Half-year Financial Report as at 30 June 2019

Volksbank

Banca Popolare dell’Alto Adige
A Public Limited Company

Registered Office and General Management: Via del Macello No. 55 – I-39100 Bolzano
Registered Capital at 30 June 2019 €201,993,752, fully paid up
Tax code, VAT No. and Companies Register No. 00129730214
Member of the Interbank Deposit Protection Fund and the National Guarantee Fund
ABI 05856.0
www.bancapopolare.it - www.volksbank.it

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Corporate positions and auditing firm

Board of Directors

Chairman	Otmar MICHAELER
Deputy Chairmen	Maria Giovanna CABION Lorenzo SALVÁ (***)
Directors	Lorenzo BERTACCO (*) (**) David COVI (*) (**) Philip FROSCHMAYR Lukas LADURNER (***) Alessandro MARZOLA (***) Giuseppe PADOVAN (***) Margit TAUBER (*) (**) Gregor WIERER (**)
	(*) Members of the Independent Directors Committee (**) Members of the Risk Committee (***) Members of the Credit Committee

Board of Statutory Auditors

Chairman	Astrid KOFLER
Statutory auditors	Georg HESSE Emilio LORENZON
Alternate auditors	Nadia DAPOTZ Markus WISTHALER

Head Office

General Manager	Johannes SCHNEEBACHER
Deputy General Manager	Stefan SCHMIDHAMMER

Financial Reporting Officer Alberto CALTRONI

Independent auditors KPMG S.p.A.

VOLKSBANK
THE TERRITORIAL NETWORK

BANCA POPOLARE DELL'ALTO ADIGE
A Public Limited Company
Listed in the Bolzano Companies Register at No. 00129730214
A Member of the Interbank Deposit Protection Fund
ABI 05856.0

HEAD OFFICE
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BRANCHES

BOLZANO PROVINCE	
Appiano – Eppan Via J. G. Plazer 56 - J.-G.-Plazer-Straße 56	Tel. 0471-944270
Bolzano – Bozen Galleria Telser 1 - Telsergalerie 1	Tel. 0471-944190
Bolzano – Bozen Piazza Mazzini 2 - Mazziniplatz 2	Tel. 0471-944020
Bolzano – Bozen Via C. Augusta 5 - C.-Augusta-Straße 5	Tel. 0471-944250
Bolzano – Bozen Via del Ronco 15 - Neubruchweg 15	Tel. 0471-944260
Bolzano – Bozen Via Galvani 3/f - Galvanistraße 3/f	Tel. 0471-944320
Bolzano – Bozen Via Leonardo da Vinci 2 – Leonardo-da-Vinci-Straße 2	Tel. 0471-996151
Bolzano – Bozen Via Resia 132/b - Reschenstraße 132/b	Tel. 0471-944290
Bolzano – Bozen Via Roma 45 - Romstraße 45	Tel. 0471-944200
Bolzano – Bozen Viale Druso 64 - Drususallee 64	Tel. 0471-944340
Bolzano – Bozen Vicolo Gumer 7 (sportello economale) Gumergasse 7 (Schatzamtsschalter)	Tel. 0471 996123
Bressanone – Brixen Portici Maggiori 2 - Große Lauben 2	Tel. 0472-811213
Bressanone – Brixen Via J. Durst 28 - J.-Durst-Straße 28	Tel. 0472-811600
Bressanone – Brixen Via Plose 38/b - Plosestraße 38/b	Tel. 0472-811560
Brunico – Bruneck Bastioni 24 - Graben 24	tel. 0474-544700
Brunico – Bruneck Via Valle Aurina 30 – Ahrntalerstraße 30	Tel. 0474-544760
Cadipietra – Steinhaus Cadipietra 105 - Steinhaus 105	Tel. 0474-544800
Caldaro – Kaltern Piazza Principale 13 - Marktplatz 13	Tel. 0471-944220
Caldaro – Kaltern Via Stazione 10 - Bahnhofstraße 10	Tel. 0471-944235
Campo Tures - Sand in Taufers Via Municipio 4 - Rathausstraße 4	Tel. 0474-544740
Chienes – Kiens Via Chienes 1 - Kiener Dorfweg 1	Tel. 0474-544730
Chiusa – Klausen Piazza Tinne 5 - Tinneplatz 5	Tel. 0472-811540
Dobbiaco – Toblach Viale S. Giovanni 23 - St.-Johannes-Straße 23	Tel. 0474-544770
Egna – Neumarkt Largo Municipio 32 - Rathausring 32	Tel. 0471-944280

BOLZANO PROVINCE	
La Villa – Stern Via Colz 56 - Colz Straße 56	Tel. 0471-944010
Laces – Latsch Via Stazione 1/b - Bahnhofstraße 1/b	Tel. 0473-254440
Laives – Leifers Via Kennedy 123 - Kennedystraße 123	Tel. 0471-944240
Lana Piazza Tribus 17 - Tribusplatz 17	Tel. 0473-254350
Lasa – Laas Via Venosta 44 - Vinschgaustraße 44	Tel. 0473-254310
Lazfons – Latzfons San Giacomo 3 - St. Jakob 3	Tel. 0472-811620
Luson – Lüsen Vicolo Dorf 19 - Dorfgasse 19	Tel. 0472-811590
Malles Venosta – Mals Via Stazione 9/b - Bahnhofstraße 9/b	Tel. 0473-254400
Merano – Meran Piazza del Grano 3 - Kornplatz 3	Tel. 0473-254111
Merano – Meran Via Goethe 74/a - Goethestraße 74/a	Tel. 0473-254300
Merano – Meran Via Matteotti 43 - Matteottistraße 43	Tel. 0473-254330
Merano – Meran Via Monte Tessa 34 - Texelstraße 34	Tel. 0473-254390
Merano – Meran Via Roma 278 - Romstraße 278	Tel. 0473-254420
Monguelfo – Welsberg Via Parrocchia 13 - Pfarrgasse 13	Tel. 0474-544750
Naturno – Naturns Via Principale 37/b - Hauptstraße 37/b	tel. 0473-254370
Nova Levante – Welschnofen Via Roma 8 - Romstraße 8	Tel. 0471-944090
Ora – Auer Via Stazione 8 - Bahnhofstraße 8	Tel. 0471-944040
Ortisei - St. Ulrich Piazza S. Durich 3 - S.-Durich-Platz 3	Tel. 0471-944330
Racines – Ratschings Stanghe 18 - Stange 18	Tel. 0472-811610
Renon – Ritten Via del Paese 14, Frazione Collalbo - Dorfstraße 14, Fraktion Klobenstein	Tel. 0471-944370
Rio di Pusteria – Muehlbach Via K. Lanz 50 - K.-Lanz-Straße 50	Tel. 0472-811520
S. Leonardo in Passiria - St. Leonhard in Passeier Via Passiria 14 - Passeirer Straße 14	Tel. 0473-254380
S. Lorenzo di Sebato - St. Lorenzen Via Josef Renzler 17 - Josef-Renzler-Straße 17	Tel. 0474-544780
Scena – Schenna Piazza Arciduca Giovanni 7 - Erzh.-Johann-Platz 7	Tel. 0473-254430
Selva Gardena – Wolkenstein Via Meisules 155/a - Meisulesstraße 155/a	Tel. 0471-944000
Silandro – Schlanders Via Covelano 10 - Göflaner Straße 10	Tel. 0473-254410
Siusi – Seis Via Sciliar 16 - Schlernstraße 16	Tel. 0471-944300
Vandoies – Vintl Via J. A. Zoller 8 - J.-A.-Zoller-Straße 8	Tel. 0472-811640
Varna – Vahrn Via Brennero 101 - Brennerstraße 101	Tel. 0472-811650
Velturno – Feldthurns Paese 12 - Dorf 12	Tel. 0472-811580
Vipiteno – Sterzing Via Città Nuova 22/a - Neustadt 22/a	Tel. 0472-811500

PROVINCE OF BELLUNO	
Auronzo di Cadore Via Corte 33	Tel. 0435-505650
Belluno Via Caffi 15	Tel. 0437-356700
Cencenighe Agordino Via XX Settembre 107	Tel. 0437-356640
Cortina d' Ampezzo Largo delle Poste 49	Tel. 0436-863500
Domegge di Cadore Via Roma 48	Tel. 0435-505620
Dosoledo Piazza Tiziano 2	Tel. 0435-505670
Feltre Via Monte Grappa 28	Tel. 0439-842600
Forno di Zoldo Via Roma 70/b	Tel. 0437-356620
Limana Via Roma 116/118	Tel. 0437-356690
Longarone Via Roma 89	tel. 0437-356720

PROVINCE OF BELLUNO	
Mel Via Tempietto 33/a	Tel. 0437-356660
Padola Piazza San Luca 22	Tel. 0435-505690
Ponte nelle Alpi Viale Roma 87	Tel. 0437-356630
S. Stefano di Cadore Via Venezia 30	Tel. 0435-505630
Santa Giustina Via Feltre 17	Tel. 0437-356680
Sedico Via Cordevole 2/b	Tel. 0437-356650
Tai di Cadore Via Ferdinando Coletti 15	Tel. 0435-505600
Valle di Cadore Via XX Settembre 76	Tel. 0435-505660

PROVINCE OF PADUA	
Carmignano di Brenta Via Marconi 36	Tel. 049-6950010
Cittadella Via Riva Pasubio 5	Tel. 049-6950040
Padua Corso Milano 99	Tel. 049-6950020
Piazzola sul Brenta Via dei Contarini 36	Tel. 049-6950050
Tombolo Via Vittorio Veneto 1	Tel. 049-6950000

PROVINCE OF PORDENONE	
Pordenone Via Galvani 8	Tel. 0434-786520
Sacile Via Martiri Sfriso 9	Tel. 0434-786500

PROVINCE OF TRENTO	
Ala Via della Roggia 10	Tel. 0464-912520
Arco Via S. Caterina 20	Tel. 0464-912510
Borgo Valsugana Via Hippoliti 11/13	Tel. 0461-211060
Cavalese Viale Libertà 7	Tel. 0462-248500
Cles Piazza Navarrino 16/17	Tel. 0463-840510
Fund Via Cesare Battisti 39	Tel. 0463-840500
Lavis Via Rosmini 65	Tel. 0461-211070
Mezzolombardo Via A. Degasperi 4	Tel. 0461-211030
Moena Piaz de Ramon 24	Tel. 0462-248510
Mori Via della Terra Nera 48/d	Tel. 0464-912500
Pergine Viale Venezia 44	Tel. 0461-211050
Riva del Garda V. Damiano Chiesa 4/g-h	Tel. 0464-912560
Rovereto Via G. M. Della Croce 2	Tel. 0464-912530
Tione Via Circonvallazione 56	Tel. 0465-338500
Trento Piazza Lodron 31	Tel. 0461-211000
Trento Via Brennero 302/a	Tel. 0461-211080
Trento Via Enrico Fermi 11	Tel. 0461-211090

PROVINCE OF TREVISO	
Casale Sul Sile Via G. Marconi 3	Tel. 0422-508170
Castelfranco Veneto Borgo Treviso 62	Tel. 0423-974610
Conegliano Via Cavour 11	Tel. 0438-907770
Conegliano Via Cesare Battisti 5	Tel. 0438-907740
Crocetta del Montello Via Andrea Erizzo 64	Tel. 0423-974620
Loria - Ramon di Loria Via Poggiana 4	Tel. 0423-974670
Mogliano Veneto Via degli Alpini 16/g/f/e	Tel. 041-5446660
Montebelluna Via Montegrappa 24/c	Tel. 0423-974660
Motta Di Livenza - Via Padre Leonardo Bello/Angolo Via Cigana 1	Tel. 0422-508180
Oderzo Via degli Alpini 24/26	Tel. 0422-508100
Paese Via Cesare Battisti 3	Tel. 0422-508140
Pieve di Soligo Via Nubie 3/d	Tel. 0438-907700
Preganziol Piazza Gabbin 16	Tel. 0422-508120
Quinto Di Treviso Via Vittorio Emanuele 11	Tel. 0422-508190
Spresiano Piazza Luciano Rigo 49	Tel. 0422-508130
Treviso Viale Brigata Treviso 1	Tel. 0422-508210
Treviso Via San Vito 12	Tel. 0422-508150
Treviso Viale IV Novembre 13/a	Tel. 0422-508110
Treviso Viale Montegrappa 46	Tel. 0422-508201
Valdobbiadene Foro Boario 21-23-13	Tel. 0423-974600
Vittorio Veneto Galleria Tintoretto 3	Tel. 0438-907710

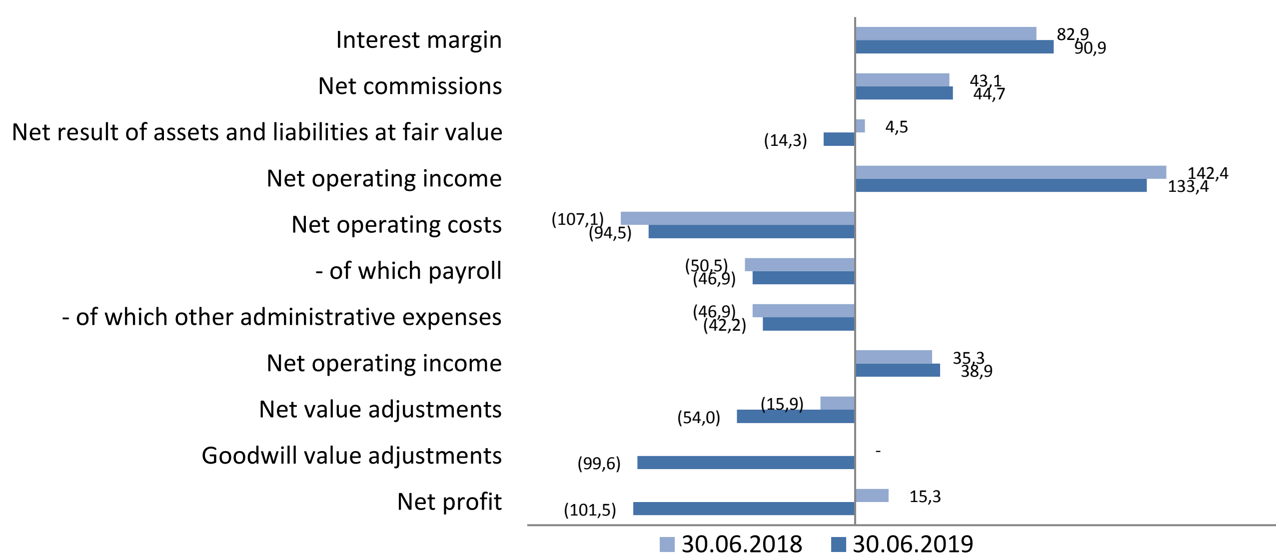
PROVINCE OF VENICE	
Venezia Campo SS Apostoli Sestriere Cannaregio 4547/4552	Tel. 041-5446810
Fossò Via Roncaglia 1	Tel. 041-5446690
Marcon Viale della Repubblica 2	Tel. 041-5446680
Martellago Via Friuli 28	Tel. 041-5446780
Mira Via Venezia, 120	Tel. 041-5446730
Mirano Via Cavin in Sala 39	Tel. 041-5446710
Noale Via Tempesta 31	Tel. 041-5446630
Portogruaro Via S. Agnese 28	Tel. 0421-480810
San Donà di Piave Via Vizzotto 98/100	Tel. 0421-480800
Spinea Piazza Marconi 17	Tel. 041-5446670
Venezia Mestre Piazza Mercato 51 - Fraz. Marghera	Tel. 041-5446800
Venezia Mestre Via Miranese 256/h - Fraz. Chirignago	Tel. 041-5446600
Venezia Mestre Via Torre Belfredo 23 - Villa Toesca	Tel. 041-5446750
Venezia-Jesolo Lido – Via Firenze 6	Tel. 0421-480820

PROVINCE OF VICENZA	
Asiago Piazza Carli 42	Tel. 0424-596090
Bassano Del Grappa Piazza Garibaldi 8	Tel. 0424-596100
Bassano Del Grappa Piazzale Firenze 2	Tel. 0424-596060
Bassano Del Grappa Villaggio S. Eusebio 94/a	Tel. 0424-596080
Belvedere di Tezze sul Brenta Via Nazionale 47	Tel. 0424-596020
Breganze Piazza Mazzini 2	Tel. 0445-617050
Bressanvido Via Roma 94	Tel. 0444-577000
Calvene Via Roma 22	Tel. 0445-617030
Camisano Vicentino Piazza Pio X 2	Tel. 0444-577010
Cassola Via Martiri del Grappa 3	Tel. 0424-596040
Cassola Via Pio X/Angolo G. D'Arezzo – Loc. S. Giuseppe	Tel. 0424-596240
Conco Piazza San Marco 20	Tel. 0424-596170
Dueville Piazza Monza 30/31	Tel. 0444-577020
Malo Via Vicenza 97 – Loc. San Tomio	Tel. 0445-617070
Marostica Via Mazzini 84	Tel. 0424-596200
Mason Vicentino Via Marconi 85	Tel. 0424-596000
Monticello Vigardolo Via Spine 3B	Tel. 0444-577090
Mussolente Via Vittoria 47	Tel. 0424-596050
Nove Via Molini 2	Tel. 0424-596110
Romano D'Ezzelino Via Roma 62	Tel. 0424-596140
Rosa' Via Dei Tigli 7	Tel. 0424-596150
Sandrigo Via Roma 34	Tel. 0444-577040
Sarcedo Via Schio 34	Tel. 0445-617010
Schiavon Via Roma 120	Tel. 0444-577050
Schio Via Cementi 8	Tel. 0445-617090
Tezze sul Brenta Via Risoramento 23	Tel. 0424-596180
Thiene Viale Bassani 26/28	Tel. 0445-617110
Vicenza Laghetto Via dei Laghi 135	Tel. 0444-577060
Vicenza Porta Castello Viale Roma 10	Tel. 0444-577070
Villavla Via S. Antonio, 43	Tel. 0445-617130
Zane' Via Trieste 110	Tel. 0445-617140

SUMMARY DATA AND ALTERNATIVE PERFORMANCE INDICATORS

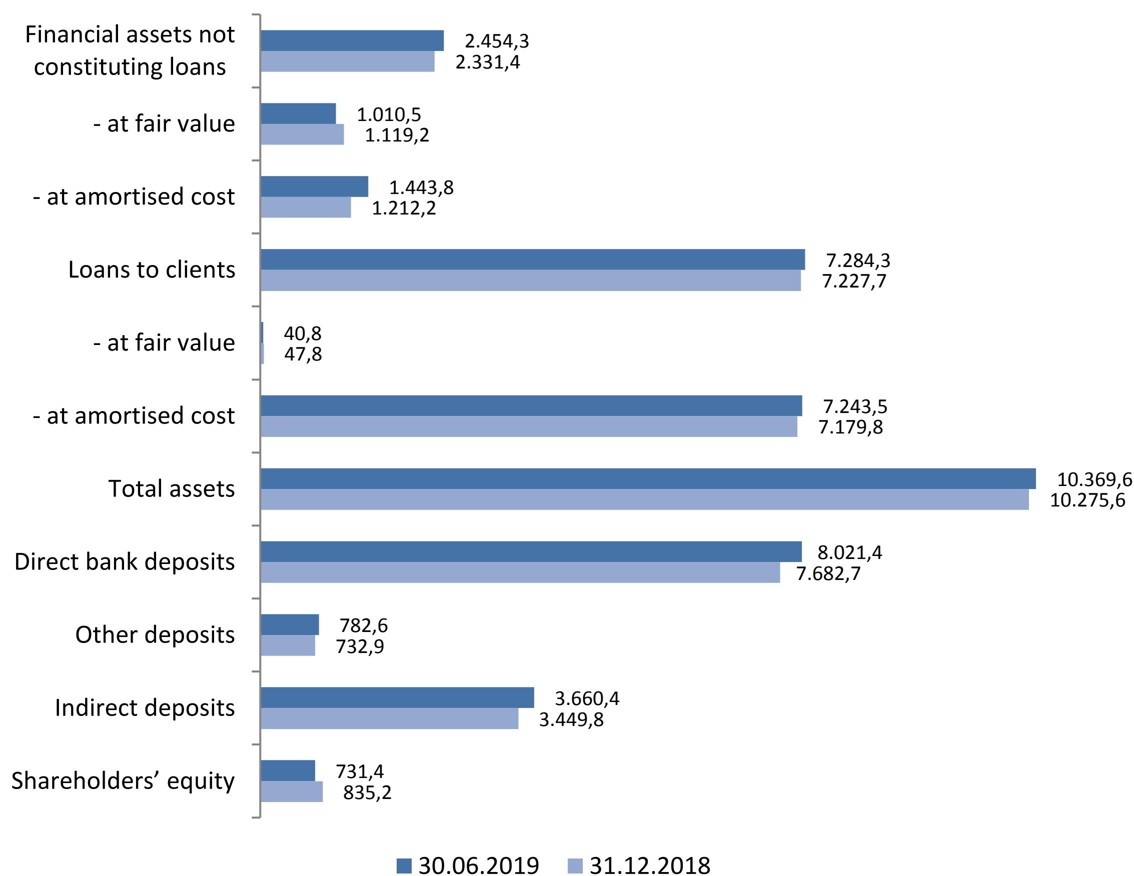
This section, the Interim Report on Operations and the Condensed Half-Year Financial Statement contain information not directly referable to the financial statements. The methods for aggregation of balance sheet items in order to produce this information are described in the Explanatory Notes section of the Condensed Half-Year Financial Statement.

Key economic data



Profit and loss figures	30.06.2019	30.06.2018	Changes	
(€ million)			**Absolute**	**% Change**
Interest margin	90.9	82.9	8.0	9.6%
Net commissions	44.7	43.1	1.6	3.7%
Net result of assets and liabilities at fair value	(14.3)	4.5	(18.8)	-422.2%
Net operating income	133.4	142.4	(9.0)	-6.3%
Net operating costs	(94.5)	(107.1)	12.6	-11.8%
- of which payroll	(46.9)	(50.5)	3.5	-7.0%
- of which other administrative expenses	(42.2)	(46.9)	4.7	-10.1%
Net operating income	38.9	35.3	3.6	10.2%
Net value adjustments	(54.0)	(15.9)	(38.1)	239.9%
Goodwill value adjustments	(99.6)	0.0	(99.6)	n.a.
Net profit	(101.5)	15.3	(116.9)	-762.1%

Key balance sheet data



Balance sheet data	**30.06.2019**	**31.12.2018**	**Changes**	
(€ million)			**Absolute**	**% Change**
Financial assets not constituting loans	2,454.3	2,331.4	122.9	5.3%
- at fair value	1,010.5	1,119.2	(108.6)	-9.7%
- at amortised cost	1,443.8	1,212.2	231.5	19.1%
Loans to clients	7,284.3	7,227.7	56.6	0.8%
- at fair value	40.8	47.8	(7.1)	-14.8%
- at amortised cost	7,243.5	7,179.8	63.7	0.9%
Total assets	10,369.6	10,275.6	94.0	0.9%
Direct bank deposits	8,021.4	7,682.7	338.7	4.4%
Other deposits	782.6	732.9	49.7	6.8%
Indirect deposits	3,660.4	3,449.8	210.6	6.1%
Shareholders' equity	731.4	835.2	(103.8)	-12.4%

Main indicators

Economic, financial indicators and other information	30.06.2019	31.12.2018
Structural indicators		
Financial assets / total assets	94.2%	93.5%
Gross loans to clients / Direct funding from clients (retail)	96.3%	99.6%
Fixed assets / total assets	1.6%	2.5%
Total risk-weighted assets (RWA) / Total assets	60.1%	63.0%
Goodwill / Total assets	0.0%	1.0%
Number of employees	1,303	1,327
Number of branches	162	170
Profitability indicators		
ROE	(24,7%)	4.2%
ROA (net profit/total assets)	(1.0%)	0.4%
Cost to income ratio	67.0%	66.4%
Risk ratios		
Net non-performing loans / Net loans to customers	2.3%	2.5%
Net non-performing loans /net equity	22.3%	21.7%
Texas ratio (Net non-performing loans/tangible equity)	46.3%	51.8%
Gross non-performing loans / gross loans to clients	8.8%	8.7%
% coverage of bad debts	60.1%	55.5%
% coverage of non-performing loans	50.9%	44.0%
% coverage of performing loans	0.8%	0.9%
Regulatory aggregates and ratios		
Class 1 Primary Capital (CET 1)	731,681	727,860
Total own funds	861,681	857,860
Total risk-weighted assets (RWA)	6,228,918	6,471,938
CET 1 Ratio - Primary Tier 1 capital	11.7%	11.2%
Total Capital Ratio - Total own funds	13.8%	13.3%
Leverage ratio (fully phased-in CET 1 definition)	6.1%	6.1%
Leverage ratio (transitional CET 1 definition)	6.6%	6.7%
Equity security		
Book value per share	14.94	17.06
Tangible book value per share	14.55	14.63
Basic EPS (earnings per share)	(4.15)	0.70
Diluted EPS (earnings per share)	(4.15)	0.70
Listing prices of the share (Hi-Mtf Market)		
- minimum price	11.90	11.90
- maximum price	11.90	11.90
- average price	11.90	11.90
Price/equity	0.80	0.70
Price/tangible equity	0.82	0.81

Indicator	Description/reconciliation
Cost to income ratio	Relationship between (i) operating costs and (ii) reclassified net operating income
ROA (net profit/total assets)	Ratio between (i) net profit and (ii) average total assets

INTERIM MANAGEMENT REPORT

THE OPERATIONAL CONTEXT DURING THE FIRST HALF OF 2019

THE MACROECONOMIC SCENARIO ([1])

The prospects for the international economy continue to be affected by the risks associated with a further escalation of global trade tensions and a slowdown in growth in China. Doubts remain as to when and how the UK will leave the European Union (Brexit).

The outlook for the global economy looks weak, despite growth in the first quarter of 2019. Of the advanced countries, the US and Japan, the expansion of output in the first three months of this year was mainly due to a fall in imports and the accumulation of stocks, in a context of weak domestic final demand. According to the latest assessments of manufacturing purchasing managers (the PMI, or purchasing managers' index), cyclical conditions deteriorated in all major economies in the second quarter.

In Brazil, India and Russia, GDP growth slowed in the first quarter. In China growth remained stable, but the latest economic indicators point to a slowdown in activity in the spring.

Global trade contracted further in the first three months of 2019 (down 0.8% year-on-year). Imports from the United States, Japan and emerging Asia, particularly from China, fell while imports from the Euro area increased moderately. International trade was affected both by the trade restrictions imposed since last year and the consequent deterioration in business investment and confidence.

The US administration strengthened protectionist measures, particularly against China, and has suggested further protectionist measures, also against other countries, adding to concerns about further trade tensions.

Consumer inflation remains moderate in major advanced economies, despite generally good labour market conditions. Expectations for long-term inflation derived from financial market yields declined in both the US and the Eurozone. According to the forecasts released by the OECD in May, global GDP is expected to slow to 3.2% this year.

At its July 31 meeting, the Federal Reserve cut interest rates for the first time in ten years, in an attempt to sustain the long trajectory of economic growth, also by insulating the economy from growing global risks.

The long-awaited cut of a quarter point cut is the first such decision since 2008, when it set interest rates at near-zero levels. But, unlike the 2008 move to avoid a recessionary phase, the manoeuvre at the end of July appears to be a preventive measure to protect the US economy from the slowdowns of the Chinese and European economies and from uncertainties arising from commercial tensions created by President Trump.

Economic activity in the Euro area remains weak and subject to downside risks. Inflation remains at low values. The Governing Council of the European Central Bank (ECB) prolonged monetary expansion and opened discussions on the further expansionary measures that will need to be taken if the macroeconomic environment does not improve.

([1]) Sources: ABI Monthly Outlook, ISTAT, Bank of Italy – Economic Bulletin – European Central Bank – Eurosystem – European Commission

Output grew by 0.4% year on year in the first quarter, driven by domestic demand and the weak positive contribution of foreign trade. Among the major countries, activity accelerated in Spain, Germany, and, to a lesser extent, Italy, but has begun to slow in France.

The most recent economic indicators suggest that GDP in the region this spring increased at a slower pace than in the first three months of the year, mainly due to the effects of trade tensions on foreign demand, which affected the German manufacturing sector in particular. In June Eurocoin (€-coin) indicator developed by the Bank of Italy, which estimates the underlying dynamics of output, remained at very low levels. SMEs report a decline in manufacturing activity and moderate growth in services. Firms' expectations of foreign sales are weak, particularly in Germany.

According to projections made in June by Eurosystem central banks, GDP is to increase by 1.2 per cent in 2019 and by 1.4 per cent per year in the two-year period 2020-21 (round 0.3 percentage points less than forecast in March). These projections bear downside risks.

Twelve-month inflation remained moderate during the spring. In June, on the basis of preliminary data, it stood at 1.2%. The performance of the underlying component was also contained (1.1% in June), affected above all by the weak trend in the prices of non-energy industrial goods.

In the projections formulated in June by the experts of the Eurosystem, the inflation forecast for 2019 is 1.3% on average in the year; in 2020 and 2021, price growth is expected to reach 1.4% and 1.6% respectively.

The Governing Council of the ECB announced expansionary measures: it extended the minimum horizon within which it expects to maintain its reference rates unchanged and confirmed its decision to fully reinvest the capital redeemed on maturing securities under the Expanded Asset Purchase Programme (APP) for an extended period of time after the first official rate hike. It also announced details of the new Targeted Longer-Term Refinancing Operations (TLTRO3), with the aim of helping to maintain expansionary monetary conditions. It was also stressed that, in the absence of improvements in the macroeconomic framework, an additional monetary stimulus would be needed, taking into account all available instruments.

After the modest increase recorded in the first three months of 2019, economic activity in Italy should have remained static or slightly decreased in the spring. The weakness of the industrial cycle, which mainly reflects the persistence of international trade tensions, would only have been partly offset by the favourable trend in services and construction.

In the first quarter, GDP growth returned to a barely positive level (0.1 per cent compared to the previous period). This activity was supported by foreign trade, investments in construction and consumption, but was held back by the accumulation of inventories and a reduction in investments in machinery, equipment and means of transport. The sharp fall in imports was mainly due to a fall in the demand for means of transport. The increase in value added was robust in construction, moderate in industry in the strict sense, while services contracted.

According to the information available so far, GDP is expected to remain steady or slightly decline in the second quarter. The weakness of the manufacturing cycle has particularly affected Italy and Germany, countries with strong manufacturing and commercial ties.

Available economic indicators suggest that industrial production would fall again in the second quarter after rising in winter. In the coming months, companies are expecting a slowdown in demand, due to a deterioration of the foreign component, and point to a modest increase in investment plans for the year as a whole.

Industrial activity grew by 0.9% in May, thanks to the rebound in the production of capital and consumer goods, only partially recovering from the decline in the previous two months. On the basis of estimates for June, industrial production as a whole was to fall by 0.7% in the second quarter.

Despite a strong recovery in disposable income, household spending grew only slightly in the first three months of 2019. The propensity to save continued to rise. The most recent economic data also suggests weak consumption growth in the second quarter.

Household consumption increased by 0.1% in the first quarter compared to the previous period, as a result of a new rise in expenditure on services. On the other hand, purchases of goods, in particular durable goods, decreased.

The expansion of consumption only partly reflected the strong increase in disposable income net of inflation (up 0.9% quarter-on-quarter), which was sustained by a rise in income from employment. The propensity to save has risen, a phenomenon that is related to the increased uncertainty regarding the economic outlook reported by household confidence surveys.

According to our estimates, based on the most recent economic information, consumption grew at a very low rate in the spring, while expenditure on non-durable goods stagnated. On the other hand, sustainable consumption, which accounts for about one tenth of household expenditure, made a positive contribution, linked to the sharp increase in car registrations, but it is still below the level prior to the entry into force, in September of last year, of the new emissions legislation. After a temporary increase in May, the household confidence index fell again, continuing the trend evident since late 2018. Expectations for the overall economic situation and employment have deteriorated.

Italian exports increased slightly in the first quarter, despite a contraction in world trade. In the first four months of the year, the current account surplus widened and foreign investors purchased Italian government securities. The Bank of Italy's debit balance on the TARGET2 payment system was reduced. Italy's net foreign position is close to balance.

In the first quarter, exports of goods and services by volume increased by 0.2% over the previous period. The slowdown in the goods component was marked, particularly in markets outside the European Union (EU), where the fall in sales in the United States, following strong growth in the final months of 2018, weighed heavily.

Inflation declined slightly, impacted by the slowdown in energy and food prices and by the weakness of the core component. Business, household, and analyst expectations remain weak, although they have been revised slightly upwards compared to the first quarter.

The year-on-year variation in the Harmonised Index of Consumer Prices (HICP) in June was 0.8%, based on preliminary data. The seasonally adjusted, year-on-year change over three months was zero.

Net of the food and energy components, inflation stood at 0.4%. The weakness of the underlying component, consistent with the stagnation of the economic cycle, reflected the fall in the prices of non-energy industrial goods and the modest dynamics of service prices.

FINANCIAL AND MONEY MARKETS

The aggravation of commercial tensions and the deterioration of growth prospects were reflected in a broad-based decline in long-term yields in the major advanced economies. Equity price volatility has increased. The outlook for the Euro against the dollar remains uncertain.

In the second quarter of the year, long-term interest rates continued to fall in all major economies as a result of worsening growth prospects and the consequent expectations of a prolonged period of monetary accommodation by the major central banks.

German ten-year government bond yields fell by around 30 basis points to -0.36% between late March and early July. Sovereign risk premiums fell across all Euro area countries: on ten-year maturity, German government bond spreads narrowed 130 by basis points in Greece, 75 in Italy, and 50 in Portugal and Spain. The fall was more limited in Belgium, France and Ireland.

Equity prices in major advanced countries fluctuated widely, with prices rising again in June, recovering the losses they had suffered in the previous month as a result of signs of cyclical deterioration and the renewed

trade tensions between the US and China. The implicit volatility of stock indices increased temporarily, but remained well below the levels reached during previous episodes of particular market stress.

The Euro exchange rate remained broadly stable against the dollar in the second quarter, while strengthening in nominal effective terms, mainly due to its appreciation against the pound sterling and the Chinese Yuan. In the valuations of derivatives markets, the outlook for the Euro's bilateral exchange rate against the dollar is uncertain. On one hand, the Euro positions of non-commercial operators are negative, suggesting a risk that the common currency; will weaken. On the other hand, the one-month risk reversal indicates that the cost of insuring against a significant appreciation against the US currency is slightly higher than that of insuring against a sharp depreciation of the currency.

EQUITY AND BOND MARKETS

Share prices and government bond yields fluctuated widely. In May, Italian financial market conditions were adversely affected not only by the intensification of trade tensions between the United States and China and the signs of cyclical weakening, but also by uncertainty as to the direction of budgetary policies. They subsequently benefited from the general reduction in risk premiums fostered by the increased monetary accommodation and, in early July, the review of the expected deficit for the current year and the consequent decision of the European Commission not to recommend the launch of an excessive deficit procedure for Italy.

Italy's sovereign risk premiums, as measured by the yield spreads between Italian and German government bonds, increased sharply as uncertainty as to the direction of fiscal policies intensified, reaching 287 basis points over a ten-year period in May. This phase also saw an increase in the premium component corresponding the risk of redenomination of debt, calculated as the difference between the premiums on credit default swaps (CDS) on Italian government bonds regulated by the new International Swaps and Derivatives Association 2014 (ISDA 2014) regulation, and premiums on CDS entered into on the basis of the previous regulation.

The prospect of greater monetary accommodation has led to a general decline in long-term yields and risk premiums in the Euro area. This contraction was accompanied by a decline in spreads between Italian and German government bonds, which was further encouraged at the beginning of July by the deficit review expected in this year and the consequent decision by the European Commission not to recommend the launch of an excessive deficit procedure for Italy. The ten-year spread fell below 200 basis points in the second week of July, around 70 points above the level prevailing in April 2018. The premium component attributable to the risk of redenomination of the country's debt also decreased. The volatility implicit in derivative contracts on the Italian 10-year bond increased in spring, though it remained far from the peaks seen in 2018.

In May, share prices were impacted by the escalation of trade tensions between the US and China, as well as Italian government bond tensions. The general increase in investor risk aversion led to a rebalancing of portfolios towards less assets considered less risky. Share prices then rallied and volatility declined, in line with global trends. The banking index only partially recovered from the decline observed in connection with the rise in Italian sovereign risk, due in part to the downward revision of expectations for the sector's profitability. Premiums on CDS by major credit institutions have fallen.

In the first quarter of 2019, Italian banks and non-financial corporations made net bond redemptions. In the second quarter, on the basis of preliminary data from Dealogic sources for gross issues alone, bank placements were lower (to around €9 billion, from €13 billion in the previous period), while those of non-financial companies were roughly unchanged (at around €8 billion).

In the first quarter of 2019, the net outflow of savings from Italian open-end mutual funds (under domestic and foreign law) continued, albeit at a slower pace than at the end of last year (€0.4 billion, compared with

€8.9 billion in the fourth quarter of 2018, according to Assogestioni data). Investor portfolios continued to incline towards assets deemed safer, benefiting bond and money market funds, while flexible, equity and speculative funds experienced net outflows.

ASSET AND FUND MANAGEMENT

The latest data on the total number of securities held with Italian banks (both under management and directly held by customers) - amounting to approximately €1,199.3 billion in April 2019 (approximately €58 billion more than a year before; an annual increase of 5.1%) - show that approximately 23.5% is held directly by consumer households (+2.8%), 24.3% by financial institutions (+18%), 43.3% by insurance companies (+4% annual change), 4.3% by non-financial companies (-19.7%) and approximately 2.8% by public administrations and family businesses. Non-resident securities, which accounted for approximately 1.7% of the total, fell by 17.3% over the past year.

Bank asset management in the fourth quarter of 2018 amounted to approximately €114.9 billion, a year-on-year increase of -5.1% (down €7.2 billion compared to the third quarter of 2018).

Overall, the individual portfolio management assets of banks, investment firms and UCITS management companies in Italy amounted to approximately €827.1 billion in December 2018, a decrease of -2.0% (down €9.8 billion compared to the previous quarter).

Assets administered by 'SIM' investment firms, amounting to approximately €11.6 billion, fell by 18.3% year-on-year, while those of 'SGR' asset management companies, amounting to €700.7 billion, recorded an annual decrease of 1.2% (down €1.6 billion, compared to the previous quarter).

In April 2019, the assets of open-ended Italian and foreign funds increased to around €1,013 billion (up €9.3 billion on the previous month).

24.1% of these assets are Italian funds and the remaining 75.9% are foreign funds. Compared to April 2018, equity funds decreased by €4.7 billion, bond funds by €9.1 billion and hedge funds by €252 million, which corresponded to a rise of €3.9 billion in flexible funds, €4.3 billion in monetary funds and €16.6 billion balanced funds. With particular regard to the composition of assets by fund type, it should be noted that in the last year, the share of balanced funds rose from 9.9% in April 2018 to 11.5% in April 2019, flexible funds rose from 24.7% to 24.8%, money market funds rose from 2.8% to 3.2%, while the share of bond funds fell from 39.4% to 38.1% and the share of equity funds fell from 22.7% to 22%. The portion consisting of hedge funds remained unchanged at 0.4%.

An analysis of the latest available data on household financial assets in Italy shows that this aggregate stood at €4,218 billion in the fourth quarter of 2018, down by 3.6% on an annual basis. The main trends of its components can be summarised as follows.

On the rise:

- the trend in banknotes, coins and bank deposits (both on demand and time deposits) showed an upward trend of 2.1%. The share of this aggregate in total household financial assets was 33% (up from 31.1% a year earlier);
- life insurance, pension funds and employee severance indemnities rose by 0.8%. The share of this aggregate was 23% (22% in the same period a year earlier).

In decline:

- bonds continued their downward trend (down by 6.7%) in the bank component (down 28.1%), while the public component rose (up 5.4%). This aggregate share of total household financial assets was 6.9% (7.2% in the previous year).

- shares and equity investments, down 13.3% year-on-year, make up 21.3% of total financial assets (down from 23.7% a year earlier).
- mutual fund shares decreased by 7.1% year-on-year and accounted for 11.5% of household financial assets (down slightly from 12% in the same period of the previous year).

THE BANKING SYSTEM

The trend in lending remains positive and solid for households, but slightly negative for businesses. The transmission of past increases in the cost of wholesale bank borrowing to interest rates on loans to customers continues to be very limited, but there are still signs that financing terms for some categories of companies have tightened. The improvement in credit quality continues. In May the three-month increase in credit to the non-financial private sector was slightly positive (0.7%, on an annual basis and adjusted for seasonal factors). The robust expansion in lending to households was offset by a moderate contraction in lending to non-financial corporations. Corporate lending has declined compared to the situation twelve months earlier, more markedly for small companies. This was due to weak credit growth in the manufacturing and service sectors and a sharp contraction in loans to construction companies.

Bank funding

Italian bank deposits increased moderately between February and May. The increase in deposits held by residents more than offset the decline in net wholesale funding in the form of repos conducted through central counterparties. Overall, the proportion of loans not financed by retail funding (the funding gap) has decreased further and is close to zero.

After rising in May as tensions on government bonds increased, Italian bank bond yields on the secondary market fell sharply. However, at the beginning of July they stood at around 10 basis points higher than in April 2018, while for banks in the rest of the Euro area they were 50 basis points lower.

According to initial estimates by SI-ABI in May 2019, funding from clients of all banks in Italy, consisting of deposits of resident customers (current account deposits, deposits with and agreed maturity, net of those connected with assignation of debts, deposits redeemable at notice and repurchase agreements - deposits are net of transactions with central counterparties) and bonds (net of those repurchased by banks) rose by 2.1% compared with a year earlier.

More specifically, bank funding from resident amounted to €1,765.2 billion. Before the start of the crisis – at the end of 2007 – bank funding amounted to approximately €1,549 billion (up approximately €216 billion since the end of 2007), broken down as follows: €1,024.5 billion in customer deposits (up €501 billion since the end of 2007) and €524.5 billion in bonds (down €284 billion since 2007). Observation of the various components continues to show a clear divergence between short and medium-term sources and long-term sources. Resident customer deposits (current accounts, certificates of deposit, repos net of operations with central counterparties, deposits with agreed maturity associated with assignation of debt transactions) showed an upward trend 3.8% in May 2019, marking an increase in absolute value on an annual basis of €55.3 billion.

Total deposits amounted to €1,525.2 billion in May 2019.

The annual variation in bonds was downward by 7.4% (down 8.1 in the preceding month), a decrease of €19 billion in absolute terms on an annual basis. The total figure for bonds stood at approximately €240 billion.

Deposits from abroad increased in April 2019. In particular, deposits in Italian banks amounted to approximately €329.3 billion, up 7.9% on the previous year's figure (up 12% on the preceding month). The

proportion of deposits from abroad in total funding stood at 13.4% (12.8% a year ago). The net flow of funds from abroad between April 2018 and April 2019 rose by approximately €24 billion.

In April 2019, net inflows from abroad (foreign deposits minus foreign loans) amounted to approximately €101.4 billion (up 14.6%).

This was to 5.7% of total domestic lending (4.8% a year earlier), while foreign lending – at the same date – amounted to approximately €228 billion. The ratio of foreign loans to foreign deposits was 69.2% (71% a year earlier).

The harmonised statistics of the European System of Central Banks show that the average rate of customer bank funding (which includes the return on Euro deposits, bonds and repos applied to the household and non-financial company sectors) stood at 0.57% in May 2019. The Euro deposit rate applied to households and non-financial companies was 0.33%, outstanding bonds 2.37%, and repurchase agreements 1.73%.

On the secondary market for government securities, the Rendistato, i.e. the figure for the sample of securities with a residual maturity of more than one year traded on the Italian Stock Exchange (M.O.T.), stood at 1.94% in May 2019, 8 basis points higher than the previous month (0.66% in August 2016: a historical minimum), and higher than the value in May 2018 (1.49%).

Gross return on the CCT secondary market was 1.47% in April 2019 (1.44% in March 2019; 0.06% in April 2018). With regard to the Italian government bond contracts (BTPs), the average return was 2.37% (1.60% in April 2018). Finally, the annualised gross annual return of BOTs (treasury bills) went from -0.46% in April 2017 to -0.06% in April 2019.

Bank lending

According to the banks interviewed last March as part of the Eurozone Bank Lending Survey, the supply criteria for new home loans to households tightened slightly in the first quarter of this year, while the criteria for corporate loans remained unchanged. Intermediaries reported that the general terms and conditions for access to credit were moderately affected by the higher costs of bank funding and, with reference to businesses, by the increased perception of risk on the macroeconomic outlook. Banks indicate that the growth in demand for funding has ceased.

Surveys of companies conducted in June (the Bank of Italy's quarterly survey of companies with at least 50 employees, and the ISTAT confidence survey, which includes smaller companies) confirm a general tightening of the conditions for access to credit in the second quarter of the year: the percentage of companies reporting a deterioration in conditions remained slightly higher than that of companies reporting an improvement. This stiffening is more pronounced for construction companies and, within manufacturing, for small companies.

The increase in the burden of credit funding for banks last year has so far only been only modestly passed on to customers in the form of interest rates on loans, partly due to the financial soundness of intermediaries and the widespread use of stable sources of funding. In May, the average cost of new loans to businesses stood at 1.4% and the cost of new loans to households for house purchases was 1.9% This was slightly higher than the level prevailing before the outbreak of tensions in the government bond market in the spring of last year.

In the most recent surveys conducted by ISTAT, the Italian National Statistics Institute, and the Bank of Italy, companies – especially those operating in the construction sector and smaller firms – reported that the terms for access to credit tightened further in the second quarter. In the first quarter, the flow of new non-performing loans as a percentage of total loans, net of seasonal factors and on an annual basis, fell again slightly (to 1.3%, below the average level in the two-year period preceding the global financial crisis). The

ratio fell more for loans to all companies (by two tenths of a percentage point, to 1.9%), despite a slight increase in the construction and manufacturing sectors.

The process of reforming the cooperative credit sector has recently been completed with the establishment of two groups – headed respectively by ICCREA and the Cassa Centrale Banca – to which a total of more than 220 intermediaries have adhered. As a result of these operations, Cassa Centrale Banca became the twelfth most significant group for supervisory purposes. The ICCREA group, which had already been classified as significant prior to the reform, was joined by 143 banks.

A comparison between the figures at the end of March and at the end of December last year (which, for reasons of comparability, refer to the sample of significant banks on a consistent basis over time, obtained by excluding the two newly formed co-operative group) shows a decrease in the impact of non-performing loans on total loans, both gross and net of adjustments, which is in line with plans for their reduction. The coverage rate also increased slightly.

In the first three months of 2019, again with reference to the homogeneous sample of significant banks, profitability declined compared with the same period of the previous year, affected by the fall in net commissions, although it continued to benefit from decreased operating costs and impairment losses on loans. The average level of capitalisation remained at the end of December levels, well above the regulatory minimum.

On the basis of initial estimates, total loans to Italian residents (private sector plus public administrations, net of repos with central counterparties) stood at €1,707.4 billion in May 2019, marking an annual change of +1.1%9 (+0.8% the previous month), calculated including loans not recognised in bank balance sheets because they are securitised and net of changes in stocks not linked to transactions (for example, changes due to exchange rate fluctuations, value adjustments or reclassifications).

At the end of 2007 - before the onset of the crisis - these loans amounted to €1,673 billion, increasing in absolute terms of around €34 billion since then.

Private sector loans to Italian residents increased by 1.19%9, amounting to €1,440.8 billion in May 2019.

Loans to households and non-financial companies stood at €1,298 billion in the same month. Based on estimates based on data published by the Bank of Italy, the annual change in loans to households and businesses calculated by including loans not reported in banks' financial statements as securitised and net of changes on balances not related to transactions (for example, changes due to exchange rate fluctuations, value adjustments or reclassifications) was 1.0%, up slightly on the previous month (0.9%). At the end of 2007, these loans amounted to €1,279 billion, an increase of €19 billion over the period in absolute terms.

According to official Bank of Italy data, in April 2019 the trend in loans to non-financial companies was down 0.69%9 (also down 0.6% in the previous month, down 5.9% at its lowest point in November 2013).

Total loans to households grew by 2.6% (2.5% in the previous month; down 1.5% in November 2013). The dynamics of loans to households remained solid, both in terms of mortgages for house purchase and consumer credit. In particular, the proportion of purchases financed by mortgage loans rose by almost two percentage points compared to the July-September quarter, reaching 80.5%. The ratio between the size of the loan and the value of the property remained just below 75%. Analysis of the distribution of bank lending by sector of economic activity shows that in April 2019 manufacturing, mineral extraction and services accounted for approximately 55.7% of the total, whereas manufacturing activity alone accounted for 25.7%. Financing for trade and for the hotel and catering business accounted for about 21.9% of the total, the construction sector for 12% and agriculture represented 5.5%. The residual sectors represented approximately 4%.

Credit continues to be influenced by the trend in investments and the economic cycle, the dynamics of which remain modest. Specifically, if the real value of gross fixed capital formation was equal to 100 in the fourth quarter of 2007, in the first quarter of 2019 the index was 81.8, an overall loss of 18.2 points.

The number of bankruptcies of companies is decreasing on an annual basis: the data published by Cerved show that in the first three months of 2019 2,823 companies went bankrupt, a decrease of 6.5% compared to the first quarter of 2018. This is confirmation of a positive trend which has continued for 11 quarters and which has reduced defaults to the levels of the early 2000s. However, this improvement was not evident throughout the peninsula: bankruptcies have increased once more in the Centre and North-East of the country areas, mainly affecting the Marche, Umbria and Veneto regions.

Non-bankruptcy insolvency proceedings are also down, due to the fall in forced liquidations (down 65% on an annual basis). However, after a long decline, arrangements with creditors are on the rise again, increasing by 25% compared to the first three months of 2018.

In the first quarter of 2019, the number of performing companies that were liquidated by the entrepreneur increased: according to estimates, more than 17,000 companies were closed, an increase of 6.2% compared to the previous year. This increase was observed in all sectors and areas of the country.

According to the latest Bank Lending Survey dated April 2019, the first quarter of 2019 the criteria for offering loans to businesses was unchanged. The criteria for home loans to households became slightly more restrictive. For the current quarter, intermediaries expect unchanged supply policies for corporate loans and a slight tightening for household mortgages. In the first few months of the year, the expansion in demand for finance by both businesses and households came to a halt. For businesses, the expansionary contribution of fixed investment and low interest rates have been offset by wider recourse to alternative sources of financing. Looking ahead, demand for loans from businesses is expected continue to weaken in the current quarter, while demand from households will strengthen.

In particular, the demand for corporate financing linked to investment has stabilised (in terms of the indicator expressed by the net percentage: +10%; +10% also in the fourth quarter of 2018).

There was no change in demand for financing: mergers, incorporations, restructuring of corporate structures, stock, working capital and debt restructuring all remained constant. The figure was +20%, linked to the level of interest rates.

SI-ABI reports show that in May 2019 the rate for loans in Euro to households for house purchases - which summarises the performance of fixed and variable rates and is also influenced by the change in loan composition according to the type of loan - stood at 1.84%. Almost three quarters of total new loan disbursements are fixed-rate loans: in the last month the share of the flow of fixed-rate loans was 72.6%. The average rate on new Euro loans to non-financial companies was 1.46%. Finally, the weighted average rate of total loans to households and non-financial companies stood at 2.58% in May 2019.

Differentials between rates

The spread between the average lending rate and the average borrowing rate to households and non-financial companies was 201 basis points in May 2019. Before the onset of the financial crisis, this spread exceeded 300 points.

Considering the margins on loans by banks to businesses and households in the main European countries (calculated as the difference between banks' interest rates for new loans and a weighted average rate of new deposits of households and non-financial corporations) in April 2019, for businesses the margin is 66 basis points in Italy, a value lower than the 108 basis points of Germany, 132 basis points of France and 171 basis points of Spain. For the household sector, the margin was 106 basis points in Italy, lower than the figure of 155 basis points in Germany, 126 basis points in France and 203 basis points in Spain.

The difference between the average rate on interest-bearing assets denominated in Euro vis-à-vis households and non-financial companies and the average rate in Euro on customer deposits consisting of households and non-financial companies stood at 1.69 percentage points in May 2019.

The difference in April 2019 is the result of the figure of 2.26% for the average interest rate on interest-bearing assets with households and non-financial company clients, and the figure of 0.57% for of the average cost of funding from households and non-financial companies.

Non performing bank loans

Non-performing loans, net of write-downs and provisions already made by banks with their own resources, amounted to €32.7 billion in April 2019, down sharply from €50.9 billion in April 2018 (a fall of €18 billion, or 36%) and €77.4 billion in April 2017 (down €44.8 billion, or 58%).

The reduction was in excess of €56 billion (down 63.3%), if the maximum level of net non-performing loans reached in November 2015 is considered.

The ratio of net non-performing loans to total lending was 1.87% (2.96% in April 2018, 4.43% in April 2017 and 4.89% in November 2015).

SIGNIFICANT EVENTS

SIGNIFICANT EVENTS DURING THE HALF-YEAR

Shareholders' Meeting

On 30 March 2019, the Shareholders' Meeting, in addition to approving the 2018 Financial Statements, the allocation of the profit for the year and the distribution of the dividend to shareholders, at its ordinary sitting approved, *inter alia*, a plan for the purchase and disposal of treasury shares pursuant to articles 2357 and 2357-ter of the Italian Civil Code, subject to the authorisation of the Bank of Italy.
The authorisation is for the purchase of treasury shares, in one or more tranches, up to a maximum of 420,000 (four hundred and twenty thousand) ordinary shares - calculated on the weighted average price of the weekly auctions of the last 3 months (€11.90) - excluding treasury shares already held in portfolio, and in any event, if lower, up to the maximum number of shares permitted by legislation applicable at the time, in all cases up to a maximum value of €5 million.
Authorisation to purchase treasury shares is granted for the maximum duration permitted by Article 2357, paragraph 2, of the Italian Civil Code, i.e. for a maximum period of eighteen months as of the date of the shareholders' meeting resolution authorising the purchase.
An authorisation to dispose of, transfer and/or use treasury shares without time limits was sought, in view of the absence of regulatory restrictions in this regard and to enable maximum flexibility, in terms of the time frame, for any disposal of treasury shares.
The purchases will be made on the Hi-MTF regulated market according to the operating procedures laid down in the regulations for the organisation and management of the said market.

The Shareholders' Meeting also elected the Board of Statutory Auditors by list vote for the three-year period 2019 - 2021, in accordance with articles 32 and 33 of the Articles of Association:

Astrid Kofler 03.04.1978 – Chartered Accountant and Statutory Auditor	Chairman of the Board of Statutory Auditors
Georg HESSE 24.08.1973 – Chartered Accountant and Statutory Auditor	Statutory auditor
Emilio LORENZON 17.06.1962 – Chartered Accountant and Statutory Auditor	Statutory auditor
Nadia Dapoz 13.11.1980 – Chartered Accountant and Statutory Auditor	Alternate auditor
Markus WISTHALER 24.10.1969 – Chartered Accountant and Statutory Auditor	Alternate auditor

The Shareholders' Meeting of 30 March 2019 also adopted a resolution on the remuneration of the Statutory Auditors appointed for the three-year period 2019 - 2021. The resolution provided as follows:

- €96,000 per year for the position of Chairman of the Board of Statutory Auditors
- €64,000 per year for the position of Statutory Auditor

- €250 daily for participation in meetings of the Board of Directors and Board Committees. The attendance allowance is also granted for the meetings of the Board of Statutory Auditors.

The attendance allowance does is not cumulative for multiple meetings on the same day. The gross emoluments and attendance allowances approved by the Shareholders' Meeting are unchanged from those paid to the outgoing Board in 2016-2018.
The approval of the financial statements for the year ended 31.12.2018 also marks the conclusion of the mandate for the statutory audit of the accounts granted to the auditing firm BDO Italia S.p.A., without possibility of renewal.
Accordingly, the shareholders' meeting conferred a new mandate pursuant to Article 13 of Legislative Decree No. 39/2010, on the basis of an explanatory report by the Board of Directors accompanied by the recommendation of the Board of Statutory Auditors, established the remuneration for the term of the mandate and the criteria for any adjustment of the fee during the term of office.
The award of the mandate for the statutory audit of the accounts to the auditing firm KPMG S.p.A. was approved for the period 2019-2027 in accordance with the applicable provisions and procedure pursuant to Articles 13, paragraph 1, and 17, paragraph 1, of Legislative Decree 39 of 27 January 2010 as amended, respectively, by Articles 16 and 18 of Legislative Decree No 135 of 17 July 2016, and by Article 16 of Regulation (EU) No 537/2014 of the European Parliament and of the Council of 16 April 2014.

Inspections by the Supervisory Board

On 18 February the Bank of Italy commenced an ordinary general inspection, which concluded on 12 June. At the date of drafting of this report, the relevant assessments have not yet been received.

Atypical or unusual transactions

With reference to Consob Communication No. 6064293 of July 28, 2006, there were no atypical and/or unusual transactions during the first half of 2019. Atypical or unusual transactions are understood, in accordance with Consob Communications No. DAC/98015375 of 27 February 1998 and No. DEM/1025564 of 6 April 2001, as transactions that are not part of normal business operations and which, due to their significance and/or importance, the nature of the counterparties, the method of determining the transfer price and the timing of the event, may give rise to doubts as to the correctness and completeness of the information in the financial statements, conflicts of interest, the safeguarding of the company's assets and the protection of shareholders.

Rating

Standard & Poor's

On 30 October 2018, S&P Global Ratings confirmed Volksbank's long-term rating at "BB+" with a "stable" outlook. At the same time, it also confirmed its short-term credit rating as "B". These ratings remain unchanged since the previous assessment.

According to the Agency, Volksbank benefits from good positioning in the Trentino-Alto Adige region, which traditionally has an average GDP per capita that is higher than the Italian average and low levels of

unemployment. S&P also pointed to the solidity of the bank's funding profile, which is concentrated on retail funding, as an additional strength.

S&P believes that Volksbank will be able to maintain an asset quality above the average of the Italian banking system without any impact on its capitalisation, and at the same time expects non-performing exposures to decrease as a percentage of the loan portfolio.

On the other hand, S&P's rating is affected by limited diversification and market coverage, an area of profitability that needs to be strengthened, and the still modest internal generation of capital.

DBRS

On 30 May 2019, DBRS Ratings Limited (DBRS) confirmed its rating of Volksbank, i.e. its "Long-Term Issuer Rating" at BBB ("low") and its "Short-Term Issuer Rating" of R-2 (middle). Similarly, the trend rating was maintained at "stable".

According to the Agency, the confirmation of the rating reflects the Bank's solid market share in its territory of reference, i.e. the Trentino-Alto Adige region, its stable funding position, and the progress made in reducing its stock of impaired loans. The assessment also took account of the low level of profitability and the still significant stock of impaired loans covered by modest levels of coverage.

FITCH

On 31 May 2019, Fitch Ratings confirmed the "Long-Term Issuer Default Rating (IDR)" at level BB+ and the "Viability Rating (VR)" at bb+. The long-term trading trend is considered "stable".

According to the agency, the assigned rating reflects the profile of a properly managed and operating regional bank with a business model that is not very diversified compared to that of larger domestic players and some of its direct competitors. It also reflects: the progress achieved in reducing impaired loans, which enabled a simultaneous reduction of risk capital, stable funding and liquidity profiles, although characterised by limited diversification, and modest profitability.

ONGOING PROJECTS

PSD2

On 23 December 2015 the EU Directive 2015/2366 of the European Parliament and of the Council on payment services in the internal market (so-called PSD 2 - Payment Services Directive 2) was published, and was implemented by Member States on 13 January 2018.

The main aims of the legislation are harmonisation within the European retail payments market, increased competition between operators and between products and channels, and increased attention to the new instruments made available by the rapid technological development that increasingly characterises the market for new retail payment products.

The Bank has completed the first phase of the project (intervention for foreign operations in January 2018) in line with regulatory deadlines. A second phase of the project is under way with the objective of fulfilling the most innovative requirements introduced by the legislation. These are designed to increase remote access security and to open account access to third parties with the consent of the account holder. This second strand of the project, concerning the security and access component, is being developed in accordance with the established deadlines (September 2019 and intermediate deadlines). These

developments will give the Bank the opportunity to pursue a number of opportunities, such as the creation of new services through partnerships with third parties.

GDPR

Regulation (EU) No 2016/679 establishes uniform levels of protection for the personal data of European Union citizens. This protection is the result of obligations incumbent on data controllers (companies and public bodies) and the rights that any data subject (natural person) may exercise in order to monitor the use of their personal data, in an age characterised by the digitisation and rapid circulation of information.

The confidentiality and protection of information has always been afforded special protection within Volksbank. This protection is achieved, including for the purposes of banking supervision obligations, through high levels of efficiency in its hardware and software systems, the security of the communication networks used, and control over its own system administrators. All processing is performed to high standards of protection, including when performed by authorised suppliers.

Volksbank adopts technical and organisational measures in accordance with the requirements established in Regulation (EU) No 2016/679 and the orders affecting the banking sector issued by the Italian Data Protection Authority and constantly updates them in response to the introduction or modification of products, services and technologies.

The Board of Directors, in its capacity as Data Controller, governs the privacy and data protection organisational model, with the support of the Data Protection Officer (DPO) and the internal offices responsible for overseeing the (physical and logical) security of personal data.

Volksbank processes personal data in accordance with the consent given, amended, or refused by each data subject with respect to the purpose of each act of processing.

All Bank employees undergo regular training and refresher courses in matters of privacy, given that they are the persons authorised, in their daily work, to process personal data and therefore play the most important role in all internal regulations.

Alongside regulatory planning, a number of business projects have been undertaken in order to support the transformation process undertaken by the Bank. The main project areas are:

Branch digitalisation

In recent years, the Bank has launched several initiatives for the automation and digitalisation of the Bank's branches and distribution channels, both internally and in collaboration with its IT services centre. In particular, the following lines of action were pursued during the first half of 2019:

- a plan to digitalise cheques was completed. This enables the Bank to transmit flows electronically to other banks, automating the check management processes and unifying them throughout the banking system, thus reducing the frequency of courier transports;
- plans to introduce cash recyclers and to replace traditional ATM devices with Evolved multi-function ATMs continue. These enable the recycling of cash and a reduction in the need feed cash to ATM machines (cash-in and cash-out functions);
- dematerialisation initiatives continue in branches, with the objective of making more documents available in electronic format. The use of advanced electronic signature (“AES”) is also being extended to the most frequent operations.

New omnichannel service model

The Bank aims to increase the level of its omnichannel offer, with a view to offering a seamless user experience, regardless of the *touchpoint* used (physical or digital). The ultimate goal is to offer the same products, services and level of support, on all currently active *touchpoints*, whether physical or digital, and to set the priorities for interventions on the basis of the real needs of customers.

As part of a dedicated project, the current model for the delivery of products and services was mapped through the various channels and the target omnichannel model was identified on the basis of customer needs. The mapping was performed using Personas and Journey Map techniques to track the delivery process ("as-is" and "to-be") of the Bank's main services on the various channels, and the interaction between them. A list of strategic actions and areas for action needed to close the gaps compared to the ideal model was then defined on the basis of the results of this first phase of the project. In the first half of 2019, work continued on implementing the various strategic initiatives with omni-channel focus.

New distribution model

A rethinking of the distribution model is a key initiative for the Bank's path to transformation over the next 3-5 years.

The project site is oriented towards understanding the digital propensity of customers and assessing the implications on the distribution model in the short and medium term. To this end, the importance of the Bank's presence on the territory and the level of dissemination of digital channels among the various customer segments were analysed. The findings that emerged were then validated through quantitative analysis, in order to rethink the delivery of products and services by exploiting new channels to increase engagement with the customer and gain greater knowledge of customers in order to optimise the sales channels.

On the basis of the analyses that were conducted, a new optimal service model was defined that adapts the Bank's strategy for the distribution of products and services, with objective of responding to the expectations of existing customers and finding new customers through a rethinking of the strategy for the use of the channels and for their integration. The model also takes account of the geographical diversity of the Bank's various areas of operation, proposing general guidelines that are tailored to the Bank's specific characteristics.

The first phase of the project was successfully completed with the approval of the new model by the Board of Directors in December 2018.

In a second design phase that began in early 2019, the new distribution model was tested through a pilot project in two selected and limited territorial areas. Using a pilot project enables the Bank to assess the effectiveness of the model, identify the measures required for improvement, define a plan for the gradual implementation of the distribution model over the rest of the Bank's perimeter, ensuring a customer experience that is consistent in all areas covered.

The new model will enable the Bank to make the current model efficient, operationally and economically, and to create new business opportunities for itself through the full exploitation and control of a distribution model focused on real needs.

Data platform

The project, which is at the launch stage, aims to develop a modern data architecture, i.e. a *data platform* capable of storing, managing, analysing and developing large quantities of data and offering relevant insights through the selective collection of data from both internal and external sources.

State-of-the-art data architecture can provide real and complete customer knowledge, make internal processes involving data searches and knowledge of the customer more efficient and faster, collect, homogenise and process large amounts of data in order to make Volksbank's service provision more effective, provide useful information to enable data-driven business logics, and create business intelligence tools for consulting near real time data. The analysis is preliminary to the development of predictive logic for improvement of the commercial service provision and of the user experience.

The main objectives are:

- Ownership of data, operational independence, and internal efficiency in the management of the Data Platform and data analysis.
- Aggregation of various data sources - including external data;
- Development of new client engagement opportunities.

Migration to new PREMIA procedure

In the first half of 2019, a project was launched for migration from the current procedure used by the bank to the new "PREMIA" procedure, which has become the market standard as it is in use by a large number of Italian banks.

The preparatory work for migration from the current foreign procedure to the new procedure has a major impact on the information system, as many interfaces require review and testing by the various ledgers in use at the bank (accounting, reporting, product manufacture, counterparties, finance, receivables, management control, anti-money laundering, etc.). The new procedure is scheduled to be activated in the first week of 2020. From then on, the network and internal offices will have a new, more efficient and technologically advanced system to offer customers a higher service in the foreign sector.

DWH (Data Warehouse) activation

Digital Transformation brings continual and far-reaching changes. Processes change, the way in which stakeholders interact evolves, and information timing (the quality and quantity of information) is increasingly decisive in competitive decisions. The effective introduction of the Information Governance (IG) framework requires the adoption of several architectural software components. These include the Datawarehouse/Data Lake (DW/DL), Data Glossary/Lineage (DG/DL), Data Quality (DQ) and Business Intelligence (BI) platforms.

The various regulatory sources also define an important perimeter of reference for corporate data governance standards that involve adequate data/information management and a reporting model. In particular, if a company data warehouse is used for analysis and reporting purposes, the procedures for data extraction, transformation, control and uploading to the centralised archives - as well as the data exploitation functions - are documented in detail to enable verification of data quality, and the reporting system enables the production of prompt, high quality information for the supervisory authority and the market.

Thus the new Datawarehouse establishes a new service model between SEC and Volksbank, based on the option of autonomously accessing certified data without the assistance of professionals with specific IT knowledge. The bank intends to introduce the Datawarehouse into the standard practice, continuously increase the quality of information, reduce the analysis timescales and automate reporting processes. The work that commenced in the final months of 2018 accelerated sharply in the first half of 2019, and it was hoped that the project will be mostly completed by the end of this year.

Bancassurance of the future

Within the scope of the definition of "Bancassurance of the future", three strategic pointers were identified that are indispensable for the launch of the project:

- Vision: to develop a new concept of distribution that, in accordance with the new legislation, is based on the centrality of the customer's requirements, not those of the product;
- Objective: to make customers perceive the Bank as the only place where they can find answers to all their requirements, not just financial requirements, but also those of an insurance protection nature;
- New business approach: simplification, IT tools, efficient processes, commitment, omnichannel sales and communication are all milestones to be reached in order to create added value and provide it to the end customer.

The project aims to improve the 360° insurance sector, targeting mainly individual customers in all managed segments, but with differentiated approaches.

Building the "bancassurance" model of the future is crucial to remaining competitive with a view to diversifying distribution channels, increasing margins, updating and standardising the day-to-day operation of contractors and, naturally, meeting the ever more complex needs of customers.

In preparing the project, an in-depth analysis was conducted using sophisticated and innovative approaches (e.g. design thinking), in order to understand clients' various needs, ranging from the moment of a client's perception of a risk, to the occurrence of an event covered by the individual insurance policy, to the handling of a claim.

The project, which began in the first few months of 2019 and will continue throughout 2020, provides a single access platform for our consultants, regardless of the insurance company with which the policy will be contracted. The platform will significantly optimise the user experience, with positive impacts that will inevitably be reflected in advise given to clients.

"Dream home" project

The home loan a key product for the bank, as it enables the bank to establish a lasting relationship with the client. Given the importance of this product, during 2018, a strategic project entitled "Expansion of the value chain - dream home" was launched with the objective of going beyond the provision of a mortgage product to accompany the client through all phases of the dream home process.

New agile design methodologies entitled 'design thinking' - a client-centred approach to the relationship - been applied in this project.

During the project, various proposals for services were identified in order to position the bank as a point of reference for the dream home in our territory.

The dream home concept has also been the subject of discussion of the "*Our Future*" project, in which interesting ideas are identified for inclusion in planning.

As provided in the 2019-2021 strategic plan, the plan is to become the reference bank for the dream home concept by combining new services, specialist professionals and mortgage advice.

Targeted information and advertising campaigns will inform clients of a tool enabling clients themselves to avail of this new service.

Wealth Management 2.0

As part of the plan to evolve the investment advice services provided by the Bank, an advanced version of the Objectway consulting platform is being developed. The objective of the project is to improve investment

consultancy services from an IT standpoint, but especially in terms of approach. It is specifically directed at private clients in all segments, but uses differentiated approaches.

Redefining the approach to the investment advice service is crucial to remaining competitive. This can be achieved by diversifying distribution channels, expanding the commercial offer in line with developments in the market and client profiles, updating and standardising the daily operations of contractors, and of course meeting ever more complex client requirements.

CRM phase 2

CRM is an enabling factor for the supply and management of the omnichannel business models that our industry is evolving towards: channel integration, automation of commercial processes and increasingly targeted analysis/use of data are keys to the future success of banks.

In particular, some developments in CRM constitute enabling factors for the supply of a new distribution model.

The CRM - phase 2 project aims to:

- expand the number of channels integrated into the CRM (mobile banking, ATM, kiosk, new direct banking functions, CTC outbound, Chat, Mail, etc.), giving priority to the channels and enabling functions for the new distribution model (outbound contact centre, lead management in particular)
- activate the analysis functions (Cognos, interface with commercial DWH), but with a lower priority than integrating channels (in accordance with budget)
- gradually activate all available new channels.

Covered Bond

Covered bonds (CBs) were introduced into the Italian legal system in 2005 and are regulated by second-level regulations.

Against a backdrop of the wider European market, the issue of these particular bonds have been of increasing importance in the Italian market, which was driven by both the "supply" side (the offer of a series of advantages and benefits, such as an expansion of funding and a reduction in the average cost of funding) and the "demand" side (the growing need for protection, e.g. instruments not subject to "bail-in" or dual form of guarantee).

RISK MANAGEMENT

The integrated measurement and control of financial, credit, counterparty, operational, reputational and strategic risks, together with the assessment of capital adequacy (ICAAP process) and liquidity risk (ILAAP process), are the responsibility of the risk management and control function (Risk Management Area), and are governed by a specific mandate ("Risk management charter") approved by the Board of Directors. The Area is hierarchically and functionally placed under the direct authority of the Board of Directors in order to give it the necessary autonomy, authority and independence.

As in previous years, the Risk Management Area has collaborated in the definition, implementation and verification of the Risk Appetite Framework (RAF) and related risk management policies, through an specific management process, as required by the relevant national and international regulatory authorities. At the highest level, the RAF defines risk tolerance and risk appetite, both of which are used to establish both the absolute level of risk that the Bank is a priori willing to assume, and the actual limits that it sets itself within this maximum level. Once risks within individual assets and changes in their structure over time have been identified, the objective to ensure prompt and accurate risk control and management. Any unfavourable changes can thus be recognised early thanks to systematic oversight, ensuring that corrective action on the risk structure is possible.

The level of risk assumption is therefore a function of the Bank's ability or willingness to assume risk and depends on its capital base, which is set to hedge risk, its income capacity, and the risk that it is willing to assume in order to achieve its economic and strategic objectives. The ICAAP (Internal Capital Adequacy Assessment Process) is responsible for verification of capital adequacy, while the ILAAP (Internal Liquidity Adequacy Assessment Process) is responsible for assessment and monitoring of liquidity risk.

With reference to the first half of 2019, this section describes the dynamics of the main risks, the evolution of monitoring and control systems, activities relating to the second pillar, and finally some information on the foreseeable evolution of company risks.

THE FIRST HALF OF 2019

The work of the risk control office in the first half of 2019 was guided by the Programmatic Plan for 2019, as approved by the Board of Directors on 20 February 2019. From a general standpoint, the intention of the Plan is the familiar objective of intensifying efforts to encourage an ever deeper penetration and dissemination of the risk culture at all management and management levels, on the basis of the guidelines established in the Risk Management Policy, a document that defines, in an organic and systematic manner, the policies for identifying, measuring, managing and controlling risks, together with the creation of conditions for such risks to be consciously assumed. On the other hand, its primary objective is to monitor the bank's risk profile on a continuous basis in order to identify and prevent any deviations from the bank's risk appetite as set out in the *Risk Appetite Framework* (RAF) and related *statements* (RAS), as approved by the Board of Directors on 21 December 2018.

The most significant and prominent risk control activities include:

- the first two-year review of the Bank's recovery plan, updated in accordance with the expectations of the Supervisory Authority, which defines, on the one hand, the indicators and the relevant thresholds that determine the activation of the plan and, on the other hand, the actions to be taken for recovery within appropriate timescales under normal business conditions;
- support for the preparation and submission, pursuant to the Implementing Regulation (EU) of 23/10/2018, of the new supervisory report for the preparation and implementation of a resolution plan for financial institutions;

- the production of a feasibility study on the possibility of transitioning from the current standard (Standardised Approach) to the AIRB (Advanced Internal Rating Based) approach for the calculation of capital requirements relating to credit risk exposure;
- the strengthening level 2 controls and checks on the risk classification processes for credit exposures and their analytical and flat-rate assessment in accordance with IFRS9 accounting standards;
- use testing and support activities for the new company *datawarehouse* (DWH) produced by the outsourcer of the information system;
- the strengthening of *data governance* and *data quality* controls for the monitoring of IT risk and outsourcing risk.

Financial Risks

Market risk is defined as the risk of loss on proprietary financial instruments arising from possible fluctuations in financial market variables (rates, volatility, exchange rates, share prices), considering the possibility that each individual financial instrument is exposed to one or more of the above risks. Volksbank therefore measures market risk as changes in the value of stocks due to market movements.

Volksbank adopts a system for measuring and controlling market risks based on the Value-at-Risk (*VaR*) method, on which it bases a system of maximum tolerable risk and loss limits (risk capital) over various time horizons. The *VaR* method calculates the maximum potential loss of a portfolio during a given time horizon and with a given probability under normal market conditions. Value-at-Risk is a homogeneous measurement system, applicable to all financial instruments. Thus risk values calculated in terms of time and daily profitability can be compared. For the calculation of the *VaR*, the Bank uses the parametric model of variance-covariance provided by the company Prometeia, supported by hybrid type internal models used for the necessary verifications.

In addition to the analysis of VaR and maximum sustainable loss, the monitoring of market risk is based, through specific systems of limits, on the control of counterparty risk, country risk, the sensitivity of the portfolio to market rate risk (*basis point value*) and credit risk (*credit risk sensitivity*).

In order to avoid and prevent possible overruns of authorised risk limits, a standardised daily reporting system monitors and verifies any approach of the thresholds.

The verification and control of the market risk profile of assets held are discussed weekly at the Internal Finance Committee and monthly at the Finance Committee, during which a specific monthly report is presented by the Risk Management Area.

Finally, the risk management area is responsible for validating and continuously verifying the system of pricing of the financial instruments held, in order to maintain a reliable price profile and a member of market prices (fair value).

Credit risk

Credit risk is the risk of the total or partial insolvency of a borrower and constitutes the Bank's main risk factor, in line with its with its own characterisation as a bank oriented towards *retail* customers and small and medium-sized enterprises.

Volksbank's credit risk management is therefore aimed, on the one hand, at improving the processes for granting credit lines so that they are compatible with the underlying risks, while on the other hand identifying in advance any deterioration in the solvency of a client with a credit line, through increasingly effective and reliable monitoring systems.

The Credit Risk Policy sets out in a single document the guidelines for management of all possible forms of credit risk, as defined in the more general Risk Management Policy (insolvency risk, risk of changes in the degree of solvency, risk of foreign currency exposures, risk of concentration of the credit portfolio, residual risk). In particular, the document sets out:

- the definition of economic *risk appetite* in relation to client credit risk;
- the scope of application, with explicit mention of the Bank's reference values in its lending activities as applied in its Annual Credit Strategy and management policies;
- the organisational model, specifying the minimum responsibilities and duties assigned to each of the company departments involved;
- a description of the credit risk management and control process, broken down into five key phases: the credit granting phase, the control and monitoring phase for assigned positions, the risk measurement and quantification phase, the adverse scenario analysis phase (stress tests) and the non-performing credit management phase;
- for each phase, the essential activities for execution and monitoring and control are outlined, with regular references to the detailed internal documentation;
- risk mitigation techniques, i.e. the collateral obtention and management process, with its implications for capital requirements;
- the system for monitoring loan positions, which is based on five pillars: precise monitoring by means of periodic reviews, performance monitoring through the internal rating system, performance monitoring of individual exposures by the Risk Management office as part of the second level controls, the supervisory and *early warning* mechanism for positions at risk, and monitoring of risk mitigation instruments;
- the model for determining the probability of default of the loan portfolio and the quantification of the expected and unexpected loss;
- the effects of credit risk on the Bank's assets and balance sheet, i.e.: identification of capital requirements for credit risk (pillar I); regulatory and internal limits for concentration risk (pillar II); criteria adopted for value adjustments due to loan impairment.

From an operational standpoint, the credit monitoring process is guaranteed on a continuous basis through an automatic system for classifying anomalous positions (GDC, Credit Management). It uses an *early warning* engine which, based on performance rating and an extensive series of indicators calculated and entered on a daily basis, can quickly identify the emergence of deteriorations. Moreover, the system facilitates a streamlining of the internal process of classification and management of problem clients, which in turn is governed by specific regulations containing details of the controls to be performed, the procedure for classifying anomalous positions, and operating instructions for the administration and management of such positions.

In addition to the usual risk classes for non-performing loans established by the supervisory board (bad debts, probable defaults, past due exposures and/or impaired overruns, exposures subject to the granting of "*forborne exposures*" tolerance measures) the system also provides for two classes of "performing" customers, graduated according to the presence of anomaly indicators which, while not requiring classification in the category of non-performing loans, nonetheless require more careful management of the risk profile.

In particular, a system is in place for monitoring and managing so-called "*pre-past two*" positions, i.e. positions in a state of overdraft persisting for more than 30 days, in order to prevent them from attaining "*past two*" status. Pursuant to Bank of Italy Circular 285/2013, within the credit monitoring process, the Risk Management function verifies the correct monitoring of individual credit exposures, in particular non-performing exposures, and the assessment of the consistency of classifications and the fairness of allocations. In particular, the Risk Management function:

- verifying that the monitoring of both performing and non-performing exposures takes place methodically according to a systematic approach, in accordance with internal organisational processes;
- checks that the monitoring uses methodologies and procedures that enable
  - prompt identification and reporting any anomalies;
  - adequate adjustments and write-offs;
- assessment, with reference to credit management, of
  - the consistency of classifications, i.e. the correspondence of the allocation into credit classes with the provisions of internal regulations;
  - the appropriateness of provisions, i.e. the adequacy of coverage of the non-performing loan;
- assessment of the adequacy of the debt recovery process, in particular
  - the correct classification of non-performing loans;
  - the reliability of estimates of recovery times and of the degree of irrecoverability of non-performing loans;
  - the processing of guarantees, including the updating of expert reports.

Risk management controls take the form of

- spot checks, using predefined logic, for all categories of receivables;
- systematic controls, through the adoption of synthetic remote indicators applied to all outstanding exposures, at each stage of the life of the receivable.

In the event of conflicting assessments, the assessments made by the risk control function apply.

The adoption of *Credit Risk Mitigation* methodologies for the calculation of the capital requirement for credit risk in accordance with the Basel III provisions continues to determine the definition of the processes for the estimation, valuation and periodic revaluation of immoveable property used as mortgage guarantees, in order to scrupulously comply with the eligibility criteria and admissibility of such guarantees. During the first half of 2019, the entire portfolio of mortgage guarantees granted was subjected to periodic geo-referential revaluation by Nomisma, in order to assess, in view of the performance of the real estate market, which was significantly affected by the crisis, the state of the value of the properties and their adequacy with respect to the credit that they cover.

Monthly and quarterly credit risk reports produced for the Board of Directors and preliminarily discussed by the Internal Credit Committee are the main tool for monitoring the performance of lending activities and related risks, as well as compliance with risk objectives (RAFs) and guidelines defined in medium and long-term strategic planning. These include, *inter alia*, assessments of risk indices (probability of default and estimate of expected losses), methodologies used in calculations, scenario analyses to verify the behaviour of the loan portfolio in the face of unexpected events and analysis of the main risk phenomena.

COUNTERPARTY RISK

This is the risk that the counterparty to a transaction will fail to fulfil its obligations according to the procedures and timescales established in the contract.

Counterparty risk is regulated through a specific system of operating limits, based on a series of criteria for assessing the creditworthiness of counterparties, in separate manner according to their type (*corporate* or *financial*). The general rule is that all financial transactions must be executed exclusively with approved counterparties.

The limit of each counterparty is set by the Board of Directors and may be used by the treasury and investment services in accordance with specific percentage quotas of the limit, assigned to homogeneous categories of financial instruments.

Operational Risks

In contrast to credit and market risks, which the Bank knowingly assumes in return for risk, operational risks can generate losses, sometimes very significant losses, without the Bank obtaining any remuneration. Operational risks are naturally inherent in the execution of processes, in the characteristics of the products and services offered, and in the possibility of being subject to fraudulent or accidental events.

For these reasons, the bank is required to analyse the causes of operational losses and systematically detect and measure events with the aim of limiting and reducing the associated risks.

In accordance with the definitions of the Basel Committee, Volksbank considers operational risk to be "the risk of losses resulting from errors or inadequacies in internal processes, human resources and systems, or from external events". Legal risks are included, but strategic, reputational and systemic risks are excluded. The definition of operational risk therefore does not include opportunity risks (lost business), reputational damage and risks involving the entire banking system.

In 2003, Volksbank introduced an internal system for the detection and measurement of operating losses (*loss data collection*) with the aim of better managing potential sources of danger that could undermine the stability of the company. This system is based on a similar initiative, to which the bank adheres, which is undertaken at national level by the Italian Banking Association (ABI). With its DIPO (Italian Operational Losses Database) project, the ABI intends to raise awareness and assist banks in the implementation of these procedures, as well as creating a national database that enables banks to obtain more extensive and indicative statistical data and information.

The operational loss collection process is based on an internal reporting system, which detects and forwards to a central collection point, located in the risk management area, all events classified as operating losses above a minimum threshold of €500. These reports are integrated with losses arising from legal actions, complaints from customers, employment disputes, etc.

The systematic collection and analysis of this information over the past year has provided valuable insights and suggestions for the evaluation and optimisation of the Bank's processes and activities.

An assessment of operational risks also forms part of the assessment conducted by the company's control bodies upon the introduction of new products, services or other commercial initiatives, and the introduction or modification of new operating processes.

Management of operational risks is the responsibility of the Risk Management Area. In the context of the System of Internal Controls, operational risk management also comes within the ambit of Internal Controls Committee, which meets on a monthly basis in order to coordinate all company control functions (Internal Audit, Compliance and Risk Management), issue control perimeters and the results of verifications, direct corrective actions to be implemented by operational offices and develop and disseminate a risk and control culture among operating structures.

Each quarter, the Risk Management Area produces a report on the bank's operational risk situation for discussion in the Internal Control Committee and submits it to the Board of Directors. The Board then has the task of identifying all potential critical situations, proposing countermeasures to prevent them, identifying operating processes that require review and those that remain to be defined.

THE ICAAP PROCESS AND PILLAR II RISKS

The ICAAP (Internal Capital Adequacy Assessment Process) is designed to provide support, even in advance of regulatory planning, in dealing with the impact of the introduction of the new Basel III regulatory framework, by which the supervisory authorities intend to reinforce the prudential rules of the international banking system by the introduction of a new definition of capital that is designed to strengthen capital through stricter requirements in terms of capital-quality instruments, the establishment of additional measures to reduce the pro-cyclicality of the rules (capital buffers), establish limits on leverage, and promote new liquidity management rules.

It should be recalled with regard to this process as of late 2012, Volksbank calculates the "first pillar" capital requirements for credit, market and operational risks using the so-called standardised methodology.

As is the case every year, the annual report was compiled and forwarded to the Supervisory Authorities in April. At the same time, the methodologies for calculating and analysing all risk types and the relevant stress tests to be performed were refined. Among other measures, the prospective analysis was extended to include the entire time horizon of the strategic plan (2019-2021/23) and capital absorption was broken down according to the logic of Volksbank's business lines, as defined in the strategic plan itself. The ICAAP process has also been adjusted where necessary to ensure consistency with the risk structure and objectives imposed by the Risk Appetite Framework.

The annual report demonstrated that, on the basis of company planning, capital is expected to remain fully adequate in the future, both with regard to the risks assumed and that may be assumed in the context of medium to long-term planning and with regard to the regulatory limits, which will become increasingly stringent. In particular, the assessment concluded that the good overall quality of the capital, the low level of leverage and the prevalence of a traditional business model, essentially linked to financing the real economy, should make it less onerous to align with the new regulatory requirements. Nevertheless, the bank remains committed to capital management and proper allocation in order to identify possible ways to strengthen/optimize capital and optimize capital absorption (RWA optimization) using all the levers available in the business model.

Under Pillar II, concentration risk is defined as the risk arising from credit exposures to counterparties, groups of connected counterparties, counterparties in the same economic sector or engaged in the same activity.

As part of the ICAAP process and in compliance with the relevant regulatory provisions, specific methods have been defined to calculate the risk of geo-sector concentration, i.e. the risk arising from exposure to counterparties operating in the same economic sector or geographical area.

Concentration risk per borrower is measured in accordance with the provisions of Bank of Italy Circular 285 using the Granularity Adjustment (GA) method.

A complex system of limits is also in place that monitors and circumscribes the guidelines for limiting the level of risk of concentration of the bank's loan portfolio.

Concentration risk, in its various forms, is also monitored in the quarterly credit report and is the subject of discussion at meetings of the Internal Credit Committee.

In terms of the banking book, which corresponds to the bank's entire commercial operation in relation to the transformation of the maturities of all balance sheet assets and liabilities, treasury and hedging derivatives, changes in market interest rate structures may have adverse effects on net interest income and capital and thereby constitute a source of risk (interest rate risk). The management and investment strategies of this portfolio are based on criteria for optimising the risk/return profile and implemented on the basis of expectations regarding interest rate trends. The bank's investment policy is therefore focused on optimising interest margins and minimising their volatility (Asset & Liability Management).

The guidelines and rules for the management of interest rate risk in the banking book are contained in the ALM Policy with the associated limits and operating powers for finance and liquidity. Two indicators are identified here, relating respectively to the sensitivity of the interest margin and the present value of assets to unfavourable changes in the interest rate curve.

In particular, interest rate risk is monitored by monthly data processing using the 'Ermas' IT procedure Ermas provided the firm Prometeia, the model of which has gradually been refined in order to treat all assets and liabilities in the banking book in the most realistic and reliable manner possible.

During the first half of 2019, the risk profile of the bank's banking book remained within the limits imposed by the risk assessment, both in terms of the sensitivity of the net interest income and the sensitivity of the asset value.

The verification and control of the interest rate risk profile are discussed on a weekly basis at the level of the Internal Finance Committee and monthly at the Finance Committee, during which a specific monthly report (the ALM report) is presented by the Risk Management Office. In particular, the reports include a so-called fixing analysis that provides a day-by-day picture of the amount of the most significant balance sheet items subject to rate changes, and which is also broken down by indexing parameter. This enables, *inter alia* , monitoring of the effective natural hedging capacity of the banking book, both in terms of timing and amount between assets and liabilities.

The Risk Management Policy identifies and defines the following additional risk categories that are subject to periodic analysis and evaluation:

- strategic risk that is divided into the following sub-types with respect to the time horizon of the event:
    - short-term risk (business or commercial risk), i.e. the risk of losses due to unexpected changes in sales volumes (lower revenues) and/or expected margins (higher costs due to technological innovation, the tightening of the tax regime, a change in the regulatory environment, etc.);
    - strategic risk in the strict sense or positioning risk, i.e. the risk of current or prospective losses, a decrease in profits or capital arising from changes in the operating context or poor company decisions, inadequate implementation of decisions, or insufficient response to changes in the competitive scenario;
- risks arising from securitisation transactions;
- equity investment risk, i.e. the risk that the book value of an equity investment may be reduced as a result of a reduction in its price on the stock markets, in the case of listed companies, or of the equity default of the investee, which makes it necessary/advisable to revise its book value in the financial statements, in the case of unlisted companies;
- reputational risk, i.e. the current or prospective risk of a decline in profits or capital arising from a negative perception of the Bank by stakeholders or any entity with which the Bank has entered into a relationship.

The ILAAP Process and Liquidity Risk

Liquidity risk is the risk that the bank will be unable to meet its payment obligations when due and/or to finance increases in its assets. It mainly takes the form of:

- the inability to raise funds by financing itself on the market (funding liquidity risk);
- the inability to liquidate funds by selling assets on the market (asset liquidity risk).

Awareness of the importance of liquidity risk was a key and constant subject of focus in the first half of 2019.

In particular, in accordance with the reporting requirements arising from the SREP guidelines of the European Banking Authority, the process for assessing the adequacy of internal liquidity, known as the ILAAP (the

Internal Liquidity Adequacy Assessment Process) has been defined and formalised. The results of this process, as at 31 December 2018, were submitted to the Supervisory Authority in April as part of a specific report drafted together with the ICAAP report, in accordance with orders issued in the first half of 2018 by the Bank of Italy, and reflect the guidelines of the European Banking Authority on the matter.

Liquidity management is based on the instructions and operating guidelines contained in the Liquidity and funding Policy, a document that is constantly updated. An essential element of management is the distinction between short-term operating liquidity (with a time horizon of up to 12 months) and medium to long-term structural liquidity (with a time horizon of longer than 12 months). The former is designed to avoid situations of sudden liquidity stress, caused by specific bank or market systemic shocks; the latter responds to the need to ensure optimal management, from a strategic standpoint, of the transformation of maturities between funding and lending, through an appropriate balance of the maturities of assets and liabilities to prevent future liquidity crisis situations.

The measurement and control of operating and structural liquidity was defined through a system of indicators, limits and periodic reporting, including on a daily basis. In addition, the organisational structure of the departments and functions responsible for liquidity management and its associated controls are clearly defined, as are the contingency funding plans (CFPs) to be implemented in the event of stress or crisis.

Liquidity risk is calculated using the Liquidity at Risk (LaR) method, which estimates - at different confidence intervals - the liquidity requirement, which cannot be directly influenced by the Bank, over predefined time horizons. The liquidity flows of interest in analysing the LaR are daily imbalances not attributable to choices made by the Bank, in other words liquidity flows directly attributable to customer activity. This approach is used to verify the level of reserves and to determine, including from an ICAAP perspective, any internal capital requirement to be allocated to meet liquidity risk.

The liquidity situation is constantly monitored by the relevant bodies on a daily, weekly and monthly basis. The Contingency Funding Plan also provides for a warning system based on the so-called Liquidity Monitor, which measures early warning indicators based on both systemic and specific crisis indicators. Indicators are appropriately weighted in order to identify three separate operating situations attributable to the progressive deterioration of the Bank's liquidity position: normal operating conditions - in turn broken down into regular, under observation and attention - stress conditions (emergency), and crisis situations (major emergency).

The Treasury Service, responsible for managing operating liquidity, also uses the so-called synoptic liquidity chart, a daily report that briefly and exhaustively describes the situation of liquidity in the short to medium term enabling the prompt identification of critical situations and the maintenance of the indicator values at the desired levels.

The system for calculation and forwarding to the Supervisory Authority of monthly reports on the liquidity indicators provided for in the Basel III regulations has been definitively in place since 2015. This is the short-term indicator, the so-called Liquidity Coverage Ratio (LCR) and the long-term indicator, the so-called Net Stable Funding Ratio (NSFR).

During the first half of 2019, an analysis of the Bank's liquidity situation did not reveal any particular short- or long-term tensions, despite being conducted in a context characterised by a decline in confidence among operators, particularly in view of the country risk associated with several Eurozone nations, including Italy.

The Bank's policy has favoured the maintenance of substantial and consistent liquidity reserves which are always sufficient to cope with possible stress situations. To this end, all available instruments have been used, including those implemented by the European Central Bank and the Italian Government. The Bank's proprietary securities portfolio is configured to ensure a large holding and easily available reserves for liquidity management over time, establishing to this end appropriate investment rules in terms of duration, sector, issuer risk, eligibility, etc. In 2016 the ABACO refinancing channel, through which loans that meet specific eligibility requirements can be collateralised with the ECB, was used extensively.

ANNUAL REPORTS OF THE CONTROL FUNCTIONS (COMPLIANCE AND RISK MANAGEMENT)

At least once per year, the internal control functions Compliance and Risk Management report on their work, pursuant to the joint Bank of Italy-Consob regulation pursuant to Article 6, paragraph 2-bis, of the Consolidated Finance Act (TUF) and Bank of Italy Circular 285/2013.

In particular:

- Article 13 of the joint regulation establishes that the risk management function is required to collaborate in defining the company's risk management system, oversees the operation of the company's risk management system, and verifies compliance with, adequacy and effectiveness of measures taken to remedy shortcomings detected in the company's risk management system. Article 13 also specifies that the function submits reports on its work to company bodies, at least once a year and provides consultancy to them;
- Article 16 of the aforementioned Regulation assigns the following responsibilities to the Control (Compliance) Function: regular monitoring and assessment of the adequacy and effectiveness of procedures and measures adopted to remedy any shortcomings in the fulfilment of obligations by the intermediary; the provision of consultancy and support to the relevant heads of the services in fulfilling the obligations laid down in the implementing provisions of Directive 2004/39/EC and its relevant implementing provisions. The compliance control function also submits reports on its activities to company bodies at least once a year;
- Point 2 of Part I, Title IV, Chapter 3, Section III requires that the regulatory compliance and risk control functions submit an annual activity programme to the corporate bodies, each according to their respective responsibilities, identifying and assessing the main risks to which the bank is exposed and planning the relevant management actions. At the end of the business cycle, i.e. on an annual basis, the control functions submit a report on their activities to the corporate bodies, describing the verifications performed, the results that have emerged, any weaknesses detected and the measures to be taken to remedy them.

In compliance with these regulatory obligations, the Bank's Compliance and Risk Management functions reported to the company bodies during the first half of the year on their activities during the previous year. The functions respectively submitted their annual reports on their activities to the Board of Directors on the dates of 15 and 25 March 2019.

PUBLIC DISCLOSURE (PILLAR III)

As of 1 January 2014, the new harmonised regulations for banks and investment firms contained in Regulation (EU) No 575/2013 (including the CRR - Capital Requirements Regulation) and Directive 2013/36/EU (also CRD IV, the Capital Requirements Directive IV), both dated 26 June 2013, apply the standards established by the Basel Committee on Banking Supervision (Basel III) to the European Union regulatory framework.

In order to implement and facilitate the application of the new Community regulations and to undertake a comprehensive review and simplification of banking supervisory regulations, on 19 December 2013 the Bank of Italy issued Circular 285 on "Prudential Supervisory Provisions for Banks".

The prudential supervision regulations are structured around three "pillars":

- the first pillar defines the methodologies for calculating the capital requirement to counter the risks typical of banking and financial activity (credit, counterparty, market and operational), characterised by various levels of complexity of measurement and control;

- the second pillar requires banks to adopt control strategies and processes aimed at ensuring current and prospective capital adequacy (ICAAP, Internal Capital Adequacy Assessment Process), to formalise these strategies and processes in a specific document (the "ICAAP Report"), and to independently and accurately identify the risks to which they are exposed in relation to their operations and reference markets, taking into account risks other than those of the first pillar;
- the third pillar introduces public disclosure requirements concerning capital adequacy, risk exposure, and organisational arrangements for identifying, monitoring and measuring such risks.

Volksbank's public disclosure with respect to its situation as at 31 December 2018 complies with the third pillar supervisory provisions for banks, providing qualitative and quantitative information as required by the aforementioned Bank of Italy circular.

The public disclosure as at 31 December 2018 is posted on the Bank's website at www.volksbank.it.

Future evolution of the Bank's risks/objectives

The Bank puts into effect measures for the selection, assumption, governance and mitigation of risks originating from banking and financial activities in pursuit of the objective of stable and sustainable growth over time, in line with the general guidelines adopted by the Board of Directors.

The guidelines include: a strong emphasis on the spreading of credit risks with a view to mainly financing households and small and medium-sized enterprises; the assumption of market risks that are closely related to commercial requirements; the careful monitoring of liquidity in order to ensure the ability to promptly meet expected and unexpected financial requirements, and the exclusion of risks not related to specific activities.

The implementation of these guidelines is a guarantee that enables us to cope in the best possible way with adverse and sometimes unpredictable economic and financial developments.

The Bank intends to continue its careful policy of selection, assumption, governance and mitigation of risks originating from banking and financial activities in pursuit of the objective of stable and sustainable growth over time.

With respect to credit risk, the Bank will focus its growth efforts on the household and SME segment, maintaining strong roots in its historical areas of reference, but above all pursuing a high degree of fragmentation of its loan portfolio. Sovereign risk will be taken on mainly in relation to commercial requirements, given the ongoing uncertainty surrounding the evolution of the macro-economic situation at the international level.

The objective is to maintain the character of a commercial bank, confirming the marginal position of financial risks compared to the overall risks to be faced. In any case, the methodologies for measuring market risks will continue to be refined, particularly given the increasing complexity of products and persistent market volatility.

In terms of liquidity risk, in addition to pursuing constant improvement of the control instruments at its disposal, including by adopting internal models to simulate liquidity effects arising from extreme scenarios, the Bank follows a policy that on the one hand favours balanced financial maturities, while on the other hand growing its liquidity reserves so as to ensure its stability and operational capacity in the event of a sudden and significant reduction in the liquidity of the system.

The Risk Management Area constantly monitors the risks arising from the introduction of new products or services, formulating proposals and conducting verifications of control measures.

EXPOSURE TO DEBT SECURITIES AND LOANS TO SOVEREIGN STATES

In its "Communication on information to be provided in financial reports on exposures held by listed companies in sovereign debt securities", No. DEM/11070007 of 5 August 2011, Consob (the Italian National Stock Exchange Supervisory Commission) refers to the application of European Securities and Markets Authority (ESMA) document No. 2011/266 of 28 July 2011 concerning information on sovereign debt to be included in the annual and half-yearly financial reports issued by listed companies adopting IAS/IFRS international accounting standards.

As stated in the ESMA document, "sovereign debt" relates to bonds issued by central and local governments and government bodies, and to loans granted to them. The following tables indicate in greater detail exposure to debt securities by accounting portfolio, maturity timeframe and fair value hierarchy .

The table below shows, for each individual country, the book value of sovereign credit risk exposures.

Composition of sovereign debt securities portfolio – by issuing country	30.06.2019	31.12.2018
EU countries		
- Italy	1,921,016	1,531,235
- Germany	-	50,081
- The Netherlands	-	2,079
Total portfolio	**1,921,016**	**1,588,412**

Composition of sovereign debt securities portfolio - Financial assets at fair value through profit or loss

State	maturity by 2019	maturity in 2020	maturity in 2021	maturity in 2022	maturity in 2023	maturity after 2024	**Total**	LEVEL 1	LEVEL 2	LEVEL 3
Italy	-	-	-	-	-	-	-	-	-	-
Total	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**

Composition of sovereign debt securities portfolio - Financial assets at fair value with an impact on comprehensive income

State	maturity by 2019	maturity in 2020	maturity in 2021	maturity in 2022	maturity in 2023	maturity after 2024	**Total**	LEVEL 1	LEVEL 2	LEVEL 3
Italy	32,670	188,898	63,374	82,188	49,122	107,090	**525,343**	520,342	5,001	-
Total	**32,670**	**188,898**	**63,374**	**82,188**	**49,122**	**107,090**	**525,343**	**520,342**	**5,001**	**-**

Portfolio composition of sovereign debt securities - Financial assets at amortised cost

State	maturity by 2019	maturity in 2020	maturity in 2021	maturity in 2022	maturity in 2023	maturity after 2024	**Total**	LEVEL 1	LEVEL 2	LEVEL 3
Italy	-	37,321	59,688	134,254	210,402	954,007	**1,395,673**	1,395,673	-	-
Total	**-**	**37,321**	**59,688**	**134,254**	**210,402**	**954,007**	**1,395,673**	**1,395,673**	**-**	**-**

DISCLOSURE OF EXPOSURE TO STRUCTURED CREDIT PRODUCTS AND SPECIAL PURPOSE ENTITIES

In accordance with the recommendations of the Financial Stability Forum (now the Financial Stability Board) and the Bank of Italy (Communication No. 671589 of 18 June 2008), the following information is provided on the risks relating to exposures to structured credit products, asset backed securities and collateralised debt obligations, as well as special purpose vehicles for securitisations originated by Volksbank or resulting from the issue of covered bank bonds.

Note that third-party bond issues backed by guarantees based on credit portfolios are not considered relevant for the purposes of the disclosure required in this paragraph, since they are instruments in which the underlying structure constitutes an additional guarantee to the issuer's solvency.

EXPOSURE TO SPECIAL PURPOSE ENTITIES

Special Purpose Entities (SPEs) are entities set up on an *ad hoc* basis to achieve a specific objective, normally the securitisation of receivables and operations for the issue of Covered Bonds.

For securitisation transactions, reference is made to special-purpose vehicles incorporated pursuant to Article 3 of Law No. 130 of 30 April 1999, which place on the market the debt instruments issued to finance the purchase of the securitised loans. These receivables are used to guarantee the repayment of liabilities issued by the vehicle company.

Covered Bond transactions, governed by Law 130 of 30 April 1999, are issues of debt securities by credit institutions specifically guaranteed by a portfolio of assets identified and separate from the issuer's assets. These assets are sold by the issuer to a duly incorporated special-purpose vehicle.

There were no changes compared with the situation as at 31 December 2018. In particular, the Company holds a portion of the senior tranche of the HIPOCAT 15.1.50 TV security, entered among the instruments measured at fair value at fair value through profit or loss of €0.5 million relating to the securitisation of receivables (€0.5 million at 31.12.2018).

EXPOSURE TO STRUCTURED PRODUCTS

As at 30 June 2019, the total exposure to covered bonds was €67.5 million, modest to the total portfolio (approximately 2.2% of the total). All are financial instruments issued by EU banks or financial companies, classified as HTCS ("Hold To Collect And Sell") and are measured at fair value with changes in fair value recognised in the valuation reserve. All these instruments have a residual maturity of six years or less.

Structured securities, which have a book value of €70.0 million (2.8% of the total portfolio) measured at fair value with an impact on comprehensive income ("HTCS - Hold To Collect And Sell"). All these instruments have a residual maturity of seven years or less.

RELATED PARTY DISCLOSURES

This half-year financial report incorporates the regulatory amendments made to IAS 24 - Related Party Disclosures - published in November 2009 by the IASB (Reg. EC No 632/2010 of 19/07/2010) on the definition of the scope of a related party.

For details of existing relationships, see the section entitled "Related Party Disclosures" in the Explanatory Notes to the Condensed Half-Year Financial Statement.

BUSINESS OUTLOOK

The indications from the main forecasters are that world trade will weaken in 2019, in a context of marked international trade tensions and a slowdown in global activity. Trade will then gradually recover in 2020-2021. Foreign demand for Italian products, weighted by the target markets, are expected to expand at a much lower rate than previously, by 2% in the current year (down from 3.3 in 2018), before gradually accelerating in 2020-21.

This scenario assumes that monetary conditions will remain very accommodative, in line with the ECB Governing Council's policy stance. Interest rates on Italian 10-year government bonds will be 2.4% on average this year and will increase progressively over the next two years. In line with what has been observed over the last 12 months, it is assumed that the level of sovereign yields will gradually be passed on to private sector funding conditions.

In the light of the most recent economic trends, GDP is expected to grow by 0.1% on average in 2019, by 0.8% in 2020 and by 1.0% in 2021. Over this period, economic activity will mainly be driven by household spending and exports.

Consumption will continue to expand, albeit at a slower pace than in the last three years, strengthening in the second half of 2019, assisted by measures to support disposable income. The savings rate of consumer households will rise slightly to 8.7% in 2021.

Employment, which in 2018 returned to the levels reached before the global financial crisis in terms of the number of people in work, will increase further but at a more moderate pace, particularly between the second half of this year and 2020. This trend will also be affected by increased outflows from the labour market associated with the introduction of new forms of early retirement, which in line with past trends, will only partially be replenished by new forms of employment. The unemployment rate, which fell in the first half of 2019, is expected to remain at around 10% over the three-year forecast period.

Expenditure on capital goods will decrease this year and next, partly due to the end of fiscal stimulus from 2020, and will rise again in 2021. The construction investment component, on the other hand, will continue to expand, supported by the gradual improvement of the real estate market and the planned increase in public investment. The ratio of capital investment to GDP, which last year was close to pre-recession figures, will fall slightly over the three-year period. For the component construction in 2021, this ratio would still be around 2 percentage points below pre-crisis levels.

Exports of goods and services will be affected by the trend in world trade, but Italian companies will retain their market shares, as they have done in recent years: foreign sales once again grow at rates slightly above those of foreign demand weighted by destination markets (around 3% per year on average). The dynamics of imports will be less sustained, due to the weakness of investment in capital goods (the component of demand with the highest foreign input content). This will result in an increase in the balance of payments current account surplus to more than 3% of GDP.

Inflation, calculated with the change in the Harmonised Index of Consumer Prices (HICP), will fall to 0.7% in 2019, before gradually rising to 1.4% per cent in 2021, driven mainly by the dynamics of the core component. Domestic inflation, as measured by the GDP deflator, is expected to be 1.0% this year, rising to 1.1% and 1.5% in 2020 and 2021 respectively, mainly reflecting the gradual acceleration in private sector wages. Business profit margins are expected to continue to fall slightly this year, but expand again in the following two years, thanks to a gradual improvement in cyclical conditions.

Risks will continue to decline due to the growth situation. External risks of origin continue to be related mainly to tensions over trade policies: if these spread or persist, they could not only slow down global and European economic activity, but also fuel new episodes of financial volatility and have a negative impact on companies' willingness to invest. At the domestic level, heightened uncertainty about the direction of fiscal policy in the years following the current year could lead to further turbulence in the financial markets and contribute to a deterioration in household and business confidence, with repercussions for the dynamics of investment. A

boost to economic activity, on the other hand, could come from the start of a virtuous circle between expectations of budgetary policy and financial conditions.

Inflation risks are balanced. Upside risks, stemming from pressures associated with increases in energy commodity prices, are offset by the effects of possible further weakening of economic activity in our country and globally.

Partly as a result of risk reduction measures already implemented, the Bank will be able to further strengthen the overall quality of its portfolio through a strengthening of the tools available for optimising NPL management decisions.

Ordinary operations in the second half of the year will continue to focus on a return to profitability, in terms of both net interest income and fees, which will benefit from our favourable position in the region.

The trend in revenues, even in a context still characterised by high competitive pressure, may benefit from the balanced development of lending volumes and constant control of the average cost of funding, while the trend in fees, particularly those deriving from management, brokerage and advisory services, may benefit from less uncertain and volatile financial markets.

Constant cost control will be pursued by improving efficiency and implementing specific measures to optimise expenditure and rationalise corporate offices.

The focus on levels of coverage of non-performing loans will remain sharp. The reduction in stocks will continue through internal workout and initiatives to dispose of portfolios.

Bolzano, 9 August 2019

CONDENSED HALF-YEAR FINANCIAL STATEMENT

FINANCIAL STATEMENTS

Statement of financial position at 30 June 2019

Assets	30.06.2019	31.12.2018
(in Euro)		
10. Cash and cash equivalents	79,997,762	83,017,850
20. Financial assets designated at fair value through profit or loss	216,037,058	290,022,083
a) financial assets held for trading	1,195,663	3,258,439
b) financial assets designated at fair value	-	-
c) other financial assets compulsorily measured at fair value	214,841,395	286,763,644
30. Financial assets measured at fair value with impact on comprehensive income	794,490,006	829,144,042
40. Financial assets measured at amortised cost	8,762,155,590	8,488,828,633
a) loans to banks	74,880,202	83,358,663
b) loans to customers	8,687,275,388	8,405,469,970
50. Hedging derivatives	-	-
60. Value adjustment of hedged financial assets (+/-)	-	-
70. Equity investments	5,626,058	5,745,476
80. Physical assets	151,983,630	135,964,893
90. Intangible assets	19,007,736	118,731,281
of which:		
- goodwill	-	99,601,776
100. Tax assets	182,724,878	174,704,904
a) current	57,182,050	54,806,801
b) prepaid	125,542,828	119,898,103
110. Non-current assets and groups of assets held for sale	12,697,587	12,923,130
120. Other assets	144,848,389	136,479,833
Total assets	**10,369,568,694**	**10,275,562,123**

Liabilities and shareholders' equity	30.06.2019	31.12.2018
(in Euro)		
10. Financial liabilities measured at amortised cost	9,373,830,638	9,101,606,666
a) Payables to banks	1,351,653,481	1,418,187,385
b) Payables to customers	7,405,598,755	6,985,198,803
c) Outstanding securities	616,578,402	698,220,477
20. Financial liabilities held for trading	2,057,660	1,429,146
30. Financial liabilities designated at fair value (IFRS 7 par. 8 letter e)	-	-
40. Hedging derivatives	-	-
50. Value adjustment of hedged financial liabilities (+/-)	-	-
60. Tax liabilities	28,210,809	31,253,823
a) current	8,926,489	4,291,065
b) deferred	19,284,320	26,962,757
70. Liabilities associated with assets held for sale	-	-
80. Other liabilities	195,505,357	266,228,642
90. Employee severance indemnities	19,965,611	19,113,484
100. Provisions for risks and charges	18,562,061	20,728,394
a) commitments and guarantees given	6,133,629	6,848,854
b) pensions and similar obligations	-	-
c) other provisions for risks and charges	12,428,432	13,879,540
110. Valuation reserves	(1,461,281)	(15,387,237)
120. Redeemable shares	-	-
130. Equity instruments	-	-
140. Reserves	267,835,944	249,733,758
150. Issue premium	383,158,533	383,158,533
160. Capital	201,993,752	201,993,752
170. Treasury shares (-)	(18,553,559)	(18,553,559)
180. Profit (Loss) for the year (+/-)	(101,536,831)	34,256,720
Total liabilities and shareholders' equity	**10,369,568,694**	**10,275,562,123**

Income Statement at 30 June 2019

INCOME STATEMENT	30.06.2019	30.06.2018
(in Euro)		
10. Interest receivable and similar income	105,255,567	97,785,735
of which: interest income calculated according to the effective interest method	99,228,361	97,785,735
20. Interest paid and similar charges	(14,397,113)	(14,884,034)
30. Interest margin	**90,858,454**	**82,901,701**
40. Commission income	49,927,961	48,105,730
50. Commission expense	(5,249,158)	(5,040,090)
60. Net fees	**44,678,803**	**43,065,640**
70. Dividends and similar income	2,097,899	1,978,782
80. Net result of trading	566,593	1,284,088
90. Net result of hedging	-	-
100. Profits (losses) on disposal or repurchase of:	4,312,474	3,241,820
a) financial assets measured at amortised cost	2,882,715	1,476,446
b) financial assets measured at fair value with an impact on comprehensive income	1,323,258	1,595,887
c) financial liabilities	106,501	169,487
110. Net profit/loss from other financial assets and liabilities measured at fair value with an impact on the income statement	(16,334,354)	1,401,139
a) financial assets and liabilities designated at fair value	-	-
b) other financial assets compulsorily measured at fair value	(16,334,354)	1,401,139
120. Net receipts from banking	**126,179,869**	**133,873,169**
130. Net adjustments/write-backs of impairment losses of:	(56,896,135)	(17,369,287)
a) financial assets measured at amortised cost	(57,338,406)	(17,096,047)
b) financial assets measured at fair value with an impact on comprehensive income	442,271	(273,240)
140. Gains/losses from contractual amendments without write-downs	-	6,283
150. Net result of financial management	**69,283,734**	**116,510,164**
160. Administrative expenses:	(89,078,623)	(97,365,382)
a) personnel expenses	(46,924,401)	(50,473,196)
b) other administrative expenses	(42,154,222)	(46,892,186)
170. Net provisions for risks and charges	1,213,591	(4,018,185)
a) for credit risk relating to commitments and guarantees given	715,226	677,220
b) other net provisions	498,365	(4,695,406)
180. Net adjustments/write-backs on physical assets	(5,803,532)	(5,178,670)
190. Net adjustments/write-backs on intangible assets	(853,043)	(578,084)
200. Other operating income/expenses	10,356,751	9,793,767
210. Operating costs	**(84,164,856)**	**(97,346,554)**
220. Profits (losses) on equity investments	(267,800)	219,444
230. Net result of measurement at fair value of tangible and intangible assets	-	-
240. Goodwill value adjustments	(99,601,776)	-
250. Profits (losses) on disposal of investments	32,898	5,759
260. Profit (loss) from current operations before tax	**(114,717,800)**	**19,388,813**
270. Income taxes on current operations	13,180,969	(4,053,539)
280. Profit (loss) from current operations after tax	**(101,536,831)**	**15,335,274**
290. Profit (Loss) on discontinued operations after tax	-	-
300. Profit (Loss) for the year	**(101,536,831)**	**15,335,274**

Statement of comprehensive income

Items *(in Euro)*		30.06.2019	30.06.2018
10.	**Profit (Loss) for the year**	**(101,536,831)**	**15,335,274**
	Other income net of taxes not reversed to the income statement		
20.	Equity securities designated at fair value with an impact on comprehensive income	5,719,295	(209,022)
30.	Financial liabilities designated at fair value through profit or loss (changes in creditworthiness)	-	-
70.	Defined benefit plans	(893,760)	(466,859)
	Other income net of taxes reversed to the income statement		
140.	Financial assets (other than equity securities) measured at fair value with an impact on comprehensive income	6,166,459	(9,582,635)
160.	Share of valuation reserves of equity investments measured at equity	-	-
170.	Total other income after tax	10,991,994	(10,258,516)
180.	**Comprehensive income (item 10+170)**	**(90,544,837)**	**5,076,757**

Statement of changes in shareholders' equity

Statement of changes in shareholders' equity from 1 January to 30 June 2019

(in €)	Balances at 31.12.2018	Change of opening balances	Balances at 01.01.2019	Allocation of previous year's profit		Changes during the year								Shareholders' equity at 30.06.2019
						Changes in reserves	Operations on shareholders' equity						Total income as at 30.06.2019	
				Reserves	Dividends and other destinations		Issue of new shares	Purchase of treasury shares	Extraordinary dividend distribution	Change in equity instruments	Derivatives on treasury shares	Stock Options		
Capital:	**201,993,752**	**-**	**201,993,752**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**201,993,752**
a) ordinary shares	201,993,752	-	201,993,752	-	-	-	-	-	-	-	-	-	-	201,993,752
b) other shares	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Issue premium	**383,158,533**	**-**	**383,158,533**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**383,158,533**
Reserves:	**249,733,758**	**-**	**249,733,758**	**21,036,147**	**-**	**(2,933,961)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**267,835,944**
a) profits	249,733,758	-	249,733,758	21,036,147	-	(2,933,961)	-	-	-	-	-	-	-	267,835,944
b) other	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Valuation reserves:	**(15,387,236)**	**-**	**(15,387,236)**	**-**	**-**	**2,933,961**	**-**	**-**	**-**	**-**	**-**	**-**	**10,991,994**	**(1,461,281)**
Equity instruments	**-**	**-**	**-**	**-**	**-**		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Treasury shares	**(18,553,559)**	**-**	**(18,553,559)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(18,553,559)**
Profit (Loss) for the year	**34,256,720**	**-**	**34,256,720**	**(21,036,147)**	**(13,220,573)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(101,536,831)**	**(101,536,831)**
Shareholders' equity	**835,201,968**	**-**	**835,201,968**	**-**	**(13,220,573)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(90,544,837)**	**731,436,558**

Statement of changes in shareholders' equity from 1 January to 30 June 2018

(in €)	Balances at 31.12.2017	Change of opening balances	Balances at 01.01.2018	Allocation of previous year's profit		Changes during the year								Shareholders' equity at 30.06.2018
						Changes in reserves	Operations on shareholders’ equity						Total income as at 30.06.2018	
				Reserves	Dividends and other destinations		Issue of new shares	Purchase of treasury shares	Extraordinary dividend distribution	Change in equity instruments	Derivatives on treasury shares	Stock Options		
Capital:	**199,439,716**	**-**	**199,439,716**	**-**	**-**	**-**	**2,554,036**	**-**	**-**	**-**	**-**	**-**	**-**	**201,993,752**
a) ordinary shares	199,439,716	-	199,439,716	-	-	-	2,554,036	-	-	-	-	-	-	**201,993,752**
b) other shares	-	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Issue premium	**383,158,533**	**-**	**383,158,533**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**383,158,533**
Reserves:	**284,365,657**	**(46,526,499)**	**237,839,158**	**14,612,166**	**-**	**-**	**(2,592,801)**	**-**	**-**	**-**	**-**	**-**	**-**	**249,858,523**
a) profits	284,365,657	(46,526,499)	237,839,158	14,612,166	-	-	(2,592,801)	-	-	-	-	-	-	**249,858,523**
b) other	-	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Valuation reserves:	**681,778**	**2,411,711**	**3,093,489**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(10,258,516)**	**(7,165,027)**
Equity instruments	**-**	**-**	**-**	**-**	**-**		**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Treasury shares	**(18,553,559)**	**-**	**(18,553,559)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(18,553,559)**
Profit (Loss) for the year	**24,277,481**	**-**	**24,277,481**	**(14,612,166)**	**(9,665,315)**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**15,335,274**	**15,335,274**
Shareholders’ equity	**873,369,606**	**(44,114,788)**	**829,254,818**	**-**	**(9,665,315)**	**-**	**(38,765)**	**-**	**-**	**-**	**-**	**-**	**5,076,758**	**824,627,496**

Cash flow statement

A.	OPERATING ACTIVITY	30.06.2019	30.06.2018
(in Euro)			
1.	**Management**	**90,677,679**	**42,612,749**
	- interest received (+)	105,255,567	97,785,735
	- interest expense paid (-)	(14,397,113)	(14,884,034)
	- dividends and similar income (+)	2,097,899	1,978,782
	- net fees (+/-)	44,678,803	43,065,640
	- personnel costs (-)	(46,924,401)	(50,473,196)
	- other costs (-)	(42,694,327)	(48,120,093)
	- other revenues (+)	29,480,281	17,313,454
	- taxes and duties (-)	13,180,969	(4,053,539)
	- costs/revenues relating to discontinued operations net of tax effect (+/-)	-	-
2.	**Cash generated/utilized by financial assets**	**(255,291,253)**	**(332,321,736)**
	- financial assets held for trading	2,629,368	(10,220,332)
	- financial assets designated at fair value	-	-
	- other assets necessarily measured at fair value	55,587,895	(763,688)
	- financial assets designated at fair value with an impact on comprehensive income	48,305,319	(47,009,782)
	- financial assets measured at amortised cost	(346,366,074)	(271,777,169)
	- other assets	(15,447,761)	(2,550,766)
3.	**Cash generated/utilized by financial liabilities**	**197,483,086**	**303,311,880**
	- financial liabilities measured at amortised cost	272,330,473	288,027,137
	- financial liabilities held for trading	628,514	(289,747)
	- financial liabilities designated at fair value	-	(1,049,676)
	- other liabilities	(75,475,900)	16,624,166
	Net cash provided by/used in operating activities	**32,869,512**	**13,602,893**

B.	INVESTMENT ACTIVITY	30.06.2019	30.06.2018
1.	**Cash generated by**	**32,898**	**40,759**
	- sales of equity investments	-	-
	- dividends received on equity investments	-	35,000
	- sales of physical assets	32,898	5,759
	- Sales of intangible assets	-	-
	- sales of business units	-	-
2.	**Cash absorbed by**	**(22,701,925)**	**(8,338,750)**
	- purchases of equity investments	(148,382)	(0)
	- purchases of physical assets	(21,822,269)	(8,280,190)
	- purchases of intangible assets	(731,274)	(58,560)
	- purchases of business units	-	-
	Net cash generated/utilized by investment activities	**(22,669,028)**	**(8,297,991)**

C.	FUNDING ACTIVITIES	30.06.2019	30.06.2018
	- Issues/purchases of treasury shares	0	2,554,036
	- Issues/purchases of equity instruments	0	(2,592,800)
	- Distribution of dividends and other purposes	(13,220,573)	(9,665,315)
	Net cash generated/utilized by funding	(13,220,573)	(9,704,080)
	NET LIQUIDITY GENERATED/ABSORBED DURING THE YEAR	**(3,020,088)**	**(4,399,178)**

RECONCILIATION	30.06.2019	30.06.2018
Cash and cash equivalents at beginning of year	83,017,850	71,358,997
Total net cash generated/utilized during the year	(3,020,088)	(4,399,178)
Cash and cash equivalents: effect of changes in exchange rates	-	-
Cash and cash equivalents at end of year	**79,997,762**	**66,959,819**

EXPLANATORY NOTES

DECLARATION OF CONFORMITY WITH INTERNATIONAL ACCOUNTING STANDARDS

The half-yearly financial report (hereinafter also the "half-yearly report" or the "Report") was produced in accordance with the recognition and measurement criteria established in the IAS/IFRS accounting standards issued by the International Accounting Standards Board (IASB) and the relevant interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and approved by the European Commission, as established by Regulation (EC) No 1606 of 19 July 2002.

The accounting policies used to produce the Half-Yearly Report, with respect to the phases of classification, recognition, measurement and derecognition of financial assets and liabilities, as well as the methods of recognising revenues and costs, have changed compared to those adopted in the 2018 Financial Statements of Volksbank. These amendments essentially derive from the mandatory application, as of 1 January 2019, of international accounting standard IFRS 16 "Leasing", issued by the IASB in January 2016 and approved by the European Commission through Regulation No 1986/2017, with regard to the accounting, measurement, presentation and disclosure of leasing contracts.

IFRS 16 has an impact on the method of accounting for lease agreements as well as lease, rental and commodatum agreements, introducing a new definition based on the transfer of the "right of use" of a leased asset. The new standard requires that all lease contracts be recorded by the lessee in the balance sheet as assets and liabilities. A different method of recognising costs was also introduced: whereas in IAS 17, lease payments were recognised under the income statement item relating to administrative expenses, according to IFRS 16, the expense is recognised both by amortisation of the assets relating to the "right of use" and as interest expense on the debt.

As of the first half of 2019, the reclassified statements have been modified to take account of the application of the new standard. In particular, specific sub-items have been added to the balance sheet respectively under tangible and intangible assets, to provide separate evidence of usage rights acquired under the right of use, and the Other liability item, to separately highlight payables for contracts that give rise to a right of use.

For the purposes of first-time adoption (FTA) of IFRS 16, the Bank has chosen to adopt the "modified retrospective" approach, which allows, as provided for in the standard, the cumulative effect of applying the standard at the date of first-time adoption to be recognised and does not require the restatement of comparative data from the financial statements of first-time adoption of the standard. Therefore the figures in the financial statements for the year 2019 and for the previous year are not comparable with the valuation of the rights of use and the corresponding lease payable.

In order to enable comparison on a like-for-like basis, the reclassified balance sheet and income statement figures affected by the new standard have been restated. In particular, the reclassified balance sheet at 30 June 2019 is compared with the corresponding balances at 1 January 2019, which also include the effects of the first-time adoption of IFRS 16.

GENERAL PRINCIPLES OF DRAFTING

The Half-yearly Financial Report, produced pursuant to Article 154-ter of Legislative Decree 58 of 24 February 1998 (the Consolidated Finance Act) and subsequent amendments, consists of the condensed half-year financial statements and an interim report on operations containing significant events during the half-year, information on transactions with related parties and a description of the main risks and uncertainties, including those related to foreseeable business trends.

The condensed half-year financial statement (hereinafter also "Condensed Half-Year Financial Statement") consists of the balance sheet, the income statement, the statement of comprehensive income, the statement

of changes in shareholders' equity, the cash flow statement and the explanatory notes and commentary on the results for the period.

The reporting formats have been produced in accordance with Bank of Italy Circular no. 262 of 22 December 2005 "Bank financial statements: formats and rules for preparation" and subsequent updates (most recently the 6th update published on 30 November 2018).

The reclassified balance sheet and income statement schedules contained in the condensed half-yearly financial statements have been produced on the basis of the new financial statements. The reclassification criteria are detailed in the specific section of the Condensed Financial Statements. The purpose of presenting these reclassified financial statements is to provide a more immediate picture of the financial position, results of operations and cash flows for the half-year.

The half-yearly report as at 30 June 2019 was produced using the Euro as the reporting currency. Amounts indicated in the Financial Statements and in Explanatory Notes are expressed in Euro unless indicated otherwise.

The half-yearly report as at 30 June 2019, approved by the Board of Directors on 9 August 2019, is accompanied by the declaration of the Financial Reporting Officer, pursuant to Article 154-bis of the Italian Consolidated Finance Act and is subjected to a limited audit by the auditing company KPMG S.p.A.

UNCERTAINTIES REGARDING THE USE OF ESTIMATES IN DRAFTING THE HALF-YEAR REPORT

Financial reporting requires the use of estimates and assumptions that may have significant effects on the values recognised in the balance sheet and the income statement, and on information on contingent assets and liabilities disclosed in the financial statements. The production of such estimates involves the use of the available information and the adoption of subjective assessments, also based on historical experience, used to make reasonable assumptions for the recognition of operating events. By their nature, the estimates and assumptions used may vary from one year to the next and, therefore, it cannot be excluded that in subsequent years the values recognised in the financial statements may also vary significantly as a result of changes in the subjective assessments used.

The main situations in which management is required to make subjective assessments include:

- quantification of the impairment losses on loans, equity investments and, in general, other financial assets;
- the use of valuation models to recognise the fair value of financial instruments not listed on active markets;
- assessment the appropriateness of the value of goodwill and other intangible assets;
- quantification of the fair value of properties;
- quantification of provisions for personnel and for risks and charges;
- estimates and assumptions regarding the recoverability of deferred tax assets;
- the estimated recoverable value of properties held for investment purposes.

For some of the cases listed above, the main factors subject to estimate can be identified and therefore contribute to the determination of the book value of assets and liabilities. Without claiming to be exhaustive, it should be noted that:

- in order to determine the fair value of financial instruments not listed on active markets, if it is necessary to use parameters that cannot be inferred from the market, the main estimates concern, on the one hand, the evolution of future financial flows (or even income flows, in the case of shares), possibly

contingent on future events and, on the other hand, the level of certain input parameters not listed on active markets;

- for allocation to the three credit risk stages envisaged in IFRS 9 of receivables and debt securities classified among financial assets at amortised cost and among financial assets at fair value, with an impact on total profitability and the calculation of the relevant expected losses, the main estimates concern:
  a) the determination of the parameters for a significant increase in credit risk, based essentially on models for measuring the probability of default (PD) at the origination of financial assets and at the reporting date;
  b) the inclusion of forward looking factors, including macroeconomic factors, for the determination of PD and LGD;
  c) the determination of the probability of the sale of non-performing financial assets, through the realisation of positions on the market;
- for the determination of the estimates of future cash flows from non-performing loans, certain factors are taken into account: expected recovery times, certain elements are taken into consideration: the expected recovery time, the estimated realisable value of any guarantees, as well as the costs that are expected to be incurred for the recovery of the credit exposure;
- to determine the value in use of intangible assets with an indefinite useful life (goodwill) in relation to the Cash Generating Unit (CGU), future cash flows in the analytical forecast period and the flows used to determine the terminal value generated by the CGU are estimated separately and appropriately discounted. The cost of capital is included among the items assessed;
- to determine the value in use of intangible assets with a finite life (the “client relationship”), the useful life is assessed on the one hand, and the future cash flows of the assets on the other. In the case of intangible assets with a finite useful life, the cost of capital is also included in the estimates;
- the determination of the fair value of real estate is made through the valuers’ reports. Estimates are made of rent, sale prices, discount rates and capitalisation in the compilation of real estate valuers’ reports;
- for the quantification of provisions for pensions and similar obligations, the present value of the obligations is assessed, taking into account the flows, appropriately discounted, arising from statistical historical analyses, and the demographic curve;
- for the quantification of provisions for risks and charges, the amount of the disbursements necessary to fulfil the obligations is estimated, where possible, taking into account the actual probability of having to invest resources;
- for the determination of the items relating to deferred taxation, the probability of actual future tax liability (taxable temporary differences) is estimated, and the degree of reasonable certainty – if any – of future taxable amounts at the time tax deductibility becomes apparent (deductible temporary differences).

THE MAIN BALANCE SHEET ITEMS

The transition to the IFRS 16 International Financial Reporting Standard

The regulatory provisions

Regulation No 1986/2017 replaced, with effect from 1 January 2019, IAS 17 Leasing, IFRIC 4 "Determining Whether an Arrangement Contains a Lease", SIC 15 "Operating Leases – Incentives" and SIC 27 "Evaluating the Substance of Transactions in the Legal Form of a Lease ", and established the requirements for the accounting of lease agreements.

The new principle requires the identification of whether a contract is (or contains) a lease, based on the concept of control of the use of an asset identified for a given period of time. It follows that lease, rental, or commodatum agreements also fall within the scope of application of the new rules.

In view of these developments, significant changes are introduced into the accounting treatment of lease transactions in the lessee/user's financial statements, providing for the introduction of a single accounting model for lease agreements by the lessee, based on the right of use model. In particular, the main change is that the distinction between operating and financial leases in IAS 17 has been overcome: all leases must therefore be accounted for in the same way, with recognition of assets and liabilities. The accounting model provides for the recognition of the right to use the leased asset among total assets. Unlike the standards in force until 31 December 2018, payables in respect of lease payments still to be paid to the lessor are liabilities. The method of recognising the components of the income statement has also changed: while with the IAS 17, lease payments were recognised under the item relating to Administrative Expenses, according to with IFRS 16, charges relating to the amortisation of the "right of use" and interest expense on debt are recognised.

The minimum disclosure required of lessee companies includes, *inter alia*:

- a distinction between the various "classes" of leased assets;
- an analysis by maturity of the liabilities relating to lease agreements;
- information potentially useful for a better understanding of the business of the enterprise in relation to lease agreements (e.g. early redemption or extension options).

There were no substantial changes, apart from some major disclosure requirements, in the accounting for leases by lessors, where the distinction between operating leases and finance leases is maintained.

It should also be noted that on the basis of the requirements of IFRS 16 and the clarifications of IFRIC (the September 2018 document entitled "Cloud Computing Arrangements"), software is excluded from the scope of application of IFRS 16, and is recognised in accordance with IAS 38 and the relevant requirements.

Since January 1, 2019, the effects on the financial statements following the application of IFRS 16 have been identifiable for the lessee - with the same profitability and final cash flow - as an increase in assets recorded in the balance sheet (the leased assets representing the right of use), an increase in liabilities (debt on the leased assets), a reduction in administrative expenses (lease payments) and a concomitant increase in financial costs (remuneration of the recognised debt) and amortisation (relating to the right of use). With regard to the income statement, considering the entire duration of the agreements, the economic impact does not change over the time frame of the lease, either by applying the previous IAS 17 or by applying the new IFRS 16, but manifests itself with a different temporal distribution.

In 2018 the Bank launched a dedicated project for the implementation of IFRS 16 Leasing, in order to deepen and define the qualitative and quantitative impacts, as well as to identify and implement the application and organisational measures necessary for the coherent, organic and effective adoption of the new rules. A specific application was implemented to determine the values according to IFRS 16.

The scope of the contracts – lessee side. Classification and analysis of lease transactions in light of the relevant regulations

As noted above, the Standard applies to all types of contracts containing a lease, i.e. contracts that give the lessee the right to control the use of an identified asset for a certain period of time (period of use) in exchange for a consideration.

The rationale behind the Standard is that "control" over an asset requires that asset to be identified, for example when it is explicitly specified in the contract, or if it is implicitly specified at the time it is available to be used by the client. An asset is not specified if the supplier has a substantive right to replace it, or if the supplier is practically able to replace the asset with alternative assets throughout the period of use and derives economic benefits from exercising that right.

Once it has been established that the underlying value of the contract is an identified asset, it is necessary to assess whether the entity has the right to control it because it has both the right to obtain substantially all the economic benefits from the use of the asset and the right to decide on the use of that asset.

The analysis of contracts within the scope of application of the standard specifically concerned property and hardware contracts. The impact of property lease agreements represents the totality of the value of rights of use. No impacts arising from the Hardware sector were recorded, as the relevant contracts are below the materiality thresholds set by the standard.

Property lease agreements refer entirely to properties intended for office use or bank branches. The agreements generally have a term of longer than 12 months and typically have renewal and terminations options that can be exercised by the lessor and the lessee in accordance with law or specific contractual provisions.

These agreements usually do not include the option to purchase at the end of the lease or significant restoration costs for the Bank.

Accounting decisions

In the present context, it is fitting to explain some decisions made with reference to the methods of representing the effects of first-time application of the standard, as well as some rules to be applied when fully operational in order to account for leasing contracts.

As indicated above, it was decided to proceed with first-time adoption (FTA) of IFRS 16 through the "modified retrospective" approach, which allows the option, provided for by the standard, to recognise the cumulative effect of applying the standard at the date of first-time adoption and not to reproduce comparative figures of the financial statements for first-time adoption of IFRS 16. Accordingly, the figures in the financial statements for the year 2019 will not be comparable with the valuation of the rights of use and the corresponding lease payable.

On first-time application, certain options provided for in the standard in paragraph C10 et seq. were exercised. In particular, contracts with a remaining term ("lease term") of up to 12 months ("short term") were excluded.

When fully operational, it was decided not to apply the new standard to contracts with a total term ("lease term") of less than or equal to 12 months and to contracts with a value of the underlying asset, when new, of less than or equal to €5,000 ("low value"). In this case, lease payments relating to such leases are recognised as a cost – as in the past – on a straight-line basis for the term of the lease or according to another systematic criterion if it is more representative of the way in which the lessee receives the benefits.

Contract Term

The term of the lease is determined by the non-cancellable period during which the Bank is entitled to use the underlying asset, also considering: (i) the periods covered by the lease extension option, if the lessee is reasonably certain of exercising the option; and (ii) the periods covered by the lease termination option, if the lessee is reasonably certain of not exercising the option.

At the transition date and the start date of each contract concluded after 1 January 2019, the term of the lease was defined, on the basis of facts and circumstances existing on that date, which have an impact on the reasonable certainty of exercising the options included in the lease agreements.

With specific regard to property leases, it was decided to consider only the first renewal period for all new contracts (as well as at the date of FTA), as reasonably certain, unless there are specific contractual clauses, facts or circumstances, that lead us to consider additional renewals or determine the end of the lease.

On the basis of the characteristics of Italian lease agreements and the provisions of Law 392/1978, in the event of the signing of a new lease agreement with a contractual term of six years and the option of tacitly renewing the agreement every six years, the total lease term will be at least twelve years. This general indication is exceeded if the agreement contains new elements or contemplates specific situations.

Discount rate

With respect to the discounting rate, based on the requirements of IFRS 16, the implicit interest rate is used for each lease agreement, where available. In some cases, f for example in the case of leases, the implicit interest rate cannot always be determined promptly without using estimates and assumptions, as the lessee does not have sufficient information about the unsecured residual value of the leased asset. In these cases, a methodology has been developed to define the incremental interest rate as an alternative to the implicit interest rate.

The incremental interest rate is the rate at which the lessee would be willing to pay, on a similar due date and for a similar asset, the funds necessary to obtain an asset of comparable value to the asset with a right of use in similar economic conditions. The following aspects were taken into account when calculating the incremental interest rate:

- the interest rate equates to the rate at which the Bank would borrow funds for the duration of the right of use;
- is the rate at which the Bank would finance itself to purchase an asset of comparable value to the asset corresponding to the right of use;
- reflects the rate for secured financing for an asset comparable to that expressed by the right of use.

This rate, since it takes into account the creditworthiness of the lessee, the nature and quality of the collateral provided and the economic environment in which the transaction takes place, is therefore in line with the requirements of the standard.

Lease and non-lease components

It should also be noted that it was decided not to separate the service components from the leasing components and therefore to recognise the entire contract as a lease, as the service components are not significant.

The effects of the first application (FTA) of IFRS 16

The adjustment of the opening financial statements following the application of IFRS 16 using the amended retrospective approach resulted in an increase in assets following the recognition of new rights of use at Group level of €20.1 million, and financial liabilities (payable to the lessor) of the same amount. The first-time adoption of the standard did not therefore have an impact on shareholders' equity since, following the decision to adopt the "modified approach", at the time of the first application, the values of assets and liabilities coincide, net of the reclassification of accruals and the exposure of leases previously classified as financial leases, applying IAS 17.

At first-time adoption of IFRS 16, the decision was made not to restate the scope of application defined by IAS 17, but to apply the standard only to lease agreements identified on the basis of IAS 17 and IFRIC 4 (paragraph C3 a) requirements of IFRS 16.

It should also be noted that in the financial statements at 31 December 2018, no contracts classified as finance leases pursuant to IAS 17 were identified. Accordingly, the scope of application of IFRS 16 consists exclusively of rights of use acquired following the inclusion of property lease agreements. The rights of use acquired through real estate lease contracts are indicated in sub-item "b) buildings".

Financial assets designated at fair value through profit or loss (FVTPL)

Classification criteria

This category includes financial assets other than those classified as financial assets at fair value with an impact on total profitability and as financial assets valued at amortised cost. This item specifically includes:

- financial assets held for trading, mainly consisting of debt and equity securities and the positive value of derivative contracts held for trading;
- financial assets that must be measured at fair value, consisting of financial assets that do not meet the requirements for measurement at amortised cost, or at fair value with an impact on comprehensive income. These are financial assets with contractual terms that do not only provide for repayments of principal and interest on the principal amount to be repaid (known as "SPPI test"), or which are not held as part of a business model whose objective is to hold assets for the purpose of collecting contractual cash flows (the "Hold to Collect" Business Model), or in a business model with an objective that is achieved either by collecting contractual financial flows or by selling financial assets (the "Hold to Collect and Sell" Business Model);
- financial assets designated at fair value, i.e. the financial assets so defined at the time of initial recognition, if the requirements are met. In this case, an entity may irrevocably designate a financial asset for recognition as measured at fair value through profit or loss if, and only if, by doing so it eliminates or significantly reduces a valuation inconsistency.

This item therefore includes:

- debt securities and loans that are included in a business model Other/Trading (i.e. not attributable to the "Hold to Collect" or "Hold to Collect and Sell" business models) or that do not pass the SPPI test, including shares of syndicated loans subscribed which, from the outset, are intended for sale and which are not attributable to a Hold to Collect and Sell business model;
- equity instruments - not qualifying as control, connection or joint control - that are held for trading purposes or for which it was decided, on initial recognition, not to designate them at fair value with an impact on with an impact on comprehensive income;
- UCITS units.

This item also includes derivative contracts, recognised under financial assets held for trading, which are represented as assets if the fair value is positive and as a liability if the fair value is negative. Current positive and negative values arising from transactions with the same counterparty can only be offset if there is a current legal right to offset the amounts recognised in the accounts and the intention is to settle the net positions to be offset on a net basis.

Derivatives also include those embedded in complex financial contracts - in which the primary contract is a financial liability - which have been recognised separately because:

- their economic characteristics and risks are not closely correlated to the characteristics of the underlying contract;
- embedded instruments, even if separate, meet the definition of a derivative;
- the hybrid instruments to which they belong are not measured at fair value with the related changes recognised in the income statement.

With regard to the classification rules, IFRS 9 does not allow any reclassification for equity securities. Reclassifications are not permitted for other categories of financial assets, unless the entity amends its business model for the management of financial assets. In such cases, which are expected to be very infrequent, financial assets may be reclassified from the category measured at fair value through profit or loss into one of the two other categories envisaged in IFRS 9 (Financial assets measured at amortised cost or Financial assets designated at fair value with impact on comprehensive income). The transfer value is represented by fair value at the time of reclassification and the effects of the reclassification operate prospectively from the date of reclassification. In this case, the effective interest rate of the reclassified financial asset is determined on the basis of its fair value at the reclassification date, and this date is considered as the initial recognition date for the allocation in the various stages of credit (stage assignment) for impairment purposes.

For further information on the criteria for the classification of financial instruments, see the chapter below entitled "Classification criteria for financial assets".

Recognition criteria

Financial assets are initially recognised on the settlement date for debt and equity securities, on the disbursement date for loans and on the signature date for derivative contracts.

Upon initial recognition, financial assets measured at fair value through profit or loss are recognised at fair value, without considering transaction costs or revenues directly attributable to the instrument itself.

Valuation criteria

After initial recognition, financial assets measured at fair value through profit or loss are valued at fair value. The effects of the application of this valuation criterion are charged to the income statement.

Market prices are used to determine the fair value of financial instruments listed on an active market. In the absence of an active market, commonly used valuation methods and valuation models are used, which take account of all risk factors associated with instruments and which are based on market data such as: valuation of listed instruments with similar characteristics, calculation of discounted cash flows, option pricing models, values recorded in recent comparable transactions, etc. For equity securities and derivatives relating to equity securities that are not listed on an active market, the cost criterion is used as an estimate of fair value only to a residual extent, limited to a few circumstances, i.e. if none of the valuation methods indicated above are applicable, or if there is a wide range of possible fair value measurements, in which cost represents the most significant estimate.

Cancellation criteria

Financial assets are derecognised only if the disposal has resulted in the substantial transfer of all the risks and rewards associated with the assets. Conversely, if a significant part of the risks and rewards associated with the transferred financial assets has been retained, they continue to be recorded in the financial statements, even though legally the ownership of the assets has actually been transferred.

In the event that it is not possible to ascertain a substantive transfer of risks and rewards, financial assets are derecognised from the balance sheet if no type of control over them has been retained. Otherwise, the retention of control, even in part, entails maintaining the assets on the balance sheet to the extent of their residual involvement, measured by the exposure to changes in the value of the assets sold and to changes in the associated cash flows.

Finally, financial assets that are ceded are derecognised if the entity retains the contractual rights to receive the cash flows from the assets, but assumes a concurrent obligation to remit those cash flows - and only those cash flows - to third parties without any significant delay.

Financial assets measured at fair value with impact on comprehensive income (FVOCI)

Classification criteria

This category includes financial assets that meet both of the following conditions:

- the financial asset is held according to a business model with an objective that is pursued through the collection of contractual cash flows and through sale (a "Hold to Collect and Sell" Business Model), and
- the contractual terms of the financial asset provide, on certain dates, for cash flows consisting solely of payments of capital and interest on the amount of capital to be returned (the so-called "SPPI test" is passed).

This item also includes equity instruments not held for trading purposes, for which the option for designation at fair value with an impact on comprehensive income was exercised at the time of initial recognition.

In particular, this item includes:

- debt securities that are part of a "Hold to Collect and Sell" business model and which have passed the SPPI test;
- equity interests, which cannot be classed as controlling, connecting or joint control, that are not held for trading purposes, for which the option to designate them at fair value with an impact on comprehensive income was exercised;
- loans that are attributable to a "Hold to Collect and Sell" business model and that passed the SPPI test, including units of subscribed syndicated loans that, from the outset, are intended for sale and that are attributable to a "Hold to Collect and Sell" business model.

Reclassifications to other categories of financial assets are not permitted unless the entity amends its business model to allow for the management of financial assets. In such cases, which are expected to be very infrequent, financial assets may be reclassified from the category valued at fair value with an impact on comprehensive income into one of the other two categories set out in IFRS 9 (Financial assets measured at amortised cost or Financial assets designated at fair value with an impact through profit or loss).

The transfer value is represented by fair value at the time of reclassification and the effects of the reclassification operate prospectively from the date of reclassification. In the event of reclassification from the category in question to the amortised cost category, the cumulative profit (loss) recognised in the valuation reserve is recognised as an adjustment to the fair value of the financial asset at the date of reclassification. In the event of reclassification to the category of fair value through profit or loss, the

cumulative profit (loss) recognised previously in the valuation reserve is reclassified from shareholders' equity to profit (loss) for the year.

No reclassification is permitted for equity securities.

For further information on the criteria for the classification of financial instruments, see the chapter below entitled "Classification criteria for financial assets".

Recognition criteria

Initial recognition of financial assets occurs at settlement date for debt and equity securities and at disbursement date for loans. On initial recognition, assets are recognised at fair value, including transaction costs or revenues directly attributable to the instrument.

Valuation criteria

Following initial recognition, assets classified as fair value with an impact on comprehensive income, other than equity securities, are measured at fair value, with the impact of the application of amortised cost, the effects of impairment and any exchange rate effect recognised in the income statement, while other gains or losses deriving from a change in fair value are recognised in a specific equity reserve until the financial asset is derecognised. At the time of disposal, in whole or in part, the gain or loss accumulated in the valuation reserve is paid back, in whole or in part, to the income statement.

The equity instruments chosen for classification in this category are measured at fair value and the amounts recognised as a contra-entry to equity (statement of comprehensive income) must not be subsequently transferred to the income statement, even in the event of sale. The only component attributable to the equity securities in question that is recognised in the income statement is the relevant dividends.

The fair value is determined on the basis of the criteria illustrated above for financial assets measured at *fair value* through profit or loss.

For equity securities included in this category, which are not listed on an active market, the cost criterion is used as an estimate of fair value only to a residual extent and limited to a few circumstances, i.e. if all of the valuation methods mentioned above do not apply, or if there is a wide range of possible fair value valuations in which cost represents the most significant estimate.

Financial assets measured at fair value with an impact on comprehensive income – in the form of both debt securities and receivables – are subject to verification of the significant increase in credit risk (impairment) provided for by IFRS 9, as are assets at amortised cost, with the consequent recognition in the income statement of an impairment adjustment to cover expected losses. More specifically, on instruments classified as stage 1 (i.e. on financial assets at the time of origination, if not impaired, and on instruments for which there has been no significant increase in credit risk since the date of initial recognition), an expected loss at one year is recognised at the date of initial recognition and at each subsequent reporting date. On the other hand, for instruments classified as stage 2 (performing is for which there has been a significant increase in credit risk since the date of initial recognition) and stage 3 (non-performing exposures), an expected loss is recognised for the entire residual life of the financial instrument.

Conversely, equity securities are not subject to the impairment process.

For further information, see the section below entitled "Impairment of financial assets".

Cancellation criteria

Financial assets are derecognised only if the disposal has resulted in the substantial transfer of all the risks and rewards associated with the assets. Conversely, if a significant part of the risks and rewards associated with the transferred financial assets has been retained, they continue to be recorded in the financial statements, even though legally the ownership of the assets has actually been transferred.

In the event that it is not possible to ascertain a substantive transfer of risks and rewards, financial assets are derecognised from the balance sheet if no type of control over them has been retained. Otherwise, the retention of control, even in part, entails maintaining the assets on the balance sheet to the extent of their residual involvement, measured by the exposure to changes in the value of the assets sold and to changes in the associated cash flows.

Finally, financial assets that are ceded are derecognised if the entity retains the contractual rights to receive the cash flows from the assets, but assumes a concurrent obligation to remit those cash flows - and only those cash flows - to third parties without any significant delay.

Financial assets measured at amortised cost

Classification criteria

This category includes financial assets (particularly loans and debt securities) that meet both of the following conditions:

- the financial asset is held according to a business model with an objective that is pursued through the collection of contractual cash flows (the “Hold to Collect” Business Model), and
- the contractual terms of the financial asset provide, on certain dates, for cash flows consisting solely of payments of capital and interest on the amount of capital to be returned (the so-called “SPPI test”).

More specifically, the following are recognised under this item:

- loans with banks in the various technical forms that meet the requirements indicated in the preceding paragraph;
- loans to customers in the various technical forms that meet the requirements indicated in the preceding paragraph;
- debt securities meeting the requirements of the previous paragraph.

This category also includes operating receivables connected with the provision of financial services as defined by the Italian Consolidated Banking Act and the Italian Consolidated Finance Act (E.G. for the distribution of financial products and servicing activities).

According to the general rules laid down in IFRS 9 on the reclassification of financial assets, reclassifications to other categories of financial assets are not permitted unless the entity amends its business model to allow for the management of financial assets. In such cases, which are expected to be very infrequent, financial assets may be reclassified from the category measured at amortised cost into one of the other two categories set out in IFRS 9 (Financial assets designated at fair value with an impact on comprehensive income or Financial assets designated at fair value through profit or loss).

The transfer value is represented by fair value at the time of reclassification and the effects of the reclassification operate prospectively from the date of reclassification. Gains or losses arising from the difference between the amortised cost of the financial asset and its fair value are recognised in the income statement if they are reclassified to financial assets measured at fair value through profit or loss, and to shareholders' equity - in the relevant valuation reserve - if they are reclassified to financial assets measured at fair value with an impact on comprehensive income.

For more information on the criteria for classifying financial instruments, see the section below entitled "Classification criteria for financial assets".

Recognition criteria

Financial assets are initially recognised on the settlement date for debt securities and on the disbursement date for loans. On initial recognition, assets are recognised at fair value, including transaction costs or revenues directly attributable to the instrument.

In particular, with regard to receivables, the disbursement date normally coincides with the date of signing of the contract. If no such coincidence occurs, at the time of signing the contract a commitment to disburse funds is given which concludes on the date of disbursement of the loan. The receivable is recognised on the basis of its fair value, equal to the amount disbursed, or subscription price, including costs/income directly attributable to the individual receivable and determinable from the start of the transaction, even if settled at a later date.

Costs that, despite having the above characteristics, are subject to reimbursement by the debtor counterparty or are classifiable as normal internal administrative costs are excluded.

Valuation criteria

After initial recognition, the financial assets in question are measured at amortised cost, using the effective interest rate method. In these terms, the asset is recognised in the financial statements at an amount equal to its initial recognition value less any capital repayments, plus or minus cumulative amortisation (calculated using the effective interest rate method referred to above) of the difference between that initial amount and the amount at maturity (typically attributable to the costs/revenues charged directly to the individual asset) and adjusted by any provision to cover losses. The effective interest rate is the rate that exactly discounts the rate that equals the present value of the future flows of the asset, for principal and interest, to the amount disbursed including costs/income associated with the financial asset itself. This method of accounting, using a financial logic, makes it possible to distribute the economic effect of costs/income directly attributable to a financial asset over its expected residual life.

The amortised cost method is not used for assets – valued at cost – whose brief duration makes the application of the discounting approach negligible for assets without a fixed maturity and receivables subject to revocation.

The valuation criteria, as indicated in greater detail in the chapter entitled "Impairment of financial assets", are closely related to the inclusion of the instruments in question in one of the three stages (stages of credit risk) provided for in IFRS 9, the last of which (stage 3) includes impaired financial assets, and the remaining while the remaining two (stage 1 and 2) includes performing financial assets.

With regard to the accounting presentation of these valuation effects, value adjustments relating to this type of asset are recognised in the income statement:

- upon initial recognition, for an amount equal to the expected loss at twelve months;
- at the time of the subsequent valuation of the asset, if the credit risk was not significantly increased compared to the initial recognition, in relation to changes in the amount of impairment losses expected in the following twelve months;
- at the time of the subsequent valuation of the asset, if credit risk was significantly increased compared to initial recognition, in relation to the recognition of value adjustments for expected losses relating to the entire residual life of the asset as provided for in the contract;
- at the time of subsequent valuation of the asset, if - after there has been a significant increase in credit risk compared to initial recognition - the "significance" of this increase has ceased to exist, in relation to

the adjustment of the cumulative adjustments to take account of the transition from a expected loss over the instrument's entire residual life (its "lifetime") from one to twelve months.

If the financial assets in question are performing, they are valued in order to determine the value adjustments to be recognised in the financial statements at the level of the individual loan ratio (or "tranche" of the security), based on the risk parameters represented by probability of default (PD), loss given default (LGD) and exposure at default (EAD).

If, in addition to a significant increase in credit risk, there is objective evidence of impairment, the amount of the loss is measured as the difference between the book value of the asset – classified as "impaired", as with all other relationships with the same counterparty – and the present value of the estimated future cash flows, discounted at the original effective interest rate. The amount of the loss, to be recognised through the income statement, is defined on the basis of an analytical assessment process or determined according to homogeneous categories, and therefore is analytically attributed to each position and takes into account, as detailed in the chapter entitled "Impairment of financial assets", forward-looking information and possible alternative recovery scenarios.

The category of impaired assets includes financial instruments which have been attributed the status of doubtful, unlikely to pay or past due, according to the rules of the Bank of Italy, which are consistent with IAS/IFRS and European supervisory regulations.

Expected cash flows take into account expected recovery times and the presumed realisable value of any guarantees.

The original effective rate of each asset remains unchanged over time, even if the relationship has been restructured, resulting in a change in the contractual rate and even if the relationship in practice fails to bear the contractual interest.

If the grounds for impairment cease to apply as a result of an event occurring after the recognition of impairment, the value is reinstated and charged to the income statement. The write-back may not exceed the amortised cost that the financial instrument would have had in the absence of previous adjustments.

Reversals of write-backs related to the passage of time are recognised in net interest income.

In some cases, during the life of the financial assets in question, and in particular the receivables, the original contractual conditions are subject to subsequent amendment by the parties to the contract. When, over the life of an instrument, the contractual clauses are amended, it is necessary to check whether the original asset should continue to be recognised in the financial statements or whether, on the contrary, the original instrument is to be derecognised and a new financial instrument recognised.

In general, changes to a financial asset lead to the derecognition of the financial asset and the recognition of a new asset when the changes are "substantial". Both qualitative and quantitative elements must be taken into account in any assessment of the "substantiality" of the change. In some cases, it may be clear, without recourse to complex analyses, that the changes introduced substantially alter the characteristics and/or contractual flows of a given asset, whereas in other cases, further analyses (including quantitative analyses) will need to be conducted in order to assess their effects and to verify whether it is necessary to derecognise the asset and recognise a new financial instrument.

Analyses (which are qualitative-quantitative) conducted in order to ascertain the "substantial" nature of the contractual changes made to a financial asset must therefore consider:

- the purposes for which the changes were made: for example, renegotiations for commercial reasons and concessions due to financial difficulties of the counterparty:
    a) the former, aimed at "retaining" the customer, involve a debtor who is not in financial difficulty. This includes all renegotiation operations that are intended to adapt the burden of the debt to market conditions. Such operations involve a change in the original terms of the agreement, usually sought by the debtor, relating to the burden of the debt, with a consequent economic benefit for the debtor. In general, it is considered that whenever the bank renegotiates in order to avoid losing its customer,

such renegotiation should be considered substantial since, if it is not undertaken, the customer could seek funding from another intermediary and the bank would suffer a decrease in future expected revenues;

b) the second, performed for "credit risk reasons" (forbearance measures), has the objective of maximising the recovery of cash flows. As a rule, the underlying risks and rewards are not substantially transferred following the changes and, consequently, accounting representation is based on "modification accounting" which provides for recognition in the income statement of the difference between the book value and present value of the modified cash flows discounted at the original interest rate, without derecognition;

- the presence of specific objective elements ("triggers") that affect the characteristics and/or contractual flows of the financial instrument (such as, by way of example, a change of currency or a change in the type of risk to which it is exposed, when combined with equity and commodity parameters), that are deemed to entail derecognition in view of their impact (expected to be significant) on the original contractual flows.

Cancellation criteria

Financial assets are derecognised only if the disposal has resulted in the substantial transfer of all the risks and rewards associated with the assets. Conversely, if a significant part of the risks and rewards associated with the transferred financial assets has been retained, they continue to be recorded in the financial statements, even though legally the ownership of the assets has actually been transferred.

In the event that it is not possible to ascertain a substantive transfer of risks and rewards, financial assets are derecognised from the balance sheet if no type of control over them has been retained. Otherwise, the retention of control, even in part, entails maintaining the assets on the balance sheet to the extent of their residual involvement, measured by the exposure to changes in the value of the assets sold and to changes in the associated cash flows.

Finally, financial assets that are ceded are derecognised if the entity retains the contractual rights to receive the cash flows from the assets, but assumes a concurrent obligation to remit those cash flows - and only those cash flows - to third parties without any significant delay.

Hedging

As of the date of this report, Volksbank does not have any hedging operations in place. The option taken, in the case of new hedging transactions, which is permitted during the introduction of IFRS 9, is to continue to apply in full the provisions of IAS 39 for hedge accounting (in the 'carved out' version approved by the European Commission) for each type of hedging (both specific hedges and macro hedges).

Classification criteria: type of hedges

The purpose of risk hedging transactions is to neutralise potential losses attributable to a given risk and recognised on a given element or group of elements, should that particular risk actually arise.

The types of hedge used are as follows:

- fair value hedge: the aim is to hedge exposure to the change in the fair value (attributable to the various types of risk) of assets and liabilities recognised in the balance sheet or portions thereof, groups of assets/liabilities, irrevocable commitments and portfolios of financial assets and liabilities, including core deposits, as permitted by IAS 39 and approved by the European Commission. Generic fair value ("macro

hedge") are designed to reduce fluctuations in fair value, attributable to interest rate risk, of a monetary amount deriving from a portfolio of assets or liabilities;

- cash flow hedges: these are designed to hedge exposure to changes in future cash flows attributable to particular risks associated with balance sheet items. This type of hedge is essentially used to stabilise the interest flow of variable-rate deposits to the extent that they finance fixed-rate loans. Under certain circumstances, similar transactions are undertaken for certain types of variable-rate loans;
- hedging of a foreign currency investment: this relates to the hedging of the risks of an investment in a foreign company expressed in foreign currency.

Given the decision made to make use of the option to continue to fully apply the rules of IAS 39 for hedging relationships, it is not possible to designate the equity securities classified under financial assets measured at fair value with an impact on comprehensive income (FVOCI) as hedged items for price or exchange rate risk, since these instruments do not impact the income statement, even in the event of sale (except for dividends that are recognised in the income statement).

Recognition criteria

Hedging derivatives, like all derivatives, are initially recognised and subsequently measured at fair value.

Valuation criteria

Hedging derivatives are measured at fair value. In particular:

- in the case of fair value hedging, the change in the fair value of the hedged item is offset by the change in the fair value of the hedging instrument. This offsetting is recognised through the recognition in the income statement of changes in value, relating both to the hedged item (with regard to the changes produced by the underlying risk factor) and to the hedging instrument. Any difference, which represents the partial ineffectiveness of the hedge, therefore constitutes the net economic effect. In the case of generic fair value hedging transactions ("macro hedge"), changes in fair value with reference to the hedged risk of the hedged assets and liabilities are recognised in the balance sheet respectively under item 60 on the asset side "Value adjustment of hedged financial assets" or item 50 on the liability side "Value adjustment of hedged financial liabilities";
- in the case of cash flow hedges, changes in the fair value of the derivative are recognised in shareholders' equity, for the effective portion of the hedge, and are recognised in the income statement only when, with respect to the hedged item, there is a change in the cash flows to be offset or if the hedge is ineffective;
- hedges of an investment in foreign currency are accounted for in the same way as cash flow hedges.

The derivative instrument is designated as a hedge if there is formal documentation of the relationship between the hedged instrument and the hedging instrument and if it is effective at the time the hedge commences and, prospectively, throughout the life of the hedging instrument.

The effectiveness of the hedge depends on the extent to which changes in the fair value of the hedged instrument or the related expected cash flows are offset by those of the hedging instrument. Effectiveness is therefore appreciated by comparing the said changes, taking account of the intent pursued by the company at the time the hedge was implemented. It is effective when changes in the fair value (or cash flow) of the hedging instrument neutralise almost entirely, i.e. within the limits set by the 80-125% range, changes in the hedged instrument for the hedged risk element.

Effectiveness is assessed at each annual or interim reporting date using:

- prospective tests, which justify the application of hedge accounting, as they demonstrate its expected effectiveness;

- retrospective tests, which show the degree of effectiveness of the hedge achieved in the period to which they refer, i.e. they measure how far the actual results have deviated from the perfect hedge.

If the tests do not confirm the effectiveness of the hedge, from that moment on the hedge accounting, as indicated above, is interrupted, the hedging derivative contract is reclassified among the trading instruments and the hedged financial instrument regains the valuation criterion corresponding to its classification in the financial statements.

In the event of the interruption of a generic fair value hedging relationship, the cumulative revaluations/write-downs are recorded under item 60. Value adjustment of hedged financial assets (+/-) "Value adjustment of hedged financial liabilities" (item 50) are recognised in the income statement among interest income or expense over the residual life of the original hedging relationships, subject to verification that the conditions are met.

Equity investments

Classification, recognition and measurement criteria

The item includes investments in joint ventures and associates.

Joint ventures are entities for which, on a contractual basis, control is shared between the Bank and one or more other parties, or when decisions concerning significant activities require the unanimous consent of all parties sharing control.

Companies subject to significant influence ("associates") are those in which the Bank holds at least 20% of the voting rights (including "potential" voting rights) or in which - although with a lower percentage of voting rights - it has the power to participate in determining the financial and operating policies of the subsidiary by virtue of particular legal relationships such as participation in shareholders' agreements.

Certain interests of more than 20%, in which the Bank only holds equity rights to a portion of the investment income, has no access to management policies, and may exercise governance rights only in relation to the protection of equity interests, are not considered to be subject to significant influence.

If there is evidence that the value of an investment may have been impaired, the recoverable amount of the investment is estimated, taking into account the present value of the future cash flows that the investment may generate, including the final disposal value of the investment.

If the recoverable amount is lower than the book value, the difference is recognised in the income statement.

If the grounds for impairment cease to apply as a result of an event occurring after the recognition of impairment, the value is reinstated and charged to the income statement.

Cancellation criteria

Equity investments are derecognised when the contractual rights to the cash flows from the assets expire or when the investment is sold, along with substantially all its associated risks and rewards.

Physical assets

Classification criteria

Physical assets include land, buildings used for business purposes, investment property, valuable artistic assets, technical equipment, furniture and fittings, and equipment of any kind that is expected to be used for more than one period.

Tangible assets held for use in the production or supply of goods and services are classified as "assets for functional use" in accordance with IAS 16. Real properties held for investment purposes (in order to earn rentals or for capital appreciation) are classified as "assets held for investment purposes" in accordance with IAS 40.

The item also includes tangible assets classified in accordance with IAS 2 - Inventories, which relate both to assets deriving from the enforcement of guarantees or from a purchase at auction that the company intends to sell in the near future without undertaking significant refurbishment works, and which do not meet the requirements to be classified in the previous categories, and to the property portfolio, including building sites, buildings under construction, completed properties for sale and property development initiatives, held with a view to disposal.

Finally, rights of use acquired through leasing and relating to the use of a physical asset (for lessee companies) and the assets granted under operating leases (for leasing companies) are included.

Recognition criteria

Physical assets are initially recognised at cost, which includes, in addition to the purchase price, any additional charges directly attributable to the purchase and commissioning of the asset.

Extraordinary maintenance expenses that increase future economic benefits are recognised as an increase in the value of the assets, while other ordinary maintenance costs are recognised in the Income Statement.

According to IFRS 16, leases are accounted for on the basis of the right of use model, whereby, at the starting date, the lessee has a financial obligation to make payments due to the lessor to offset its right to use the underlying asset during the term of the lease.

When an asset is made available to the lessee for use (start date), the lessee recognises both the liability and the asset consisting of the right of use.

Valuation criteria

Physical assets are valued at cost, less any depreciation and impairment, with the exception of property for functional use and fine artistic assets that are valued according to the redetermination of value method.

Properties held for investment purposes are valued using the fair value method.

For physical assets subject to valuation using the revaluation method:

- if the book value of an asset is increased as a result of a change in value, the increase must be recognised in the statement of other comprehensive income and accumulated in equity under the revaluation reserve heading. However, if it reverses a decrease in a revaluation of the same asset previously recognised in the income statement, it must be recognised as income;
- if the book value of an asset has decreased as a result of the redetermination of its value, the decrease must be recognised in the statement of other comprehensive income as a revaluation surplus insofar as there are any credit balances in the revaluation reserve in respect of the asset; otherwise, the decrease must be recognised in the income statement.

Physical assets are systematically depreciated on a straight-line basis over their useful lives The depreciable amount is represented by the cost of the assets (or by the net re-determined value if the valuation method adopted is that of the re-determination of value) net of the residual value at the end of the depreciation process, if significant. The properties are amortised by a portion deemed appropriate to account for the deterioration of the assets over time following their use, taking account of extraordinary maintenance

expenses, which are added to the value of the assets. In order to determine the useful life of the various types of assets and the corresponding depreciation coefficients, the Group's real-estate assets were divided into four clusters: (i) historical encumbered and unencumbered real estate, (ii) free-standing properties, (iii) bank branches and (iv) other properties.

However, the following are not amortised:

- land, whether acquired individually or incorporated into the value of buildings, as it has an indefinite useful life;
- valuable artistic heritage and other artistic and decorative historical assets as their useful life cannot be estimated and their value is normally destined to increase over time;
- investment properties which, as required by IAS 40, are measured at fair value through profit or loss and therefore do not have to be depreciated.

If there is any evidence that material assets measured at cost may have become impaired, the book value of the asset its compared with its recoverable amount. Any adjustments are recognised in the income statement.

If the grounds for impairment cease to apply, the value is written back, but this write-back cannot exceed the value that the asset would have had, net of depreciation charges, in the absence of previous losses in value.

Physical assets recognised in accordance with IAS 2, and are valued at the lower of cost and net realisable value, provided that a comparison is made between the book value of the asset and its recoverable value if there is any indication that the asset may have suffered a loss in value. Any adjustments are recognised in the income statement.

With regard to the asset consisting of the right to use, recognised in accordance with IFRS 16, this is measured using the cost model in accordance with IAS 16 - Property, plant and equipment. In this case, the asset is subsequently amortised and subject to impairment testing if indicators of impairment emerge.

Cancellation criteria

A physical asset is eliminated from the Balance Sheet at the time of its disposal or when the asset is permanently withdrawn from use and no future economic benefits are expected to flow from its disposal.

Intangible assets

Classification criteria

Intangible assets include goodwill and other intangible assets governed by IAS 38. The category includes the use rights acquired through leasing and relating to the use of an intangible asset (for lessees) and the assets granted under operating leases (for lessors).

Intangible assets are recognised as such if they are identifiable and originate from legal or contractual rights. Intangible assets also include goodwill, which represents the positive difference between the purchase cost and the fair value of the assets and liabilities of an acquired company.

Recognition and measurement criteria

Intangible assets are recognised at cost, adjusted for any accessory charges only if it is probable that the future economic benefits attributable to an asset will be realised and if the cost of the asset can be reliably

determined. Otherwise, the cost of an intangible asset is recognised in the income statement in the year in which it is incurred.

For assets with finite useful lives, cost is amortised on a straight-line basis or in decreasing portions determined on the basis of the economic benefits expected to flow from the asset. Assets with an indefinite useful life are not amortised on a straight-line basis, but are tested periodically to determine whether their book value is adequate.

If there is any evidence that an asset may have become impaired, the asset's recoverable amount is estimated. The loss, recognised in the income statement, is equal to the difference between the book value of the asset and its recoverable value.

In particular, intangible assets include:

- technology-based intangible assets such as software, which are amortised on the basis of their expected technological obsolescence and in any case no longer than three years. In particular, costs incurred internally in the development of software projects constitute intangible assets and are recognised as assets only if all of the following conditions are met: i) the cost attributable to the development activity is reliably determinable; ii) the intention, availability of financial resources and the technical capacity to make the asset available for use or sale; iii) it is demonstrable that the asset is capable of producing future economic benefits. The development costs of the capitalised software include only expenses incurred which can be directly attributed to the development process. Capitalised software development costs are systematically amortised of the estimated life of the relevant product/service to reflect the ways in which the future economic benefits deriving from the activity are expected to be consumed by the entity from the start of production and throughout the estimated life of the product;
- intangible customer-related assets represented by the valuation, on the occasion of aggregation transactions, of asset management relationships, non-financial assets related to the provision of services and the insurance portfolio.

  These assets, with a finite life, are originally valued through the discounting, using a rate representing the time value of money and asset-specific risks, the cash flows representing profit margins over a period expressing the residual duration, contractual or estimated, of the relationships existing at the time of the combination. They are amortised, for asset management transactions and non-financial assets related to the provision of services, on a straight-line basis over the most significant inflow period of the expected economic benefits in the case of relationships without a fixed maturity and, for relationships related to insurance contracts, in decreasing proportions corresponding to the term of the contracts in the case of relationships with a fixed maturity (the residual life of policies).

Finally, intangible assets include goodwill.

Goodwill may be recognised as part of a business combination when the positive difference between the consideration transferred and any recognition at fair value of the minority interest and the fair value of the assets acquired is representative of future earning capacity.

If the difference is negative (badwill), or if goodwill is not justified by the of the investee company's future income-generating potential, it is recognised directly in the income statement.

A test to verify the adequacy of the value of goodwill is conducted annually (or whenever there is evidence of impairment). To this end, the cash-generating unit to allocate goodwill is identified. In Volksbank, the cash-generating unit is the business entity in its entirety. The amount of any impairment loss is determined on the basis of the difference between the book value of goodwill and its recoverable amount, if lower. This recoverable amount is equal to the greater of the fair value of the cash-generating unit, net of any costs to sell, and its value in use. The resulting adjustments are recognised through the income statement.

Cancellation criteria

An intangible asset is derecognised from the balance sheet at the time of disposal or when future economic benefits are no longer expected.

Other assets

Other assets essentially include items awaiting settlement and items not attributable to other balance sheet items, including receivables arising from the supply of non-financial goods and services, tax items other than those recognised through own account (for example related to withholding tax), gold, silver, precious metals and accrued income other than that which is capitalised on the related financial assets, including those arising from contracts with customers pursuant to IFRS 15, paragraphs 116 et seq.

Non-current assets or groups of assets/liabilities held for sale

The items "Non-current assets and groups of assets held for sale" and the liability item "Liabilities associated with assets held for sale" are classified under assets and liabilities as non-current assets or disposal groups for which a disposal process has been initiated and their sale is considered highly likely. These assets/liabilities are measured at the lower of their book value and their fair value net of costs of disposal, with the exception of certain types of assets (e.g. financial assets falling within the scope of application of IFRS 9) for which IFRS 5 specifically provides that the valuation criteria for the relevant accounting standard must be applied.

Income and expenses (net of the tax effect), attributable to groups of assets being divested or recognised as such during the year are presented in the income statement under a separate item.

Current and deferred taxation

Income taxes, calculated in accordance with national tax legislation, are accounted for as a cost on an accrual basis, in line with the method of recording the costs and revenues that generated them in the financial statements. They therefore represent the balance of current and deferred taxation relating to income for the year. Current tax assets and liabilities include the net balance of the company's tax positions vis-à-vis the Italian tax authorities. In particular, these items include the net balance between current tax liabilities for the year, calculated on the basis of a prudent forecast of the tax burden due for the year, determined on the basis of current tax regulations, and current tax assets consisting of advances and other tax credits for withholding tax incurred, or other tax credits from previous years for which the company has requested offsetting against taxes from subsequent years.

Current tax assets also include tax credits for which the company has applied for reimbursement from the competent tax authorities, and sums paid provisionally during a dispute procedure with the Tax Authorities. The risk inherent in these proceedings, in the same way as the risks inherent in proceedings that did not require provisional payments, is assessed according to the logic of IAS 37 in relation to the likelihood of using economic resources to fulfil any consequent demands.

Considering the company's adoption of the national tax consolidation scheme, tax positions relating to the companies included in the scheme are managed separately from an administrative standpoint.

Deferred taxation is calculated according to the balance sheet liability method, taking into account the tax effect of the temporary differences between the book value of the assets and liabilities and their value for tax purposes, which will determine taxable or deductible amounts in future periods. For these purposes,

"taxable temporary differences" are those that in future periods will determine taxable amounts and "deductible temporary differences" are those that in future years will determine deductible amounts.

Deferred tax liabilities are calculated by applying the tax rates currently in force to taxable temporary differences that are likely to generate a tax burden, and to the deductible temporary differences for which it is reasonably certain that there will be future taxable amounts at the time when the related tax deductibility will become apparent (the so-called 'probability test'). Deferred tax assets and liabilities related to the same tax and due in the same period are set off against one another.

If deferred tax assets and liabilities refer to items affecting the income statement, they are recognised through income taxes.

Where deferred tax assets and liabilities relate to transactions that have a direct impact on shareholders' equity without affecting the income statement (such as adjustments due to the first-time adoption of IASs/IFRSs, measurement of financial instruments recognised at fair value with an impact on comprehensive income or derivatives contracts for cash flow hedges), they are recognised with a balancing entry in shareholders' equity, involving specific reserves when provided for (e.g., valuation reserves).

Latent taxation on balance sheet items suspended for tax purposes that are "taxable in all cases of use" is recognised in the financial statements as a reduction in shareholders' equity. Deferred taxes relating to revaluations for conversion to the Euro, directly charged to a specific reserve pursuant to Article 21 of Legislative Decree No. 213/98 with suspended taxation, are recognised in the financial statements as a reduction of the reserve. Latent taxation on balance sheet items suspended for tax purposes that are "taxable only in the event of distribution" is not entered in the financial statements, since the amount of available reserves already subject to taxation allows for an assumption that no transactions involving the taxation will be undertaken.

Deferred taxes relating to companies included in the tax consolidation are recognised in their financial statements, in application of the accrual basis of accounting and in consideration of the value of the tax consolidation limited to the fulfilment of the liquidation of current tax positions.

Provisions for risks and charges

Pension funds and similar obligations

Provisions for pensions are established in accordance with company agreements and qualify as defined-benefit plans. The liability relating to these plans and the related pension cost of current employment services are determined on the basis of actuarial assumptions applying the "Projected Unit Credit Method", which provides for the projection of future disbursements on the basis of historical statistical analyses and the demographic curve and the financial discounting of these flows on the basis of a market interest rate. Contributions made in each financial year are considered as separate units, recognised and valued individually for the purposes of determining the final obligation. The discount rate used is determined on the basis of the market yields recorded at the valuation dates of primary company bonds, taking into account the average residual duration of the liability. The present value of the obligation at the balance sheet date is also adjusted for the fair value of any assets servicing the plan.

Actuarial gains and losses (i.e. changes in the present value of the obligation arising from changes in actuarial assumptions and adjustments based on past experience) are recognised in the statement of comprehensive income.

Provisions for risks and charges in respect of commitments and guarantees given

The sub-item of provisions for risks and charges in question includes provisions for credit risk recognised under commitments to disburse funds and guarantees issued that fall within the scope of application of rules on impairment in accordance with IFRS 9. For these cases, the same methods of allocation for the three stages (credit risk stages) are adopted in principle, as is the calculation of the expected loss incurred with reference to financial assets measured at amortised cost or at fair value with an impact on comprehensive income.

The aggregate also includes provisions for risks and charges for other types of commitments and guarantees given which, by virtue of their specific nature, do not fall within the aforementioned scope of application of impairment under IFRS 9.

Other provisions

Other provisions for risks and charges include provisions relating to legal obligations or employment relationships or disputes, including tax disputes, arising from a past event for which it is probable that financial resources will be disbursed to meet the obligations, provided that a reliable estimate of the relative amount can be made.

Accordingly, provision is recognised if, and only if:

- there is a current obligation (legal or implicit) as a result of a past event;
- it is likely that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- a reliable estimate can be made of the amount arising from fulfilment of the obligation.

The amount recognised as a provision is the best estimate of the expenditure required to settle the obligation at the balance sheet date and reflects the risks and uncertainties that inevitably surround various events and circumstances. Where the time element is significant, provisions are discounted using current market rates. Provisions and increases due to the time factor are recognised in the income statement.

A provision released when it becomes unlikely that resources capable of yielding economic benefits will be expended in order to discharge the obligation, or when the obligation is extinguished.

The item also includes long-term employee benefits, the charges for which are determined using the same actuarial criteria as those described in the provision for pensions. Actuarial gains and losses are all recognised immediately in the income statement.

Financial liabilities measured at amortised cost

Classification criteria

Amounts due to banks, amounts due to customers and debt securities issued include various forms of interbank funding and with customers, repurchase agreements with an obligation to repurchase, and funding through certificates of deposit, bonds and other debt securities issued, net of any amounts repurchased.

Payables entered by the company as lessee in the context of leasing transactions are also included.

Recognition criteria

Such financial liabilities are initially recognised on the date on which the contract is signed, which normally coincides with the moment of receipt of the sums collected or the issue of debt securities.

Initial recognition is based on the fair value of the liabilities, normally equal to the amount received or the issue price, plus any additional costs/income directly attributable to the individual funding or issue transaction. Internal administrative costs are excluded.

Valuation criteria

After initial recognition, financial liabilities are measured at amortised cost according to the effective interest method.

An exception is made for short-term liabilities, for which the time factor is negligible and which are recognised at the value received.

Lease payables are revalued when there is a lease modification (e.g. a change in the scope of the contract), which is not recognised/considered as a separate contract.

Cancellation criteria

Financial liabilities are derecognised when they expire or are discharged. Cancellation can also take place when previously issued bonds are repurchased. The difference between the book value of the liability and the amount paid to purchase it is recorded in the Income Statement.

The placing on the market of own securities after their repurchase is regarded as a new issue and is recognised at the new placement price.

Financial liabilities held for trading

Recognition criteria

The financial instruments in question are recorded at the subscription date or the issue date at a value equal to the fair value of the instrument, without considering any transaction costs or revenues directly attributable to the instruments themselves.

This category of liabilities includes derivative trading contracts with negative fair value, as well as embedded derivatives with negative fair value present in - but not strictly related to - complex contracts in which the primary contract is a financial liability. The category also includes liabilities arising from technical overdrafts generated by trading in securities and certificates.

Valuation criteria

All trading liabilities are measured at fair value with the result of the valuation recognised in the income statement.

Cancellation criteria

Financial liabilities held for trading are derecognised when the contractual rights to the related cash flows expire or when the financial liability is transferred with the substantial transfer of all the risks and rewards of ownership.

Financial liabilities designated at fair value

Classification criteria

This item consists of financial liabilities designated at fair value with a balancing entry in the income statement, on the basis of the option granted to companies (known as the "fair value option") under IFRS 9 and in accordance with the provisions of the relevant legislation.

Recognition criteria

These liabilities are recognised on the issue date and at their fair value, including the value of any embedded derivative and net of the placement fees paid.

Valuation criteria

These liabilities are measured at fair value and the results is recognised according to the following rules set out in IFRS 9:

- changes in fair value that are attributable to a change in its creditworthiness must be recognised in statement of comprehensive income (shareholders' equity);
- the remaining changes in fair value must be recognised in the income statement.

The amounts recognised in the statement of comprehensive income are not subsequently reclassified to the income statement. This method of accounting is not to be applied when the recognition of the effects of one's creditworthiness under shareholders' equity leads to or accentuates an accounting mismatch in the income statement. In this case, gains or losses related to the liability, including those determined as the effect of a change in the creditworthiness of the entity, must be recognised in the income statement.

Cancellation criteria

Financial liabilities measured at fair value are derecognised when the contractual rights to the related cash flows expire or when the financial liability is transferred with the substantial transfer of all the risks and rewards of ownership.

Foreign currency transactions

Initial recognition criteria

Foreign currency transactions are recorded, at the time of initial recognition, in the reporting currency, by applying the exchange rate applicable on the transaction date to the amount in foreign currency.

Subsequent recognition criteria

At each balance sheet or interim reporting date, foreign currency balance sheet items are valued as follows:

- monetary items are converted at the exchange rate on the closing date;
- non-monetary items valued at historical cost are converted at the exchange rate prevailing at the date of the transaction;
- non-monetary items measured at fair value are converted using the exchange rates in place at the closing date.

Exchange differences arising from the settlement of monetary items or the conversion of monetary items at rates other than the initial conversion rates, or the conversion rate of the previous financial statements, are recognised in the income statement for the period in which they arise.

When a gain or loss on a non-monetary item is recognised in shareholders' equity, the exchange difference relating to that item is also recognised in shareholders' equity. Conversely, when a gain or loss is recognised in the income statement, the relevant exchange rate difference is also recognised in the income statement.

Other information

Treasury shares

Any treasury shares held are deducted from shareholders' equity. Similarly, their original cost and the gains or losses arising from their subsequent sale are recognised as changes in equity.

Prepayments and accrued income

Accrued income and prepaid expenses that include expenses and income accrued during the period on assets and liabilities are recorded in the financial statements as an adjustment to the assets and liabilities to which they refer.

Leasehold improvements expenses

The costs of renovating non-owned properties are capitalised in view of the fact that for the duration of the lease agreement, the user company controls the assets and may derive future economic benefits from them. These costs, classified under 'other assets' in accordance with the Instructions issued by the Bank of Italy, are amortised for a period not exceeding the term of the lease agreement.

Employee severance indemnities

The provision for employee severance indemnities is classified as a "post-employment benefit" consisting of:

- a "defined-contribution plan" for employee severance indemnities accruing as of 1 January 2007 (the date of entry into force of the supplementary pension reform pursuant to Legislative Decree 252 of 5 December 2005), both in the case of an employee who opts for a supplementary pension scheme or in the case of allocation to the treasury fund at the Italian National Social Welfare Institution (INPS). For these indemnity payments, the amount recognised under personnel costs is determined on the basis of the contributions due without the application of actuarial calculation methods;
- the "defined-benefit plan" item is therefore recognised on the basis of its actuarial value determined using the "Projected Unit Credit" method, for the portion of staff termination benefits accrued up to 31 December 2006.

These indemnities are recognised on the basis of their actuarial value determined using the Projected Unit Credit method, without pro-rata application of the service provided, as the current service cost of the employee severance indemnity has almost entirely matured and its revaluation, for the coming years, is not considered to result in significant employee benefits.

For the purposes of discounting, the rate used is determined by reference to the market yields on bonds of leading companies taking into account the average remaining maturity of the liability, weighted according to the percentage of the amount paid and advanced, for each maturity, from the total to be paid and until the final extinction of the entire obligation.

Costs for service of the plan are recognised under personnel costs, while actuarial gains and losses are recognised in the statement of comprehensive income.

Share-based payments

Employee remuneration plans based on shares are recorded in the income statement, with a corresponding increase in shareholders' equity, on the basis of the fair value of the financial instruments assigned at the assignment date, dividing the cost over the period envisaged by the plan.

In the presence of options, their fair value is calculated using a model that considers, in addition to information such as the exercise price and the life of the option, the current price of the shares and their expected volatility, the expected dividends and the risk-free interest rate, as well as the specific characteristics of the existing plan. In the valuation model, the option and the probability of achieving the conditions on the basis of which the options were assigned are assessed separately.

The combination of the two values provides the fair value of the assigned instrument.

Any reduction in the number of financial instruments assigned is accounted for as the cancellation of a part of those instruments.

Employee benefits

Employee benefits are defined as all types of remuneration paid by the company in exchange for the work performed by employees. Employee benefits are divided into:

- short-term benefits (other than the benefits due to employees for termination of employment and salary benefits in the form of equity participation), that are expected to be fully paid up within twelve months of the end of the year in which employees rendered their employment and that are recognised entirely in the income statement at the time of vesting (this category includes, for example, wages, salaries and "extraordinary" benefits);
- post-employment benefits due after termination of the employment relationship that the company is obliged to pay its employees in the future. These include employee severance benefits and pension funds, which in turn are divided into defined-contribution plans and defined-benefit plans, or company pension funds;
- severance benefits, i.e. the compensation that the company grants to employees in return for their employment, following their decision to terminate their employment before the normal retirement date;
- long-term benefits, other than those indicated above, that are not expected to be fully extinguished within the twelve months following the financial year in which the employees performed their work.

Recognition of revenues and costs

Revenues may be recognised:

- at a specific time, when the entity fulfils its obligation to do so by transferring the promised good or service to the customer, or
- over time, as the entity fulfils its obligation to do so by transferring the promised good or service to the customer.

The asset is transferred when, or during the period in which, the customer acquires control of it. In particular:

- interest payments are recognised *pro rata temporis* on the basis of the contractual interest rate or the effective interest rate if the amortised cost is applied. Interest income (or interest expense) also includes differentials or margins, positive (or negative), accrued up to the balance sheet date, relating to financial

derivative contracts; i) hedging of assets and liabilities that generate interest; ii) classified in the balance sheet in the trading portfolio, but linked to financial assets and/or liabilities measured at fair value (fair value option); iii) linked to assets and liabilities classified in the trading portfolio that require the settlement of differentials or margins at more than one maturity;

- default interest, which may be provided for by contract, is only recognised in the income statement when actually collected;
- dividends are recognised in the income statement in the year in which their distribution is resolved;
- commissions for revenues from services are recorded, on the basis of the existence of contractual agreements, in the period in which the services were provided. Commissions considered at amortised cost for the purposes of calculating the effective interest rate are recognised as interest;
- revenues from the sale of financial instruments, determined by the difference between the consideration paid or received for the transaction and the fair value of the instrument, are recognised in the income statement when the transaction is recognised;
- gains and losses arising from trading in financial instruments are recognised in the income statement at the time of completion of the sale, based on the difference between the consideration paid or received and the book value of the instruments;
- revenues from the sale of non-financial assets are recognised at the time of finalisation of the sale, or when the obligation to perform vis-à-vis the client has been fulfilled.

Costs are recognised in the income statement on an accruals basis. The costs of obtaining and complying with contracts with customers are recognised in the income statement in the periods in which the relevant revenues are recognised.

Use of estimates and assumptions in financial reporting

Financial reporting requires the use of estimates and assumptions that may have significant effects on the values recognised in the balance sheet and the income statement, and on information on contingent assets and liabilities disclosed in the financial statements.

The production of such estimates involves the use of the available information and the adoption of subjective assessments, also based on historical experience, used to make reasonable assumptions for the recognition of operating events. By their nature, the estimates and assumptions used may vary from one year to the next and, therefore, it cannot be excluded that in subsequent years the values recognised in the financial statements may also vary significantly as a result of changes in the subjective assessments used.

The main situations in which management is required to make subjective assessments include:

- quantification of the impairment losses on loans, equity investments and, in general, other financial assets;
- the use of valuation models to recognise the fair value of financial instruments not listed on active markets;
- assessment the appropriateness of the value of goodwill and other intangible assets;
- the quantification of the *fair value* of real properties and of valuable artistic heritage;
- quantification of provisions for personnel and for risks and charges;
- estimates and assumptions regarding the recoverability of deferred tax assets;
- the demographic (linked to the prospective mortality of the insured population) and financial (deriving from the possible evolution of the financial markets) assumptions used in structuring the insurance products and in defining the bases for calculating the supplementary reserves.

For some of the cases listed above, the main factors that are estimated and that therefore contribute to determining the book value of assets and liabilities may be identified. Without claiming to be exhaustive, it should be noted that:

- in order to determine the fair value of financial instruments not listed on active markets, if it is necessary to use parameters that cannot be inferred from the market, the main estimates concern, on the one hand, the evolution of future financial flows (or even income flows, in the case of shares), possibly contingent on future events and, on the other hand, the level of certain input parameters not listed on active markets;
- for the allocation to the three credit risk stages provided for in IFRS 9 of loans and debt securities classified among financial assets at amortised cost and financial assets at fair value , with an impact on total profitability and the calculation of the relative expected losses, the main estimates refer to:
  a) the determination of the parameters for a significant increase in credit risk, based essentially on models for measuring the probability of default (PD) at the origination of financial assets and at the reporting date;
  b) the inclusion of forward looking factors, including macroeconomic factors, for the determination of PD and LGD;
  c) the determination of the probability of the sale of non-performing financial assets, through the realisation of positions on the market;
- for the determination of the estimates of future cash flows from non-performing loans, certain factors are taken into account: expected recovery times, certain elements are taken into consideration: the expected recovery time, the estimated realisable value of any guarantees, as well as the costs that are expected to be incurred for the recovery of the credit exposure;
- to determine the value in use of intangible assets with an indefinite useful life (goodwill, brand name, etc.) in relation to the Cash Generating Unit (CGU), future cash flows in the analytical forecast period and the flows used to determine the terminal value generated by the CGU are estimated separately and appropriately discounted. The cost of capital is included among the items assessed;
- to determine the value in use of intangible assets with a finite life (asset management and insurance portfolios) in relation to Cash Generating Units (CGUs), the useful life is assessed, on the one hand, and the future cash flows from the assets, on the other. In the case of intangible assets with a finite useful life, the cost of capital is also included in the estimates;
- the determination of the fair value of real properties and valuable artistic heritage is made through specific appraisals by qualified, independent companies or internal experts. For appraisals of real properties, rents, sale prices, discount and capitalisation rates were estimated, while for the appraisals of valuable artistic heritage, the estimated value was derived from the trend in prices of similar works (by technique, size, subject) of the same author, or of schools and regional movements comparable in style and technique;
- for the quantification of provisions for pensions and similar obligations, the present value of the obligations is assessed, taking into account the flows, appropriately discounted, arising from statistical historical analyses, and the demographic curve;
- for the quantification of provisions for risks and charges, the amount of the disbursements necessary to fulfil the obligations is estimated, where possible, taking into account the actual probability of having to invest resources;
- for the determination of the items relating to deferred taxation, the probability of actual future tax liability (taxable temporary differences) is estimated, and the degree of reasonable certainty – if any – of future taxable amounts at the time tax deductibility becomes apparent (deductible temporary differences).

Classification criteria for financial assets

The classification of financial assets into the three categories provided for in IFRS 9 depends on two criteria, or drivers: i) the business model under which the financial instruments (or the Business Model) are managed, and ii) the contractual characteristics of the cash flows of financial assets (or SPPI Test).

The combined provisions of the two drivers give rise to the classification of financial activities, as indicated below:

- Financial assets measured at amortised cost: assets that pass the SPPI test and come within the hold to collect (HTC) business model;
- Financial assets measured at fair value with an impact on comprehensive income (FVOCI): assets that pass the SPPI test and come within the 'Hold to collect and sell' (HTCS) business model;
- Financial assets measured at fair value through profit or loss (FVTPL): this is a residual category that includes financial instruments that are not classifiable in the previous categories on the basis of the business model test or the test on the characteristics of contractual flows (SPPI test not passed).

SPPI test

In order for a financial asset to be classified at amortised cost or at FVOCI - in addition to an analysis of the business model - the contractual terms of the asset must provide, on certain dates, for cash flows represented solely by payments of capital and interest on the principal amount to be repaid ("solely payment of principal and interest" - SPPI). This analysis must be conducted, in particular, for loans and debt securities.

The SPPI test must be conducted on each individual financial instrument when recorded in balance sheet.

After initial recognition, and as long as it is recognised in the financial statements, the asset is no longer subject to new valuations for the purposes of the SPPI test. If a financial instrument is derecognised and a new financial asset is recognised, the SPPI test must be performed on the new asset.

The following definitions apply to the application of the SPPI test:

- Capital: the fair value of the financial asset at the time of initial recognition. This value may change during the life of the financial instrument, for example as a result of repayments of part of the principal;
- Interest: this is the consideration for the time value of the money and for the credit risk associated with the outstanding capital over particular period of time. It may also include remuneration for other risks and basic costs associated with lending and a profit margin.

When assessing whether the contractual flows of a financial asset can be defined as the SPPI, IFRS 9 refers to the general concept of a "basic lending arrangement", which is independent of the legal form of the asset. When the contractual clauses introduce exposure to risks or volatility of contractual cash flows not consistent with the definition of basic lending arrangement, such as exposure to changes in the share or commodity prices, the contractual flows do not meet the SPPI definition. The application of the classification driver based on contractual cash flows sometimes requires subjective judgment and, therefore, the definition of internal application policies.

Where the time value of the money is modified ("modified time value of money") – for example when the interest rate of the financial asset is periodically re-determined, but the frequency of the redetermination or frequency of coupon payments does not reflect the nature of the interest rate (e.g. the interest rate is revised monthly on the basis of a one-year rate) or when the interest rate is periodically redetermined on the basis of an average of particular short or medium-long-term rates – an assessment is made, using both quantitative and qualitative elements, of whether the contractual flows still meet the definition of SPPI (a so-called 'benchmark cash flows test'). If the test shows that the contractual cash flows (not discounted) are "significantly different" to the cash flows (also not discounted) of a benchmark instrument (i.e. without the

modified time value element), the contractual cash flows cannot be considered as meeting the definition of SPPI.

Special analyses (known as a "look through test") are required by the standard and are therefore also implemented for multiple contractually linked instruments (CLIs) that create concentrations of credit risk for debt servicing and for non-recourse assets, for example in cases where the credit claim can be asserted only in relation to certain debtor assets, or the cash flows deriving from certain assets.

The presence of contractual clauses that may change the frequency or amount of contractual cash flows must also be considered in order to assess whether such flows meet the requirements to be considered PSPIs (e.g. prepayment options, possibility of deferring contractually established cash flows, instruments with embedded derivatives, subordinated instruments, etc.).

However, as required by IFRS 9, a characteristic of contractual cash flows does not affect the classification of the financial asset if it can only have a 'de minimis' effect on the contractual cash flows of the financial asset (in each period and cumulatively). Similarly, if a characteristic of cash flows is not realistic ("not genuine"), that is, if it only affects the contractual cash flows of the instrument when an extremely rare, very unusual, and very unlikely event occurs, it does not affect the classification of the financial asset.

To conduct the SPPI test, the company avails itself of the services provided by well-known info-providers for transactions in debt securities.

A tool based on an internally developed methodology (decision trees) has been developed for the SPPI test in the context of credit processes. In particular, given the significant different characteristics, provision is made for differentiated management for products attributable to a contractual standard (a typically retail loan portfolio) and for "tailor made" loans (typically a corporate loan portfolio).

For standard products, the SPPI test is performed when structuring the contractual standard and the outcome of the test is extended to all the individual accounts attributable to the same product. For "tailor made" products, the SPPI test is conducted for each new credit line/relationship submitted to the decision-making body through the use of the proprietary tool.

Business model

With regard to the business model, IFRS 9 identifies three cases in relation to the way in which cash flows and sales of financial assets are managed:

- Hold to Collect (HTC): this is a business model whose objective is achieved by collecting the contractual cash flows of the financial assets included in the portfolios associated with it. The inclusion of a portfolio of financial assets in this business model does not necessarily mean that it is impossible to sell the instruments, although it is necessary to consider the frequency, value and timing of sales in previous years, the reasons for sales, and expectations for future sales;
- Hold to Collect and Sell (HTCS): this is a mixed business model, the objective of which is achieved both through the collection of contractual cash flows of financial assets in the portfolio and through a sales activity that is an integral part of the strategy. Both activities (collection of contractual flows and sales) serve the purpose of the business model. Consequently, sales are more frequent and significant than a HTC business model and are an integral part of the strategies pursued;
- Others/Trading: this category includes both financial assets held for trading purposes and financial assets managed according to a business model not attributable to the previous categories (Hold to Collect and Hold to Collect and Sell). This classification generally applies to a portfolio of financial assets whose management and performance are valued on the basis of fair value.

The business model reflects the ways in which financial assets are managed to generate cash flows for the benefit of the entity and is defined by top management through the appropriate involvement of the business structures.

The business model is observed by considering the method of managing financial assets and, as a result, the extent to which the portfolio's cash flows result from the collection of contractual flows, from the sale of financial assets, or from both these assets. Evaluation is not based on scenarios which, according to the entity's reasonable forecasts, are not likely to occur, such as "worst case" or "stress case" scenarios. For example, if the entity expects to sell a certain portfolio of financial assets only in a "stress case" scenario, that scenario does not affect the assessment of the entity's business model for such assets if that scenario, based on the entity's reasonable forecasts, is not expected to occur.

The business model does not depend on the intentions that management has with respect to a single financial instrument, but rather on the ways in which financial groups are managed to achieve a given business objective.

In summary, the business model:

- Reflects the way financial assets are managed to generate cash flows;
- is defined by top management, through the appropriate involvement of business structures;
- must be observable in view of the way the financial assets are managed.

In operational terms, the "assessment" of the business model is conducted in accordance with the company's organisation, the specialisation of its business functions, the risk model, and the allocation of delegated powers (limits).

With regard to the management intentions behind holding financial assets, it should be noted that a specific document – approved at the competent governance levels – defines and sets out the constituent elements of the business model in relation to the financial assets included in the portfolios managed when undertaking operations on business structures.

For hold-to-collect portfolios, the company has defined the eligibility thresholds for sales that do not affect the classification (frequent but not significant, individually and in aggregate, or infrequent even if of significant amount) and, at the same time, the parameters have been established to identify sales consistent with this business model, as they are attributable to an increase in credit risk.

More specifically, within a HTC business model, sales are permitted:

- in the event of an increase in credit risk, which takes place:
    a) for securities, when there is a downgrade of predetermined notches compared to the origination rating. The approach adopted provides that the number of notches is differentiated according to the origination rating, in accordance with the methodology in use to identify the "significant deterioration", i.e. for staging transition;
    b) for loans, in the case of non-performing loans or loans classified in stage 2;
- when they are frequent but not significant in value or occasional even if significant in value. In order to determine these aspects, frequency and significance thresholds have been defined::
    a) the frequency is defined as the percentage ratio between the number of sold positions (ISINs or ratios) during the observation period and the total positions in the portfolio during the observation period;
    b) "significance" is defined as the percentage ratio between the nominal value of sales and the total nominal value of the instruments in portfolio in the period under review.

In cases where both frequency and significance thresholds are exceeded simultaneously, a further assessment is provided in order to confirm the consistency of the HTC business model (for example, to assess whether sales are made close to maturity).

Methods of determining amortised cost

The amortised cost of a financial asset or financial liability is the value at which the financial asset or liability is measured, at initial recognition, net of principal repayments, plus or minus the aggregate amortisation, calculated using the effective interest method, of the difference between the initial value and the value at maturity and net of any loss in value.

The effective interest rate is the rate that equals the present value of a financial asset or financial liability to the contractual flow of future payments in cash or received until maturity or the next date of price recalculation. To calculate present value, the effective interest rate is applied to the flow of future cash receipts or payments over the entire useful life of the financial asset or financial liability or for a shorter period under certain conditions (e.g. revision of market rates).

After initial recognition, the amortised cost makes it possible to allocate revenues and costs deducted from or increased by the instrument over its expected life through the amortisation process. Amortised cost is determined differently depending on whether the financial asset or financial liability to be measured is fixed or variable rate and, in the latter case, whether or not the variability of the rate is known in advance. For instruments with fixed rates or fixed rates by time bands, future cash flows are quantified according to the known interest rate (single or variable) over the life of the loan. For variable-rate financial assets/liabilities, the variability of which is not known in advance (for example, because it is linked to an index), cash flows are determined at the most recent known rate. At each rate revision date, the amortisation plan and effective interest rate are recalculated over the entire useful life of the instrument, i.e. up to its maturity date. The adjustment is recognised as a cost or income in the income statement.

Measurement at amortised cost is performed for financial assets measured at amortised cost and for those measured at fair value with an impact on comprehensive income, as well as for financial liabilities measured at amortised cost.

Financial assets and liabilities traded at market conditions are initially recognised at fair value, which normally corresponds to the inclusive amount disbursed or paid which, since they are instruments valued at amortised cost, directly attributable transaction costs and commissions.

Transaction costs are marginal internal or external costs and income attributable to the issue, acquisition or disposal of a financial instrument and not chargeable back to the customer. These commissions, which must be directly attributable to the individual financial asset or liability, affect the original effective yield and make the effective interest rate associated with the transaction different from the contractual interest rate.

Costs/income relating indistinctly to several transactions and components related to events that may occur during the life of the financial instrument, but which are not certain at the time of the initial definition, such as, for example: commissions for retrocession, for non-use, for early repayment, are excluded. Moreover, the amortised cost does not include costs that the company would have to bear independently of the transaction (e.g. administrative, office, communication costs), those that, although specifically attributable to the transaction, fall within the normal practice of managing the loan (e.g. activities for the disbursement of the credit), as well as commissions for services collected following the performance of Structured Finance activities that would have been collected independently of the subsequent financing of the transaction (such as, for example, facility and arrangement commissions).

With particular reference to loans, the following are considered costs attributable to the financial instrument: commissions paid to distribution channels, fees paid for consultancy/assistance with the organisation of and/or participation in syndicated loans and, finally, up-front commissions related to loans granted at rates higher than market rates. Revenues considered in the calculation of the amortised cost are up-front commissions related to loans granted at rates lower than market rates, unlike those for participation in syndicated transactions and brokerage commissions linked to commissions paid by brokerage firms.

In the case of securities not measured at fair value through profit or loss, transaction costs are considered to be commissions for broker agreements operating on Italian equity markets, those paid to brokers operating on foreign equity and bond markets defined on the basis of commission tables. Stamps are not regarded as attracting amortised cost as they are insignificant.

For issued securities, commission on the placement of bonds paid to third parties, shares paid to stock exchanges and fees paid to auditors for work performed for each individual issue are considered in the calculation of the amortised cost, while commission paid to rating agencies, legal and advisory/revision fees for the annual updating of prospectuses, costs for the use of indices, and commission arising during the life of the issued bond are not regarded as attracting amortised cost.

Amortised cost also applies to the valuation of the loss in value of the financial instruments listed above and to the recognition of those issued or purchased at a value other than their fair value. The latter are recorded at fair value, rather than for the amount received or paid, calculated by discounting future cash flows at a rate equal to the effective rate of return of similar instruments (in terms of creditworthiness, contractual maturities, currency, etc.), with simultaneous recognition in the income statement of a financial charge or income. After initial valuation, they are valued at amortised cost, with effective interest greater or lesser than nominal interest. Finally, structured liabilities that are not measured at fair value are also measured at amortised cost and recognised in the income statement because the derivative contract embedded in the financial instrument has been separated and recognised separately.

As indicated by IFRS 9, in some cases a financial asset is considered to be impaired at the time of initial recognition because the credit risk is very high and, in the case of purchase, it is purchased with large discounts (compared to the initial disbursement value). If the financial assets in question, based on the application of the classification drivers (i.e. SPPI test and Business model), are classified as assets valued at amortised cost or fair value with an impact on other comprehensive income, they are classified as "Purchased or Originated Credit Impaired Asset" (hereinafter "POCI") and are subject to specific treatment with regard to the impairment process. In addition, on financial assets classified as POCI, a "credit-adjusted effective interest rate" is calculated at the date of initial recognition, the identification of which requires the inclusion of initial expected losses in cash flow estimates. Therefore, for the application of amortised cost and the consequent calculation of interest, this effective interest rate adjusted for the loan applies.

Hedged financial assets and financial liabilities are not measured at amortised cost. Changes in fair value relating to the hedged risk are recognised in the income statement. However, the financial instrument is revalued at amortised cost if the hedge ceases to exist, at which point the previously recorded changes in fair value are amortised, calculating a new effective interest rate of return that considers the value of the loan adjusted by the fair value of the part subject to the hedge, until the expiry of the hedge originally envisaged. Moreover, as indicated in the paragraphs concerning financial assets and liabilities valued at amortised cost, the valuation at amortised cost does not apply to financial assets/liabilities if their short duration makes the economic effect of discounting negligible, nor to receivables without a defined maturity, or that have been revoked.

Methods of determining impairment losses

Impairment of financial assets

At each reporting date, pursuant to IFRS 9, financial assets other than those measured at fair value through profit or loss are assessed to determine whether there is evidence that the book value of such assets may not be fully recoverable. A similar analysis is also conducted for commitments to disburse funds and for the guarantees issued that are subject to impairment under IFRS 9.

If such evidence exists ("evidence of impairment"), the financial assets in question - in conjunction with all other assets belonging to the same counterparty, if any such assets exist - are considered impaired and are included in stage 3. Such exposures, consisting of financial assets classified - in accordance with the provisions of Bank of Italy Circular no. 262/2005 - among the categories of non-performing loans, probable default, and exposures outstanding for more than ninety days, must be subject to value adjustments that are equal to the expected losses relating to their entire residual life.

Impairment of performing financial assets

For financial assets for which there is no evidence of impairment (non-impaired financial instruments), it must be verified whether there are indicators that the credit risk of the individual transaction is significantly increased compared to the time of initial recognition. The consequences of this verification, from the standpoint of classification (or, more properly, staging) and assessment, are as follows:

- where such indicators exist, financial asset feeds into stage 2. In such cases, the valuation, in accordance with the international accounting standards and even in the absence of a manifest loss of value, provides for the recognition of value adjustments equal to the expected losses over the entire residual life of the financial instrument. These adjustments are reviewed at each subsequent reporting date in order to periodically verify consistency with the constantly updated loss estimates and to take into account - in the event that the indicators of a "significantly increased" credit risk are no longer available - the changed forecast period for calculating the expected loss;
- where no such indicators exist, financial asset is transferred to stage 1. In this case, the valuation, in accordance with the provisions of international accounting standards, and although there is no manifest impairment, provides for the recognition of expected losses, for the specific financial instrument, over the following twelve months. These adjustments are reviewed at each subsequent balance sheet date in order to periodically verify consistency with the constantly updated loss estimates and to take into account - in the event of indicators of a "significantly increased" credit risk - the changed forecast period for calculating the expected loss.

With regard to the valuation of financial assets and, in particular, to the identification of a "significant increase" in credit risk (a necessary and sufficient condition for the classification of the asset being valued at stage 2), the factors that - in accordance with the principle and its operating declination by the company - constitute the main determinants to be taken into account are as follows:

- the change in the probability of lifetime default with respect to initial recognition of the financial instrument. This is therefore an assessment carried out using a "relative" criterion, which qualifies as the main driver;
- the possible presence of an overdue one that – without prejudice to the "significance" thresholds identified by the regulations – have been so for at least 30 days. In other words, in such cases the exposure's credit risk is presumed to have "increased significantly", resulting in "transfer" to stage 2 (if the exposure was previously included in stage 1);
- the possible presence of forbearance measures, which - again on a presumption basis - entail the classification of exposures among those whose credit risk is "significantly increased" with respect to initial recognition;
- any "observation" database notes that qualify exposures as being on a "Watchlist" or those whose credit risk is "significantly increased" compared what was indicated at initial recognition.

The significant increase in credit risk ("SICR"), measured by the change in probability of default on the lifetime, is calculated by comparing the relative change in probability of default on the lifetime recorded between the date of initial recognition of the relationship and that of observation (Delta PD Lifetime) with predetermined thresholds of significance. The attribution of a PD Lifetime to each relationship is made by re-registering the ratings for each segment both on the date of initial recognition and on observation. Ratings are determined on the basis of internal models, where available, or management models.

This "relative" change in PD is an indicator of the increase or decrease in credit risk observed during the reference period. In order to establish whether, pursuant to IFRS 9, any increase in credit risk can be considered "significant" (and therefore involve a passage between stages), it is necessary to define specific thresholds. Lifetime PD increases below these thresholds are not considered significant and, consequently, do not involve the transfer of individual lines of credit/debt tranches from stage 1 to stage 2; such a transfer is, however, necessary in the presence of relative PD increases above the thresholds in question. The

thresholds used were estimated on the basis of a process of simulations and optimisation of predictive performance, developed using historical granular portfolio data. Specific thresholds are established for Private, Small Business and Corporate models.

The determination of thresholds was calibrated in order to find a correct balance between the performance indicators relating to the capacity of the thresholds to:

- Intercept stage 2 positions before they move to default;
- Identify positions for which reverting to stage 1 is synonymous with an effective improvement in creditworthiness.

Some specific considerations apply to the so-called "staging" of securities. Unlike receivables, for this type of exposure, buying and selling operations subsequent to the first purchase (performed with reference to the same ISIN) can usually fall within the ordinary activity of managing positions (with the consequent need to identify a methodology to be adopted for the identification of sales and repayments in order to determine the residual quantities of individual transactions to which to associate a credit quality/rating to the origination, to be compared with that of the reporting date). In this context, it was considered that the use of the "first-in-first-out" or "FIFO" method (for the repayment to the income statement of the ECL recorded, in the case of sales and redemptions) contributes to more transparent portfolio management, including from the point of view of front office operators, while at the same time enabling continuous updating of the creditworthiness assessment on the basis of new purchases.

Once the allocation of exposures in the various stages of credit risk has been defined, expected losses (ECL) are determined at the level of an individual security transaction or tranche, based on the Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD) parameters, on which appropriate corrective measures are taken to ensure compliance with the specific requirements of IFRS 9.

The following definitions apply to PD, LGD and EAD:

- PD (Probability of Default): probability of migrating from performing to impaired credit status over a one-year time horizon. In models consistent with supervisory requirements, the PD factor is typically quantified through the rating. PD values derive from the internal rating model where available, supplemented by external ratings or average segment/portfolio data;
- LGD (Loss Given Default): the percentage of loss in the event of default, quantified through the historical experience of recoveries discounted to present value on cases that have been transferred to impaired loans;
- Exposure At Default (EAD) or credit equivalent: the amount of exposure at the time of default.

With regard to multi-period EAD, in line with the provisions of IFRS 9, reference is made to amortised cost plans for both receivables and debt securities, regardless of the relevant valuation methods (amortised cost or fair value with an impact on comprehensive income). For commitments to disburse funds (margins), the EAD is, on the other hand, assumed to be the weighted nominal value for a specific Credit Conversion Factor (CCF).

The valuation of financial assets also reflects the best estimate of the effects of future conditions, especially economic conditions, on the basis of which the forward-looking PD and LGD are conditioned. In IFRS 9, including on the basis of the instructions of international regulators, information on the future macroeconomic scenarios in which the company may find itself operating, and which influence the situation of borrowers with regard to both the "risk" of migration of exposures to lower quality classes (therefore concerning "staging") and recoverable amounts (therefore concerning the determination of expected losses on exposures) are of particular importance. The macroeconomic scenario is obtained from external information providers. Alternative improvement and worsening scenarios are determined by stressing input variables in forecasting models.

Impairment of non-performing financial assets

Impaired loans classified as non-performing are subject to the following valuation methods:

- analytical-statistical assessment, which is adopted for exposures below certain thresholds, based on the application of specific LGD grids, to which an Add-On may be added in order to take account of "forward looking" information, in particular information on the impact of future macroeconomic scenarios;
- analytical-specific valuation, which is adopted for customers with exposures above certain thresholds and is based on the depreciation percentages attributed by the manager, following specific analysis and valuation processes, to which an Add-On component can be added in order to take account of "forward looking" information, in particular that relating to the impacts of future macroeconomic scenarios (with the exception of non-performing loans with mortgage guarantees, for which the impacts of future scenarios are included through the methods of determining the "haircuts" at the value of the properties under warranty);
- inclusion of sales scenarios for assignable non-performing loans: regardless of the subdivision of such exposures between those subject to analytical-statistical assessment and those subject to analytical-specific assessment (as identified above), the valuation of assignable non-performing loans also includes the additional components relating to future sales scenarios.

The assessment of “unlikely to pay” (UTP) defaults is also based on two different approaches:

- analytical-statistical assessment, for cash exposures below certain thresholds, based on the application of specific LGD statistical grids to which a component of Add-On is added in order to understand the impacts of future macroeconomic scenarios;
- analytical-specific assessment, for cash exposures above certain thresholds, based on the devaluation percentages attributed by the operator, plus an add-on component in order to take into account, in this case also, of the impact of future macroeconomic scenarios.

Non-performing loans classified and/or in excess of limits are subject to analytical valuation on statistical bases regardless of the amount of cash exposure. Here also, the adjustment defined on the basis of LGD statistical grids is supplemented to take account of the Add-On component attributable to the effect of future macroeconomic scenarios.

With reference to alternative recovery scenarios, the company, in relation to the objective of reducing the stock of non-performing loans, including in business plans, and its commitments to supervisory bodies, with specific reference to the NPL Strategy, considers the sale of certain portfolios as a strategy that can, under certain conditions, maximise the recovery of cash flows, in consideration of recovery times.

In particular, in its document published by the SSM entitled “Guidance on the management of non-performing loans for Italy’s ‘less significant institutions’” the Bank of Italy asked the banks to define a strategy designed to progressively reduce non-performing loans.

In addition to these initial instructions, further regulatory developments, including the measures introduced by the European Union in the first part of the year to reduce the risks associated with non-performing loans, aimed at determining minimum prudential provisioning levels for non-performing loans, the strategy of reducing the aggregates through internal work-out necessarily had to be strengthened and accompanied by other more effective measures through the sale of a significant portfolio of non-performing loans.

Consequently, the “ordinary” scenario, which assumes a recovery strategy based on the collection of the receivable typically through legal actions, mandates to recovery companies and the enforcement of mortgage guarantees, was accompanied - as a recovery strategy - by the scenario of the sale of the receivable itself. In the light of this development, for a defined perimeter of saleable non-performing loans, in order to determine the overall expected loss of the exposures, the recoverable values based on the ordinary internal recovery process and the amounts recoverable from the sale, estimated on the basis of market valuations, were weighted according to the share of the portfolio destined for sale, as envisaged by the NPL strategy, with respect to the total of the saleable portfolio.

In particular, the recoverable value of saleable non-performing loans was quantified as the average value between (i) its "fair value" in the event of sale and (ii) its value in the event of recovery through an internal work-out - its "value in the event of collection".

It should be noted that the "value in the event of collection" was determined according to the ordinary logic applied for impairment of non-performing loans, i.e. on the basis of an analytical assessment of exposures in excess of a defined threshold and on the basis of an analytical/statistical assessment for other exposures.

As mentioned above, it should also be noted that purchased or originated financial assets (POCI) have particular characteristics in terms of impairment. In this regard, value adjustments equal to the ECL lifetime must be recorded for the instruments in question, from the date of their initial recognition and throughout their entire life. At each subsequent balance sheet date, the ECL lifetime values must therefore be adjusted, recording the amount of any change in expected losses over the entire life of the loan as profit or loss due to impairment in the income statement. In view of this requirement, the POCI financial assets are initially recognised at stage 3, without prejudice to the possibility of subsequent transfer to performing loans, on which, however, an expected loss equal to the ECL lifetime will continue to be recorded.

In addition, in the case of non-performing loans, irrecoverable accounts are derecognised/cancelled and the remainder not yet adjusted is charged to losses, also taking into account the following cases:

- the irrecoverability of the debt, resulting from certain and precise factors (such as, by way of example, the unavailability or propertylessness of the debtor, failure to recover from the enforcement of moveable and immoveable property guarantees, negative foreclosures, closed insolvency proceedings with incomplete relief for the Bank, if there are no additional usefully enforceable guarantees, etc.);
- assignment of credit;
- renunciation of claim as a result of unilateral cancellation of the debt or residual debt in settlement agreements;
- without waiver of the receivable in the event of very remote possibilities of recovery, even without any of the factors indicated in the previous points, and in the presence of adequate means of assessment, it may be necessary to proceed with the full or partial write-off of the receivable due irrecoverability, even without closure of the legal proceedings, thereby maintaining the full right to collection of the balances subject to cancellation. The loan write-off can only concern the portion of the credit covered by provisions.

Impairment of investments

At each reporting date, investments involving subsidiaries or joint ventures are tested for impairment to determine whether there is objective evidence that the book value of such assets may not be fully recoverable.

The process of detecting any impairment involves verifying the presence of indicators of possible reductions in value and determining any write-downs. Impairment indicators can essentially be divided into two categories: qualitative indicators and quantitative indicators.

Quality indicators include:

- the achievement of negative economic results or, in any case, a significant deviation from budget objectives or targets set out in long-term plans communicated to the market;
- the announcement/commencement of bankruptcy procedures or restructuring plans;
- a downward revision of the “rating” by more than two classes;
- non-fulfilment of obligations to promptly and fully pay the debt securities issued;
- the use of industrial policy instruments to tackle serious crises or to enable companies to cope with restructuring/reorganisation processes.

Quantitative indicators include:

- a reduction in the fair value below the book value by a significant percentage or long-term deviation;
- a market capitalisation lower than the book net equity of the company, in the case of securities listed on active markets, or of a book value of the investment in the separate financial statements that is higher than the book value in the consolidated financial statements of the net assets and goodwill of the investee, or the latter's distribution of a dividend that exceeds its total income.

The presence of impairment indicators requires the recognition of a write-down to the extent that the recoverable amount is lower than the book value, to be determined by means of a specific assessment.

The recoverable amount is the higher of fair value minus costs of sale, and value in use.

The value in use is the present value of the expected cash flows arising from the asset. It reflects an estimate of the expected cash flows from the asset, an estimate of possible changes in the amount and/or timing of the cash flows, the financial value of the time, the price that compensates for the riskiness of the asset, and other factors that may influence market operators' appreciation of the expected cash flows from the asset.

In determining the value of use, the method of discounting future cash flows is used.

Impairment of other non-financial assets

Tangible and intangible assets with a finite useful life are subject to impairment testing if there is an indication that the book value of the asset can no longer be recovered. The recoverable value is determined with reference to the fair value of the tangible or intangible asset net of disposal costs, or the value in use if determinable and if it is superior to the fair value.

In the case of real property, in order to verify the presence of impairment indicators, an analysis of the various scenarios for the property markets is conducted annually. If such analyses reveal indicators of impairment, an expert report is produced on the properties for which impairment has been verified.

For other tangible assets and intangible assets (other than those recognised following aggregation operations), it is assumed that the book value normally corresponds to the value in use, since it is determined by an estimated depreciation process based on the actual contribution of the asset to the production process, and the determination of a fair value is extremely uncertain. The two values differ, resulting in impairment, in the event of damage, departure from the production process, or other similar non-recurring circumstances.

Intangible assets recognised as a result of acquisitions and in accordance with IFRS 3 at each reporting date are subject to an impairment test in order to verify whether there is objective evidence that the asset is impaired.

Intangible assets with a finite useful life, if there are indicators of impairment, are subjected to a new valuation process to verify the recoverability of sums recognised in the financial statements. The recoverable value is determined on the basis of the value in use, or the present value, estimated by using a representative rate of the time value of the money and the specific risks of the asset, of the profit margins generated by the relationships existing at the valuation date, over a time horizon that expresses its expected residual maturity.

Intangible assets with an indefinite useful life, represented by goodwill, which do not have independent cash flows, are subject to an annual assessment of the adequacy of the value recognised among assets in relation to the Cash Generating Unit (CGU) to which the values have been attributed during business combination transactions. The amount of any impairment loss is determined on the basis of the difference between the book value of the CGU and the recoverable amount of the CGU, represented by the greater of its fair value, net of any selling costs, and the value in use.

The value in use of a CGU is determined by estimating the present value of the future cash flows that are expected to be generated by the CGU. These cash flows are determined using the last available public business plan or, failing this, by the formulation of an internal anticipatory plan by management, or through

other available external evidence. Normally, the analytical forecasting period comprises a maximum time frame of five years. The flow of the last analytical forecasting exercise is projected into perpetuity, through an appropriate "g" growth rate for the purposes of the so-called "Terminal value". The "g" rate is determined by taking as a growth factor the lower of the average growth rate recorded in the analytical forecasting period and the average growth rate of Gross Domestic Product in the countries in which the flows are generated.

When determining value in use, cash flows must be discounted at a rate that reflects the current valuations of the time value of the money and the specific risks of the asset. In particular, the discounting rates used incorporate the risk-free component and equity-related risk premiums observed over a sufficiently long time period to reflect market conditions and differentiated economic cycles.

Business combinations

IFRS 3 is the accounting standard of reference for business combinations.

The transfer of control of a company (or a group of integrated activities and assets, conducted and managed as a unit) constitutes a business combination.

For this purpose, control is deemed to have been transferred when the investor is exposed to, or has rights over, variable returns arising from his or her relationship with the investee and at the same time has the capacity to affect returns by exercising power over that entity.

IFRS 3 requires that a purchaser be identified for all combination transactions. The latter must be identified as the entity that obtains control over another entity or group of assets. If no controlling entity can be identified by the definition of control described above, as for example in the case of transactions for the exchange of equity interests, the purchaser must be identified from other factors such as: the entity whose fair value is significantly greater, the entity that may pay a cash consideration, or the entity that issues new shares.

The acquisition, and therefore the first consolidation of the acquired entity, is to be accounted for on the date on which the purchaser effectively obtains control of the entity or acquired assets. When the transaction takes place through a single exchange transaction, the date of the exchange normally coincides with the date of acquisition. However, it is always necessary to verify whether there are agreements between the parties that may involve a transfer of control before the date of the exchange.

The consideration transferred as part of as part of a business combination must be determined as the sum of the fair value, at the date of exchange, of the assets sold, the liabilities incurred or assumed, and the capital instruments issued by the purchaser in exchange for control.

In transactions involving payment in cash (or where payment is made through financial instruments comparable to cash), the price is the agreed consideration, which may be discounted if payment by instalment is provided for over a period longer than the short term. If payment is made through an instrument other than cash, i.e. through the issue of equity instruments, the price is equal to the fair value of the means of payment net of costs directly attributable to the capital issue transaction.

Adjustments subject to future events are included in the consideration for the business combination at the acquisition date, if provided for by the agreements, and only if they are probable, can be reliably determined and realised within twelve months of the date of acquisition of control, while compensation for reduction in the value of the assets used is not considered because it is already considered either in the fair value of the equity instruments or as a reduction in the premium or an increase in the discount on the initial issue in the case of the issue of debt instruments.

Acquisition-related costs are the costs that the purchaser incurs in executing the business combination, including, but not limited to, professional fees paid to auditors, assessors, legal advisors, the cost of valuations and auditing, the drafting of the required disclosure documents, together with consultancy expenses incurred to identify potential targets to be acquired if it is contractually stipulated that the payment

is made only in the event of a positive outcome to the combination, and the costs of registering and issuing debt securities or shares.

The purchaser must account for acquisition-related costs as expenses in the periods in which such costs are incurred and services received, with the exception of the cost of issuing equity or debt securities, which must be recognised in accordance with IAS 32 and IFRS 9.

Business combinations are accounted for according to the "acquisition method," whereby the identifiable assets acquired (including any intangible assets not previously recognised by the acquiree) and the identifiable liabilities assumed (including potential liabilities) are recognised at their fair value at the acquisition date.

Furthermore, for each business combination, any minority interests in the acquiree may be recognised at fair value (with a consequent increase in the consideration transferred) or in proportion to the minority interest in the identifiable net assets of the acquired companies.

If control is achieved through subsequent purchases, the purchaser must recalculate its previous interest in the acquiree at its fair value at the acquisition date and recognise any difference with the previous book value in the income statement.

The excess of the consideration transferred (represented by the fair value of the transferred assets, liabilities incurred or capital instruments issued by the purchaser), possibly supplemented by the value of the minority interests (determined as described above) and the fair value of the interests already held by the purchaser, and the fair value of the assets and liabilities acquired must be recognised as goodwill. If on the other hand, such assets and liabilities are higher than the sum of the consideration, minority interests, and the fair value of shares already held, the difference must be recorded in the income statement.

The combination transaction may be provisionally booked by the end of the year in which the combination is undertaken and must be finalised within twelve months of the acquisition date.

Accounting for further equity investments in already controlled companies is considered, in accordance with IFRS 10, as a capital transaction, i.e. transactions with shareholders acting in their capacity as shareholders. Accordingly, the differences between the acquisition costs and the book value of the minority interests acquired are recognised in shareholders' equity. Likewise, sales of minority interests without loss of control do not generate gains/losses in the income statement, but rather changes in shareholders' equity.

Operations aimed at controlling, or transient control, of one or more companies that do not constitute a business activity, do not constitute a business combination, nor does it constitute a business combination if it is carried out for a the purposes of reorganisation, i.e. between two or more companies or business activities that are already controlled, and does not entail a change in control structures, regardless of the percentage of third party rights before and after the transaction (so-called business combinations subject to common control). Such operations are considered to be devoid of economic substance. Therefore, in the absence of specific instructions pursuant to IAS/IFRS and in accordance with the presumptions of IAS 8, which requires that - in the absence of a specific standard - an entity must use its judgment in applying an accounting standard that provides relevant, reliable and prudent information and reflects the economic substance of the operation, they are accounted for on the basis of continuity of the acquired entity's values in the purchaser's financial statements.

Mergers are considered to be business-to-business concentration operations and represent the most comprehensive form of business aggregation, as they entail the legal and economic unification of the entities participating in them.

Mergers, whether their own, i.e. the creation of a new legal entity or "by incorporation" with the confluence of an enterprise into another existing enterprise, are treated according to the criteria indicated above. In particular:

- if the transaction involves the transfer of control of an entity, it is treated as a aggregation under IFRS 3;

- if the transaction does not involve the transfer of control, this is accounted for by giving priority to the continuity of the values of the company being acquired.

SIGNIFICANT EVENTS AFTER THE END OF THE HALF-YEAR

There were no significant events after the end of the half-year.

DISCLOSURE ON FAIR VALUE

Assets and liabilities measured at fair value on a recurring basis: breakdown by fair value levels

(€ thousands)	31.12.2018			31.12.2017		
Financial liabilities measured at fair value	**L1**	**L2**	**L3**	**L1**	**L2**	**L3**
1. Financial assets valued at fair value through profit or loss						
a) financial assets held for trading	127	1,068	1	2,253	1,004	1
b) financial assets designated at fair value	-	-	-	-	-	-
c) other financial assets compulsorily measured at fair value	4	173,600	41,238	5	238,452	48,307
2. Financial assets measured at fair value with impact on comprehensive income	520,342	264,173	9,975	506,068	313,099	9,977
3. Hedging derivatives	-	-	-	-	-	-
4. Physical assets	-	-	-	-	-	-
5. Intangible assets	-	-	-	-	-	-
Total	**520,473**	**438,841**	**51,214**	**508,326**	**552,555**	**58,285**
1. Financial liabilities held for trading	832	1,226	-	259	1,170	-
2. Financial liabilities designated at fair value	-	-	-	-	-	-
3. Hedging derivatives	-	-	-	-	-	-
Total	**832**	**1,226**	**-**	**259**	**1,170**	**-**

Key		
L1	=	Level 1
L2	=	Level 2
L3	=	Level 3

Annual changes in assets measured at fair value on a recurring basis (level 3)

	Financial assets designated at fair value through profit or loss							
	Total	of which: a) financial assets held for trading	of which: b) financial assets designated at fair value	of which: c) other financial assets compulsorily measured at fair value	Financial assets measured at fair value with impact on comprehensive income	Hedging derivatives	Physical assets	Intangible assets
(€ thousands)								
1. Opening balances	**48,308**	**1**	**-**	**48,307**	**9,977**	**-**	**-**	**-**
2. Increases	**10,314**	**2,000**	**-**	**8,314**	**7**	**-**	**-**	**-**
2.1 Purchasing	2,000	2,000	-	-	-	-		
2.2 Profits allocated to:	768	-	-	768	7	-		

2.2.1 Income Statement	768	-	-	768	-	-		
- of which capital gains	768	-	-	768	-	-		
2.2.2 Shareholders' equity	-	X	X	X	7	-		
2.3 Transfers from other levels	-	-	-	-	-	-		
2.4 Other increases	7,546	-	-	7,546	-	-		
3. Decreases	**17,384**	**2,001**	**-**	**15,383**	**9**	**-**	**-**	**-**
3.1 Sales	2,000	2,000	-	-	-	-		
3.2 Redemptions	1,326	-	-	1,326	-	-		
3.3 Losses attributed to:	13,601	1	-	13,600	-	-		
3.3.1 Income Statement	13,601	1	-	13,600	-	-		
- of which capital losses	13,601	1	-	13,600	-	-		
3.3.2 Shareholders' equity	-	X	X	X	-	-		
3.4 Transfers to other levels	-	-	-	-	5	-		
3.5 Other decreases	457	-	-	457	4	-		
4. Closing inventories	**41,239**	**1**	**-**	**41,238**	**9,975**	**-**	**-**	**-**

Annual changes in liabilities measured at fair value on a recurring basis (level 3)

On the reporting date there were no financial liabilities measured at fair value level 3 on a recurring basis.

Assets and liabilities not measured at fair value or measured at fair value on a non-recurring basis: breakdown by fair value levels

(€ thousands)	31.12.2018				31.12.2017			
	BV	L1	L2	L3	BV	L1	L2	L3
1. Financial assets measured at amortised cost	8,762,156	1,415,825	49,393	7,731,295	8,488,829	1,104,516	84,716	7,764,386
2. Physical assets held for investment purposes	13,731	-	-	-	13,769	-	-	-
3. Non-current assets and groups of assets held for sale	12,698	-	-	12,698	12,923	-	-	12,923
Total	**8,788,585**	**1,415,825**	**49,393**	**7,743,993**	**8,515,521**	**1,104,516**	**84,716**	**7,777,309**
1. 1. Financial liabilities measured at amortised cost	9,373,831	-	482,110	8,317,416	9,101,607	-	567,461	7,999,729
4. 2. Liabilities associated with assets held for sale	-	-	-	-	-	-	-	-
Total	**9,373,831**	**-**	**482,110**	**8,317,416**	**9,101,607**	**-**	**567,461**	**7,999,729**

Key		
BV	=	Book value
L1	=	Level 1
L2	=	Level 2
L3	=	Level 3

RECLASSIFIED FINANCIAL STATEMENTS

The table below shows a reclassified balance sheet and income statement, in which the financial performance figures are presented according to faster and easier-to-interpret management criteria, in order to facilitate a more immediate reading of the situation and result for the period.

Reclassified balance sheet

The reclassified balance sheet as at 30 June 2019 has been adapted to meet the new accounting categories introduced by IFRS 16, as implemented by the 6th update of Bank of Italy Circular No. 262.

To facilitate reading the balance sheet, the reclassified statement of financial position is shown below. Reclassification only involved the aggregation of balance sheet items. In particular, note as follows:

- Cash and cash equivalents is included in the residual item Other asset items;
- financial assets constituting loans to banks and loans to customers, are entered separately regardless of the respective accounting portfolios they are allocated to;
- financial assets that do not constitute loans are entered separately, distinguishing between financial assets measured at amortised cost, financial assets measured at fair value through profit or loss, and financial assets measured at fair value with an impact on comprehensive income, net of the reclassification to loans to banks and loans to customers;
- tangible and intangible assets are aggregated into a single item;
- separate disclosure of assets and liabilities for rights of use pursuant to IFRS 16;
- payables to banks at amortised cost are entered separately;
- the total sums due to customers at amortised cost and of outstanding securities are aggregated into a single item;
- "Provisions for risks and charges" groups funds designated for a specific use (employee severance benefits, provisions for risks and charges, provisions for commitments and financial guarantees issued) into a single item;
- Reserves are indicated in an aggregate manner, net of any own shares.

Reclassified asset items	**30.06.2019**	**31.12.2018**	**Change**	
(€ thousands)			**Absolute**	**%**
Loans to banks	74,880	48,929	25,951	53.0%
Loans to customers	7,284,269	7,275,467	8,802	0.1%
- at amortised cost	7,243,515	7,227,655	15,860	0.2%
- at fair value with an impact on the income statement	40,754	47,812	(7,058)	-14.8%
- at fair value with an impact on comprehensive income	-	-	-	n.a.
Financial assets measured at amortised cost other than loans	1,443,760	1,212,245	231,515	19.1%
Financial assets at fair value through profit or loss	175,284	242,210	(66,926)	-27.6%
Financial assets at fair value with impact on comprehensive income	794,490	829,144	(34,654)	-4.2%
Equity investments	5,626	5,745	(119)	-2.1%
Tangible and intangible assets	152,938	254,697	(101,759)	-40.0%
Assets for Rights of Use	18,053	20,125	(2,072)	-10.3%
Tax assets	182,725	174,705	8,020	4.6%
Non-current assets and groups of assets held for sale	12,698	12,923	(225)	-1.7%
Other asset items	224,846	219,497	5,349	2.4%
Total assets	**10,369,569**	**10,295,687**	**73,882**	**0.7%**

Reclassified liability items	**30.06.2019**	**31.12.2018**	**Change**	
(€ thousands)			**Absolute**	**%**
Payables to banks at amortised cost	1,351,653	1,418,187	(66,534)	-4.7%
Financial liabilities to customers at amortised cost	8,004,279	7,683,419	320,860	4.2%
- amounts due to customers	7,387,701	6,985,199	402,502	5.8%
- outstanding securities	616,578	698,220	(81,642)	-11.7%
Financial liabilities held for trading	2,058	1,429	629	44.0%
Financial liabilities measured at fair value	-	-	-	n.a.
- amounts due to customers	-	-	-	n.a.
- outstanding securities	-	-	-	n.a.
- other financial liabilities measured at fair value	-	-	-	n.a.
Tax liabilities	28,210	31,254	(3,044)	-9.7%
Liabilities associated with assets held for sale	-	-	-	n.a.
Provisions for risks and charges	18,562	20,729	(2,167)	-10.5%
Other liabilities	215,473	285,341	(69,868)	-24.5%
Payables for Rights of Use	17,897	20,125	(2,228)	-11.1%
Shareholders' equity:	731,437	835,203	(103,766)	-12.4%
- Capital	183,440	183,440	-	0.0%
- Earnings reserves	650,995	632,893	18,102	2.9%
- Valuation reserves	(1,461)	(15,387)	13,926	-90.5%
- Result for the period	(101,537)	34,257	(135,794)	-396.4%
Total liabilities and shareholders' equity	**10,369,569**	**10,295,687**	**73,882**	**0.7%**

Reclassified income statement

A reclassified income statement is presented below to facilitate reading of the results for the year. As provided in Consob communication No. DEM/6064293 of 28 July 2006, a description of the reclassifications and aggregations made is provided below:

- the item “Dividends and gains (losses) from investments valued at equity” consists of the income statement item “Dividends and similar income” and the item “Gains (losses) on equity investments”;
- the item “Net result of financial assets and liabilities at fair value” includes the "Net result of trading”, "Gains (losses) on the sale or repurchase of financial assets at fair value with an impact on overall profitability" and the “Net result of other financial assets and liabilities at fair value with an impact on the income statement";
- the item “Other operating income/expenses” includes “Gains (losses) on the disposal or repurchase of financial liabilities” and “Other operating income/expenses”;

- the item "Administrative expenses" shows the balance of item 160 b) of the income statement net of taxes and charges relating to the banking system, which are included in a specific item of the reclassification;
- the item "Value adjustments to tangible and intangible assets" includes the income statement items "Adjustments/write-backs on impairment of tangible assets" and "Adjustments/write-backs on impairment of intangible assets";
- the item "Net adjustments to loans and other financial transactions" includes "Gains (losses) on the sale or repurchase of financial assets valued at amortised cost" and "Net adjustments/write-backs on credit risk of financial assets valued at amortised cost", both limited to components relating to financial assets that constitute loans;
- the item "Net adjustments to other assets" includes "Gains (losses) on the sale or repurchase of financial assets valued at amortised cost" and "Net adjustments/write-backs on credit risk of financial assets valued at fair value with an impact on overall profitability", both limited to components relating to financial assets that do not constitute loans and "Gains/losses from contractual amendments without write-downs".
- the item "Value adjustments to goodwill net of taxes" refers to the impairment of goodwill indicated in item 240 of the income statement scheme, as provided for in Bank of Italy Circular 262, stated net of the tax effect;

The ordinary and extraordinary charges introduced against banks by virtue of the single resolution mechanisms ("FRU") and national resolution mechanisms ("FRN") and the deposit guarantee scheme ("DGS") are presented, net of the relevant tax effect, in a separate item of the reclassified income statement entitled "Levies and charges relating to the banking system net of taxes".

Reclassified income statement	**30.06.2019**	**30.06.2018**	**Change**	
(€ thousands)			*Absolute*	*%*
Net interest	90,858	82,902	7,956	9.6%
Dividends and profits (losses) of investments valued at equity	1,830	2,198	(368)	-16.7%
Financial margin	92,688	85,100	7,588	8.9%
Net fees	44,679	43,066	1,613	3.7%
Net result of financial assets and liabilities at FV	(14,445)	4,281	(18,726)	-437.4%
Other operating income/expenses	10,463	9,963	500	5.0%
Other operating income	40,697	57,310	(16,613)	-29.0%
Net operating income	133,385	142,410	(9,025)	-6.3%
Personnel expenses	(46,924)	(50,473)	3,549	-7.0%
Administrative expenses	(35,775)	(38,988)	3,213	-8.2%
Value adjustments to tangible and intangible assets	(6,657)	(5,757)	(900)	15.6%
Operating costs	(89,356)	(95,218)	5,862	-6.2%
Operating income	44,029	47,192	(3,163)	-6.7%
Net adjustments to loans and other financial transactions	(57,200)	(17,096)	(40,104)	234.6%
Net adjustments to other assets	3,187	1,209	1,978	163.6%
Net provisions for risks and charges	1,214	(4,018)	5,232	-130.2%
Gains (losses) on disposal of equity investments	33	6	27	450.0%
Gross profit (loss) from current operations	(8,737)	27,293	(36,030)	-132.0%
Taxes on income from current operations	(797)	(6,631)	5,834	-88.0%
Value adjustments of goodwill net of taxes	(87,378)	-	(87,378)	n.a.
Levies and charges relating to the banking system net of taxes	(4,625)	(5,327)	702	-13.2%
Profit (Loss) for the year	(101,537)	15,335	(116,872)	-762.1%

In accordance with the indications of Consob Communication No. DEM/6064293 of 28 July 2006, please note the following information on the effects that events or transactions of a non-recurring nature have had on the economic results of the periods compared.

The following criteria are generally used to identify non-recurring components:

- the results of sales of all fixed assets (equity investments, tangible fixed assets) are considered non-recurring;
- gains and losses on non-current assets held for sale are considered non-recurring;
- economic items connected with operations to improve efficiency, restructuring, etc. (e.g. charges for recourse to the redundancy fund, voluntary redundancy packages) are considered non-recurring;
- economic items of a significant amount that are not expected to recur frequently (e.g. penalties, impairment of fixed assets, effects related to changes in regulations, exceptional results) are considered non-recurring.
- on the other hand, the economic impacts, albeit significant, deriving from valuation aspects and/or parameter changes in the application of the valuation methods adopted on a continuous basis are considered recurring.

In light of the criteria set out above, the economic result for the first half of 2019 was affected by the following non-recurring impacts:

- the "Interest Margin" item includes interest income on the TLTRO II loan for a total of €2.0 million, gross of tax effects;
- the item "Levies and charges relating to the banking system net of taxes" of €4.6 million (€6.4 million gross) includes €0.8 million relating to additional contributions relating to the National Resolution Fund net of the related tax effect of €0.4 million. Ordinary contributions to the National Resolution Fund are €2.4 million, net of the tax effect of €0.9 million, while contributions to the deposit guarantee scheme are €1.3 million, net of the tax effect of €0.5 million;
- an accounting adjustment to the value of goodwill of €99.6 million.

RESULTS AS AT 30 JUNE 2019

Income Statement

The main items of the income statement reclassified at 30 June 2019 are illustrated below, compared with the corresponding period of the previous year.

Net interest

The interest margin stands at €90.9 million. This figure includes interest paid on liabilities relating to IFRS 16 for a total of €68 thousand.

The result of equity investments measured at equity was positive by €1.8 million, down 16.7% compared with €2.2 million in the same period last year. The main contribution to this aggregate was dividends (up €2.1 million, and €6.0% on the first half of 2018) and net adjustments to equity investments of €0.3 million.

Analysis of net commissions	**30.06.2019**	**30.06.2018**	**Change**	
			Absolute	*%*
Management, brokerage and advisory services	14,384	13,017	1,368	10.5%
Management and maintenance of c/a and customer relations	20,334	20,475	-141	-0.7%
Collection and payment services	3,520	3,686	-166	-4.5%
Guarantees given	1,703	1,720	-16	-0.9%
Other services	4,738	4,168	569	13.7%
Total	44,679	43,066	1,613	3.7%

Net commission income amounted to €44.7 million, an increase of 3.7% compared to the first half of 2018 which recorded net commission income of €431 million.

The main changes were in the brokerage, management and advisory services segment, which contributed €14.4 million, up 10.5% (€1.4 million)on the first half of 2018. The contribution of current accounts and customer relations was stable at €20.3 million (€20.5 million in the first half of 2018). The contribution of "other services" increased to €4.7 million, compared to €4.1 million in the first half of 2018.

The net result of financial assets and liabilities at fair value was -€14.4 million, compared with -€4.3 million in the same period last year. This result derives from the contribution of +€0.6 million trading assets (+€1.3 million in the first half of 2018), from net earnings on financial assets at fair value, which had an impact on comprehensive income of +€1.3 million (+€1.6 million in the first half of 2018), affected by market volatility in the first half and the net result of other financial assets and liabilities at fair value through profit or loss, a loss of €16.3 million, mainly attributable to loans to customers (+€1.4 million in the first half of 2018).

Other net operating income amounted to €10.4 million, up 5.0% from €10.0 million in the first half of 2018.

As a result of the performance described above, net operating income amounted to €133.4 million, compared to €142,4 million in the first half of 2018 (down 6,3%).

Personnel expenses amounted to €46.9 million, down 7.0% from €50.5 million in the same period last year. Personnel costs decreased mainly as a result of the absence of premium expenses. The total number of employees stood at 1,303 at 30 June 2019, compared with 1,327 at the end of 2018.

Administrative expenses came in at €35.8 million, down 8.2% compared with the same period a year earlier (€38.9 million). The aggregate does not include "systemic charges", consisting of contributions to the Single Resolution Fund (SRF) and deposit guarantee scheme (DGS), presented, net of the related tax effect, in a

separate item of the reclassified income statement. Other administrative expenses include related costs for IT services of €7.1 million and expenses for valuations and inquiries of €1.3 million. This figure is not fully comparable with the figure for the previous year, since no rental costs totalling €2.1 million were recognised following the application of IFRS 16.

Net value adjustments to physical and intangible assets for the period amounted to €6.7 million, up by €0.9 million compared with €5.8 million at 30 June 2018. This figure is not fully comparable with that of the previous year, since following the application of IFRS 16, depreciation related to IFRS 16 was recognised for a total of €2.1 million.

Total operating expenses amounted to €89.4 million, down by 6.2% compared to the first half of 2018 (when the figure was €95.2 million).

Net adjustments to loans to customers amounted to -€57.2 million. The change of -€17.1 million in the first half of 2018 was due, *inter alia*, to the increased safeguards against credit risk, including in the case of unlikely-to-pay loans, which incorporate the effects of numerous regulatory developments affecting the non-performing loans segment.

In particular, on 17 April 2019 the European Commission approved Regulation 630/2019 amending Regulation 575/2013 ("CRR") regarding the minimum levels of coverage of non-performing exposures. The provision provides that, for loans disbursed after the entry into force of the provision, from the time they become impaired, they must be written down in full within 3 years if they are not, and within 10 years if they are secured. The portion of the write-down not recorded in the financial statements must be deducted from the primary quality capital (CET1). In particular, the rule does not distinguish between debtors who, as they are no longer operating their business, are no longer able to repay their debts and for whom, therefore, the only possibility of recovery is the initiation of enforcement and/or insolvency or forced recovery procedures, and companies in difficulty but which, because they are still active, are still able to operate their normal business, even if they have been properly restructured and financially assisted. As a result, loans to debtors which are likely to regain the status of 'performing' must therefore be subject to the same provisioning rules as for non-performing loans.

The cost of credit, measured by the ratio of net impairment losses on loans to net loans, was 157 bps, higher than the figure for the first half of 2018 of 47 bps. The level of credit adjustments reflects an assessment approach designed to maintain high levels of coverage and take any additional opportunities to accelerate the risk reduction process.

Net reversals of securities and other financial assets amounting to €3.2 million were also recognised in the income statement for the first half of the year (compared to net reversals of €1.2 million as at 30th June 2018).

Net provisions for risks and charges amounted to +€1.2 million, compared to -€4.0 million in the same period last year.

As a result of the trends described above, profit from continuing operations before tax and systemic charges amounted to -€8.7 million compared with the figure of €27.3 million recorded in the first half of the previous year.

Taxes on income from continuing operations amounted to -€0.8 million at 30 June 2019 (-€6.6 million at 30 June 2018).

Goodwill impairment losses amounted to €99.6 million, compared to the zero figure for the first half of 2018. Net of the tax effect, the adjustment came to €87.4 million.

The income statement for the first half of the year includes levies and charges relating to the banking system net of taxes amounting to €4.6 million (€5.2 million in the corresponding period last year), which include, net of the associated tax effect, ordinary contributions to the Single Resolution Fund ("SRF") of €4.6 million gross (€3.6 million gross in the first half of 2018) and to €1.8 million relating to the Deposit Guarantee Schemes ("DGS").

The first half of 2019 closed with a loss of €101.5 million, compared to net profit of €15.3 million for the same period of the previous year.

Statement of financial position

a) Credit intermediation activities

Direct deposits

Technical forms of direct deposits *(€ thousands)*	**30.06.2019**	**31.12.2018**	**Changes**	
			Absolute	*%*
Savings and current account deposits	6,331,798	6,002,816	328,982	5.5%
Repurchase agreements on securities	381,503	369,899	11,604	3.1%
Outstanding securities	482,110	567,460	(85,350)	-15.0%
Deposit certificates	-	-	-	n.a.
Subordinated liabilities	134,468	130,760	3,708	2.8%
Other deposits	692,298	612,484	79,814	13.0%
Total Direct Collection	8,022,177	7,683,419	338,758	4.4%

Direct deposits as at 30 June 2019 amounted to €8.0 billion, an increase of 4.4% compared to €7.7 billion as at 31 December 2018.

Direct deposits confirm the trend already underway in the previous year, which favours the on demand component, as a result of a greater propensity towards liquidity, partly as a result of the significant volatility and uncertainty that characterises the current market situation, and due to a situation of particularly low rates, in addition to the need to ensure adequate portfolio diversification.

The increase was due to the current accounts and demand deposits of the commercial network, which rose by €329.0 million (5.5%), whereas repo liabilities stood at €381.5 million, up 3.1% on the figure of €370.0 million at year end, outstanding securities confirm the reduction already under way since last year and stood at €482.1 million, down by 15% compared to the year end. The trend of gradual reduction continued, due to the context of yields which are now close to zero, pushing customers towards other forms of investment. The evolution is also in line with the strategy of progressive reduction of the cost of funding thanks to the reduction of its more expensive forms. Other forms of funding stood at €692.3 million (up €79.8 million - 13.0% - compared to €612.5 million at the end of 2018).

Subordinated liabilities, totalling €134.5 million, consist of 3 issues with the following characteristics:

	Issue 01.8.2017	**Issue 06.10.2017**	**Issue 03.10.2018**
Degree of Subordination	Tier 2 qualifying subordinated liabilities	Tier 2 qualifying subordinated liabilities	Tier 2 qualifying subordinated liabilities
ISIN	XS1663201942	XS1694763142	XS1885681228
Amount	5,000,000	100,000,000	25,000,000
Date of Issue	01.08.2017	06.10.2017	03.10.2018
Maturity Date	17.08.2029	06.10.2027	30.10.2028
Currency	EUR	EUR	EUR
Rate	5.625%	5.625% per annum, payable in arrears until 06.10.2022 (equal to 5yr MS + 536.8 bps), then rate reset to mid-swap fixing + 536.8 bps margin.	6.000% per annum, payable in arrears up to 03.10.2023 (equal to 5yr MS + 589.4 bps), then resetting the rate at mid-swap fixing + 589.4 bps margin
Price	99.25		97.717
Listing	Luxembourg Stock Exchange	Luxembourg Stock Exchange	No

Indirect deposits

Indirect deposits consist entirely of assets under administration and amount to €3.7 billion at 30 June 2019, up by 6.1% compared to 31 December 2018.

In greater detail, the assets under administration relating to third party products amounted to €2,526.5 million, up 8.5% from €2,327.8 million at 31 December 2018. Mutual funds increased 8.8% to €1,744.8 million, pension funds and pension insurance increased by 13.8% to €91.1 million, while life insurance provided by third parties increased by 7.3% to €689.1 million.

The assets under administration component, consisting of securities, came to €1,133.9 million, up by €11.9 million. In particular, third-party securities grew by 2.7%, principally as a result of the growth of shares in the portfolio (10.6%), whereas government bonds were stable (down 0.6%) and bonds declined by 14.1%.

Technical forms of indirect deposits *(€ thousands)*	**30.06.2019**	**31.12.2018**	**Changes**	
			Absolute	%
Assets under administration – third party products	2,526,531	2,327,816	198,715	8.5%
Assets under administration - third party securities and own shares	1,133,898	1,122,011	11,888	1.1%
Total	**3,660,429**	**3,449,826**	**210,603**	**6.1%**

The overall growth of aggregate indirect funding has benefited, first and foremost, from the positive trend in prices. The first half also saw the continuation of the gradual replacement of bond deposits with other forms of investment. Both components of indirect administered deposits (third-party products and third-party securities) benefited from these uncertain conditions, partly as a result of the prolonged situation of rates at historical lows, somewhat reinforced by the renewal of expectations, on the part of operators and policy makers, of continued expansionary monetary policies.

Loans to customers at amortised cost

Various types of loans *(€ thousands)*	**30.06.2019**	**31.12.2018**	**Changes**	
			Absolute	%
Current accounts	1,016,503	1,168,899	(152,396)	-13.0%
Advances and loans	503,975	467,870	36,105	7.7%
Mortgages	5,281,943	5,118,812	163,131	3.2%
Trade receivables	**6,802,421**	**6,755,581**	**46,840**	**0.7%**
Repurchase agreements	-	-	-	n.a.
Receivables represented by securities	90,418	87,144	3,274	3.8%
Non-performing loans	329,571	370,806	(41,235)	-11.1%
Various other receivables	21,105	14,122	6,983	49.4%
Other loans to customers	**441,094**	**472,072**	**(30,978)**	**-6.56%**
Total loans to customers	**7,243,515**	**7,227,653**	**15,862**	**0.22%**

Net lending to customers amounted to €7.3 billion at 30 June 2019, substantially unchanged from the end of 2018 (up 0.2%). The aggregate of performing loans grew by 0.8% compared to 31 December 2018.

Loans increased by 3.2% to €5,281.9 million (up €163.1 million) and advances and loans were up 7.7% to €504.0 million (€467.9 million at the end of 2018). Current accounts fell (down 13.0% and €152.4 million).

Due to these dynamics, customer financial assets increased to €10.9 billion, up 4.8% on the end of 2018 (when it stood at €10.4 billion).

The following table shows the figures for financial assets of customers only.

Customer financial assets	**30.06.2019**	**31.12.2018**	**Changes**	
(€ thousands)			**Absolute**	**%**
Direct bank deposits (excluding Wholesale collection)	7,239,581	6,950,527	289,054	4.2%
Indirect deposits	3,660,429	3,449,826	210,603	6.1%
Total customer assets	**10,900,010**	**10,400,353**	**499,657**	**4.8%**

b) Credit Quality

The following tables show cash loans to customers as at 30 June 2019, compared with the corresponding exposure as at 31 December 2018.

Loans to customers measured at amortised cost	**30.06.2019**	**31.12.2018**	**Changes**	
(€ thousands)		***IAS 39***	**Absolute**	**%**
Non-performing exposures				
A) bad debts				
gross amounts	409,896	407,836	2,060	0.51%
value adjustments	(246,488)	(226,513)	(19,975)	8.82%
net non-performing loans	163,408	181,323	(17,915)	-9.88%
b) unlikely to pay				
gross amounts	246,084	248,054	(1,970)	-0.79%
value adjustments	(93,998)	(64,705)	(29,293)	45.27%
net unlikely to pay	152,086	183,349	-31,263	-17.05%
c) past due exposures				
gross amounts	14,668	6,659	8,009	120.27%
value adjustments	(591)	(526)	(65)	12.36%
net past-due exposures	14,077	6,133	7,944	129.53%
d) Subtotal non-performing exposures (a+b+c)				
gross amounts	670,648	662,549	8,099	1.22%
value adjustments	(341,077)	(291,744)	(49,333)	16.91%
net non-performing exposures	329,571	370,805	-41,234	-11.12%
Performing Exposures				
e) performing loans - stage 1				
gross amounts	6,105,183	6,156,732	(51,549)	-0.84%
value adjustments	(25,686)	(28,818)	3,132	-10.87%
net performing loans - stage 1	6,079,497	6,127,914	-48,417	-0.79%
f) performing loans - stage 2				
gross amounts	776,703	673,698	103,005	15.29%
value adjustments	(32,674)	(31,908)	(766)	2.40%
net performing loans - stage 2	744,029	641,790	102,239	15.93%
g) Subtotal performing loans (e+f)				
gross amounts	6,881,886	6,830,430	51,456	0.75%
value adjustments	(58,360)	(60,726)	2,366	-3.90%
net performing loans	6,823,526	6,769,704	53,822	0.80%
Performing loans consisting of securities				
h) performing exposures represented by securities - stage 1				
gross amounts	90,711	87,400	3,311	3.79%
value adjustments	(293)	(256)	(37)	14.45%
net performing exposures represented by securities - stage 1	90,418	87,144	3,274	3.76%
i) performing exposures represented by securities - stage 2				
gross amounts		-		
value adjustments		-		
net performing exposures represented by securities - stage 2		-		
j) Subtotal performing loans consisting of securities (H+I)				
gross amounts	90,711	87,400	3,311	3.79%
value adjustments	(293)	(256)	(37)	14.45%
net performing exposures represented by securities	90,418	87,144	3,274	3.76%
Total loans to customers measured at amortised cost (d+g+j)				
gross amounts	7,643,245	7,580,379	62,866	0.83%
value adjustments	(399,730)	(352,726)	(47,004)	13.33%
Total net loans to customers	7,243,515	7,227,653	15,862	0.22%
- of which forborne performing	*51,134*	*73,731*	*(22,597)*	*-30.65%*

- of which non-performing forborne	*92,899*	*107,910*	*(15,011)*	*-13.91%*

At 30 June 2019, total gross non-performing loans (bad debts, unlikely to pay and/or past due positions) amounted to €670.6 million, up 1.2% (up €8.1 million compared to €662.5 million at the end of 2018). The impact of the non-performing portfolio on total gross loans to customers was 8.8%, largely unchanged from 8.7% at the end of 2018. In particular:

- Gross non-performing loans were essentially stable (up 0.5%) at €409.9 million (up 2.0 million), while net non-performing loans stood at €163.4 million, down 9.9% from €181.3 million at the end of 2018 (€17.9 million). The reduction in the net aggregate was due to the increase in value adjustments (up €20.0 million). Gross non-performing loans accounted for 5.4% of total gross loans, unchanged compared with the end of 2018. The coverage ratio for bad loans was 60.1%, a significant increase compared to 55.5% at 31 December 2018;
- gross unlikely to pay positions, totalling €246.1 million, were down €0.8% from €248.1 million at the end of 2018. Net unlikely to pay positions amounted to €152.1 million, down by 17.1% compared to the end of 2018. The coverage level for unlikely to pay positions stood at 38.2%, up from 26.1% at the end of 2018, as mentioned above;
- gross past-due exposures of €14.7 million increased by €8.1 million (compared to €6.7 million at the end of 2018). Net past-due exposures stood at €14.1 million, up by €7.9 million compared to €6.1 million in the previous year. The coverage ratio for past-due exposures was 4.0%, down from 7.9% at the end of 2018.

Collective adjustments amounted to 0.85% of performing loans, compared to 0.89% at the end of 2018. In further detail, the coverage of performing loans classified as "Stage 1" was 0.42% (compared to 0.47% at the end of 2018), while the receivables in "*Stage 2*" had a coverage of 4.21% (4.74% at the end of 2018).

Credit coverage rates	**30.06.2019**	**31.12.2018**
% coverage of bad debts	60.1%	55.5%
Coverage of unlikely to pay positions	38.2%	26.1%
Overdue Exposure Coverage	4.03%	7.9%
% coverage of non-performing loans	50.9%	44.0%
Performing exposures Coverage	0.85%	0.89%

The main indicators of credit quality are as follows:

Asset quality ratios	**30.06.2019**	**31.12.2018**
Gross non-performing loans/gross uses	8.77%	8.74%
Net non-performing loans/net loans	4.55%	5.13%
Gross bad debts/gross loans	5.36%	5.38%
Net bad debts/net loans	2.26%	2.51%
Gross unlikely to pay/gross loans	3.22%	3.27%
Net unlikely to pay/net loans	2.10%	2.54%
Gross bad debts/gross loans	0.19%	0.09%
Net bad debts/net loans	0.19%	0.08%

c) Financial assets

Financial assets	**30.06.2019**	**31.12.2018**	**Changes**	
(€ thousands)			Absolute	% Change
Financial assets valued at FV with an impact on the income statement	216,037	290,022	(73,985)	-25.5%
- financial assets held for trading	1,196	3,258	(2,063)	-63.3%
- FV-designated financial assets	0	0	0	n.a.
- financial assets compulsorily valued at FV	214,841	286,764	(71,922)	-25.1%
Financial assets valued at FV with impact on comprehensive income	794,490	829,144	(34,654)	-4.2%

CA-rated securities that do not constitute loans	1,443,760	1,212,245	231,516	19.1%
Total financial assets	**2,454,287**	**2,331,411**	**122,877**	**5.3%**

Financial assets other than loans to customers totalled €2,454.3 million, up 5.3% from €2,331.4 million at 31 December 2018. This aggregate mainly includes debt securities of €2,230.3 million (compared with €1,982.8 million at the end of 2018), equity securities and UCITS shares of €183.1 million and the fair value of derivatives of €0.1 million.

In addition, financial assets (amounting to €40.7 million) also include loans to customers, which must be measured at fair value.

The overall increase compared to the end of 2018 was due to the growth of the debt securities in the "Hold to Collect" portfolio (€231.5 million), while the assets classified at fair value through profit or loss fell (down €74.0 million, or 25.5%) and "Hold to Collect & Sell" (down €34.7 million, or 4.2%). Government bonds totalled €1,921.0 million (€332.6 million compared to 31 December 2018).

As at 30 June 2019, valuation reserves, net of tax effects, were negative in all securities classified in the Hold to Collect & Sell portfolio, at a total of -€1.5 million (they stood at -€15.4 million at the end of 2018), a reduction mainly due to the sale of a significant component of the portfolio classified as FVOCI, as well as to the positive trend in prices during the first half of the year.

Financial assets designated at fair value through profit or loss

Financial assets valued at FV with an impact on the income statement *(€ thousands)*	**30.06.2019**	**31.12.2018**	**Changes Absolute**	**% Change**
Bonds and other Debt Securities	1,539	3,531	(1,992)	-56.4%
Equity securities	173,612	238,465	(64,853)	-27.2%
Net value of derivative contracts for trading	132	214	(82)	-38.3%
Cash assets	40,754	47,812	(7,058)	-14.8%
Total financial assets valued at FV with an impact on the income statement	**216,037**	**290,022**	**(73,985)**	**-25.5%**

Most of the assets in question consist of Level 3 equity securities €173.6 million (previously €238.5 million) as well as cash assets of €40.8 million (previously €47.8 million).

Financial assets measured at fair value with impact on comprehensive income

Financial assets measured at fair value with impact on comprehensive income *(€ thousands)*	**30.06.2019**	**31.12.2018**	**Changes Absolute**	**% Change**
Equity securities	9,465	62,094	(52,629)	-84.8%
Debt securities	785,025	767,050	17,975	2.3%
- of which stage 1	785,025	767,050	17,975	2.3%
- of which stage 2	0	0	0	n.a.
- of which stage 3	0	0	0	n.a.
Financial assets valued at FV with impact on comprehensive income	**794,490**	**829,144**	**(34,654)**	**-4.2%**

Financial assets measured at fair value with an impact on comprehensive income amounted to €794.5 million, down 4.2% (€34.7 million) compared to the end of 2018 (previously €829.1 million).

This item consists of bonds and other debt securities amounting to €785.0 million (of which only €0.5 million at level 3), an increase of 2.3% compared to €767.1 million at the end of 2018, and equity instruments amounting to €9.5 million (entirely at level 3), a sharp fall compared to €62.1 million at the end of 2018.

Debt securities of governments and central banks consist entirely of Italian government securities. Of the total debt securities of governments and central banks, €448.3 million are due within 5 years and €77.0 million more than 5 years.

Financial assets measured at amortised cost that do not constitute loans

financial assets at amortised cost that do not constitute loans	**30.06.2019**	**31.12.2018**	**Changes**	
(€ thousands)			**Absolute**	**% Change**
Debt securities	1,443,760	1,212,245	231,515	19.1%
- of which stage 1	1,443,760	1,212,245	231,515	19.1%
- of which stage 2	0	0	0	n.a.
- of which stage 3	0	0	0	n.a.
Total financial assets at amortised cost that do not constitute loans	**1,443,760**	**1,212,245**	**231,515**	**19.1%**

Financial assets at amortised cost other than loans consist of €1,395.7 million in Italian government securities (of which €658.5 million has a maturity of under 5 years and €737.2 million has a maturity of over 5 years).

Equity investments

In addition to the investment portfolio, there is a subsidiary Voba CB, a special purpose vehicle for the issue of corporate bonds.

Name	**Headquarters**	**% shareholding**	**% availability of votes**
A. WHOLLY CONTROLLED SUBSIDIARIES			
1. Voba Invest S.r.l. in liquidation	Bolzano (BZ)	100%	100%
2. Valpolyella A.S.A. S.r.l	Bolzano (BZ)	100%	100%
3. Quartiere Brizzi S.r.l.	Chienes (BZ)	100%	100%
4. Voba Invest S.r.l.	Conegliano (TV)	60%	60%
B. JOINTLY CONTROLLED SUBSIDIARIES			
C. COMPANIES SUBJECT TO SIGNIFICANT INFLUENCE			
1. Casa cure Villa S. Anna S.r.l.	Merano (BZ)	35.00%	35.00%
2. Three S.r.l.	Trento (TN)	30.00%	30.00%

The following table shows the accounting information for the investee companies, as shown in the latest available financial statements:

Names	**Book value of investments**	**Total assets**	**Total liabilities**	**Total revenue**	**Profit (loss) from current operations after tax**	**Profit (loss) of groups of assets held for sale, net of taxes**	**Profit (Loss) for the year (1)**	**Total other income after tax (2)**	**Comprehensive income (3) = (1)+(2)**
A. Wholly controlled subsidiaries									
1. Voba Invest S.r.l. in liquidation	2,078	2,191	113	123	(37)	-	(37)	-	(37)
2. Valpolyella Alta Società Agricola S.r.l.	2,830	4,387	4,482	261	(117)	-	(117)	-	(117)
3. Quartiere Brizzi S.r.l.	-	6,031	5,795	499	(119)	-	(119)		(119)
4. Voba CB S.r.l.	6	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
									-
B. Jointly controlled subsidiaries									
									-
C. Companies subject to significant influence									
1. Casa di cura Villa S. Anna	672	8,736	6,256	6,546	438	-	438	-	438
2. Three S.r.l.	165	367	285	1	(2)	-	(2)		(2)

d) Tangible and intangible assets

At the end of the half-year, tangible assets amounted to €152.0 million, up 11.8% compared to €136.0 million at 31 December 2018. As a result of the application of IFRS 16 with effect from 1 January 2019, €18.1 million related to the right of use was recognised.

Intangible assets amounted to €19.0 million, after a full adjustment of goodwill, as described in greater detail in the following paragraph, consisting of a customer relationship of €18.0 million, recognised upon the incorporation of the Banca Popolare di Marostica Group, and software of €1.0 million.

e) Impairment test of goodwill

The definition of Cash Generating Units (CGUs)

The estimate of value in use, for the purposes of impairment testing of intangible assets with an indefinite life (including goodwill), which do not generate cash flows except with the assistance of other company assets, requires the preliminary allocation of these intangible assets to organisational units that are substantially independent in terms of management, which are capable of generating cash flows that are largely independent of those produced by other areas of activity, but interdependent within the organisational unit that generates them.

In the terminology of IAS/IFRS, these organisational units are referred to as Cash Generating Units (CGUs). For the identification of the CGUs, the meaning of the impairment test is relevant.

The impairment test on goodwill requires the identification of the CGUs at a level correlated with the level of internal reporting at which the management controls the management dynamics. The definition of this level is closely dependent on organisational models and the allocation of management responsibilities for the purposes of defining the operational activity guidelines and the consequent monitoring. Organisational models may not depend on the structure of the legal entities through which operations are developed and, very often, are closely related to the definition of the operating segments of the business that form the basis of the segment reporting required by IFRS 8.

The criteria for determining the CGUs for the impairment test of goodwill are also consistent with the definition of recoverable value of an asset - the determination of which is the basis of the impairment test - according to which the amount that the company expects to recover from that asset is significant, considering the synergies with other assets.

In the Volksbank organisational model:

- management decisions are highly centralised at the Board of Directors and the Executive Board;
- strategies, commercial initiatives, product and service policies are identified and managed centrally;
- planning and control processes and reporting systems are managed centrally;
- the transversal functions of product support and development are carried out centrally, to the benefit of the commercial functions and structures in direct contact with customers;
- the management of financial risks is highly centralised, partly in order to manage the overall balance between capital allocation policies and the financial risks assumed.

As a result of this unitary and centralised governance structure, revenue flows are highly dependent on the policies formulated at the level of the Board of Directors and General Management, in order to ensure the organic development of the business as a whole, in the absence of autonomous operating divisions or operational areas between which a distinction is made by management.

The corporate complex as a whole corresponds to the Bank CGU and constitutes the basic area of operation to which impairment testing refers. Accordingly, the corporate entity as a whole constitutes the smallest group of assets that generates independent cash inflows and, as mentioned above, the minimum level at

which planning and internal reporting processes are managed by the Bank. It constitutes the minimum level to which goodwill can be allocated according to non-arbitrary and monitored criteria.

The book value of the CGU

The book value of CGUs must be determined in a manner consistent with the criteria used to estimate their recoverable value. From the perspective of a banking company, it is not possible to identify flows generated by a CGU without considering flows arising from financial assets/liabilities, since the latter represent the core business of the company. Therefore, the recoverable amount of CGUs is affected by these flows and therefore the book value of the CGUs must be determined in accordance with the scope of the estimate of recoverable value and must therefore also include financial assets/liabilities.

In the specific case of Volksbank, since the CGU coincides with the corporate entity as a whole, the book value of the CGU is identified as the sum of the book values of the assets and liabilities as stated in the annual accounts, including goodwill and other intangible assets associated with the CGU.

Criteria for estimating the Value in use of CGUs

The value in use of the CGUs is determined by estimating the present value of the future cash flows that are expected to be generated by the CGUs. These cash flows are usually estimated using the latest available public company plan, or, failing that, through the use of analyses and evaluations developed internally by management, making use, insofar as they are available, of public data and estimates.

The analytical forecasting period consists of a maximum time frame of five years. The flow of the last analytical forecasting exercise is projected into perpetuity through the use of a perpetual annuity formula, measured by applying a perpetual growth rate "g" for the purposes of calculating the "Terminal Value". The "g" rate is determined, in line with current valuation practice on the Italian market, in line with long-term inflation expectations for the Italian economy.

When determining value in use, cash flows are discounted at a rate, estimated on the basis of the Capital Asset Pricing Model (CAPM), which reflects current valuations of the time value of money and the risks specific to the assets, such as to express the cost of capital in the configuration consistent with the assumptions underlying the development of cash flows. In particular, the discount rate incorporates the current market values with regard to the risk free component and the risk premium for the equity component observed over a sufficiently long period of time to reflect market conditions and economic cycles, and, in order to take account of the risk level of specific banking operations, the Beta coefficient.

Estimation of cash flows

The cash flows expected in the explicit period are determined on the basis of the prospective economic and financial data, taking into account the minimum level of capitalisation set by the last SREP financial year applicable to the bank, with respect to the expected evolution of risk-weighted assets.

The estimate of cash flows for the period 2019-2023 nevertheless refers to the Plan approved by the Board of Directors on 22 December 2018, as it still represents the Bank's strategic approach.

However, this Plan incorporates a macroeconomic scenario that is significantly different from the one that later emerged, following the evolution recorded in the last part of the half-year.

Overall, the global macroeconomic scenario has been progressively penalised by the growing uncertainties linked to the trade tensions between the US and China, the growing fears of a currency war between the various world central banks, as well as the growing uncertainty related to the effects of Brexit.

In Europe, the leading indicators that emerged in the first half of the year do not provide any indications of a recovery in the economic cycle, with the domestic component stable and the production and export component falling.

Unlike the outlook outlined at the end of 2018, the new scenario, also as outlined by the forecasts of authoritative institutions, envisages the continuation of highly expansionary monetary policy choices for a prolonged period of time.

In June the ECB stated that the economic outlook did not improve and therefore confirmed that additional stimulus would be required and that further interest rate cuts could be part of the instruments available.

At its meeting of 25 July 2019, the Governing Council of the European Central Bank (ECB) decided that the interest rates on the main refinancing operations, the marginal lending facility and the deposit facility would remain unchanged at 0.00%, 0.25% and -0.40% respectively.

The last meeting also reinforced the expectation that the ECB's key interest rates would to remain at or below their current levels during the first half of 2020 and in any case as long as it is necessary to ensure that inflation continues to converge steadily towards its medium-term objective.

It was also confirmed that the intention was to continue to fully reinvest the capital redeemed on maturing securities under the asset purchase programme for an extended period of time after the start of the ECB's key interest rate increase, and in any event as long as it is necessary to maintain favourable liquidity conditions and a large degree of monetary accommodation, has also been confirmed.

Finally, the ECB confirmed the need for a highly accommodative monetary policy stance for an extended period of time as actual and projected inflation rates have been persistently below levels in line with the intended value. Thus, if the medium-term inflation outlook remains below target value, the ECB confirmed its determination to act, in line with its commitment to a symmetric inflation target. The ECB also confirmed its intention to use all policy instruments at its disposal, where appropriate, to ensure that inflation is kept close to the target level on a permanent basis.

The current scenario of below-potential growth and the evolution of inflation still far from the objective of keeping the inflation rate below, but close to, 2% in the medium term, is therefore the main justification for an extended period of an expansionary scenario.

This implies, on the one hand, the expectation that ECB official rates will remain at or below current levels for an extended period and, on the other hand, the prospect of further action to ensure an expansionary monetary policy path if necessary.

For longer-term rates, the extended period of very accommodative monetary policy is considered to justify a flattening of the yield curve, also in view of the anticipated extraordinary monetary policy measures to counter this trend.

In terms of the impact on planning, it emerges that the significant prolongation of a particularly low level of market rates, well beyond the expectations existing at the date of preparation of the business plan, together with the growing uncertainties surrounding the economic growth prospects for the next few years, determine an increase in the risk surrounding the ability to effectively achieve the economic objectives of the Plan, particularly from a prospective point of view. It is therefore appropriate, for the sole purpose of the impairment test, to consider this greater risk by revising income flows downwards.

Since the level of interest rates is the main variable capable of influencing the Bank's profitability, the analytical estimates contained in the 2019 - 2023 business plan have been revised by projecting in all the forecasting exercises the impact resulting from the lowest level of market rates expected at the current date. Given the ongoing uncertainty and volatility of the macroeconomic scenario, the new scenario was constructed by adopting a rigorous and prudent outlook, incorporating the most recent forecasts for the performance of the macroeconomic scenario and rates, prepared by external companies in July 2019.

Within the framework of financial valuation criteria, such as the one used to estimate the Value in Use, the value of a company at the end of the analytical flow forecasting period (the so-called "Terminal Value") is generally determined by capitalising infinitely, at an appropriate "g" rate, the cash flow that can be obtained "at full capacity".

With regard to the estimate of the terminal value, in accordance with the time period covered by the plan, the last year of analytical forecasts was considered to be a "full" flow and was therefore projected into perpetuity. This value, which stood at 1.5%, was determined in full continuity with the criteria adopted in previous impairment testing.

The discount rates of flows

When determining the Value of use, cash flows must be discounted at a rate that reflects the current market valuations of the time value of the money and the specific risks of the asset.

Current market conditions result in the determination of all parameters based on the most up-to-date information available at the reference date of the estimate, in order to better consider current market valuations. Specifically, aspects related to inflation, country risk and other risk factors that could be expressed, pursuant to IAS 36, in flows or rates, are important. Note that since goodwill by definition has an indefinite useful life, the expected cash flows of goodwill are normally projected in perpetuity.

This long-term perspective should be reflected in all of the parameters of the discount rate by an appropriate choice of each, so that they express “normal” conditions in the long term.

In the case of banking companies, the rate is estimated from the equity side, i.e. considering only the cost of equity capital (Ke), in accordance with the methods of determining flows which, as already noted, include flows from financial assets and liabilities.

In this specific case, the cost of capital was determined using the Capital Asset Pricing Model (CAPM). On the basis of this model, the cost of capital is determined as the sum of the return on risk-free investments and a risk premium, which in turn depends on the specific riskiness of the business (meaning both the riskiness of the operating segment and the geographical riskiness represented by the so-called "country risk").

The cost of equity capital, assumed to be 9.8%, was estimated on the basis of the Capital Asset Pricing Model (CAPM), considering the following parameters:

- Risk-free rate of 2.87% (annual average gross yield on 10-year BTPs);
- Beta of 1.21 (average of the coefficient determined on a sample of comparable companies based on 5-year observations);
- Market risk premium of 5.70% (in line with current valuation practice on the Italian market).

The Terminal Value was estimated on the basis of a dividend deemed sustainable beyond the explicit period and an assumed long-term growth rate of 1.5%, in line with current valuation practice on the Italian market and with long-term inflation expectations for the Italian economy.

The cost of capital was estimated in full continuity of method with previous impairment tests and in line with the provisions of IAS 36 and the guidelines issued by the Italian Valuation Body (OIV).

The results of the impairment test

The results of the impairment test indicated the need to make a full adjustment to the value of intangible assets with an indefinite useful life represented by goodwill (CGU coinciding with the banking entity as a whole). In particular, the reasons for the recognition of the value adjustment at 30 June 2019 are entirely attributable to changes in the reference scenario.

Shareholders' equity

Shareholders' equity as at 30 June 2019, including valuation reserves and net profit for the period, amounted to €731.4 million, compared with €835.2 million at the end of 2018. The change observed during the period is due to the effects of the loss for the year and the positive change in valuation reserves (up €11.0 million).

The following table shows a breakdown of assets and reserves in relation to their possible use.

Transaction Type/Values *(€ thousands)*	**Amount**	**Possible use**	**Available portion**	**Uses in the previous three years**	
				Coverage of losses	**Other uses**
Capital	**201,994**	**-**	**-**		
Treasury shares	**(18,554)**	**-**	**-**		
Issue premium	**383,159**	**A,B,C**	**383,159**		**173**
Earnings reserves					
- Legal reserve	122,100	A(2),B	81,701		
- Extraordinary reserve	155,227	A,B,C	155,227		
- Reserve unavailable pursuant to Article 6 of Legislative Decree 38.2005	1,368	B, (*)	-		
- other					
a) Special reserve Law 218/90	8,584	A,B,C (3)	8,584		
b) FTA reserve	(16,384)	A,B,C	-		
c) Reserves from the sale of equity securities measured at fair value with an impact on comprehensive income	(3,059)	A,B,C	-		
Valuation reserves					
- Equity securities designated at fair value with an impact on comprehensive income	-	(*)	-		
- Financial assets (other than equity securities) measured at fair value with an impact on comprehensive income	1,784	(*)	1,784		
- Actuarial gains (losses) relating to defined-benefit pension plans	(3,245)	(*)	-		
Equity instruments	**-**		**-**		
Profits carried forward	**(101,537)**		**-**		
Total	**731,437**				**173**

A = for free capital increase
B = to cover losses
C = for distribution to shareholders
(*) the reserve is unavailable pursuant to Article 6 of Legislative Decree No. 38.2005
(1) only the part of the reserve exceeding the amount necessary for the legal reserve to reach one fifth of the share capital can be distributed (Article 2431 of the Italian Civil Code).
(2) only the part exceeding one fifth of the share capital the reserve can only be used (Article 2430, paragraph 1 of the Italian Civil Code).
(3) the reserve, if not allocated to the capital, may be reduced only in compliance with the provisions of paragraphs 2 and 3 of Article 2445 of the Italian Civil Code. If the reserve is used to cover losses, no profits may be distributed until the reserve is supplemented or reduced accordingly. The reduction must be made by resolution of the extraordinary shareholders' meeting, without observing the provisions of the second and third paragraphs of Article 2445 of the Italian Civil Code. If distributed to shareholders, it contributes to the company's taxable income.

Dividends distributed

Dividends totalling €13.2 million were distributed to shareholders during the period, corresponding to 27 cent for each of the 48,965,086 shares entitled to the dividend for 2018. At the reporting date the Bank holds 1,533,352 treasury shares.

Earnings per share

The method of calculating basic earnings per share is defined in IAS 33 - Earnings per share. Basic earnings per share is defined as the ratio of profit or loss attributable to holders of ordinary equity instruments to the weighted average number of ordinary shares outstanding during the year.

Average number of outstanding shares	30.06.2019	31.12.2018
Weighted average of ordinary shares	48,965,086	48,965,086

There were no outstanding dilutive effects as at 30 June 2019.

Earnings per share	30.06.2019	31.12.2018
Basic earnings per share	(4.15)	0.70
Diluted earnings per share	(4.15)	0.70

Own Funds and Solvency Ratios

	30.06.2019	31.12.2018
A. Common equity tier 1 (CET1) capital prior to the application of prudential filters	**731,436**	**821,981**
of which CET1 instruments subject to transitional arrangements	-	-
B. CET1 prudential filters (+/-)	**(1,013)**	**(1,121)**
C. CET1 gross of deductions and effects of the transitional regime (A +/- B)	**730,423**	**820,860**
D. Elements to be deduced from CET1	**(53,690)**	**(154,412)**
E. Transitional regime – Impact on CET1 (+/-)	**54,948**	**61,412**
F. Total common equity tier 1 (CET1) capital (C – D +/-E)	**731,681**	**727,860**
G. Additional Tier 1 (AT1) capital gross of deductions and effects of the transitional regime	**-**	**-**
of which AT1 instruments subject to transitional arrangements	-	-
H. Items to be deducted from AT1	**-**	**-**
I. Transitional regime – Impact on AT1 (+/-)	**-**	**-**
L. Total Tier 1 (AT1) additional capital (G - H +/- I)	**-**	**-**
M. Tier 2 – T2 capital gross of the elements to be deducted and the effects of the transitional regime	**130,000**	**130,000**
of which T2 instruments subject to transitional arrangements	-	-
N. deductions from T2	**-**	**-**
O. Transitional regime – Impact on T2 (+/-)	**-**	**-**
P. Total tier 2 (T2) capital (M - N +/- O)	**130,000**	**130,000**
Q. Total own funds (F + L + P)	**861,681**	**857,860**

Own funds, risk-weighted assets and solvency ratios as at 30 June 2019 were determined in accordance with the harmonised regulation for banks and investment firms contained in Directive 2013/36/EU (CRD IV) and Regulation (EU) 575/2013 (CRR) of 26 June 2013, transposing into the European Union the standards defined by the Basel Committee on Banking Supervision (the so-called Basel III framework), and on the basis of the Bank of Italy Circulars.

The prudential ratios at 30 June 2019 take account of the adjustments provided for in the transitional provisions for 2019.

Own funds amounted to €861.7 million at 30 June 2019, compared to a weighted asset of €6,228.9 million, deriving mainly from credit and counterparty risks and, to a lesser extent, operational and market risks.

As required by the CRR, the loss for the period was taken into account in the primary Class 1 Capital.

With regard to the introduction of IFRS 9, on 12 December 2017 the European Parliament issued Regulation (EU) 2017/2395, updating the CRR, incorporating the new Article 473-bis "Introduction of IFRS 9", which offers the possibility of mitigating the impacts on own funds arising from the introduction of the new accounting standard.

In this regard, Volksbank has chosen to adopt the so-called "dynamic approach", which permits the re-introduction into the Common Equity Tier I of a progressively decreasing share until 2022 (95% in 2018, 85% in 2019, 70% in 2020, 50% in 2021 and 25% in 2022) of the impact of IFRS 9, calculated net of the tax effect, of the amount of the following two aggregates:

- a comparison between IAS 39 value adjustments as at 31 December 2017 and IFRS 9 value adjustments as at 1 January 2018, excluding the reclassification of financial instruments (including adjustments to stage 3 positions);
- a comparison between value adjustments as at 1 January 2018 and subsequent reporting periods up to 31 December 2022, limited to increases in value adjustments of exposures classified as stage 1 and 2 (excluding adjustments to stage 3 positions).

Regulation (EU) 2017/2395 also governs the reporting requirements that entities are required to publish, referring specific guidelines on the matter to the EBA. In accordance with the regulations, on 12 January 2018 the EBA issued specific guidelines according to which banks adopting transitional treatment in relation to the impact of IFRS 9 are required to publish the consolidated values "Fully loaded" (as if the transitional

treatment had not been applied) and "Transitional" Common Equity Tier 1 (CET1) capital, Tier 1 capital, Total Capital, Total risk-weighted assets, Capital Ratios and Leverage Ratio.

At 30 June 2019, taking into account the transitional treatment adopted to mitigate the impact of IFRS 9, Own Funds amounted to €861.7 million and primary Class 1 Share Capital amounted to €731.7 million, compared with weighted assets of €6,228.9 million, deriving predominantly from credit and counterparty risks and, to a lesser extent, operational and market risks. On the same date, considering the full inclusion of the impact of IFRS 9, Own Funds amounted to €806.7 million, and the Class 1 Primary Capital amounted to €676.7 million, compared with a weighted asset of €6,175.1 million.

Based on the above, the solvency ratios at 30 June 2019 calculated taking into account the transitional treatment for the impact of IFRS 9 ("IFRS 9 Transitional") are as follows: Common Equity ratio 11.7%, Tier 1 ratio 11.7% and Total capital ratio 13.8%. Considering the full inclusion of the impact of IFRS 9 ("IFRS 9 Fully Loaded"), the solvency ratios at 30 June 2019 are as follows: Common Equity ratio 11.0%, Tier 1 ratio 11.0% and Total capital ratio 13.1%.

It should be recalled that on 30 May 2019, Volksbank received the Bank of Italy decision regarding the capital requirements to be met as of 1 January 2019. In fact, the requirements already communicated at the end of the 2017 SREP cycle were confirmed. The total capital requirement to be met in terms of the Common Equity Tier 1 ratio is 7.7%, Tier I Ratio is 9.438% and Total Capital Ratio is 11.75%.

Risk activities and capital requirements	**Unweighted amounts**		**Weighted amounts/requirements**	
	30.06.2019	**31.12.2018**	**30.06.2019**	**31.12.2018**
Categories/Values				
A. RISK ACTIVITIES				
A.1 Credit and counterparty risk	**11,195,354**	**10,596,802**	**5,781,156**	**6,023,307**
1. Standardised Methodology	11,195,354	10,596,802	5,781,156	6,023,307
2. Internal Ratings Based Methodology	-		-	-
2.1 Base	-	-	-	-
2.2 Advanced	-	-	-	-
3. Securitisations	-	-	-	-
B. REGULATORY CAPITAL REQUIREMENTS				
B.1 Credit and counterparty risk			**462,492**	**481,865**
B.2 Credit assessment adjustment risk				**-**
B.3 Settlement risk			**-**	**-**
B.4 Market risk			**830**	**899**
1. Standard Methodology			830	899
2. Internal models			-	-
3. Concentration risk			-	-
B.5 Operational risk			**34,991**	**34,991**
1. Base method			-	-
2. Standardised Method			34,991	34,991
3. Advanced method			-	-
B.6 Other prudential requirements			**-**	**-**
B.7 Other elements of the calculation			**-**	**-**
B.8 Total prudential requirements			**498,313**	**517,755**

RISK ASSETS AND REGULATORY RATIOS		**30.06.2019**	**31.12.2018**
C.1	Risk-weighted activities	6,228,918	6,471,938
C.2	Common Equity Tier 1/Risk-weighted assets (CET 1 capital ratio)	11.75%	11.25%
C.3	Tier 1 capital/Risk-weighted assets (Tier 1 capital ratio)	11.75%	11.25%
C.4	Total capital/risk weighted assets (Total capital ratio)	13.83%	13.26%

SEGMENT REPORTING

Criteria for identifying and aggregating operating segments

Segment reporting is based on the elements that management uses to make its own operating decisions (known as a "management approach") and is therefore consistent with the disclosure requirements of IFRS 8. The segments were identified by management and approved by the Board of Directors:

- Retail
- Corporate
- Private
- Finance
- Workout.

In addition to these operating segments, there are also support structures represented by other central departments and internal services.

The allocation of economic and financial results to the various business sectors is based on criteria that are independent of those used in the preparation of the financial statements. Accordingly, their breakdown is based on the management logic used internally by the Bank to assess the results of the individual operating sectors. For the purposes of preparing the segment report, the data represented in the "Total" column of this section is reconciled with the data indicated in the Half-yearly Report.

Distribution by business segment: economic data

Profit and loss figures	**Retail**	**Corporate**	**Individuals**	**Finance/ALM**	**Workout**	**Head office**	**Total**
(EUR 000)							
Margin of interest income	50,197	27,735	391	17,178	6,486	-	105,256
Margin of interest payable	(4,736)	(602)	(1,013)	(4,776)	-	-	(14,397)
Interest margin	**45,462**	**27,132**	**(622)**	**12,403**	**6,486**	**-**	**90,858**
Net fees	34,990	7,186	2,628	(125)	-	-	44,679
Financial margin	-	-	-	3,976	(13,333)	-	(9,357)
Net receipts from banking	**80,452**	**34,318**	**2,006**	**16,253**	**(6,847)**	**-**	**126,180**
Net adjustments to loans and other fin trans	1,526	824	15	1,387	(60,648)	-	(56,896)
Net result of financial management	**81,978**	**35,143**	**2,021**	**17,640**	**(67,495)**	**-**	**69,284**
Administrative expenses	(52,631)	(7,422)	(2,937)	(1,742)	(3,978)	(20,369)	(89,079)
Provisions for risks and charges	-	-	-	-	-	1,214	1,214
Amortisation of tangible & intangible assets.	-	-	-	-	-	(6,657)	(6,657)
Other operating income/expenses	8,088	1,661	607	-	-	-	10,357
Operating costs	**(44,543)**	**(5,760)**	**(2,330)**	**(1,742)**	**(3,978)**	**(25,812)**	**(84,165)**
Profits (losses) on equity / disposal of investments	-	-	-	-	-	(235)	(235)
Profit (loss) from current operations before tax	**37,435**	**29,382**	**(309)**	**15,898**	**(71,474)**	**(26,046)**	**(15,116)**

Distribution by business segment: balance sheet data

Balance sheet data (€ thousands)	**Retail**	**Corporate**	**Private**	**Finance/ALM**	**Workout**	**Head office**	**Total**
(€ thousands)							
Loans to banks	-	-	-	74,880	-	-	74,880
Loans to customers	4,461,844	2,408,827	43,273	1,443,760	329,571	-	8,687,275
Financial assets measured at fair value	50,642	27,340	491	937,680	-	-	1,016,153
Payables to banks	-	-	-	1,351,653	-	-	1,351,653
Direct deposits	5,321,057	832,786	649,791	1,087,245	-	131,298	8,022,177
- Due to customers	4,939,291	831,146	559,546	955,816	-	119,800	7,405,599
- Securities issued	381,766	1,640	90,245	131,429	-	11,498	616,578
Indirect deposits	2,167,234	80,569	858,252	-	-	-	3,106,056
RWA	2,508,332	2,365,849	64,531	409,297	468,731	411,881	6,228,918

It should be noted that the company's operating income is earned and its activities are performed in Italy, confirming its roots in its territory of origin, a factor of strategic importance in the company's development.

With respect to information by geographical segment, Volksbank operates on a regional basis and does not have a geographical structure that is divided into separate areas of economic and strategic importance. Furthermore, the characteristics and opportunities of the reference market are also homogeneous. Therefore, no segment reporting by geographical area is presented, as it does not have any particular value.

INFORMATION ON VOLKSBANK SHARES

As at 30 June 2019, there were 48,965,086 outstanding shares. On the same date, the Company held 1,533,352 treasury shares. Therefore, a total of 50,498,438 shares have been issued.

DISCLOSURE OF PAYMENT AGREEMENTS BASED ON OWN EQUITY INSTRUMENTS

A. Qualitative disclosure

The reference legal framework for payment agreements based on own shares is represented by the supervisory provisions for banks, Bank of Italy Circular No. 285/2013, Part One, Title IV, Chapter 2 "Remuneration and Incentivisation Policies and Practices", which implements the European Directive 2013/36/EU (CRD IV-Capital Requirements Directive). The following are also highlighted:

- Article 114-bis of the Italian Consolidated Finance Act on market disclosure;
- the joint communication from the Bank of Italy and Consob concerning the "Implementation of guidelines issued by ESMA", aimed at promoting greater consistency in the interpretation and fulfilment of existing obligations regarding conflicts of interest pursuant to the MiFID on remuneration, published on 29 January 2014;
- the technical requirements, Regulatory Technical Standard (RTS) defined by the EBA for the identification of the categories of personnel whose professional activities have a significant impact on the company's risk profile, approved on 4 March 2014 by the European Commission under Commission Delegated Regulation (EU) No. 604/2014; Regulation (EU) No. 575/2013 (CRR) on prudential requirements for credit institutions and investment firms, and indicating in Article 450 information to be published on remuneration policies;
- EU Delegated Regulation No 527/2014 specifying the categories of financial instruments appropriate for use for the purposes of variable remuneration.

Finally, it should be noted that the Guidelines on Sound Remuneration policies published by the EBA on 21 December 2015 apply as of 1 January 2017. The Guidelines aim to promote the adoption of remuneration policies in line with the Bank's risk profile and, in general, to ensure that remuneration and incentive systems are always guided by the principles of sound and prudent management.

With the 25th update of Circular no. 285/2013 published on 26 October 2018, the Bank of Italy took action to amend the provisions of Part 1, Title IV, Chapter 2 concerning the policies and practices for remuneration and incentives for banks and banking groups in order to adapt the Italian regulatory framework to the European Banking Authority (EBA) Guidelines on this matter.

On 22 February 2019, the Volksbank Board of Directors approved a new incentive plan that provides, *inter alia*, for the valuation of a portion of the variable component of remuneration of "key personnel" by allocating ordinary shares of Volksbank, conditional on the achievement of specific objectives to be achieved during the year.

The beneficiaries of the plan are the entities that come within the categories of the "Key Personnel", who are granted, pursuant to the Remuneration Policies, incentives in financial instruments representative of the Bank's economic value with a net amount equivalent to more than €15,000 per year, or employees, although not Key Personnel, who possess "severance" incentives as governed by the Remuneration Policies.

The stock allocation of the Stock Grant Plan is subject to the achievement of the performance targets for the 2019 financial year and compliance, for the individual periods of the plan, with the economic-financial, capital and bank liquidity ratios as indicated in the remuneration policies.

Shares may be granted if and only if, at the end of each period of the plan, the economic-financial, capital and liquidity ratios that constitute the "access conditions" to the incentive system are achieved. Under these conditions, 25% of the 2019 incentive is paid in shares provided that, in the year in which the units are allocated, the equivalent value in shares exceeds the materiality threshold indicated in the remuneration policies.

The shares are subject to a retention commitment with unavailability equal to one year from the date of allocation of the shares. For the shares to be recognised in relation to financial year 2019 together with the shares of one or more periods of the 2019 plan, the unavailability interval is 1 year from the date of the Board's resolution to ascertain the existence of the Bank's economic-financial, equity and liquidity indices necessary to access the portion of the deferred incentive respectively in 2020 and 2021.

For shares servicing the severance agreed with an individual agreement for early termination of employment, the retention undertaking has an annual duration, for spot assignments and a term of 1 year for deferred assignments of 1 or 2 years, respectively.

B. Quantitative disclosures

The table of annual changes is not corroborated because the Bank did not meet the requirements for share-based payment in relation to the performance premiums for the year 2019 to be paid in 2020.

BUSINESS COMBINATIONS INVOLVING COMPANIES OR BUSINESS UNITS

Transactions undertaken during the period

No business combinations were undertaken during the half-year.

Transactions undertaken after the end of the period

No business combinations were undertaken after the end of the half-year.

RELATED-PARTY TRANSACTIONS

Information on the remuneration of Directors and key employees

The following table sets out the remuneration paid to directors, statutory auditors, strategic executives and key employees, i.e. those with the power and responsibility, directly or indirectly, for planning, managing and controlling the company's activities.

Remuneration paid is governed by the Remuneration Policies approved by resolution of the shareholders' meeting.

Remuneration *(€ thousands)*	**30.06.2019**
Directors	511
Auditors	175
Key Employees	1,796
Total	**2,482**

Key Employees *(€ thousands)*	**30.06.2019**
of which	
- short-term benefits	1,571
- post-employment benefits	150
- other long-term benefits	75
- benefits payable to employees upon termination of employment	-
- share-based payments	-
Total	**1,796**

Information on transactions with related parties

According to the indications of IAS 24, applied to the organisational and governance structure of the Bank, the following natural and legal persons are considered to be related parties:

- subsidiaries, companies over which the Bank directly or indirectly exercises control, as defined in IAS 27;
- associated companies, companies in which the Bank exercises significant direct or indirect influence, as defined by IAS 28;
- jointly controlled companies, companies over which the Bank exercises direct or indirect joint control, as defined by IAS 31;
- executives with strategic responsibilities and control bodies, i.e. directors, statutory auditors, the general manager, the deputy general manager;
- other related parties, which include:
  - immediate family members (cohabitants, children, cohabitant children, dependants of the person concerned or cohabitant) of Directors, Statutory Auditors, General Manager and the Deputy General Manager of the Bank;
  - subsidiaries, jointly controlled companies or companies subject to significant influence by the Directors, Statutory Auditors, General Manager and Deputy General Manager of the Bank and their close relatives as defined above.

The main capital and economic relationships with subsidiaries and affiliates are indicated below.

Transactions with subsidiaries

(€ thousands)	Loans granted	Bonds subscribed	Payables for loans received	Bonds issued	Guarantees	Pledges
30.06.2019	9,190	-	1,555	-	22	-
Incidence	*0.13%*	*0.00%*	*0.02%*	*0.00%*	*0.00%*	*0.00%*
	Interest income on loans granted	**Interest income on subscribed bonds**	**Interest expense on loans received**	**Interest expense on bonds issued**	**Fees and other revenues**	**Fees and other costs**
I semester 2019	55	-	-	-	3	-
Incidence	*0.05%*	*0.00%*	*0.00%*	*0.00%*	*0.01%*	*0.00%*

Transactions with associated companies

(€ thousands)	Loans granted	Bonds subscribed	Payables for loans received	Bonds issued	Guarantees	Pledges
30.06.2019	470	-	57	-	-	-
Incidence	*0.01%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*
	Interest income on loans granted	**Interest income on subscribed bonds**	**Interest expense on loans received**	**Interest expense on bonds issued**	**Fees and other revenues**	**Fees and other costs**
I semester 2019	2	-	-	-	2	-
Incidence	*0.00%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*

The main financial and economic relationships existing with directors, statutory auditors and members of the General Management are indicated below.

Transactions with Directors, Statutory Auditors, members of the general management and central departments

Data as of 30.06.2019 *(€ thousands)*		Directors		Auditors		Strategic Executives		Total
		Direct	**Indirect**	**Direct**	**Indirect**	**Direct**	**Indirect**	
Credit granted		52,290	16,544	580	990	20	372	70,795
Loans		38,724	14,820	403	611	5	66	54,629
	Incidence	*0.53%*	*0.20%*	*0.01%*	*0.01%*	*0.00%*	*0.00%*	*0.75%*
Unsecured credit		2,728	6,201	-	12	-	-	8,942
	Incidence	*0.44%*	*1.00%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*	*1.44%*
Direct deposits		21,374	2,783	528	311	152	164	25,312
	Incidence	*0.27%*	*0.03%*	*0.01%*	*0.00%*	*0.00%*	*0.00%*	*0.32%*
Indirect deposits		1,707	8,169	25	14	2	200	10,118
	Incidence	*0.05%*	*0.22%*	*0.00%*	*0.00%*	*0.00%*	*0.01%*	*0.28%*
Interest received		472	188	4	6	0	0	670
	Incidence	*0.45%*	*0.18%*	*0.00%*	*0.01%*	*0.00%*	*0.00%*	*0.64%*
Interest paid		20	0	0	0	0	0	21
	Incidence	*0.14%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*	*0.00%*	*0.15%*
Commission and other income		49	21	2	6	0	1	79
	incidence	*0.10%*	*0.04%*	*0.00%*	*0.01%*	*0.00%*	*0.00%*	*0.16%*

Management of Related Party Transactions

Transactions with related parties are governed by the Consob Regulation referred to in Resolutions No. 17221 of 12 March 2010 and No. 17389 of 23 June 2010, and by the Bank of Italy Provisions of 12 December 2011 entitled "Risk activities with related parties".

By resolution of the Board of Directors, after obtaining the favourable opinion of the Committee of Independent Directors and of the Board of Statutory Auditors, the Bank adopted internal regulations on risk activities and conflicts of interest in relation to related parties and related party control policies, authorised by the Board of Directors on 23 October 2015 and posted on the Bank's websites www.bancapopolare.it and www.volksbank.it.

Transactions with related parties, identified in accordance with the provisions of IAS 24, the aforementioned Consob Regulation and the Bank of Italy's instructions, are part of the Bank's normal operations.

No related-party transactions undertaken in the period under review had a material impact on the Bank's financial position or results of operations. In addition, there were no changes to and/or developments in related-party transactions concluded by 30 June 2019.

In the first half of 2019, there were no significant non-recurring transactions subject to the regulations of related parties. Furthermore, no positions or transactions arising from atypical or unusual transactions were reported within the period,, i.e. any transactions that are extraneous to the normal management of the company, which due to their significance/relevance, the nature of the counterparties, the method of determining the transfer price and its timing of occurrence, could give rise to doubts as to the completeness of the information in the financial statements, the safeguarding of the company's assets, or the protection of shareholders.

CERTIFICATION OF THE ABRIDGED HALF-YEARLY REPORT PURSUANT TO ART. 81-TER OF CONSOB REGULATION NO. 11971 DATED 14 MAY 1999, AS AMENDED

1. The undersigned, Otmar Michaeler, as Chairman of the Board of Directors of Banca Popolare dell'Alto Adige, a joint-stock company, and Alberto Caltroni, as the Manager responsible for the preparation of corporate accounting documents for Banca Popolare dell'Alto Adige joint-stock company, certify, taking account of the provisions of art. 154-bis, paragraphs 3 and 4 of Italian Legislative Decree no. 58 of 24 February 1998:

   the adequacy with reference to the characteristics of the enterprise and

   the effective application

   of the administrative and accounting procedures for forming the abridged half-yearly report, during the first half of 2019.

2. It is further certified that:

   2.1. the abridged half-yearly report:

   a) was drawn up in compliance with the applicable international accounting principles accepted within the European Community pursuant to Regulation (EC) no. 1606/2002 of the European Parliament and of the Council, dated 19 July 2002;

   b) corresponds to the records in the accounting books and entries;

   c) is suited to providing a true and correct view of the equity, income and cash flow position of the issuer.

   2.2. The interim directors' report includes a reliable analysis of references to the major events occurring in the first six months of the year and their impact on the abridged half-yearly report, together with a description of the main risks and uncertainties for the remaining six months of the year. The interim directors' report also includes a reliable analysis of the disclosure on transactions with related parties.

Bolzano, 9 August 2019

Chairman of the Board of Directors

Otmar Michaeler

Manager responsible for the preparation of corporate accounting documents

Alberto Caltroni

REPORT OF THE INDEPENDENT AUDITORS

(Translation from the Italian original which remains the definitive version)

Report on review of condensed interim financial statements

To the board of directors of
Banca Popolare dell'Alto Adige S.p.A.

INTRODUCTION

We have reviewed the accompanying condensed interim financial statements of Banca Popolare dell'Alto Adige S.p.A., comprising the statement of financial position as at 30 June 2019, the income statement and the statements of comprehensive income, changes in equity and cash flows for the six months then ended and notes thereto. The bank's directors are responsible for the preparation of these condensed interim financial statements in accordance with the International Financial Reporting Standard applicable to interim financial reporting (IAS 34), endorsed by the European Union. Our responsibility is to express a conclusion on these condensed interim financial statements based on our review.

SCOPE OF REVIEW

We conducted our review in accordance with International Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity". A review of condensed interim financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing (ISA Italia) and, consequently, does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion on the condensed interim consolidated financial statements.

CONCLUSION

Based on our review, nothing has come to our attention that causes us to believe that the condensed interim financial statements of Banca Popolare dell'Alto Adige S.p.A. as at and for the six months ended 30 June 2019 have not been prepared, in all material respects, in accordance with the International Financial Reporting Standard applicable to interim financial reporting (IAS 34), endorsed by the European Union.

Bolzano, 9 September 2019

KPMG S.p.A.

(signed on the original)

Andrea Rosignoli
Director of Audit