

Nova Ljubljanska banka d.d., Ljubljana

# **Pillar 3 Disclosures for NLB Group 2017**

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## Abbreviations

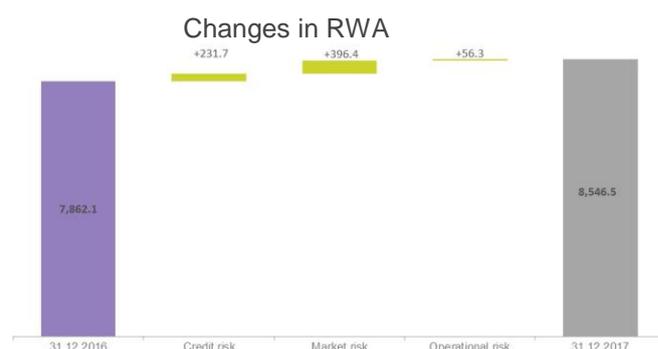
<b>ALCO</b>	Asset and Liability Committee	<b>IRB</b>	Internal ratings-based approach
<b>ALM</b>	Asset and Liability Management	<b>IRRBB</b>	Interest rate risk in the banking book
<b>AE</b>	Asset Encumbrance	<b>ISDA</b>	International Swaps and Derivatives Association
<b>AT1</b>	Additional Tier 1 capital	<b>IT</b>	Information Technology
<b>AVA</b>	Additional Valuation Adjustments	<b>IVS</b>	International Valuation Standards
<b>BCBS</b>	Basel Committee on Banking Supervision	<b>LCR</b>	Liquidity coverage ratio
<b>BPV</b>	Basis point value	<b>LGD</b>	Loss given default
<b>CBR</b>	Combined buffer requirement	<b>LTD</b>	Loan-to-deposit
<b>CCB</b>	Capital Conservation Buffer	<b>LTI</b>	Loan-to-income
<b>CCF</b>	Credit conversion factor	<b>LTV</b>	Loan-to-value
<b>CCR</b>	Counterparty credit risk	<b>MRSA</b>	Market Risk Standardized Approach
<b>CET 1</b>	Common equity tier 1 capital	<b>NPE</b>	Non Performing Exposures
<b>COSO</b>	Committee of Sponsoring Organisations of the Treadway Commission	<b>NPL</b>	Non Performing Loans
<b>CRD</b>	Capital Requirements Directive	<b>NPV</b>	Net Present Value
<b>CRD IV</b>	Capital Requirements Directive & Regulation	<b>NSFR</b>	Net Stable Funding Ratio
<b>CRM</b>	Credit Risk Mitigation	<b>OCR</b>	Overall capital requirement
<b>CRR</b>	Capital Requirements Regulation	<b>OpRC</b>	Operational Risk Committee
<b>CSA</b>	Credit Support Annex	<b>O-SII</b>	Other systemically important institutions
<b>CVA</b>	Credit valuation adjustment	<b>OTC</b>	Over-the-counter
<b>CVaR</b>	Conditional Value at Risk	<b>OU</b>	Organisational unit
<b>D-SIB</b>	Domestic systemically important banks	<b>PD</b>	Probability of default
<b>DVA</b>	Debit Valuation Adjustments	<b>P2R</b>	Pillar 2 Requirement
<b>EAD</b>	Exposure at default	<b>QCCP</b>	Qualifying Central Counterparty
<b>EBA</b>	European Banking Authority	<b>RAF</b>	Risk Appetite Framework
<b>ECAI</b>	External Credit Assessment Institutions	<b>RICS</b>	Royal Institution of Chartered Surveyors
<b>ECB</b>	European Central Bank	<b>RP</b>	Recovery plan
<b>EEPE</b>	Effective Expected Positive Exposure	<b>RWA</b>	Risk-weighted assets
<b>EHQLA</b>	Extremely High-quality Liquid Assets	<b>SA</b>	Standardized Approach
<b>EMIR</b>	European Market Infrastructure Regulation	<b>SEE</b>	Southeast Europe
<b>ESRB</b>	European Systemic Risk Board	<b>SFT</b>	Securities Financing Transactions
<b>EU</b>	European Union	<b>SME</b>	Small Medium Enterprise
<b>EVE</b>	Economic Value of Equity	<b>SREP</b>	Supervisory Review and Evaluation Process
<b>EVS</b>	European Valuation Standards	<b>SSM</b>	Single Supervisory Mechanism
<b>EWS</b>	Early Warning System	<b>ST</b>	Stress test
<b>FX</b>	Foreign Exchange	<b>T2</b>	Tier 2 capital
<b>GLTDF</b>	Gross Loans to Deposit Flows ratio	<b>TSCR</b>	Total SREP capital requirement
<b>G-SIB</b>	Global systemically important banks	<b>UMAR</b>	Institute of Macroeconomic Analysis and Development
<b>HQLA</b>	High-quality liquid assets	<b>VaR</b>	Value at risk
<b>ICAAP</b>	Internal Capital Adequacy Assessment Process	<b>ZBan-2</b>	Banking Act
<b>IFRS</b>	International Financial Reporting Standards	<b>ZGD</b>	Companies Act
<b>ILAAP</b>	Internal Liquidity Adequacy Assessment Process	<b>ZPPOGD</b>	Act Governing the Remuneration of Managers of Companies with Majority Ownership Held by the Republic of Slovenia or Self-Governing Local Communities

## Key highlights

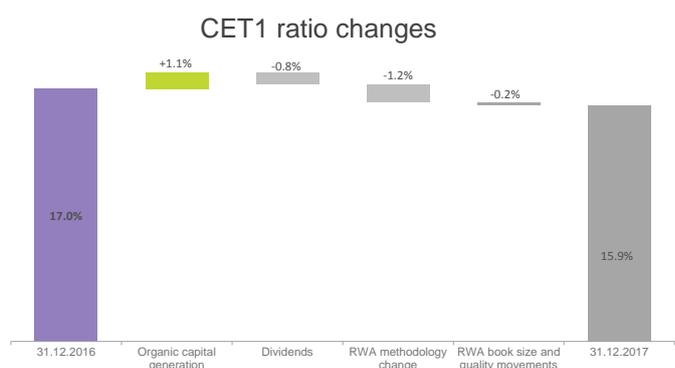
Table 1 – Key metrics

NLB Group	31.12.2017	31.12.2016
<b>Available capital</b>		
Common equity tier 1 (CET 1)	1,362,140	1,336,241
Tier 1	1,362,140	1,336,241
Total capital	1,362,140	1,336,241
<b>Risk weighted assets</b>		
Total RWA	8,546,482	7,862,128
<b>Capital ratios</b>		
Common equity tier 1 ratio (%)	15.9%	17.0%
Tier 1 ratio (%)	15.9%	17.0%
Total capital ratio (%)	15.9%	17.0%
<b>Additional CET1 buffer requirements as a % of RWA</b>		
Capital conservation buffer requirement	1.25%	0.675%
Countercyclical buffer requirement	0.0%	0.0%
Bank G-SIB and /or D-SIB additional requirements	0.0%	0.0%
Total of bank CET1 specific buffer requirements	1.25%	0.675%
CET1 available after meeting the bank's minimum Pillar 1 capital requirements	11.4%	12.5%
<b>Leverage ratio</b>		
Total leverage ratio exposure measure	14,044,985	13,804,603
Leverage ratio (%)	9.70%	9.68%
<b>Liquidity Coverage Ratio</b>		
Total HQLA	2,466,737	2,199,969
Total net cash outflow	893,680	663,215
LCR ratio	276%	332%

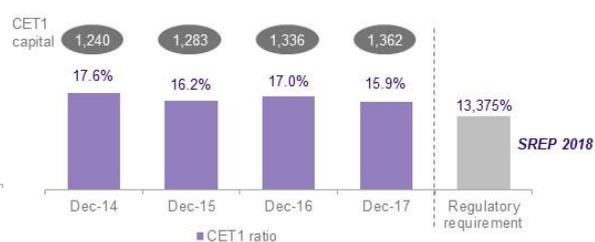
Key ratios and figures are reflected throughout the Pillar 3 disclosures for 2017 and a summary is presented in Table 1.



RWA analysis



CET 1 capital movement



## Statement of Management of Risk

(Articles 435 f of CRR)

NLB's Management Board and Supervisory Board provide herewith a concise statement of the risk management according to Article 17 of the Regulation on Internal Governance Arrangements, the Management body and the Internal Capital Adequacy Assessment Process for Banks and Savings Banks (*Official Gazette of the RS*, no. 73/2015, 49/2016 and 68/2017), and Regulation (EU) 575/2013 (date of publication 27 July 2013), article 435 (Risk management objectives and policies), point (e) and (f), as well as EBA Guidelines on Disclosure requirements (EBA GL/2016/11).

Risk management at NLB and in the Group is implemented in accordance with the established internal policies and procedures which take into account European banking regulations, the regulations adopted by the BoS, the current EBA guidelines, and relevant good banking practices. The Group pays great attention and importance to the risk culture and awareness of all relevant risks within the entire Group.

The risk management function represents an important part of the overall management and governance system in the Group. The Group's risk management framework is defined and organised with regard to the Group's business and risk profile, based on forward looking perspective to meet internal objectives and all external requirements. The proactive risk management and control system is based on risk strategy, which is consistent with the Group's risk appetite and business strategy, and is focused on early identification and efficient risk management. Set governance and different risk management tools enable adequate oversight of the Group's risk profile, and proactively support its business operations and its management by incorporating escalation procedures and using different mitigation measures when necessary. Nevertheless, the Group is constantly enhancing and complementing the existing methods and processes in all risk management segments.

The Group plans a prudent risk profile, optimal capital usage, and profitable operations in the long run, considering the risks assumed. The business strategy, the risk appetite, the risk strategy, and the key internal risk policies of the Group, approved by the Management Board and the Supervisory Board of NLB, specify the strategic objectives and guidelines concerning risk assumption, the approaches and methodologies of monitoring, measuring, mitigating, and managing all types of risk. Moreover, main strategic risk guidelines are integrated into the annual business plan review and budgeting process. The Group regularly monitors its target risk appetite profile, representing the key component of risk mitigation process. The risk profile enables detailed monitoring and proactive management. The usage of risk profile limits and potential deviations from limits and target values are reported regularly to the respective committees and/or the Management Board of the Bank, the Risk Committee of the Supervisory Board, and the Supervisory Board of the Bank.

Additionally, the Group established a comprehensive stress testing framework and other early warning systems in different risk areas with the intention of strengthening the existing internal controls and timely responding when necessary. The robust and uniform stress testing framework includes all material types of risk and several relevant stress scenarios, according to the vulnerability of the Group's business model. It is integrated into Risk appetite, ICAAP, ILAAP, and Recovery plan to support proactive management of the Group's overall risk profile, namely the capital and liquidity position on a forward looking perspective. Additionally, other partial risk assessments are covered by sensitivity analysis based on relevant stressed risk parameters.

In accordance with the Risk Appetite Statement, the Group, as the largest Slovenian banking and financial group, intends to be a sustainably profitable banking group, predominantly working with clients in those core markets. The Group's Risk Appetite Statement is further deployed to the core subsidiaries within the Group under consideration of the approved proportionality orientations. Based on the Group's business strategy the key risks are credit risk, interest rate risk in the banking book, liquidity risk, operational risk, market risk, and other non-financial risks. Regular risk identification and their assessment is performed within ICAAP with the aim of assuring their overall control and proactive risk management.

Management of credit risk, which is the most important risk in the Group, focuses on the taking of moderate risks – diversified credit portfolio, adequate credit portfolio quality, sustainable cost of risk, and ensuring an optimal return considering the risks assumed. The liquidity risk tolerance is low. The Group must maintain an appropriate level of liquidity at all times to meet its short-term liabilities, even if a specific stress scenario is realised. Further, with the aim of minimising this risk, the Group pursues an appropriate structure of

sources of financing. In the area of currency risk, the Group thus pursues the goals of low-to-moderate exposure. The Group's basic orientation in the management of interest rate risk is to prevent negative effects on revenues that would arise from changed market interest rates and, therefore, a low tolerance for this risk is stated. The conclusion of transactions in derivative financial instruments at NLB is primarily limited to servicing customers and hedging NLB's own positions. When assuming operational risks, the Group pursues the orientation that such risk must not significantly impact its operations and, therefore, the risk appetite for operational risks is low-to-moderate. The tolerance for all other risk types (for example, reputation risk, profitability risk, and others) is low with a focus on minimising their possible impacts on the Group's operations. These also include non-financial risks.

The main risk appetite objectives of the Group are following:

- Preservation of a prudent level of capital adequacy including regulatory requirements and capital buffers.
- Maintenance of a solid level and structure of liquidity minimising potential shortfalls.
- Customers' deposits as the main funding base.
- Adequate quality of the credit portfolio, sustainable cost of risk, ensuring sustainable, limited credit risk volatility, and limited exposure to project financing.
- Diversification of risk in exposures to banks and sovereigns.
- Limited exposure to interest rate risk in the banking book and to consolidated FX risk (from transactional risk).
- Ensuring sustainable profitability in terms of risk-return.
- Ensuring the sustainable and limited size of subsidiary banks.

The values of the most important risk appetite indicators of the Group as at the end of 2017, reflecting interconnection between strategic business goals, risk strategy, and targeted risk appetite profile, were as follows:

- CET1 15.9%,
- cost of risk – 62 bps,
- the share of NPE by EBA 6.7%,
- LTD 70.8%,
- LCR 276%,
- NSFR 149%,
- BPV sensitivity (of 200 bps) 5.7% of capital.

Consequently, the Group concluded the year 2017 within its target risk appetite, with a strong capital and liquidity position.

The Condensed Statement of the management of risk is also published on the NLB intranet, to foster strict adherence of the Banks' employees in daily operations of the Bank, concerning the definition and importance of a consistent tendency of the adopted risks, and ways to take into account when adopting its daily business decisions.

Ljubljana, 13 April 2018

**The Supervisory Board**



**Primož Karpe**  
Chairman of the  
Supervisory Board

**The Management Board**



**László Pelle**  
Member of the  
Management Board



**Archibald Kremser**  
Member of the  
Management Board



**Andreas Burkhardt**  
Member of the  
Management Board



**Blaž Brodnjak**  
President & CEO

## 1. Introduction

The purpose of this Report is to provide disclosures as required by the global regulatory framework for capital and liquidity, established by the Basel Committee on Banking Supervision. On the European level these are implemented in the disclosure requirements as laid down in Part Eight of the 'Regulation (EU) No. 575/2013 on prudential requirements for credit institutions and investment firms' (Capital Requirements Regulation, or 'CRR') and the 'Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms' (Capital Requirements Directive IV, or 'CRD'). The CRD IV commonly refers to both CRR and CRD, which were published in the Official Journal of the EU on 27 June 2013. The CRR had a direct effect in EU member states while the CRD was required to be implemented through national legislation in EU member states by 31 December 2013. Slovenia implemented these CRD requirements into national law with the Slovene Banking Act (Zakon o bančništvu – ZBan-2).

In the context of this document, the CRD IV describes the package of CRR, CRD and regulatory and technical standards. CRD IV is commonly referred to as containing the following three Pillars:

- Pillar 1 contains mechanisms and requirements for the calculation by financial institutions of their minimum capital requirements for credit risk, market risk and operational risk
- Pillar 2 is intended to ensure that each financial institution has sound internal processes in place to assess the adequacy of its capital, based on a thorough evaluation of its risks. Supervisors are tasked with valuating how well financial institutions are assessing their capital adequacy needs relative to their risks. Risks not considered under Pillar 1 are considered under this Pillar.
- Pillar 3 is intended to complement Pillar 1 and Pillar 2. It requires that financial institutions disclose information on the scope of application of CRD IV requirements, particularly covering capital requirements / risk-weighted assets (RWA) and resources, risk exposures and risk assessment processes.

The Group is required to comply with the CRD IV disclosure requirements at 31 December 2017. For ease of reference, the requirements are referred to as 'Pillar 3' in this Report. Pillar 3 contains both qualitative and quantitative disclosure requirements. In December 2016, the European Banking Authority (EBA) published final guidelines on the Pillar 3 disclosure requirements aimed at improving and enhancing the consistency and comparability of institutions' disclosures. These guidelines apply from 31 December 2017 and the Group's disclosures have been prepared in accordance with these guidelines.

All disclosures are prepared on a consolidated basis and in EUR thousand, unless otherwise stated.

### *Areas covered*

In accordance with Pillar 3 requirements, the areas covered by the Group's Pillar 3 disclosures include the Group's CRD IV capital requirements and resources, credit risk, counterparty credit risk, market risk, operational risk, liquidity risk, encumbered and unencumbered assets, leverage ratio and the Group's remuneration disclosures.

NLB Group uses the following approaches for the calculation of capital requirements:

- credit risk – standardised approach,
- market risk – standardised approach, and
- operational risk – basic indicator approach.

Thus, the disclosures relating to other approaches, such as IRB approach, securitisation, advanced measurement approach for operational risk and disclosures related to internal models for the calculation of market risk capital requirements not used by NLB Group are not applicable. In addition, disclosures that relate to types of transactions that NLB Group is currently not involved in are also not applicable and therefore not disclosed in this report. Rows and columns in prescribed templates, related to transactions, not applicable to NLB Group are, in accordance with the EBA guidance, deleted.

### Frequency of disclosures and media

CRD IV and EBA guidelines require the Group to disclose information at a minimum on an annual basis. To ensure the effective communication of the Group's business and risk profile, the Group also pays particular attention to the possible need to provide information more frequently than annually. We publish Pillar 3 disclosures annually on the NLB's website [www.nlb.si](http://www.nlb.si), following the release of annual report for NLB Group. A separate Pillar 3 document will also be published quarterly following our Interim Report disclosure in 2018.

### Verifications and source of information

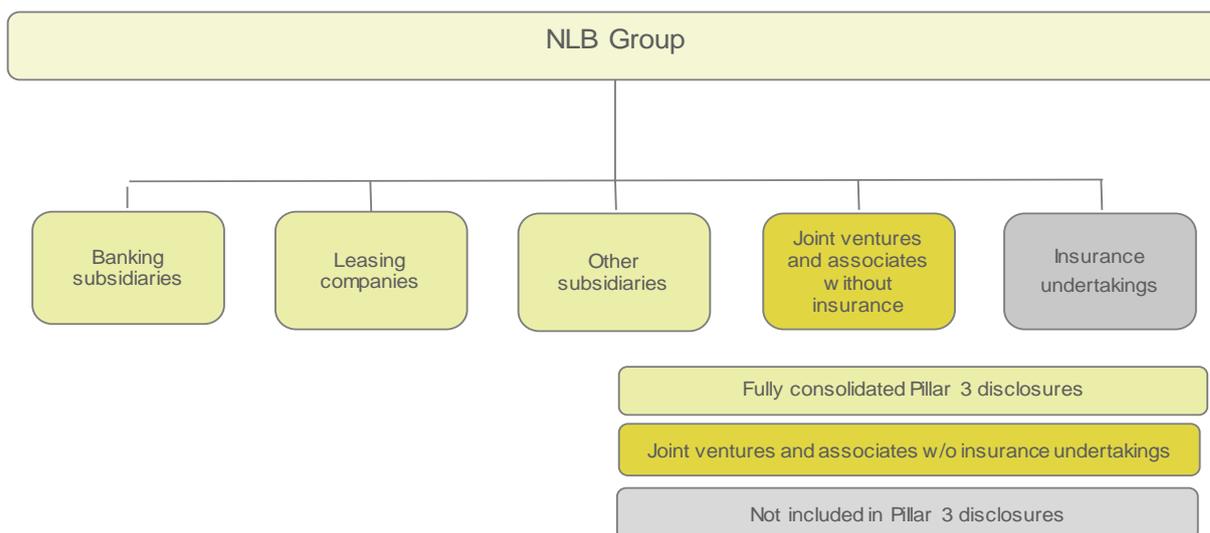
The Pillar 3 report is subject to a robust internal control and governance process. It was adopted by the Management Board of NLB d.d. (here after 'NLB') and acknowledged by the Audit Committee. An external auditor reviewed the compliance of the disclosures with the underlying legislation, including EBA guidance. Nevertheless, the report is unaudited.

It should be noted that while some quantitative information in this document is based on financial data contained in the Annual Report for NLB Group 2017, other quantitative data is sourced from the regulatory reporting (Finrep and Corep) and is calculated according to regulatory requirements. Pillar 3 quantitative data is thus not always directly comparable with the quantitative data contained in the Annual Report for NLB Group 2017. Some details of the key differences between the Group's accounting and regulatory exposures are set out in table 2 - EU LI1.

## 2. Scope of application

(Articles 436 b, c and d of CRR)

In accordance with the capital legislation, NLB has the position of an "EU parent bank" and is therefore obliged to disclose information on a consolidated basis. Consolidated financial statements for the purpose of Pillar 3 disclosures are based on CRR requirements (regulatory scopes of consolidation). A summarised representation of the regulatory consolidation group is presented below.



Significant subsidiary of NLB Group that exceeds 10% Group's RWA is NLB Banka a.d., Skopje. Detailed information are disclosed in annual report published on website <http://www.nlb.mk>.

Table EU LI1 represents the main differences between the basis of consolidation and carrying values as reported in published financial statements in the Annual Report for NLB Group 2017 and under the scope of regulatory consolidation.

The differences between the scope of consolidation for regulatory purposes and accounting purposes (pursuant to the IFRS) of NLB Group (entity by entity) as at 31 December 2017 are seen from table EU LI3 (disclosed in Appendix 5). The consolidation for *accounting purposes* comprise all:

- subsidiaries (banking, leasing and other subsidiaries) controlled by the Bank or the Group,

- associated companies in which NLB directly or indirectly holds between 20% and 50% of voting rights, has a material impact but does not control them and
- jointly controlled companies (i.e. jointly controlled by NLB Group based on a contractual agreement).

In contrast to accounting consolidation the *regulatory consolidation* only includes (in accordance with the definitions under Article 4 of CRR credit institutions, financial institutions, ancillary service undertakings and asset management companies. As regards NLB Group, this means that the regulatory consolidation does not include companies operating in the area of insurance.

Concerning consolidation method there are no differences between the accounting and regulatory consolidation as at 31 December 2017, as companies from the Prvi Faktor Group (see table EU LI3) are excluded from the regulatory consolidation (that would otherwise require the proportional consolidation method, in accordance with CRD IV) due to immateriality in accordance with CRR. In accounting consolidation, net assets of the Prvi Faktor Group using the equity method amounts to zero. More details are disclosed in the Annual Report for NLB Group 2017 - note 5.12 b (page 244).

Table 2 – EU LI1 – Differences between accounting and regulatory scopes of consolidation and the mapping of financial statement categories with regulatory risk categories of NLB Group

	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	Carrying values of items			Not subject to capital requirements or subject to deduction from capital
			Subject to the credit risk framework	Subject to the CCR framework	Subject to the market risk framework	
<b>31.12.2017</b>						
Cash, cash balances at central banks, and other demand deposits at banks	1,256,481	1,256,481	1,256,481	-	-	-
Trading assets	72,189	72,189	-	12,229	72,189	-
Financial assets designated at fair value through profit or loss	5,003	5,003	5,003	-	5,003	-
Available-for-sale financial assets	2,276,493	2,276,493	2,276,493	-	-	-
Derivatives - hedge accounting	1,188	1,188	-	1,188	-	-
Loans and advances						
- debt securities	82,133	82,133	67,090	-	-	15,043
- loans and advances to banks	510,107	510,107	510,107	-	-	-
- loans and advances to customers	6,912,333	6,912,333	6,911,717	-	-	616
- other financial assets	66,077	66,084	66,084	-	-	-
Held-to-maturity financial assets	609,712	609,712	609,712	-	-	-
Fair value changes of the hedged items in portfolio hedge of interest rate risk	719	719	-	-	-	719
Non-current assets and disposal group classified as held for sale	11,631	6,224	6,224	-	-	-
Property and equipment	188,355	188,355	188,355	-	-	-
Investment property	51,838	51,838	51,838	-	-	-
Intangible assets	34,974	34,974	-	-	-	34,974
Investments in associates and joint ventures	43,765	12,359	10,971	-	-	-
Current income tax assets	2,795	2,795	2,795	-	-	-
Deferred income tax assets	18,603	18,603	18,603	-	-	-
Other assets	93,349	93,349	93,349	-	-	-
<b>Total assets</b>	<b>12,237,745</b>	<b>12,200,939</b>	<b>12,074,822</b>	<b>13,417</b>	<b>77,192</b>	<b>51,352</b>
Trading liabilities	9,502	9,502	-	9,502	9,502	-
Financial liabilities designated at fair value through profit or loss	635	635	-	-	-	-
Derivatives - hedge accounting	25,529	25,529	-	25,529	-	-
Financial liabilities measured at amortised cost						
- deposits from banks and central banks	40,602	40,602	-	-	-	-
- borrowings from banks and central banks	279,616	279,616	-	-	-	-
- due to customers	9,878,378	9,878,809	-	-	-	-
- borrowings from other customers	74,286	74,286	-	-	-	-
- subordinated liabilities	27,350	27,350	-	-	-	-
- other financial liabilities	111,019	111,019	-	-	-	-
Liabilities of disposal group classified as held for sale	440	-	-	-	-	-
Provisions	88,639	88,639	-	-	-	-
Current income tax liabilities	2,894	2,894	-	-	-	-
Deferred income tax liabilities	1,096	1,096	-	-	-	-
Other liabilities	9,596	9,596	-	-	-	-
<b>Total liabilities</b>	<b>10,549,582</b>	<b>10,549,573</b>	<b>-</b>	<b>35,031</b>	<b>9,502</b>	<b>-</b>
<b>Equity and reserves attributable to owners of the parent</b>						
Share capital	200,000	200,000	-	-	-	-
Share premium	871,378	871,378	-	-	-	-
Accumulated other comprehensive income	26,752	16,989	-	-	-	-
Profit reserves	13,522	13,522	-	-	-	-
Retained earnings	541,901	515,147	-	-	-	-
Non-controlling interests	34,610	34,330	-	-	-	-
<b>Total equity</b>	<b>1,688,163</b>	<b>1,651,366</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total liabilities and equity</b>	<b>12,237,745</b>	<b>12,200,939</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	Carrying values of items			Not subject to capital requirements or subject to deduction from capital
			Subject to the credit risk framework	Subject to the CCR framework	Subject to the market risk framework	
<b>31.12.2016</b>						
Cash, cash balances at central banks, and other demand deposits at banks	1,299,014	1,299,313	1,299,313	-	-	-
Trading assets	87,699	87,699	-	19,077	87,699	-
Financial assets designated at fair value through profit or loss	6,694	6,694	6,694	-	6,694	-
Available-for-sale financial assets	2,072,153	2,068,470	2,068,470	-	-	-
Derivatives - hedge accounting	217	217	-	217	-	-
Loans and advances						
- debt securities	85,315	85,315	67,492	-	-	17,823
- loans and advances to banks	435,537	434,597	434,597	-	-	-
- loans and advances to customers	6,912,067	6,904,216	6,902,783	-	-	1,433
- other financial assets	61,014	65,656	65,656	-	-	-
Held-to-maturity financial assets	611,449	611,449	611,449	-	-	-
Fair value changes of the hedged items in portfolio hedge of interest rate risk	678	678	-	-	-	678
Non-current assets and disposal group classified as held for sale	4,263	4,263	4,263	-	-	-
Property and equipment	196,849	196,869	196,869	-	-	-
Investment property	83,663	84,206	84,206	-	-	-
Intangible assets	33,970	33,926	-	-	-	33,926
Investments in associates and joint ventures	43,248	16,024	14,540	-	-	-
Current income tax assets	2,888	3,942	3,942	-	-	-
Deferred income tax assets	7,735	7,740	2,719	-	-	5,021
Other assets	94,558	94,438	94,438	-	-	-
<b>Total assets</b>	<b>12,039,011</b>	<b>12,005,712</b>	<b>11,857,431</b>	<b>19,294</b>	<b>94,393</b>	<b>58,881</b>
Trading liabilities	18,791	18,791	-	18,791	18,791	-
Financial liabilities designated at fair value through profit or loss	2,011	2,011	-	-	-	-
Derivatives - hedge accounting	29,024	29,024	-	29,024	-	-
Financial liabilities measured at amortised cost						
- deposits from banks and central banks	42,334	42,334	-	-	-	-
- borrowings from banks and central banks	371,769	380,732	-	-	-	-
- due to customers	9,437,147	9,436,195	-	-	-	-
- borrowings from other customers	83,619	83,619	-	-	-	-
- debt securities in issue	277,726	277,726	-	-	-	-
- subordinated liabilities	27,145	27,145	-	-	-	-
- other financial liabilities	110,295	110,354	-	-	-	-
Provisions	100,914	89,716	-	-	-	-
Current income tax liabilities	3,146	3,117	-	-	-	-
Deferred income tax liabilities	727	711	-	-	-	-
Other liabilities	8,703	8,764	-	-	-	-
<b>Total liabilities</b>	<b>10,513,351</b>	<b>10,510,239</b>	<b>-</b>	<b>47,815</b>	<b>18,791</b>	<b>-</b>
<b>Equity and reserves attributable to owners of the parent</b>						
Share capital	200,000	200,000	-	-	-	-
Share premium	871,378	871,378	-	-	-	-
Accumulated other comprehensive income	29,969	20,102	-	-	-	-
Profit reserves	13,522	13,522	-	-	-	-
Retained earnings	380,444	360,329	-	-	-	-
Non-controlling interests	30,347	30,142	-	-	-	-
<b>Total equity</b>	<b>1,525,660</b>	<b>1,495,473</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Total liabilities and equity</b>	<b>12,039,011</b>	<b>12,005,712</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>

Table 2 (EU LI 1) provides the reconciliation of the accounting consolidated financial statements (as presented in the Annual Report for NLB Group 2017 (Audited Financial Statements of the NLB Group Pursuant to the International Financial Reporting Standards) to the regulatory consolidated financial statements. Certain assets can be subject to multiple RWA frameworks. Details of items not subject to capital requirement or subject from deduction from capital or explanation of differences with the comparative period is explained below;

- None of NLB Group's investments in subsidiaries, associated companies, and jointly controlled companies represents a deduction from capital. The total amount of investments that could become deductions from capital is relatively low and remains under the statutory thresholds.
- In accordance with CRR article 36 (b), intangible assets are a deduction item from capital.
- Positive amounts resulting from hedge accounting are excluded from positions, subject to credit risk;
- Compared to 2016, in 2017 NLB Group changed the approach for recognition of deferred tax assets namely, in previous periods, NLB Group presented deferred tax assets on all temporary differences and deducted them to the amount that, given future profit estimates, is expected to be reversed in the foreseeable future (i.e. within five years). For the purpose of regulatory capital, deductions from DTA were proportionally distributed to all deferred tax assets. In 2017, NLB Group recognised deferred tax assets on all temporary differences, except for impairments of non-strategic capital investments where deferred tax assets are recognised in the amount that, taking into account other recognised deferred tax

assets, reaches the total amount of deferred tax assets, for which a reversal is expected within five years. Deferred tax assets arising from tax losses are not recognised.

Any current or foreseen material practical or legal impediment to the prompt transfer of own funds or repayment of liabilities among the parent undertaking and its subsidiaries are disclosed in Appendix 6.

Table 3 – EU LI2 – Main sources of differences between regulatory exposure amounts and carrying values in financial statements of NLB Group

31.12.2017	Total	Items subject to		
		Credit risk framework	CCR framework	Market risk framework
<b>1 Assets carrying value amount under the scope of regulatory consolidation (as per template EU LI1)</b>	12,165,431	12,074,822	13,417	77,192
2 Liabilities carrying value amount under the regulatory scope of consolidation (as per template EU LI1)	(44,533)	-	(35,031)	(9,502)
3 Total net amount under the regulatory scope of consolidation	12,155,929	12,074,822	13,417	67,690
4 Off-balance-sheet amounts	1,890,531	1,890,531	-	-
5 <i>Differencies due to derivatives</i>	9,455	-	9,455	-
<b>6 Exposure amounts considered for regulatory purposes</b>	<b>14,055,915</b>	<b>13,965,353</b>	<b>22,872</b>	<b>67,690</b>

31.12.2016	Total	Items subject to		
		Credit risk framework	CCR framework	Market risk framework
<b>1 Assets carrying value amount under the scope of regulatory consolidation (as per template EU LI1)</b>	11,971,118	11,857,431	19,294	94,393
2 Liabilities carrying value amount under the regulatory scope of consolidation (as per template EU LI1)	(66,606)	-	(47,815)	(18,791)
3 Total net amount under the regulatory scope of consolidation	11,952,327	11,857,431	19,294	75,602
4 Off-balance-sheet amounts	1,839,771	1,839,771	-	-
5 <i>Differencies due to derivatives</i>	8,132	-	8,132	-
<b>6 Exposure amounts considered for regulatory purposes</b>	<b>13,800,230</b>	<b>13,697,202</b>	<b>27,426</b>	<b>75,602</b>

Table 3 – EU LI2 presents carrying values of items, subject to credit risk, CRR and market risk framework (see table 2 - EU LI1) and other items (potential liabilities from financial and non-financial guarantees, commitments to extent credit and credit replacement value for derivative financial instruments) and adjustment of derivative valuation, together presenting the total exposure considered for regulatory purposes.

### 3. Capital and capital requirements

#### 3.1. Capital adequacy

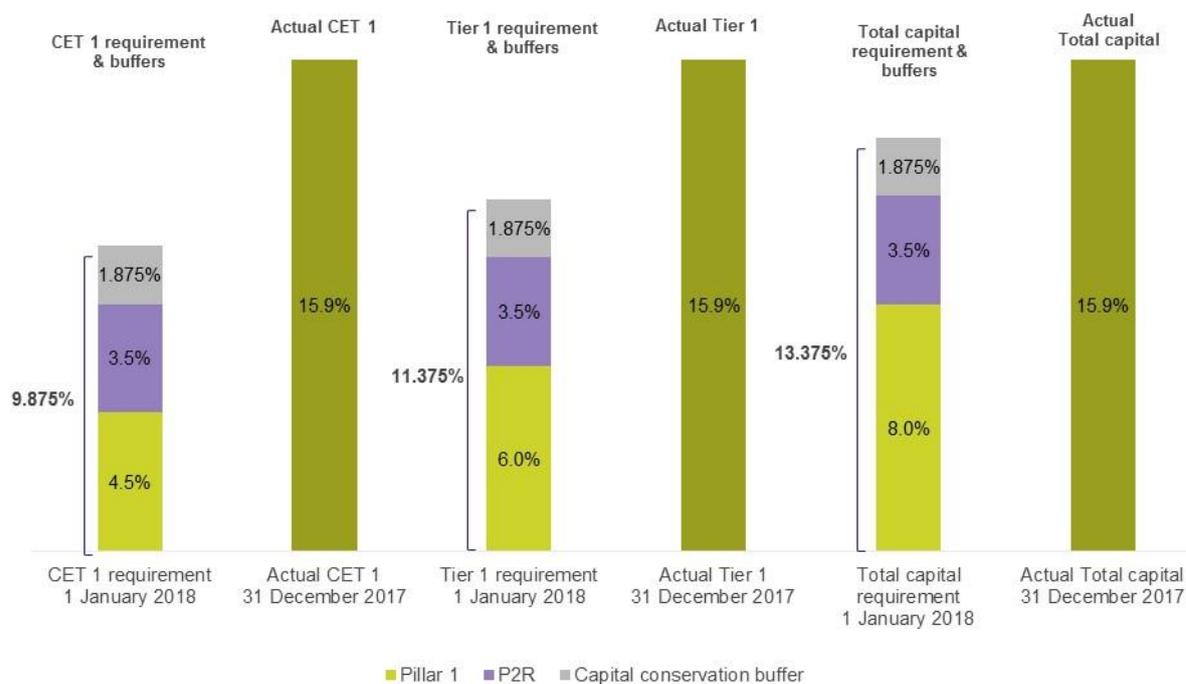
European bank capital legislation - CRD IV, is based on the Basel III guidelines. The legislation defines three capital ratios reflecting a different quality of capital:

- Common Equity Tier 1 ratio (ratio between common or CET1 capital and risk-weighted exposure amount or RWA), which must be at least 4.5%;
- Tier 1 capital ratio (Tier 1 capital to RWA), which must be at least 6%; and
- Total capital ratio (total capital to RWA), which must be at least 8%.

In addition to the aforementioned ratios, which form the Pillar 1 requirement, the Bank must meet other requirements and recommendations that are imposed by the supervisory institutions or by the legislation:

- Pillar 2 Requirement (SREP requirement): bank-specific, obligatory requirement set by the supervisory institution through the SREP process (together with the Pillar 1 requirement it represents the minimum total SREP capital requirement – TSCR);
- Applicable combined buffer requirement (CBR): system of capital buffers to be added on top of TSCR – breach of the CBR is not a breach of capital requirement but triggers limitations in payment of dividends and other distributions from capital. Some of the buffers are prescribed by law for all banks and some of them are bank specific, set by the supervisory institution (CBR and TSCR together form the overall capital requirement – OCR);
- Pillar 2 Guidance: capital recommendation over and above the OCR, set by the supervisory institution through the SREP process. It is bank specific and as a recommendation not obligatory. Any non-compliance does not affect dividends or other distributions from capital, however it might lead to intensified supervision and imposition of measures to re-establish a prudent level of capital.

Table 4 – Capital requirements and buffers



As of 1 January 2017, NLB was required to maintain the OCR at the level of 12.75% on a consolidated basis and meet the following capital requirements on a consolidated basis:

- 9.25% CET 1 ratio (transitional),
- 10.75% Tier 1 ratio (transitional),
- 12.75% Total Capital ratio (transitional).

All capital ratios are inclusive of 3.5% Pillar 2 Requirement (P2R) and 1.25% Capital Conservation Buffer (CCB). As prescribed by CRD IV and the ZBan-2, CCB is increasing linearly and will reach the fully loaded level of 2.5% in 2019, whereas the Bank of Slovenia requires NLB to apply the O-SII buffer at the rate of 1% on the consolidated level from 2019 on.

In 2018, NLB is required to maintain the OCR at the level of 13.375% on a consolidated basis. The increase of the requirement in comparison to the 2017 level is due to the phasing-in of the capital conservation buffer as prescribed by law.

Table 5 – Capital adequacy of NLB Group:

	31.12.2017	31.12.2016
Paid up capital instruments	200,000	200,000
Share premium	871,378	871,378
Retained earnings - from previous years	296,773	246,656
Current result	29,280	49,890
Accumulated other comprehensive income	(11,450)	(6,053)
Other reserves	13,522	13,522
Minority interest	-	-
Prudential filters: Additional Valuation Adjustments (AVA)	(2,389)	(2,213)
(-) Goodwill	(3,529)	(3,529)
(-) Other intangible assets	(31,445)	(30,397)
(-) Deferred tax assets that rely on future profitability and do not arise from temporary differences net of associated tax liabilities	-	(3,013)
<b>COMMON EQUITY TIER 1 CAPITAL (CET1)</b>	<b>1,362,140</b>	<b>1,336,241</b>
Additional Tier 1 capital	-	-
<b>TIER 1 CAPITAL</b>	<b>1,362,140</b>	<b>1,336,241</b>
Tier 2 capital	-	-
<b>TOTAL CAPITAL</b>	<b>1,362,140</b>	<b>1,336,241</b>
Risk exposure amount for credit risk	7,096,413	6,864,737
Risk exposure amount for market risks	499,726	104,175
Risk exposure amount for CVA	850	463
Risk exposure amount for operational risk	949,493	892,753
<b>TOTAL RISK EXPOSURE AMOUNT (RWA)</b>	<b>8,546,482</b>	<b>7,862,128</b>
Common Equity Tier 1 Ratio	15.9%	17.0%
Tier 1 Ratio	15.9%	17.0%
Total Capital Ratio	15.9%	17.0%

The capital adequacy of NLB Group at the end of year 2017 remains strong, at a level which covers all current and announced regulatory capital requirements, including capital buffers and other currently known requirements, and the Pillar 2 Guidance. Moreover, it is within the stated risk appetite limit and above the EU average as published by the EBA.

In 2017, the capital of the Group consists merely of the components of top quality CET1 capital (no subordinated instruments that would rank in lower capital categories) which is why all three capital ratios are the same.

At the end of December 2017, the capital ratios for NLB Group stood at 15.9% (or 1.1 p.p. lower than at the end of 2016). The Group's lower capital adequacy derives from higher risk-weighted assets (RWA). The drivers behind the differences between the RWAs as of 31 December 2017 and 2016 are explained in chapter 3.2 Capital requirements in the Table 6 – EU OV1 – Overview of RWAs.

In March 2018, NLB received a letter from the ECB on the ECB's intention to adopt the decision to restrict distributions by NLB to its shareholders and to require a Contingent Capital Plan. Details are disclosed in the Annual Report for NLB Group 2017, chapter 22 (page 177) and note 9 (page 342). On 5 April 2018, NLB received final ECB decision on this matter.

### 3.2. Capital requirements

(Article 438 c, e and f and 445 of CRR)

NLB Group uses the following approaches to calculate Pillar 1 capital requirements on a consolidated basis:

- credit risk – standardised approach,
- market risk – standardised approach, and
- operational risk – basis indicator approach.

In the calculation of capital ratios, risk is expressed as a risk exposure amount or a capital requirement. The capital requirement for an individual risk amounts to 8% of the total exposure to the individual risk.

The table below shows the detailed composition of the capital requirements of NLB Group at the end of 2017 and 2016.

Table 6 – EU OV1 – Overview of RWAs

	31.12.2017		31.12.2016	
	RWA	Minimum capital requirement - 8% of RWA	RWA	Minimum capital requirement - 8% of RWA
1 <b>Credit risk (excluding CCR)</b>	<b>6,993,567</b>	<b>559,485</b>	<b>6,794,482</b>	<b>543,559</b>
2 Of which the standardised approach	6,993,567	559,485	6,794,482	543,559
6 <b>CCR</b>	<b>20,983</b>	<b>1,679</b>	<b>23,233</b>	<b>1,859</b>
7 Of which mark to market	20,133	1,611	22,770	1,822
12 Of which CVA	850	68	463	37
13 <b>Settlement risk</b>	-	-	-	-
19 <b>Market risk</b>	<b>499,726</b>	<b>39,978</b>	<b>104,175</b>	<b>8,334</b>
20 Of which the standardised approach	499,726	39,978	104,175	8,334
22 <b>Large exposures</b>	-	-	-	-
23 <b>Operational risk</b>	<b>949,493</b>	<b>75,959</b>	<b>892,753</b>	<b>71,420</b>
24 Of which basic indicator approach	949,493	75,959	892,753	71,420
27 <b>Amounts below the thresholds for deduction (subject to 250% risk weight)</b>	<b>82,713</b>	<b>6,617</b>	<b>47,485</b>	<b>3,799</b>
<b>29 Total</b>	<b>8,546,482</b>	<b>683,719</b>	<b>7,862,128</b>	<b>628,970</b>

RWA for credit risk increased by EUR 231.7 million, mainly for retail exposure due to consumer and housing loans growth. RWA for market risks and CVA increased by EUR 395.9 million, particularly as a result of the requested correction of the treatment of the FX position on a consolidated level and treatment of equity investments in non-euro subsidiary banks. The correction requested by the regulator relates to structural positions arising from operations of NLB Group's non-euro subsidiary banks. These positions are long, non-trading and deliberately taken. On a consolidated level foreign exchange translation differences from these positions are recognised in the consolidated capital and do not have an impact on the Group's profit and loss. By keeping the structural position open NLB Group maintains capital ratio insensitive to foreign exchange movements. The Bank will try to partly or fully exclude this position from open FX position in the future (by getting the approval of the regulator) and partly mitigate this capital adequacy decrease on a consolidated and an individual level. The increase in the RWA for operating risks (EUR 56.7 million) arises from the higher three-year income average, which represents the basis for the calculation.

### 3.3. Summary of the approach to assessing the internal capital needed for current and planned activities

(Article 438 a of CRR)

The Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) of NLB Group meets the requirements of the CRR, the recommendations of the European Central Bank (ECB), EBA and follows good banking practice. Additionally, banking members operating in other SEE countries also follow their own local regulation requirements.

The main purpose of implementation of the ICAAP and ILAAP processes is to provide the following:

- assurance of adequate identification and measurement of risks,
- adequate capital, funding and liquidity of NLB Group in connection with risk appetite,
- assured robust risk management process (from the organisational and methodological point of view) on an ongoing and forward-looking basis.

The key activities for maintaining adequate capitalisation and sufficient liquidity position on an ongoing and forward-looking basis are:

- a strategic planning process which aligns risk appetite and strategy with commercial objectives;
- constant monitoring process of fulfilling approved risk appetite and risk profile,
- regular risk reporting to the Management and Supervisory Boards,
- enabling sufficient economic capital, liquidity reserves and funding in normal and stress conditions (defined within a uniform stress testing framework for the ICAAP, ILAAP; Recovery Plan and risk assessment purposes).

The ICAAP process in NLB Group is integrated into the decision-making process at the strategic and operating level, including the budgeting and capital planning process. With the active role of the Management and Supervisory Boards, it represents one of the key components of the Group's proactive

management, with the aim to ensure stable long-time operations. Pursuant to the EBA guidelines, NLB Group is constantly upgrading the ICAAP process.

NLB Group plans a prudent risk appetite and optimally profitable operations in the long run, considering the risks assumed, while at the same time meeting all regulatory requirements. The Strategy of NLB Group, the Risk Appetite, the Risk Strategy and the key internal risk policies of NLB Group approved by the Management Board and the Supervisory Board of NLB specify the strategic objectives and guidelines concerning risk assumption, the approaches and methodologies of monitoring, measuring, mitigating and managing all types of risk.

When considering the ICAAP process, risk identification and assessment are carried out on the basis of internal methodologies. They take into account the complexity of the structure of NLB Group's operations with a tendency to constantly enhance and complement existing risk management approaches in line with best banking practices. The ICAAP process includes at least regular quarterly monitoring and reporting at the level of the Management and Supervisory Boards of NLB and defines a set of corrective measures for managing and mitigating risks.

The internal assessment of NLB Group's capital requirements consists of the following steps:

- the identification of all risks, the definition of materially significant risks and their treatment in the context of the ICAAP process,
- selection of the approach to the calculation of regulatory capital requirements (Pillar 1),
- definition of the internal methodology for the identification, measurement and calculation of capital requirements for risks not covered within the scope of Pillar 1 (Pillar 2 – ICAAP baseline scenario),
- within established stress testing framework implementation of relevant selected stress scenarios (ICAAP adverse scenario),
- proactive risk management within the ICAAP limits framework from the aspect of fulfilling strategic objectives and use of mitigation measures when necessary.

In the scope of regulatory (Pillar 1) risks, which include credit risk, operational risk and market risk, NLB Group uses the standardised approach for credit and market risks while the calculation of the capital requirement for operational risks is made according to the basic indicator approach. The same approaches are used for calculating the capital requirements for NLB on a standalone basis, except for calculation of the capital requirement for operational risks, where the standardised approach is used.

In the preparation of the internal capital adequacy assessment NLB Group identifies risks not included in the calculation under the regulatory approach (Pillar 1), which have a significant impact on its operation. The scope of additional credit risks also includes concentration risk – to individual clients and groups of related parties, at the level of activity – and collateral concentration risk. NLB Group calculates the capital requirement for non-financial risks (which include profitability risk, strategic risk, divestment risk and reputation risk) if it assesses that an individual risk is crucial for NLB Group. In addition, an adverse scenario includes the effects of stress scenarios for credit (deterioration of the credit rating structure, decrease in real estate market prices), currency, liquidity, interest rate risk in the banking book, credit spread risk, and market risk arising from debt securities.

The comprehensive procedure for the ICAAP and ILAAP processes in NLB Group is defined in an internal document in line with the EBA document "Guidelines on ICAAP and ILAAP information collected for SREP purposes". Besides this, NLB Group banking members operating in other SEE countries set up their own ICAAP process in line with the common Group guidelines, including the specifics of their regulatory requirements, strategic business and risk guidelines and relevant macroeconomic environment.

### **3.4. Capital instruments included in the capital**

(Article 437.1 b and c of CRR)

In 2017, the capital of NLB Group solely consisted of Common Equity Tier 1 capital; the only instruments included in Common Equity Tier 1 capital were the ordinary shares of the parent company NLB d.d.

In 2017, NLB Group had no capital instruments issued that would be eligible for inclusion in Additional Tier 1 capital or Tier 2 capital. Two subsidiary banks in NLB Group do have subordinated instruments, which they themselves use as a capital component, but because of the non-comparability of the legislation, these instruments do not meet the conditions for inclusion in the capital of NLB Group. Subordinated liabilities for

NLB Group are disclosed in the Annual Report for NLB Group 2017- note 5.16 d Subordinated liabilities (page 252).

Table 7 – The main characteristics of the ordinary shares of NLB d.d.:

1	Issuer	NOVA LJUBLJANSKA BANKA d.d., Ljubljana
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	SI002117344
3	Governing law(s) of the instrument	Companies Act (ZGD-1), Banking Act (ZBan-2), Regulation (EU) No. 575/2013 (CRR), Financial Instruments Market Act (ZTFI) and the Book-Entry Securities Act (ZNVF-1)
<b>Regulatory treatment</b>		
4	Transitional CRR rules	Common Equity Tier 1
5	Post-transitional CRR rules	Common Equity Tier 1
6	Eligible at solo/ (sub-)consolidated/ solo&(sub-)consolidated	Solo and Consolidated
7	Instrument type (types to be specified by each jurisdiction)	Ordinary share
8	Amount recognised in regulatory capital (Currency in million, as of most recent reporting date)	Paid up capital and related share premium: 1,071,378
9	Nominal amount of instrument	N/A – No par value shares (20,000,000 shares)
9a	Issue price	EUR 77.55
9b	Redemption price	N/A
10	Accounting classification	Shareholders' equity
11	Original date of issuance	18.12.2013
12	Perpetual or dated	Perpetual
13	Original maturity date	No maturity
14	Issuer call subject to prior supervisory approval	N/A
15	Optional call date, contingent call dates and redemption amount	N/A
16	Subsequent call dates, if applicable	N/A
<b>Coupons / dividends</b>		
17	Fixed or floating dividend/coupon	N/A
18	Coupon rate and any related index	N/A
19	Existence of a dividend stopper	N/A
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary
20b	Fully discretionary, partially discretionary or mandatory (in terms of amount)	Fully discretionary
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 (specify instrument type immediately senior to instrument)	First loss absorbent instrument, subordinated to all instruments
36	Non-compliant transitioned features	No
37	If yes, specify non-compliant features	N/A

N/A – not relevant for this instrument

The ordinary shares are fully included in the Common Equity Tier 1 capital of NLB Group as the only source. The shares meet all the conditions for inclusion in the capital as stated under the relevant provisions of CRR.

### 3.5. Capital buffers - Countercyclical buffer (Article 440 of CRR)

On 1 January 2016, the Bank of Slovenia introduced a macro-prudential measure: a countercyclical capital buffer intended to protect the banking sector from losses potentially caused by cyclical risks in the economy. The purpose of the countercyclical capital buffer is to ensure that the Bank has a sufficient capital base in periods of credit growth, to be used in stress periods or when the conditions for lending are less favourable, i.e. to absorb losses. When the defined buffer rate is more than 0%, or when the already established rate is increased, the new buffer rate applies 12 months after publication (except for extraordinary cases). The buffer value may fluctuate between 0% and 2.5% of the amount of total risk exposure (in exceptional cases also more) and depends on the amount of risk in the system.

The buffer value for exposures in Slovenia was 0% as at 31 December 2017 and stayed the same as the one that was in force from 1 January 2016. To define the buffer rate, the Bank of Slovenia followed the methodology of the BCBS, ESRB, and the credit cycle assessment for Slovenia. The buffer rates applicable to exposure in other countries of the European Economic Area are those defined on the ESRB

website, refreshed quarterly, while the buffer rate applying to credit exposures to countries not listed on that page nor prescribed by the Bank of Slovenia or a competent authority of that country are 0%. Countercyclical capital rates have generally been set at 0%, except for Sweden and Norway, which have as at 31 December 2017 a countercyclical capital rate of 2.0%, and the Czech Republic and Slovakia with a rate of 0.5%.

The obligation to disclose information with regard to the geographic distribution of credit exposure, appropriate to calculate the countercyclical capital buffer, capital requirements, and the rates of the bank-specific countercyclical capital buffer is quarterly, or must be made public at least once a year, depending on the date of publication of financial statements, and applies from 1 January 2016.

A calculation of the bank-specific countercyclical capital buffer is made on an individual, as well as consolidated level. The Bank defines the geographic distribution of exposures, which are subject to the calculation of capital requirement for credit risk using the standardised approach and the special risk or risk of non-payment, and migrations for exposures from the trading book. If the Bank's exposures represent less than 2% of its total risk-weighted exposures, these exposures may be presented at the geographic location of the Bank and additionally explained.

The rate of the bank-specific countercyclical capital buffer is composed of the weighted average of countercyclical capital buffer rates used in those countries where the relevant credit exposures of this institution are located.

Table 8 – Amount of bank-specific countercyclical capital buffer:

<b>31.12.2017</b>	<b>NLB Group</b>	<b>NLB</b>
Total risk exposure amount	415,869	267,649
Institution specific countercyclical buffer rate	0.00%	0.00%
Institution specific countercyclical buffer requirement	-	-

Table 9 – Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer in NLB Group

31.12.2017	General credit exposures		Own funds requirements		Own funds requirement weights	Countercyclical capital buffer rate
	Exposure value for SA	Of which: General credit exposures	Total			
Slovenia	3,927,225	237,654	237,654	0.57	-	
Macedonia	824,249	53,361	53,361	0.13	-	
Bosnia and Herzegovina	652,053	41,927	41,927	0.10	-	
Kosovo	393,036	25,405	25,405	0.06	-	
Montenegro	316,129	22,538	22,538	0.05	-	
Serbia	324,545	20,680	20,680	0.05	-	
Croatia	55,439	5,005	5,005	0.01	-	
United Kingdom	53,774	4,293	4,293	0.01	0.5	
United States	28,264	2,258	2,258	0.01	-	
Germany	10,896	866	866	0.00	-	
Netherlands	8,584	668	668	0.00	-	
France	4,224	332	332	0.00	-	
Belgium	2,570	205	205	0.00	-	
Czech Republic	1,476	144	144	0.00	0.5	
Switzerland	1,961	143	143	0.00	-	
Austria	1,703	119	119	0.00	-	
Norway	1,122	68	68	0.00	2.0	
Luxembourg	1,118	66	66	0.00	-	
Bulgaria	321	36	36	0.00	-	
Slovakia	427	34	34	0.00	0.5	
Cyprus	599	28	28	0.00	-	
United Arab Emirates	245	13	13	0.00	-	
Italy	153	10	10	0.00	-	
Latvia	129	8	8	0.00	-	
Other	132	8	8	0	2	
<b>Total</b>	<b>6,610,374</b>	<b>415,869</b>	<b>415,869</b>	<b>1.00</b>	<b>-</b>	

Table 10 – Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer in NLB

31.12.2017	General credit exposures		Own funds requirements		Countercyclical capital buffer rate
	Exposure value for SA	Of which: General credit exposures	Total	Own funds requirement weights	
Slovenia	3,939,506	240,303	240,303	0.90	0
Serbia	65,923	5,830	5,830	0.02	0
Croatia	45,362	4,400	4,400	0.02	0
Montenegro	45,293	4,387	4,387	0.02	0
United Kingdom	53,758	4,292	4,292	0.02	0.5
Switzerland	39,249	3,126	3,126	0.01	0
United States	22,099	1,765	1,765	0.01	0
Germany	10,153	802	802	0	0
Bosnia and Herzegovina	8,440	709	709	0	0
Netherlands	8,571	667	667	0	0
Macedonia	3,109	378	378	0	0
France	4,224	332	332	0	0
Czech Republic	1,474	143	143	0	0.5
Austria	1,663	117	117	0	0
Kosovo	1,809	110	110	0	0
Norway	1,122	68	68	0	2
Luxembourg	1,118	66	66	0	0
Bulgaria	315	36	36	0	0
Slovakia	427	34	34	0	0.5
Belgium	297	23	23	0	0
Cyprus	496	23	23	0	0
United Arab Emirates	243	13	13	0	0
Italy	149	10	10	0	0
Latvia	129	8	8	0	0
Other	97	4	4	0	2
<b>Total</b>	<b>4,255,026</b>	<b>267,646</b>	<b>267,646</b>	<b>1.00</b>	<b>-</b>

### 3.6. Detailed presentation of capital elements

(Article 437 d and e, and 492.3 of CRR)

The table below shows in detail the elements of the calculation of the capital of NLB Group at the end of the years 2017 and 2016 in the form prescribed by the EBA implementing technical standards, published as Commission Implementing Regulation (EU) No. 1423/2013 of 20 December 2014 (Annex VI – presentation of items in the transitional period). A summarised substantive presentation of the elements relevant for NLB Group is given in Chapter 3.1.

In line with the regulation, the second column of table 11 (Amounts subject to pre-CRR or prescribed residual amount of CRR) includes amounts that are temporarily excluded from the calculation of capital adequacy according to the provisions on the transitional period (residual amounts). Had the provisions applied fully, i.e. without the transitional period, the calculation would present the amount from the first column (Amounts at the disclosure date (transitional arrangements as prescribed for this date) added by the amounts in the second column).

NLB Group does not have any capital instruments (issued before the implementation of CRR) that would no longer be eligible for inclusion and therefore subject to pre-CRR treatment.

Table 11 – Transitional own funds for NLB Group

	31.12.2017		31.12.2016		
	Amount at disclosure date (transitional arrangements as prescribed for this date)	Amounts subject to pre-CRR or prescribed residual amount of CRR	Amount at disclosure date (transitional arrangements as prescribed for this date)	Amounts subject to pre-CRR or prescribed residual amount of CRR	
<b>Common equity Tier 1 (CET1) capital: instruments and reserves</b>					
1	Capital instruments and the related share premium accounts of which: ordinary shares	1,071,378	-	1,071,378	-
		1,071,378	-	1,071,378	-
2	Retained earnings	296,773	-	246,656	-
3	Accumulated other comprehensive income (and other reserves)	30,511	28,439	33,624	26,155
3a	Funds for general banking risk	-	-	-	-
5	Minority interest (amount allowed in consolidated CET1)	-	-	-	-
5a					
	Independently reviewed interim profits net of any foreseeable charge or dividend	29,280	-	49,890	-
<b>6</b>	<b>Common Equity Tier 1 (CET1) capital before regulatory adjustments</b>	<b>1,427,942</b>	<b>28,439</b>	<b>1,401,548</b>	<b>26,155</b>
<b>Common Equity Tier 1 (CET1) capital: regulatory adjustments</b>					
7	Additional value adjustments (negative amount)	(2,389)	-	(2,213)	-
8	Intangible assets (net of related tax liability) (negative amount)	(34,974)	(6,995)	(33,926)	(13,570)
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)	-	-	(5,021)	(2,008)
26	Regulatory adjustments applied to Common Equity Tier 1 in respect of amounts subject to pre-CRR treatment	-	-	-	-
26a	Regulatory adjustments related to unrealised gains and losses pursuant to Articles 467 and 468	(28,439)	-	(26,155)	-
	of which: filter for unrealised loss - exposures to central governments	126	-	717	-
	of which: filter for unrealised loss - other exposures	4,325	-	9,788	-
	of which: filter for unrealised gains - exposures to central governments	(31,302)	-	(30,190)	-
	of which: filter for unrealised gains - other exposures	(1,588)	-	(6,470)	-
26b	Amount to be deducted from or added to Common Equity Tier 1 capital with regard to additional filters and deductions required pre CRR	6,995	-	15,578	-
	of which: intangible assets (including goodwill)	6,995	-	13,570	-
	of which: deferred tax assets that rely on future profitability and do not arise from temporary differences net of associated tax liabilities	-	-	2,008	-
27	Qualifying AT1 deductions that exceed the AT1 capital of the institution (negative amount)	(6,995)	-	(13,570)	-
<b>28</b>	<b>Total regulatory adjustments to Common Equity Tier 1 (CET1)</b>	<b>(65,802)</b>	<b>(6,995)</b>	<b>(65,307)</b>	<b>(15,578)</b>
<b>29</b>	<b>Common Equity Tier 1 (CET1) capital</b>	<b>1,362,140</b>	<b>21,444</b>	<b>1,336,241</b>	<b>10,577</b>
<b>Additional Tier 1 (AT1) capital: regulatory adjustments</b>					
41	Regulatory adjustments applied to Additional Tier 1 in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out as prescribed in Regulation (EU) no 575/2013 (i.e. CRR residual amounts)	-	-	-	-
41a	Residual amounts deducted from Additional Tier 1 capital with regard to deduction from Common Equity Tier 1 capital during the transitional period pursuant to Article 472 of Regulation (EU) no 575/2013	6,995	6,995	13,570	13,570
	of which: intangible assets (including goodwill)	6,995	6,995	13,570	13,570
41b	Residual amounts deducted from Additional Tier 1 capital with regard to deduction from Tier 2 capital during the transitional period pursuant to Article 475 of Regulation (EU) no 575/2013	-	-	-	-
41c	Amount to be deducted from or added to Additional Tier 1 capital with regard to additional filters and deductions required pre- CRR	-	-	-	-
42	Qualifying T2 deductions that exceeded the T2 capital of the institution	(6,995)	-	(13,570)	-
<b>43</b>	<b>Total regulatory adjustments to Additional Tier 1 (AT1)</b>	<b>-</b>	<b>6,995</b>	<b>-</b>	<b>13,570</b>
<b>44</b>	<b>Additional Tier 1 (AT1) capital</b>	<b>-</b>	<b>6,995</b>	<b>-</b>	<b>13,570</b>
<b>45</b>	<b>Tier 1 capital (T1= CET1 + AT1)</b>	<b>1,362,140</b>	<b>28,439</b>	<b>1,336,241</b>	<b>24,147</b>
<b>58</b>	<b>Tier 2 (T2) capital</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>59</b>	<b>Total capital (TC = T1 + T2)</b>	<b>1,362,140</b>	<b>28,439</b>	<b>1,336,241</b>	<b>24,147</b>
59a	Risk weighted assets in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out as prescribed in Regulation (EU) No 575/2013 (i.e. residual amounts)	-	-	-	-
	Items not deducted from T2 items (Regulation (EU) No 575/2013 residual amounts) (items to be detailed line by line, e.g. Indirect holdings of own T2 instruments, indirect holdings of non-significant investments in the capital of other financial sector entities, indirect holdings of non-significant investments in the capital of other financial sector entities, etc.)	-	-	-	-
<b>60</b>	<b>Total risk weighted assets</b>	<b>8,546,482</b>	<b>(33,085)</b>	<b>7,862,128</b>	<b>(21,002)</b>
<b>Capital ratios and buffers</b>					
61	Common Equity Tier 1 (as a percentage of total risk exposure amount)	15.9%	-	17.0%	-
62	Tier 1 (as a percentage of total risk exposure amount)	15.9%	-	17.0%	-
63	Total capital (as a percentage of total risk exposure amount)	15.9%	-	17.0%	-
64	Institution specific buffer requirement (CET1 Requirement in accordance with Article 92(1)(a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus systemically important institution buffer expressed as a percentage of risk exposure amount)	5.75%	-	5.125%	-
65	of which: capital conservation buffer requirement	1.25%	-	0.625%	-
66	of which: countercyclical buffer requirement	0.0%	-	0.0%	-
67	of which: systemic risk buffer requirement	0.0%	-	0.0%	-
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	N/A	-	N/A	-
68	Common Equity Tier 1 available to meet buffers (as a percentage of total risk exposure amount)	7.9%	-	9.0%	-

<b>Amounts below the threshold for deduction (before risk weighting)</b>					
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)	1,692	-	2,138	-
73	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 (amount below 10% threshold and net of eligible short positions)	14,482	-	16,236	-
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)	18,603	-	2,719	-
<b>Applicable caps on the inclusion of provisions in Tier 2</b>					
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	-	-	-	-
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	N/A	N/A	N/A	N/A
78	Credit risk adjustments included in T2 in respect of exposures subject to internal ratings-based approach (prior to the application of the cap)	-	-	-	-
79	Cap on inclusion of credit risk adjustments in T2 under internal ratings-based approach	N/A	N/A	N/A	N/A
<b>Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2014 and 1 Jan 2022)</b>					
80	Current cap on CET1 instruments subject to phase out arrangements	N/A	N/A	N/A	N/A
81	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	-	-	-	-
82	Current cap on AT1 instruments subject to phase out arrangements	N/A	N/A	N/A	N/A
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	-	-	-	-
84	Current cap on T2 instruments subject to phase out arrangements	N/A	N/A	N/A	N/A
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	-	-	-	-

N/A – not relevant

### 3.7. Reconciliation of items with financial statements (Articles 437 a and f, and 447 e of CRR)

Calculations of the capital and capital ratios are based on the financial statements of NLB Group prepared according to regulatory consolidation. Essentially, the capital of NLB Group consists of the elements of equity of the balance sheet (not all elements and not fully) and, in addition, it is reduced by deduction items and prudential filters.

The table below shows to what extent individual balance sheet items are included in the calculation of capital and capital adequacy. In addition to the amounts actually included in the capital calculation for the end of the year (second column – Included in capital as reported), the amounts of these items in their full extent are also presented, i.e. the amounts that would have been taken into account in the calculation of capital adequacy had there been no transitional period arrangements (third column – Fully-loaded capital (transitional agreements not applied)).

Because of the gradual introduction of certain provisions, the capital actually taken into account in the calculation of capital adequacy for the end of 2017 is EUR 28,439 thousands lower than it would have been had all the requirements fully entered into force. The difference arises from accumulated comprehensive income resulting from positive valuation of exposures, mainly related to central governments.

Table 12 – Mapping of the balance sheet items (statement of financial position items) and capital for the purpose of capital adequacy of NLB Group

	31.12.2017			31.12.2016		
	Prudential consolidation	Included in capital as reported	Fully-loaded capital (transitional agreements not applied)	Prudential consolidation	Included in capital as reported	Fully-loaded capital (transitional agreements not applied)
Cash, cash balances at central banks and other demand deposits at banks	1,256,481	-	-	1,299,313	-	-
Trading assets	72,189	(72)	(72)	87,699	(88)	(88)
Financial assets designated at fair value through profit or loss	5,003	(5)	(5)	6,694	(7)	(7)
Available-for-sale financial assets	2,276,493	(2,276)	(2,276)	2,068,470	(2,068)	(2,068)
Derivatives - hedge accounting	1,188	-	-	217	-	-
Loans and advances	7,570,657	-	-	7,489,784	-	-
Held to maturity financial assets	609,712	-	-	611,449	-	-
Fair value changes of hedged items in portfolio hedge of interest rate risk	719	-	-	678	-	-
Non-current assets classified as held for sale	6,224	-	-	4,263	-	-
Property and equipment	188,355	-	-	196,869	-	-
Investment property	51,838	-	-	84,206	-	-
Intangible assets	34,974	(34,974)	(34,974)	33,926	(33,926)	(33,926)
Goodwill	3,529	(3,529)	(3,529)	3,529	(3,529)	(3,529)
Other intangible assets	31,445	(31,445)	(31,445)	30,397	(30,397)	(30,397)
Investments in associates and joint ventures	12,359	-	-	16,024	-	-
Current income tax assets	2,795	-	-	3,942	-	-
Deferred income tax assets	18,603	-	-	7,740	(3,013)	(5,021)
<i>That rely on future profitability and do not arise from temporary differences</i>	-	-	-	5,021	(3,013)	(5,021)
<i>That rely on future profitability and arise from temporary differences</i>	18,603	-	-	2,719	-	-
Other assets	93,349	-	-	94,438	-	-
<b>Total assets</b>	<b>12,200,939</b>	<b>-</b>	<b>-</b>	<b>12,005,712</b>	<b>-</b>	<b>-</b>
Trading liabilities	9,502	(10)	(10)	18,791	(19)	(19)
Financial liabilities designated at fair value through profit or loss	635	(1)	(1)	2,011	(2)	(2)
Derivatives - hedge accounting	25,529	(25)	(25)	29,024	(29)	(29)
Financial liabilities measured at amortised cost	10,411,682	-	-	10,358,105	-	-
Provisions	88,639	-	-	89,716	-	-
Current income tax liabilities	2,894	-	-	3,117	-	-
Deferred income tax liabilities	1,096	-	-	711	-	-
Other liabilities	9,596	-	-	8,764	-	-
<b>Total liabilities</b>	<b>10,549,573</b>	<b>-</b>	<b>-</b>	<b>10,510,239</b>	<b>-</b>	<b>-</b>
Share capital	200,000	200,000	200,000	200,000	200,000	200,000
Share premium	871,378	871,378	871,378	871,378	871,378	871,378
Accumulated other comprehensive income	16,989	(11,450)	16,989	20,102	(6,053)	20,102
<i>From debt securities</i>	33,695	1,914	33,695	32,063	1,124	32,063
<i>AFS exposures to central governments - positive effects</i>	31,302	-	31,302	30,190	-	30,190
<i>AFS exposures to central governments - negative effects</i>	(629)	(503)	(629)	(1,793)	(1,076)	(1,793)
<i>Other exposures</i>	3,022	2,417	3,022	3,666	2,200	3,666
<i>From equity securities</i>	3,735	2,988	3,735	11,017	6,610	11,017
<i>From hedge of net investment in foreign operation</i>	754	603	754	754	452	754
<i>Foreign currency translation</i>	(16,826)	(13,461)	(16,826)	(20,115)	(12,069)	(20,115)
<i>Actuarial defined benefit pension plans</i>	(4,369)	(3,495)	(4,369)	(3,617)	(2,170)	(3,617)
Profit reserves	13,522	13,522	13,522	13,522	13,522	13,522
Retained earnings	515,147	326,053	326,053	360,329	296,546	296,546
<i>Retained earnings - from previous years</i>	296,773	296,773	296,773	246,656	246,656	246,656
<i>Retained earnings - current results</i>	218,374	29,280	29,280	113,673	49,890	49,890
Treasury shares	-	-	-	-	-	-
Non-controlling interests	34,330	-	-	30,142	-	-
<b>Total equity</b>	<b>1,651,366</b>	<b>-</b>	<b>-</b>	<b>1,495,473</b>	<b>-</b>	<b>-</b>
<b>Total liabilities and equity</b>	<b>12,200,939</b>	<b>-</b>	<b>-</b>	<b>12,005,712</b>	<b>-</b>	<b>-</b>
<b>Sum of balance sheet items</b>		<b>1,362,140</b>	<b>1,390,579</b>		<b>1,336,241</b>	<b>1,360,388</b>
<b>Capital</b>		<b>1,362,140</b>	<b>1,390,579</b>		<b>1,336,241</b>	<b>1,360,388</b>

Table 13 – Reconciliation of the accounting capital to the regulatory capital for the calculation of capital adequacy of NLB Group

	Equity - Prudential consolidation	Dividends	Exclusion of minority interest not eligible according to CRR requirements	Exclusion of 100% of unrealised profits from exposures to central governments (in transitional period)	Exclusion of 20% of unrealised losses from exposures to central governments (in transitional period)	Exclusion of 20% of unrealised losses and profits from other exposures (in transitional period)	Prudential filters and deduction items from capital	Capital (included in calculation of capital adequacy)	
<b>31.12.2017</b>									
Share capital	200,000	-	-	-	-	-	-	200,000	Paid in capital instruments
Share premium	871,378	-	-	-	-	-	-	871,378	Share premium
Accumulated other comprehensive income	16,989	-	-	(31,302)	126	2,737	-	(11,450)	Accumulated other comprehensive income
Profit reserves	13,522	-	-	-	-	-	-	13,522	Other reserves
Retained earnings - from previous years	296,773	-	-	-	-	-	-	296,773	Retained earnings - from previous years
Retained earnings - current results	218,374	(189,094)	-	-	-	-	-	29,280	Current results
Minority interest	34,330	-	(34,330)	-	-	-	-	-	Minority interest
							(2,389)	(2,389)	Prudential filter: Additional valuation adjustment (AVA) (Article 34)
							(3,529)	(3,529)	Deduction item: Goodwill (Article 36.b)
									Deduction item: Other intangible assets (Article 36.b)
							(31,445)	(31,445)	
<b>Total equity</b>	<b>1,651,366</b>	<b>(189,094)</b>	<b>(34,330)</b>	<b>(31,302)</b>	<b>126</b>	<b>2,737</b>	<b>(37,363)</b>	<b>1,362,140</b>	<b>Common Equity Tier 1 (CET1) capital</b>
									- Additional Tier 1 capital
									<b>1,362,140 Tier 1 capital</b>
									- Tier 2 capital
									<b>1,362,140 Total capital</b>
	Equity - Prudential consolidation	Dividends	Exclusion of minority interest not eligible according to CRR requirements	Exclusion of 100% of unrealised profits from exposures to central governments (in transitional period)	Exclusion of 40% of unrealised losses from exposures to central governments (in transitional period)	Exclusion of 40% of unrealised losses and profits from other exposures (in transitional period)	Prudential filters and deduction items from capital	Capital (included in calculation of capital adequacy)	
<b>31.12.2016</b>									
Share capital	200,000	-	-	-	-	-	-	200,000	Paid in capital instruments
Share premium	871,378	-	-	-	-	-	-	871,378	Share premium
Accumulated other comprehensive income	20,102	-	-	(30,190)	717	3,318	-	(6,053)	Accumulated other comprehensive income
Profit reserves	13,522	-	-	-	-	-	-	13,522	Other reserves
Retained earnings - from previous years	246,656	-	-	-	-	-	-	246,656	Retained earnings - from previous years
Retained earnings - current results	113,673	(63,783)	-	-	-	-	-	49,890	Current results
Minority interest	30,142	-	(30,142)	-	-	-	-	-	Minority interest
							(2,213)	(2,213)	Prudential filter: Additional valuation adjustment (AVA) (Article 34)
							(3,529)	(3,529)	Deduction item: Goodwill (Article 36.b)
									Deduction item: Other intangible assets (Article 36.b)
							(30,397)	(30,397)	
									Deduction item: Deferred tax assets that rely on future profitability and do not arise from temporary differences net of associated liabilities (Article 36.c)
							(3,013)	(3,013)	
<b>Total equity</b>	<b>1,495,473</b>	<b>(63,783)</b>	<b>(30,142)</b>	<b>(30,190)</b>	<b>717</b>	<b>3,318</b>	<b>(39,152)</b>	<b>1,336,241</b>	<b>Common Equity Tier 1 (CET1) capital</b>
									- Additional Tier 1 capital
									<b>1,336,241 Tier 1 capital</b>
									- Tier 2 capital
									<b>1,336,241 Total capital</b>

During 2017 total accounting equity increased by EUR 156 million to EUR 1,651 million as at 31 December 2017, primarily due to retained earnings from previous years (NLB Group's result for year 2016 deducted for dividend payment in 2017) and net profit of current year, deducted for dividend payments, which also reflects in the increase of the regulatory capital.

## 4. Risk management, objectives and policies

### 4.1. General information on risk management, objectives and policies

(Articles 435.1 a, b, c, d, e and f and 435.2 e of CRR)

NLB Group is the largest banking and financial group in Slovenia with a strategic focus on selected markets in SEE, namely Bosnia and Herzegovina, Serbia, Montenegro, Macedonia and Kosovo. The Group is comprised of NLB as the parent entity in Slovenia, six subsidiary banks in SEE, several companies for ancillary services (asset management, insurance, real estate management, etc.), and a limited number of non-core subsidiaries in a controlled wind-down. The Group has a leading position in selected SEE markets with significant growth potential, focusing mainly on corporate and retail lending. Moreover, it has a very strong retail deposit-taking franchise, whereby providing asset management services is also important. The Group's strategy foresees enhancement of the Bank's commercial proposition, rightsizing of costs, and increased digitalisation. Its implementation is expected to improve the Group's operations, enhance revenues, reduce costs, and improve its growth prospects.

NLB Group pays great attention to and places great importance on risk culture and awareness of all relevant risks within the entire Group. The Group is committed to developing a culture of client focus, risk awareness, integrity, efficient organisation, and social responsibility. The trust of the Group's clients, employees, shareholders, and the society in which it works is seen by the Group as a profound responsibility. Risk management in NLB Group is implemented in accordance with the established internal policies and procedures which take into account the European banking regulations, the regulations adopted by the Bank of Slovenia, the current EBA guidelines and relevant good banking practice. All strategic risk documents and policies are subject to at least regular yearly revision.

In accordance with its business model and strategy, the Group plans a prudent risk profile, optimal capital usage and profitable operations in the long run, considering the risks assumed. The NLB Group Risk Management Framework is defined and organised with regard to the Group's business and risk profile, based on a forward-looking perspective to meet internal objectives and all external requirements. The Group's Risk Management Framework supports business decision-making at a strategic and operating level, comprehensive steering and proactive risk management by incorporating:

- the Risk Appetite Statement and risk strategy orientations,
- yearly review of strategic goals, budgeting and the capital planning process,
- the ICAAP process and the ILAAP process,
- recovery and resolution plan activities,
- other internal stress-testing capabilities and comprehensive risk analysis.

#### Risk appetite

NLB Group's Risk Appetite Statement represents a strategic statement defining the maximum level of risk the Group is willing to assume or to avoid, based on its risk-bearing capacity, in order to achieve the strategic business objectives. Risk appetite is defined through qualitative assertions and quantitative measures. Qualitative statements define key risk principles regarding risk management, while quantitative metrics provide directions for risk steering from a forward-looking perspective in terms of capital, liquidity and risk-return optimisation. As such, Risk Appetite codifies the existing risk culture, principles, objectives and measures in NLB Group.

In accordance with the Risk Appetite Statement, NLB Group as the largest Slovenian banking and financial group, intends to be a sustainably profitable banking group, predominantly working with clients in its defined core markets. The Group's Risk Appetite Statement is further deployed to the core subsidiaries within the Group under consideration of the approved proportionality orientations. Based on the Group's business strategy the key risks are credit risk, interest rate risk in the banking book, liquidity risk, operational risk, market risk and other non-financial risks. Regular risk identification and their assessment is performed within the ICAAP with the aim to assure their overall control and proactive risk management.

Management of credit risk, which is the most important risk in NLB Group, focuses on the taking of moderate risks – diversified credit portfolio, adequate credit portfolio quality, sustainable cost of risk and ensuring an optimal return considering the risks assumed. The liquidity risk tolerance is low. NLB Group must maintain an appropriate level of liquidity at all times to meet its short-term liabilities, even if a specific stress scenario is realised. Further, with the aim of minimising this risk, the Group pursues an appropriate structure of sources of financing. In the area of currency risk, NLB Group thus pursues the goals of low to moderate exposure. NLB Group's basic orientation in the management of interest rate risk is to prevent

negative effects on revenues that would arise from changed market interest rates and, therefore, a low tolerance for this risk is stated. The conclusion of transactions in derivative financial instruments at NLB is primarily limited to servicing customers and hedging NLB's own positions. When assuming operational risk, NLB Group pursues the orientation that such risk must not significantly impact its operations and, therefore, the risk appetite for operational risks is low to moderate. The tolerance for all other risk types (for example, reputation risk, profitability risk and others) is low with a focus on minimising their possible impacts on the Group's operations. These also include non-financial risks.

The main NLB Group risk appetite objectives are the following:

- Preservation of a prudent level of capital adequacy including regulatory requirements and capital buffers;
- Maintenance of a solid level and structure of liquidity minimising potential shortfalls;
- Customers' deposits as the main funding base;
- Adequate quality of the credit portfolio, sustainable cost of risk, ensuring sustainable, limited credit risk volatility and limited exposure to project financing;
- Diversification of risk in exposures to banks and sovereigns;
- Limited exposure to interest rate risk in the banking book and to consolidated FX risk (from transactional risk);
- Ensuring sustainable profitability in terms of risk-return;
- Ensuring sustainable and limited size of subsidiary banks.

The values of the most important risk appetite indicators of NLB Group as at the end of 2017, reflecting interconnection between strategic business goals, risk strategy and targeted risk appetite profile, were the following:

- CET1 15.9%,
- cost of risk – 62 bps,
- the share of NPE by EBA 6.7%,
- LTD 70.8%,
- LCR 276%,
- NSFR 149%,
- BPV sensitivity (of 200 bps) 5.7% of capital.

Consequently, NLB Group concluded the year 2017 within its target risk appetite, with strong capital and liquidity position.

In addition, NLB Group established risk profile limits, based on Risk Appetite and Risk Strategy with the aim to support mid- and long-term risk strategy. Such risk management governance ensures comprehensive oversight of risk decisions and of overall risk strategy execution. Mitigation measures are undertaken within the regular risk management process, with aim of ensuring risk appetite indicators within the targeted profile.

### **Risk management, hedging and mitigation**

The key goal of NLB Group's Risk Management is to proactively manage, assess, and monitor risks within the Group. A sound and holistic understanding of risk management is embedded into the entire organisation, focusing on risk identification in a very early stage, efficient risk management and mitigation of risk with the aim to ensure the prudent and economic use of its capital. The key risk guidelines of NLB Group are defined by its Risk Appetite and Risk Strategy with regards to the Group's business model, based on a forward-looking perspective, which are regularly revised and enhanced. The Strategy of NLB Group, the risk appetite and risk strategy guidelines and the key internal policies of NLB Group – which are approved by the Management Board and by the Supervisory Board – specify the strategic goals, risk appetite guidelines, approaches, and methodologies for monitoring, measuring, and managing all types of risk in order to meet internal objectives and all external requirements. In addition, main strategic risk guidelines are integrated into the annual business plan review and budgeting process.

NLB regularly monitors its target risk appetite profile, both for NLB Group and NLB, representing the key component of the risk mitigation process. Risk profile, on a strategic and operational level, enables detailed monitoring and proactive management of exposure to credit, market, interest, liquidity, and operational risk, while non-financial and other risks are managed within the ICAAP process. The usage of risk profile limits and potential deviations from limits and target values are reported regularly to the respective committees and/or the Management Board of the Bank. A comprehensive Risk Report is reviewed quarterly both by the Management Board, the Risk Committee of the Supervisory Board, and the Supervisory Board of the Bank.

The banking subsidiaries within NLB Group have adapted a corresponding approach to monitor their target risk profiles. Set governance and different risk management tools enable adequate oversight of the Group's risk profile. Besides this, they proactively support the Group's business operations and its management by incorporating escalation procedures and different mitigation measures when necessary. Additionally, the Group has set up early warning systems in different risk areas with the intention of strengthening existing internal controls and responding in a timely way when necessary.

For the purpose of an efficient risk mitigation process, NLB Group applies a single set of standards to retail and corporate loan collateral with the aim of efficient credit risk mitigation and consuming capital economically. The Group applies a cash-flow based credit policy that considers the repayment capacity of the client when approving or extending the loan or other credit exposure. Received collateral represents a secondary source of repayment. In the area of project finance a careful monitoring process is established by different experts within relevant phases of the project, namely in terms of fulfilling requested conditions and criteria before disbursement. Project finance status is regularly reported to the respective committees.

NLB Group has a system for monitoring and reporting collateral at fair (market) value in accordance with the International Valuation Standards (IVS). The Collateral Management Policy additionally defines requirements regarding collateral enforceability and a list of acceptable and eligible types of collateral. The eligibility of different types of collateral, by types and ratios, referring to prudent lending criteria, is further set within internal lending guidelines. Credit portfolio and collateral structure, also in terms of concentrations, and other relevant analysis are regularly reported to the respective committees. In the Retail segment special focus is placed on monitoring of fulfilment of macro-prudential guidelines (LTV, LTI). The Group has also established guidelines with respect to prudent foreign exchange (FX) lending across different SEE markets where the Group members operate, where market practices vary along with different business strategies.

The Group operates its main business activities in euros, while in the case of the subsidiary banks, beside their domestic currencies, they also partly operate in euros, which is the Group's reporting currency. The Group's net open FX position from transactional risk is relatively low and proactively managed on a daily basis. NLB Group's profitability is to a large extent based on its respective net interest income levels. For that reason, stabilising net interest income is the Group's primary goal when managing interest rate risk, where the Group monitors its interest rate sensitivity from the aspects of income and economic value. All Group members manage their interest rate risk positions proactively, in accordance with relatively conservative interest rate risk policies and limits. When hedging market risks, namely interest rate risk and foreign exchange risk, in line with the set risk appetite, NLB Group follows the principle of natural hedge or using derivatives in line with hedge accounting principles.

NLB Group has defined detailed Standards for Liquidity Risk Management, where regulatory and internally developed measures, approaches and stress test capabilities are constantly monitored, controlled, managed and further developed in line with the latest banking practices. Additionally, all banking members have established a Contingency Plan, focusing on measures for overcome potential temporary and/or long-term liquidity disruptions.

### **Stress testing**

NLB Group is subjected to external stress tests conducted by the EBA and the ECB. The last comprehensive ECB Stress Test was executed in the year 2016, meanwhile the Group will participate in an already announced stress test exercise in 2018. In 2017, the Group was included in the ECB Stress Test, focusing on sensitivity analysis and various components of interest rate risk on the banking book. The results reflected in the favourable adjustment of Pillar 2 Guidance as a part of overall SREP requirements.

NLB Group has established a comprehensive internal stress testing framework and other early warning systems in different risk areas with the intention to strengthen the existing internal controls and ensure a timely response when necessary. The robust and uniform stress-testing framework includes all material types of risk (by including all relevant exposures on the Group level) and several relevant stress scenarios, according to the vulnerability of the Group's business model. Such a stress-testing framework also enables additional robustness of the risk management framework, focusing on proactive risk management and steering in stressed circumstances. It is integrated into Risk Appetite, the ICAAP, ILAAP and the Recovery Plan to support proactive management of the Group's overall risk profile, namely the capital and liquidity position from a forward-looking perspective. Additionally, other partial risk assessments are covered by sensitivity analysis based on relevant stressed risk parameters.

The complex internal stress test methodology is based on the presumption of severe but plausible stress scenarios. NLB Group employs a so-called bottom-up stress-testing approach, using its internally developed models and sensitivity analysis, related to identifying the material risk of the Group within the risk identification process. In general, three types of stress scenarios are performed – system level (real economy crisis), idiosyncratic, and combined stress scenarios. Additionally, reverse stress tests are also used for certain risk categories, whereby stress testing starts from the identification of the pre-defined outcome and then explores scenarios and circumstances that might cause this to occur.

These models incorporate scenarios according to ECB forecasts, forecasts of UMAR and other relevant own assumptions. With such an approach a high level of data granularity is requested, with the use of available external data mainly related to relevant risk factors per each selected risk category. Furthermore, in most scenarios a methodological assumption of “static balance sheet” is used, meaning a constant balance sheet and an unchanged or stable business model is presumed throughout the projected stress test time horizon. The severity of the scenario means the degree of deterioration (from baseline to adverse scenarios), expressed by the underlying macroeconomic and other financial variables, and including any other scenario-related assumptions. Greater severity of the stress test scenario, in general, translates to a larger impact on the Group’s performance, capital adequacy and liquidity indicators.

The table below sketches risk groups, areas of corresponding stress testing procedures and the relevant decision-making bodies where results are presented.

Risk category	Stress test type	Decision making body	Frequency
Credit risk: stress test (scenario: economic crisis and weak operating environment for banks)	ICAAP, RP, ECB/EBA	ALCO, Supervisory Board	Quarterly
Credit risk: individual concentration	ICAAP, RP	ALCO, Supervisory Board	Quarterly
Credit risk: industry concentration	ICAAP, RP	ALCO, Supervisory Board	Quarterly
Credit risk: FX lending	ICAAP, ECB/EBA	ALCO, Supervisory Board	Quarterly
Operational risks	ICAAP, RP, ECB/EBA, other internal ST,	ALCO, Supervisory Board, OpRC	Expected yearly (frequently if necessary)
Market risk: FX risk	ICAAP, ILAAP, RP, ECB/EBA, other internal ST	ALCO, Supervisory Board	Monthly/ Quarterly
Other market risks	ILAAP, ICAAP	ALCO, Supervisory Board	Quarterly
IR risk in banking book	ICAAP, ILAAP, RP, ECB/EBA, other internal ST	ALCO, Supervisory Board	Monthly/ Quarterly
Credit spread risk/valuation risk	ICAAP, ILAAP, RP, ECB/EBA, other internal ST	ALCO, Supervisory Board	Monthly/ Quarterly
Liquidity risk: overall liquidity position	ICAAP, ILAAP, RP, other internal ST	ALCO, Supervisory Board	Monthly
Liquidity risk: intraday liquidity	ILAAP, other internal ST	ALCO	Monthly
Liquidity risk: stability of sight deposits	ILAAP, other internal ST	ALCO	Monthly

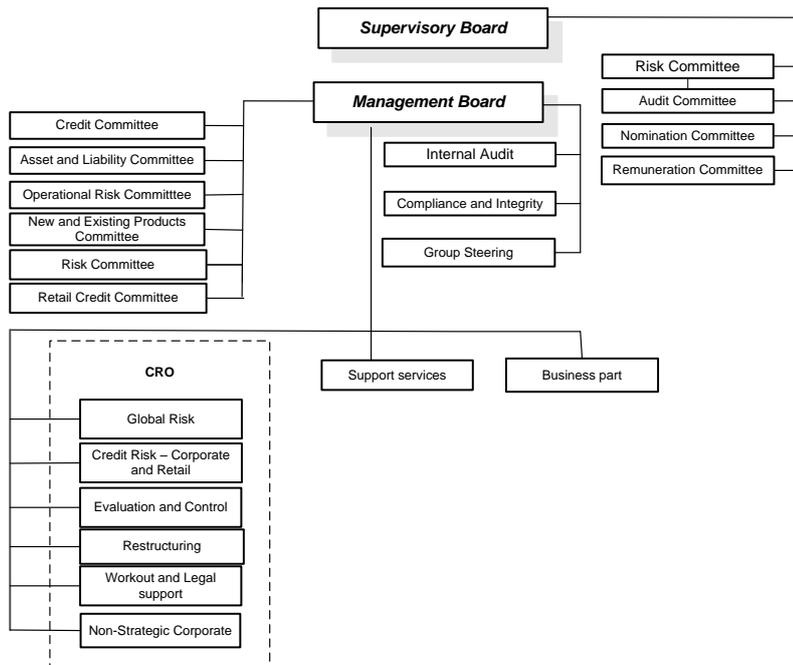
\* RP=Recovery plan, ST=Stress test

The most complex stress test is represented by the NLB Group Recovery Plan, which covers indicators (calibrated to trigger the initiation of stressed circumstances in a timely manner), various severe/extreme stress scenarios and recovery options for these stress scenarios. Recovery options are defined separately for solvency or liquidity extreme stress test circumstances, by defining options for the return of the Group to normal operations. Reverse stress tests are used for the purpose of defining maximum available recovery options capability. The ICAAP covers overall risk identification and distribution of capital for covering potential risks in baseline and adverse scenarios, while the ILAAP covers the whole process of liquidity management and stress testing in the area of liquidity management. The methodological approach in all these processes is similar, but using different density of potential shocks (extreme, adverse, baseline and reverse).

The stress-testing framework described above is fully integrated into the NLB Group Risk Management Framework through regular comprehensive risk reporting, monitoring and managing at the highest decision-making level, by including the Management Board, the Risk Committee of the Supervisory Board, and the Supervisory Board of the Bank.

## Risk management structure and organisation

### Risk management structure within NLB



The tasks and responsibilities of Global Risk, Compliance, and Internal Audit are set out in accordance with the definitions of the Zban-2, under which all such functions are independent and have direct access to NLB's Supervisory Board. Several layers of management provide cohesive risk governance. The responsibilities of specific risk management bodies are described below.

#### *Management Board and its working bodies*

The Management Board of NLB leads, presents and acts in the name of the Bank individually and on its own responsibility and has authority in accordance with law and the Act of the Bank itself.

With the aim of appropriate and effective performance management, the Management Board has created a system of adequate risk management, internal audit and corporate management. The Management Board of NLB is a working body where the Management Board manages its business process and adopts key management decisions. Additional working bodies of the Management Board, where risk-related issues are the subject of discussion and decision-making, are:

- Credit Committee whose role is to accept decisions on grading classifications, set exposure limits and approve loans in commercial banking, in line with the Rules on Authorisations and Signing, including materially important clients within the NLB Group.
- Asset and Liability Committee (ALCO) whose role is to analyse balance sheet positions, changes and trends, and also to form decisions to achieve the balance sheet structure in line with the Bank's business policy. Its wider role includes overseeing normal banking activity; that goals are set and targets are achieved.
- Operational Risk Committee whose role is monitoring, guiding and supervising operational risk and other risks related to operational risk (such as IT and physical security, incidents, risk associated with projects, internal controls, etc.) management in NLB and NLB Group.
- New and Existing Products Committee whose role is assessing and mitigating risks when introducing new products and when substantial changes of existing products is proposed.
- Risk Committee whose role is to discuss, oversee, follow up and periodically review risk and risk-commercial related issues and submit them to the Management Board for a decision. Information on up of a risk committee and the number of times the Risk Committee has met is disclosed in Appendix 1.
- Retail Credit Committee whose role is to accept decisions on lending and other investments with terms and conditions deviating from the regular offer and exceeding authorisations of retail network directors defined by the Management Board.

### *Supervisory Board and its working bodies*

The Supervisory Board of NLB is composed of members who are appointed and recalled by the General Meeting of the Bank. Its task is to monitor and supervise the management of NLB and its operations. There are four working committees of the Supervisory Board, namely:

- Risk Committee monitors and drafts resolutions for the Supervisory Board in all areas of risk relevant to NLB's operations. It consults on the current and future Risk Appetite and the Risk Management Strategy and it helps exercise control over senior management as regards implementation of the Risk Management Strategy.
- Audit Committee monitors and prepares draft resolutions for the Supervisory Board on financial reporting, internal control and risk management, internal audit, compliance, external audit and supervises the implementation of regulatory measures.
- Nomination Committee drafts proposed resolutions for the Supervisory Board concerning the appointment and dismissal of Management Board members, recommends candidates for Supervisory Board members to the General Meeting of NLB, recommends to the Supervisory Board the dismissal of members of the Management Board and the Supervisory Board, prepares the content of executive employment contracts for the President and members of the Management Board, evaluates the performance of the Management Board and the Supervisory Board, and assesses the knowledge, skills and experience of individual members of the Management Board and Supervisory Board as a whole. The Committee proposes amendments to the Management Board's policy on the selection and appointment of suitable candidates for senior management of NLB.
- Remuneration Committee carries out expert and independent assessments of remuneration policies and practices and on this basis formulates initiatives for measures related to improving the management of NLB's risks, capital and liquidity, prepares proposals for decisions of the Supervisory Board in relation to remuneration, and supervises the remuneration of senior management performing risk management and compliance functions.

### *Risk management role in NLB Group*

The robust Risk Management Framework is comprehensively integrated into the decision-making, steering and mitigation processes within the Group in order to proactively support its business operations. Risk Management in NLB Group is in charge of managing, assessing, and monitoring risks within NLB as the parent entity in Slovenia, and the competence centre for six banking subsidiary banks. Furthermore, NLB is also responsible to several companies for ancillary services, and a number of non-core subsidiaries which are in a controlled wind-down.

Overall, the organisation and delineation of competencies in NLB Group's risk management structure is designed to prevent conflicts of interest and ensure a transparent and documented decision-making process, subject to an appropriate upward and downward flow of information. Risk Management in NLB Group is centralised within the Risk Management business line. The Risk Management business line is a specialised business line encompassing several professional areas, for which Global Risk, Corporate and Retail Credit Analysis and Evaluation and Control are responsible within NLB, and which reports to the Assets and Liabilities Committee of the Management Board and the Risk Committee of the Supervisory Board. The Risk Management business line is in charge of formulating and controlling the risk management policies of NLB Group, overseeing the harmonisation of risk management policies within NLB Group, monitoring NLB Group's risk exposures, and the preparation of external and internal reports. The "NLB Group Risk Management Standards" are guidelines which represent the basis for the establishment and organisation of risk management and associated activities at each NLB Group member. These guidelines and standards in the area of credit, market, liquidity, operational and other non-financial risk management represent the basis for the adaptation of NLB Group members' business policies, organisational structures, work procedures and reporting systems. NLB prescribes the methodologies and procedures and governs and controls NLB Group in accordance with EU and Slovenian regulation. At the same time, NLB Group members must also fulfil the requirements set out in local legislation.

All members of NLB Group which are included in the financial statements of NLB Group report their exposure to risks to the competent organisational units (here after 'OU') within the Risk Management business line. These OUs then report all relevant risk information to the ALCO of the Management Board and the Risk Committee of the Supervisory Board, which is where the Management Board and the Supervisory Board adopt appropriate measures.

Credit ratings of clients that are materially important to NLB Group and the issuing of credit risk opinions are centralised via the Credit Committee of NLB. The process follows the co-decision principle, in which the credit committee of the respective group member first approves their decision, following which the Credit

Committee of NLB gives their opinion. The resolution of the Credit Committee of NLB is made on the basis of all available documentation, including a non-binding rating opinion prepared by the underwriting department of NLB (Corporate and Retail Credit Analysis). This same principle and process is also set for the issuing of credit exposures for the materially important clients of NLB Group.

#### *Risk management in NLB Group members*

The primary responsibility for managing the risks assumed by NLB Group members within the framework of their business strategy lies with each NLB Group member's management. An NLB Group member's management, in accordance with the set limits, targets and other guidelines established at NLB Group level, pursue NLB Group's strategic goals, implement NLB Group's planned business results and monitor and manage risks. In furtherance of this, NLB Group members each adopt appropriate risk management policies approved by the supervisory board of the applicable member. The supervisory board of each NLB Group member also monitors the implementation of that member's risk management policies and assesses their effectiveness.

Risk monitoring in NLB Group members is centralised within an independent OU. The centralised monitoring of risks aims to establish standardised and systemic approaches to risk management, and therefore, a comprehensive overview of the Group's and of each member's statement of financial position. In compliance with the risk management policies of NLB Group, risk monitoring in each NLB Group member is separated from risk management and business function in order to maintain the objectivity required when assessing business decisions. The OU for managing risks directly reports to the Management Board and its committees (Credit Committee, ALCO and Operational Risk Committee), which report to the Supervisory Board (Risk Committee of the Supervisory Board or Board of Directors).

#### **Risk measurement and reporting systems**

As a systemic bank, NLB is subject to the Single Supervisory Mechanism (SSM), which is supervised by the Joint Supervisory Team of the ECB and the Bank of Slovenia. Each NLB Group member complies with ECB regulation while NLB Group subsidiaries operating outside Slovenia are also compliant with the rules set by the local regulators. NLB Group's measurement systems and the risk management principles are crucial elements of the risk management policies. They are, for the purpose of consolidated control, aligned with all regulatory acts and requirements of the Bank of Slovenia and the ECB, taking into account the provisions of the CRD, CRR, and EBA guidelines.

In regards to capital adequacy, NLB Group applies the standardised approach to credit and market risk and the basic approach (a simplified approach with less data granularity) to operational risks, with the exception of NLB which applies the standardised approach.

NLB Group performs a uniform assessment and management of risks across the entire Group, taking into account the specifics of the markets in which individual Group members are operating in line with the Group's Risk management standards. For the purposes of measuring of exposure to credit, market, interest, operational, and non-financial risks, in addition to prescribed regulations, NLB Group uses internal methodologies and approaches that enable more detailed monitoring and management of risks. These internal methodologies are aligned with the Basel and EBA guidelines, as well as best practices in banking methodologies.

As for risk reporting, NLB Group's internal guidelines reflect, in addition to internal requirements, the substance and frequency of reporting required by the Bank of Slovenia and the ECB. In addition, each member of NLB Group also complies with the requirements of its local regulations. Risk reporting is carried out in the form of standardised reports, pursuant to risk management policies founded on reasonable methodologies for measuring and harmonising exposure to risks, appropriate databases and the automation of report preparation, which ensures the quality of reports and reduces the possibility of errors.

Management Board statement regarding risk management systems in NLB Group is disclosed in chapter 16.4, Appendix 4. The statement is part of the Capital adequacy statement of NLB Group at 31 December 2017, adopted by the Management Board.

#### **Internal control framework**

As an important element of its Risk Management function and organisation, NLB Group uses the three lines of defence framework. Within this framework, the Business Line on one side and Risk Management on the other both bear full responsibility for the assumption of risk. Internal Audit reviews key risks in its operations and provides independent and comprehensive supervision of the internal control system. Beyond monitoring fulfilment of legal and regulatory requirements Compliance is also concerned with ethics and integrity within the whole Group.

Therefore, the three lines of defence are:

- the Business parts constitutes the first line, proposing business decisions within the framework of defined internal policies and authorisations, and consequently assuming responsibility for the risks assumed;
- the Risk Management function comprises the second line, defining rules about the risk appetite, risk strategy, risk monitoring and management on one side, and analysing and co-deciding on the risks suggested by the business part, and thereby assuming responsibility for the analysis and the risks assumed (in relation to underwriting opinion, restructuring and workout decisions). However, additional independent controls regarding risk management decisions and compliance with risk strategy targets are carried out within Global Risk in order to prevent any potential conflict of interest. Global Risk as a function is directly responsible to the Management Board and has direct access to the Supervisory Board;
- Compliance function also makes up the second line of defence, whereas the Internal Audit as the third line of defense monitors decision-making process in all areas of NLB Group, reviews key risks in its operations, advises management at all levels, and deepens the understanding of the Bank's operations. Furthermore, it provides independent and impartial assurances regarding the management of key risks, management of the Group and operation of internal controls. Compliance function focuses on the systematic monitoring of the legal and regulatory environment, including evaluation of its effects on the Group's operations. Beyond purely regulatory issues, the Compliance function deals also with ethics and integrity within the organisation. A great emphasis is put on prevention, namely preventing harmful conduct and incidents in the Group. To ensure that appropriate standards are met, internal audit and compliance functions are organised within the NLB Group, in line with Corporate Governance Policy of the NLB Group. Specific standards and requirements are made for NLB Group members which ensure harmonisation of approaches and implementation of policies and procedures related to compliance risk management, as well as standards for internal audit functions. Internal Audit and Compliance functions in NLB Group report thereon to the competent expert services and management bodies, and have direct access to the Supervisory Board.

The specialised Risk Management function within Global Risk covers overarching aspects of risk management. Its mandate is to provide an increased focus on holistic risk management and cross-risk oversight to further enhance risk steering and mitigation within the whole Group. Key objectives refer to:

- providing a strategic and forward-looking perspective on the key risk issues for discussion at senior levels within the Group (Risk Appetite, Risk Strategy, the ICAAP and ILAAP, Recovery Plan, stress testing framework);
- strengthening risk culture in the bank in cooperation with other OUs and
- fostering the implementation of consistent risk management standards.

NLB Group, through its Internal Audit seeks to adequately monitor key risks which might jeopardise the achievement of its strategy and goals, related control systems and governance processes. By providing assurances and advice, and with a deep understanding of operations, Internal Audit helps to strengthen and protect the value of NLB Group. The best practice examples and international guidelines established by the Committee of Sponsoring Organisations of the Treadway Commission ("COSO") are the criteria Internal Audit uses to cover all control objectives and risk management.

Internal Audit serves as an advisory tool for the systematic and professional assessment of the success of NLB Group's risk management procedures, control system, and governance of NLB Group operations. Following risk-based methodology, Internal Audit prepares the yearly audit plan, which was approved by the Management Board and the Supervisory Board. On that basis, Internal Audit serves as an impartial guide to the Management Board and the Supervisory Board regarding those areas of NLB and of NLB Group with the highest risk in order to help ensure such risks are managed appropriately. Internal Audit also performs "Group audits" in which internal auditors of NLB Group members participate in order to provide assurance at NLB Group level, as well as to provide additional expertise and assistance. Furthermore, a review of the quality of the internal audit service performance was carried out on all six banking members of NLB Group.

Internal Audit dedicates significant resources to verifying whether audit recommendations have been fulfilled, providing training, consultancy to the management, and promoting assurance of high-quality and professional operations of the internal audit function. Internal Audit is introducing uniform rules of operation as part of the internal audit function and supervising compliance with these rules across the entire Group.

Internal Audit and other internal audit services in NLB Group operate in accordance with the International Standards for the Professional Practice of Internal Auditing, the ZBan-2 or other relevant laws which regulate the operations of a member, the Code of Ethics of Internal Auditors, and the Code of Internal Auditing Principles.

Compliance and Integrity performs the compliance function with respect to the main following areas: (a) prevention and development, including regulatory compliance, coordination and harmonisation of policies and practices within NLB Group, ethics and integrity; (b) supervision and internal investigations, including data and privacy data protection, and (c) anti-money laundering and anti-terrorist financing protocols. In close cooperation with different OUs, the Compliance and Integrity helps in assessing and managing compliance risks in different areas of operations in NLB Group. The main activities of the Compliance and Integrity Centre are:

- conducting compliance checks at various areas covered by the compliance audits, identification of shortcomings in this regard, suggestion of mitigation measures to be undertaken and monitoring of improvement;
- managing the system for reporting of suspected harmful practices (directing the system for reporting on violations through different channels) and conducting internal investigations of the reported cases;
- providing advisory services on compliance-related issues and regular analysis of compliance trends or observed problems and weaknesses in the Group;
- identifying and assessing compliance and integrity risks in the process of (new) product and services development;
- providing compliance communication, training, workshops and targeted surveys for employees;
- overseeing the regulatory compliance management system (monitoring, reporting and adopting changes required in NLB's legal environment);
- central management and monitoring of all communication with regulators and monitoring of the status of implementation of regulators' recommendations and measures; and
- managing the Compliance and Integrity Business Line for ensuring the same standards throughout NLB Group, with higher requirements for the core subsidiaries.

As regulatory risk is one of the top compliance risks, the Group has in place a regulatory compliance management system for handling and managing changes in the legal environment. This system is managed centrally by the compliance function, while implementation processes are decentralised. This means that OUs responsible for certain areas affected by a change in applicable regulations prepare action plans and lead implementation processes, thus ensuring NLB Group's compliance. The Compliance and Integrity function oversees the relevant regulatory changes' effects and the status of implementation. Focusing also on other compliance and integrity risks specific to the SEE region where NLB Group operates, specific policies and procedures are in place to identify and manage other types of compliance and integrity risks within NLB Group, where higher requirements are set for core subsidiaries.

As part of its approach to standards for conduct within NLB Group and building a risk culture within the NLB and NLB Group, NLB Group has in place a uniform NLB Group Code of Conduct which prohibits any breaches of internal acts (including risk procedures and policies). Dedicated reporting channels are established within NLB Group to ensure that any suspected violations or breaches are reported and dealt with to prevent damages to NLB Group members as well as prevent prohibited or harmful practices.

During the year 2017 there were no material changes in functions that presents the second and third line of defence of the internal control framework (Global Risk, Compliance and Internal Audit in NLB) neither such changes are planned. These functions are in accordance with the ZBan-2 independent functions and have direct access to NLB's Supervisory Board.

#### 4.2. The number of directorships held by members of the management body

(Articles 435.2 a of CRR)

Director	Number of directorships	External directorships as counted under Article 91(3) and 91(4) of Directive 2013/36/EU
Blaž Brodnjak	6	President of the Association of Banks in Slovenia
Andreas Burkhardt	4	None
Archibald Kremser	4	None
Laszlo Pelle	1	None

Details on functions, held by members of the management body are disclosed in the Annual Report for NLB Group 2017, chapter Corporate Governance (page 124).

#### 4.3. The recruitment policy for the selection of the management body and their actual knowledge, skills and expertise

(Articles 435.2 b of CRR)

According to the ZBan-2, the Supervisory Board sets the framework for the selection and appointment of suitable Management Board candidates. The framework is defined with the selection process policy, with the goal of the Management Board as a whole to possess the whole spectrum of relevant knowledge, skills, and experience required for the in-depth understanding of the Bank's activities and the risks to which it is exposed. The Management Board selection policy determines the professional standards of the selection process, as well as the professionally managed candidate selection, which gives the Supervisory Board a solid basis for their selection as well as fulfils their duty of care in line with the highest ethical standards and diligence in the selection process. This approach ensures that the Management Board consists of individuals with a different base of knowledge and experience, so that it will dispose of a balanced set of skills, relevant knowledge, and experience in regard to the Bank's size, complexity, and risk profile. Professionally led operations are not only in the best interest of the Bank, but also in the best interest of the selected candidates by deterring all possible doubts with regard to their expertise, references, and the appropriateness of their selection.

##### *NLB Group member's management*

Beside all legal and statutory set conditions, Management Board member candidates need to have adequate experience, skills, expertise, and competences, including their individual personal integrity and ability to dedicate adequate time to carry out their duties in view of possible other candidate's activities outside the Bank. By this the candidates are able to carry out their duties diligently, responsibly, effectively, as well as define and determine the values of the Bank and strategy of its operations in the way of following the objectives of its long-term success and coherent with the Bank's best interests and highest ethical standards of its management. Management Board candidates need to demonstrate the ability of constructively-critical cooperation when addressing the most important issues of the Bank with the objective of the continuous pursuit of the Bank's best interest, and with this the ability of active involvement in Bank's operations and its risk management. Management Board candidates must subordinate their personal interests, partial interest of third parties, as well as interests which could arise from the candidate's past functions or other activities, economic, professional, and private relationships (including the Management Board and Supervisory Board members), which could by any means influence decision-making in the Bank's best interest.

In case of any circumstances, which could lead to conflict of interest and consequently jeopardise the adopting of independent decisions in best interest of the Bank, such conflicts should be disclosed in the selection process, and a member should accept full responsibility to take timely measures to eliminate such conflicts of interest. During the Management Board member selection process the recommendation of both genders being appropriately represented is followed.

The selection of Management Board Members should strive for the Management Board as a whole to have all the necessary expertise, knowledge, skills, and experience at their disposal for successfully managing the Bank. Besides meeting all conditions for their work, Members of the Management Board need to act complementarily in line with the Bank's objectives, strategies, and policies in order to follow the Bank's best interest.

The Management Board comprises of 4 members; namely the Chairman of the Board (CEO) – who is also responsible for the Large Corporates area, Retail Banking and Private Banking; CRO; CFO; and COO –

who is besides the IT area, also responsible for the Procurement and CREM area, as well the Back Office area.

With regard to the wide range of relevant knowledge, skills, and experience from international environment, as well as a number of successfully completed projects, the Management Board as a whole has the appropriate expertise, skills, and experience to effectively and successfully lead the Bank. There are no foreseeable changes within overall composition of the management body.

**4.4. The policy on diversity with regard to selection of members of the management body, its objectives and any relevant targets set out in that policy, and the extent to which these objectives and targets have been achieved**  
(Article 435.2 c of CRR)

The Bank accepted the Policy of Supervisory Board diversity on 8 August 2016 and published it on its internet page. In 2017, there was no change or complement of it.

With the policy of assuring diversity of the Supervisory Board, based on Article 34 of ZBan-2, NLB sets the framework which enables the composition of the Supervisory Board in such a way that it, as a whole, possesses the relevant knowledge, skills, and experience that are required for the in-depth understanding of the Bank's operations and the risks to which it is exposed, as well as the realisation of the objectives of its strategy. The policy is focused on the selection of the Supervisory Board members, who primarily fulfil the requirements of the highest ethical and professional standards, exercise the highest level of diligence, as well as form the most competent governing body as a whole. Taking into account the policy, the Supervisory Board shall be composed in a way that it, as a whole, possesses the relevant knowledge, skills, and experience that are required with regard to the size, complexity, and risk profile of the Bank. Diversity of the Supervisory Board is recognised as one of the key business advantages of the Bank. According to the ZBan-2 and other grounds, as covered by the Policy, only a person who fulfils all set of the conditions for the Supervisory Board member in the Bank can be a member of the Supervisory Board.

Beside these qualifications, Supervisory Board Members need to possess adequate experience, skills, knowledge, and competences, including personal integrity and the possibility of dedication of sufficient time to perform the Supervisory Board member functions, regardless of their possible external activities. All listed requirements need to enable the Supervisory Board Members to monitor the Bank's operations diligently, responsibly and effectively with which, together with Management Board, the values and the strategy of the Bank are defined in the way they assure the Bank's long-term success, and are coherent with its best interests and the general ethical standards of the Bank's governance. Supervisory Board members need to demonstrate the ability of constructively-critical cooperation when addressing the most important issues of the Bank, with the objective of the continuous pursuit of the Bank's best interest, and with this the ability of active involvement in the monitoring of the Bank's management.

Supervisory Board members must subordinate their personal interests, partial interest of third parties, as well as interests which could arise from the candidate's past functions or other activities, and economic, professional and private relationships (including Management Board and Supervisory Board members), which could by any means influence their decisions in monitoring the Bank. In the composition of the Supervisory Board the recommendation of both genders being appropriately represented is followed.

The Supervisory Board annually assesses its structure, activities, potential conflict of interests of individual members, as well the operations of individual members, and the Supervisory Board as a whole. In addition, the efficiency and performance of the Supervisory Board's cooperation with the Management Board is assessed. If the Supervisory Board establishes that:

- the number of members is not appropriate,
- it is necessary to add an additional member,
- the members of the Supervisory Board are no longer qualified for performing the function due to non-compliance with the prescribed conditions,
- if due to inappropriateness of a single or more Supervisory Board member(s) in the aspect of duties of an individual member, the current structure does not assure the diversity of qualifications, knowledge, and experience for monitoring the Bank,

the Supervisory Board notifies Slovenian Sovereign Holding (SDH) – as the single Bank's shareholder – for a general shareholder's meeting to appoint new member(s).

The Supervisory Board is comprised of 8 members, of which there are two female members, and as a whole fulfils the objective of representation of both genders. The diversity of expertise, experience, and skills is ensured in the following areas: strategy and development, privatisation, finance, financial investments, investment banking, accounting and auditing, risk control and risk management, retail banking, corporate banking, banking and general legislation HRM.

## 5. Credit risk and general information on CRM

### 5.1. General qualitative information on credit risk

(Article 435.1 a, b, c, and d of CRR)

In addition to information disclosed in chapter 4.1 (General information on risk management, objectives and policies), specifics related to credit risk are disclosed below.

#### *Credit risk management strategies and policies*

Considering core business activities NLB Group will continue to pursue a continuous focus on clients with the aim to improve effectiveness of the sales force, intensified development of distribution channels and new solutions for clients. On the Slovenian market focus is on providing appropriate solutions for retail, medium-sized and small enterprises segments, while on the corporate segment the Group intends to reinforce the cooperation with selected corporate clients (through different types of lending or investment instruments). Furthermore, via the international desk functionality in all the Group's banking members, NLB Group will approach and service clients in a more structured and consistent way across the region. Nevertheless, even in such circumstances the Group is oriented towards appropriate credit portfolio diversification and collateral coverage in order to avoid large concentration. NLB Group carefully monitors its loan portfolio and new approved loans from different aspects, including their migration and default rate.

In recent years, NLB Group has focused on active NPL management and used the positive momentum of macroeconomic recovery in order to improve its portfolio quality. As part of the NPL Management Strategy, the NPL level was reduced from 19.3% in 2015 to 13.8% in 2016 and reached 9.2% at the end of 2017. The NPL Reduction Strategy follows the aim to reduce the existing NPL by using different measures and at the same time a conservative credit policy enables very low NPL formation from new business.

#### *Credit Risk appetite*

With the aim to maintain the medium-term and long-term sustainability of operations, NLB Group strives to maintain the adequate quality of the credit portfolio and increase the profitability based on a better ratio between the return and the assumed risks. While maintaining a balanced overall risk profile, NLB will foster the development of micro and small companies to support their evolution into a robust backbone of target markets' economies. NLB Group places great emphasis on monitoring the concentration risk (top concentration, industry, group of related persons) to avoid the exposure to excessive risk. More detailed guidelines concerning the credit portfolio's quality and its concentration are defined in the NLB Group Risk Strategy and NLB Group Risk profile, whereby the target values and limits are the subject of a regular, at least quarterly review.

#### *Credit risk management and mitigation*

In its operations, NLB Group is exposed to credit risk or the risk of losses due to the failure of a debtor to settle its liabilities to NLB Group. For that reason, it proactively and comprehensively monitors and assesses the aforementioned risk. In that process, NLB Group follows the International Financial Reporting Standards, regulations issued by the Bank of Slovenia, and the EBA guidelines. This area is governed in detail by the internal methodologies and procedures set out in internal acts.

Through regular reviews of the business practices and the credit portfolios of NLB Group members, NLB ensures that the credit risk management of those entities function in accordance with NLB Group's risk management standards in order to ensure meaningfully uniform procedures at the consolidated level.

NLB Group manages credit risk at two levels:

- At the level of the individual customer or group of customers, where appropriate procedures are followed in various phases of the relationship with a customer prior to, during, and after the conclusion of an agreement. Prior to concluding an agreement, a customer's performance, financial position, and past cooperation with NLB are assessed. The Group applies a cash-flow based credit policy that considers the repayment capacity of the client when approving or extending the loan or other credit exposure. It is also important to secure high-quality collateral that does not affect a customer's credit

rating. This is followed by various forms of monitoring a customer, in particular an assessment of its ability to generate sufficient cash flows for the regular settlement of its liabilities and contractual obligations. As regards to detection of risks, regular monitoring of clients within the Early Warning System (EWS) is important. For the purpose of objectively assessing a client's operation comprehensively, internal scoring models for particular client segments have been developed.

- The quality of the credit portfolio, including on-balance and off-balance sheet exposures, is actively monitored and analysed at the level of the overall portfolio of NLB Group and NLB. Comprehensive analyses are regularly performed in terms of client segmentation (depending on the client type and size), credit rating structure, volume of non-performing, past due and restructured loans, coverage with impairments and provisions, collateral received, concentrations arising from a group of related clients and concentrations within an industry, currency exposure, and other indicators of risks in the credit portfolio. A lot of attention is put on regular monitoring of new deals, vintage analysis and other changes or trends, with the emphasis on the early detection of increased risks and their optimisation in relation to profitability. NLB Group appropriately diversifies its portfolio to mitigate specific components of credit risk (i.e. the risk deriving from operations with a specific customer, sector, positions in financial instruments, or other specific events). Increasing emphasis is also placed on stress tests that forecast the effects of negative macroeconomic movements on the portfolio on the level of impairments and provisions, and on capital adequacy within the second pillar. Capital requirements for credit risk at NLB Group level within the Pillar 1 are calculated according to the standardised approach, while within the Pillar 2 as credit risk add-on and concentration risk assessment are carried out. From forward looking prospective also stress test results are taken into consideration within own estimation of Pillar 2 requirements.

The Group is constantly developing a wide range of advanced approaches, supported by mathematical and statistical models, in the area of credit risk assessment in line with best banking practises to further enhance existing risk management tools. In order to manage exposures with higher risk, the Group established several measures, including the introduction of an early warning system and a loan watch committee. The restructuring approaches built in the past are focused on early warning detection of clients with potential financial difficulties and their proactive resolving. These approaches encompass systematic usage of standardised tools for the timely restructuring of exposures. Moreover, the Group has taken an active approach to the management of non-performing exposures through the implementation of its NPL reduction strategy, under which the use of different alternative measures to reduce the Group's NPL level is planned. The realisation of NPL Strategy is subject of regular follow-up by the Management board and Supervisory board, including the implementation of mitigation measures necessary to fulfil internally set targets.

#### *Structure and organisation of the credit risk management and control function*

The credit risk management function in NLB is organised within the Risk (CRO), headed by the member of the Management Board responsible for risk area. The credit risk management function is performed by the Global Risk. The Global Risk is in functional and organisational terms separate from other functions where business decisions are adopted and where conflict of interest may arise with the risk management function. The head of the risk management function has direct access to the Management Board of the NLB and at the same time unhindered and independent access to the Supervisory Board.

The risk management function is organised in a way that the head of the risk management function obtains the information (and must be informed) by the directors of other OUs in the NLB and NLB Group members (primarily directors within risk area) about all major risks and circumstances that influence or could influence the specific development of risks and the risk profile of the NLB and NLB Group. The head of the risk management function thus ensures that all major risks in the NLB and NLB Group are identified and reported. In NLB Group members, the risk management function is organised according to the local legislation and Group's guidelines, as defined in "Risk Management Standards in NLB Group". The guidelines on risk management provide NLB Group members on the main principles, which they have to align their business policies, organisation, work procedures and reporting system.

#### *Credit process*

General principles of lending to non-financial clients in NLB Group are:

- NLB Group finances only clients that it knows (Know Your Client) and trusts, and only those acting according to ethical and moral values, conducting legal business and transparently disclosing their operations;
- NLB Group finances only clients with sufficient level of anticipated free cash flow, as the primary source of repayment. Furthermore credit approval is not based only on client's financial statements,

a comprehensive analysis are done by taking into account also client's industry specifics, future cash flow generation capability, the references and competences of owners and management bodies, critical judgement of future financial plans;

- The received collateral cannot influence on the client creditworthiness assessment. The accepted collateral represents a secondary source of repayment as a risk mitigation tool.
- In case of restructuring NLB Group primarily follows restructuring criteria and measures with aim to optimally resolve client's financial difficulties. Before restructuring, a detailed analysis is performed testing the client's viability to reach sustainable financial indebtedness in mid-term and the willingness to cooperate in the restructuring process. For Corporate clients different economic options are tested and the option that maximizes the NPV for the bank is selected.

More detailed principles and rules are defined in NLB Group's Lending policy and measures and procedures.

For materially important clients of NLB Group the credit ratings and the issuance of credit risk opinions are centralised via the Credit Committee of NLB. The process follows the co-decision principle, in which the credit committee of the respective group member first approves their decision, following which the Credit Committee of NLB gives their opinion. The resolution of the Credit Committee of NLB is made on the basis of all available documentation, including a non-binding rating opinion prepared by the underwriting department of NLB (Corporate and Retail Credit Analysis). This same principle and process is set also for the issuing of credit exposures for the materially important clients of NLB Group.

As part of credit granting process, the Validation and control function ensures that all contractual covenants are met, before the funds are actually transferred, including the minimum preconditions regarding collateral. By following strict procedures before credit transfer, the bank makes sure to have credit risk mitigation measures in place for the case of repayment problems.

#### *Restructuring and collection*

NLB Group banking members have in place an early warning system (EWS) for identifying increased credit risk and thus, in a systematic manner, identifying in the early stage the clients with high credit risk for inclusion in the watch list or for commencing the process of restructuring. An action plan is compiled for such clients and its implementation is regularly monitored with the aim of implementing the measures for the improvement of the client's financial position.

If the financial position of the clients deteriorates significantly special attention and treatment is required. In line with the relevant methodologies that regulate restructuring and legal collection area, clients must be transferred from the sales segments into special and separate units for managing non-performing loans, Restructuring or Work-out and legal support, while the sales units must focus only on the healthy part of the credit portfolio.

In the segment of restructuring NLB Group performs different measures in order to ensure financial and business restructuring of the clients, with the purpose to proactively prevent them becoming non-performing clients, while on the other side it performs different restructuring measures with already non-performing clients when the client's business model is assessed as viable. Focus is on a fast and active approach in order to start to resolve the client's financial difficulties in the early stages.

Clients suitable for the restructuring procedures are identified via the EWS on the basis of individual indicators - high risk criteria. Those clients whose business model is not assessed as viable, do not meet the criteria for restructuring and are transferred to the Work-out and Legal Support Unit. The decisions for restructuring or collection (liquidation) are based on the analysis (viability check), defined in the Group's relevant methodologies which regulate restructuring and work-out activities. Minimum activities for NLB Group members are set in the standards "Restructuring and non-performing loan management in NLB Group members".

All decisions on the restructuring of transactions must be consequently documented and must include a comparison of the proposed solution and alternative options (scenarios), which justifies NLB Group, with the help of the selected solution, ensure the highest net present value (minimise loss). In line with the EBA guidance, claims or clients retain the status of a non-performing loan for at least 12 months after they begin to regularly service their liabilities arising from the restructured claims.

Within the framework of NPE management, NLB Group uses a wide range of possible collection measures. The principal mission in the work-out area is to optimally resolve the collection of unpaid claims through (out of) court and by conducting litigation, which also requires constant professional and ethical communication with third parties. Other approaches to resolve NPL are liquidation of collateral, where the bank established a group of real-estate management specialists, to enable optimal recovery. Furthermore, individual or package sales of claims are performed and finally unpaid part of facilities are written-off based on Bank of Slovenia guidelines. The Group's goal is to achieve the maximum value of repayments and thus minimise the losses with the existing NPL portfolio.

NPL Management and Reduction Strategy on the level of NLB Group describes all above-mentioned NPL management and reduction measures and sets anticipated results of single measures and mid-term objectives in terms of NPL reduction. Targets defined in the NPL Strategy and yearly budget are regularly monitored and revised at least on yearly basis.

*Internal control assessment in credit risk function*

In 2017, Internal Audit performed several reviews in the area of credit risk management and mitigation. As the leading strengths, they identified an enhanced automatization of the credit process in the Retail and SME segment. Furthermore, as part of the audit reviews an intensified activity in scoring models' development, improved rating methodologies and improved loan collateral management were identified. Internal Audit also sees that NPL Strategy, regular monitoring of NPL and achievement of the mid-term goals as a major strength of credit risk management process.

Internal Audit also identified certain weaknesses that represent room for improvement of credit risk process. A changing and very complex regulatory environment was identified as one of major threats of existing system. Further, a deficiency in the IT support of the credit process was detected, which hinders the automatization of the credit process and its quality. Some deficiencies regarding the extensiveness of internal instruction were detected. However, modification activities are already underway. Internal Audit also sees difficulties in high regulatory expectations regarding NPL reduction and complex reporting to the regulator. All the identified flaws in the credit management process have to be addressed and mitigated by the corresponding OUs.

## 5.2. General quantitative information on credit risk (Article 442 c, 444 e and 453 f and g of CRR)

Table 14 – EU CRB-B – Total and average net amount of exposures of NLB Group

	2017		2016	
	Net value of exposures at the end of the period	Average net exposures over the period	Net value of exposures at the end of the period	Average net exposures over the period
Central governments or central banks	3,061,676	2,954,752	2,907,773	2,732,987
Regional governments or local authorities	110,016	113,289	117,800	125,227
Public sector entities	88,563	90,520	128,420	114,200
Multilateral development banks	69,399	58,259	41,318	41,458
International organisations	-	-	-	24,691
Institutions	1,318,979	1,329,830	1,333,779	1,265,941
Corporates	3,186,049	3,210,014	3,375,387	3,495,926
<i>Of which: SMEs</i>	1,088,190	1,116,165	1,234,526	1,319,185
Retail	4,201,708	4,066,568	3,852,314	3,737,900
<i>Of which: SMEs</i>	871,456	830,386	757,551	741,743
Secured by mortgages on immovable property	710,275	675,602	593,010	598,574
<i>Of which: SMEs</i>	114,004	105,404	81,040	86,125
Exposures in default	347,546	408,048	541,761	624,638
Items associated with particularly high risk	90,762	87,076	6,709	7,978
Covered bonds	89,191	65,188	50,418	51,519
Collective investments undertakings	45,662	45,383	44,570	44,587
Equity exposures	26,660	27,095	49,547	49,906
Other exposures	618,869	639,849	654,396	643,112
<b>Total standardised approach</b>	<b>13,965,353</b>	<b>13,771,474</b>	<b>13,697,202</b>	<b>13,558,644</b>
<b>Total</b>	<b>13,965,353</b>	<b>13,771,474</b>	<b>13,697,202</b>	<b>13,558,644</b>

The highest net exposure is reached in the segments of Retail, Corporate and Central government and central banks. The highest increase of net exposure compared to 31 December 2016 is shown in the retail segment due increased lending activities in all strategic markets in NLB Group and in the Central government segment. The highest decrease is shown in the exposures in default due to an ambitious NPL Reduction Strategy.

## 5.3. Geographical breakdown of exposures (Article 442 d of CRR)

Table 15 – EU CRB-C – Geographical breakdown of exposures of NLB Group

31.12.2017	Slovenia	Macedonia	Bosnia and Herzegovina	Kosovo	Montenegro	Serbia	Other countries	Total
Central governments or central banks	1,347,553	257,132	299,785	131,854	139,026	97,168	789,158	3,061,676
Regional governments or local authorities	74,134	4,519	25,954	-	5,381	26	2	110,016
Public sector entities	18,208	22,345	28,717	171	2,486	3,326	13,310	88,563
Multilateral development banks	-	-	-	-	-	-	69,399	69,399
Institutions	23,214	10,286	8,006	1,226	26	6,091	1,270,130	1,318,979
Corporates	2,252,234	311,987	225,952	175,197	37,640	56,767	126,273	3,186,049
Retail	2,348,100	626,896	495,537	272,792	221,872	231,967	4,544	4,201,708
Secured by mortgages on immovable property	709,255	-	-	-	-	-	1,020	710,275
Exposures in default	204,730	12,022	16,569	3,159	61,039	38,621	11,407	347,546
Items associated with particularly high risk	26,386	7,034	11,165	10,637	12,737	3,755	19,047	90,762
Covered bonds	-	-	-	-	-	-	89,191	89,191
Collective investments undertakings	45,662	-	-	-	-	-	-	45,662
Equity exposures	16,380	2,679	69	-	10	-	7,522	26,660
Other exposures	290,475	85,824	64,296	28,751	65,554	55,922	28,046	618,869
<b>Total standardised approach</b>	<b>7,356,329</b>	<b>1,340,724</b>	<b>1,176,049</b>	<b>623,786</b>	<b>545,771</b>	<b>493,644</b>	<b>2,429,049</b>	<b>13,965,353</b>
<b>Total</b>	<b>7,356,329</b>	<b>1,340,724</b>	<b>1,176,049</b>	<b>623,786</b>	<b>545,771</b>	<b>493,644</b>	<b>2,429,049</b>	<b>13,965,353</b>

31.12.2016	Slovenia	Macedonia	Bosnia and Herzegovina	Kosovo	Montenegro	Serbia	Other countries	Total
Central governments or central banks	1,472,913	238,003	278,921	107,895	137,876	83,179	588,987	2,907,773
Regional governments or local authorities	73,911	5,664	31,543	-	6,621	8	52	117,800
Public sector entities	68,008	21,619	30,523	1,264	353	1,234	5,419	128,420
Multilateral development banks	-	-	-	-	-	-	41,318	41,318
Institutions	58,422	10,732	6,033	817	22	6,011	1,251,743	1,333,779
Corporates	2,500,370	305,444	203,637	170,211	50,750	45,018	99,957	3,375,387
Retail	2,233,464	573,485	454,099	230,151	196,986	160,163	3,965	3,852,314
Secured by mortgages on immovable property	590,089	-	-	-	-	-	2,921	593,010
Exposures in default	285,597	11,015	43,219	1,083	86,424	59,395	55,027	541,761
Items associated with particularly high risk	3,282	3,014	21	-	374	4	14	6,709
Covered bonds	-	-	-	-	-	-	50,418	50,418
Collective investments undertakings	44,570	-	-	-	-	-	-	44,570
Equity exposures	39,625	2,660	349	-	10	-	6,904	49,547
Other exposures	301,842	86,590	63,846	31,244	87,547	55,922	27,406	654,396
<b>Total standardised approach</b>	<b>7,672,094</b>	<b>1,258,225</b>	<b>1,112,191</b>	<b>542,665</b>	<b>566,963</b>	<b>410,934</b>	<b>2,134,130</b>	<b>13,697,202</b>
<b>Total</b>	<b>7,672,094</b>	<b>1,258,225</b>	<b>1,112,191</b>	<b>542,665</b>	<b>566,963</b>	<b>410,934</b>	<b>2,134,130</b>	<b>13,697,202</b>

The table shows net exposures by country. The materiality threshold was determined in such a way, that all countries where NLB Group has banking subsidiaries are included. In this display, exposures to 'Other countries' have thresholds below 3.5%, of which Germany 3.3% and the rest of countries below 2%. The net exposure at the end of 2017 in Slovenia represents 53% of total, followed by Macedonia (10%), Bosnia and Herzegovina (8%) and Kosovo, Montenegro and Serbia (4%). Other countries mostly include different EU member states, where a bulk of exposure is on Central government and Institutions for liquidity management purposes.

Compared to end of 2016, the net exposure in Slovenia decreased mainly on the Corporate segment, exposure to Public sector (including Central governments or central banks) and exposure in default, whereas exposure to Retail (including exposures Secured by mortgages on immovable property) increased. NLB as a parent bank maintained its leading position in the Retail segment in Slovenia with a market share of 23.4%. In other markets of NLB Group net exposures increased mainly due to increased lending activity in Retail and Central governments or central banks.

## 5.4. Concentration of exposures by industry or counterparty types (Article 442 e of CRR)

Table 16 – EU CRB-D – Concentration of exposures by industry or counterparty types of NLB Group

	Agriculture, forestry and fishing	Mining and quarrying	Manufacturing	Electricity, gas, steam and air conditioning supply	Water supply	Construction	Wholesale and retail trade	Transport and storage	Accommodation and food service activities	Information and communication	Real estate activities	Professional, scientific and technical activities	Administrative and support service activities	Public administration and defence, compulsory social security	Education	Human Health services and social work activities	Arts, entertainment and recreation	Other services	Total
<b>31.12.2017</b>																			
Central governments or central banks	-	-	97	-	-	-	-	-	-	-	-	-	-	-	-	-	-	3,061,579	3,061,676
Regional governments or local authorities	-	-	-	-	-	-	-	-	-	3	25	-	14	109,973	0	-	-	0	110,016
Public sector entities	176	-	4,589	4,352	2,414	47	31	4,765	2,279	4,474	4	1,575	40	30,543	8,496	993	2,095	21,691	88,563
Multilateral development banks	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	69,399	69,399
Institutions	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,318,979	1,318,979
Corporates	28,441	13,354	806,230	186,685	31,195	213,555	542,454	622,008	39,747	190,645	48,647	110,004	170,040	-	3,838	12,625	25,488	141,095	3,186,049
Retail	64,895	3,450	171,902	6,921	5,608	98,591	260,113	84,511	24,400	16,375	12,081	37,763	27,783	612	2,584	11,349	7,677	3,365,093	4,201,708
Secured by mortgages on immovable property	1,191	58	72,658	48	4,376	4,777	34,512	20,380	11,499	3,048	4,444	18,101	3,818	391	530	1,809	1,156	527,480	710,275
Exposures in default	4,609	2,698	27,827	8,077	906	52,676	111,319	10,711	26,764	4,848	32,336	8,933	1,584	39	59	3,973	3,291	46,896	347,546
Items associated with particularly high risk	36	0	246	7,791	3	55,910	880	344	214	111	19,527	5,200	7	-	10	35	2	444	90,762
Covered bonds	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	89,191	89,191
Collective investments undertakings	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	45,662	45,662
Equity exposures	-	-	10	28	-	-	-	480	3,056	6,847	-	-	-	-	-	-	-	16,239	26,660
Other exposures	68	-	27,132	17	110	5,132	472	352	20	692	38,296	433	40	6	40	-	72	545,984	618,869
<b>Total standardised approach</b>	<b>99,416</b>	<b>19,561</b>	<b>1,110,691</b>	<b>213,918</b>	<b>44,612</b>	<b>430,688</b>	<b>949,781</b>	<b>743,551</b>	<b>107,979</b>	<b>227,043</b>	<b>155,360</b>	<b>182,009</b>	<b>203,327</b>	<b>141,564</b>	<b>15,557</b>	<b>30,783</b>	<b>39,780</b>	<b>9,249,730</b>	<b>13,965,353</b>
<b>Total</b>	<b>99,416</b>	<b>19,561</b>	<b>1,110,691</b>	<b>213,918</b>	<b>44,612</b>	<b>430,688</b>	<b>949,781</b>	<b>743,551</b>	<b>107,979</b>	<b>227,043</b>	<b>155,360</b>	<b>182,009</b>	<b>203,327</b>	<b>141,564</b>	<b>15,557</b>	<b>30,783</b>	<b>39,780</b>	<b>9,249,730</b>	<b>13,965,353</b>
<b>31.12.2016</b>																			
Central governments or central banks	-	-	-	-	-	-	-	-	14	-	-	-	-	-	-	-	-	2,907,759	2,907,773
Regional governments or local authorities	-	-	-	-	1	-	-	-	-	3	-	-	40	117,755	-	0	0	0	117,800
Public sector entities	534	-	4,400	6,199	3,287	7	27	6,043	30	2,684	4	1,149	10	29,549	10,228	1,881	2,194	60,194	128,420
Multilateral development banks	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	41,318	41,318
Institutions	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	1,333,779	1,333,779
Corporates	21,312	29,514	740,109	211,373	23,174	195,888	523,429	642,725	35,013	192,744	52,007	156,963	385,766	-	3,140	13,086	30,590	118,553	3,375,387
Retail	35,154	2,894	159,319	7,296	5,632	83,050	230,952	72,247	17,900	14,450	12,481	35,615	25,581	899	2,400	9,063	7,842	3,129,540	3,852,314
Secured by mortgages on immovable property	1,306	806	45,352	60	4,341	6,706	28,783	19,017	9,095	4,952	3,012	10,543	1,026	564	770	1,937	223	454,516	593,010
Exposures in default	7,500	4,368	62,882	9,451	1,465	104,614	166,005	15,572	32,745	2,400	51,338	23,135	2,330	649	89	3,085	3,713	50,420	541,761
Items associated with particularly high risk	171	0	577	9	4	340	2,174	214	189	489	6	1,838	11	0	11	7	3	665	6,709
Covered bonds	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	50,418	50,418
Collective investments undertakings	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	44,570	44,570
Equity exposures	-	-	75	225	-	-	20,534	283	3,330	8,727	-	-	-	-	-	-	-	16,373	49,547
Other exposures	-	-	32,551	17	0	6	1,746	475	16	1,019	63,896	594	47	58	34	-	97	553,840	654,396
<b>Total standardised approach</b>	<b>65,976</b>	<b>37,582</b>	<b>1,045,266</b>	<b>234,629</b>	<b>37,904</b>	<b>390,610</b>	<b>973,652</b>	<b>756,577</b>	<b>98,334</b>	<b>227,467</b>	<b>182,743</b>	<b>229,836</b>	<b>414,813</b>	<b>149,474</b>	<b>16,672</b>	<b>29,058</b>	<b>44,663</b>	<b>8,761,946</b>	<b>13,697,202</b>
<b>Total</b>	<b>65,976</b>	<b>37,582</b>	<b>1,045,266</b>	<b>234,629</b>	<b>37,904</b>	<b>390,610</b>	<b>973,652</b>	<b>756,577</b>	<b>98,334</b>	<b>227,467</b>	<b>182,743</b>	<b>229,836</b>	<b>414,813</b>	<b>149,474</b>	<b>16,672</b>	<b>29,058</b>	<b>44,663</b>	<b>8,761,946</b>	<b>13,697,202</b>

The prevailing industries at the end of 2017 are Manufacturing, Wholesale and the Retail trade. Other services include segments that cannot be attributed to an industry for example Central government, Institutions and Retail. The highest increase in net exposure was noticed in the Manufacturing and Construction sector as a result of new financing, while the largest decrease is noticed in Administrative and support service activities due to loan repayment.

## 5.5. Maturity of exposures (Article 442 f of CRR)

Table 17 – EU CRB-E – Maturity of exposures of NLB Group

31.12.2017	Net exposure value				Total
	On demand	Up to1 year	1 year to 5 years	Over 5 years	
Central governments or central banks	798,757	583,392	898,744	779,252	3,060,144
Regional governments or local authorities	-	156	26,234	82,805	109,195
Public sector entities	-	12,150	17,685	44,973	74,807
Multilateral development banks	-	6,512	30,048	32,839	69,399
Institutions	188,025	808,797	234,527	34,237	1,265,587
Corporates	36,460	821,502	1,043,622	336,567	2,238,151
Retail	-	1,114,953	1,505,384	790,520	3,410,857
Secured by mortgages on immovable property	-	146,658	161,593	388,883	697,134
Exposures in default	-	74,092	149,019	73,889	297,000
Items associated with particularly high risk	-	29,822	27,880	11,990	69,692
Covered bonds	-	1,552	31,993	55,646	89,191
Collective investments undertakings	-	36	-	45,626	45,662
Equity exposures	-	6,684	-	21,364	28,048
Other exposures	269,697	15,658	63,031	271,571	619,957
<b>Total standardised approach</b>	<b>1,292,939</b>	<b>3,621,963</b>	<b>4,189,759</b>	<b>2,970,161</b>	<b>12,074,822</b>
<b>Total</b>	<b>1,292,939</b>	<b>3,621,963</b>	<b>4,189,759</b>	<b>5,052,834</b>	<b>12,074,822</b>

At the end of 2017, 34.6% of net on-balance exposure has remaining maturity 1 year to 5 years, followed by the Up to 1 year category with 30% and Over 5 years with 24.7%. In the last year the highest increase was noticed in the Over 5 year's category and the highest decrease was noticed in the Up to 1 year category.

31.12.2016	Net exposure value				Total
	On demand	Up to1 year	1 year to 5 years	Over 5 years	
Central governments or central banks	776,649	666,532	910,559	560,133	2,913,873
Regional governments or local authorities	-	656	23,037	92,917	116,610
Public sector entities	-	54,331	22,050	42,214	118,595
Multilateral development banks	-	3,822	26,258	11,238	41,318
Institutions	262,028	747,903	236,936	52,398	1,299,266
Corporates	19,655	999,759	1,099,696	292,463	2,411,572
Retail	-	1,079,789	1,297,257	744,524	3,121,571
Secured by mortgages on immovable property	-	131,444	127,652	320,669	579,765
Exposures in default	-	158,457	153,576	138,074	450,107
Items associated with particularly high risk	-	2,082	3,385	366	5,834
Covered bonds	-	21,639	28,779	-	50,418
Collective investments undertakings	-	-	-	44,570	44,570
Equity exposures	-	5,129	-	44,418	49,547
Other exposures	260,611	21,207	67,387	305,179	654,384
<b>Total standardised approach</b>	<b>1,318,943</b>	<b>3,892,752</b>	<b>3,996,572</b>	<b>2,649,163</b>	<b>11,857,430</b>
<b>Total</b>	<b>1,318,943</b>	<b>3,892,752</b>	<b>3,996,572</b>	<b>5,052,834</b>	<b>11,857,430</b>

## 5.6. Credit quality of exposures by exposure class and instrument types (Article 442 g and h of CRR)

Table 18 – EU CR1-A – Credit quality of exposures by exposure class and instrument types of NLB Group

	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges of the period	Net values
	Defaulted exposures	Non-defaulted exposures					
<b>31.12.2017</b>							
16 Central governments or central banks	-	3,061,690	-	14	130	12	3,061,676
17 Regional governments or local authorities	-	113,326	-	3,310	-	(5,965)	110,016
18 Public sector entities	-	92,265	-	3,702	1	(2,220)	88,563
19 Multilateral development banks	-	69,399	-	-	-	-	69,399
21 Institutions	-	1,319,943	-	964	1	(360)	1,318,979
22 Corporates	-	3,251,092	-	65,044	40	(6,296)	3,186,049
23 <i>Of which: SMEs</i>	-	1,116,840	-	28,650	-	(12,449)	1,088,190
24 Retail	-	4,254,231	-	52,523	186	(22,484)	4,201,708
25 <i>Of which: SMEs</i>	-	893,598	-	22,142	177	(9,960)	871,456
Secured by mortgages on immovable property							
26	-	716,083	-	5,808	-	(2,745)	710,275
27 <i>Of which: SMEs</i>	-	116,806	-	2,802	-	(1,302)	114,004
28 Exposures in default	850,290	-	502,744	-	231,878	(3,088)	347,546
29 Items associated with particularly high risk	89,120	69,075	64,353	3,081	27,702	(324)	90,762
30 Covered bonds	-	89,191	-	-	-	-	89,191
32 Collective investments undertakings	-	45,662	-	1	-	-	45,662
33 Equity exposures	3,602	23,058	-	-	-	-	26,660
34 Other exposures	5,993	615,501	50	2,576	612	-	618,869
35 <b>Total standardised approach</b>	<b>949,005</b>	<b>13,720,516</b>	<b>567,147</b>	<b>137,020</b>	<b>260,551</b>	<b>(43,470)</b>	<b>13,965,353</b>
36 <b>Total</b>	<b>949,005</b>	<b>13,720,516</b>	<b>567,147</b>	<b>137,020</b>	<b>260,551</b>	<b>(43,470)</b>	<b>13,965,353</b>
37 <i>Of which: Loans</i>	854,832	8,286,217	533,180	133,201	260,551	(40,001)	8,474,669
38 <i>Of which: Debt securities</i>	798	2,900,286	798	73	-	(10)	2,900,213
39 <i>Of which: Off- balance-sheet exposures</i>	83,715	1,843,731	33,170	3,746	-	(3,459)	1,890,531

	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges of the period	Net values
	Defaulted exposures	Non-defaulted exposures					
<b>31.12.2016</b>							
16 Central governments or central banks	-	2,907,905	-	132	11	(3)	2,907,773
17 Regional governments or local authorities	-	126,957	-	9,158	-	(1,793)	117,800
18 Public sector entities	-	134,276	-	5,855	-	(719)	128,420
19 Multilateral development banks	-	41,318	-	-	-	-	41,318
21 Institutions	-	1,334,516	-	737	21	14	1,333,779
22 Corporates	-	3,453,647	-	78,260	19	(13,677)	3,375,387
23 <i>Of which: SMEs</i>	-	1,269,884	-	35,358	-	(7,268)	1,234,526
24 Retail	-	3,905,429	-	53,115	154	(10,414)	3,852,314
25 <i>Of which: SMEs</i>	-	781,360	-	23,809	132	(4,472)	757,551
Secured by mortgages on immovable property							
26	-	598,932	-	5,922	-	(1,969)	593,010
27 <i>Of which: SMEs</i>	-	83,709	-	2,668	-	(479)	81,040
28 Exposures in default	1,443,527	-	901,767	-	460,441	62,168	541,761
29 Items associated with particularly high risk	-	7,129	-	420	15	-	6,709
30 Covered bonds	-	50,418	-	-	-	-	50,418
32 Collective investments undertakings	-	44,570	-	-	-	-	44,570
33 Equity exposures	3,738	45,809	-	-	147	-	49,547
34 Other exposures	6,776	652,805	2,644	2,542	2,365	-	654,396
35 <b>Total standardised approach</b>	<b>1,454,042</b>	<b>13,303,712</b>	<b>904,411</b>	<b>156,142</b>	<b>463,173</b>	<b>33,608</b>	<b>13,697,202</b>
36 <b>Total</b>	<b>1,454,042</b>	<b>13,303,712</b>	<b>904,411</b>	<b>156,142</b>	<b>463,173</b>	<b>33,608</b>	<b>13,697,202</b>
37 <i>Of which: Loans</i>	1,316,370	8,142,392	864,163	152,870	463,173	43,957	8,441,729
38 <i>Of which: Debt securities</i>	798	2,674,609	798	83	-	83	2,674,526
39 <i>Of which: Off- balance-sheet exposures</i>	130,870	1,751,232	39,217	3,114	-	(10,432)	1,839,771

In 2017, gross exposure decreased by EUR 505 million, which was primarily driven by a considerable decrease in default exposure segment (by EUR 593 million). The increase in the high-risk exposure segment is a result of new interpretation of the segment encouraged by ECB supervisory review. Decrease in gross defaulted exposures was partially compensated by additional non-default exposures, primarily in the Retail segment. The decrease of default exposures was achieved mostly due to measures of defaulted exposure management. The volume of specific risk adjustment was reduced by EUR 337 million, mostly due to default exposure reduction.

Table 19 – EU CR1-B – Credit quality of exposures by industry or counterparty types of NLB Group

31.12.2017	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges	Net values
	Defaulted exposures	Non-defaulted exposures					
Agriculture, forestry and fishing	11,273	97,619	6,596	2,880	801	(579)	99,416
Mining and quarrying	4,361	17,281	1,663	418	1	(4,475)	19,561
Manufacturing	83,166	1,111,907	55,208	29,174	55,451	(20,131)	1,110,691
Electricity, gas, steam and air conditioning supply	12,534	209,960	4,429	4,147	1,336	(2,692)	213,918
Water supply	1,233	44,381	217	785	2,157	313	44,612
Construction	162,089	370,532	92,724	9,209	50,648	2,947	430,688
Wholesale and retail trade	305,606	865,027	194,047	26,805	71,781	5,327	949,781
Transport and storage	36,144	736,394	24,952	4,035	2,440	(3,416)	743,551
Accommodation and food service activities	34,737	81,096	4,917	2,937	7,419	(3,064)	107,980
Information and communication	7,833	226,906	2,907	4,788	197	(1,009)	227,043
Real estate activities	100,012	112,414	54,473	2,593	7,682	167	155,360
Professional, scientific and technical activities	34,563	176,734	25,628	3,659	8,389	(4,083)	182,009
Administrative and support service activities	4,885	203,187	3,270	1,475	11,956	(4,928)	203,327
Public administration and defence, compulsory social security	2,384	145,769	2,345	4,244	376	(6,311)	141,564
Education	456	15,986	398	488	7	175	15,557
Human health services and social work activities	6,643	27,839	2,671	1,028	2,212	2,832	30,783
Arts, entertainment and recreation	8,169	38,448	4,870	1,967	45	(657)	39,780
Other services	132,914	9,239,037	85,832	36,388	37,655	(3,885)	9,249,730
<b>Total</b>	<b>949,005</b>	<b>13,720,516</b>	<b>567,147</b>	<b>137,020</b>	<b>260,552</b>	<b>(43,470)</b>	<b>13,965,353</b>

31.12.2016	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges	Net values
	Defaulted exposures	Non-defaulted exposures					
Agriculture, forestry and fishing	19,242	60,895	11,743	2,418	3,201	(4,297)	65,976
Mining and quarrying	9,164	35,369	4,796	2,155	228	(524)	37,582
Manufacturing	230,322	1,010,234	166,683	28,607	102,471	(6,736)	1,045,266
Electricity, gas, steam and air conditioning supply	17,401	230,466	7,926	5,312	14,479	(950)	234,629
Water supply	9,226	37,258	7,761	819	1,620	2,150	37,904
Construction	233,843	293,684	129,228	7,687	61,864	7,286	390,610
Wholesale and retail trade	437,303	835,587	269,859	29,379	98,537	19,652	973,652
Transport and storage	47,985	745,133	31,666	4,876	8,020	(133)	756,577
Accommodation and food service activities	51,222	66,274	15,146	4,016	21,584	1,926	98,334
Information and communication	5,919	231,092	3,519	6,025	10,774	2,605	227,467
Real estate activities	134,366	134,809	83,028	3,403	28,061	7,102	182,743
Professional, scientific and technical activities	62,837	210,705	39,469	4,237	17,168	(2,343)	229,836
Administrative and support service activities	9,805	415,150	7,443	2,699	10,115	2,646	414,813
Public administration and defence, compulsory social security	3,126	158,945	2,477	10,120	163	(2,203)	149,474
Education	528	16,897	439	314	910	454	16,672
Human health services and social work activities	6,715	27,293	3,630	1,320	169	(1,123)	29,058
Arts, entertainment and recreation	8,906	43,148	5,168	2,223	2,058	795	44,663
Other services	166,131	8,750,775	114,428	40,532	81,752	7,302	8,761,946
<b>Total</b>	<b>1,454,042</b>	<b>13,303,712</b>	<b>904,411</b>	<b>156,142</b>	<b>463,174</b>	<b>33,608</b>	<b>13,697,202</b>

Manufacturing and Wholesale and the Retail trade remain the strongest industries at the end of 2017, each representing around 8% of total gross exposure, even though both industries saw the highest reduction of default exposure in 2017. Non-defaulted exposures increased most in the Wholesale and Retail trade segments and in the Construction industry. Other services represent all client segments that are not considered non-financial corporations (including Central government, Retail and Institutions).

Table 20 – EU CR1-C – Credit quality of exposures by geography of NLB Group

31.12.2017	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges	Net values
	Defaulted exposures	Non-defaulted exposures					
Slovenia	402,555	7,199,546	194,806	50,966	27,964	(6,646)	7,356,329
Macedonia	56,421	1,368,554	44,171	40,080	8,981	(3,977)	1,340,724
Bosnia and Herzegovina	94,580	1,178,566	76,849	20,248	87,111	(26,156)	1,176,049
Kosovo	16,741	635,799	13,551	15,203	2,763	1,971	623,786
Montenegro	162,312	482,279	93,190	5,630	21,583	1,816	545,771
Serbia	101,859	456,831	60,924	4,122	25,112	10	493,644
Other countries	114,537	2,398,940	83,656	772	87,037	(10,488)	2,429,049
<b>Total</b>	<b>949,005</b>	<b>13,720,516</b>	<b>567,147</b>	<b>137,020</b>	<b>260,552</b>	<b>(43,470)</b>	<b>13,965,353</b>

31.12.2016	Gross carrying values of		Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs	Credit risk adjustment charges	Net values
	Defaulted exposures	Non-defaulted exposures					
Slovenia	520,180	7,441,345	233,165	56,267	221,433	13,058	7,672,094
Macedonia	64,169	1,290,996	52,536	44,403	36,421	4,770	1,258,225
Bosnia and Herzegovina	226,349	1,098,863	182,345	30,676	10,733	7,474	1,112,191
Kosovo	17,132	554,667	16,018	13,117	2	3,078	542,665
Montenegro	200,030	486,166	113,600	5,632	27,063	4,166	566,963
Serbia	170,139	354,350	109,124	4,431	61,209	2,249	410,934
Other countries	256,043	2,077,325	197,622	1,615	106,313	(1,186)	2,134,130
<b>Total</b>	<b>1,454,042</b>	<b>13,303,712</b>	<b>904,411</b>	<b>156,142</b>	<b>463,174</b>	<b>33,608</b>	<b>13,697,202</b>

Slovenia is the biggest market for NLB Group with 52% of gross exposure at the end of 2017, followed by Macedonia (10%), Bosnia and Herzegovina (9%) and other countries where the Group's banking subsidiaries are established. Nevertheless, the growth of gross exposure in countries where banking subsidiaries are established exceeds the growth in Slovenia, where default as well as non-default gross exposures decreased in 2017. The increase of non-default exposures was the highest in 'Other countries', however this also includes exposures to Central governments and Institutions as part of liquidity management.

Table 21 – EU CR1-D – Ageing of past-due exposures of NLB Group

31.12.2017	Gross carrying values					
	Up to 30 days	30 days to 60 days	60 days to 90 days	90 days to 180 days	180 days to 1 year	Over 1 year
Loans	673,913	67,103	31,682	23,409	38,188	433,883
Debt securities	-	-	-	-	-	-
<b>Total exposures</b>	<b>673,913</b>	<b>67,103</b>	<b>31,682</b>	<b>23,409</b>	<b>38,188</b>	<b>433,883</b>

31.12.2016	Gross carrying values					
	Up to 30 days	30 days to 60 days	60 days to 90 days	90 days to 180 days	180 days to 1 year	Over 1 year
Loans	740,830	69,576	39,418	19,314	83,815	670,007
Debt securities	-	-	-	-	-	-
<b>Total exposures</b>	<b>740,830</b>	<b>69,576</b>	<b>39,418</b>	<b>19,314</b>	<b>83,815</b>	<b>670,007</b>

The value of exposure in delays decreased in 2017 by EUR 355 million (or 22%), which is to be attributed to Default exposure decrease. At the end of 2017, past-due exposures represent 8.6% of the total gross exposure.

### 5.7. Non-performing and forbore exposures (Article 442 a, b and i of CRR)

The bank uses a unified definition of past due and default exposures that is aligned with Article 178 of CRR. Defaulted clients are rated D, DF or E based on the Bank's internal rating system and contain clients with material delays over 90 days, as well as clients that were assessed as unlikely to pay. The retail clients are rated on the facility level, however the rating can be deteriorated based on the rating of other credit facilities of the same client.

The Bank has objective credit rating classification methodology that classifies all past-due exposures to D, DF or E credit rating. Based on that assessment of (individual or collective) impairments and provisions is performed.

The Bank prepares individual impairments for all defaulted exposures exceeding the materiality threshold, while clients with lower exposure obtain collective impairments and provisions. These are based on 100% PD and LGDs applicable based on available collateral and expected repayments from other sources.

A forbore loan (or restructured financial asset) is a financial asset in relation to which forbearance has been introduced. The most frequent forbearance measures in NLB Group are, but not limited to:

- extension or forbearance on asset repayment,
- lower interest rates and/or other fees,
- lower amount of receivables resulting from a contractually agreed debt waiver and ownership restructuring,

- debt to equity swap,
- takeover of other assets (including collateral liquidation) for a full or partial repayment.

Table 22 – EU CR1-E – Non-performing and forborne exposures of NLB Group

	Gross carrying values of performing and non-performing exposures							Accumulated impairment and provisions and negative fair value adjustments due to credit risk				Collaterals and financial guarantees received	
	Total	Of which performing but past due 30 to 90 days		Of which non-performing			On performing exposures		performing exposures		On non-performing exposures	Of which forborne exposures	
		Of which performing forborne	Total	Of which defaulted	Of which impaired	Of which forborne	Total	Of which forborne	Of which forborne				
<b>31.12.2017</b>													
Debt securities	2,916,127	-	-	798	798	798	-	73	-	798	-	-	
Loans and advances	9,141,690	79,671	78,129	855,447	885,447	885,447	534,202	133,201	9,204	533,180	323,263	279,886	
Off-balance-sheet exposures	1,927,446	5,663	1,128	83,715	83,715	83,715	9,510	3,746	-	33,170	-	13,059	
												3,421	

	Gross carrying values of performing and non-performing exposures							Accumulated impairment and provisions and negative fair value adjustments due to credit risk				Collaterals and financial guarantees received	
	Total	Of which performing but past due 30 to 90 days		Of which non-performing			On performing exposures		performing exposures		On non-performing exposures	Of which forborne exposures	
		Of which performing forborne	Total	Of which defaulted	Of which impaired	Of which forborne	Total	Of which forborne	Of which forborne				
<b>31.12.2016</b>													
Debt securities	2,693,229	-	-	798	798	798	-	83	-	798	-	-	
Loans and advances	9,460,204	54,448	114,896	1,317,802	1,317,802	1,317,802	836,638	152,870	16,398	864,163	520,699	394,819	
Off-balance-sheet exposures	1,882,102	3,889	1,151	130,240	130,240	130,240	22,485	3,114	-	39,217	-	15,399	

Table 23 – EU CR2-A – Changes in the stock of general and specific credit risk adjustments of NLB Group

	31.12.2017		31.12.2016	
	Accumulated specific credit risk	Accumulated general credit risk	Accumulated specific credit risk	Accumulated general credit risk
<b>1 Opening balance</b>	(864,961)	(152,953)	(1,246,117)	(174,141)
Increases due to amounts set aside for estimated loan				
<b>2 losses during the period</b>	(74,065)	(84,429)	(253,316)	(170,943)
Decreases due to amounts reversed for estimated				
<b>3 loan losses during the period</b>	75,163	123,342	209,396	170,820
Decreases due to amounts taken against				
<b>4 accumulated credit risk adjustments</b>	256,622	3,930	460,730	2,444
<b>5 Transfers between credit risk adjustments</b>	(21,005)	21,005	(30,835)	30,835
<b>8 Other adjustments</b>	94,268	(44,169)	(4,819)	(11,968)
<b>9 Closing balance</b>	(533,978)	(133,274)	(864,961)	(152,953)
Recoveries on credit risk adjustments recorded				
<b>10 directly to the statement of profit or loss</b>	19,621	-	17,581	-
Specific credit risk adjustments directly recorded to				
<b>11 the statement of profit or loss</b>	-	-	-	-

In 2017 the Group released net impairments, which was the result of some successful collections, resolution of non-performing receivables, and improvement in the quality of the credit portfolio's structure. Positive trends in the economic environment, and consequently a lower transition of performing customers into default in years 2016 and 2015 contributed positively to lower percentages of PD's, and consequently to lower general credit risk in 2017 – mainly in the segment of corporate clients. The effect of the release of the impairments for general credit risk in the segment of corporate clients amounts to approximately EUR 21 million. In contrast, in 2016 additional impairments related to the non-performing portfolio sale in the amount of EUR 25.8 million were formed, reflected in increase of impairments for specific credit risk. Accordingly, the net cost of risk decreased from 38 basis points in year 2016 to -62 basis points in year 2017.

Table 24 – EU CR2-B – Changes in the stock of defaulted and impaired loans and debt securities of NLB Group

	31.12.2017	31.12.2016
	Gross carrying value defaulted exposures	Gross carrying value defaulted exposures
<b>Opening balance</b>	<b>1,317,167</b>	<b>1,850,816</b>
Loans and debt securities that have defaulted or impaired since the last reporting period	60,566	133,495
Returned to non-defaulted status	(63,849)	(75,605)
Amounts written off	(260,552)	(463,174)
Other changes	(197,702)	(128,364)
<b>Closing balance</b>	<b>855,630</b>	<b>1,317,167</b>

In 2017 based on the NPL Strategy, there was a material decrease of default exposures that amounted to EUR 462 million or 35% of the initial default exposure volume. The measures that led to such increase were repayments, sale of portfolio, sale of individual facilities, liquidation of collateral and write-offs (final and those to off-balance based on the Bank of Slovenia regulation). New default flow is a result of normal portfolio movements and represents 7% of the portfolio at the end of 2017.

## **5.8. Use of credit risk mitigation techniques**

(Article 453 b, c, e, f and g of CRR)

### **Credit protection policy**

NLB Group applies a single set of standards to retail and corporate loan collateral, as developed by the members through the collateral harmonisation project. The master document regulating loan collateral in NLB Group is the Loan Collateral Policy in NLB Group and NLB. The Policy has been adopted by the Management Board of NLB and by the supervisory bodies of respective members for other members of NLB Group. The Policy represents the basic orientations bank employees must take into account when signing, evaluating, monitoring, and reporting collateral, with the aim of reducing credit risk.

NLB Group primarily accepts collateral complying with the Basel II requirements with the aim of improving credit risk management and consuming capital economically. In accordance with Basel II, collateral may consist of pledged deposits, government guarantees, bank guarantees, debt securities issued by central governments and central banks, bank debt securities, and real-estate mortgages (the real estate must be located in the European Economic Area for the effect on capital to be recognised).

Loans made to companies and sole proprietors may be secured by other forms of collateral as well (for example, a lien on movable property, a pledge of an equity stake, collateral by pledged/assigned receivables, etc.) if it is assessed that the collateral could generate a cash flow if it were needed as a secondary source of payment. In the case of a lower probability that such an item of collateral would generate a cash flow, a conservative approach is followed, namely, such collateral can be taken, but for reporting purposes the value is zero.

### **The processes for valuing collateral**

Pursuant to the law, NLB Group has set up a system for monitoring and reporting collateral at fair (market) value.

The market value of real estate or movable property used as collateral is obtained from valuation reports of licensed appraisers or, for low contract amounts, from sales agreements not older than one year. In NLB and members of NLB Group, most reports of external appraisers are controlled. Controls are performed by internal appraisers. The subject of control is the content, value, scope and format of the report, its compliance with international valuation standards and the estimated value. If they notice deviations, they estimate needed correction of the value of the external valuation (in %) and correct the value of the external valuation. The value adjustment can only be negative and can be applied only in a limited range. For the purposes of business decisions and the calculation of the necessary impairments and provisions, additional deductions (hair-cuts) are applied to the eventual adjusted market value, depending on the type of collateral. These haircuts are for real estate in the range between 30 and 70%, depending on the type of real estate and location, for movables they range between 50 and 100% depending on the type of movable.

The market value of financial instruments held by NLB Group is obtained from the organised market – the stock exchange – for listed financial instruments or determined in accordance with the internal methodology for unlisted financial instruments (such collateral is used exceptionally and on a small scale in loans granted to companies and sole proprietors).

NLB has compiled a reference list of licensed appraisers. All appraisals must be made for the purpose of secured lending and in accordance with the International Valuation Standards (IVS). Appraisals related to retail loans are generally ordered only from appraisers with whom the Bank has a contract for real-estate valuations. For corporate loans, appraisals are usually submitted by clients. If a client submits an appraisal not made by an appraiser included on the Bank's reference list, the expert department employing licensed appraisers (certified appraisers in construction with licences granted by the Ministry of Justice, and certified real-estate value appraisers with licences granted by the Slovenian Institute of Auditors) will verify the appraisal. The expert department is also responsible for reviewing valuations of real estate serving as collateral for large loans.

Other NLB Group members obtain valuations from in-house appraisers and outsourced appraisers, all having the necessary licences. NLB Group has compiled a reference list of appraisers for valuations of real estate located outside Slovenia. Appraisals must be made in accordance with the international valuation standards (IVS, EVS, and RICS). For larger loans, real-estate evaluations must be reviewed by an internal licensed appraiser with knowledge of the local real-estate market. If the appraisal does not correspond to

the international valuation standards or if the value adjustment is greater than certain limit, the appraisal is rejected as inadequate.

When assuring collateral, NLB Group follows the internal regulations which define the minimum security or pledge ratios. NLB Group strives to obtain collateral with a higher value than the underlying exposure (depending on the borrower's rating, loan maturity etc.) with the aim of reducing negative consequences resulting from any major swings in market prices of the assets used as collateral. In the case of a reduced value of collateral and/or deteriorated debtor credit rating, additional collateral is sought as necessary and in accordance with the contractual provisions. If real estate, movable property, and financial instruments serve as collateral, the Bank's lien should be entered as top ranking. Exceptionally, where the value of the mortgaged real estate is large enough, the lien can be entered with a different priority order.

NLB Group monitors the value of collateral during the loan repayment period in accordance with the mandatory periods and internal instructions. For example, the value of collateral using mortgaged real estate is monitored annually by either preparing individual assessments or using the internal methodology for preparing an own value appraisal of real estate (which applies to Slovenia, Serbia, Montenegro and Bosnia and Herzegovina) based on public records and indexes of real-estate value published by the relevant government authorities (the Surveying and Mapping Authority in Slovenia). The value of pledged movable property is monitored once a year (in NLB automated, with a straight-line depreciation over the period of the remaining useful life).

### **The main types of collateral taken by the Bank**

NLB Group accepts different forms of material and personal security as loan collateral.

Material loan collateral gives the right in case of the debtor (borrower) defaulting on their contractual obligations to sell specific property to recover claims, keep specific non-cash property or cash, or reduces or offsets the amount of exposure against the counterparty's debt to the Bank.

NLB Group accepts the following material types of loan collateral:

- asset-backed collateral:
  - collateral backed by business and residential real estate: land, buildings and individual parts of buildings in a storeyed property intended for living in or performing a business activity, such as land in the area foreseen for construction, apartments, residential buildings, garages and holiday homes, business premises, industrial buildings, offices, shops, hotels, branches and warehouses, forests, parking spaces, ... Objects can be completed or under construction. Priority is given to property where the pledge right of the bank is entered in the first place and real estate is already owned by the debtor and / or the pledger. For real estate, there must be a market, and it must be redeemable within a reasonable time.
  - collateral backed by movable property: priority is given to the types of movable property, that are highly likely to be sold in the event of execution, and the funds received are used to repay the collateralised claims (their market value must be estimated with considerable reliability). Among the appropriate types of movable property, the bank includes motor vehicles, agricultural machinery, construction machinery, production lines and series-produced machines and some custom-made production machines.
- collateral by a pledge of financial assets (bank deposits or cash-like instruments, debt securities of different issuers, investment fund units, equity securities, or convertible bonds):
  - cash receivable collateral; bank deposits and savings with bank are appropriate in domestic and foreign currency.
  - debt securities: shares and bonds which, according to the bank's assessment, are suitable for securing investments and are traded on a regulated market (marketable securities of higher-quality Slovene and foreign issuers). In the area of legal entities, the Bank conditionally accepts non-marketable securities, subject to appropriate conditions.
  - the pledge of investment coupons of mutual funds managed by management companies (a priority company NLB Skladi, asset management d.o.o.) and are, according to the bank assessment, suitable for insurance of investments.
- pledge of an equity stake: non-marketable capital shares with a credit rating of at least B are adequate.
- pledge or assignment of receivables as collateral: cash receivables must have longer maturities than the maturity of the investment and they must not be due and not be paid.

- other material forms of loan collateral (life insurance policies pledged to the Bank, etc.): the Bank accepts products of NLB Vita, life insurance company d.d. Ljubljana – pledge of an investment life insurance policy and a life insurance policy with a guaranteed return that includes saving, in addition to insurance.

Personal loan collateral is a method for reducing credit risk whereby a third party undertakes to pay the debt in case of the primary debtor (borrower) defaulting.

NLB Group accepts the following types of personal loan collateral:

- joint and several guarantees by retail and corporate clients: for the collateralisation of private individuals loans, employees or pensioners are adequate guarantors. They must not be in the process of personal bankruptcy. They are responsible for fulfilling the debtor's obligations for loans with a repayment period not exceeding 60 months. For the collateralisation of legal entities investments, legal entities, private individuals or private individuals are adequate guarantors.
- bank guarantees;
- government guarantees (e.g. of the Republic of Slovenia);
- guarantees by national and regional development agencies with which the Bank has a contract on the acceptance of guarantees (egg. Slovene Enterprise Fund).
- insurance with contractual insurance company (with payment of insurance premium).

Loans are very often secured by a combination of collateral types.

The general recommendations on loan collateral are specified in the internal instructions and include the elements specified below. The decision on the type of collateral and the coverage of loan by collateral depends on the analysis of data on the debtor (the debtor's credit rating and creditworthiness) and loan maturity; the difference arises from whether the loan is granted to retail or a corporate client. Corporate clients (companies and sole proprietors) must submit bills of exchange with written authorities for the creditor to fill them. NLB has also created, in the area of real-estate loan collateral, an 'on-line' connection with the Surveying and Mapping Authority in Slovenia which allows direct and immediate verification of the existence of property.

NLB Group strives to ensure the best possible collateral for long-term loans, namely mortgages in most cases. Thus, the mortgaging of real estate is the most frequent form of loan collateral of corporate and retail clients. In corporate loans, it is followed by government and corporate guarantees. In retail loans, it is followed by insurance companies and guarantors.

### Concentration that arises due to CRM measures and may prevent CRM instruments from being effective

The CRR eligible collateral that allow a decrease in RWA for credit risks amounts to EUR 808 million and represents 7.1 % of the net exposure pre CCR and CRM. The prevailing types of collateral used as CRM are government guarantees and cash deposits, the bank does not use credit derivatives to manage capital requirements. The low volume of eligible collateral shows the low concentration from CRM point of view.

Table 25 – EU CR3 – CRM techniques – Overview of NLB Group

	Exposures unsecured – Carrying amount	Exposures secured – Carrying amount	Exposures secured by collateral	Exposures secured by financial guarantees	Exposures secured by credit derivatives
<b>31.12.2017</b>					
Total loans	7,748,685	725,983	700,613	643,827	-
Total debt securities	2,776,733	123,480	123,480	123,480	-
<b>Total exposures</b>	<b>10,525,418</b>	<b>849,463</b>	<b>824,093</b>	<b>767,307</b>	-
Of which defaulted	8,929	29,079	614	225	-
<b>31.12.2016</b>					
Total loans	7,625,081	816,648	799,365	741,690	-
Total debt securities	2,531,204	143,322	143,322	143,322	-
<b>Total exposures</b>	<b>10,156,285</b>	<b>959,970</b>	<b>942,687</b>	<b>885,012</b>	-
Of which defaulted	18,140	31,613	2,502	361	-

At the end of 2017, the secured part of the portfolio represents 7.1% of the total portfolio. However, it has to be considered that such low share is due to stick rules applied to the eligible collateral in the standardised approach. The values of secured exposure decreased in 2017, primarily due to repayment of exposure with state guarantees.

Table 26 – CRM techniques – Overview by exposure classes of NLB Group

31.12.2017	Exposures unsecured – Carrying amount	Exposures secured – Carrying amount	Exposures secured by collateral	Exposures secured by financial guarantees
<b>Exposure classes</b>				
Central governments or central banks	3,037,756	-	-	-
Regional government or local authorities	109,193	-	-	-
Public sector entities	67,236	7,401	7,398	7,398
Multilateral development banks	69,399	-	-	-
International organisations	-	-	-	-
Institutions	1,220,730	40,681	40,681	40,681
Corporates	1,499,155	740,065	726,582	716,423
Retail	3,358,948	50,910	44,619	334
Secured by mortgages on immovable property	697,134	-	-	-
Exposures in default	296,133	749	614	225
Exposures associated with particularly high ri	60,025	9,656	4,198	2,246
Covered bonds	89,191	-	-	-
Institutions and corporates with a short-term c	-	-	-	-
Collective investment undertakings	1,147	-	-	-
Equity	-	-	-	-
Other items	19,371	1	1	-
<b>Total</b>	<b>10,525,418</b>	<b>849,463</b>	<b>824,093</b>	<b>767,307</b>
<b>31.12.2016</b>				
<b>Exposure classes</b>				
Central governments or central banks	2,899,121	-	-	-
Regional government or local authorities	116,608	-	-	-
Public sector entities	59,246	59,301	59,300	59,296
Multilateral development banks	41,318	-	-	-
International organisations	-	-	-	-
Institutions	1,234,887	60,035	60,030	60,030
Corporates	1,632,056	785,594	773,485	765,189
Retail	3,068,871	52,108	47,071	136
Secured by mortgages on immovable property	579,765	-	-	-
Exposures in default	447,406	2,633	2,502	361
Exposures associated with particularly high ri	5,530	299	299	-
Covered bonds	50,418	-	-	-
Institutions and corporates with a short-term c	-	-	-	-
Collective investment undertakings	-	-	-	-
Equity	-	-	-	-
Other items	21,059	-	-	-
<b>Total</b>	<b>10,156,285</b>	<b>959,970</b>	<b>942,687</b>	<b>885,012</b>

Table 27 – EU CR4 – Standardised approach – Credit risk exposure and CRM effects of NLB Group

31.12.2017		Exposures before CCF and CRM		Exposures post CCF and CRM		RWAs and RWA density	
		On-balance-sheet amount	Off-balance-sheet amount	On-balance-sheet amount	Off-balance-sheet amount	RWAs	RWA density
Exposure classes							
1	Central governments or central banks	3,060,144	1,532	3,884,233	12,788	1,031,854	26%
2	Regional government or local authorities	109,195	821	109,195	175	50,094	46%
3	Public sector entities	74,807	13,756	67,410	3,496	54,043	76%
4	Multilateral development banks	69,399	-	69,399	-	-	-
6	Institutions	1,265,587	53,392	1,224,909	14,310	523,027	42%
7	Corporates	2,240,628	945,421	1,514,045	273,243	1,743,491	98%
8	Retail	3,410,857	790,851	3,366,237	175,452	2,538,590	72%
9	Secured by mortgages on immovable property	697,134	13,142	697,134	4,186	264,396	38%
10	Exposures in default	297,001	50,545	296,386	11,820	365,169	118%
11	Exposures associated with particularly high risk	69,692	21,070	65,494	5,780	106,911	150%
12	Covered bonds	89,191	-	89,191	-	12,260	14%
14	Collective investment undertakings	45,662	-	45,662	-	6,489	14%
15	Equity	26,660	-	26,660	-	48,383	181%
16	Other items	618,867	2	618,868	0	351,706	57%
17	<b>Total</b>	<b>12,074,822</b>	<b>1,890,531</b>	<b>12,074,822</b>	<b>501,250</b>	<b>7,096,414</b>	<b>56%</b>

31.12.2016		Exposures before CCF and CRM		Exposures post CCF and CRM		RWAs and RWA density	
		On-balance-sheet amount	Off-balance-sheet amount	On-balance-sheet amount	Off-balance-sheet amount	RWAs	RWA density
Exposure classes							
1	Central governments or central banks	2,906,237	1,536	3,848,922	18,171	864,356	22%
2	Regional government or local authorities	116,610	1,190	116,610	238	58,175	50%
3	Public sector entities	118,595	9,825	59,296	3,870	54,385	86%
4	Multilateral development banks	41,318	-	41,318	-	-	-
6	Institutions	1,299,266	34,513	1,239,238	12,374	540,002	43%
7	Corporates	2,419,208	956,178	1,645,723	306,174	1,745,284	89%
8	Retail	3,121,571	730,743	3,074,499	169,148	2,328,861	72%
9	Secured by mortgages on immovable property	579,765	13,245	579,765	4,371	214,583	37%
10	Exposures in default	450,108	91,653	447,606	23,073	566,336	120%
11	Exposures associated with particularly high risk	5,834	875	5,535	506	9,060	150%
12	Covered bonds	50,418	-	50,418	-	7,416	15%
14	Collective investment undertakings	44,570	-	44,570	-	5,794	13%
15	Equity	49,547	-	49,547	-	75,829	153%
16	Other items	654,384	12	654,384	2	394,655	60%
17	<b>Total</b>	<b>11,857,431</b>	<b>1,839,771</b>	<b>11,857,431</b>	<b>537,928</b>	<b>6,864,736</b>	<b>55%</b>

The table shows exposures before CRM and CCF, exposure post-CCF and -CRM and RWA for all customer segments. In 2017, the increase of both types of exposures was noticed in the Retail segment, which is in line with the findings in other disclosure tables. The last column shows RWA density or the average risk weight for each client segment. The average weight increased from 55.4% in 2016 to 56.4% in 2017, the main reason being a transfer of exposures to the high-risk exposure segment (based on a new interpretation of the segment encouraged by the ECB supervisory review).

## 6. Use of ratings by external rating institutions (ECAI)

(Article 444 a, b, c and d of CRR)

For calculating the capital requirement for credit risk, NLB Group uses the standardised approach as prescribed by CRR. Calculation of the capital requirement takes into account the effect of loan collateral as a secondary source repayment. NLB Group uses the simple calculation method for collateral. According to this methodology, the capital requirement is calculated depending on the segment of a clients, their credit quality (in case ECAI was nominated for the segment and external credit rating is available) and the quality of collateral which must be adequately evaluated and at the same time satisfy the prescribed minimum requirements.

For the calculation of capital requirement for credit risk, NLB Group nominated Fitch Ratings credit rating agency, which was estimated to be an eligible external credit assessment institution, at the same time the

mapping to the credit quality steps was determined by the EBA. The credit assessments of this agency are used for the categories of exposure:

- to the central government or central bank, and
- to institutions, including the exposure to institutions with short-term credit assessment.

The weight for each category of exposure is determined based on CRR.

In exposure categories for which a credit assessment institution was designated, the weight is assigned based on the financial instrument's rating. If such rating is not available, the higher of the weights applying to long-term credit rating of the debtor or other financial instruments of the same debtor or country is used.

For categories of exposure for which a credit assessment institution was not appointed, the risk weight is assigned according to the prescribed legislation, meaning that it is assigned based on the rating of the debtor's country or specific rules applying to the respective exposure category.

Table 28 – EU CR5 – Standardised approach of NLB Group

31.12.2017	Risk weight															Deducted	Total	
	0%	2%	4%	10%	20%	35%	50%	70%	75%	100%	150%	250%	370%	1250%	Others			
1 Central governments or central banks	2,782,364	-	-	-	101,015	-	59,621	-	-	935,418	-	18,603	-	-	-	-	-	3,897,021
2 Regional government or local authorities	-	-	-	-	74,095	-	-	-	-	35,275	-	-	-	-	-	-	-	109,370
3 Public sector entities	13,639	-	-	-	252	-	6,044	-	-	50,971	-	-	-	-	-	-	-	70,906
4 Multilateral development banks	69,399	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	69,399
6 Institutions	-	-	-	-	361,930	-	853,297	-	-	23,993	-	-	-	-	-	-	-	1,239,219
7 Corporates	-	-	-	-	-	-	-	-	-	1,787,287	-	-	-	-	-	-	-	1,787,287
8 Retail	-	-	-	-	-	-	-	-	3,541,689	-	-	-	-	-	-	-	-	3,541,689
9 Secured by mortgages on immovable property	-	-	-	-	-	531,446	169,874	-	-	-	-	-	-	-	-	-	-	701,320
10 Exposures in default	-	-	-	-	-	-	-	-	-	194,280	113,926	-	-	-	-	-	-	308,206
11 Exposures associated with particularly high risk	-	-	-	-	-	-	-	-	-	-	71,274	-	-	-	-	-	-	71,274
12 Covered bonds	-	-	-	55,778	33,413	-	-	-	-	-	-	-	-	-	-	-	-	89,191
14 Collective investment undertakings	-	-	-	-	-	-	-	-	-	1,147	-	-	-	-	44,514	-	-	45,662
15 Equity	-	-	-	-	-	-	-	-	-	12,178	-	14,482	-	-	-	-	-	26,660
16 Other items	256,594	-	-	-	13,211	-	-	-	-	349,063	-	-	-	-	-	-	-	618,869
<b>17 Total</b>	<b>3,121,996</b>	-	-	<b>55,778</b>	<b>583,916</b>	<b>531,446</b>	<b>1,088,835</b>	-	<b>3,541,689</b>	<b>3,389,613</b>	<b>185,200</b>	<b>33,085</b>	-	-	<b>44,514</b>	-	-	<b>12,576,073</b>

31.12.2016	Risk weight															Deducted	Total	
	0%	2%	4%	10%	20%	35%	50%	70%	75%	100%	150%	250%	370%	1250%	Others			
1 Central governments or central banks	2,961,824	-	-	-	54,042	-	3,219	-	-	845,289	-	2,719	-	-	-	-	-	3,867,093
2 Regional government or local authorities	-	-	-	-	73,342	-	-	-	-	43,506	-	-	-	-	-	-	-	116,848
3 Public sector entities	5,717	-	-	-	85	-	5,990	-	-	51,373	-	-	-	-	-	-	-	63,166
4 Multilateral development banks	41,318	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	41,318
6 Institutions	-	-	-	-	331,021	-	893,588	-	-	27,004	-	-	-	-	-	-	-	1,251,612
7 Corporates	-	-	-	-	-	-	-	-	-	1,951,898	-	-	-	-	-	-	-	1,951,898
8 Retail	-	-	-	-	-	-	-	-	3,243,648	-	-	-	-	-	-	-	-	3,243,648
9 Secured by mortgages on immovable property	-	-	-	-	-	455,901	128,235	-	-	-	-	-	-	-	-	-	-	584,136
10 Exposures in default	-	-	-	-	-	-	-	-	-	279,366	191,313	-	-	-	-	-	-	470,679
11 Exposures associated with particularly high risk	-	-	-	-	-	-	-	-	-	-	6,040	-	-	-	-	-	-	6,040
12 Covered bonds	-	-	-	26,671	23,747	-	-	-	-	-	-	-	-	-	-	-	-	50,418
14 Collective investment undertakings	-	-	-	-	-	-	-	-	-	-	-	-	-	-	44,570	-	-	44,570
15 Equity	-	-	-	-	-	-	-	-	-	29,534	3,738	16,275	-	-	-	-	-	49,547
16 Other items	255,771	-	-	-	4,951	-	-	-	-	393,664	-	-	-	-	-	-	-	654,386
<b>17 Total</b>	<b>3,264,631</b>	-	-	<b>26,671</b>	<b>487,187</b>	<b>455,901</b>	<b>1,031,032</b>	-	<b>3,243,648</b>	<b>3,621,635</b>	<b>201,091</b>	<b>18,994</b>	-	-	<b>44,570</b>	-	-	<b>12,395,359</b>

The exposure values post-CRM and post-CCR in each specific risk-weight class are distributed based on the standardised approach rules. The 0% weight prevails in the Central government segment, 20% and 50% for the Institutions (depending on ECAI rating and residual maturity of the exposure), 35% for Secured by real estate exposure and 75% in the Retail segment, while 100% is applied to all other segments. The 150% weight is only applied to high-risk exposures and those default exposures, whose provision coverage does not exceed 20%. In 2017, the highest increase was noticed on the 75% weight, due to the increase of exposure in the Retail segment, while the highest decrease appeared under 100% weight, predominantly in the Corporate segment.

## 7. Exposure to counterparty credit risk

### 7.1. Goals and Principles of Counterparty Credit Risk Management

(Article 435.1 a, b, c and d of CRR)

#### Management of Counterparty Credit Risk

Counterparty Credit Risk (CCR) arises when NLB Group engages in derivative transactions with a counterparty for instruments like exchange-traded (futures) and OTC derivatives (forwards, swaps traded off the exchange) or due to long settlement transactions (meaning that a delivery date is later than the earliest of the market standard for the particular transaction). The purpose of entering into the derivatives is to support corporate customers and financial institutions in their management of financial exposures. This is managed within Investment Banking and Custody, Financial Markets and Evaluation and Control. Financial Markets also use derivatives to protect cash flows and fair values of financial assets and liabilities of NLB Group.

CCR is defined as the risk that the counterparty to a transaction may default before the settlement of the transaction. CCR is a particular case of a general credit risk and creates a bilateral risk of loss, therefore the market value of the transaction can be positive or negative to either counterparty of the transaction. The market value is uncertain and can vary over time with the movement of underlying market factors. CCR exposure is estimated considering the effect of a period of stress and the collateral management practices.

Limits for counterparty exposures are set in the regular credit process. Evaluation and Control identifies, measures, reports and follows up on NLB Group's counterparty credit risk. The risk is measured daily and reported monthly to the ALCO.

CCR for OTC derivatives is the sum of relevant replacement cost (i.e. positive market value) and potential replacement costs resulting from potential future changes in market values (FX prices, interest rates, etc.). A dedicated IT solution is in place for monitoring, along with customisation made to meet specific needs. It enables us to monitor CCR on a real-time basis, a deal-by-deal level as well as on a group level by individual counterparty or counterparty group. Limits must be checked before any transaction is agreed upon and confirmed.

In settling the concluded financial transactions, NLB Group is exposed to the settlement risk which is a risk that one of the parties would not (be able to) meet its liabilities arising from the transactions in accordance with the agreed conditions, after the counterparty has already met its part of the obligations. The tolerance towards the assumptions of the settlement risk is low. NLB Group has adopted internal regulations and a system of performing settlements, as well a system of control mechanisms for the management of settlement risk. The standardised approach is used to determine the regulatory capital charge for the settlement risk.

#### Organisation

Credit risks from derivatives are fully integrated into the general credit risk management system. CCR risk is measured and monitored on a daily basis by an independent risk management unit Evaluation and Control. Global Risk is responsible for calculation of own fund requirements for CCR risk according to a standardised approach.

#### Risk Measurement and control of CCR

CCR risk is monitored and controlled at transaction level as well as at client level. Market value of derivative transactions fluctuate during the term to maturity, for this reason the uncertainties of future market conditions have to be taken into consideration when measuring credit exposure to derivatives.

For calculation of a regulatory capital for counterparty credit risk, NLB Group uses a standardised approach (SA) for the derivatives. NLB Group currently uses the Current Exposure Method (also referred to as marked-to-market method) according to the CRD IV.

### **Credit valuation adjustment (CVA) and debit valuation adjustment (DVA)**

Counterparty credit risk in derivatives affects the Bank's profit and loss through credit/debt valuation adjustments (CVA/DVA), reflecting the credit risk associated with the derivative positions. These adjustments depend on credit rating or/and credit spread of a certain client. NLB Group uses the standardised approach to calculate the regulatory capital requirement for CVA. Where collateral exists, it is taken into consideration when CVA/DVA is calculated. Calculation is done on a monthly basis. DVA is not recognised in the Profit or Loss Statement but only calculated for internal purposes.

### **7.2. Risk mitigation – netting and collateral**

(Article 439 b of CRR)

NLB Group mitigates CCR risk from derivatives through the use of close-out netting agreements such as ISDA Master Agreement, Global Master Repurchase Agreement (GMRA), and the Slovene Framework Agreement. Along with these agreements, collateral agreements (e.g. ISDA Credit Support Annex) are in place to substantially reduce credit risk arising out of derivatives transactions. In addition to this, clearing transactions via a clearing house is in place for relevant derivatives transactions.

Daily margin call calculations are in place for each relevant counterparty. Portfolio reconciliation is agreed as per European Market Infrastructure Regulation (EMIR).

### **7.3. Internal capital allocation and definition of credit limits for CCR exposures**

(Article 439 a of CRR)

The CRR exposures of NLB Group are not material thus NLB Group sets aside capital for CCR exposures in Pillar 1 while no additional capital is held within Internal Capital Adequacy Assessment (Pillar 2). In addition, there is a set of internal credit limits in place for CCR exposure which are guided by the internal policies and methodologies.

NLB Group has in place instructions for determining derivative financial instrument limits. There is a set of guidelines in use when concluding derivative transactions with clients. Each client has to have a limit in place and all transactions are concluded by using the contract. Only standard interest and foreign exchange derivatives can be subject to proposal and/or approval. The limit is treated as an arrangement decided in line with the credit process. Only clients rated as A and B credit rating group and clients classified as CCC rating class are suitable for new limits. To approve the new limits, the underlying preconditions have to be met as follows: the primary business has to have sustainable cash flow, the client has to be able to cover derivatives exposure and potential negative effect, and the derivative is subject to support primary business transactions.

NLB Group has an important risk management tool in place which is an early warning system for exposures towards banking groups, sovereigns and international corporates. The respective exposures are limited by the risk appetite, monitored, and reported to the senior management and Supervisory Board on a regular basis.

### **7.4. Securing of collateral and establishing of reserves**

(Article 439 b of CRR)

Framework agreements signed with the relevant counterparty provide the ability to collect collateral for the purpose of reducing CCR. As mentioned in previous chapters, NLB Group calculates net positive market value for individual counterparty exposure on a daily basis and as a result, collateral is adjusted accordingly. For the vast majority of framework agreements only cash is eligible collateral. Where other forms of collateral are possible, haircuts are applied as per the credit rating of such collateral along with the days to maturity. If securities are an eligible collateral form, only top-rated bonds are permitted. All this results in the fact that NLB Group only takes into account top-rated collateral and therefore we do not create any additional reserves to mitigate CCR.

## 7.5. Wrong-way risk management (Article 439 c of CRR)

In accordance with risk mitigation techniques in place (real-time monitoring, framework agreements, collateral agreements, daily margining process, CVA/DVA calculation...), NLB Group does not find wrong-way risk exposures as material.

## 7.6. Downgrading impacts on collateralisation (Article 439 d, e and f of CRR)

Framework agreements covering derivatives transactions usually do not have provisions that would reflect any additional collateral posting due to credit rating change of NLB Group. Therefore, downgrading impacts on collateralisation are not material.

Table 29 – EU CCR1 – Analysis of CCR exposure by approach for NLB Group

	a	b	c	f	g
	Notional	Replacement cost/current market value	Potential future credit exposure	EAD post CRM	RWAs
<b>31.12.2017</b>					
1 Mark to market	-	12,229	10,641	22,872	20,133
<b>11 Total</b>	-	-	-	-	<b>20,133</b>

	a	b	c	f	g
	Notional	Replacement cost/current market value	Potential future credit exposure	EAD post CRM	RWAs
<b>31.12.2016</b>					
1 Mark to market	-	19,077	8,349	27,426	22,770
<b>11 Total</b>	-	-	-	-	<b>22,770</b>

Table 30 - EU CCR2 – CVA capital charge for NLB Group

	31.12.2017		31.12.2016	
	Exposure value	RWAs	Exposure value	RWAs
4 All portfolios subject to the standardised method	2,607	850	2,529	463
EU4 Based on the original exposure method	-	-	-	-
<b>5 Total subject to the CVA capital charge</b>	<b>2,607</b>	<b>850</b>	<b>2,529</b>	<b>463</b>

Table 31 – EU CCR8 – Exposures to CCPs of NLB Group

	31.12.2017		31.12.2016	
	EAD post CRM	RWAs	EAD post CRM	RWAs
<b>1 Exposures to QCCPs (total)</b>	-	<b>14,059</b>	-	<b>3,482</b>
Exposures for trades at QCCPs (excluding initial margin and default				
2 fund contributions); of which	14,059	14,059	3,482	3,482
3 OTC derivatives	14,059	14,059	3,482	3,482
7 Segregated initial margin	21,691	-	5,318	-
<b>11 Exposures to non-QCCPs (total)</b>	-	-	-	-
20 Unfunded default fund contributions	-	-	-	-

Table 32 – EU CCR3 – Standardised approach – CCR exposures by regulatory portfolio and risk of NLB Group

31.12.2017		Risk weight											Total	Of which unrated
Exposure classes	0%	2%	4%	10%	20%	50%	70%	75%	100%	150%	Others			
1 Central governments or central banks	2,782,364	-	-	-	-	101,015	59,621	-	-	935,470	8	17,912	3,896,390	3,896,390
2 Regional government or local authorities	-	-	-	-	-	74,095	-	-	-	35,296	11	-	109,402	109,402
3 Public sector entities	13,639	-	-	-	-	252	6,044	-	-	57,675	3	2,514	80,128	80,128
4 Multilateral development banks	69,399	-	-	-	-	-	-	-	-	-	-	-	69,399	69,399
6 Institutions	-	-	-	55,778	395,342	853,297	-	-	23,993	65	214	1,328,689	346,271	
7 Corporates	-	-	-	-	-	65,559	-	-	1,134,209	62,152	3,409	1,265,330	1,265,330	
8 Retail	-	-	-	-	-	104,315	-	3,541,689	859,938	122,954	584,995	5,213,891	5,213,891	
10 Other items	256,594	-	-	-	-	13,211	-	-	343,033	7	-	612,845	598,776	
<b>11 Total</b>	<b>3,121,996</b>	<b>-</b>	<b>-</b>	<b>55,778</b>	<b>583,916</b>	<b>1,088,835</b>	<b>-</b>	<b>3,541,689</b>	<b>3,389,613</b>	<b>185,200</b>	<b>609,045</b>	<b>12,576,073</b>	<b>11,579,586</b>	

31.12.2016		Risk weight											Total	Of which unrated
Exposure classes	0%	2%	4%	10%	20%	50%	70%	75%	100%	150%	Others			
1 Central governments or central banks	2,961,824	-	-	-	54,042	3,219	-	-	845,289	9	46,764	3,911,147	3,911,147	
2 Regional government or local authorities	-	-	-	-	73,342	-	-	-	44,113	20	-	117,475	117,475	
3 Public sector entities	5,717	-	-	-	85	5,990	-	-	59,191	16	2,465	73,464	73,464	
4 Multilateral development banks	41,318	-	-	-	-	-	-	-	-	-	-	41,318	41,318	
6 Institutions	-	-	-	26,671	354,768	893,588	-	-	27,004	454	183	1,302,666	167,934	
7 Corporates	-	-	-	-	-	53,658	-	-	1,182,827	73,869	3,409	1,313,763	1,313,763	
8 Retail	-	-	-	-	-	74,577	-	3,243,648	1,076,290	126,723	466,644	4,987,881	4,987,881	
10 Other items	255,771	-	-	-	4,951	-	-	-	386,921	-	-	647,643	532,529	
<b>11 Total</b>	<b>3,264,631</b>	<b>-</b>	<b>-</b>	<b>26,671</b>	<b>487,187</b>	<b>1,031,032</b>	<b>-</b>	<b>3,243,648</b>	<b>3,621,634</b>	<b>201,091</b>	<b>519,465</b>	<b>12,395,358</b>	<b>11,145,513</b>	

The exposure values are distributed to the prescribed segments and the risk weights that apply based on the riskiness of the exposure in accordance with the standardised approach. The 0% weight prevails in Central government segment, 20% and 50% for the Institutions (depending on ECAI rating and residual maturity of the exposure), 75% in the Retail segment, while 100% is applied to all other segments. The 150% weight is applied to Retail and Corporate customers that represent High risk exposures and those Default exposures, whose provision coverage does not exceed 20%. In 2017, the highest increase was noticed on the 75% weight, due to the increase of exposure in the Retail segment, while the highest decrease appeared under 100% weight, predominantly in the Corporate segment.

Table 33 – EU CCR5-A – Impact of netting and collateral held on exposure values for NLB Group

	Gross positive fair value or net carrying amount	Netting benefits	Netted current credit exposure	Collateral held	Net credit exposure
<b>31.12.2017</b>					
1 Derivatives	13,703	3,976	9,717	1,516	8,201
<b>4 Total</b>	<b>13,703</b>	<b>3,976</b>	<b>9,717</b>	<b>1,516</b>	<b>8,201</b>
	Gross positive fair value or net carrying amount	Netting benefits	Netted current credit exposure	Collateral held	Net credit exposure
<b>31.12.2016</b>					
1 Derivatives	19,211	5,211	14,000	300	13,700
<b>4 Total</b>	<b>19,211</b>	<b>5,211</b>	<b>14,000</b>	<b>300</b>	<b>13,700</b>

Table 34 – EU CCR5-B – Composition of collateral for exposures to CCR of NLB Group

	Collateral used in derivative transactions			
	Fair value of collateral received		Fair value of posted collateral	
	Segregated	Unsegregated	Segregated	Unsegregated
<b>31.12.2017</b>				
Cash	1,516	-	52,905	-
<b>Total</b>	<b>1,516</b>	<b>-</b>	<b>52,905</b>	<b>-</b>
	Collateral used in derivative transactions			
	Fair value of collateral received		Fair value of posted collateral	
	Segregated	Unsegregated	Segregated	Unsegregated
<b>31.12.2016</b>				
Cash	300	-	36,686	-
<b>Total</b>	<b>300</b>	<b>-</b>	<b>36,686</b>	<b>-</b>

## 8. Unencumbered assets

(Article 443 of CRR)

### General narrative information on asset encumbrance

Asset encumbrance presents an important aspect of liquidity risk management. The Group regularly monitors and reports on asset encumbrance. The increase in the volume of encumbered assets contributes to higher liquidity risk and the risk of financing, since an institution with encumbered assets has less available assets for pledging, used as liquidity reserve for unexpected liquidity needs (e.g. approved credit lines, margin calls on derivatives).

The Group must ensure that it has at every moment enough high-quality liquid assets so it is able to meet all liquidity needs. Possible operations for asset encumbrance:

- pledge of securities,
- repo transactions via interbank or ECB funding,
- derivatives trading (CSA contracts),
- issue of covered bonds,
- financing on capital and interbank markets.

Monthly reports on the Group's asset encumbrance are submitted to ALCO by the Financial Markets (for each banking member and on consolidated level), while the Global Risk (Market and Liquidity Risk) quarterly reports to the Bank of Slovenia on solo and consolidated level.

In the Group, all assets that are pledged are reported as encumbered assets. Regarding a transparent way of reporting, the Group has no example of giving the pledge which then would not be included in AE reporting. There is also no difference between the regulatory consolidation scope and liquidity requirements on an IFRS consolidated basis.

At the structural level the goal of liquidity management is to achieve such a structure of the Group's balance sheet that will ensure the Group's long-term stability and liquidity based on the criteria of long-term maturity match, forms and concentration of the sources of financing.

In alignment with Liquidity Risk Management Policy the unencumbered assets represent a liquidity buffer, which includes cash, money market placements, high-quality debt securities and ECB eligible loans.

The Group holds an adequate amount of unencumbered High-Quality Liquid Assets (HQLA) that can be converted easily and immediately into cash. The Group can use those stocks of assets as a source of contingent funds that are available to fill funding gaps between cash inflows and outflows at any time during the 30-day stress period. According to Basel III, the Group demonstrates monthly that its LCR ratio — HQLA divided by total net cash outflows — is always greater than 100% (276% at the end of December 2017) which indicates that the Group does not need any additional liquidity to withstand cash outflows during a “significant stress scenario” lasting 30 days. Also from this point of view, there is no need to carry a greater extent of encumbered assets. However, all assets that have been pledged are treated and reported as encumbered and most of them are derived mainly from the parent bank.

The Group has a strong liquidity position, all internal liquidity indicators and liquidity reserves are high and well above required standards, which means that the Group encumbers assets only because of regulatory aspects, such as the deposit guarantee scheme and the resolution fund.

As at 31 December 2017 the Group and NLB had a large share of unencumbered assets. On the Group level the amount of encumbered assets equalled EUR 122.1 million. On the solo level the amount of encumbered assets equalled EUR 116.6 million.

Encumbered assets consist of debt securities of which: issued by general governments (EUR 63.3 million on the Group level and on the solo level EUR 62.6 million) and placed deposits (EUR 58.8 million on the Group level and on the solo level EUR 54 million). Group members are self-funded and have a strong liquidity position, therefore NLB has the majority of encumbered assets in the Group.

The amount of encumbered assets is denominated in EUR currency which is the most significant currency of the Group. There are no other significant currencies of AE to be reported.

The calculation of asset encumbrance was made based on median values in such a way that they rolled over the previous 12 months on a quarterly basis and were determined by interpolation (used for display in tables 35 to 39)

Table 35 – Encumbered and unencumbered assets of NLB Group

	Carrying amount of encumbered assets		Fair value of encumbered assets		Carrying amount of non-encumbered assets		Fair value of non-encumbered assets	
		of which notionally eligible EHQLA and HQLA		of which notionally eligible EHQLA and HQLA		of which EHQLA and HQLA		of which EHQLA and HQLA
<b>31.12.2017</b>								
<b>Assets</b>	<b>130,593</b>	<b>81,440</b>	-	-	<b>11,882,668</b>	<b>2,790,387</b>	-	-
Equity instruments	-	-	-	-	67,595	-	-	-
Debt securities	82,551	81,440	89,457	88,293	2,699,660	2,008,040	2,745,337	2,052,425
of which: issued by general governments	74,214	73,327	80,989	80,025	1,839,693	1,387,497	1,884,552	1,440,230
of which: issued by financial corporations	8,105	8,092	8,272	8,258	698,673	550,689	699,415	551,434
of which: issued by non-financial corporations	-	-	-	-	97,821	94,662	92,144	88,738
Other assets	48,975	-	-	-	9,105,204	783,954	-	-

Table 36 – Collateral received of NLB Group

	Fair value of encumbered collateral received or own debt securities issued		Non-encumbered	
			Fair value of collateral received or own debt securities issued available for encumbrance	
		of which notionally eligible EHQLA and HQLA		of which EHQLA and HQLA
<b>31.12.2017</b>				
<b>Collateral received</b>	-	-	<b>7,719,007</b>	-
Loans on demand	-	-	-	-
Equity instruments	-	-	184,659	-
Loans and advances other than loans on demand	-	-	123,100	-
Other collateral received	-	-	7,409,502	-
<b>Own debt securities issued other than own covered bonds or asset-backed securities</b>	-	-	-	-
<b>Own covered bonds and asset-backed securities issued and not yet pledged</b>	-	-	-	-
<b>TOTAL ASSETS, COLLATERAL RECEIVED AND OWN DEBT SECURITIES ISSUED</b>	<b>130,593</b>	<b>74,175</b>		

Table 37 – Encumbered and unencumbered assets of NLB

	Carrying amount of encumbered assets		Fair value of encumbered assets		Carrying amount of non-encumbered assets		Fair value of non-encumbered assets	
		of which notionally eligible EHQLA and HQLA		of which notionally eligible EHQLA and HQLA		of which EHQLA and HQLA		of which EHQLA and HQLA
<b>31.12.2017</b>								
<b>Assets</b>	<b>125,720</b>	<b>81,440</b>	-	-	<b>8,642,269</b>	<b>2,790,387</b>	-	-
Equity instruments	-	-	-	-	57,499	-	-	-
Debt securities	82,551	81,440	89,457	88,293	2,225,771	2,008,040	2,271,842	2,052,425
of which: issued by general governments	74,214	73,327	80,989	80,025	1,448,457	1,387,497	1,493,314	1,440,230
of which: issued by financial corporations	8,105	8,092	8,272	8,258	698,096	550,689	698,838	551,434
of which: issued by non-financial corporations	-	-	-	-	97,821	94,662	92,144	88,738
Other assets	40,597	-	-	-	6,341,191	783,954	-	-

Table 38 – Collateral received of NLB

	Fair value of encumbered collateral received or own debt securities issued		Non-encumbered	
			Fair value of collateral received or own debt securities issued available for encumbrance	
		of which notionally eligible EHQLA and HQLA		of which EHQLA and HQLA
<b>31.12.2017</b>				
<b>Collateral received</b>	-	-	<b>4,013,015</b>	-
Loans on demand	-	-	-	-
Equity instruments	-	-	171,692	-
Loans and advances other than loans on demand	-	-	37,431	-
Other collateral received	-	-	3,801,123	-
<b>Own debt securities issued other than own covered bonds or asset-backed securities</b>	-	-	-	-
<b>Own covered bonds and asset-backed securities issued and not yet pledged</b>	-	-	-	-
<b>TOTAL ASSETS, COLLATERAL RECEIVED AND OWN DEBT SECURITIES ISSUED</b>	<b>125,720</b>	<b>74,175</b>		

Table 39 – Sources of encumbrance of NLB Group and NLB

	Matching liabilities, contingent liabilities or securities lent	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered
<b>31.12.2017</b>		
<b>Carrying amount of selected financial liabilities</b>	<b>5,158,148</b>	<b>125,720</b>

## 9. Exposure to market risk

(Article 445 of CRR)

Market risk is the risk that the Bank's earnings and/or economic value may be negatively affected by changes in market rates and parameters that effect on- and off-balance sheet positions (for example changes in foreign exchange rates, fluctuations in interest rates, credit spreads, equity prices, implied volatilities and market liquidity). Market risks predominately arise from the Bank's core business activities – the banking book and the liquidity portfolio needed to support these activities.

Table 40 – EU MR1 – Market risk under the standardised approach of NLB Group

		31.12.2017		31.12.2016	
		RWAs	Capital requirements	RWAs	Capital requirements
Outright products					
1	Interest rate risk (general and specific)	5,638	451	27,975	2,238
3	Foreign exchange risk	494,088	39,527	76,200	6,096
4	Commodity risk				
<b>9</b>	<b>Total</b>	<b>499,726</b>	<b>39,978</b>	<b>104,175</b>	<b>8,334</b>

In 2017, the RWA for position risk decreased by EUR 22 million due to the sale and maturing of debt securities and the RWA for foreign exchange risk increased by EUR 418 million due to the adjusted methodology for calculation of FX positions which include all non-euro equity investments in subsidiaries of NLB Group.

### 9.1. Goals and principles of Market risk management

(Article 435.1 a, b, c and d of CRR)

#### The objectives and risk management policy

The key objectives of NLB Group Market Risk Management as an independent risk function is to:

- regularly identify, evaluate and assess all material market risk.
- monitor, manage, control and steer market risk.
- define limits for trading activities consistent with the Group's Risk Appetite Framework (RAF), NLB Group Risk Strategy and business strategy in order to align top-down management targets with bottom-up business initiatives.
- ensure that NLB Group business lines do not expose the bank to unacceptable losses outside of the risk appetite and to contribute to income stability via independent identification, assessment and understanding of market risk.
- constantly develop and upgrade market risk models and methodologies, including stress-testing and early warning systems.

Market Risk Management aims to accurately measure all types of market risks by a comprehensive set of risk metrics reflecting economic and regulatory requirements. To achieve this objective, market risk management works closely with business lines and other control and support groups.

NLB Group strategy is to secure cost-efficient funding from several diversified sources with emphasis on ensuring of long-term stable deposit basis, not to be exposed to large refinancing risk and arrange lending with assurance of optimised risk-adjusted profitability. This gives rise to foreign exchange risk and structural interest risk due to mismatches in the Bank's assets and liabilities in terms of currency composition, maturity profile and interest rate characteristics.

The Bank's security portfolio held for liquidity purposes is exposed to interest rate risk and credit spread risk, for example potential decline in market value due to perceived change in credit quality of the issuers of the securities held in the portfolio.

NLB as the parent bank is the only member of NLB Group, which has a trading book according to the CRR. The bank maintains a small-size trading portfolio allocated to the position management for the purpose of achieving the additional earnings and monitoring market signals in the global markets. The Bank's tolerance for interest rate risk and credit spread risk in the trading portfolio is low.

## **Structure and organisation**

Financial Markets (Trading, Treasury and ALM) and Investment Banking and Custody together with Global Risk and Evaluation and Control manage market risk in NLB Group. Investment Banking and Custody is responsible for customer sales, Financial Markets is responsible for short- and long-term funding activities and investments for NLB Group's own account, for asset and liability management, liquidity portfolio collateral account portfolios as well as other banking activities. These Business Lines are responsible for managing the risk under the framework (principally through limits) as set by the Management Board and controlled by the ALCO.

NLB Group Market Risk Management operates under the three lines of defence framework as described in chapter 4.1 (General information on risk management, objectives and policies).

In order to effectively manage NLB Group's market risks, the organisational structure allows to clearly distinct between market risk methods and risk models, valuations and reporting. Market Risk is organised in following units:

- Global Risk, responsible for defining rules on risk appetite, Global Standards and Policies and for the financial risk reporting coherence and coordination across the Group, as well as development of the ICAAP/ILAAP.
- Market and Liquidity Unit of Global Risk, responsible for governing and checking the Group's market and liquidity risk, parameterisation of the internal VaR limit system, calculation of capital requirement for the trading book position, improvements and development of methodologies, as well as for internal and regulatory stress testing and reporting to senior management and external reporting for regulatory purposes.
- Control and Evaluation, responsible for monitoring trading activities and its compliance, designing stop-loss limits, controlling credit counterparty exposures and evaluating the financial instruments and additional valuation adjustments for managerial P/L.

The key responsibility of Global Risk is overseeing and controlling Group Market Risk through the assessment of strategies, policies and the proposal of relevant risk limits and regulation. The department manages a coordination of the market risk operations of the banking subsidiaries, according to NLB Group Risk Management Standards and integrates the risk culture throughout the Group. Additionally, it formulates and modifies Group Methodologies and Market Risk Measurement Framework and takes into account the recommendations of regulators and the market best practices. The department ensures compliance of the market risk management with applicable laws and regulations.

The existing organisational structure assures a functional capability of governance, alignment and monitoring market risk activities at an integrated portfolio level with dedicated and specialised risk managers and thus contributes to bring management processes in line with the best international practices.

Global Risk provides independent oversight of all significant market risks, supporting the Risk Committee, the ALCO and the Financial Markets with risk measurement, analysis, daily monitoring and reporting.

## **Risk measurement and control**

The Management Board of NLB bank sets strategic objectives for exposing to market risk, which is aligned with the risk appetite and intended to create value for shareholders and holding an adequate level of capital related to market risk. There are two committees responsible for market risk, namely the Group ALCO and the Risk Committee.

The Group ALCO monitors and addresses risk profile and area of asset and liability of NLB Group. It is engaged in monitoring and analysing the developments in the global markets, changes and trends associated with the risk profile, balance sheet structure and financial statements of NLB Group, and formulating conclusions and guidance to achieve target balance sheet structure.

The Committee's key objectives are defining and monitoring implementation of NLB Group policies related to risk management and balance sheet, defining methodologies and limits for interest rate risk in banking book, liquidity risk, foreign currency risk, transfer pricing, Funding Plan and Contingency Funding Plan. The Group ALCO also discusses the profitability of security portfolios and other activities in the area of treasury and investment banking. Further, the Committee ensures the alignment of practices and methodologies of NLB subsidiaries to NLB Group best practices in the respective areas and targets to optimise the liquidity and capital management aligned with Group Business Strategy and Risk Appetite.

The Risk Committee is responsible for advising on a general and future risk-taking and regarding a risk strategy. It supports a supervisory function on the top management related to the implementation of the risk strategy, reviewing the remuneration and incentives whether they are linked to the risk, capital and liquidity and checking whether the product pricing is aligned with the business model and risk strategy of the bank.

As regards the trading activities, the most significant market risks identified are interest rate risk (together with basis risk), credit spread risk and foreign exchange risk. Market risk from trading activities is managed and monitored daily within the trading market risk framework which includes all derivative book and bond trading book. A prudent limit and control structure is in use. Market risk is guided by separate policies and methodologies, such as the Trading Book Market Risk Policy, the IRRBB Policy and the FX Risk Policy.

Proper control is exercised over all elements in the process of market risk measurement and monitoring, including collection and delivery of data about positions, market factors, key preconditions, calculation of risk amount and reporting of risk exposure via appropriate chains of rights and responsibilities.

In relation to the market risk framework, several key risk metrics complimentary to each other are reported in order to measure and monitor businesses:

- Market risk models for limit setting: value at risk (VaR), stressed value at risk (CVaR) and basis point value approach (BPV) for a trading book.
- Stress testing: portfolio stress testing and event risk scenarios.
- Other market metrics: sensitivities.

The impact of larger market disruptions on the portfolio's present value is quantified by stress testing. The scenarios used are calibrated to historically observed market data and defined by hypothetical but plausible parameter changes. Scenario analyses are performed for interest rate, FX rates, credit spread and share price. Daily backtesting is employed to identify and analyse the potential exceedance of the value at risk.

To manage market risk, the internal limits are set that correspond to NLB Group Risk Profile and thereby prevent market risk from exceeding our ability to withstand losses based on our financial strength represented by capital. The risk appetite towards market risk is low.

The amount of market risk in the trading book is limited by a value at risk (VaR) that may arise in order to close relevant positions. With the VaR model, the Bank seeks to approximate the changes in value the Bank's value would experience in response to changes in the underlying risk factors. VaR identifies the probability that losses will be greater than a pre-specified threshold level. The Bank estimates VaR with a variance-covariance method. The VaR measure is computed daily with a 10-day holding period at a 99% confidence level.

For banking activities, the position limits are based on interest rate sensitivity using basis point value approach (BPV). It assumes a parallel curve shift by 200 bps and NII sensitivity of 50 bps.

## **9.2. Policies for hedging or mitigating risk**

(Article 435.1 d of CRR)

NLB Group separately identifies, measures, monitors and controls market risk for banking and trading book. Hedges of positions are separated on these two books.

When hedging interest rate risk in the banking book, in the majority of cases, NLB Group applies hedge accounting principles. Within that process, NLB Group regularly measures hedge effectiveness of hedges on a monthly basis. Hedging in the banking book is well documented where a description is given of the reasons for hedging, description of the hedged risk, hedged items and derivatives, hedge accounting method (fair value hedge or cash flow hedge), method for measuring effectiveness of hedge and how the results of hedges are recognised in our accounting statements. The trading book items are directly recognised in the income statement. NLB Group has BPV, VaR and stop-loss limits in place and open positions are managed within those limits.

### **Data Management and Reporting**

The Evaluation and Control provides and maintains data quality in the front office system for market data in a trading book and utilises tools to control accuracy of report results. The Back Office provides and maintains data input and quality in reporting systems for market data in a banking book. Global Risk is

responsible for defining a reporting structure and calculation methodology. The bank uses a centralised system for providing market data.

Global Risk reports timely, accurate and material market risk data internally and externally. There is a close alignment with the front and middle office in order to assess market risk at the integral level. This overall view is essential to inform management discussions that seek alignment between portfolios and integrated risk appetite.

An adequate internal reporting system reflecting the Group's exposure to market risk consists of:

- Daily measurement and limit control of the market risk in a trading book (VaR, sensitivity, stop-loss limit and P/L reporting to Management),
- Weekly Report on the interest rate risk from the banking book,
- Comprehensive monthly and quarterly reports including Risk Reports and Stress Testing Results to Group ALCO and Supervisory Board and own funding requirements for market risk in the trading book and interest rate risk in the banking book,
- Stress testing.

External reporting is as follows:

- Capital requirements based on the standardised approach,
- Quarterly report to the regulators.

### **Own funds requirement for Market Risk**

Global Risk monitors exposures and addresses risk issues and concentrations of certain exposures under a specific Market Risk Standardised Approach (MRSA). MRSA is used to determine the regulatory capital charge for the market risk of the trading book as set out in CRR.

In the standardised approach for market risk arising from position risk involving interest rate risk and derivatives, the minimum capital requirement is expressed in terms of two separately calculated charges. The capital charge for specific risk is modelled to protect against adverse movements in the price of an individual security due to factors related to the individual issuer. The capital charge for a general market risk is designed to measure the risk of loss arising from the changes in the market. In the case of foreign currency risk, the methods involved include measuring the exposure in a single currency position and measuring the risk inherent in a bank's mix of long and short positions in different currencies. For the capital requirements due to general position risk at NLB Group, the maturity-based approach is used. Share price risk is not relevant for NLB Group.

Global Risk quarterly assesses and computes additional own fund requirements within Pillar II for market risk in a trading book (ICAAP). It is computed for a position risk of debt securities and shares. The purpose of an ICAAP is to determine the adequate capitalisation of the bank, given the risks endured as well as future risks arising from growth, new markets and expansion of the product portfolio.

### **Compliance with the Article 104 of CRR regarding Inclusion in the Trading Book**

Compliance with an Article 104 of the CRR is ensured by appropriate policies and is regularly reviewed. The definition of the trading book is included in the Separation of Trading and Banking Book Policy.

### **Trading Book**

The Trading Book includes the positions in financial instruments held either with trading intent or in order to hedge other elements of the Trading Book itself. Trade separation to the banking and trading book is done on the basis of the content. The risk that the value of a financial instrument changes over time is determined by the following standard market risk factors: credit spreads, equity risk, interest rate risk, foreign exchange risk.

### **Banking Book**

The main components of market risk in the Banking Book are:

- credit spread risk.
- interest rate risk.
- foreign currency risk.

More precisely, the different and complementary perspectives involve:

- Economic value (EVE) perspective.
- Earnings at Risk (EaR) perspective.

### **Compliance with the Article 105 of CRR regarding Prudent Valuation**

All trading positions are valued according to the prudent valuation specified in Article 105 of CRR. Valuation is done on real-time basis as well as via end of day procedures. Senior management is being briefed on regular basis as well. All procedures are standardised and well documented. The prudent valuation is set in the Financial Instruments Evaluation Methodology and other internal operational guides. Valuation adjustments are made where applicable (e.g. low liquid assets). On a daily level, different types of controls are performed to ensure that real-time data gathered for valuation purposes are appropriate.

## **10. Interest rate risk on positions not included in the trading book**

(Article 448 of CRR)

### **10.1. The nature of the interest rate risk and the key assumptions (including assumptions regarding loan prepayments and behaviour of non-maturity deposits), and frequency of measurement of the interest rate risk**

Interest rate risk in the Banking Book is measured and monitored within a framework of Interest rate risk management policy that establishes consistent methodologies, models, limit systems and controls. Group regularly measures interest rate risk exposure in banking book under various standardised and additional scenarios of changes in level and shape of interest rate yield curve and, furthermore, applies cash flow modelling approach for positions with uncertain maturity and behavioural options. The latter was upgraded in 2017 according to new Basel standards with renewal of Non-maturing deposits allocation methodology and with the introduction of methodology on treatment of positions with behavioural options.

The management of NLB Group's interest rate exposure is decentralised. Each member is responsible for its own interest rate risk policy, which includes limit system and is in line with local regulatory requirements as well as the parent Bank's guidelines and standards. NLB monitors the interest rate risk exposure on weekly basis and of individual member of NLB Group on a monthly basis in accordance with the Standards for Risk Management in NLB Group.

Interest rate risk exposure arises mainly from banking book positions, particularly in current low interest rate environment where Group records increased volume of fixed interest rate loans and long-term banking book securities on assets side and transformation from term to sight deposits on liability side.

### **10.2. The variation in earnings, economic value or other relevant measure used by the management for upward and downward rate shocks according to management's method for measuring the interest rate risk, broken down by currency**

Interest rate risk is the risk to the Group's capital and earnings arising from changes in market interest rates. Interest rate risk management of the Group includes all interest rate-sensitive on- and off-balance sheet assets and liabilities which are divided into trading and banking book according to regulatory standards. It takes into account the positions in each significant currency (EUR, USD, CHF and other). Interest rate risk management in the Group is adopted in accordance with conservative risk strategy and is based on general Basel standards and EBA guidelines.

Group is managing interest rate risk exposure through two main measures:

- Economic value sensitivity – using BPV method (Basis Point Value), which measures the extent to which the value of the portfolio would change if interest rates changes according to the scenario.
- Sensitivity of net interest income – using EaR method (Earnings at Risk), which measures the impact of the interest rate change on future net interest income over a one-year period, assuming constant balance sheet volume and structure.

The Group manages interest rate positions and stabilises its interest rate margin through an appropriate pricing policy and a fund transfer pricing policy. An important part of managing interest rate risk is also the securities portfolio of the banking book, whose primary purpose is to maintain adequate liquidity reserves, while it also contributes to the stability of the interest rate margin, which is why a valuation risk has been included in the Group's interest rate risk management model. The Group also manages risk by using plain vanilla derivative financial instruments (interest rate swaps, overnight index swaps, cross currency swaps and forward rate agreements), most of which are treated according to hedge accounting.

## 11. Equity holdings not in the trading book

(Article 447 of CRR)

Group's non-trading book equity holdings primarily consist of available-for-sale assets of which the main part represents the National Resolution Fund which was funded and is controlled by the Bank of Slovenia in accordance with the Bank Authority and Fund Act (ZOSRB).

Table 41 – Equity holdings not in the trading book

		31.12.2017	31.12.2016
1	Investments in associates and joint ventures	12,359	16,024
2	Non-current assets classified as held for sale	2,123	-
3	Equity investments - available-for-sale	53,184	73,620
3a	of which: National Resolution Fund	44,514	44,570
4	<b>Total</b>	<b>67,666</b>	<b>89,644</b>

### *Accounting treatment and valuation*

NLB Group's exposure to available-for-sale equity securities has a balance sheet value of EUR 53,184 thousand (2016: EUR 73,620 thousand) of which quoted on active market amounted to EUR 3,598 thousand (2016: EUR 24,312 thousand).

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. At the subsequent measurements, equity investments are measured at fair value. The fair value of financial instruments traded on active markets is based on the price that would be received at the sale of the assets, excluding transaction costs. If there is no active market, the fair value of the instruments is estimated using discounted cash flow techniques or pricing models.

In the consolidated financial statements, investments in associates and joint ventures are accounted for using the equity method of accounting. NLB classified the subsidiary NLB Nov Penziski Fond, Skopje as the disposal group held for sale, due to its expected sale. In March 2018, NLB Group sold its subsidiary NLB Nov Penziski Fond, Skopje and realised profit in amount of EUR 12 million on NLB Group and EUR 9 million on NLB.

By selling equity securities available for sale, NLB Group realised a net gain in the amount of EUR 9,964 thousand (2016: EUR 13,478 thousand). Unrealised gains and losses on equities in amount of EUR 3,735 thousand (2016: EUR 11,017 thousand) were fully recognised in CET1 for 2017.

## 12. Liquidity risk management – goals and principles of Risk management

(Article 435.1 of CRR)

### **Liquidity Risk Management Framework**

Liquidity Risk Management is considered as one of the most important risk and consequently managed very deliberately. Liquidity Risk Management of the Group is defined as the capacity to meet its cash and obligations without incurring potential losses that are not aligned with risk appetite. Adequate liquidity is dependent upon the Group's ability to efficiently meet both expected and unexpected cash flows and collateral needs without adversely affecting daily operations and the financial position of the Group. The primary role of liquidity risk management is to assess the need for funds to meet obligations and ensure the availability of cash or collateral to fulfil those needs on time by coordinating the various sources of funds available to the Group under normal and stressed conditions.

Liquidity risk is related to funding liquidity risk (the Group's liquidity on the liabilities side) and market liquidity risk (liquidity reserves on the assets side). On the liabilities side, liquidity risk can result in a loss if the Group is unable to settle all of its liabilities or when the bank, because of its incapacity to provide sufficient funds to settle its obligations, is forced to provide the necessary funds at a cost which significantly exceeds the normal cost. On the assets side, the liquidity risk is related to the market value of liquidity reserves and arises in the case of significant reduction of market value of an individual financial instrument and may result in insufficient value of liquidity reserves to cover the Bank's liquidity needs.

### **Strategies and processes in the management of liquidity risk**

The Group has set up a sound Liquidity Risk Management Framework which enabled a reliable process for identifying, measuring, monitoring and controlling liquidity risk in the short and long-term period. The Group defined the risk appetite towards liquidity risk wherein the tolerance was determined as low. It is in line with

the Group's business strategy and aligned with the most important strategic business, financial and risk objectives.

The Group identified key liquidity risk drivers, set limit system framework, liquidity score, designed liquidity stress testing scenarios, prepared contingency funding plan, set determination of appropriate level of liquidity buffer. The Group has active strategies and clearly defined measurable tolerances to manage liquidity and funding risk, which were established through the Liquidity Risk Management Policy.

Further, the Group defines liquidity risk tolerance with several indicators such as LCR, NSFR and LTD. The respective risk bearing capacity is accordingly taken into account in Group's daily operations and in financial planning activities.

The goal of the Group is that it fulfils the regulatory liquidity requirements at any point of time. In this regard, the Group focuses on exceeding short-term liquidity disruptions (LCR) and exceeding a stable funding profile in relation to the composition of assets and off-balance sheet activities (NSFR).

The LCR is designed to ensure that financial institutions have the necessary assets on hand to ride out short-term liquidity disruptions. The Group is required to hold an amount of highly liquid assets, such as cash and bonds equal to or greater than the potential outflow position over a 30-day period. Under the Basel regulation, an LCR of 100% is required since 2018.

The NSFR requires banks to maintain a stable funding profile in relation to the composition of assets and off-balance sheet activities. A sustainable funding structure is intended to reduce the probability that disruptions to the Group's regular sources of funding will erode its liquidity position in a way that would increase the risk of its failure and potentially lead to broader systemic stress.

Furthermore, the Group established the ILAAP process with the aim to ensure a robust management of liquidity risk and comprehensive internal liquidity adequacy assessment on a solo and consolidated level. The Group strategic guidelines for liquidity risk are aligned with the Risk Appetite and the Risk Strategy, while elaborated into more details in an internal liquidity policy. At the operational level it describes how liquidity management is executed, supported and controlled in the Group.

More detailed rules, limits, guidelines and competences related to risk management are defined in the individual internal guidelines, policies and rules on the level of the Group (for an example NLB Group Risk Management Standards) or on the level of each individual member of the Group.

Due to local specifics (macroeconomic conditions, requirements of the local regulation), some sets also include more detailed guidelines for bank members of the Group, but nevertheless all group members should follow the uniform key risk guidelines at the Group level established by the parent bank NLB.

As regards assuming and managing liquidity risk, the Group has rules and the system of responsibility specified in:

- Definition of the risk profile and risk appetite at the level of NLB Group,
- ILAAP process in NLB Group.
- Liquidity Risk Management Policy of NLB with appendixes,
- NLB Group Risk Management Standards and Guidelines for managing liquidity risk in NLB Group,
- Methodology of implementing the ICAAP process in NLB Group in the area of liquidity risk,
- Operating instructions and lists of work procedures in the Bank's liquidity management,
- Rules of Procedure of the Assets and Liabilities Committee of NLB Group,
- Assets and Liabilities Management Policy of NLB Group,
- Funds Transfer Pricing - manual.

### **Structure and organisation of the liquidity risk management function**

Liquidity governance is established in a way that enables reliable process for identifying, measuring, monitoring and controlling liquidity risk. Ensuring of appropriate volume of liquidity and the management of liquidity reserves in the Group is carried out in a decentralised manner, in accordance with the requirements of the local regulations and the applicable internal guidelines and policies inside the Group.

The Management Board is obliged to define the Group's risk appetite (risk profile of the Group) as a framework for the determination of the method of managing liquidity risk in the Group. The Management is also responsible for adopting of decisions in the area of liquidity management, ordinarily through

membership in and participation in the work of the ALCO. The Management Board is also responsible for the establishment of appropriate procedures for the measurement, management, supervision and reporting in the area of liquidity risk management.

There are two committees responsible for liquidity risk management of the Group: ALCO and Risk Committee. ALCO adopts decisions concerning liquidity risk management and provides guidelines, defines the structural and income criteria in order to ensure an adequate volume of liquid investments, sets up the basic criteria for the structure of bank sources, establishes internal control mechanisms in the field of liquidity risk management and analyses the findings of audit services in this area, approves and revises the Liquidity Risk Management Policies approves and revises the Contingency Funding Plan and ensures its implementation in the case of activation.

The Liquidity Risk in NLB Group is managed in several departments as follows:

- **Global Risk, Market and Liquidity Risk Unit** is responsible for setting liquidity risk appetite and risk capacity bearing, Liquidity Risk Management Framework by establishing policies, methodologies and limits on solo and consolidated level. Global Risk independently controls and measures liquidity risk, reports liquidity risk independently to senior management, Supervisory Board and regulators. Global Risk prepares ILAAP with other relevant departments, performs a set of liquidity stress tests, prepares static liquidity gaps, prepares Minimal Liquidity Standards of NLB Group and delegates implementation of methodologies in banking members etc.
- **Financial Markets, Assets & Liabilities Management (ALM) Unit** is responsible for adopting liquidity management decisions compliant with the policies and limits. ALM Unit is responsible for internal transfer pricing and long-term borrowings on the capital markets. ALM prepares dynamic liquidity projections and several simulations, taking care of the rational use of the Group's secondary liquidity reserves and regularly reports to ALCO.
- **Financial Markets, Trading and Treasury Unit** is responsible for managing debt securities portfolio, providing liquidity within a single day, derivatives for the needs of liquidity in a certain currency and placing liquidity surpluses on the interbank market, preparing Group's liquidity based on the plan of transactions and others.

### **Scope of nature of liquidity risk reporting and measurement systems**

The Group identifies and manages several liquidity risk types such as market liquidity risk, operational, structural and intraday liquidity risk, stressed liquidity risk, funding concentration risk and foreign exchange liquidity risk.

The Group implemented different tools for measuring liquidity risk in the form of maturity structures, stress tests, stability of sight deposits, liquidity projections of future cash flows, scoring model and other relevant indicators. Internal methodological approaches enable monitoring liquidity on the operating (including intraday liquidity) as well as the structural level, including the definition of a crisis plan and liquidity management in exceptional circumstances. Liquidity risk management is continuously reviewed and liquidity situation regularly evaluated.

The Group measures and manages its liquidity in three stages: current exposure and compliance, forward looking and stress testing and liquidity in exceptional circumstances. Overall assessment of liquidity position of the Group (including all three stages) is assessed in the ILAAP process.

Global Risk calculates a larger set of internal liquidity ratios on solo level for NLB on a monthly basis and reports them to the Assets and Liabilities Committee of the Group. Limits and warning levels are defined for each liquidity ratio, separately for core (banking members) and non-core members and for consolidated level. Global Risk in NLB as a parent bank determines internal liquidity ratios, limits and warning levels for other banking members. For other Group members internal liquidity ratios are monitored monthly and reported quarterly to the ALCO, including results on consolidated level. Reports on the liquidity risk management are submitted to senior management, ALCO, the Supervisory Board and regulators on a regular basis.

Global Risk reports liquidity risk such as:

- Monthly Reports to the ALCO (Calculations of internal liquidity ratios and monitoring results for other group members, Results of the Scoring Model, Results of Liquidity Reserves, Liquidity Gaps, Stressed Stability of Sight Deposits, Results of the Regular and Intraday Liquidity Stress Tests).
- Monthly Reports to the Central Bank (LCR, ALM metrics).
- Quarterly Reports to the ALCO and Supervisory Board.

- Quarterly Reports to the Central Bank (asset encumbrance, GLTDF indicator, NSFR ratio, liquidity ladder).

### **Policies for hedging and mitigating the liquidity risk and strategies and processes for monitoring the continuing effectiveness of hedges and mitigants**

The Group mitigates liquidity risk in a several ways such as planning liquidity needs for different periods, maintaining sufficient liquidity reserves, monitoring early warning indicators, performing stress testing and updating Contingency Funding Plan for an extreme circumstance.

Global Risk conducts liquidity stress tests and reverse stress tests on a monthly basis. The Group performs stress tests under three scenario types (market, idiosyncratic and combined) and five intensities.

Based on the stress tests, the minimum and optimum amount of unencumbered liquidity reserves is determined for each banking member that it has to hold in order to cover potential unexpected outflows.

The limits set are:

- minimum level of liquidity reserves equals outflows in two months of severe stress scenario
- optimum level of liquidity reserves equals outflows in three months of severe stress scenario.

In planning cash flows, the Group must consider several possible situations, scenarios, which have different impacts on the Bank's liquidity. The first projection of cash flows must be prepared in the so-called normal or current circumstances in which the Group operates and satisfies daily requirements for liquid funds (baseline scenario, assumptions used according to the budget). The second projection of cash flows is prepared on the basis of the first, basic projection, taking into account deterioration of current circumstances, less inflows and more outflows from the Group's operations are foreseen, as well as deteriorated situation in fund raising and negative effects of the debt securities' credit quality which represent the largest part of liquidity reserves, so-called moderate scenario. Furthermore, the Group prepares adverse scenarios, taking into account additional deterioration of liquidity situation of the Bank and future cash flows.

Dynamic liquidity projections are prepared monthly or, if necessary, more often. Static liquidity gaps are prepared by the Global Risk, Market and Liquidity Risk. Dynamic liquidity projections are prepared by the Financial Markets, Assets and Liabilities Management, namely it includes in the projection of cash flows also the real assumptions and information on new transactions from business plans and the known business events. The Assets and Liabilities Management presents the dynamic liquidity projections to the ALCO which then adopts the necessary decisions for successful management of the Bank's liquidity in the future, based on the presented results.

The Group has developed methodology for intraday liquidity stress testing in order to define minimum level of liquidity reserves that have to be held for intraday liquidity purposes.

The purpose of the Contingency Funding Plan is to establish guidelines for liquidity management in stressed circumstances. The objective of the Contingency Funding Plan is timely identification of potential problems, drafting proposals and finding resolutions for performing activities in stressed circumstances. Contingency Funding Plan is prepared on standalone basis, taking into account only liquidity stress of NLB. Each banking member of the Group has its own document describing potential funding sources and roles and responsibilities of units and decision-makers in times of stressed circumstances.

In early warning system (EWS), warning limits for liquidity indicators were defined for each banking member of the Group. The main goal of a warning limit is to prevent any exceeding in the future and to activate at an early stage a warning that a member is moving towards the limit. If a bank or banking member exceeds the limit this would result in a higher Liquidity Score of that bank, which is closely correlated with the Contingency Funding Plan activation. If the Contingency Funding Plan is activated there are detailed activities defined in the plan that would enable the bank or a member to restore its liquidity position. Additionally, Recovery Plan has been set up on the Group level, where detailed recovery options are defined and would enable the Group to recover from liquidity run-off shock back to normal business.

The Group maintains the appropriate level of liquidity reserves in the form of cash and other highly liquid and unencumbered assets that are available in a relatively short time. Liquidity reserves enable the settling of overdue liabilities within a predefined short period of stressed liquidity situation. Unencumbered assets represent liquidity buffer, which includes cash, money market placements, high quality debt securities and

ECB eligible loans. At the end of December 2017, the Group had 41.09% of unencumbered liquidity reserves in total assets (39.82% at the end of 2016).

Declaration of the management on the adequacy of liquidity risk arrangements and a liquidity risk statement approved by the management board associated with the business strategy are disclosed in Appendix 2 and Appendix 3.

### **Liquidity coverage ratio**

The liquidity coverage ratio (LCR) refers to highly liquid assets (HQLA), which consist of cash or assets that can be converted into cash at little or no loss of value in private markets to meet its liquidity needs for a 30-calendar day liquidity stress scenario. The LCR aims to protect the Group from runs by increasing the creditor's confidence in such a way to rely more on equity and less on debt. LCR may also reduce their maturity mismatches by means of extension in the liability maturities and the reduction of asset maturities. The minimum liquidity coverage is set at 100%.

### **Concentration of funding and liquidity sources**

In accordance with the Risk appetite statement of the Group tolerance for liquidity risk is low. Therefore, the goal of the funding strategy is to ensure a sufficient, stable and well-diversified funding base in the long term and compliance with relevant regulatory frameworks.

Funding strategy in NLB is established in a way that enables diversification, minimises concentration risk and limits the reliance on a short-term wholesale funding or other unstable sources. With the objective to efficiently manage liquidity and funding risk, the Group regularly performs stress tests and makes liquidity projections under different scenarios. With this approach the Group is able to early detect any potential liquidity and funding needs.

In accordance with the business model the primary source of funding of the Group represent non-banking sector deposits. The Group's deposit base is highly stable and diversified. Due to high importance of non-banking deposits in Group's funding, it is very important limiting high concentration. The desired diversification is achieved through the use of different instruments, including the application of limits by type of counterparty. Dependence on wholesale funding is low. The Group takes into consideration concentration of funding in order to have well diversified sources of funding and to prevent unwanted effects of concentration. For non-banking sector deposits as main funding sources of the Group, limit is set to prevent too high concentration of depositors.

Limits values are also set for other Group members and defined in the Group Risk Management Standards members must adopt limits values in their policy and comply with limits. Any deviations from limits values must be reported and justified to the parent bank. Funding structure is presented on ALCO on a monthly basis.

ALM metrics are prepared internally on solo and Group level. In terms of funding providers, product and assets in the counterbalancing are monthly monitored and reported to the Central Bank.

On the Group level, at the end of 2017, the top 30 counterparties provided 2.89% of total liabilities, mostly by retail, while top 30 counterparties in NLB provided 3.64% of total liabilities.

### **Derivative exposures and potential collateral calls**

The Group enters into the derivatives to support corporate customers and financial institutions in their management of financial exposures (sales business) and in order to manage the Group's risks such as interest rate risk and FX risk.

To mitigate risk arising from derivatives, the Group uses netting agreements such as ISDA Master Agreement, Global Master Repurchase Agreement (GMRA), and Slovene framework agreement. Further, collateral agreements (e.g. ISDA Credit Support Annex) are in place to substantially reduce credit risk arising out of derivatives transactions. Additionally, clearing transactions via clearing house is in place for relevant derivatives transactions. Daily margin call calculations are in place for each relevant counterparty. Portfolio reconciliation is agreed as per European Market Infrastructure Regulation (EMIR). NLB is calculating net positive market value for individual counterparty exposure on daily basis and as a result, collateral is being adjusted accordingly. Regarding the LCR, the CCR exposure from the derivatives is low and there are no significant outflows to be recorded.

## Currency mismatch in the LCR

Parent bank NLB actively manages liquidity risk exposures and funding needs within and across legal entities, business lines and currencies, taking into account legal, regulatory and operational limitation to the transferability of liquidity. Specific characteristics and liquidity risks of foreign exchange positions are taken into account, particularly when preparing the plan of cash flows by currency.

In the Group, there are no currency mismatches in the LCR. The LCR indicator is fulfilled in all currencies because the Group has enough liquidity reserves in all currencies where the outflows might happen. The most significant currency of the Group is euro currency. Besides, the Group also reports LCR in a second significant currency and that is the Macedonian denar (MKD). In the last quarter of 2017, the aggregate liabilities in MKD was 5.85% of total liabilities of the Group, therefore MKD is qualified as significant currency.

## A description of the degree of centralisation of liquidity management and interaction between the group's units

All core members of the Group (banking members) are self-funded. Intragroup funding is provided only to non-core members that are in the process of disinvestment. Liquidity risk management is decentralised under strict monitoring by NLB as a parent bank. Reporting to NLB by all group members is done on a daily and monthly basis.

## Other items in the LCR calculation that are not captured in the LCR disclosure table

The Group is focused on the retail banking activities therefore the structure of the balance sheet does not include any complex products. There are no other items in the LCR calculation that are not captured in the LCR disclosure table.

Liquidity of the bank is strong, volume of unencumbered liquidity reserves is at high level. The Global Risk view is, that liquidity position is strong and it will continue to maintain at high levels as also reflected in liquidity planning and cash flow forecasting.

Table 42 – LIQ1 – LCR disclosure table, on quantitative information of LCR which complements Article 435.1 f of CRR of NLB Group

Quarter ending on	Total unweighted value (average)				Total weighted value (average)				
	31.12.2017	30.9.2017	30.6.2017	31.3.2017	31.12.2017	30.9.2017	30.6.2017	31.3.2017	
<b>Number of data points used in the calculation of averages</b>	12	12	12	12	12	12	12	12	
<b>High-quality liquid assets</b>									
1	Total high-quality liquid assets (HQLA)	-	-	-	-	2,322,374	2,318,111	2,380,347	2,344,910
<b>Cash-outflows</b>									
2	Retail deposits and deposits from small business customers, of which:	6,381,155	6,120,144	5,965,424	5,844,199	464,845	444,888	432,626	422,729
3	<i>Stable deposits</i>	4,243,212	4,108,308	4,082,870	4,100,265	212,161	205,415	204,143	205,013
4	<i>Less stable deposits</i>	2,137,943	2,011,836	1,882,554	1,743,935	252,684	239,473	228,483	217,716
5	Unsecured wholesale funding	1,251,102	1,200,457	1,182,720	1,137,388	643,035	604,544	588,065	547,864
7	<i>Non-operational deposits (all counterparties)</i>	1,227,596	1,176,951	1,159,214	1,137,388	619,529	581,038	564,559	547,864
8	<i>Unsecured debt</i>	23,506	23,506	23,506	-	23,506	23,506	23,506	-
10	Additional requirements	1,100,042	1,103,184	1,129,226	1,164,867	91,889	97,451	109,968	128,039
11	<i>Outflows related to derivative exposures and other collateral requirements</i>	9,931	15,060	20,753	27,710	9,931	15,060	20,753	27,710
13	<i>Credit and liquidity facilities</i>	1,090,111	1,088,125	1,108,472	1,137,158	81,957	82,392	89,214	100,329
14	Other contractual funding obligations	31,058	36,072	41,787	44,044	19,671	24,124	20,525	10,716
15	Other contingent funding obligations	728,820	740,663	764,726	797,175	60,591	61,646	61,337	61,047
16	TOTAL CASH OUTFLOWS					1,280,030	1,232,652	1,212,520	1,170,395
<b>Cash-inflows</b>									
18	Inflows from fully performing exposures	627,599	591,103	595,044	622,438	473,566	448,849	459,373	490,532
19	Other cash inflows	23,940	25,638	26,508	24,986	23,940	25,638	26,508	24,986
EU-19b	(Excess inflows from a related specialised credit institution)	-	-	-	-	-	-	-	-
20	<b>TOTAL CASH INFLOWS</b>	<b>651,539</b>	<b>616,741</b>	<b>621,552</b>	<b>647,424</b>	<b>497,506</b>	<b>474,486</b>	<b>485,881</b>	<b>515,518</b>
EU-20c	<i>Inflows subject to 75% cap</i>	<b>651,539</b>	<b>616,741</b>	<b>621,552</b>	<b>647,424</b>	<b>497,506</b>	<b>474,486</b>	<b>485,881</b>	<b>485,881</b>
TOTAL ADJUSTED VALUE									
21	<b>LIQUIDITY BUFFER</b>	-	-	-	-	<b>2,322,374</b>	<b>2,318,111</b>	<b>2,380,347</b>	<b>2,344,910</b>
22	<b>TOTAL NET CASH OUTFLOWS</b>	-	-	-	-	<b>782,524</b>	<b>758,166</b>	<b>726,639</b>	<b>654,877</b>
23	<b>LIQUIDITY COVERAGE RATIO (%)</b>	-	-	-	-	<b>301%</b>	<b>311%</b>	<b>337%</b>	<b>361%</b>

Table 43 – LIQ1 – LCR disclosure table, on quantitative information of LCR which complements Article 435.1 f of CRR of NLB

Quarter ending on	Total unweighted value (average)				Total weighted value (average)			
	31.12.2017	30.9.2017	30.6.2017	31.3.2017	31.12.2017	30.9.2017	30.6.2017	31.3.2017
<b>Number of data points used in the calculation of</b>	12	12	12	12	12	12	12	12
<b>High-quality liquid assets</b>								
1 Total high-quality liquid assets (HQLA)	-	-	-	-	2,169,728	2,171,685	2,231,134	2,192,072
<b>Cash-outflows</b>								
2 Retail deposits and deposits from small business customers, of which:								
3 <i>Stable deposits</i>	4,822,513	4,672,791	4,540,997	4,417,215	326,904	317,711	304,847	290,674
4 <i>Less stable deposits</i>	3,704,656	3,605,657	3,558,665	3,533,256	185,233	180,283	177,933	176,663
5 Unsecured wholesale funding	1,117,857	1,067,134	982,333	883,959	141,671	137,428	126,914	114,011
7 <i>Non-operational deposits (all counterparties)</i>	967,834	929,631	871,668	775,452	539,409	507,311	474,501	415,139
8 <i>Unsecured debt</i>	944,328	906,125	848,162	775,452	515,903	483,805	450,995	415,139
10 Additional requirements	23,506	23,506	23,506	-	23,506	23,506	23,506	-
11 <i>Outflows related to derivative exposures and other collateral requirements</i>	884,836	896,243	926,822	962,512	89,087	95,847	106,829	122,119
13 <i>Credit and liquidity facilities</i>	9,931	15,060	20,672	27,503	9,931	15,060	20,672	27,503
14 Other contractual funding obligations	874,904	881,184	906,150	935,008	79,155	80,787	86,157	94,616
15 Other contingent funding obligations	28,549	29,321	33,985	33,987	17,160	17,373	14,284	5,380
16 <b>TOTAL CASH OUTFLOWS</b>	495,159	510,338	535,286	559,938	26,665	28,219	30,101	31,800
<b>Cash-inflows</b>								
18 Inflows from fully performing exposures	999,223	966,460	930,563	865,112	999,223	966,460	930,563	865,112
19 Other cash inflows	384,343	359,802	348,054	348,960	274,872	260,122	255,033	260,557
EU-19b (Excess inflows from a related specialised credit institution)	23,937	25,638	26,508	24,986	23,937	25,638	26,508	24,986
20 <b>TOTAL CASH INFLOWS</b>	408,281	385,440	374,563	373,946	298,810	285,759	281,542	285,544
EU-20c <i>Inflows subject to 75% cap</i>	408,281	385,440	374,563	373,946	298,810	285,759	281,542	285,544
	TOTAL ADJUSTED VALUE							
21 <b>LIQUIDITY BUFFER</b>	-	-	-	-	2,169,728	2,171,685	2,231,134	2,192,072
22 <b>TOTAL NET CASH OUTFLOWS</b>	-	-	-	-	700,414	680,701	649,022	579,569
23 <b>LIQUIDITY COVERAGE RATIO (%)</b>	-	-	-	-	314%	324%	355%	383%

### 13. Leverage

(Article 451 of CRR)

The leverage ratio is calculated after January 2014 in line with the enforcement of provisions from the CRR and CRD, or as of January 2015 pursuant to the amendments in relation to the calculation published in Commission Delegated Regulation (EU) No. 2015/62. As of 1 January 2015, the additional requirement to disclose information concerning the leverage is in force. In February 2016 Regulation (EU) No. 2016/200 was adopted, laying down implementing technical guidance with regard to disclosure of the leverage ratio. In March 2016, the Implementing Regulation (EU) No. 2016/428 was adopted, setting out guidelines for supervisory reporting of the leverage ratio.

The leverage ratio was introduced into the Basel III framework as a simple, transparent, non-risk based supplementary measure to the risk-based capital requirements. The purpose of the leverage ratio is to limit the size of bank balance sheets with a special emphasis on exposures which are not weighted within the framework of the existing capital requirement calculations. Therefore, the leverage calculation uses Tier 1 as the numerator, and the denominator is the total exposure of all active balance sheet and off-balance-sheet items after the adjustments are made, in the context of which the exposures from individual derivatives, exposures from transactions of security funding and other off-balance sheet items are especially pointed out. According to the discretionary right of the Bank of Slovenia and the changes to the calculation brought about by Commission Delegated Regulation (EU) 2015/62, the leverage ratio in the transition period is calculated quarterly and not based on the simple arithmetic mean of monthly leverage ratios for the quarter.

The leverage ratio of NLB Group, amounted to 9.70% (transitional) or 9.90% (fully phased in) and is above the 3% threshold defined by the Basel Committee on Banking Supervision (BCBS). In the so-called transitional period from 1 January 2014 to end of 2017, the leverage ratio is monitored together with its constituent parts and its interaction. As of 1 January 2018, the leverage ratio become one of the binding minimum capital requirements.

Since the minimum requirement was exceeded so significantly, the risk of excessive leverage is not material. Leverage risk is assessed and monitored quarterly as part of the ICAAP process and monitored in the context of the system of early warning regarding risk indicators. In this monitoring system, the leverage ratio has set certain limits, or as well as in the case of any exceeding of defined triggers and the defined notification system. The leverage ratio is regularly, quarterly monitored and reported to ALCO, and the Management Board and Supervisory board of NLB. The monitoring of excess leverage is also included in stress tests and recovery plan measures if and whenever a bank would be required to maintain an adequate capital level. The testing for any case of extraordinary circumstances is especially important as it is future-oriented: if the leverage ratio also remains stable in extraordinary, stress conditions, the risk of a forced decrease in the Bank's assets is low.

Leverage ratio calculated according to the transitional definition as at 31 December 2017 amounted to 9.70%, and slightly increased by 0.02 percentage points compared to the previous year. The increase occurred primarily due to the higher value of the total leverage exposure calculated in accordance with Article 111 of the CRR by EUR 240 million. The higher amount of total leverage exposure arose from increased on-balance sheet exposures especially banking book exposures such as retail exposures, exposures secured by immovable properties and sovereign exposures, while amounts of derivative and off-balance sheet exposures was decreasing in comparison with the previous year. The impact of capital decrease on the leverage ratio was relatively minor (EUR 26 million).

As at 31 December 2017, the leverage exposure was mainly driven by on-balance sheet exposures (96.5%), and other off-balance sheet exposure (3.4%), the rest was exposure from derivatives which is not significant. Among on-balance sheet exposures the most significant were Retail exposures (25%), exposures treated as Sovereigns (23%), exposures to Corporates (17%) and 16% to Other exposures.

Table 44 – Leverage ratio of NLB Group

	31.12.2017		31.12.2016	
	Transitional definition	Fully phased in definition	Transitional definition	Fully phased in definition
Tier 1 capital	1,362,140	1,390,579	1,336,241	1,360,388
Total leverage exposures	14,044,985	14,044,985	13,804,603	13,802,595
<b>Leverage ratio</b>	<b>9.70%</b>	<b>9.90%</b>	<b>9.68%</b>	<b>9.86%</b>

Table 45 – LRCom - Leverage ratio common disclosure

	31.12.2017		31.12.2016	
	CRR leverage ratio exposures			
<b>On-balance sheet exposures (excluding derivatives and SFTs)</b>				
1 On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	13,584,533	13,584,533	13,284,338	13,284,338
2 (Asset amounts deducted in determining Tier 1 capital)	(37,363)	(37,363)	(39,152)	(41,160)
<b>3 Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)</b>	<b>13,547,170</b>	<b>13,547,170</b>	<b>13,245,186</b>	<b>13,243,178</b>
<b>Derivative exposures</b>				
4 Replacement cost associated with <i>all</i> derivatives transactions (ie net of eligible cash variation margin)	14,212	14,212	19,153	19,153
5 Add-on amounts for PFE associated with <i>all</i> derivatives transactions (mark-to-market method)	22,719	22,719	11,755	11,755
7 (Deductions of receivables assets for cash variation margin provided in derivatives transactions)	(2,229)	(2,229)	-	-
8 (Exempted CCP leg of client-cleared trade exposures)	(11,831)	(11,831)	-	-
<b>11 Total derivative exposures</b>	<b>22,871</b>	<b>22,871</b>	<b>27,985</b>	<b>27,985</b>
<b>Securities financing transaction exposures</b>				
<b>16 Total securities financing transaction exposures</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Other off-balance sheet exposures</b>				
17 Off-balance sheet exposures at gross notional amount	1,890,516	1,890,516	1,851,195	1,851,195
18 (Adjustments for conversion to credit equivalent amounts)	(1,415,572)	(1,415,572)	(1,319,763)	(1,319,763)
<b>19 Other off-balance sheet exposures</b>	<b>474,944</b>	<b>474,944</b>	<b>531,432</b>	<b>531,432</b>
<b>Exempted exposures in accordance with CRR Article 429 (7) and (14) (on and off balance sheet)</b>				
<b>Capital and total exposures</b>				
20 Tier 1 capital	1,362,140	1,390,579	1,336,241	1,360,388
<b>21 Total leverage ratio exposures</b>	<b>14,044,985</b>	<b>14,044,985</b>	<b>13,804,603</b>	<b>13,802,595</b>
<b>Leverage ratio</b>	<b>9.70%</b>	<b>9.90%</b>	<b>9.68%</b>	<b>9.86%</b>
<b>Choice of transitional arrangements and amount of derecognised fiduciary items</b>				
EU-23 Choice on transitional arrangements for the definition of the capital measure	Transitional	Fully phased in	Transitional	Fully phased in

Table 46 – LRSum – Summary reconciliation of accounting assets and leverage ratio exposures

LRSum: Summary reconciliation of accounting assets and leverage ratio exposures		31.12.2017	31.12.2016
1	<b>Total assets as per published financial statements</b>	<b>12,237,745</b>	<b>12,005,712</b>
2	Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	(36,806)	(33,299)
4	Adjustments for derivative financial instruments	8,659	8,832
6	Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	474,944	531,432
7	Other adjustments	1,360,443	1,291,926
8	<b>Leverage ratio total exposure measure</b>	<b>14,044,985</b>	<b>13,804,603</b>

Table 47 – LRSpl – Split-up of on balance sheet exposures

		31.12.2017	31.12.2016
		<b>CRR leverage ratio exposures</b>	<b>CRR leverage ratio exposures</b>
<b>EU-1</b>	<b>Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:</b>	<b>13,584,533</b>	<b>13,284,338</b>
EU-2	Trading book exposures	59,164	68,756
EU-3	Banking book exposures, of which:	13,525,369	13,215,582
EU-4	Covered bonds	89,191	50,418
EU-5	Exposures treated as sovereigns	3,060,144	2,906,237
EU-6	Exposures to regional governments, MDB, international organisations and PSE <b>not</b> treated as sovereigns	253,401	276,523
EU-7	Institutions	1,265,587	1,299,266
EU-8	Secured by mortgages of immovable properties	697,134	579,765
EU-9	Retail exposures	3,410,857	3,121,571
EU-10	Corporate	2,240,627	2,419,208
EU-11	Exposures in default	297,000	450,108
EU-12	Other exposures (eg equity, securitisations, and other non-credit obligation assets)	2,211,428	2,112,486

## 14. Operational risk management

(Article 446 of CRR)

### 14.1. Approaches for the assessment of own funds requirements for operational risk

The capital requirement for operational risk is calculated using the basic indicator approach at NLB Group level and using the standardised approach at the NLB level.

### 14.2. Description of other internal approaches and methodologies in the area of operational risk

When assuming operational risks, NLB Group follows the guideline that such risks may not materially impact its operations and, therefore, the risk appetite for operational risks is low to moderate. Currently, the complexity of NLB Group operations is on a moderate level, although it is constantly reducing through the divestment of non-core activities. The Group has set up a system of collecting loss events, identification, assessment, and management of operational risks, all with the aim of ensuring quality management of operational risks.

All core members of NLB Group monitor the upper limit of tolerance to operational risk, defined as the limit amount of net loss that an individual member still allows in its operations. If the sum of net loss exceeds the tolerance limit, a special treatment of major loss events is required and, if necessary, taking of additional measures for the prevention of the same or similar loss events. The critical limit of loss events is also defined, representing the limit above which the member considers a possible increase in the capital requirement for operational risk within ICAAP and other possible risk management measures. The key risk indicators are regularly monitored (at least quarterly) within NLB Group's Risk Profile. In addition, the Bank has developed special methodology for monitoring key risk indicators, which could indicate increasing of operational risk. Indicators are defined at the level of the Bank.

As the highest authority in the area of operational risk management, NLB appointed an Operational Risk Committee. Relevant operational risk committees were also appointed at other NLB Group banking members. The management board serves in this role at other subsidiaries. The main task of the aforementioned bodies is to discuss the most significant operational risks and loss events, and to monitor and support the effective management of operational risks within an individual entity. All NLB Group entities included in the consolidation have adopted relevant documents that are in line with NLB Group Risk management standards. In core members, these documents are in line with the development of operational

risk management and regularly updated. The whole NLB Group uses uniform software support, which is also regularly upgraded.

In NLB Group, the reported incurred net loss arising from loss events in 2017 was lower than in the previous year, and represents a relatively small part of the capital requirement for operational risk. In general, considerable attention is paid to reporting loss events and defining operational risks in all segments. To treat major loss events appropriately and as soon as possible, the Bank has introduced an escalation scale for reporting loss events to the top levels of decision-making at NLB and the Supervisory Board of NLB. Additional attention is paid to the reporting of potential loss events in order to improve the internal controls, and thus minimise those and similar events.

Through comprehensive identification of operational risks, possible future losses are identified, estimated, and appropriately managed. The major operational risks are actively managed with the measures taken to reduce them. An operational risk profile is prepared once a year on the basis of the operational risk identification. Special emphasis is put on the most topical risks, among which in particular are those with a low probability of occurrence and very high potential financial influence. For this purpose the Bank has developed the methodology of stress testing for operational risk. The methodology is a combination of modelling loss event data and scenario analysis for exceptional, but plausible events. Scenario analysis are made based on experience and knowledge of experts from various critical areas.

## 15. Remuneration policy

### 15.1. Information on the decision-making process used for determining the Remuneration Policy, as well as the number of meetings held by the main body overseeing remuneration during the financial year, including, if applicable, information about the composition and the mandate of a remuneration committee, the external consultant whose services have been used for the determination of the remuneration policy and the role of the relevant stakeholders

(Article 450.1 a of CRR)

In compliance with the ZBan-2, the Regulation on Internal Management Arrangements, Management Body and Internal Capital Adequacy Assessment Process for Banks and Savings Banks and the Regulation of the Bank of Slovenia on the application of the Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of CRR, the Bank is obliged to enforce the Remuneration Policy for the employees performing special work at the level of NLB and NLB Group. The Policy of Remuneration for the Employees Performing Special Work (hereinafter: the Remuneration Policy) entered into force on 1 January 2012. The Policy is regularly revised and aligned, in compliance with the requirements of the abovementioned regulations, the relevant guidelines, the Slovenian Corporate Governance Code for Joint-Stock Companies and the Corporate Governance Code for Companies with a State Capital Investment. The Policy was partly revamped in 2017 in terms of alignment with the guidelines of the EBA and will be adopted by the end of the first quarter 2018 by the competent bodies of the Bank.

The Remuneration Policy regulates the remuneration of employees performing special work, i.e. those who can significantly impact the risk profile of the Bank in the scope of their tasks and activities. Through the system of governance and supervision of NLB Group the Remuneration policy, as described in the continuation, is also implemented at the level of all NLB Group members, in compliance with the local legislation and other regulation (i.e. restrictions imposed on NLB according to the Act Governing the Remuneration of Managers of Companies with Majority Ownership held by the Republic of Slovenia or Self-Governing Local Communities (ZPPOGD)).

The decision-making process about the formulation, amendments and supplements to the Remuneration Policy involves the expert services, the Management Board, the Remuneration Committee and the Supervisory Board of NLB, whereby the latter also approves the Remuneration Policy. No external consultant was engaged in the formulation, preparation or implementation of the Remuneration Policy.

**The Remuneration Committee of the Supervisory Board of NLB** held four meetings in 2017. The members of the Remuneration Committee were replaced in 2017 as follows:

- until 7 April 2017:
  - Uroš Ivanc, Chair
  - Matjaž Titan, Deputy Chair
  - David Kastelic, Member

- David E. Simon, Member
- from 7 April 2017 to 11 May 2017:
  - Matjaž Titan, Deputy Chair (until 21 April 2017)
  - David Kastelic, Member
  - David E. Simon, Member
- from 11 May 2017 to 6 October 2017:
  - Primož Karpe, Chair
  - David Kastelic, Deputy Chair (until 8 September 2017)
  - Andreas Klingen, Member
  - David E. Simon, Member
- from 6 October 2017 onwards:
  - Vida Šeme Hočevar, Chair
  - Simona Kozjek, Deputy Chair
  - Primož Karpe, Member
  - László Urbán, Member

Pursuant to Article 52 of the ZBan-2 the **Remuneration Committee** discharges the following duties:

- preparing proposals of general principles of remuneration policies, including the formulating of opinions on individual aspects of remuneration policies;
- assessing the adequacy of established methodologies, based on which the remuneration system promotes adequate risk, capital and liquidity management;
- preparing recommendations for the Supervisory Board on implementation of remuneration policies;
- preparing draft decisions about remuneration of employees, including those affecting the Bank's risks and their management;
- assessing the appropriateness of the external consultant whose services the Supervisory Board commissioned to determine the remuneration policy of the Bank;
- examining the adequacy of general principles of the remuneration policies and their implementation;
- examining the compliance of remuneration policies with the business policy of the Bank over a long period;
- direct supervision over remuneration of the categories of employees performing special work within the internal control system and other control functions.

## 15.2. Information on the link between pay and performance (Article 450.1 b of CRR)

The Remuneration Policy provides clear orientations for prudent remuneration of employees performing special work in accordance with the above regulations and with the aim of ensuring prudent and efficient risk management.

The Remuneration Policy supports the business strategy of the Bank as well as its goals, organisational culture and long-term interests. The Remuneration Policy does not stimulate the employees performing special work to assume non-proportionally high risks or risks that exceed the ability of the Bank to assume risks. The Bank ensures pursuing of this goal with an appropriate structure, amount and method of payment of remuneration.

In terms of payment of the variable part of the salary, the Remuneration Policy takes into account the fulfilment of obligations or achievement of goals referring to capital or liquidity. Variable remuneration of the employees performing special work in the Bank is additionally limited in line with NLB's commitments for the restructuring period from 2013 to 31 December 2017.<sup>1</sup>

The Remuneration Policy applies to the Management Board of the Bank<sup>2</sup>, senior management and other employees performing special work in the Bank who have service contracts or conclude transactions that affect the Bank's risk profile.

<sup>1</sup> Commission Decision of 18/12/2013 on state aid SA.33229 (2012/C) (ex 2011/N) – Restructuring of NLB.

<sup>2</sup> During the validity of the Act Regulating the Incomes of Managers of Companies Owned by the Republic of Slovenia and Municipalities (ZPPOGD), the remunerations of the President and Members of the Management Board of NLB d.d. are regulated in compliance with the abovementioned Act.

The following financial and non-financial performance criteria are defined every year for assessing the performance of employees performing special work. The financial criteria consist of the goals of NLB that are approved by the Supervisory Board every year and apply to all employees performing special work. The performance criteria for employees performing special work who are included in the supervisory function are established on the basis of the goals of the supervisory function and are independent from the efficiency of the organisational work they supervise.

Table 48 shows the variations in the payment of the variable part which depend on the achievement of the goals by the employees performing special work, and the amount of variable part to which employees performing special work are entitled in case the following are achieved:

- goals of NLB,
- goals of the relevant OU or
- personal goals of the employee performing special work.

Table 48 – Presentation of possible variants for payment of variable part

Performance criterion	Achieved or exceeded goals	Achieved or exceeded goals			
1. Goals of the NLB Group (for the Management Board) and/or NLB	yes	no	yes	no	yes/no
2. OU goals	yes	yes	no	no	yes/no
3. Personal goals	yes	yes	yes	yes	no
Entitlement to the variable part of salary	yes	yes	yes	yes	no
Amount of the variable part of salary arising from:	For the Management Board and the front offices:	For the Management Board and the front offices:	For the Management Board and the front offices:	For the Management Board and the front offices:	
- the goals of the NLB Group/NLB d.d.	up to 2 salaries +	up to 2 salaries +	up to 2 salaries +	up to 1 salary	No payment of the variable part
- the goals of the OU	up to 2 salaries +	up to 1 salary	up to 1 salary	up to 1 salary	
- personal goals	up to 1 salary				
	= up to 5 salaries in total	= up to 3 salaries in total	= up to 3 salaries in total	= up to 1 salary in total	
Amount of the variable part of salary arising from:	For other employees:	For other employees:	For other employees:	For other employees:	
- the goals of the NLB Group/NLB d.d.	up to 1 salary +	up to 1 salary +	up to 1 salary +	up to 1 salary	No payment of the variable part
- the goals of the OU	up to 1 salary +	up to 1 salary	up to 1 salary	up to 1 salary	
- personal goals	up to 1 salary				
	= up to 3 salaries in total	= up to 2 salaries in total	= up to 2 salaries in total	= up to 1 salary in total	

Table 49 defines the maximum possible remuneration of an employee based on the assessment of achievement of individual goal.

Table 49 – Definition of the amount of remuneration

Assessment of performance	Front office	Other than front office	Front office and other
	Goals of the NLB and goals of the OU	Goals of the NLB and goals of the OU	Personal goals
5 – all goals exceeded	up to 2 salaries	up to 1 salary	up to 1 salary
4 – most of the goals exceeded	up to 1.5 salary	up to 0.75 salary	up to 0.75 salary
3 – goals achieved	up to 1 salary	up to 0.5 salary	up to 0.5 salary
2 – goals partly not achieved	-	-	-
1 – goals not achieved	-	-	-

The Remuneration Policy stipulates that a decision on whether the performance criteria have been achieved and the decision to pay the annual variable part of salary to the Management Board members are adopted by the Supervisory Board, whereas for other employees performing special work they are adopted by the Bank's Management Board. An employee is not entitled to the annual variable part of salary if they fail to achieve their personal goals, regardless of whether or not the goals the Bank and the OU have been achieved.

When assessing the performance of the Management Board and when determining the scores, the Supervisory Board may take into account the interim situation on the banking and economic market and assess the Management Board's achievement of goals considering its activities aimed at pursuing the Bank's best interest.

For 2017, employees performing special work received the annual variable part of the salary, the amount of which depended on their assessed achievement of the financial and non-financial performance criteria and on the duration of the term of office of each employee performing special work.

### **15.3. The essential components of the policy of remuneration for employees performing special work** (Article 450.1 c of CRR)

The Remuneration Policy promotes prudent and effective risk management.

The salary of the employees performing special work is composed of:

- a fixed part of the salary, and
- a variable part of the salary which depends on the following:
  - performance of NLB Group (for the Management Board) and NLB (for other employees performing special work),
  - performance of the OU of the employee performing special work,
  - individual performance of employee performing special work.

Performance of employees performing special work is measured using special financial (quantitative) and non-financial (qualitative) performance criteria that must be included in at least one of the abovementioned groups of goals.

Annual interviews are held with employees performing special work, where the expected results or goals are defined for every employee based on the NLB Strategy, the goals of NLB as well as its development and project goals.

#### **Goals of NLB and NLB Group**

The Management Board sets the goals of NLB and NLB Group for each business year and the Supervisory Board approves them. The goals that are set for NLB Group also apply to the Management Board. The goals that are set for NLB also apply to other employees performing special work.

The maximum possible amount of the variable part of the salary, subject to achievement of NLB or NLB Group goals, are two salaries for the Management Board and employees performing special work who are included in the business function, and one salary for other employees performing special work.

The definition of NLB Group goals is based on the financial and non-financial performance indicators. The 2017 indicators were as follows:

- Financial performance indicators (achievement of the planned values):
  - Net profit after tax
  - Return on equity (ROE) after tax
  - Total revenues
  - Total costs
  - Cost/Income Ratio (CIR)
  - Net cost of risk<sup>3</sup>
- Non-financial indicators:
  - Achievement of the planned value of the share of non-performing exposures (NPE ratio according to the EBA definition)
  - Reduction in the volume of NPE
  - Fulfilment of the commitments towards the European Commission
  - Achievement of the set goals related to social responsibility
  - Implementation of activities related to privatisation (according to the plan)

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<sup>3</sup> Net cost of risk = net established credit impairments and provisions in a period / average net loans to non-banking sector

### **Goals of the OU of the employee performing special work**

The goals of the OUs, which arise from the goals of NLB Group and/or NLB, are imposed on the employees performing special work by their superior who is a member of the Management Board and are based on both financial and non-financial criteria (mainly in non-front-office OUs). When determining the goals of the OU, the cross-functional goals of different OUs, goals related to the goals of NLB Group by the relevant business line, the inclusion in projects etc. are considered.

The maximum amount of the variable part of the salary, subject to achievement of OU goals, is two salaries for the Management Board and the employees performing special work who are included in a business function, and one salary for other employees performing special work.

### **Personal goals of the employee performing special work (development, project and other goals)**

Development and/or personal goals represent non-financial criteria of performance of an employee performing special work and include personal development of the relevant employee that can be measured with the results of the corporate climate and improved competencies, which can be measured using the 360° assessment tool.

The maximum amount of the variable part of the salary shall be one salary for other employees performing special work.

#### *Deferred payment of the variable part*

In line with the decision of the European Commission on state aid procedure the variable part of salary of employees performing special work shall be until the end of December 2017 paid according to the following model:

- 50% is payable upon confirmation of business results at the Bank's General Meeting,
- 50% is paid after three years.

The deferred part of the variable part of the salary shall be aligned with the growth in consumer price index during the period of deferment.

After the period of deferment, the payment is made no later than within three months after the confirmation of the performance results at the Bank's General Meeting.

Prior to the payment of the deferred variable part of the salary, NLB must check if all conditions for the payment of the deferred variable part of the salary have been met. The Management Board of the Bank may adopt a unilateral decision on the amount of the payment of the deferred variable part of the salary, namely:

- An employee performing special work is paid 100% of the deferred variable part of the salary in the case that there are no negative trends in the Bank's operations during the deferment period that resulted from the decisions made by the employee performing special work and in the case the employee performing special work did not commit any severe violations of the regulations and the Bank's internal regulations, abuses or inefficient acts. When assessing these acts NLB will act according to the zero tolerance principle and will consider as a severe violation of the regulations those acts that show the signs of a criminal offence, violation, breach of obligations arising from employment and/or those acts that constitute a conflict of interests with the Bank's business interests as well as corruptive acts that constitute or reinforce non-transparency in adopting of business decisions while performing the functions in the Bank. All acts that are committed intentionally or from gross negligence and cause damage to the Bank are considered as inefficient conduct;
- An employee performing special work is not paid the deferred variable part of the salary in the case that the Bank's performance in the period of deferred payment shows material negative trends that result from the decisions adopted by the employee performing special work.

#### *Amount of payment of the variable part of the remuneration for 2016*

Pursuant to Item 7 of Article 170 of the ZBan-2, the Bank's remuneration policy stipulates that at least 50% of the variable part of the remuneration of each employee performing special work should be composed of ordinary or preference shares of the Bank, or of instruments related to shares or equal non-cash instruments when the Bank's shares are not listed on the regulated market, whereby the person obtaining the shares or instruments may only transfer them upon the Bank's approval which may only be issued after at least two years of the obtaining. Pursuant to the second paragraph of the above Article, the Bank must follow this principle (like other principles of the remuneration policies) in a way and to the extent compliant

with its size, internal organisation and nature, as well as the volume and complexity of its activities. As the Bank's shares are not listed on the stock exchange, part of the variable salary should be paid in the abovementioned financial instruments, however, according to the guidelines of the Bank of Slovenia, this rule does not apply when the variable part is less than EUR 50,000 gross.

The Supervisory Board adopted a resolution on payment of remuneration to the members of the Management Board on 7 April 2017. On 18 April 2017, the Management Board approved the resolution to pay to the employees performing special work the pertaining variable part based on the actual assessments of the entitlement to variable remuneration, namely to pay 50% of the variable part immediately and to defer 50% and pay it after 3 years. The payment was made on 21 April 2017.

#### *Defining the goals of employees performing special work in 2017*

Planning of goals and assessment of the employees performing special work are conducted once a year; the planning of the goals is usually carried out by the end of January and the assessment of performance by the end of March or when the results of operations are known.

In 2017, the goals of NLB were approved by the Supervisory Board and were included in the forms for monitoring performance of all employees performing special work. *The goals for individual OUs* were defined top-down which means that each member of the Management Board set goals for their directly subordinate employees performing special work, whereas the latter set goals down the line of management. The goals of the OU can be financial or non-financial and must be defined according to the SMART method, which means that they have to be specific, measurable, achievable, relevant, and time bound.

*Personal goals* for all employees performing special work were set on an individual basis for each employee, depending on the assessment of the superior director or member of the Management Board for the area where development of the employee performing special work is required and on the assessment based on testing of DNLA, results of the corporate climate and personal development guidelines.

#### **15.4. The ratio between fixed and variable remuneration** (Article 450.1 d of CRR)

The ratio between fixed and variable remuneration depends on the function performed by each individual, namely:

- For employees performing special work who are included in a business function the ratio between the fixed and the variable part of the salary can be 60%:40%;
- for the employees performing special work who are included in a joint (other professional services) and supervisory function the ratio between the fixed and the variable part of the salary can be 80%:20%.

The employment contract can stipulate a predetermined variable part of the salary of an employee performing special work only for the first year of their employment.

The Supervisory Board may request from a member of the Management Board, and the Management Board can request from other employees performing special work to return the already paid variable part of the salary or its proportionate part (the third paragraph of Article 270 of the ZGD-1):

- if the nullity of the annual report is established with a binding effect and the grounds for nullity refer to the items or facts based on which the performance bonus was defined, or
- based on a special auditor's report establishing that the criteria for defining remuneration were applied incorrectly or that the critical accounting, financial and other data and indicators were incorrectly established or applied.

The maximum amount of the variable remuneration for the annual distribution of the variable remuneration is defined as follows:

- for employees performing special work who are included in a business function the maximum amount of the variable part of the salary can be five salaries of the employee performing special work;
- for other employees performing special work the maximum amount of the variable part of the salary can be three salaries of the employee performing special work.

	Goals of NLB (or NLB Group for Core Group Steering)	Goals of organisational unit	Development (personal) goals of employee performing special work	Maximum amount of the variable part of salary
Front-office function	up to 2 salaries	up to 2 salaries	up to 1 salary	up to 5 salaries
Other than front-office function	up to 1 salary	up to 1 salary	up to 1 salary	up to 3 salaries

At the time NLB uses redeemable extraordinary aid granted by the Republic of Slovenia to overcome an extraordinary financial situation, the maximum amount of the variable part of the salary may be lower than the one stipulated in the Remuneration Policy (i.e. 5 salaries for front-office staff and 3 salaries for non-front-office staff), in accordance with the rules defined by the Bank of Slovenia in the secondary legislation.

Pursuant to the decision of the European Commission in relation to the state aid procedure<sup>4</sup>, the maximum possible amount of the total income of an employee performing special work is limited to 15-times the average gross salary of employees in the Republic of Slovenia or 10-times the average gross salary of employees in NLB for the period of the Bank's restructuring, i.e. until the end of December 2017. The maximum amount of income is limited to the higher of the two indicated amounts.

The last known data of the Statistical Office of the Republic of Slovenia in the month of the payment of the variable part of the salary to the employee performing special work is used for the calculation of the maximum amount of payment.

To calculate the maximum amount of the variable part in 2017, the following data were used:

MAX 15 average gross salaries<sup>5</sup> in the RS: EUR 1,626.95 x 12 months x 15 = **EUR 292,851.00**  
 MAX 10 average gross salaries<sup>6</sup> in the NLB: EUR 2,374.54 x 12 months x 10 = **EUR 284,944.80**

#### **15.5. Information on the performance criteria on which the entitlement to shares, options, or variable components of remuneration are based** (Article 450.1 e of CRR)

According to the new Bank of Slovenia Guidelines in relation to the application of the principle of proportionality in the implementation of remuneration policies of 22 November 2016, the minimum variable remuneration not used for the purpose of item 7 of the first paragraph of Article 170 of the ZBan-2 is EUR 50,000.00 gross.

An equal amount, taking into account the principle of proportionality, is also set at NLB Group level. Accordingly, the variable remuneration in 2017 was not paid in ordinary or preference shares of the Bank or instruments related to shares or equal non-cash instruments.

#### **15.6. Main parameters and rationale for any variable component scheme and any other non-cash benefits** (Article 450.1 f of CRR)

The main parameters of variable components are specified in the employment contract according to the Act Governing the Remuneration of Managers of Companies with Majority Ownership Held by the Republic of Slovenia or Self-Governing Local Communities (ZPPOGD) and the ZBan-2.

The variable pay is limited pursuant to the ZPPOGD. Pursuant to the Bank's Remuneration Policy the amount of the variable pay is limited to 5 salaries for the Management Board and the front-office staff, and 3 salaries for the non-front-office staff.

Other rights of the members of the Management Board are determined in the Rules on determining other rights under management employment contracts and other acts of the Bank.

<sup>4</sup> Commission Decision of 18/12/2013 on state aid SA.33229 (2012/C) (ex 2011/N) – Restructuring of NLB.

<sup>5</sup> Data for the January-December 2017 period – average monthly gross salary was EUR 1,626.95

<sup>6</sup> Data for the January-December 2017 period – average monthly gross salary was EUR 2,374.54

The Rules regulate the list and limitations of any other rights of managers, which can be defined in the employment contract, while in accordance with the provisions of the ZPPOGD such rights are regulated with a special documents or rules of the Bank's Supervisory Board. The list of other rights encompasses:

- company car for both business and private purposes,
- company car with a driver,
- company mobile phone,
- air travel,
- accommodation in Ljubljana,
- family separation allowance,
- housing loans for the staff,
- Eurocard NLB business card,
- entertainment allowance,
- accident insurance,
- health insurance,
- voluntary collective supplementary pension insurance,
- executive health screen,
- education and training,
- membership fees,
- parking space,
- accommodation while on a business trip,
- third-party liability insurance,
- holiday allowance and
- payment of education expenses of minor family members of members of the Management Board.

#### 15.7. Quantitative information on remuneration (Article 450.1 g and h of CRR)

Table 50 – Accounted remuneration for 2017, combined by operating segment

	MB Supervisory function	MB Management function	Investment banking	Retail banking	Asset management	Corporate functions	Independent control functions	All other
Members (Headcount)	34	48	-	-	-	-	-	-
Number of identified staff in FTE	-	-	3,00	38,40	7,98	9,27	21,74	91,47
Number of identified staff in senior management positions	-	-	3,00	39,00	8,00	10,00	23,00	92,00
Total fixed remuneration (in EUR)	330,876	4,441,184	195,445	3,135,419	428,966	483,990	1,136,671	5,221,280
Of which: fixed in cash	330,876	4,441,184	195,445	3,135,419	428,966	483,990	1,136,671	5,221,280
Total variable remuneration (in EUR)	-	852,932	55,226	782,747	86,769	117,292	179,498	866,487
Of which: variable in cash	-	852,932	55,226	782,747	86,769	117,292	179,498	866,487
Total amount of variable remuneration awarded in year which has been deferred (in EUR)	-	392,540	26,026	378,345	40,707	52,840	81,336	406,896
Of which: deferred variable in cash in year	-	392,540	26,026	378,345	40,707	52,840	81,336	406,896
<b>Additional information regarding the amount of total variable remuneration</b>								
Total amount of outstanding deferred variable remuneration awarded in previous periods and not in year (in EUR); Art 450 h(iii)CRR;	-	602,867	26,933	558,737	73,809	49,993	112,507	551,066

MB Supervisory function includes the Supervisory Board of NLB and the Supervisory Boards of NLB Group subsidiaries where employees performing special work of NLB are also members. These employees do not receive a compensation for performing a supervisory function. Payments to the individual members of the Management Board of NLB (parent bank), other key management personnel and members of the Supervisory Board of NLB (parent bank) are disclosed in the Annual Report for NLB Group 2017 in chapter 8 Related-party transactions (page 157).

#### 15.8. The information on individuals being remunerated EUR 1 million or more (Article 450.1 i and j of CRR)

None of the employees performing special work was paid EUR 1 million or more in 2017. Payments to individual members of the Management Board are disclosed in the Annual Report for NLB Group 2017 in chapter 8 - Related-party transactions (page 157).

## 16. Appendices

### 16.1. Appendix 1

**Information on whether or not the institution has set up a separate risk committee and the number of times the Risk Committee has met**  
(Article 435.2 d of CRR)

NLB has the Risk Committee as an advisory body of the Supervisory Board. Five meetings of the Risk Committee were held in 2017.

### 16.2. Appendix 2

**Declaration of the Management of the adequacy of liquidity risk arrangements**

The Management Board of NLB has a firm position that the Group is:

- in alignment of adequacy of liquidity management arrangements with regard to the Group's Risk Appetite Strategy and
- having an adequate liquidity risk management system in place with regard to the Group's Risk Appetite Strategy.

Management Board of NLB

### 16.3. Appendix 3

**A liquidity risk statement approved by the Management Board associated with the business strategy**

From the point of view of the NLB Group Management Board the Group has a strong liquidity position and robust liquidity risk management in place. According to the Risk Appetite Statement, tolerance for liquidity risk is low therefore the Group maintains sufficient level of liquidity reserves at any time and well diversified funding sources. Liquidity reserves are presented by high-quality financial assets which can be converted into cash or pledged as collateral for secured funding in normal times and times of stress.

Governance is established in a way that enables a reliable process for identifying, measuring, monitoring and controlling liquidity risk in the short and long term. Liquidity position and developments are continuously reviewed. The Group has implemented different tools for measuring liquidity risk in the form of maturity structures, stress tests, liquidity projections of future cash flows, scoring model etc.

All core members of NLB Group (banking members) are self-funded. Intragroup funding is provided only to non-core members which are in the process of disinvestment (liquidation).

The limit system is aligned with Risk Appetite and reflects the Group risk tolerance. Limits are set at levels that enable timely identification and mitigation of risk.

Structural liquidity indicators are appropriate and within prescribed limits. The main function of these risk limits/targets is to examine and confirm whether certain activities are leading the Group's risk appetite toward the common strategic objectives. All banking members are highly liquid. The Group is facing strong liquidity. In such an environment the bank dedicates a lot of attention to the structure and concentration of the liquidity reserves.

<b>Liquidity</b>	<b>NLB Group</b>		<b>NLB</b>	
	<b>31.12.2017</b>	<b>31.12.2016</b>	<b>31.12.2017</b>	<b>31.12.2016</b>
LCR	276%	332%	300%	350%
NSFR	149%	147%	144%	140%
LTD net	70.8%	74.2%	67.4%	74.5%
Encumbered liquidity reserves	68,140	108,939	62,625	99,700
Unencumbered liquidity reserves	5,028,186	4,794,191	4,079,316	3,984,322
Unencumbered liquidity reserves in total assets	41%	40%	47%	45%
Share of non-banking sector deposits	81%	78%	78%	75%

\*Liquid reserves do not include obligatory reserves with central banks.

#### **16.4. Appendix 4 Management Board statement regarding risk management systems in NLB Group**

NLB d.d Management Board has established conservative Risk management framework throughout NLB Group. Key risk guidelines of the Group are defined by its Risk Appetite and Risk Strategy with regards to the Group's business model, based on forward looking perspective, which are regularly revised and enhanced. In addition main strategic risk guidelines are integrated into annual business plan review and budgeting process. Our established Risk management framework on the Group level supports business decision-making at strategic and operating level, comprehensive steering and proactive risk management.

The Management Board pursues proactive management, assessment, and monitoring of risks within the Group, on consolidated level and on the level of each group member as well. Risk identification is embedded in a very early stage focusing on the efficient risk management and mitigation of them with aim to ensure the prudent and economic use of its capital. The Management Board is not aware of material risks beyond identified within risk identification process in the ICAAP.

As an important element of its risk management function and organisation, the NLB Group is using the three lines of defence framework. Within this framework, the Business line on one side and Risk management on the other both bear full responsibility for the assumption of risk. Internal Audit reviews key risks in its operations and provides independent and comprehensive supervision of the internal control system. Beyond monitoring fulfilment of legal and regulatory requirements Compliance concerns also with ethics and integrity within the whole Group. Specialized risk management function within Global risk covers overarching aspects of risk management. Its mandate is to provide an increased focus on holistic risk management and cross-risk oversight to further enhance risk steering and mitigation within the whole Group.

## 16.5. Appendix 5

### EU LI3 – Outline of the differences in the scopes of consolidation (entity by entity) of NLB Group

Name of the entity	Method of accounting consolidation	Method of regulatory consolidation				Deducted	Description of the entity
		Full consolidation	Equity method	Proportional consolidation	Neither consolidated nor deducted		
NLB Banka a.d., Skopje	Full consolidation	X					Banking
NLB Banka a.d., Podgorica	Full consolidation	X					Banking
NLB Banka a.d., Banja Luka	Full consolidation	X					Banking
NLB Banka sh.a., Priština	Full consolidation	X					Banking
NLB Banka d.d., Sarajevo	Full consolidation	X					Banking
NLB banka a.d., Beograd	Full consolidation	X					Banking
NLB Srbija d.o.o., Beograd	Full consolidation	X					Real estate
NLB Skladi d.o.o., Ljubljana	Full consolidation	X					Asset management
NLB Nov penziski fond a.d., Skopje	Full consolidation				X		Insurance
NLB Crna gora d.o.o., Podgorica	Full consolidation	X					Real estate
NLB Leasing d.o.o. - v likvidaciji, Ljubljana	Full consolidation	X					Finance
Optima Leasing d.o.o., Zagreb "u likvidaciji"	Full consolidation	X					Finance
NLB Leasing Podgorica d.o.o. "u likvidaciji"	Full consolidation	X					Finance
NLB Leasing d.o.o., Beograd "u likvidaciji"	Full consolidation	X					Finance
NLB Leasing d.o.o., Sarajevo	Full consolidation	X					Finance
NLB Lizing d.o.o.e.l., Skopje "vo likvidacija"	Full consolidation	X					Finance
TARA HOTEL d.o.o., Budva	Full consolidation	X					Real estate
PRO-REM d.o.o., Ljubljana "v likvidaciji"	Full consolidation	X					Real estate
OL Nekretnine d.o.o., Zagreb "u likvidaciji"	Full consolidation	X					Real estate
BH-RE d.o.o., Sarajevo	Full consolidation	X					Real estate
REAM d.o.o., Beograd	Full consolidation	X					Real estate
REAM d.o.o., Podgorica	Full consolidation	X					Real estate
REAM d.o.o., Zagreb	Full consolidation	X					Real estate
SR-RE d.o.o., Beograd	Full consolidation	X					Real estate
SPV 2 d.o.o., Beograd	Full consolidation	X					Real estate
NLB Propria d.o.o., Ljubljana "v likvidaciji"	Full consolidation	X					Real estate
CBS Invest d.o.o., Sarajevo	Full consolidation	X					Real estate
NLB InterFinanz AG, Zurich "in likvidation"	Full consolidation	X					Finance
NLB InterFinanz Praha	Full consolidation	X					Finance
NLB InterFinanz Beograd	Full consolidation	X					Finance
Prospera Plus d.o.o.	Full consolidation	X					Tourist and catering trade
LHB AG, Frankfurt	Full consolidation	X					Finance
Prvi Faktor, Beograd "v likvidaciji"	Equity method				X		Finance
Prvi Faktor, Ljubljana "v likvidaciji"	Equity method				X		Finance
Prvi Faktor, Sarajevo "v likvidaciji"	Equity method				X		Finance
Prvi Faktor, Zagreb "v likvidaciji"	Equity method				X		Finance
NLB Vita d.d., Ljubljana	Equity method				X		Insurance
Arg Nepremicnine d.o.o.	Equity method		X				Real estate
Bankart d.o.o., Ljubljana	Equity method		X				Card processing
SPD d.d., Ljubljana	Equity method				X		Insurance

Entities that are neither consolidated nor deducted are not consolidated:

- in accordance with Article 19 of the CRR (this refers on members of Prvi Faktor Group)
- or because they are insurances (NLB Vita, SPD d.o.o. and NLB Nov penziski fond).

## 16.6. Appendix 6

### Material practical or legal impediment to the prompt transfer of own funds or repayment of liabilities among the parent undertaking and its subsidiaries; (Article 436 c and d of CRR)

In NLB Group, there are no substantial practical or legal impediments to the prompt transfer of capital or repayment of liabilities between the parent undertaking and its subsidiaries. In case of capital transfer provided by NLB it is necessary to follow the provisions regarding the minimum capital in accordance with CRR and the ZBan-2. For subsidiary banks the provisions regarding liquidity, capital adequacy and level of capital to cover all risks are also taken into account, all in accordance with local legislation.

In asset management, company (NLB Skladi) provisions regarding capital adequacy and level of capital to cover all risks arise from the Law on Investment Funds and Management Companies.

For several non – core companies that are in the liquidation process there is a restriction according to local Companies Law stipulating that during the duration of the liquidation process dividends are not paid out nor are assets disbursed to stakeholders until all claims are paid. The liquidation process can be concluded after all the court disputes are brought to an end and the assets that are to be distributed to stakeholders, but exceed the subscribed share capital of a stakeholder, are considered as a dividend.

There are also contractual restrictions that are to be taken into account and arise from subordinated loans that NLB granted to one of the subsidiary banks, namely NLB Banka a.d., Skopje and one of the company NLB InterFinanz Zürich AG in Liquidation. According to the nature of the subordinated loan it can be repaid after claims arising from all priority obligations are settled and to the extent permitted by the rest of the Bank's assets in the bankruptcy or liquidation procedure.

Subsidiary banks in Bosnia and Herzegovina face legal impediments in dividend pay-outs as well as impediments arising from credit agreements concluded with NLB

All subsidiaries of NLB Group not included in the prudential consolidation met the minimum capital requirements as at 31 December 2017.

## 16.7. Appendix 7

### List of all disclosures required under Part 8 of CRR

Art.	Requirement	Chapter	Page
<b>435</b>	<b>Risk management objectives and policies</b>		
<b>1.</b>	<b>Objectives and policies regarding the relevant risks</b>		
	(a) the strategies and processes to manage those risks;	4.1, 7.1, 9.1	24-32, 54-55, 61-65
	(b) the structure and organisation of the relevant risk management function, including information on its authority and statute, or other appropriate arrangements;	4.1, 7.1, 9.1	24-32, 54-55, 61-65
	(c) the scope and nature of risk reporting and measurement systems;	4.1, 7.1, 9.1	24-32, 54-55, 61-65
	(d) the policies for hedging and mitigating risk, and the strategies and processes for monitoring the continuing effectiveness of hedges and mitigants;	4.1, 7.1, 9.1	24-32, 54-55, 61-65
	(e) a declaration approved by the management body on the adequacy of risk management arrangements of the institution providing assurance that the risk management systems put in place are adequate with regard to the institution's profile and strategy;	4.1	24-32
	(f) a concise risk statement approved by the management body succinctly describing the institution's overall risk profile associated with the business strategy. This statement shall include key ratios and figures providing external stakeholders with a comprehensive view of the institution's management of risk, including how the risk profile of the institution interacts with the risk tolerance set by the management body.	4.1	24-32
<b>2.</b>	<b>Information, including regular, at least annual updates, regarding governance arrangements</b>		
	(a) the number of directorships held by members of the management body;	4.2	33
	(b) the recruitment policy for the selection of members of the management body and their actual knowledge, skills, and expertise;	4.3	33-34
	(c) the policy on diversity with regard to selection of members of the management body, its objectives and any relevant targets set out in that policy, and the extent to which these objectives and targets have been achieved;	4.4	34-35
	(d) whether or not the institution has set up a separate risk committee and the number of times the risk committee has met;	16.1	82-83
	(e) the description of the information flow on risk to the management body.	4.1	24-32
<b>436</b>	<b>Scope of application</b>		
	(a) the name of the institution to which the requirements of this Regulation apply;	1	8
	(b) an outline of the differences in the basis of consolidation for accounting and prudential purposes, with a brief description of the entities therein, explaining whether they are: fully consolidated, proportionally consolidated, deducted from own funds, neither consolidated nor deducted;	2, 16.5	9-12, 85
	(c) any current or foreseen material practical or legal impediment to the prompt transfer of own funds or repayment of liabilities among the parent undertaking and its subsidiaries;	2, 16.6	9-12, 85-86
	(d) the aggregate amount by which the actual own funds are less than required in all subsidiaries not included in the consolidation, and the name or names of such subsidiaries;	2, 16.6	9-12, 85-86
	(e) if applicable, the circumstance of making use of the provisions laid down in Articles 7 and 9.	/	/
<b>437</b>	<b>Capital (Own funds)</b>		
	(a) a full reconciliation of CET1 items, AT1 items, Tier 2 items and filters and deductions applied pursuant to Articles 32 to 35, 36, 56, 66 and	3.7	21-23

	79 to own funds of the institution and the balance sheet in the audited financial statements of the institution;		
	(b) a description of the main features of the CET1 and AT1 instruments and T2 instruments issued by the institution;	3.4	16-17
	(c) the full terms and conditions of all CET1, AT1 and Tier 2 instruments;	3.4	16-17
	(d) separate disclosure of the nature and amounts of the following:		
	(i) each prudential filter applied pursuant to Articles 32 to 35;		
	(ii) each deduction made pursuant to Articles 36, 56 and 66;	3.6	19-21
	(iii) items not deducted in accordance with Articles 47, 48, 56, 66 and 79;		
	(e) a description of all restrictions applied to the calculation of own funds in accordance with this Regulation and the instruments, prudential filters and deductions to which those restrictions apply;	3.6	19-21
	(f) where institutions disclose capital ratios calculated using elements of own funds determined on a basis other than that laid down in this Regulation, a comprehensive explanation of the basis on which those capital ratios are calculated.	3.7	21-23
<b>438</b>	<b>Capital requirements</b>		
	(a) a summary of the institution's approach to assessing the adequacy of its internal capital to support current and future activities;	3.3	15-16
	(b) upon demand of the relevant competent authority, the result of the institution's internal capital adequacy assessment process including the composition of the additional own funds requirements based on the supervisory review process as referred to in point (a) of Article 104(1) of Directive 2013/36/EU;	/	/
	(c) (SA approach:) for institutions calculating the risk-weighted exposure amounts in accordance with Chapter 2 of Part Three, Title II, 8% of the risk-weighted exposure amounts for each of the exposure classes specified in Article 112 (= SA categories);	3.2	14-15
	(d) (IRB approach:) for institutions calculating risk-weighted exposure amounts in accordance with Chapter 3 of Part Three, Title II, 8% of the risk-weighted exposure amounts for each of the exposure classes specified in Article 147. The institutions calculating the risk-weighted exposure amounts in accordance with Article 153(5) or Article 155(2) shall disclose the exposures assigned to each category in Table 1 of Article 153(5), or to each risk weight mentioned in Article 155(2);	/	/
	(e) (market risks:) own funds requirements calculated in accordance with points (b) and (c) of Article 92(3); (1) position risk; (2) large exposures exceeding the limits specified in Articles 395 to 401, to the extent an institution is permitted to exceed those limits; (3) foreign-exchange risk; (4) settlement risk; (5) commodities risk;	3.2	14-15
	(f) (operational risk:) own funds requirements calculated in accordance with Part Three, Title III, Chapters 2, 3 and 4 and disclosed separately.	3.2	14-15
<b>439</b>	<b>Exposure to counterparty credit risk</b>		
	(a) a discussion of the methodology used to assign internal capital and credit limits for counterparty credit exposures;	7.3	55
	(b) a discussion of policies for securing collateral and establishing credit reserves;	7.4	55
	(c) a discussion of policies with respect to wrong-way risk exposures;	7.5	56
	(d) a discussion of the impact of the amount of collateral the institution would have to provide given a downgrade in its credit rating;	7.6	56-58
	(e) gross positive fair value of contracts, netting benefits, netted current credit exposure, collateral held and net derivatives credit exposure. Net derivatives credit exposure is the credit exposure on derivatives transactions after considering both the benefits from legally enforceable netting agreements and collateral arrangements;	7.6	56-58
	(f) measures for exposure value under the methods set out in Part Three, Title II, Chapter 6, Sections 3 to 6, whichever method is applicable;	7.6	56-58
	(g) the notional value of credit derivative hedges, and the distribution of current credit exposure by types of credit exposure;	/	/
	(h) the notional amounts of credit derivative transactions, segregated between use for the institution's own credit portfolio, as well as in its intermediation activities, including the distribution of the credit derivatives products used, broken down further by protection bought and sold within each product group;	/	/
	(i) the estimate of $\alpha$ if the institution has received the permission of the competent authorities to estimate $\alpha$ .	/	/
	<b>Capital buffers</b>		

440	1. Countercyclical capital buffer:		
	(a) the geographical distribution of its credit exposures relevant for the calculation of its countercyclical capital buffer;	3.5	17-19
	(b) the amount of its institution-specific countercyclical capital buffer.	3.5	17-19
	2. G-SII buffer:		
441	1. Institutions identified as G-SIIs in accordance with Article 131 of Directive 2013/36/EU shall disclose, on an annual basis, the values of the indicators used for determining the score of the institutions in accordance with the identification methodology referred to in that Article.	/	/
<b>442</b>	<b>Credit risk adjustments</b>		
	(a) the definitions for accounting purposes of 'past due' and 'impaired';	5.7	45-47
	(b) a description of the approaches and methods adopted for determining specific and general credit risk adjustments;	5.7	45-47
	(c) the total amount of exposures after accounting offsets and without taking into account the effects of credit risk mitigation, and the average amount of the exposures over the period broken down by different types of exposure classes;	5.2	39
	(d) the geographic distribution of the exposures, broken down in significant areas by material exposure classes, and further detailed if appropriate;	5.3	39-40
	(e) the distribution of the exposures by industry or counterparty type, broken down by exposure classes, including specifying exposure to SMEs, and further detailed if appropriate;	5.4	41
	(f) the residual maturity breakdown of all the exposures, broken down by exposure classes, and further detailed if appropriate;	5.5	42
	(g) by significant industry or counterparty type, the amount of:		
	(i) impaired exposures and past due exposures, provided separately;	5.6	43-45
	(ii) specific and general credit risk adjustments;		
	(iii) charges for specific and general credit risk adjustments during the reporting period;		
	(h) the amount of the impaired exposures and past due exposures, provided separately, broken down by significant geographical areas including, if practical, the amounts of specific and general credit risk adjustments related to each geographical area;	5.6	43-45
	(i) the reconciliation of changes in the specific and general credit risk adjustments for impaired exposures, shown separately. The information shall comprise:		
	(i) a description of the type of specific and general credit risk adjustments;		
	(ii) the opening balances;		
	(iii) the amounts taken against the credit risk adjustments during the reporting period;	5.7	45-47
	(iv) the amounts set aside or reversed for estimated probable losses on exposures during the reporting period, any other adjustments including those determined by exchange rate differences, business combinations, acquisitions and disposals of subsidiaries, and transfers between credit risk adjustments;		
	(v) the closing balances.		
	Specific credit risk adjustments and recoveries recorded directly to the income statement shall be disclosed separately.	5.6	43-45
<b>443</b>	<b>Unencumbered assets</b>		
	EBA has prepared regulatory technical standards for disclosure of unencumbered assets – Regulation (EU) No 2017/2295.	8	58-60
<b>444</b>	<b>Use of ECAIs</b>		
	(a) the names of the nominated ECAIs and ECAs and the reasons for any changes;	6	51-53
	(b) the exposure classes for which each ECAI or ECA is used;	6	51-53
	(c) a description of the process used to transfer the issuer and issue credit assessments onto items not included in the trading book;	6	51-53
	(d) the association of the external rating of each nominated ECAI or ECA with the credit quality steps prescribed in Part Three, Title II, Chapter 2, taking into account that this information needs not be disclosed if the institution complies with the standard association published by EBA;	6	51-53
	(e) the exposure values and the exp. values after credit risk mitigation associated with each credit quality step prescribed in Part Three, Title	6, 5.2	51-53, 39

	II, Chapter 2 as well as those deducted from own funds.		
<b>445</b>	<b>Exposure to market risk</b>		
	Separately for each risk + the own funds requirement for specific IRR of securitisation positions.	9	61-65
<b>446</b>	<b>Operational risk</b>		
	Institutions shall disclose the approaches for the assessment of own funds requirements for operational risk that the institution qualifies for; a description of the methodology set out in Article 312(2), if used by the institution, including a discussion of relevant internal and external factors considered in the institution's measurement approach, and in the case of partial use, the scope and coverage of the different methodologies used.	14	74-75
<b>447</b>	<b>Exposures in equities not included in the trading book</b>		
	(a) the differentiation between exposures based on their objectives, including for capital gains relationship and strategic reasons, and an overview of the accounting techniques and valuation methodologies used, including key assumptions and practices affecting valuation and any significant changes in these practices;	11	66
	(b) the balance sheet value, the fair value and, for those exchange-traded, a comparison to the market price where it is materially different from the fair value;	11	66
	(c) the types, nature and amounts of exchange-traded exposures, private equity exposures in sufficiently diversified portfolios, and other exposures;	11	66
	(d) the cumulative realised gains or losses arising from sales and liquidations in the period; and	11	66
	(e) the total unrealised gains or losses, the total latent revaluation gains or losses, and any of these amounts included in the original or additional own funds.	11	66
<b>448</b>	<b>Exposure to interest rate risk on positions not included in the trading book</b>		
	(a) the nature of the interest rate risk and the key assumptions (including assumptions regarding loan prepayments and behaviour of non-maturity deposits), and frequency of measurement of the IRR;	10.1	65
	(b) the variation in earnings, economic value or other relevant measure used by the management for upward and downward rate shocks according to management's method for measuring the interest rate risk, broken down by currency.	10.2	65
<b>449</b>	<b>Exposure to securitisation positions</b>	/	/
<b>450</b>	<b>Remuneration policy</b>		
1	For those categories of staff whose professional activities have a <u>material impact on its risk profile</u> :		
	(a) information concerning the decision-making process used for determining the remuneration policy, as well as the number of meetings held by the main body overseeing remuneration during the financial year including, if applicable, information about the composition and the mandate of a remuneration committee, the external consultant whose services have been used for the determination of the remuneration policy and the role of the relevant stakeholders;	15.1	75-76
	(b) information on the link between pay and performance;	15.2	76-77
	(c) the most important design characteristics of the remuneration system, including information on the criteria used for performance measurement and risk adjustment, deferral policy and vesting criteria;	15.3	78-80
	(d) the ratios between fixed and variable remuneration set in accordance with Article 94(1)(g) of Directive 2013/36/EU;	15.4	80-81
	(e) information on the performance criteria on which the entitlement to shares, options or variable components of remuneration is based;	15.5	81
	(f) the main parameters and rationale for any variable com. scheme and any other non-cash benefits;	15.6	81-82
	(g) aggregate quantitative information on remuneration, broken down by business area;	15.7	82
	(h) aggregate quantitative information on remuneration, broken down by senior management and members of staff whose actions have a material impact on the risk profile of the institution, indicating the following:	15.7	82

	(i) the amounts of remuneration for the financial year, split into fixed and variable remuneration, and the number of beneficiaries;		
	(ii) the amounts and forms of variable remuneration, split into cash, shares, share-linked instruments and other types;		
	(iii) the amounts of outstanding deferred remuneration, split into vested and unvested portions;		
	(iv) the amounts of deferred remuneration awarded during the financial year, paid out and reduced through performance adjustments;		
	(v) new sign-on and severance payments made during the financial year, and the number of beneficiaries of such payments;		
	(vi) the amounts of severance payments awarded during the financial year, number of beneficiaries and highest such award to a single person;		
	(i) the number of individuals being remunerated with EUR 1 million or more per financial year, for remuneration between EUR 1 million and EUR 5 million broken down into pay bands of EUR 500,000 and for remuneration of EUR 5 million and above broken down into pay bands of EUR 1 million;	15.8	82
	(j) upon demand from the Member State or competent authority, the total remuneration for each member of the management body or senior management.	15.8	82
<b>451</b>	<b>Leverage</b>		
	(a) the leverage ratio and how the institution applies Article 499(2) and (3);	13	72-74
	(b) a breakdown of the total exposure measure, as well as a reconciliation of the total exposure measure with the relevant information disclosed in published financial statements;	13	72-74
	(c) where applicable, the amount of derecognised fiduciary items in accordance with Article 429(11);	/	/
	(d) a description of the processes used to manage the risk of excessive leverage;	13	72-74
	(e) a description of the factors that had an impact on the leverage ratio during the period to which the disclosed leverage ratio refers.	13	72-74
<b>452</b>	<b>Use of the IRB Approach to credit risk</b>	/	/
<b>453</b>	<b>Use of credit risk mitigation techniques</b>	/	/
	(a) the policies and processes for, and an indication of the extent to which the entity makes use of, on- and off- balance sheet netting;	/	/
	(b) the policies and processes for collateral valuation and management;	5.8	47-51
	(c) a description of the main types of collateral taken by the institution;	5.8	47-51
	(d) the main types of guarantor and credit derivative counterparty and their creditworthiness;	/	/
	(e) information about market or credit risk concentrations within the credit mitigation taken;	5.8	47-51
	(f) for institutions calculating risk-weighted exposure amounts under the Standardised Approach or the IRB Approach, but not providing own estimates of LGDs or conversion factors in respect of the exposure class, separately for each exposure class, the total exposure value (after, where applicable, on- or off-balance sheet netting) that is covered — after the application of volatility adjustments — by eligible financial collateral, and other eligible collateral;	5.2, 5.8	39, 47-51
	(g) for institutions calculating risk-weighted exposure amounts under the Standardised Approach or the IRB Approach, separately for each exposure class, the total exposure (after, where applicable, on- or off-balance sheet netting) that is covered by guarantees or credit derivatives. For the equity exposure class, this requirement applies to each of the approaches provided in Article 155.	5.2, 5.8	39, 47-51
<b>454</b>	<b>Use of the Advanced Measurement Approaches to operational risk</b>	/	/
<b>455</b>	<b>Use of Internal Market Risk Models</b>	/	/
<b>492</b>	<b>Transitional provisions for disclosure of own funds</b>		
3	During the period from 1 January 2014 to 31 December 2017, institutions shall disclose the following additional information about their own funds:		
	(a) the nature and effect on CET1 capital, AT1 capital, Tier 2 capital and own funds of the individual filters and deductions applied in accordance with Articles 467 to 470, 474, 476 and 479;	3.6	19-21
	(b) the amounts of minority interests and AT1 and Tier 2 instruments, and related retained earnings and share premium accounts, issued		

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- by subsidiaries that are included in consolidated CET1 capital, AT 1 capital, Tier 2 capital and own funds in accordance with Section 4 of Chapter 1;
  - (c) the effect on CET1 capital, AT1 capital, Tier 2 capital and own funds of the individual filters and deductions applied in accordance with Article 481;
  - (d) the nature and number of items that qualify as CET1 items, Tier 1 items and Tier 2 items by virtue of applying the derogations specified in Section 2 of Chapter 2.
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4 During the period from 1 January 2014 to 31 December 2021, institutions shall disclose the number of instruments that qualify as CET 1 instruments, AT1 instruments and Tier 2 instruments by virtue of applying Article 484 (capital instruments that are not eligible under new legislation, but can be gradually excluded). / /

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