Regional Investment Bank

AS "Reģionālā investīciju banka"

Pilar III

Information Disclosure year 2018

Introduction

The information disclosure report is prepared according to the article 36.[3] paragraph (3) of Latvian Republic Credit Institution Law and part 8 of European Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013.
The report provides additional information to the information provided by the annual report concerning risk management of the Bank, capital adequacy, risk exposures, capital buffers, leverage ratio, unencumbered assets and remuneration policy.

Information about the Bank

The information is published by the Group and the Bank on its website at least once a year. If the difference between the results of the bank and the Group is insignificant, information is disclosed about The Group or the Bank with the explanation of the difference in the results.
In August 2016, the Bank established a 100% subsidiary - the limited liability company *Grunewald Residence*. The total direct Bank's investment into this subsidiary, as at December 31, 2018 was 92.42% or 6.1 million EUR. The Bank and the subsidiary are fully consolidated. The is no any current or foreseen material practical or legal impediment to the prompt transfer of own funds or repayment of liabilities among the Bank and its subsidiary.

Risk Management

Risk management is an integral part of the Bank's core business activities. The Risk Management Strategy has been developed for the purpose the Bank's risk management, which is based on the principle of performing banking activities without incurring losses and is oriented to achieve an optimal balance between profitability of the Bank's commercial operations and acceptable level of risks.

The Risk Management Strategy of the Bank implies :

- compliance to strategic goals set by the Council of the Bank;
- effective management of available own capital and sufficient level of capitalization;
- accounting for the level of risks when evaluating performance of the Bank;
- development of adequate risk management system/environment and its effective functioning;
- development and documentation of risk management policies and control procedures at least for significant risks identifies by the Bank which include:
- methods and regularity of risk measurement and evaluation;
- adequate risk control procedures, including setting maximal limits and restrictions, risk minimization methods, control procedures in order to minimize quantitatively insignificant risks;
- regular flow of information among the Council of the Bank, The Board of the Bank and the heads of the departments of the Bank concerning the existing risks of the Bank, levels and tendencies of these risks, their impact on the amount of the Bank's capital and level of its adequacy and other important related information for decision making;
- risk management policy and control procedures, i.e. procedures of controlling and monitoring of limits' and restrictions' fulfillment;
- division of responsibilities, obligations and rights in risk management.

Risk identification, risk measurement, risk monitoring, risk control and minimization are main principals of risk management of the Bank.

The following risks are identified as significant for the Bank's activities: credit and residual risk, liquidity risk, concentration risk, prevention of money laundering and terrorism financing risk, business model risks, compliance and reputational risks.

Credit Risk and Residual Risk

Credit risk is a risk of losses in case the borrower (loan taker, debtor) or business partner of the Bank is unable or refuses to fulfill his/her obligations towards the Bank under the agreement provisions. Credit risk is related to the Bank’s operations which create claims of the Bank against other parties and which are reflected in the Bank’s balance and off-balance sheets.

The residual risk is a risk that the credit risk mitigation methods used by the Bank might turn out to be less efficient than planned.

The Bank’s principles with respect to assessment, monitoring and accepting of credit risk have been described and approved within the Credit Policy, Business Partner Policy and Investment Policy.

The Bank categorizes and controls its credit risk by determining limits of different types and amounts: limits for the acceptable risk for each debtor, related debtors’ groups, geographic regions, business sectors, types and amounts of guarantees, currencies, terms and ratings granted by international agencies.

Credit risk is also regularly monitored individually for each debtor evaluating the debtor’s ability to repay the principal amount and interest, as well as changing the limits set, if necessary.

The Bank's exposure to credit risk is also monitored and minimized by ensuring adequate collaterals and registering the guarantees on behalf of the Bank. The real value of these guarantees and collaterals is regularly reviewed.

The collateral is a property or rights which can serve as the alternative source of the loan repayment in a case, if the Customer does not meet his/her debt obligations.

As collateral, the Bank accepts assets that meet the following criteria:

- has the market value of assets as determined in the pledge assessment by independent expert and its changes are predictable within the loan agreement term. Both the market value of assets and value in case of urgent, forced sale are considered;
- assets are liquid, i.e. they may be disposed in a comparatively short term for a price which is close to the urgent, forced sale value (or market value);
- there is a legal and actual opportunity to control these assets in order to prevent their misuse by the debtor or asset owner;
- the Bank's rights to these assets have a legal priority over other creditors of the owner’s assets (or over those creditors’ rights which are in a more privileged position with respect to the Bank’s rights in the total amount, which makes up an insignificant amount in comparison with the collateral value), as the exception admitting the legal priority of Bank Pivdennyi’s claims

Only certain types of assets are accepted as collateral, and each type of collateral has its own defined limits with respect to the maximum loan amount against such collateral. Most frequently accepted types of collaterals:

- time deposits placed with the Bank;
- real estate;
- industrial production facilities;
- land (depending on its geographical location, possibilities of its use, communications, cadastral value, etc.);
- unused motor (passenger) cars;
- unused lorries, tractors;
- used (second-hand) motor (passenger) cars, which are not older than 7 years, and the lorries, which are not older than 9 years, the tractors, which are not older than 5 years;
- other motor cars/lorries and tractors;
- ships/vessels;
- stocks (goods in the customs warehouses or otherwise controlled goods in the warehouse of their owner);
- technological equipment and machinery;
- other fixed assets of the company;

- accounts receivable (as a totality of objects;
- securities, capital shares, bills of exchange;
- guarantees.

The value of the real estate shall be determined based on the opinion of the independent experts and this evaluation shall be corrected, based on the Bank's experience and normative documents.

The market value of the stocks (the goods in the customs warehouses or otherwise controlled goods) and the market value of the stocks (the goods in the warehouse of its owner) shall be determined, based on the publicly available prices, the pricing mechanism of which is understandable and acceptable for the Bank.

The market value of the technological equipment and machineries shall be determined, according to the balance sheet residual value of the equipment, if the fixed assets accounting methods, applied by the Customer, correspond to the generally accepted practice, and if possible, it is also recommended to receive the experts' opinion. If the residual value of the fixed asset is big, then the documents, confirming the purchase value of this fixed asset, shall be checked.

The collateral security – movable or immovable objects, which are evaluated by the appraisal companies, appointed by the Bank, except for the cases, when the Bank's Board has authorized a competent employee to make an appraisal.

Any collateral, except land, securities, debtor debts and other nonmaterial assets, must be secured on behalf of the Bank for the loan agreement's term.

In order to efficiently manage credit risk and assess performance of the Bank's activity, the Bank carries out regular evaluation and classification of assets (incl. loans) and off-balance sheet liabilities. "Stages" of the credit risk in accordance with International Financial Reporting Standard 9 (IFRS 9):

- "Stage 1" – credit exposure not subject to a significant increase in credit risk.
- "Stage 2" – credit exposure subject to a significant increase in credit risk.
- "Stage 3" – loans in respect of which default has occurred.

The main assessment criteria for assets and contingent liabilities are the Customer's (borrower's) discounted future cash flow, creditworthiness, and days past due (DPD).

In assessing losses caused by deterioration in credit quality, the following factors shall be considered:

- information regarding overdue payments, and
- other justified information to be considered with regard to future forecasting, which is freely available with no extra charge.

Regardless of the type of information used, it is assumed that the credit risk of a credit exposure has increased significantly since initial recognition, if payments for the credit exposure have been past due by more than 30 days at least once within the last 3 months. The Bank revises the duration of this period at least once a year, based on the current available information.

Non-performing exposures (NPE) are those whose risk of non-repayment has increased significantly compared to the risk accepted at the time of the loan granting, and which satisfy either or both of the following criteria:

- the fulfilment of any borrower's material credit obligations towards the Bank, its parent company or any of its subsidiary companies is more than 90 days past due;
- the borrower is assessed as unlikely to pay its credit obligations in full without realisation of collateral.

The Bank uses a number of criteria to assess whether a borrower is able to make a repayment, the basic criteria of which are as follows:

- Losses, which have occurred as a result of past or present events, affect one or several credit exposures.
- A loan has a non-profitable status.
- A loan is in the process of recovery.
- Write-down or reservation of specific loan loss provisions (LLP).
- The forbearance of a loan, which will most likely diminish financial commitments (distressed restructuring), or the loans of a particular borrower have already been forborne more than once.

- The borrower has applied for or bankruptcy proceedings or a similar protection activity has been commenced against the borrower, as the result of which the repayment of a loan to the Bank might be delayed or not take place at all.
- The borrower's regular sources of income are no longer sufficient for the repayment of obligations.
- There are justified concerns regarding the borrower's ability to generate stable and sufficient cash flows in future.
- The Bank has requests the enforcement of pledge or guarantee.
- The Bank has identified fraudulent activities in relation to a particular credit transaction.
- The deferment/prolongation of loan payments, which exceeds the economically justified duration (usually, the loan period cannot exceed 10 years, except loans disbursed in accordance with the Loan Description: "Real Estate Acquisition Loan" (II.07.30), for which the period cannot exceed 15 years).
- Non-observance of the maximum LTV if funding is implemented on the basis of assets.
- The Bank stops the deduction of interest (also partially or conditionally).
- The claim sold with losses which refer to the loan.

The size of high-risk and overdue high-risk transactions as well as the size of the provisions set aside to cover bad loans by most important industries, thous. EUR is as follows:

	31.12.2017		31.12.2017		The Average Size in 2018	
High-risk Transactions by Industries	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount
Forestry, agriculture	8 916	108	4 062	422	6 489	265
Manufacturing, processing industry	7 641	907	5 435	1 764	6 538	1 336
Trade	45 302	9 619	37 480	3 161	41 391	6 390
Transport	29 684	2 484	31 937	4 173	30 811	3 329
Financial services	3 482	2 176	3 784	632	3 633	1 404
Real estate operations and construction	15 405	6 873	19 126	7 591	17 266	7 232
Accommodation and food services	3 139	1 386	629	153	1 884	770
Other services	587	0	920	526	754	263
Natural persons, overdrafts	10 966	2 935	6 386	3 192	8 676	3 064
The total size of high-risk transactions	125 121	26 488	109 759	21 614	117 440	24 051
	31.12.2017		31.12.2018		The Average Size in 2018	
Overdue (>90 days) High-Risk Transactions by Industries	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount
Forestry, agriculture	0	0	332	102	166	51
Manufacturing, processing industry	907	907	1 645	1 545	1 276	1 226
Trade	7 020	5 161	1 824	739	4 422	2 950
Transport	2 742	2 309	2 806	2 563	2 774	2 436
Financial services	0	0	484	406	242	203
Real estate operations and construction	6 889	3 800	10 390	6 943	8 640	5 372
Accommodation and food services	1 386	1 387	149	149	768	768
Other services	0	0	920	526	460	263
Natural persons, overdrafts	1 982	1 982	745	745	1 364	1 364

The total size of high-risk transactions	20 926	15 625	19 295	13 718	20 111	14 672

The size of overdue high-risk transactions as well as the size of the provisions set aside to cover bad loans by most important regions, thous. EUR is as follows:

	31.12.2017		31.12.2018		The average extent in 2018	
Risk Transactions by Most Important regions*, EUR	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount
UAE	0	0	346	0	173	0
USA	607	0	3 410	7	2 009	4
Australia	0	0	354	1	177	1
Austria	9 839	0	10 306	191	10 073	96
Bulgaria	375	0	0	0	188	0
Canada	0	0	171	0	86	0
Russia	20 716	0	17 175	3 619	18 946	1 810
China	0	0	341	0	171	0
Latvia	43 350	15 622	36 731	14 837	40 041	15 230
United Kingdom	7	0	708	1	358	1
Ukraine	44 730	10 494	37 054	2 585	40 892	6 540
Germany	5 343	372	3 135	372	4 239	372
Other	154	0	28	1	91	1
The total size of high-risk transactions	125 121	26 488	109 759	21 614	117 440	24 051
	31.12.2017		31.12.2018		The average extent in 2018	
Risk Transactions by Most Important regions*, EUR	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount	The Loan Balance to be Repaid	Special Provisions to Cover the Principal Amount
Germany	372	372	372	372	372	372
Latvia	16 699	12 227	18 764	13 270	17 732	12 749
Ukraine	3 854	3 026	159	76	2 007	1 551
The total size of high-risk transactions	20 926	15 625	19 295	13 718	20 111	14 672

The description of assets pledged to the bank as of the 31st of December 2017 can be found in annual report.

The given in the report data represents credit risks exposures of the loan portfolio of the Bank. The loan portfolio of the Group is different of that of the Bank's only in one credit risk exposure, i.e. the loan issued to an affiliated company which is registered in Latvia - SIA "Grunewald Residence". The total amount of the loan as on 31.12.2018. was 2 761 443 EUR, special provisions amounted to 695 EUR. The company operates in immovable property operations' sector, and the creditor fulfills all his obligations on time. The loan is mainly issued against the pledge of a deposit hold at the Bank (more than 96% of the loan is covered by this deposit)

Operational Risk

Operational risk is a risk to incur losses due to inadequate or failing internal processes of the Bank, activity of people and system, or due to effect of external conditions. The operational risk means that the Bank's income may decrease/additional expenditure may occur to the Bank (and, as a result, the equity capital might decrease) due to errors in transaction with customers/business partners, information processing, making of inefficient decisions, insufficient human resources, or insufficient planning of external conditions effects.

For the evaluation of the operational risk, self-evaluation process of the operational risk is used during which the Bank assesses performed operations against the types of the operational risk; the Bank's strong and weak sides regarding the management of the operational risk are identified.
The Bank has developed and maintains the Operation Risk Events and Losses Data Base in which the internal data on operational risk events and related losses is collected, summarized and classified.
The basic elements of the operational risk management:

- operational risk monitoring;
- operational risk control and minimisation:
- development of internal normative documents which exclude/minimise the possibility of operational events;
- compliance with the principle of division of duties;
- control of execution of internal limits;
- compliance with the defined procedure when using IT and other Bank's resources;
- appropriate training of employees;
- regular checks of transactions and account documents;
- ensuring the continuity of operation;
- stress testing.

Market Risk

The Bank's activity is exposed to market risk through the Bank's investments in the interest rates and currency product positions. All these products are exposed to systematic and specific market fluctuations. The Bank controls market risks by diversifying its financial instruments portfolio, setting restrictions for different types of financial instruments and carrying out sensitivity analysis which reflects the effect of the respective risks on the Bank's assets and equity capital.

Position Risk

Position risk – possibility to incur losses due to revaluation of position of debt securities or capital securities, when the price of the respective securities changes. The position risk can be categorised as specific and systematic risk:

- specific risk – possibility to incur losses if the debt securities' or capital securities' price will change due to factors related to the securities issuer;
- systematic risk – possibility to incur losses if the securities' price will change due to factors related to interest rate changes (in case of debt securities) or with significant changes in the capital market (in case of capital securities), which are not related to the specific securities issuer.

Basic elements of position risk management:

- evaluation and analysis of securities' portfolio;
- analysis and monitoring of issuers' financial position;
- setting of internal limits on exposures/diversification (stop-loss; issuers, countries, regions, terms, credit rating groups etc.);
- control of execution of the internal limits.

Interest Rate Risk

The interest rate risk is characterized by the influence of the market rate changes on the Bank's financial results. The Bank's everyday activity depends on the interest rate risk, which is influenced by the terms of repayment of assets and liabilities related to the interest income and expenditures or interest rate review dates. This risk is controlled by the Bank's Assets and Liabilities Committee by defining the limits of the interest rate coordination and evaluating the interest rate risk undertaken by the Bank.
For the evaluation of interest rate risk, the effect of interest rate changes on the Bank's economic value is assessed, incl. the evaluation of interest rate risk from the perspective of income and the evaluation of interest rate risk from the perspective of economic value. The evaluation of the interest rate risk is carried

out once per month. Furthermore, at least 2 times per year, the stress tests of the interest rate risk are applied.

For monthly evaluation of the interest rate risk, for all balance sheet positions interest rate changes of +/-50/-+/-100 basis points are applied; for stress testing of interest rate risk – +/-200 basis points. Division of assets, liabilities and off-balance positions by term in the groups of term structures is carried out on the basis of:

- shortest term from the outstanding repayment/settlement/clearance term – for financial instruments with fixed interest rate;
- term until the next interest rate changes date or interest rate re-evaluation term – for financial instruments with a floating interest rate.

Basic elements of interest rate risk management:

- sensitivity analysis of interest rate risk;
- setting of internal limits (limit for decrease in economic value and for duration of securities' portfolio);
- control of compliance to the internal limits;
- carrying out of interest rate stress tests and analysis of their results;
- carrying out of hedging operations, if necessary.

Currency Risk

The Bank's activity is exposed to the risk of exchange of the main currencies involved in it, which influences both the Bank's financial result and cash flow. The Bank controls the foreign currency assets and liabilities in order to avoid inadequate currency risk. The Board determines the limits for the open positions of foreign currencies, and these limits are being supervised every day. The legislation of Latvia states that no individual foreign currency open position of the credit institution shall exceed 10% of the equity capital of the credit institution, and the total foreign currency open position shall not exceed 20% of the equity capital. During 2018, the Bank did not exceed these limits.

The Bank's foreign currency risk evaluation is based on the following basic principles:

- evaluation with respect to how the Bank's assets, liabilities and off-balance sheet items value changes due to changes in currency rates;
- how the Bank's income/expenditure changes due to changes in currency rates;
- the currency risk stress testing is performed.

Basic elements of currency risk management:

- evaluation of currency risk;
- setting of limits and restrictions;
- control of execution of these limits;
- currency risk stress testing and analysis of the results;
- carrying out of hedging operations, if necessary.
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Transaction Concentration Risk

Transaction concentration risk is a risk that occurs from transaction concentration. In order to restrict the transaction concentration risk, the Bank determines limits for investments in various assets, instruments, markets etc. One of the most significant transaction concentration risks is the concentration of geographic regions (country risk).

Country Risk

Country risk – country partner risk – the possibility to incur losses if the Bank's assets are invested in a country whose changing economic and political factors may create problems for the Bank to retrieve its assets in the planned time and extent. A partner's and issuer's default occurs mainly due to currency devaluation, unfavorable changes in legislation, creation of new restrictions and barriers and other conditions, including force majeure factors.

For the country risk analysis, information of the international rating agencies (incl. credit ratings, their dynamics), economic indicators of countries and other related information is used.

Fundamental elements of risk control:

- setting of internal limits by regions, countries and transaction types in individual countries;
- control of execution of the internal limits;
- country risk analysis and monitoring;
- review of internal limits.

Assets, liabilities and off-balance sheet country risk is attributable to a country which may be considered the customer's main country of entrepreneurship. If the loan is granted to a resident of another country against a pledge, and this pledge is physically located in another country which is not the legal person's country of residence, the country risk is transferred to the country where the loan's pledge is actually located.

Compliance and reputational risk

Compliance risk is a risk that the bank may incur losses, or certain legal obligations may be imposed on it, or it may face certain sanctions, or its reputation may be damaged due to non-compliance with or violation of certain legislative acts, regulations and standards.

Reputational risk is a risk that the bank's clients, partners, shareholders, regulatory institutions and other stakeholders may form a negative opinion with respect to the bank. As a result, it may have a negative impact on the bank's ability to maintain existing or establish new business relationships with its clients and other business partners as well as having a potential negative impact on the bank's access to financing. Reputational risk incidents may also raise the level of risks stemming from other areas of the bank's activities (credit risk, liquidity risk, market risk etc.), thus having a negative impact on the bank's profitability, size of the capital base and liquidity.

In accordance with legislative acts the bank establishes and maintains an effective compliance and reputational risk management framework which ensures the bank's compliance with legislative acts, regulations and standards and in doing so preventing possible losses from happening, the imposition of legal obligations, the application of sanctions or the worsening of the bank's reputational profile. The bank's compliance control function stems from a risk-based approach, thus ensuring that the focus of compliance oversight and consultation activities is reasonable and up-to-date.

The primary tasks of the bank's compliance control function is as follows:

- identifying, assessing and managing compliance and reputational risk which, among other things, provides for a regular monitoring of applicable legislative requirements and an assessment of related risks, controlling the incorporation of applicable legislative requirements into the bank's processes and documents, compliance oversight audits in accordance with Council-approved work plans etc.
- implementing preventive activities with the aim to timely and fully define, document and assess bank-related compliance and reputational risks at an initial phase, including, among other things, developing adequate internal regulations before introducing new products and services or making significant changes in their design, training employees and providing guidance on compliance-related topics etc.
- creating the bank's business reputation by ensuring compliance with the bank-related regulatory requirements as well as complying with professional ethics standards, including preventing conflicts of interests and corruption while conducting the bank's activities as well as proper oversight over the complaint process.

The bank has developed and approved a Compliance and Reputational Risk Management Policy which provides for compliance and reputational risk management objectives, tasks and major principles, bank management and business units' tasks and responsibilities in the field of compliance and reputational risk as well as procedures regulating the report preparation and information provision process.

The bank has established a structural unit whose responsibility is to manage compliance and reputational risks, to ensure an independent control as well as to regularly and comprehensively assess respective risks and to submit reports to the Board and the Council.

Prevention of money laundering and terrorism financing (AML/CFT) risk

The AML/CFT risk refers to the possibility of using a credit institution in the process of legalizing criminally acquired funds or financing terrorist activities.

The Bank has developed an internal AML/CFT risk management control system. It is based on a clear understanding of possible AML/CFT risks and necessary, relevant, proportionate and sufficient measures aimed at the prevention of such risks.

The bank has developed control policies, procedures and mechanisms based on the KYC-Know-Your-Customer principles. The risk-based approach ensures that one applies sufficient and proportionate measures with respect to each client in accordance with his/her risk profile.

The bank complies with Latvian and international legislative requirements which regulate anti-laundering and terrorism financing prevention, ensures compliance with sanctions imposed in accordance with EU regulations, UN and OFAC acts as well as compliance with professional and ethical standards.

The bank has developed internal regulations which define the responsibility of its executive officers and employees in the field of AML/CFT risk management, describe the framework for a timely and rigorous identification of AML/CFT risks in the context of the bank's services, products and internal processes.

In order to manage the AML/CFT risk there is a permanent risk monitoring. Its major objective is to ensure a timely identification and elimination of shortcomings in the bank's internal documentation and daily work processes and a proper function of the AML/CFT risk management process under changing circumstances in order not to allow a weakening of the internal control mechanism. There is a regular assessment of AML/CFT risks and a preparation of relevant reports as well as a regular update of the risk management strategy and processes.

The bank's Council and the Board bear responsibility to manage the AML/CFT risks in an effiecient way. The bank's Council approves an AML/CFT policy and appoints Board members responsible for managing the AML/CFT risks.

There is a decision-making entity within the bank in the form of a AML/CFT risk management committee which ensures that there is an efficient client oversight and a daily AML/CFT risk management.

In order to reduce the AML/CFT risk the bank employs the following main methods:

- The identification of the AML/CFT risks by clearly determining existing and residual risks and by introducing relevant and efficient procedures to reduce these risks.
- Procedures define processes of client identification, approval and monitoring, instructions for client inquiries and extended inquiries, a course of action when providing a new product to a client, cooperation with correspondent banks and partners and other processes;
- A relevant oversight/monitoring system to cover a client's activities and transactions which comprises specialized IT tools to automatically scan and map transactions with reference lists, comparison with previously defined scenarios and limit controls in order to ensure the identification of unusual and suspicious transactions;
- A client oversight is conducted in accordance with automatically assigned client risk groups (low, moderate, high, very high), thus ensuring the automated maintenance and usage of a limit and restriction system to oversee a client's activities based on risk factors such as a client type, residence, expected/existing transaction size, a politically exposed person status, expected/existing types of services to be used etc.
- An extended client examination for high-risk clients, including a course of action to follow when initiating and maintaining relationships with politically exposed persons;
- Procedures to initiate relationships with correspondent banks and partners, including a course of action to follow when assessing, examining and monitoring relevant risks;

- Information flow management, namely, the storage of information obtained when conducting the control and examination processes as well as the maintenance of required processes to ensure regular client information updates;
- A course of action to follow when discovering and reporting unusual and suspicious transactions.

The bank follows a Three-Defense-Line principle while managing the AML/CFT risks. Client relationship units have a primary role to play in the process of a client identification and verification as well as a unusual and suspicious transactions identification and further reporting. AML/CFT risk management units form a second line of defense, thus ensuring daily control activities. The Internal Audit unit forms a third line by conducting, not less than once in 18 months, the efficiency assessment of the AML/CFT risk management functions.

The bank also provides for an independent assessment of the AML/CFT internal control system not less than once in 18 months by hiring independent and professional outside assessors.

Business model risk

Business model risk refers to a risk that certain changes in the bank's business environment and its inability to react to these changes in due time or the bank's inappropriate or incorrectly selected development strategy, or the bank's inability to provide for sufficient resources to implement a strategy may have an adverse effect on the bank's profitability, capital size and liquidity.

In late 2018 the bank's management reviewed and approved a 5-year strategy in accordance with which lending is one the bank's priority activities.

To manage business model risk the bank undertakes the following activities:

- strategic planning for the period of 5 years;
- developing a current financial plan;
- capital planning;
- stress testing.

Liquidity Risk

The Bank is subject to the daily risk that it might need to use the available funds and short-term liquid assets for the fulfillment of its short-term liabilities. The term relation of assets and liabilities, as well as off-balance items, is related to liquidity risk and reflects to what extent funds would be necessary to fulfill the existing liabilities.

Terms and capabilities of the assets and liabilities to replace the liabilities, which inflict interest and have a due payout term, at acceptable costs are significant factors for determination of the Bank's liquidity and its exposure to the changes in the interest rates and currency rates.

Such coordination of assets and liabilities, and control of this coordination is one of the Bank's most important daily management tasks.

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The Bank is using the following methods for the measurement of liquidity risk:

- evaluation of existing and planned assets, liabilities, and off-balance sheet liabilities term-structure broken down by financial instruments, various term intervals in all currencies together and individually, in which the Bank performs a significant amount of transactions (i.e. currency the proportion of which in the Bank's assets/liabilities exceeds 5%) or which has a non-liquid market;

- determining liquidity indicators used for liquidity risk analysis and control;
- determining internal limits:
- assets and liabilities term structure net liquidity positions in euro and all foreign currencies in which the Bank performs a significant amount of transactions (i.e., currency the proportion of which in the Bank's assets/liabilities exceeds 5%) or which has a non-liquid market;
- for deposit concentration;
- for other liquidity indicators which the Bank has specified for the liquidity risk control;
- stress testing.

By specifying the calculation procedure of liquidity indicators and by its determining limits, the Bank takes into account its operational targets and the acceptable risk level.

The Bank determines and regularly analyses the early warning indicator system which may help to identify the vulnerability of the Bank's liquidity position and the necessity to attract additional financing.

On the basis of data of the early warning indicator system, the Bank identifies the negative tendencies which affect liquidity, analyses them and evaluates the necessity to carry out measures reducing the liquidity risks.

The liquidity risk management methods (basic elements) are as follows:

- fulfillment of liquidity indicator limits;
- determining of net liquidity position limits;
- determining restriction on deposit concentration;
- control of compliance with the defined limits;
- liquidity stress testing and analysis of the results;
- proposals for solving liquidity problems;
- setting and monitoring of a set of indicators for liquidity evaluation;
- maintenance of an adequate liquidity buffer which covers the positive difference between the planned outgoing and incoming cash flows within the term interval of up to 7 days and 30 days.

In accordance with FCMC's requirements, the Bank maintains sufficient liquid assets for the fulfillment of its obligations.

Liquidity Coverage Ratio

The ratio was calculated in line with the Liquidity Coverage Ratio Disclosure Principles to comply with the European Banking Authority's (EBA) Regulation in addition to the European Union's Liquidity Risk Management Disclosure Regulation No. 575/2013, paragraph 435.

The Bank, thous. EUR		**Total Corrected Value**			
		31.03.18	30. 06.18	30.09.18	31.12.18
21	Liquidity Reserves	229 754	192 996	154 233	155 280
22	Total Net Cash Outflow	72 300	64 804	46 772	53 265
23	Liquidity Coverage Ratio (%)	318%	298%	330%	292%

The Group, thous. EUR		**Total Corrected Value**			
		31.03.18	30. 06.18	30.09.18	31.12.18
21	Liquidity Reserves	134 446	132 940	130 344	116 233
22	Total Net Cash Outflow	44 800	42 119	56 811	60 246
23	Liquidity Coverage Ratio (%)	300%	316%	229%	193%

Assumptions and clarifications with respect to the calculation of the Liquidity Coverage Ratio.

The bank recognizes the following assets as the Level I ones:

- coins and banknotes;

- transactions with the central banks of the member countries;
- the bank's reserves placed with the central bank;
- assets issued or guaranteed by the governments of the member countries;
- assets issued or guaranteed by the governments of other countries given these are allocated to the 1st credit quality category within the credit assessment process in accordance with the EU Regulation 575/2013.

The bank applies a 0% discount rate for those assets.

The bank recognizes the following assets as the Level II ones:

- 2.A assets: The bank does not possess such assets at the moment.
- 2.B assets: Corporate debt securities which comply with the EU Regulation 2015/61's requirements.

The bank applies at least a 50% discount rate for the market value of those assets.

The bank classifies as the LSR Liquid assets (LSR liquidity reserves) those assets which comply with the EU Regulation 2015/61's general and operational requirements.

Net expected cash outflow.

The net expected cash outflow is calculated as a difference between the amount of expected cash outflows and the amount of expected cash inflows in accordance with the calculation procedure as set in Paragraph 20 of the EU Regulation 2015/61.
The cash outflows and the cash inflows are assessed during a 30-day stress period given the assumption of a combined institution-level and market-wide stress scenario as mentioned in Paragraph 5 of the EU Regulation 2015/61.

Assumptions with respect to the expected cash outflow.

The expected cash outflow is calculated as the balance value of the bank's obligations and off-balance-sheet obligations multiplied with respective rates reflecting the speed with which those positions are expected to decline during a stress period.
A 10% discount rate is applied to the deposits placed by natural persons and SMEs.
Enterprises are classified as commercial companies. A 20% discount rate is applied to the state-guaranteed share of a deposit while a 40% expected cash-outflow discount rate is applied to the non-guaranteed share.
A 15% discount rate and a 20% discount rate is applied to the deposits placed by natural persons and SMEs with an elevated probability of cash outflow.
A 10% cash-outflow discount rate is applied to such off-balance-sheet obligations as credit lines and overdrafts.
A 5% cash-outflow discount rate is applied to such off-balance-sheet obligations as trade transactions.
A 100% cash-outflow discount rate is applied to the following instruments:

- Derivative-related cash outflows.
- Obligations towards monetary financial institutions and other financial institutions.
- Other obligations.

Assumptions with respect to the expected cash inflow.

The expected cash inflow should be assessed during a 30-calendar-day period. It is comprised of cash inflows, as stipulated by respective contracts, resulting only from those high-risk transactions which are not classified as being delayed as well as there is no basis for the bank to expect them to get delayed within a 30-calendar-day period.

The bank sets operational deposits as being equal to 15% of the balance value of correspondent accounts and applies a 5% cash-inflow rate to this share of correspondent accounts.

When calculating the LSR the bank sets a limit amounting to 75% of the total expected cash inflow.

The planned revenue from the loan principal repayments being made by non-financial clients are reduced by 50% from the size of the repayment.

A 100% rate is applied to the following instruments:

- cash claims towards monetary financial institutions;
- securities with the maturity of up to 30 calendar days which are not classified as highly liquid ones;
- net derivative-related cash inflows.

Information disclosure with respect to encumbered and unencumbered assets

Information disclosure with respect to encumbered and unencumbered assets is prepared in accordance with the Commission-delegated Regulation 2017/2295's requirements.

Asset encumbrance in the context of the bank's balance sheet is quantitatively insignificant, given that the bank's encumbered assets primarily serve the purpose of ensuring its ability to provide services. The bank places its assets in such a way as to maintain a high level of liquidity and to be able to meet its current obligations towards clients at any time.

The bank's assets are primarily encumbered when conducting trade finance transactions and when placing required collateral in transactions involving service provision to the bank's clients.

There are no transactions involving asset encumbrance between the bank and its subsidiaries.

In its calculations of the risk value of encumbered assets for the year 2018 the bank used the median of the sums of four quarterly end-of-period values over the previous 12 months.

Encumbered and unencumbered assets of the Bank according to specifics of the Bank, thous. EUR

Encumbered and unencumbered assets		Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	of which EHQLA and HQLA*	Fair value of unencumbered assets	of which EHQLA and HQLA*
		010	040	060	80	090	100
010	Assets of the reporting institution	4 636	0	53 005	0	0	0
030	Equity instruments	0	0	243	0	8	0
040	Debt securities	0	0	26 476	23 982	26 476	23 982
050	of which: covered bonds	0	0	0	0	0	0
060	of which: asset-backed securities	0	0	0	0	0	0
070	of which: issued by financial corporations	0	0	23 242	23 242	23 242	23 242
080	of which: issued by financial corporations	0	0	1 747	0	1 747	0
090	of which: issued by non-financial corporations	0	0	1 487	740	1 487	740
120	Other assets	4 363	0	26 286	0	0	0
121	of which: collateral in payment-card transactions	1 228	0	0	0	0	0

121	of which collateral for investment services	3 408	0	0	0	0	0
121	of which: fixed assets and intangibles	0	0	14 122	0	0	0
121	of which: equity participations in subsidiaries	0	0	6 100	0	0	0

Encumbered and unencumbered assets of the Group according to the specifics of the Group, thous. EUR

Encumbered and unencumbered assets		Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	of which EHQLA and HQLA*	Fair value of unencumbered assets	of which EHQLA and HQLA*
		010	040	060	80	090	100
010	Assets of the reporting institution	4 636	0	53 051	0	0	0
030	Equity instruments	0	0	243	0	8	0
040	Debt securities	0	0	26 476	23 982	26 476	23 982
050	of which: covered bonds	0	0	0	0	0	0
060	of which: asset-backed securities	0	0	0	0	0	0
070	of which: issued by financial corporations	0	0	23 242	23 242	23 242	23 242
080	of which: issued by financial corporations	0	0	1 747	0	1 747	0
090	of which: issued by non-financial corporations	0	0	1 487	740	1 487	740
120	Other assets	4 363	0	28 813	0	0	0
121	of which: collateral in payment-card transactions	1 228	0	0	0	0	0
121	of which collateral for investment services	3 408	0	0	0	0	0
121	of which: fixed assets and intangibles	0	0	14 122	0	0	0
121	of which: equity participations in subsidiaries	0	0	6 100	0	0	0

Comments:
*EHQLA – assets of extremely high liquidity and credit quality;
HQLA- assets of high liquidity and credit quality.

The bank's assets are primarily encumbered when conducting trade finance transactions and the value located at the intersection of row 120 and column 010 consists of the assets which serve as collateral in client transactions involving payment cards.

The value located at the intersection of row 060 and column 040 is available to the bank for asset encumbrance. The most significant percentage of this value is comprised of government-issued debt securities.

The bank would not consider the assets located at the intersection of row 060 and column 120 as available for possible encumbrance while undertaking ordinary commercial activities. The most significant percentage of these assets consists of fixed assets and equity participations in subsidiaries.

Collateral received (The Group and the Bank), thous. EUR

Collateral received		Fair value of encumbered collateral received or own debt securities issued	Unencumbered Fair value of collateral received or own debt securities issued available for encumbrance
		010	040
130	Collateral received by the reporting institution	0	0
140	Loans on demand	0	0
150	Equity instruments	0	0
160	Debt securities	0	0
170	of which: covered bonds	0	0
180	of which: asset-backed securities	0	0
190	of which: issued by financial corporations	0	0
200	of which: issued by non-financial corporations	0	0
210	of which: issued by non-financial corporations	0	0
220	Loans and advances other than loans on demand	0	0
230	Other collateral received	0	0
240	Own debt securities issued other than own covered bonds or asset-backed securities	0	0
241	Own covered bonds and asset-backed securities issued and not yet pledged	0	0
250	TOTAL ASSETS, COLLATERAL RECEIVED AND OWN DEBT SECURITIES ISSUED	4 636	0

Sources of encumbrance (the Group and the Bank), thous. EUR

	Sources of encumbrance	Matching liabilities, contingent liabilities or securities lent	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered
		010	030
010	Carrying amount of selected financial liabilities	90	0
011	of which: Over-The-Counter	90	0

Capital Adequacy

Capital adequacy reflects the Bank's capital resources necessary to secure itself against risks related to assets and off-balance sheet items.

The Bank has the Capital Adequacy Assessment Process Policy, the aim of which is to ensure that the amount, elements and proportion of the Bank's equity capital are adequate to cover the substantial risks inherent to the Bank's current and planned operation.

For Pillar I risks, the capital requirement is calculated using the following approaches or methods:

- the credit risk requirement is calculated in accordance with a standardized approach;
- for the credit risk mitigation, simple method is used for financial collateral;
- capital requirements to cover a CVA risk in accordance with a standardized approach;

- the foreign currency risk capital requirements, debt securities' and capital securities' position risk, the payment/settlement risk capital requirements are calculated by using the standardized approach;
- debt securities' systematic risk capital requirement is determined by using the term method;
- the operational risk minimum capital requirement is calculated in accordance with the basic indicator approach.

For the calculation of the minimum capital requirements for the purpose of determining the transaction risk degree, the Bank applies the FCMC's recognized ECRA (rating agency) evaluations/ratings. ECRA are nominated for each risk transaction category, into which the Bank's risk transactions are divided into. If the Bank has no transactions, which can be included into any of the risk transaction categories, then, for this category, ECRA is nominated, when the actual risk transaction/-s of this category appears.

The following ECRA are nominated for the risk transaction categories:

Risk transaction category	Nominated ECRA
Claims against the central governments and central banks (CG and CB)	FitchRatings; Standard & Poor's Ratings Services; Moody's Investors Service.
Claims against the institutions with the exception of such institutions, for which the short-term rating is available	FitchRatings; Standard & Poor's Ratings Services; Moody's Investors Service.
Claims against the commercial companies with the exception of such institutions, for which the short-term rating is available	FitchRatings; Standard & Poor's Ratings Services; Moody's Investors Service.
The overdue risk transactions	FitchRatings; Standard & Poor's Ratings Services; Moody's Investors Service.
Claims against the institutions and commercial companies with the short-term ratings	FitchRatings; Standard & Poor's Ratings Services; Moody's Investors Service.
Other claims	FitchRatings; Standard & Poor's Ratings Services; Moody's Investors Service.

The Bank examines whether the fulfillment of the minimum capital requirements ensures that the Bank's capital is adequate to cover all potential losses related with the risks mentioned above.

In order to calculate the capital requirements to cover Pillar II risks the bank assesses its likely losses that may arise as a result of bank-specific risks, including the assessment of likely losses resulting from risks for which there is no generally accepted unified quantitative risk measuring approach. For this purpose the bank conducts a business-specific evaluation of at least:

- a non-trading portfolio's interest rate risk;
- concentration risk;
- anti-money laundering and counterterrorism financing risk;
- liquidity risk;
- other substantial bank-specific risks, including reputation risk, business model risk and others.

In order to assess the bank's capital adequacy to cover Pillar II risks the bank follows a simplified approach outlined in the FCMC Regulations on the Internal Capital and Liquidity Adequacy Assessment Processes as well as conducts the assessment of their applicability to the bank's activities.

In order to calculate the capital requirements to cover additional risks the bank sets a recommended capital reserve to ensure that the bank's capital is adequate to cover losses in the event of likely adverse scenarios as well as to ensure that the size of the bank's existing capital is sufficient over the entire length of a business cycle. This implies that throughout periods of economic expansion the bank accumulates a capital reserve to cover losses that may arise during economic slowdowns.

In its calculations of the capital reserve amount the bank evaluates, assesses and documents its likely development scenarios over the next three years subject to various macroeconomic development scenarios, events or changes in market conditions as well as assesses the impact of these scenarios, events and changes in market conditions on the bank's overall financial situation, viability and sustainability of its business model, the size of the bank's existing own capital, capital requirements and capital adequacy by taking into account the interaction of bank-specific risks, particularly, credit risk, market risk and liquidity risk.

The recommended size of the capital reserve is calculated by incorporating the results of an annual stress test scenario with the severest adverse impact on the bank's activities given, following the results of that year's stress test scenario, there is a need for an additional capital to cover likely bank-specific risks above the size of the required capital to cover Pillar I and Pillar II risks and in compliance with the aggregate amount of the total capital reserve requirements stipulated in Paragraph IV of the Credit Institution Law.

Methods to ensure total size of the required capital are as follows:

- meeting the capital adequacy requirements;
- reviewing the compliance with the capital adequacy requirements;
- maintaining the capital adequacy target ratio;
- complying with the individual capital ratio within the time frame agreed upon with FCMC;
- calculating and planning the size of the required total capital to cover substantial existing and potential bank-specific risks;
- assessing and evaluating all substantial risks;
- developing stress test scenarios, conducting stress tests and reviewing obtained results;
- developing the capital adequacy maintenance plan.

On 31 December 2017, the Bank's calculated capital adequacy ratio was 30.12% (on 31 December 2016, it was 30.51%) which exceeds the minimum and the sum of capital conservation buffer minimum (10.5%) laid down in the European Parliament and Council Regulation (EU) No 575/2013 that own funds ratio against the risk weighted assets and off-balance sheet items must be at least 8% and the capital conservation buffer must be at least 2.5%. In the end of 2017, the Financial and Capital Market Commission recalculated the Bank's individual capital adequacy ratio and set it at 15.7%. The Bank observes and meets this individual capital adequacy requirement.

Capital adequacy evaluation results as of 31.12.2018

The capital required to cover risks of the Group, thous. EUR

	Minimum regulatory capital requirements	Bank's assessment of the requiredcapital
Credit Risk	12 304	12 304
Market Risks	333	333
Currency Risk	103	103
Tradable Debt Instruments, securities	230	230
Operational Risk	2 289	2 289
Other significant risks for which the minimum regulatory capital requirements have not been defined		9 705
Capital Reserve		4 664
Total	14 926	29 295

*Taking into account the FCMC's individual capital requirements, Pillar II requirements and capital preservation requirements set at 2.5%.

The Group's Existing capital, thous. EUR

Own Capital	Calculation of the Bank's capital
50 293	50 293
Capital deficit/surplus in accordance with the Bank's assessment	20 998

Own Capital	50 293
Tier 1 Capital including:	***37 640***
Common equity Tier 1 Capital including:	*37 640*
Paid up capital instruments	32 835
Previous years retained earnings	-303
Profit or loss attributable to owners of the parent	6 134
Part of interim or year-end profit not eligible	-6 134
Goodwill accounted for as intangible asset	-503
Other reserves	95
Value adjustments due to requirements for prudent valuation	-26
IFRS9 transitional arrangements	5 541
Tier 2 Capital	***12 654***

In the following table, the Group's risk transaction category values before and after the credit risk mitigation are presented, as well as the total amount of the risk transactions, which have been concluded with the adequate collateral (thous. EUR):

Credit risk: the risk transaction categories	The risk transactions before the credit risk mitigations	Collateral (simple method)	The risk transactions after the credit risk mitigations*	The risk weighted assets of the risk transactions
Claims against the central governments or central banks	94 173	0	94 173	0
0% risk degree	94 173	0	94 173	0
Claims against the institutions	22 230	0	22 230	4 446
20% risk degree	22 230	0	22 230	4 446
Claims against the commercial societies	118 936	0	95 953	103 338
100% risk degree	97 419	0	81 182	81 182
150% risk degree	21 517	0	14 771	22 156
High risk transactions	3 232	0	3 232	4 848
150% risk degree	3 232	0	3 232	4 848
Overdue risk transactions	9 285	0	8 053	9 860
100% risk degree	4 440	0	4 440	4 440
150% risk degree	4 845	0	3 613	5 420
Other claims	52 607	13 645	46 802	31 032
0% risk degree	21 493	13 645	15 688	0
20% risk degree	103	0	103	21
100% risk degree	31 011	0	31 011	31 011
Capital securities	284	0	284	284
100% risk degree	284	0	284	284
Total	300 747	13 645	270 727	153 808

Note: *taking into the account conversion factor.

The average net amount of the risk transactions of the Group within the reporting period, broken down into different risk transaction categories after the credit risk mitigation application (thous. EUR):

Credit risk: the risk transaction categories	The risk weighted assets of the risk transactions in 2018	Average risk weighted assets of the risk transactions in 2018	The risk weighted assets of the risk transactions in 2017	Average risk weighted assets of the risk transactions in 2017
Claims on central governments and central banks	0	0	0	0
A 0% risk weight	0	0	0	0
Claims on financial institutions	**4 446**	**5 813**	**11 943**	**11 184**

A 20% risk weight	4 446	5 641	11 537	9 074
A 50% risk weight	0	172	406	2 110
A 100% risk weight	0	0	0	0
Claims on companies	**103 338**	**99 700**	**104 017**	**108 069**
A 0% risk weight	0	0	0	0
A 20% risk weight	0	0	0	0
A 100% risk weight	81 182	77 499	80 991	81 561
A 150% risk weight	22 156	22 201	23 026	26 508
Speculative risk transactions	**4 848**	**3 945**	**1 789**	**8 222**
A 0% risk weight	0	0	0	0
A 150% risk weight	4 848	3 945	1 789	8 222
Overdue risk transactions	**9 860**	**10 033**	**9 416**	**9 944**
A 100% risk weight	4 440	5 200	6 330	8 419
A 150% risk weight	5 420	4 833	3 086	1 525
Equity securities	**284**	**247**	**235**	**106**
A 100% risk weight	284	247	235	106
Other claims	**31 032**	**31 391**	**18 706**	**23 657**
A 0% risk weight	0	0	0	0
A 20% risk weight	21	25	202	66
A 100% risk weight	31 011	31 366	18 504	23 591
Total	**153 808**	**141 096**	**152 703**	**161 182**

The geographical composition of the Bank's credit risk exposure for transactions that are significant in the calculation of the Group's countercyclical capital buffers (EUR, thousand):

Country	Initial pre-adjustment risk exposure value	Specific credit-risk exposure adjustments (for provisioning purposes)	Risk exposure value	Risk exposure risk-weighted value
United Arab Emirates	2 349	9	1 749	140
Austria	10 326	8	10 318	825
Bangladesh	58	0	0	0
Belgium	13	0	13	1
Bulgaria	4 788	0	4 630	370
Belorussia	414	0	414	50
Kazakhstan	8	0	8	1
Switzerland	17	0	10	1
China	525	0	525	10
Czech Republic	0	0	0	0
Germany	13 967	585	9 382	741
Estonia	11 614	9	11 600	928
Great Britain	630	66	565	22
Israel	8	0	4	0
Luxembourg	0	0	0	0
Latvia	56 311	14 617	50 841	3 053
Monaco	5 497	97	5 385	431
Poland	0	0	0	0
Russia	23 764	47	23 143	1 855
Ukraine	47 964	1 511	32 043	3 167
USA	4 968	0	4 968	402
Other countries	0	0	0	0
Total	183 221	16 949	155 598	11 997

Leverage ratio

Leverage ratio calculation as on 31.12.2018:	EUR, thousand
Off-balance sheet items with a conversion factor of 10%	922

Off-balance sheet items with a conversion factor of 20%	124
Off-balance sheet items with a conversion factor of 50%	967
Off-balance sheet items with a conversion factor of 100%	6 727
Other assets	288 158
Tier 1 capital – fully phased-in definition	37 640
Tier 1 capital – transitional definition	37 640
Amount to be added according to second subparagraph of Article 429 (4) of the CRR	0
Amount to be added according to second subparagraph of Article 429 (4) of the CRR – transitional definition	0
Regulatory adjustments — Tier 1 capital — fully passed-in definition; of which	0
Regulatory adjustments regarding own credit risk	0
Regulatory adjustments — Tier 1 capital — transitional definition	-503*
Leverage ratio using the fully phased-in definition of Tier 1 capital, %	12.70%
Leverage ratio using the transitional definition of Tier 1 capital, %	12.70%

* non-material assets

In order to manage the leverage risk, the Bank has revised and supplemented the Capital Adequacy and Liquidity Assessment Process Policy, and the strategic planning process is being implemented taking into account the leverage ratio requirements.

As compared to 2017, in 2018, the Group's deposit portfolio has decreased by 26.5% and amounted to EUR 217,8 million at the end of the year, whereas the amount of assets decreased by 22.9% and amounted to EUR 283.1 million on 31 December 2018.

The Group's loan portfolio was 85.5 million EUR as on 31 December 2018, and decreased by 11.2% compared to the end of 2017. As compared to 2017, the amount of the bank's equity capital decreased to 50.3 million EUR at the end of 2018 (56.5 million EUR as of the end of 2017). The decrease in the group's equity capital was due to dividends division of 6.95 million EUR.

The ratios of the Bank's capital adequacy are not significantly different with the amount of the equity capital amounting to 50.0 million EUR, including 37,3 million EUR of Tier I capital. The capital adequacy ratio is 27,21%, the Tier I capital ratio is 20.32%, while the leverage ratio is 12.60%

During transitional period from January 1st, 2018 until December 31st, 2022 equity capital and equity capital ratios are calculated according to Regula (EC) 2017/2395, the purpose of which is for transitional period to mitigate the effect of the IFRS9 introduction on the equity capital, and also on limits set for large exposures. Transitional coefficients set in the article 473a paragraph 6 of the Regula are used for capital calculation.

Capital adequacy and leverage ratios as if IFRS 9 or analogous ECLs transitional arrangements had not been applied and had been applied (thous. EUR):

	Available capital (amounts)	31.12.2018 Bank	31.12.2018 Group
1	Common Equity Tier 1 (CET1) capital	37 309	37 640
2	Common Equity Tier 1 (CET1) capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	31 768	32 098
3	Tier 1 capital	37 309	37 640
4	Tier 1 capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	31 768	32 098
5	Total capital	49 962	50 293
6	Total capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	44 421	44 752
	Risk-weighted assets (amounts)		
7	Total risk-weighted assets	183 618	186 581

8	Total risk-weighted assets as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	177 997	180 961
	Capital ratios		
9	Common Equity Tier 1 (as a percentage of risk exposure amount)	20.32	20.17
10	Common Equity Tier 1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	17.85	17.74
11	Tier 1 (as a percentage of risk exposure amount)	20.32	20.17
12	Tier 1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	17.85	17.74
13	Total capital (as a percentage of risk exposure amount)	27.21	26.96
14	Total capital (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	24.96	24.73
	Leverage ratio		
15	Leverage ratio total exposure measure	296 053	296 394
16	Leverage ratio	12.60	12.70
17	Leverage ratio as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	10.93	11.03

Information on Management Arrangements

The bank's policy on the assessment of the suitability of members of the management body provides for the criteria used to assess the suitability of the bank's Council and Board members which should be complied with when assessing the suitability of nominated or elected Council and Board members as well as provides for actions to be taken when these persons are considered unsuitable for a respective position. With respect to Council and Board members one takes into account the fact that Council and Board members should devote a considerable amount of time and effort in performing their duties. Council and Board members, both individually and as a group, should possess a required specific knowledge, experience, competence, understanding (including understanding the business and related risks of the bank's subsidiaries) and personal characteristics (including professionalism and integrity) to allow the proper performance of the duties which in the case of Council members cover the supervision over the bank's or its subsidiary's Board activities, while in the case of Board members these cover the management of the bank's or subsidiary's activities. Council and Board members should possess a relevant information with respect to the bank's or subsidiary's activities not only at a level sufficient to perform his / her duties, but also should have an understanding of activities for which they do not bear the direct responsibility, while still bearing the overall responsibility.

The policy defines the evaluation process of the members of the Council and the Board and its regularity as well as standards defined for the position for a new member of the Council or the Board.

The bank shapes its internal organizational structure so that business units that ensure the performance of certain functions within the bank's activities report to a Board member who bears the respective responsibility for these functions and possesses the relevant competence.

Pursuant to the bank's Statutes:

- The Council is composed of five members. The Shareholders' Meeting elects the Council for a period not exceeding five years. Following the election of the Council the Shareholders' Meeting monitors the general competence of Council members to enable the Council to perform its duties in an efficient way. Council members elect a Council Chairman and at least one Deputy Chairman from their midst.
- The Board is composed of five members* A Board member is elected for a term not exceeding five years. Board members are elected by the Council. When electing Board members the Council monitors the general competence of Board members to enable the Board, as a whole, to perform its duties in an efficient way. The Council elects a Board Chairman from among the members of the Board.

*At this point the Board is composed of three members with two Board member positions being vacant.

Considering the amount, complexity and specifics of the Bank's operations as well as its organizational structure, there is no special risk committee at the Bank. The Council of the Bank is responsible for supervision of risk management of the Bank.

A remuneration policy and practice

The Bank has developed its remuneration policy, the aim of which is to define the key principles of remuneration of the Bank's employees pursuant to the Bank's strategy, business direction and risk profile to recruit and retain best employees. The remuneration policy is binding for all employees in the bank and its subsidiaries as well as for those employees in the bank's representative offices in Ukraine to the extent it is not in contradiction with this country's specific legal requirements.

The task of the Remuneration Policy is to determine such a remuneration system at the Bank, which would ensure conformity of remuneration to the employee's performance, coherence and fairness of remuneration at the Bank, conformity and competitiveness of remuneration in the labour market.

With regard to the positions that are affecting the Risk Profile of the Bank, the aim of the remuneration policy is to create a remuneration system which is:

- not promoting the undertaking of risks above the level set in the Bank's Risk Management Strategy and documents subordinate thereto, as well as in the respective policy for each crucial type of risk;
- not limiting the ability of the Bank to enhance its equity capital in line with the regulations on creating the fund of the variable part, developed by the Bank;
- conforming to the Bank's standards of ethics, long-term interests, goals of operations outlined in the development strategy, as well as complying with and promoting cautious risk management and prevention of conflicts of interests;
- not contradicting to the principles of protecting the interests of customers or investors.

The Council of the Bank is the main structural unit supervising remuneration. In 2018, the Council of the Bank conducted 30 meetings. The Council of the Bank determines and approves the fundamental principles of the Remuneration Policy; is responsible for introduction of the Policy and monitoring of its observance; determines remuneration for members of the Board of the Bank, Head of the Internal Audit Department, Head and employees of the Compliance Department, the Chief Risk Officer, heads of representative offices of the Bank and members of the board and of the council of subsidiary companies, as well as for employees whose remuneration is equal to or exceeds the lowest remuneration set for any of the members of the Bank's Board; approves the Internal Audit Action Plan on compliance of introduction and observance of the Remuneration Policy to the approved fundamental principles; lays down the procedures pursuant to which reports on performed inspections of internal control functions and their results are submitted to the Council of the Bank, as well as on the effects of the Remuneration Policy on the Bank's risk profile and the quality of risk management;

The Board of the Bank is responsible for observance of fundamental principles of remuneration; assesses the positions affecting the Bank's risk profile; determines remuneration for employees, determination of whose remuneration is not within the competence of the Bank's Council; is responsible for development of relevant internal regulatory documents, their approval and observance, taking into account that remuneration to employees holding positions that ensure internal control functions is determined regardless of the achieved performance results in the areas of activity controlled by internal control functions.

The structure of remuneration may consist of the following:

- The fixed part of remuneration, i.e., salary, which mainly reflects the employee's professional experience and level of responsibility set in the job description of the respective employee. The following is considered to be components of the fixed part of remuneration: salary; special payments to employees (child's birth benefit; health insurance; benefit due to the death of an employee's relative, etc.) and other monetary payments and benefits, which are constant and do not depend on the goals achieved by the employee;

- The variable part of remuneration reflects the employee's performance results, which exceed the requirements set in the employee's job description, their sustainability and the assessment of associated existing and potential risks.

Variable part of remuneration

Bonuses for achievement of qualitative and quantitative indicators and targets, individual bonus payments for special achievements are considered to be a variable part of remuneration. To assess employee's performance results, individual/structural unit's/Bank's Goal Maps can be developed, including therein quantitative (financial targets (for example, fulfilment of the budget, profit, liquidity, and other indicators), customer service targets (for example, internal/external customer satisfaction indicators, attraction of new customers, etc.), process goals (for example, indicators of observance of normative acts, i.e., indicators of observance of external/internal normative acts and limits, which can affect the Bank's risk profile and financial indicators respectively, etc.)) and qualitative goals (for example, professional improvement, project/field management to develop particular competence, the variability indicator of structural unit's employees, satisfaction of structural unit's employees with work, etc.).

If employee's actions or negligence has resulted in incidents posing a threat to the Bank's reputation, especially, if money laundering and terrorism financing prevention requirements are violated, the variable part of remuneration is not paid to the respective (involved) employees.

For employees holding positions that affect the risk profile, the variable part can be paid according to the fulfilment of indicators of the Goal Map once a year after the approval of the Bank's audited annual report at the shareholders' meeting of the Bank.

If the variable part of remuneration for employees holding positions that affect the risk profile is determined:

- in the amount of up to 35% of the fixed part of the respective employee's remuneration during the reporting year up to 40% of the variable part of remuneration is postponed for one year according to the amount of the deferred part set for the relevant risk profile position;

- in the amount of 35% (including) up to 100% (excluding) of the fixed part of the respective employee's remuneration during the reporting year, 40% of the variable part of remuneration is postponed for three years according to the amount of the deferred part set for the relevant risk profile position.

When calculating the variable part of remuneration for a position affecting the risk profile, the individual employee's performance results are taken into account in combination with the assessment of performance of a structural unit or area, for the operation of which the employee is responsible in accordance with the signed employment contract and job description, and in combination with general performance results at the level of the Bank, as well as assessments expressed by experts, for example, Bank's employees who control risks, on performance. Before the pay-out of the deferred variable part of remuneration to employees holding positions that affect the risk profile, the performance results used in determining the variable part of remuneration, their sustainability and associated risks are assessed, taking into account the fact that the use of tools and methods, which facilitate avoidance of observing requirements set forth in the Policy and other binding normative acts, is unacceptable.

Variable part of salary for positions that influence risk profile of the Bank for the year cannot exceed 100% of the fixed salary before taxes according to current legislation of Latvian Republic.

There were no significant changes in remuneration policy in 2018, except that the list of position categories whose professional activities can influence risk profile of the Bank was enlarged.

The tables specify the amounts of the gross remuneration paid by the Group (the Bank, the representative offices, affiliated company "Grunewald Residence" Ltd.), excluding the employer's obligatory state social security payments or other payments resulting from taxation system of other countries. In 2018, remuneration was not paid for launching employment relations.

Bonuses for particular achievements were paid to the bank's employees in 2018. Personal performance of the employees and departments were not taken into the account when setting the variable part of remuneration, and therefore there were no postponed parts of the variable remuneration for the employees who influence the risk profile of the Bank.

1. Table Information on employees' remuneration in 2018 (EUR)

	Council	Board	Investment services	Providing services to private persons or small and medium companies	Asset management	Corporate support function	Internal control function	Other types of activity
The number of employees at the end of the year	5	5	3	5	1	112	12	8
Total remuneration EUR	178 080	417 287	110 122	185 667	*	3 234 812	448 501	149 297
Including: variable part of remuneration			6 355	6 858	*	111 719	15 726	5 848

2. Table Information on employees influencing the Bank's risk profiles (EUR)

		Council	Board	Investment services	Providing services to private persons or small and medium companies	Asset management	Corporative support function	Internal control function	Other types of activity
	The number of employees influencing the institution's risk profile	5	5	1	2	*	10	3	
	Including the number of employees influencing the risk profile in the highest management positions			1	1		9	3	
Remuneration on invariable part	**Total invariable part**	178 080	417 287	*	88 964		566 934	129 031	
	Including money and other means of payment	178 080	417 287	*	88 964		566 934	129 031	
	Including shares and the related instruments								
	Including other instruments								

Remuneration variable part	**Total remuneration variable part**	*	5 160		24 297	7 274
	Including money and other means of payment	*	5 160		24 297	7 274
	Including shares and the related instruments					
	Including other instruments					
The related variable part of remuneration	**Total variable part of remuneration deferred at the end of the reporting year**					
	Including the deferred amount in the form of money and other means of payment					
	Including the deferred amount in the form of shares and related instruments					
	Including the deferred amount in the form of other instruments					
	Total unpaid part of the deferred remuneration allocated before the reporting year					
	Including the part, to which the irrevocable parts are obtained					
	Including the part, to which the irrevocable parts are not obtained					
	Total part of the deferred remuneration paid at the end of the reporting year					
Adjustment of variable part of remuneration	*Adjustment of the variable part of remuneration during the reporting year that concerns the variable part of*					

	remuneration allocated in the previous years	
Variable part of guaranteed remuneration	*Number of persons receiving the guaranteed variable part of remuneration (sign-on payments)*	
	The amount of the variable part of guaranteed remuneration (sign-on)	
Remuneration for termination of employment relations	*Number of employees that received a compensation for termination of legal employment relations*	
	Amount of compensation for termination of legal employment relations paid in the reporting year	1
	Amount of the largest compensation for a single person for termination of legal employment relations	*
Benefits related to retirement	*Number of employees that receive benefits related to retirement*	
	Amount of benefits related to retirement	

*) taking into the consideration data protection principals for private persons (data would be provided for 1 specified person), the information on remuneration for these employees cannot be disclosed.