the business model, within which a financial asset is held;
  - determining that equity securities not held for trading will be measured at fair value through other comprehensive income.
- As the starting point in the classification of loans into stages, the Group took into account the balance of loans as at 31 December 2015. This is the first date of the end of the year after Abanka and Banka Celje were merged and consequently data are harmonised and comparable. From that date onwards, the Group has checked whether a significant risk occurred for the customers who have been classified into the highest (Stage 1) rating grades as at 31 December 2015.
- For the purpose of transition to IFRS 9, material financial assets (without taking into account guarantees) granted to certain debtors classified into D or E credit rating categories as at 31 December 2015 were classified as purchased or originated credit-impaired (POCI) financial assets. The Group assessed that it was not necessary to calculate the effect of contract modification as at 1 January 2018, as the latter would have been immaterial.

Impacts of transition to IFRS 9

The total impact of the introduction of IFRS 9 on the Group's retained earnings from the transition to IFRS 9 as at 1 January 2018 is EUR 10,763 thousand (Note 44.1.2), while the impact on retained earnings of the Bank amounted to EUR 10,937 thousand (Note 44.1.1). The impact of the Bank is accounted for by:
- an increase of EUR 4,614 thousand resulting from the impact of classification and measurement (an increase of EUR 7,750 thousand from equity securities valued at fair value through profit or loss and a decrease of EUR 3,136 thousand from loans mandatorily measured at fair value through profit or loss),
- an increase of EUR 6,627 thousand resulting from the impact of impairments and provisions (an increase of EUR 10,302 thousand from provisions and a decrease of EUR 3,675 thousand from impairments),
- a decrease of EUR 304 thousand resulting from the impact of current and deferred taxes.

Upon transferring a portion of the NPL portfolio to the newly established company, the Bank reversed the release of impairments for receivables following the transition to IFRS 9 in the amount of EUR 646 thousand and reduced retained earnings arising from the transition to IFRS 9.

In the second half of 2018, based on the interpretation of the FURS (Financial Administration of the Republic of Slovenia), the Bank changed the tax treatment of deferred taxes from impairments of equity securities reclassified into the category at fair value through profit or loss and increased net profit by EUR 200 thousand generated from the net income from current and deferred taxes.

Regulatory capital increased by EUR 1,076 thousand. Changes in classification and measurement led to a decrease in regulatory capital by EUR 4,269 thousand, and changes in impairments and provisions to its increase by EUR 5,345 thousand. The impact on regulatory capital is presented in Note 44.1.3.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

44.1.1 The breakdown of the impact of transition to IFRS 9 as at 1 January 2018 – Abanka

The introduction of IFRS 9 impacted the classification and measurement of financial assets as at 1 January 2018 as described below.

- Assets held for trading and derivatives designated as a hedging instrument, which were classified as financial assets held for trading and measured at fair value through profit or loss in accordance with IAS 39, continue to be measured at fair value through profit or loss even in accordance with IFRS 9.
- Loans classified as loans and receivables and measured at amortised cost in accordance with IAS 39 continue to be, for the most part, measured at amortised cost in accordance with IFRS 9; however, a few are measured at fair value because they failed the SPPI test.
- Securities classified as held-to-maturity investments and measured at amortised cost in accordance with IAS 39 continue to be measured at amortised cost in accordance with IFRS 9.
- In accordance with IFRS 9, debt securities classified as available-for-sale financial assets in accordance with IAS 39 are to a greater extent measured at amortised cost and to a lesser extent at fair value through other comprehensive income. Due to the reversal of revaluation of debt securities measured at amortised cost in accordance with IFRS 9, the regulatory capital of the Group decreased by EUR 3,830 thousand.
- The majority of equity securities classified as available-for-sale financial assets in accordance with IAS 39 are measured at fair value through profit or loss in accordance with IFRS 9. In relation to equity securities held for long-term strategic purposes and which are of infrastructure nature for the Group and not held for trading, as at 1 January 2018 the Group chose the irrevocable option of valuation at fair value through other comprehensive income.

a) Financial assets

The following table shows the measurement categories of financial assets in accordance with IAS 39 and the new measurement categories in accordance with IFRS 9 as at 1 January 2018:

	Classification under IAS 39	Classification under IFRS 9	IAS 39 carrying amount	IFRS 9 carrying amount 1 January 2018
Cash, cash balances with the central bank and other demand deposits with banks	Cash, cash balances with the central bank and other demand deposits with banks	Cash, cash balances with the central bank and other demand deposits with banks	411,665	411,665
Financial assets held for trading	Fair value through profit or loss (held for trading)	Fair value through profit or loss (held for trading)	3,048	3,048
Debt securities	Available for sale	Fair value through other comprehensive income	142,828	142,828
Debt securities	Available for sale	Amortised cost	901,893	875,001
Shares and equity holdings	Available for sale	Fair value through profit or loss (non-trading financial assets mandatorily measured at fair value through profit or loss)	15,178	15,178
Shares and equity holdings	Available for sale	Fair value through other comprehensive income	30,791	30,791
Loans to banks	Loans and receivables	Amortised cost	60,745	60,732
Loans to non-bank customers[1]	Loans and receivables	Amortised cost	1,952,599	1,950,975
Loans to non-bank customers	Loans and receivables	Fair value through profit or loss (non-trading financial assets mandatorily measured at fair value through profit or loss)	29,538	26,402
Other financial assets[1]	Loans and receivables	Amortised cost	23,661	23,710
Other assets	Other assets	Other assets	2,302	2,303
Debt securities	Held to maturity	Amortised cost	15,408	15,408
Total financial assets			**3,589,656**	**3,558,041**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

The following table reconciles the carrying amounts of financial assets under IAS 39 to the carrying amounts under IFRS 9 as at 1 January 2018:

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
At amortised cost				
Cash, cash balances with the central bank and other demand deposits with banks	411,665			411,665
Debt securities measured at amortised cost				
Opening balance	–			
Reclassification from the category held to maturity (IAS 39)		15,408		
Reclassification from the category available for sale (IAS 39)		901,893		
Remeasurement – from fair value to amortised cost			(26,744)	
Remeasurement – formed impairments			(148)	
Closing balance				890,409
Loans to banks measured at amortised cost				
Opening balance	60,745			
Remeasurement – formed impairments			(13)	
Closing balance				60,732
Loans to non-bank customers measured at amortised cost				
Opening balance	1,982,137			
Reclassification to the category non-trading financial assets mandatorily at fair value through profit or loss		(29,538)		
Transfer of unamortised fees for approval to liabilities		89		
Remeasurement – impairments (additionally formed or released)			(1,713)	
Closing balance[1]				1,950,975
Other financial assets measured at amortised cost				
Opening balance	23,661			
Remeasurement – released impairments			49	
Closing balance[1]				23,710
Held-to-maturity investments				
Opening balance	15,408			
Reclassification to the category debt securities measured at amortised cost		(15,408)		
Closing balance				–
Other assets				
Opening balance	2,302			
Remeasurement – released impairments			1	
Closing balance				2,303
Total financial assets measured at amortised cost[1]	**2,495,918**	**872,444**	**(28,568)**	**3,339,794**

[1] In the second half of 2018, upon transferring a portion of the NPL portfolio to the newly established company, the Bank reversed the release of impairments of loans to non-bank customers following the transition to IFRS 9 in the amount of EUR 649 thousand (the closing balance as at 1 January 2018 amounted to EUR 1,950,326 thousand) and reversed the impairments of other financial assets made following the transition in the amount of EUR 3 thousand (the closing balance as at 1 January 2018 amounted to EUR 23,713 thousand).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS
(continued)

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
At fair value through profit or loss				
Financial assets held for trading	3,048			3,048
Non-trading financial assets mandatorily at fair value through profit or loss				
Opening balance	–			
Reclassification from the category loans to non-bank customers (amortised cost)		29,538		
Reclassification of debt securities from the category available for sale (IAS 39)		15,178		
Remeasurement of loans – from amortised cost to fair value			(3,136)	
Closing balance				41,580
Total financial assets measured at fair value through profit or loss	**3,048**	**44,716**	**(3,136)**	**44,628**

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
At fair value through other comprehensive income				
Available-for-sale financial assets				
Opening balance	1,090,690			
Reclassification to the category at amortised cost (securities)		(901,893)		
Reclassification to the category non-trading financial assets mandatorily at fair value through profit or loss		(15,178)		
Reclassification to the category at fair value through other comprehensive income (debt instruments)		(142,828)		
Reclassification to the category at fair value through other comprehensive income (equity instruments)		(30,791)		
Closing balance				–
Financial assets measured at fair value through other comprehensive income (debt instruments)				
Opening balance	–			
Reclassification from the category available for sale (IAS 39)		142,828		
Closing balance				142,828
Financial assets measured at fair value through other comprehensive income (equity instruments)				
Opening balance	–			
Reclassification from the category available for sale (IAS 39)		30,791		
Closing balance				30,791
Total financial assets measured at fair value through other comprehensive income	**1,090,690**	**(917,071)**	**–**	**173,619**

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

b) Financial liabilities

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
At fair value through profit or loss				
Financial liabilities designated at fair value through profit or loss				
Opening balance	–			
Effects of measurement of undrawn loan commitments mandatorily measured at fair value through profit or loss			1,871	
Closing balance				1,871

c) Income tax assets and liabilities

	IAS 39 carrying amount 31 December 2017	Increase or (decrease)	IFRS 9 carrying amount 1 January 2018
Income tax assets			
Opening balance	12,408		
Deferred income tax assets for impairment of debt securities measured at amortised cost		28	
Closing balance			12,436
Income tax liabilities			
Opening balance	5,960		
Corporate income tax liability – transition to IFRS 9[1]		304	
Reversal of deferred income tax liability on valuation of debt securities available for sale under IAS 39, reclassified to the category at amortised cost at transition to IFRS 9		(5,081)	
Deferred income tax liability on valuation of equity securities available for sale under IAS 39, reclassified to the category non-trading financial assets mandatorily at fair value through profit or loss at transition to IFRS 9[2]		80	
Closing balance			1,263

[1] In the second half of 2018, based on the interpretation of the FURS (Financial Administration of the Republic of Slovenia), the Bank changed the tax treatment of deferred taxes from impairments of equity securities reclassified into the category at fair value through profit or loss and formed additional tax liabilities of EUR 199 thousand against the net profit. Total tax liability from the transition thus amounted to EUR 503 thousand.

[2] Following the changed tax treatment of deferred taxes arising from impairments of equity securities reclassified into the category at fair value through profit or loss, the Bank additionally formed deferred tax assets in the amount of EUR 399 thousand.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

d) Impairments and provisions

The following table reconciles the closing impairment allowance under IAS 39 and provisions under IAS 37 to the opening expected credit loss allowance under IFRS 9 (ECL):

	Impairments in accordance with IAS 39 / Provisions in accordance with IAS 37 31 December 2017	Interest impairments 31 December 2017	Reclassification	Remeasurement	Impairments in accordance with IFRS 9 1 January 2018
Loans and receivables in accordance with IAS 39 / Financial assets at amortised cost in accordance with IFRS 9	(182,384)	(12,479)	69,467	(1,199)	(126,595)
Loans and receivables – to banks	–	–	–	(13)	(13)
Loans and receivables – to non-bank customers[1]	(182,030)	(11,714)	69,467	(1,713)	(125,990)
Loans and receivables – other financial assets[1]	(354)	(765)	–	527	(592)
Held-to-maturity investments in accordance with IAS 39 / Financial assets at amortised cost in accordance with IFRS 9	–	–	–	(1)	(1)
Loans and receivables in accordance with IAS 39 / Financial assets at fair value through profit or loss in accordance with IFRS 9	(26,556)	(1,333)	27,889	–	–
Debt securities available for sale in accordance with IAS 39 / Financial assets at amortised cost in accordance with IFRS 9	–	–	–	(148)	(148)
Debt securities available for sale in accordance with IAS 39 / Debt instruments at FVOCI in accordance with IFRS 9	–	–	–	(8)	(8)
Total impairments	**(208,940)**	**(13,812)**	**97,356**	**(1,356)**	**(126,752)**
Provisions for guarantees and commitments	(29,644)	–	–	10,302	(19,342)
Total impairments and provisions	**(238,584)**	**(13,812)**	**97,356**	**8,946**	**(146,094)**

[1] In the second half of 2018, upon transferring a portion of the NPL portfolio to the newly established company, the Bank reversed the release of impairments of loans to non-bank customers following the transition to IFRS 9 in the amount of EUR 649 thousand and reversed the impairments of other financial assets made following the transition in the amount of EUR 3 thousand.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

e) Other comprehensive income

	IAS 39 carrying amount 31 December 2017	Transition effects	IFRS 9 carrying amount 1 January 2018
Opening balance	33,317		
Reversal of valuation due to the transfer of debt securities to the amortised cost category		(26,744)	
Transfer of valuation due to the transfer of equity securities from the category available for sale to the category mandatorily measured at fair value through profit or loss		(9,667)	
Reversal of deferred taxes (debt and equity securities) due to transfer between categories[1]		6,917	
Additional impairments of debt securities measured at fair value through other comprehensive income		8	
Closing balance			3,831

[1] Following the changed tax treatment of deferred taxes arising from impairments of equity securities reclassified into the category at fair value through profit or loss, the Bank additionally formed deferred tax assets in the amount of EUR 399 thousand.

f) Retained earnings

	IAS 39 carrying amount 31 December 2017	Transition effects	IFRS 9 carrying amount 1 January 2018
Opening balance	60,457		
Transfer of valuation and deferred taxes[1] due to the transfer of equity securities to the category mandatorily measured at fair value through profit or loss		7,750	
Remeasurement of loans due to transfer from amortised cost to fair value		(3,136)	
Remeasurement of loans – additional impairments (loans to non-bank customers)[2]		(1,713)	
Remeasurement of loans – additional impairments (loans to banks)		(13)	
Remeasurement of debt securities – additional impairments		(148)	
Impairments of debt securities measured at fair value through other comprehensive income		(8)	
Deferred tax receivables from debt securities measured at amortised cost		28	
Remeasurement of other financial assets and other assets[2]		50	
Effects of measurement of financial liabilities		(1,871)	
Remeasurement of provisions for guarantees and commitments		10,302	
Corporate income tax liability – transition to IFRS 9		(304)	
Closing balance			71,394

[1] Following the changed tax treatment of deferred taxes arising from impairments of equity securities reclassified into the category at fair value through profit or loss, the Bank additionally formed deferred tax assets in the amount of EUR 399 thousand.
[2] Upon transferring a portion of the NPL portfolio to the newly established company, the Bank reversed the release of impairments following the transition to IFRS 9 and reduced retained earnings arising from impairments in the amount of EUR 646 thousand.

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

44.1.2 The breakdown of the impact of transition to IFRS 9 as at 1 January 2018 – Group

The total impact of the introduction of IFRS 9 on the Group's retained earnings as at 1 January 2018 is EUR 10,763 thousand. The impact of the Group was accounted for by:

- an increase of EUR 4,614 thousand resulting from the impact of classification and measurement (an increase of EUR 7,750 thousand from equity securities valued at fair value through profit or loss and a decrease of EUR 3,136 thousand from loans mandatorily measured at fair value through profit or loss);
- an increase of EUR 6,453 thousand resulting from the impact of impairments and provisions (an increase of EUR 10,295 thousand from provisions and a decrease of EUR 3,842 thousand from impairments);
- a decrease of EUR 304 thousand resulting from the impact of current and deferred taxes.

Upon transferring a portion of the NPL portfolio to the newly established company, the Bank reversed the release of impairments for receivables following the transition to IFRS 9 in the amount of EUR 646 thousand and reduced retained earnings arising from the transition to IFRS 9.

In the second half of 2018, based on the interpretation of the FURS, the Bank changed the tax treatment of deferred taxes from impairments of equity securities reclassified into the category at fair value through profit or loss and increased net profit by EUR 200 thousand generated from the net income from current and deferred taxes.

The impact on the Group slightly differs from the transition to IFRS 9 at the bank level, due to consolidation entries. The table below shows only those items whose transition differs from the effects shown for the bank in note 44.1.1.

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
Loans to non-bank customers measured at amortised cost				
Opening balance	1,967,460			
Reclassification to the category non-trading financial assets mandatorily at fair value through profit or loss		(29,538)		
Transfer of unamortised fees for approval to liabilities		89		
Remeasurement – impairments (additionally formed or released)			(1,881)	
Closing balance[1]				1,936,130
Provisions for guarantees and commitments	(29,637)	–	10,295	(19,342)

[1] In the second half of 2018, upon transferring a portion of the NPL portfolio to the newly established company, the Bank reversed the release of impairments of loans to non-bank customers following the transition to IFRS 9 in the amount of EUR 649 thousand (the closing balance as at 1 January 2018 amounted to EUR 1,950,326 thousand) and reversed the impairments of other financial assets made following the transition in the amount of EUR 3 thousand (the closing balance as at 1 January 2018 amounted to EUR 23,713 thousand).

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

44.1.3 Impact on (regulatory) capital

In the calculation of regulatory capital as at 1 January 2018, the impact of the transition to IFRS 9 (including reversal of the effects of the transition on receivables that were excluded when a portion of the NPL portfolio was transferred) resulting from other comprehensive income (both on a solo and consolidated basis in the amount of EUR -10,089 thousand) and prudential filters – requirements for prudential valuation (both on a solo and consolidated basis in the amount of EUR 874 thousand) was recognised, whereas due to the transition to IFRS 9 retained earnings will be included after the audit of the financial statements for 2018 (on a solo basis in the amount of EUR 10,291 thousand and on a consolidated basis in the amount of EUR 10,117 thousand). Following the introduction of the expected credit loss model, the Group will not use the option of a progressive phase-in regime to mitigate the impact on regulatory capital as provided for by Regulation (EU) 2017/2395.

The total risk exposure amount of the Bank as at 1 January 2018 was EUR 2,087,575 thousand, up by EUR 22,057 thousand compared to the 2017 year-end. If retained earnings had already been included due to the transition, the regulatory capital of the Bank as at 1 January 2018 would have amounted to EUR 502,505 thousand, up by EUR 1,076 thousand compared to the 2017 year-end. Furthermore, as at 1 January 2018, total capital ratio, Tier 1 capital ratio and Common Equity Tier 1 capital ratio of the Bank would have stood at 24.07%, down by 20 basis points compared to the 2017 year-end.

The total risk exposure amount of the Group as at 1 January 2018 was EUR 2,072,461 thousand, up by EUR 21,921 thousand compared to the 2017 year-end. If retained earnings had already been included due to the transition, the regulatory capital of the Group as at 1 January 2018 would have amounted to EUR 504,530 thousand, up by EUR 902 thousand compared to the 2017 year-end. Furthermore, as at 1 January 2018, total capital ratio, Tier 1 capital ratio and Common Equity Tier 1 capital ratio of the Group would have stood at 24.34%, down by 22 basis points compared to the 2017 year-end.

IMPACT ON REGULATORY CAPITAL AND TOTAL RISK EXPOSURE AMOUNT – ABANKA D.D.

The impact of IFRS 9 resulting from retained earnings has already been taken into account in CET 1 for information purposes in the tables below, while it will be included in the actual CET 1 calculation following the audit of the financial statements for 2018.

	Equity from the statement of financial position	Common Equity Tier 1 capital (transitional period)	Common Equity Tier 1 capital (fully loaded)
Balance as at 31 December 2017	**578,943**	**501,429**	**520,918**
IFRS 9 impact on retained earnings (before taxes), of which:	11,241	11,241	11,241
Classification and measurement	4,614	4,614	4,614
Impairments and provisions	6,627	6,627	6,627
Taxes	(304)	(304)	(304)
IFRS 9 impact on retained earnings, net of tax	10,937	10,937	10,937
Reversal of the transition effects upon transferring a portion of the NPL portfolio	(646)	(646)	(646)
IFRS 9 impact on accumulated other comprehensive income	(29,486)	(29,486)	(29,486)
IFRS 9 impact due to regulatory deductions or prudential filters, of which:	–	20,271	874
Regulatory adjustments related to unrealised gains and losses	–	19,397	–
Prudential filters	–	874	874
Balance as at 1 January 2018	**559,748**	**502,505**	**502,597**

	Total risk exposure amount (transitional period)	Total risk exposure amount (fully loaded)
Balance as at 31 December 2017	**2,065,518**	**2,052,629**
IFRS 9 impact on total risk exposure amount	22,057	22,057
Balance as at 1 January 2018	**2,087,575**	**2,074,686**
Common Equity Tier 1 capital ratio as at 31 December 2017	24.28%	25.38%
Common Equity Tier 1 capital ratio as at 1 January 2018	24.07%	24.23%
Change in base points	(20)	(115)

(All amounts in EUR thousand unless otherwise stated)

NOTES TO THE FINANCIAL STATEMENTS (continued)

IMPACT ON REGULATORY CAPITAL AND TOTAL RISK EXPOSURE AMOUNT – GROUP

The impact of IFRS 9 resulting from retained earnings has already been taken into account in CET 1 for information purposes in the tables below, while it will be included in the actual CET 1 calculation only after the audit of the financial statements for 2018.

	Equity from the statement of financial position	Common Equity Tier 1 capital (transitional period)	Common Equity Tier 1 capital (fully loaded)
Balance as at 31 December 2017	**580,283**	**503,628**	**523,111**
IFRS 9 impact on retained earnings (before taxes), of which:	11,067	11,067	11,067
Classification and measurement	4,614	4,614	4,614
Impairments and provisions	6,453	6,453	6,453
Taxes	(304)	(304)	(304)
IFRS 9 impact on retained earnings, net of tax	10,763	10,763	10,763
Reversal of the transition effects upon transferring a portion of the NPL portfolio	(646)	(646)	(646)
IFRS 9 impact on accumulated other comprehensive income	(29,486)	(29,486)	(29,486)
IFRS 9 impact due to regulatory deductions or prudential filters, of which:	–	20,271	874
Regulatory adjustments related to unrealised gains and losses	–	19,397	–
Prudential filters	–	874	874
Balance as at 1 January 2018	**560,914**	**504,530**	**504,616**

	Total risk exposure amount (transitional period)	Total risk exposure amount (fully loaded)
Balance as at 31 December 2017	**2,050,540**	**2,047,052**
IFRS 9 impact on total risk exposure amount	21,921	21,921
Balance as at 1 January 2018	**2,072,461**	**2,068,973**
Common Equity Tier 1 capital ratio as at 31 December 2017	24.56%	25.55%
Common Equity Tier 1 capital ratio as at 1 January 2018	24.34%	24.39%
Change in base points	(22)	(116)

INDEPENDENT AUDITOR'S REPORT

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INDEPENDENT AUDITOR'S REPORT
to the shareholders of ABANKA d.d.

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of the ABANKA d.d. (hereinafter 'the Company'), which comprise the statement of financial position as at 31 December 2018, and the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

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

Basis for Opinon

We conducted our audit in accordance with International Standards on Auditing (ISAs) and Regulation (EU) 537/2014 of the European Parliament and of the Council, dated 16 April 2014, on specific requirements regarding statutory audit of public-interest entities. Our responsibilities under those rules are further described in *the Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and other 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. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit 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 year ended 31 December 2018. 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.

Impairment of loans to customers (expected credit losses)

In its financial statements for the year ended 31 December 2018 the Company presented loans from customers in the amount of EUR 2,002 million and total expected credit loss in the amount of EUR 67 million.

Key audit matter	How the matter was addressed in our audit
Measurement of impairment allowances for expected credit losses on loans from customers is deemed a key audit matter since high level of significant judgements is applied by Management as well as the use of complex models. Additionally, from 1 January 2018, the Bank has adopted IFRS 9 – Financial Instruments ('IFRS 9'), resulting in impairment allowances being recognised when losses are	Based on our risk assessment and industry knowledge, we have examined the impairment allowances for expected credit loss for loans and evaluated the methodology applied as well as the assumptions made according to the description of the key audit matter that allowed us to obtain sufficient appropriate audit evidence for our conclusion. We performed following audit procedures with respect to area of loans:

expected rather than when they have been incurred, as previously used under IAS 39 - Financial Instruments: Recognition and Measurement. Management exercise significant judgements in the following areas: • Use of historic data in the process of determining risk parameters • Estimation of the credit risk related to the exposure • Assessment of stage allocation • Assessment on the significance of subsequent changes in credit risk of an exposure for the purposes of identifying whether significant increase in credit risk has occurred, leading to changes in stage allocation and the required measurement of lifetime expected credit losses • Expected future cash flows from operations • Valuation of collateral and assessment of realization period on individually assessed credit-impaired exposures. Management has provided further information about the impairment allowance on loans from customers in notes '1.5 – Financial assets and financial liabilities', '23 – Financial assets measured at amortised costs', '16 – Impairments' and '2.1 – Credit risk'. Information regarding the transitional effect of IFRS 9 are disclosed in note '44 IFRS 9 – Financial instruments (with the transition impact)' including the impact on shareholders' equity and retained earnings at 1 January 2018.	• Reviewing the Bank's methodology for recognizing impairment allowances for expected credit losses and comparing the reviewed methodology against the requirements of IFRS 9 • Obtaining understanding of control environment and internal controls implemented by the Management within the process of measuring impairment allowance for expected credit losses • Evaluating design and inspecting implementation of identified internal controls relevant to the process of measuring impairment allowance for expected credit losses • Testing identified relevant controls for operating effectiveness • Disaggregating loans account balance based on stage allocation for the purposes of sample selection • Performing substantive tests over recognition and measurement of impairment allowance for expected credit losses on sample of loans allocated to Stage 1 and Stage 2, focusing on: i. models applied in stage allocation ii. assumptions used by the Management in the expected credit loss measurement models iii. criteria used for determination of significant increase in credit risk iv. assumptions applied to calculate lifetime probability of default v. methods applied to calculate loss given default vi. methods applied to incorporate forward-looking information • Performing substantive tests over recognition and measurement of impairment allowance for expected credit losses on sample of individually assessed non-performing loans allocated to Stage 3, which included: i. Assessment of borrower's financial position and performance following latest credit reports and available information ii. Critical assessment of judgements and assumptions applied in the calculation and measurement of expected future cash flows from operations taking into consideration borrower's financial status and performance iii. Reviewing and critically assessing estimated value of collateral and estimated realisation period iv. Critical assessment of discount rates used in the estimation of the

	expected cash flows from operations and/or collateral v. Re-performing calculation of expected credit losses by applying our own independent judgment and assumptions, based on our industry experience, on to calculation and comparing derived result of the impairment losses per certain sampled loans with the ones provided by the Bank.

Other information

Management is responsible for the other information. The other information comprises the information, included in Annual report, other than the financial statements and our auditor's report thereon. Other information were obtained prior to the date of this auditor's report, except Report from Supervisory Board, which is expected to be made available to us after that date.

Our opinion on the financial statements does not cover the other information and we express no assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, assess whether the other information is materially inconsistent with the financial statements, legal requirements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If based on our work performed we conclude that other information include material misstatement we need to report such circumstances.

In relation to this and based on our procedures performed, we report that:

- other information are, in all material respects, consistent with the financial statements;
- other information are prepared in compliance with applicable law or regulation; and
- based on our knowledge and understanding of the Company and its environment obtained in the audit, we did not identify any material misstatement of fact related to the other information.

Responsibilities of Management, Supervisory Board and Audit Committee for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs, 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 of the Company, management is responsible for assessing its ability to continue as a going concern, disclosing matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so

Supervisory Board and Audit Committee are responsible for overseeing the Company's financial reporting process and for approving audited annual report.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's 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 auditing rules 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 auditing rules, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a 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 Company's internal controls.
- 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 Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's 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 auditor's report. However, future events or conditions may cause the organization 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.

With Supervisory Board and Audit Committee we communicate the planned scope and timing of the audit and significant findings from the audit, including deficiencies in internal control we have identified during our audit.

We also provide Supervisory Board and Audit Committee with the statement of compliance with relevant ethical requirements regarding independence, and we communicate with them all relationships and other matters for which it may reasonably be thought to bear on independence, and, if appropriate, all the related safeguards.

From the matters communicated Supervisory Board and Audit Committee, 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 auditor's report unless law or regulation precludes public disclosure about the matter.

Report on Other Legal and Regulatory Requirements

Appointment of the Auditor and the Period of Engagement
Deloitte revizija d.o.o. was appointed as the statutory auditor of the Company on General Shareholders' Meeting held on 17 May 2018. Our total uninterrupted engagement has lasted 5 years.

Confirmation to the Audit Committee
We confirm that our audit opinion on the financial statements expressed herein is consistent with the additional report to the Audit Committee of the Company, which we issued on 22 March 2019 in accordance with Article 11 of Regulation (EU) No. 537/2014 of the European Parliament and the Council.

Provision of Non-audit Services
We declare that no prohibited non-audit services referred to in the Article 5(1) of Regulation (EU) No. 537/2014 of the European Parliament and the Council were provided. There are no services, in addition to the statutory audit, which we provided to the Company, and which have not been disclosed in the Annual Report.

Engagement partner responsible for the audit on behalf of Deloitte revizija d.o.o. is Katarina Kadunc, certified auditor.

DELOITTE REVIZIJA d.o.o.

Katarina Kadunc
Certified auditor

For signature please refer to the original Slovenian version.

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Ljubljana, 22 March 2019

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INDEPENDENT AUDITOR'S REPORT
to the shareholders of ABANKA d.d.

Report on the Audit of the Financial Statements

Opinion

We have audited the consolidated financial statements of the company ABANKA d.d. and its subsidiaries (hereinafter 'the Group'), which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

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

Basis for Opinon

We conducted our audit in accordance with International Standards on Auditing (ISAs) and Regulation (EU) 537/2014 of the European Parliament and of the Council, dated 16 April 2014, on specific requirements regarding statutory audit of public-interest entities. Our responsibilities under those rules are further described in *the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and other 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. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the year ended 31 December 2018. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Impairment of loans to customers (expected credit losses)

In its financial statements for the year ended 31 December 2018 the Group presented loans from customers in the amount of EUR 2,000 million and total expected credit loss in the amount of EUR 72 million.

Key audit matter	How the matter was addressed in our audit
Measurement of impairment allowances for expected credit losses on loans from	Based on our risk assessment and industry knowledge, we have examined the impairment

customers is deemed a key audit matter since high level of significant judgements is applied by Management as well as the use of complex models. Additionally, from 1 January 2018, the Group has adopted IFRS 9 – Financial Instruments ('IFRS 9'), resulting in impairment allowances being recognised when losses are expected rather than when they have been incurred, as previously used under IAS 39 - Financial Instruments: Recognition and Measurement. Management exercise significant judgements in the following areas: • Use of historic data in the process of determining risk parameters • Estimation of the credit risk related to the exposure • Assessment of stage allocation • Assessment on the significance of subsequent changes in credit risk of an exposure for the purposes of identifying whether significant increase in credit risk has occurred, leading to changes in stage allocation and the required measurement of lifetime expected credit losses • Expected future cash flows from operations • Valuation of collateral and assessment of realization period on individually assessed credit-impaired exposures. Management has provided further information about the impairment allowance on loans from customers in notes '1.5 – Financial assets and financial liabilities', '23 – Financial assets measured at amortised costs', '16 – Impairments' and '2.1 – Credit risk'. Information regarding the transitional effect of IFRS 9 are disclosed in note '44 IFRS 9 – Financial instruments (with the transition impact)' including the impact on shareholders' equity and retained earnings at 1 January 2018.	allowances for expected credit loss for loans and evaluated the methodology applied as well as the assumptions made according to the description of the key audit matter that allowed us to obtain sufficient appropriate audit evidence for our conclusion. We performed following audit procedures with respect to area of loans: • Reviewing the Group's methodology for recognizing impairment allowances for expected credit losses and comparing the reviewed methodology against the requirements of IFRS 9 • Obtaining understanding of control environment and internal controls implemented by the Management within the process of measuring impairment allowance for expected credit losses • Evaluating design and inspecting implementation of identified internal controls relevant to the process of measuring impairment allowance for expected credit losses • Testing identified relevant controls for operating effectiveness • Disaggregating loans account balance based on stage allocation for the purposes of sample selection • Performing substantive tests over recognition and measurement of impairment allowance for expected credit losses on sample of loans allocated to Stage 1 and Stage 2, focusing on: i. models applied in stage allocation ii. assumptions used by the Management in the expected credit loss measurement models iii. criteria used for determination of significant increase in credit risk iv. assumptions applied to calculate lifetime probability of default v. methods applied to calculate loss given default vi. methods applied to incorporate forward-looking information • Performing substantive tests over recognition and measurement of impairment allowance for expected credit losses on sample of individually assessed non-performing loans allocated to Stage 3, which included: i. Assessment of borrower's financial position and performance following latest credit reports and available information ii. Critical assessment of judgements and assumptions applied in the calculation and measurement of

	expected future cash flows from operations taking into consideration borrower's financial status and performance iii. Reviewing and critically assessing estimated value of collateral and estimated realisation period iv. Critical assessment of discount rates used in the estimation of the expected cash flows from operations and/or collateral v. Re-performing calculation of expected credit losses by applying our own independent judgment and assumptions, based on our industry experience, on to calculation and comparing derived result of the impairment losses per certain sampled loans with the ones provided by the Group.

Other information

Management is responsible for the other information. The other information comprises the information, included in Annual report, other than the financial statements and our auditor's report thereon. Other information were obtained prior to the date of this auditor's report, except Report from Supervisory Board, which is expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we express no assurance thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, assess whether the other information is materially inconsistent with the consolidated financial statements, legal requirements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If based on our work performed we conclude that other information include material misstatement we need to report such circumstances.

In relation to this and based on our procedures performed, we report that:

- other information are, in all material respects, consistent with the consolidated financial statements;
- other information are prepared in compliance with applicable law or regulation; and
- based on our knowledge and understanding of the Group and its environment obtained in the audit, we did not identify any material misstatement of fact related to the other information.

Responsibilities of Management, Supervisory Board and Audit Committee for the Financial Statements

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

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

Supervisory Board and Audit Committee are responsible for overseeing the Company's financial reporting process and for approving audited annual report.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's 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 auditing rules will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal controls.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the organization to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence concerning the financial information of the entities or business activities within the Group in order to express an opinion on the consolidated financial statements. We are responsible for conducting, overseeing and performing the audit of the Group. We have sole responsibility for the audit opinion expressed.

With Supervisory Board and Audit Committee we communicate the planned scope and timing of the audit and significant findings from the audit, including deficiencies in internal control we have identified during our audit.

We also provide Supervisory Board and Audit Committee with the statement of compliance with relevant ethical requirements regarding independence, and we communicate with them all relationships and other matters for which it may reasonably be thought to bear on independence, and, if appropriate, all the related safeguards.

From the matters communicated Supervisory Board and Audit Committee, 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 auditor's report unless law or regulation precludes public disclosure about the matter.

Report on Other Legal and Regulatory Requirements

Appointment of the Auditor and the Period of Engagement
Deloitte revizija d.o.o. was appointed as the statutory auditor of the Company on General Shareholders' Meeting held on 17 May 2018. Our total uninterrupted engagement has lasted 5 years.

Confirmation to the Audit Committee
We confirm that our audit opinion on the financial statements expressed herein is consistent with the additional report to the Audit Committee of the Company, which we issued on 22 March 2019 in accordance with Article 11 of Regulation (EU) No. 537/2014 of the European Parliament and the Council.

Provision of Non-audit Services
We declare that no prohibited non-audit services referred to in the Article 5(1) of Regulation (EU) No. 537/2014 of the European Parliament and the Council were provided. There are no services, in addition to the statutory audit, which we provided to the Company and its controlled undertakings, and which have not been disclosed in the Annual Report.

Engagement partner responsible for the audit on behalf of Deloitte revizija d.o.o. is Katarina Kadunc, certified auditor.

DELOITTE REVIZIJA d.o.o.

Katarina Kadunc
Certified auditor

For signature please refer to the original Slovenian version.

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Ljubljana, 22 March 2019

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