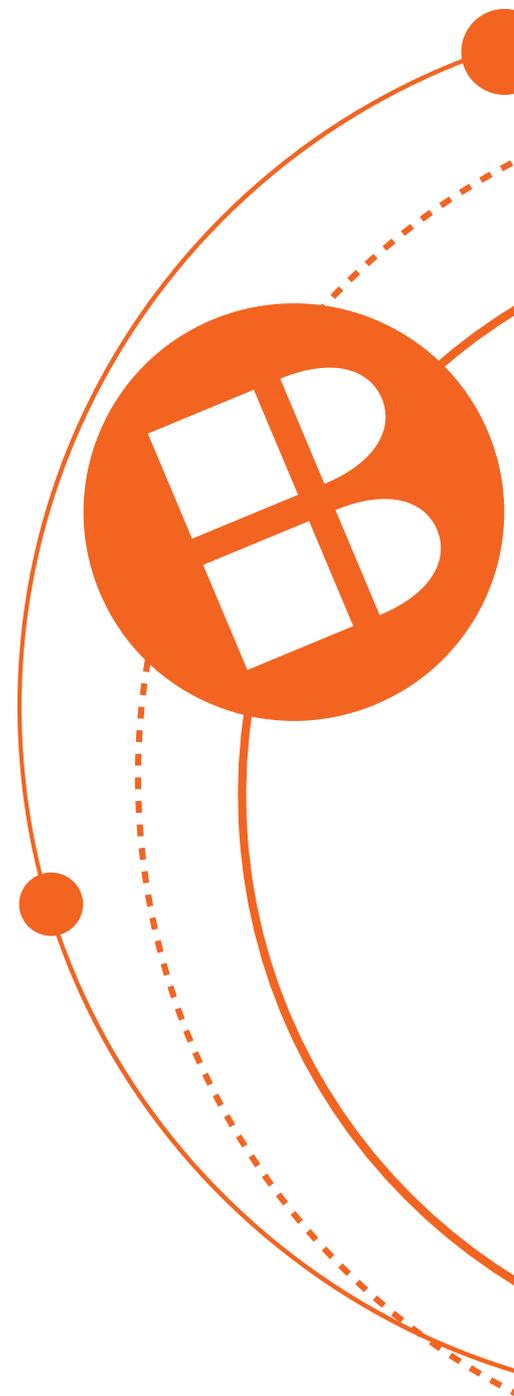


ANNUAL REPORT

2018

 **HIPOTEKARNA
BANKA**

Vama posvećena

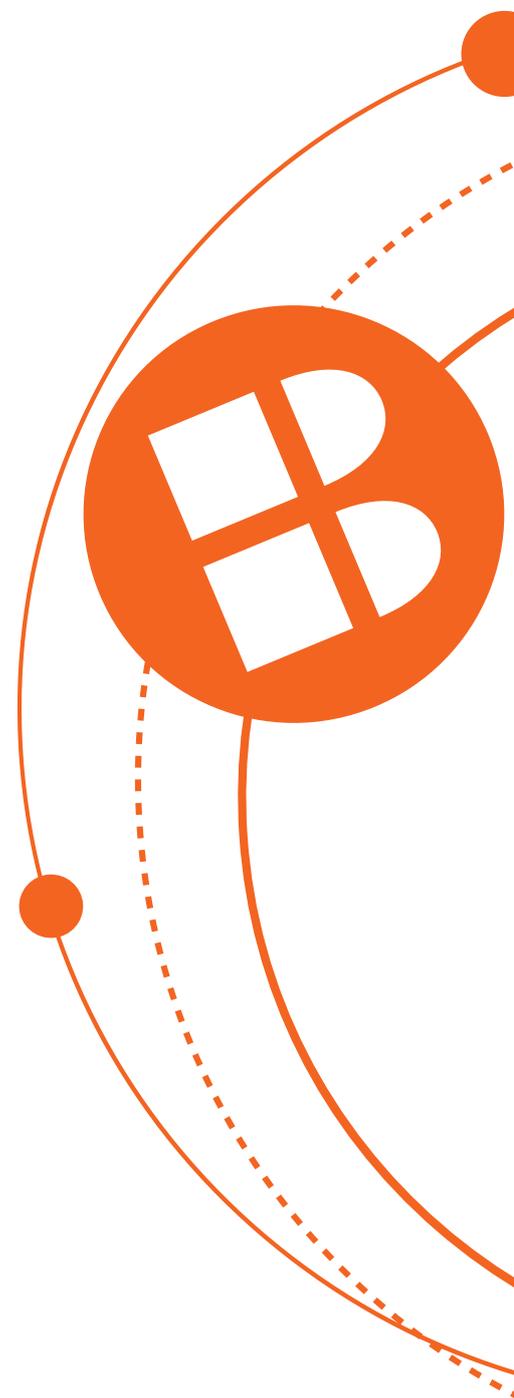


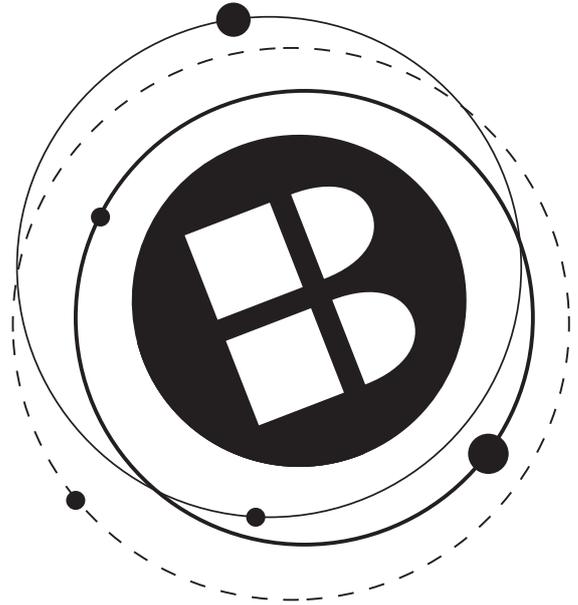
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1 FROM THE EXTERNAL AUDITOR REPORT



Društvo za reviziju Crowe MNE d.o.o. Podgorica

Žiro račun: 520-34559-91; Reg. broj: 5-0803037/1 PIB: 03152324; PDV: 30/31-17725-0
Vučedolska 7, 81 000 Podgorica

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Hipotekarna banka AD Podgorica

We have audited the accompanying financial statements of Hipotekarna Banka AD, Podgorica (hereinafter: "the Bank"), which comprise the balance sheet as at 31 December 2018, income statement, statement of changes in equity and cash flow statement for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and true and objective presentation of these financial statements in accordance with the Law on accounting of Montenegro, and other applicable legislation that regulates financial reporting of banks in Montenegro, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the applicable legislation that regulates audit of financial statements in Montenegro. This legislation which regulates accounting and auditing require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the separate financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the separate financial statements, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the entity's preparation and objective presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the separate financial statements.

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

Opinion

In our opinion, separate financial statements present truly and objectively financial position of the Bank as at 31 December 2018, financial performance and cash flows for the year then ended in accordance with the Law on accounting of Montenegro and other applicable legislation that regulates financial reporting of banks in Montenegro



Društvo za reviziju Crowe MNE d.o.o. Podgorica

Žiro račun: 520-34559-91; Reg. broj: 5-0803037/1 PIB: 03152324; PDV: 30/31-17725-0
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INDEPENDENT AUDITOR'S REPORT (CONTINUED)

To the Shareholders of Hipotekarna banka AD Podgorica (continued)

Other matter

The financial statements of the Bank as at and for the year ended 31 December 2017 were audited by another auditor, who expressed in his report dated 28 May 2018 an unmodified opinion on these financial statements.

Report on other legal and law requirements

Management of the Bank is responsible for the preparation and presentation of the Annual Management Report.

Our opinion on financial statements does not include the Annual Management Report and except to that extent that is explicitly stated in our report we do not express any form of conclusion with the expression of an assurance about them

In connection with our audit of the financial statements, our responsibility is to read the Annual Management Report and, in doing so, consider whether the Annual Management Report is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

In accordance with the requirements of the Law on Accounting in Montenegro we considered whether the Annual Management Report has been prepared in accordance with the requirements of Articles 11, 12, 13 and 14 of that Law.

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

- the information given in the Annual Management Report for the financial year for which the financial statements are prepared, is consistent with the financial statements;
- the Annual Management Report has been prepared in accordance with the requirements of Articles 11, 12, 13 and 14 of the Law on Accounting in Montenegro.

In addition, in light of the knowledge and understanding of the Bank and its environment obtained in the course of the audit, we are also required to report if we have identified material misstatements in the Annual Management Report. We have nothing to report in this respect.

Crowe MNE d.o.o. Podgorica

24 May 2019




Đorđe Dimić, Certified Auditor

(License no. 072 issued 9 March 2017)

BALANCE SHEET

In the period from 1 January to 31 December 2018
(In thousand EUR)

	<u>Note</u>	<u>2018</u>	<u>2017</u>
Interest income and similar income	3.1, 7	18,768	18,650
Interest income on impaired placements		-	-
Interest expense and similar expenses	3.1, 7	<u>(3,679)</u>	<u>(4,685)</u>
NET INTEREST INCOME		15,089	13,965
Fee and commission income	3.2, 9	14,489	12,017
Fee and commission expenses	3.2, 9	<u>(7,328)</u>	<u>(5,880)</u>
NET FEE AND COMMISSION INCOME		7,161	6,137
Net profit/loss from derecognition of financial instruments not measured at fair value through income statement.		105	300
Net foreign exchange gains		698	652
Net income/(expenses) based on derecognition of other assets		78	152
Other income	13	278	414
Staff costs	10	(5,173)	(4,807)
Depreciation/amortization cost	12	(955)	(836)
General and administrative costs	11	(8,761)	(8,224)
Net income/(expenses) based on impairment of financial instruments not valued at fair value through income statement	3.8.8, 8	(3,563)	(3,378)
Provision cost	3.14	(62)	11
Other expenses	14	(174)	(35)
OPERATING PROFIT		4,721	4,351
Income tax	3.6, 15	411	408
NET PROFIT		4,310	3,943

Notes to the following pages form an integral part of these financial statements

These financial statements are approved on behalf of Board of Directors of Hipotekarna banka A.D., Podgorica, as at 20 May 2019 in Podgorica.

Signed and approved on behalf of Hipotekarne banke A.D., Podgorica:

Esad Zaimović
Chief executive officer

Ana Golubović
Executive Director for Corporate

Jelena Vuletić
Executive Director for Risks

Nikola Špadijer
Executive director for retail

BALANCE SHEET
As at 31 December 2018
(In thousand EUR)

	Note	31 December 2018	31 December 2017
ASSETS			
Cash and deposit accounts held with central banks	3.7, 16	129,048	131,166
Financial assets at amortized value		257,272	265,721
Loans and receivables from banks	3.8.3, 17.1	25,110	50,152
Loans and receivables from clients	3.8.3, 17.2	230,313	215,438
Other financial assets		1,849	131
Financial assets at fair value through other comprehensive income		114,467	92,572
Securities	18.1	114,467	92,572
Investments in associates and joint ventures at equity method		5	8
Property, Plants and Equipment	3.10, 19	2,062	1,437
Intangible assets	3.10, 20	1,766	1,658
Deferred tax assets	15c	30	38
Other assets	21	2,188	1,935
TOTAL ASSETS		506,838	494,535
LIABILITIES			
Financial liabilities not valued at amortized cost		436,956	424,652
Deposits due to banks and Central banks	22.1	1,410	3,059
Deposits due to clients	22.2	410,316	391,657
Borrowings from clients which are not banks	22.3	25,230	29,936
Reserves	23	1,831	1,636
Current tax liabilities		417	451
Deferred tax liabilities	15c	43	311
Other liabilities	24	7,970	8,692
Subordinated debt	26	14,039	14,012
TOTAL LIABILITIES		461,256	449,754
EQUITY			
Share equity	25	16,006	16,006
Share issue premium		7,444	7,444
Retained earnings		16,235	4,831
Profit for the current year		4,310	3,943
Other reserves		1,587	12,557
TOTAL EQUITY		45,582	44,781
TOTAL EQUITY AND LIABILITIES		506,838	494,535
OFF – BALANCE SHEET	28	661,802	574,581

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Executive director for retail

TRANSLATION NOTE: This is a translation of the original document issued in the Montenegrin language. All due care has been taken to produce a translation that is as faithful as possible to the original. However, if any questions arise related to interpretation of the information contained in the translation, the Montenegrin version of the document shall prevail.

STATEMENT OF CHANGES IN EQUITY

In the period from 1 January to 31 December 2018

In thousand EUR	Share capital	Share issue premium	Profit	Other reserves	Total
Balance as at January 2017	16,006	7,444	5,462	9,930	38,842
Effects on the market value of securities available for sale	-	-	-	1,996	1,996
Transfer of the profit	-	-	(631)	631	-
Profit of the current year	-	-	3,943	-	3,943
Balance as at 31 December 2017	16,006	7,444	8,774	12,557	44,781
Effect of IFRS 9	-	-	(1,914)	(271)	(2,185)
Corrected balance as at 1 January 2018	16,006	7,444	6,860	12,286	42,596
Effect on the fair value of financial assets through other comprehensive income	-	-	-	(1,321)	(1,321)
Other impact of securities to the Equity	-	-	(3)	-	(3)
Transfer of the profit	-	-	9,378	(9,378)	-
Profit of the current year	-	-	4,310	-	4,310
Balance as at 31 December 2018	16,006	7,444	20,545	1,587	45,582

Notes to the following pages form an integral part of these financial statements

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STATEMENT OF CASH FLOWS

In the period from 1 January to 31 December 2018
(In thousand EUR)

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities		
Inflows from interest and similar income	18,178	17,608
Outflows from interest and similar expense	(3,423)	(4,814)
Inflows from fees and commissions	15,966	12,972
Outflows from fees and commissions	(7,328)	(5,880)
Outflows based on earnings of the employees and costs for suppliers	(20,693)	(13,504)
Increase/decrease of the loans and other assets	(24,577)	(1,890)
Inflow/outflow based on deposits and other liabilities	15,837	61,903
Paid tax	(961)	(902)
Other income	<u>(36,689)</u>	<u>(14,462)</u>
Net cash inflow / outflow from operating activities	(43,690)	51,031
Cash flows from investing activities		
Purchase of property and equipment	(1,326)	(519)
Purchase of intangible assets	(430)	(688)
Treasury bills	15,534	17,422
Income from sale of tangible and fixed assets	<u>67</u>	<u>3</u>
Net cash inflow / outflow from investing activities	13,845	16,218
Cash flows from financing activities		
Increase in borrowings	<u>(4,680)</u>	<u>(1,372)</u>
Net cash (outflow)/inflow from financing activities	(4,680)	(1,372)
Effects of foreign exchange in cash and cash equivalents	698	651
Net (decrease)/increase in cash and cash equivalents	<u>(33,827)</u>	<u>66,528</u>
Cash and cash equivalents, beginning of year	182,996	116,468
Cash and cash equivalents, end of year	<u>149,169</u>	<u>182,996</u>

Notes to the following pages form an integral part of these financial statements

These financial statements are approved on behalf of Board of Directors of Hipotekarna banka A.D., Podgorica, as at 20 May 2019 in Podgorica.

Signed and approved on behalf of Hipotekarne banke A.D., Podgorica:

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CAPITAL

As at 31 December 2018, total capital of the Bank amounted to 45,582 million euros. It increased y-o-y by 1.79%.

The nominal value of share capital amounted to 16,006 million euros as at 31 December 2018.

Share capital consisted of 31,305 shares, nominal value of each share was 511.29 euros.

With regard to the ownership structure of the Bank, foreign legal and natural persons accounted to 75% of share capital, while the remaining portion of share capital was owned by domestic legal and natural persons.

PROFIT AND LOSS STATEMENT

In 2018, the Bank reported profit in the amount of 4,310 million euros. Interest income increased y-o-y by 0.63%, and they amounted to 18,768 million euros, which resulted from the increase in lending activity.

Fee income increased y-o-y 20.57% and they amounted to 14,489 million euros. Net fee income stood at 38.45% of net income from regular operations of the Bank.

Other income fell y-o-y by 23.61% and it amounted to 1,159 million euros.

Expenses from regular operations, including depreciation, amounted to 15,063 million euros and they increased by 8.36% compared to the previous year. Increase in expenses was due to the expansion of business network, new number of employees as well as the increase in other expenses following the growth and development of the Bank.

Credit risk assessment and provisioning for risk loans and contingent liabilities of the Bank are based on the implementation of the principles of conservative policy and prevailing laws and regulations.

As at 31 December 2018, total reserves for assets and liabilities positions amounted to 16,762 million euros.

DISTRIBUTION OF PROFIT

The Board of Directors, upon the proposal of the management of the Bank, proposed to the General Meeting not to distribute profit in 2018 in order to increase total capital of the Bank.

INDICATORS

As at 31 December 2018, the position of the Bank in the Montenegrin banking system, according to the last, publicly known, data on financial reports of all banks in Montenegro was as follows:

- market share: the Bank ranked 4th, i.e. 11.50% of market share;
- portfolio of loans and receivables from banks and clients: the Bank ranked 5th i.e. 9.16% of market share;
- securities portfolio: the Bank ranked 1st i.e. 22.13% of market share;
- deposit portfolio: the Bank ranked 2nd, i.e. 11.86% of market share;
- net profit: the Bank ranked 5th.

Financial indicators as at 31 December 2018:

- * ROAA – 0.86%
- * ROAE – 9.54%
- * SSB – 37,034 million euros
- * Solvency ratio – 12.50%.

Business Practice: The Bank is not oriented towards financing or participating in projects that pollute or degrade the environment. However, the Bank finances and actively supports / participates in the financing of projects that provide environmental protection, in particular through the introduction of more energy efficient technologies. Also, the Bank's business practice is financing clients' projects / business goals, which pose the least possible environmental risk.

In carrying out its activities, the Bank takes care of the rational use of natural resources, that is, of providing environmental protection measures.

Particular attention was paid to this segment when using loans from the credit lines of the European institutions, primarily the European Bank for Reconstruction and Development (EBRD).

PLANNED FUTURE DEVELOPMENT

According to the available data in 2017, high level of liquidity and solvency, together with the growth of key balance sheet indicators characterizes the Montenegrin banking sector and contributes to its smooth functioning, thus preserving and strengthening financial stability. A sound banking sector and positive macroeconomic developments in 2017 are encouraging assumptions for further growth and development in 2018.

We estimate that in 2018, the legal framework in which banks operate, on the one hand, and customer needs, on the other, will be even more challenging.

Since the needs of the economy and the population for modern financial services are evident, primarily due to the drastic fall in interest rates, we are continuing our business activities, which are based on creativity and innovation. Therefore, we are focused on generating new financial services that are intended to fill in that space, in accordance with the applicable legal framework and best business practice. For clients, we provide services related to instruments characterized by liquidity and flexibility, relative to traditional banking products. Instead of deposits, as standard products offered to citizens and businesses, we plan to offer our clients a new form of investment. Professional consulting and managing of clients' assets will be an integral part of our future offer, given the long-standing experience we have gained in investing, creating and managing financial assets of the Bank and professional staff with expert knowledge acquired in international markets.

RESEARCH, DEVELOPMENT AND INVESTMENT IN EMPLOYEE EDUCATION

The Bank continuously monitors and participates in market research as well as analyses published by reputable agencies, so that it uses the information obtained to position the brand.

The key elements of success and our organizational culture are based on the knowledge, skills and dedication of our employees. Therefore, the Bank continually plans to develop and improve the skills of its employees, both by organizing trainings, with the help of experienced, competent employees, and by hiring reputable foreign consultants / consulting firms specialized in human resources management. We particularly consider it important to emphasize expert training seminars for our sales staff, that is, employees in positions where communication with clients is most commonly accomplished, with the aim of improving their communication skills, styles adapted to different stages of that communication, as well as further developing of skills for understanding clients' needs, which is in their best interest. In addition, the Bank is committed to the concept of continuous development of employees

in managerial positions, thus hiring external consulting teams to improve their skills in accordance with modern standards.





2 OVERVIEW OF MONTENEGRIN ECONOMY IN 2018

MACROECONOMIC DEVELOPMENTS

The macroeconomic area continued to show success from the previous years, showing growth of GDP of about 4.8% in 2018, which was 0.2% higher than in 2017. This growth rate was higher compared to the regional countries as well as compared to the average growth recorded in the Euro area countries and the EU. In 2018, inflation was 1.6%. The tourism, industry and construction recorded growth in their activities in the previous year, while forestry showed a decline in its activities. Positive trends were also recorded at labour market which experienced an increase in the number of employed persons and a decline in the number of unemployed persons in 2018. The banks were highly liquid, while interest rates reached their nadir. Loans and deposits also grew in the previous year.

FISCAL POLICY AND CREDIT RATING

In 2018, fiscal policy was focused on the implementation of fiscal consolidation measures. In 2018, the State Budget receipts amounted to 2,875.8 million euros or 62.5% of the estimated GDP for 2018 (4,604.5 million euros). Preliminary source revenues amounted to 1,746.4 million euros, while 1,129.5 million euros was received from other sources of financing, primarily from borrowings at foreign market. Budget revenues recorded the y-o-y increase of 180.1 million euros or 11.5%. The significant y-o-y increase in revenues resulted from the implemented fiscal consolidation measures, whereas all important categories of tax revenues recorded growth over one-year period. According to the preliminary data, the government debt amounted to 3,152.98 million euros or 68.48% of GDP at end-2018.

During Q2 2018, Montenegro issued Eurobonds in the amount of 500 million euros, of which 362.35 million euros were used to refinance bonds maturing in 2019, 2020 and 2021. In addition, a credit arrangement for budget funding in the amount of 250 million euros was signed in Q2 2018. This was a commercial arrangement that is supported by the World Bank guarantee.

Current credit ratings of the external credit rating agencies are given below.

S&P – Rating: **B+**; Outlook: Stable; the rating was given in May 2018.

Moody's - Rating: **B1**; Outlook: Stable; the rating was given in May 2018.

In 2018, average inflation rate, measured by the consumer price index, amounted 1.6%.

INFLATION RATE

INDUSTRIAL OUTPUT

In 2018, industrial output recorded a y-o-y growth of 22.4%. The growth was recorded in the manufacturing industry (12.1%) and electricity, gas and steam supply (62.1%). The decline in output was recorded in the mining and quarrying (-21,3%). In the comparative period, the largest increase in the manufacturing industry was recorded in the production of other non-metal minerals products (49.7%). The production growth in the electricity supply resulted from favourable weather conditions and beginning of operations of new production capacities (wind farm Krnovo).

TOURISM, CONSTRUCTION, TRANSPORT AND FORESTRY

In 2018, tourist arrivals and overnights continued trending upward, resulting in 2 million tourists who visited Montenegro in 2018, which was by 10.3% more than in the previous year. In total, almost 13 million tourist overnights were made, which is by 8.2% more than in 2017. According to the Central Bank's preliminary data, revenues from tourism (foreign tourists) amounted to 1 billion euros, which was by 8.6% more than in 2017. In 2018, the construction industry also saw a significant year-on-year increase in the value of executed construction works of 24.9%. In the reporting period, the growth was also recorded in transport (primarily due to the growth of passengers' turnover at the airports by 12.3%), while the forestry recorded output fall of 15.6%.

BANKING SECTOR

The banking sector accounted for the main share in the structure of financial sector assets. In 2018, the banking sector was stable, adequately capitalised, and its liquidity was at the satisfactory level. All prudential safety indicators of the sector were above the statutory minimum. A positive trend of almost continuous decline in non-performing loans and receivables from the previous period continued as well. A high level of liquid assets, growth in total deposits and loans, as well as recapitalisation of a number of banks additionally contributed to the stability of the banking system.

At the end of December 2018, total assets of banks amounted to 4.4 billion euros and they grew about 5.39% compared to the end of 2017 when it amounted to 4.2 billion euros. Loans and receivables from banks and clients, as the most important item of aggregate balance sheet of banks, amounted to 2.9 billion euros and showed a y-o-y growth of 8.51%. At the end of 2018, total deposits were 3.5 billion euros and their growth was about 5.88%. Total capital of banks amounted to 516.8 million euros at the end of 2018 and it increased by 0.55% in the comparative period. Aggregate solvency ratio was 17.23% at the end of 2018. The banking system reported profit in the amount of 28 million euros at the end of December 2018, whereby four of fifteen banks in the system reported negative financial result. At the end of 2018, two banks that were under interim administration reported loss of 23 million euros. If these two banks are excluded, the financial result of the system would be 51 million euros.

CAPITAL AND INSURANCE MARKETS

In 2018, total premium of insurance companies operating in Montenegro amounted to 71.4 million euros, which was a decline by about 12.28% compared to the end of 2017. The insurance sector continued with profitable operations, and all nine insurance companies reported net income of 5.8 million euros.

In 2018, total turnover at the Montenegro Stock Exchange amounted to 147,355,442 euros, which was a y-o-y increase of 210%. This increase resulted from the block trades with shares of Electricity Company of Montenegro (Elektroprivreda Crne Gore AD), which share in this turnover amounted to 82% (about 120 million euros). The 2018 data on the number of concluded deals showed a decline of about 43% resulting in an inactive market in 2018.

MONEX 10, which monitors the trend in 10 most liquid companies in the market, reported growth of about 7.77% in the previous year, and its value at the last trading day was 837.08 points.

FOREIGN DIRECT INVESTMENTS

According to the preliminary data, net foreign direct investments amounted to 327.6 million euros in 2018, which was a y-o-y decline of 32.4%. This trend was the result of substantially higher outflow based on the repayment of intercompany debt as well as withdrawal of equity investments of a

major company compared to the same period 2017, while total FDI inflows increased (by 27.9%), which significantly eased the decline of net FDI inflows. The 2018 portfolio investment account saw a net inflow of 135 million euros. In the comparative period, other investments reported a net inflow of 451.8 million euros, as a result of significant increase in liabilities on loans taken and increase in deposits of non-residents with domestic banks.

EMPLOYMENT

Monstat records showed that the number of employed persons in 2018 amounted to 194,085 being 0.3% lower than in the previous month and 9.3% higher compared to December 2017. In 2018, the number of employed persons grew by 4.3%, y-o-y. The growth in the number of employed persons in 2018 was recorded in thirteen out of nineteen sectors, with the highest growth recorded in the administrative and ancillary service activities (13.5%) and construction (12.5%), while the highest fall was recorded in agriculture, forestry and fishing (-12.9%). In December 2018, the largest number of persons was employed in the following sectors: wholesale and retail trade, repair of motor vehicles and motorbikes (19.8%), government administration and defence, compulsory social security (11.3%).

The Employment Agency of Montenegro registered 41,378 unemployed persons at end-2018, which represented the y-o-y decrease of 19.3%.

AVERAGE SALARY

Average salary in Montenegro in 2018 amounted to 766 euros being 0.1% higher compared to the previous year. Average salary without taxes and contributions amounted to 511 euros being 0.2% higher than in 2017.

FORECAST FOR 2019

According to the Economic Reform Programme, which was adopted by the Government of Montenegro, the model of economic growth of Montenegro for period 2019-2021 remains under strong impact of investment cycle, which will dominant influence on economic flows. Public finances consolidation measures will also influence economic activity, as well as the measures focused on optimisation of government administration. Non-diversification of Montenegrin economy significantly limits multiplication effects of investments. The value of investments and import reached record high levels, and the baseline scenario assumes that the investments will remain at the same level but will not further grow considering the limited possibilities of the government for further borrowing and low availability of domestic savings intended for these purposes. With regard to the aforesaid, according to the baseline scenario for Montenegro contained in the Economic Reform Programme, annual rate of real economic growth will amount to 2.8% in 2019; 2.3% in 2020, and 2.4% in 2021.

Sources: Montenegro Economic Reform Programme 2019 – 2021, CBCG Bulletin; Monstat – Survey on Accommodation Statistics; European Integration Office – II Annex to the Montenegro Report – European Commission.







3 BUSINESS ACTIVITIES AND ORGANISATIONAL STRUCTURE OF THE BANK

ABOUT THE BANK

Hipotekarna Banka AD Podgorica (hereinafter: the Bank) provides the widest range of banking and financial products and services to legal and natural persons in Montenegro in accordance with the licenses issued by the competent institutions.

The Banking Law, the Law on Business Organisations and Central Bank of Montenegro regulations prescribe the conditions for founding and operating of banks in Montenegro.

The provision of services performed by the Bank in the securities market is regulated by the Law on Securities i.e. Law on Capital Markets and regulations of the Capital Market Authority. The Bank also performs payment operations that are governed by the Payment System Law including the enabling regulations of the Central Bank of Montenegro.

The Bank also performs the insurance agency activities that are regulated by the Law on Insurance and relevant regulations of the Insurance Supervision Agency.

The Bank is subject to the supervision of the Central Bank of Montenegro, the control of the Capital Market Authority and the Insurance Supervision Agency.

As at 31 December 2018, the Bank had 183 employees.

BANK MANAGING BODIES

CORPORATE GOVERNANCE AND CORPORATE GOVERNANCE RULES

General Meeting of the Bank is composed of its shareholders.

Pursuant to Article 15b of the Law on Take Over of Joint Stock Companies:

1) The structure of the Bank's capital is as follows:

- Share capital of the Bank amounts to 16,005,933.45 euros and it consists of 31,305 pieces of common shares issued in the name of the holder;
- Nominal value of one share is 511.29 euros;
- Shares are dematerialised, freely transferrable and issued in the name of the holder. The excerpt for the registry with the Central Depository Agency AD Podgorica is the only evidence of the ownership of shares;

A shareholder of the Bank, as the owner of common shares, has the following rights:

1. right to attend the General Meeting,
2. right to manage proportionately to the share in capital of this class of shares,
3. right to dispose of shares, in accordance with the applicable law,
4. pre-emptive right to acquire new shares, in accordance with applicable regulations,
5. right to acquire shares free of charge in case of the increase in share capital from the Bank's funds, proportionately to its investment,
6. right to dividend payout, after the distribution of preferred shares to owners, when the General Meeting of the Bank decides to pay the dividend,
7. Right to obtain, at personal request, a copy of the balance sheet and profit and loss statement, as well as external auditor report,

8. right to have insight, thirty day prior to the session of the General Meeting and at the meeting, in the financial reports including also external auditor report,

9. right to proportionate part of assets in case of Bank's winding up and other rights in accordance with the applicable law.

2) There are no restrictions for transferring shares i.e. securities;

3) Significant direct and indirect equity investments:

Generali Financial Holdings FCP-Sif	16.8695 %
Cerere S.P.A. - Italy	13.9275 %
Lorenzo Gorgoni - Italy	12.9788 %
Antonia Gorgoni -Italy	10.0016 %
Miljan Todorović - Italy	7.3982 %
Podravska Banka DD - Croatia	2.9931%
Ibis Srl - Italy	4.8682 %
Dario Montinari - Italy	4.6159 %
Sigilfredo Montinari - Italy	4.6159 %
Piero Montinari - Italy	4.6127 %
Andrea Montinari - Italy	4.6127 %

4) There are no securities that give special control rights;

5) Applicable laws and other regulations apply to the acquisition of shares by employees;

6) There are no restrictions of voting rights, such as restriction of the voting right of the owner of a certain percentage of securities or number of shares by deadlines for exercising right to vote, and the like;

7) There is no agreement between shareholders with which the issuer is familiar and that may result in the restriction of transfer of securities and/or voting rights;

8) The manner of appointing and relieving from office members of the Board of Directors is defined by applicable laws and other regulations;

9) The powers of the members of the Board of Directors are defined by the applicable laws and other regulations;

10) There are no significant agreements in which the issuer is a contracting party and which produce legal action, are amended or terminated after the takeover of the issuer in the process of the public initial offering for taking over and their legal effects, unless these agreements are such that their disclosure would have significant harmful effects on the issuer, provided that the issuer is not explicitly obliged to publish such a data in accordance with the law;

11) Executive directors and individual directors of the organisational parts of the Bank have covenants which regulate the payment of fee for the termination of term of office in the amount ranging from 6 (six) to 12 (twelve) net monthly wages.

Board of Directors of the Bank manages the Bank. Members of the Board of Directors are elected and appointed by the General Meeting.

The structure of the Board of Directors and its bodies is as follows:

1.1. Board of Directors of the Bank:

Sigilfredo Montinari, Chair
Božana Kovačević, Deputy Chair
Renata Vinković, Member
Goran Varat, Member
Esad Zaimović, Member

1.2. Audit Committee of the Bank:

Draško Popović, Chair
Božana Kovačević, Member
Goran Knežević, Member

1.3. Credit Risk Management Committee of the Bank:

Renata Vinković, Chair
Sigilfredo Montinari, Member
Esad Zaimović, Member

Board of Directors of the Bank meets as needed and at least once a month.

During 2018, Board of Directors of the Bank passed decisions on the issues from within its competence, and it had continuously overseen the operations of the Bank by periodical review of the reports on the financial situation and operations. Also, the Board of Directors regularly discussed the reports of standing and interim bodies of the Bank, control functions and the reports on the functioning of the internal controls system.

The Board of Directors of the Bank also reviewed the reports on the completed examinations of the Central Bank of Montenegro, as well as the reports of other supervisory institutions.

The executive directors organise and manage the operations of the Bank and oversee the work of the Bank's employees on daily basis. The Bank had two executive directors until 20 August 2018, and due to the changes in the organisational structure, the Bank has had four executive directors since 20 August 2018.

Executive directors of the Bank:

Esad Zaimović, Chief Executive Officer
Božo Djurašković, Executive Director for the operation of support services, until 19 August 2018
Nikola Špadijer, Executive Director for retail operations and advanced distribution channels, since 20 August 2018;
Ana Golubović, Executive Director for corporate operations and financial markets, since 20 August 2018;
Jelena Vuletić, Executive Director for risks since 20 August 2018.

BANK MANAGEMENT

EXECUTIVE DIRECTORS

Esad Zaimović, Chief Executive Officer

Božo Djurašković, Executive Director for the operation of support services, until 19 August 2018;

Nikola Špadijer, Executive Director for retail operations and advanced sales channels, since 20 August 2018;

Ana Golubović, Executive Director for corporate operations and financial markets, since 20 August 2018;

Jelena Vuletić, Executive Director for risks since 20 August 2018

INTERNAL AUDIT DIVISION

Veselin Ivanović, Chief Internal Auditor

EXPERT FUNCTION FOR MONITORING THE COMPLIANCE OF OPERATIONS WITH REGULATIONS (COMPLIANCE)

Danka Dragičević

DIVISION FOR PREVENTION OF MONEY LAUNDERING AND TERRORIST FINANCING

Mirjana Jovanović

CHIEF INFORMATION SYSTEM SECURITY OFFICER (CISO)

Haris Dizdarević, until 19.08.2018. godine;

DEPARTMENTS

Ana Golubović, Director of the Corporate Department, until 19 August 2018;

Nikola Špadijer, Director of the Retail Department, until 19 August 2018;

Mirza Vodopić, Director of the Financial Markets Department

Jelena Vuletić, Director of the Department for Credit Risk Management until 19 August 2018;

Nataša Lakić, Director of the Department for Payment Operations, until 19 August 2018;

Božo Đurašković, Director of the Legal Department, until 19 August 2018;

Sejad Šehić, Director of the Department for Payment Cards Operations and Advanced Distribution Channels, since 20 August 2018;

Nataša Lakić, Director of the Operations Department, since 20 August 2018;

Nikola Milović, Director of the Department for Support and Organisation;

Božo Đurašković, Director of the Department for Legal Affairs and Human Resources, since 20 August 2018;

Goran Smolović, Director of the Department for Control of Risk, since 20 August 2018

INDEPENDENT SERVICES

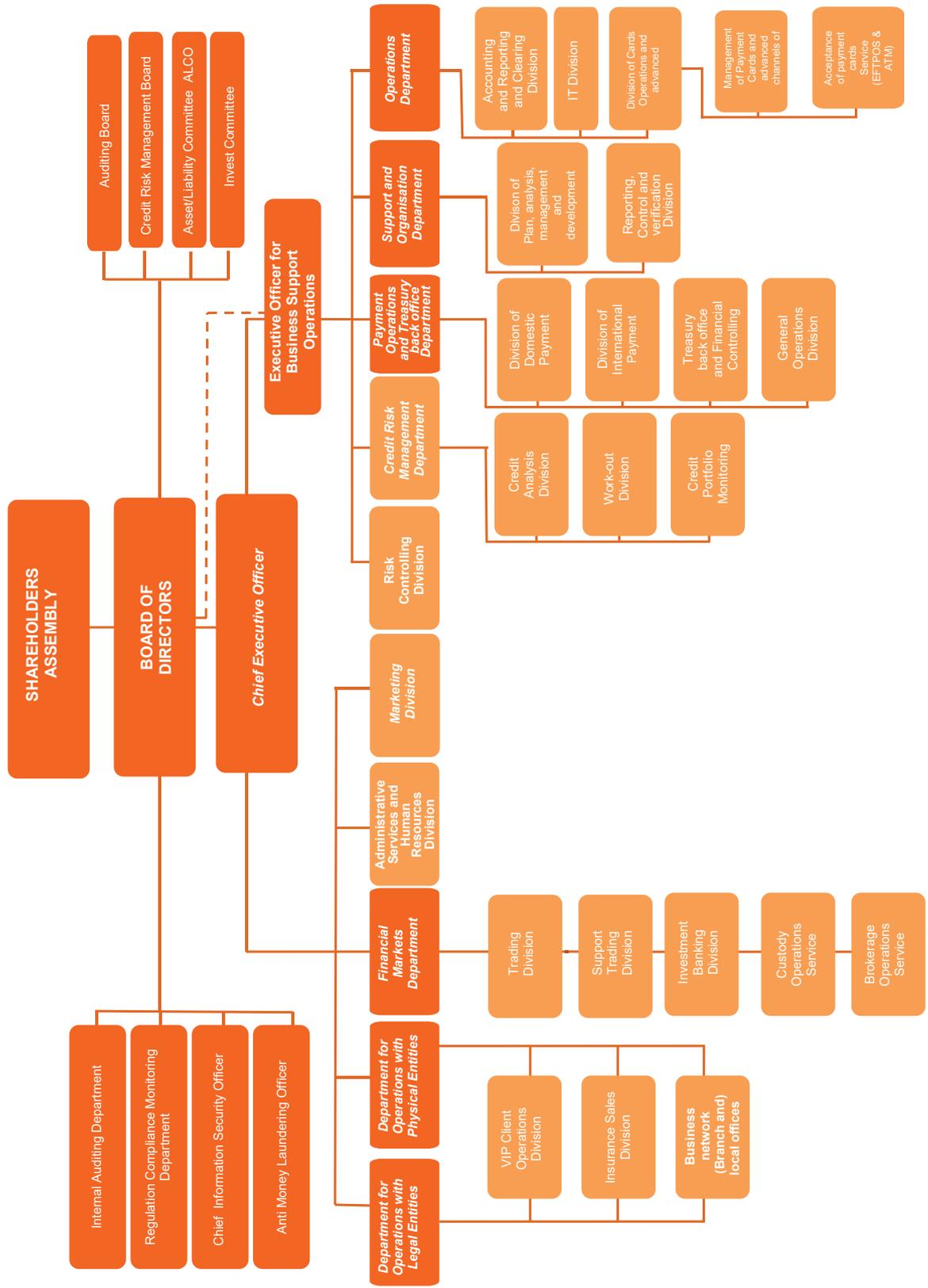
Ana Ristić, Director of the Marketing Service, until 19 August 2018;

Goran Smolović, Director of the Service for Control of Risk, until 19 August 2018;

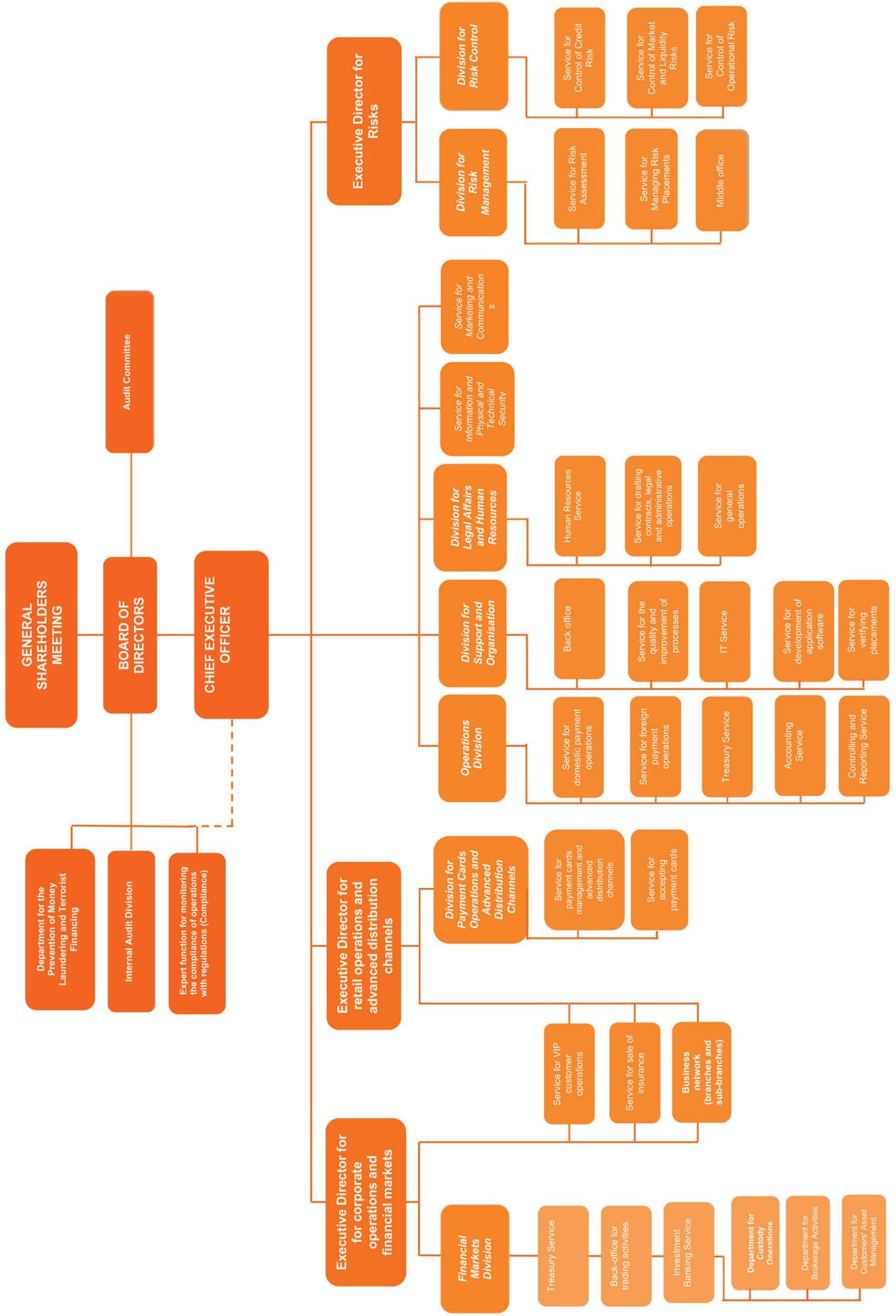
Ana Ristić, Director of the Marketing and Communications Service, since 20 August 2018;

Haris Dizdarević, Director of the Service for Information and Physical and Technical Security, since 20 August 2018

ORGANIZATIONAL CHART OF HIPOTEKARNA BANKA UNTIL 20 AUGUST 2018



ORGANIZATIONAL CHART OF HIPOTEKARNA BANKA SINCE 20 AUGUST 2018



BUSINESS NETWORK

Call Centar (+382 202) 19905

Head office of Hipotekarne Banka

Address: Josipa Broza Tita 67
81000 Podgorica
E-mail: hipotekarna@hb.co.me
Tel: +382 (0) 77 700 001
Fax: +382 (0) 77 700 071

BRANCHES

Podgorica Branch
Address: Slobode 91
81000 Podgorica
E-mail: filijala.podgorica@hb.co.me

Nikšić Branch
Address: Trg Save Kovačevića bb
81400 Nikšić
E-mail: filijala.niksic@hb.co.me

Bar Branch
Address: Ul. Maršala Tita bb
85000 Bar
E-mail: filijala.bar@hb.co.me

Budva Branch
Address: Mediteranska 4
85310 Budva
E-mail: filijala.budva@hb.co.me

Kotor Branch
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bb
85330 Kotor
E-mail: filijala.kotor@hb.co.me

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Address: Njegoševa 52
85340 Herceg Novi
E-mail: filijala.hercegnovi@hb.co.me

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Address: Slobode bb
84000 Bijelo Polje
E-mail: filijala.bijelopolje@hb.co.me

Berane Branch
Address: Mojsija Zečevića bb
84300 Berane
E-mail: filijala.berane@hb.co.me

Ulcinj Branch
Address: 26. Novembar bb
85360 Ulcinj
E-mail: filijala.ulcinj@hb.co.me

Danilovgrad Branch
Address: Baja Sekulića 8
81410 Danilovgrad
E-mail: filijala.danilovgrad@hb.co.me

SUB-BRANCHES

Sub-branch in Podgorica 24/7
Address: Bul.Svetog Petra Cetinjskog 130
Podgorica
E-mail: ekspozitura.podgorica1@hb.co.me

Sub-branch in Podgorica 2 (Blok VI)
Address: Đoka Miraševića M3
81000 Podgorica
E-mail: ekspozitura.podgorica2@hb.co.me

Sub-branch in Podgorica 3 (Alliance)
Address: Cetinjski put bb
81000 Podgorica
E-mail: ekspozitura.podgorica3@hb.co.me

Sub-branch in Cetinje
Address: Bajova 74
81250 Cetinje
E-mail: ekspozitura.cetinje@hb.co.me

Sub-branch in Tivat
Address: 21. Novembra 21
85320 Tivat
E-mail: ekspozitura.tivat@hb.co.me

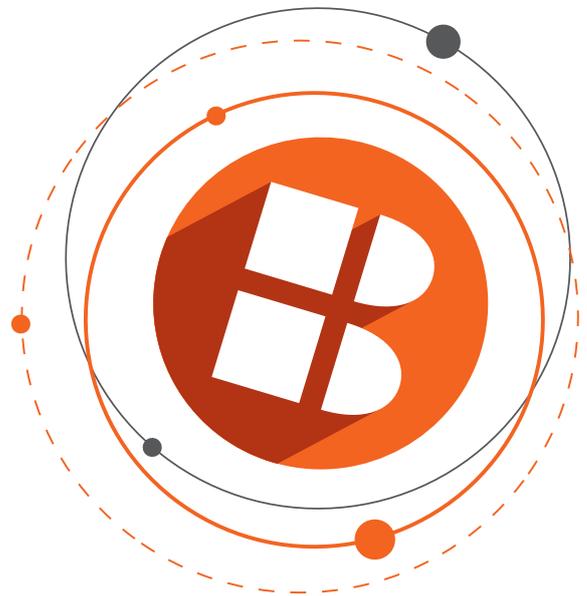
Sub-branch in Tivat – Porto Montenegro
Address: Porto Montenegro, zgrada Teuta,
Obala bb
85320 Tivat
E-mail: ekspozitura.porto.montenegro@hb.co.me

EMPLOYEES

As at 31 December 2017, the Bank had 172 employees with qualifications needed and IT skills for qualitative performance of banking operations.

Continuous education and professional development are set as Bank's top priorities. In 2017, a large number of employees underwent training in both internal and external programmes on various areas relevant to the Bank operations. The Bank hires young professionals who can contribute to Bank's effective development.

As at 31 December 2017, educational background of the employees of the Bank was as follows: 12 hold an MSc, 90 university, and 33 a Bachelor of Science degrees, while 13 have two-year post-secondary, and 50 a secondary school education.







4

**BUSINESS
OPERATIONS**

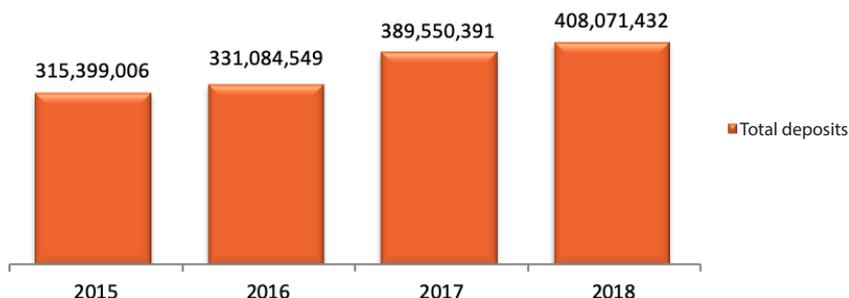
DEPOSITS

DEPOSITS

In 2018, deposits saw a y-o-y growth of 4.75%, which indicates the confidence of households and corporate sectors in the Bank. In addition to higher growth in deposits recorded in 2017, deposits grew steadily in 2018 as it was the case in the previous years. The growth in demand deposits was significant and it accounted for 12.17%, which was particularly important besides the stable growth of all types of deposits.

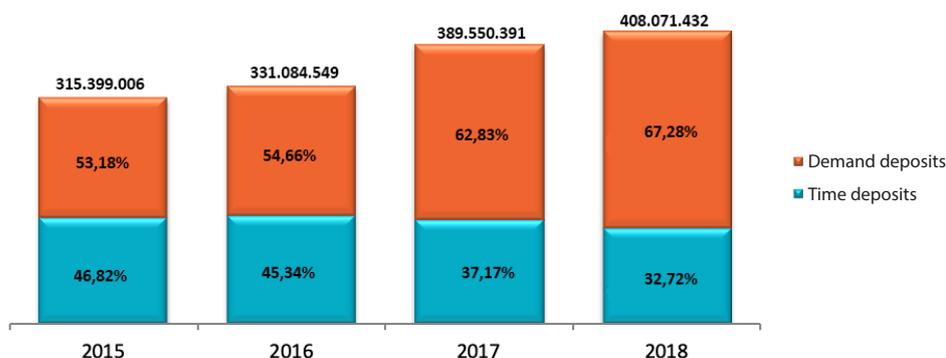
Balance of total deposits

	Total deposits	% of change
2015	315,399,006	-
2016	331,084,549	4.97%
2017	389,550,391	17.66%
2018	408,071,432	4.75%

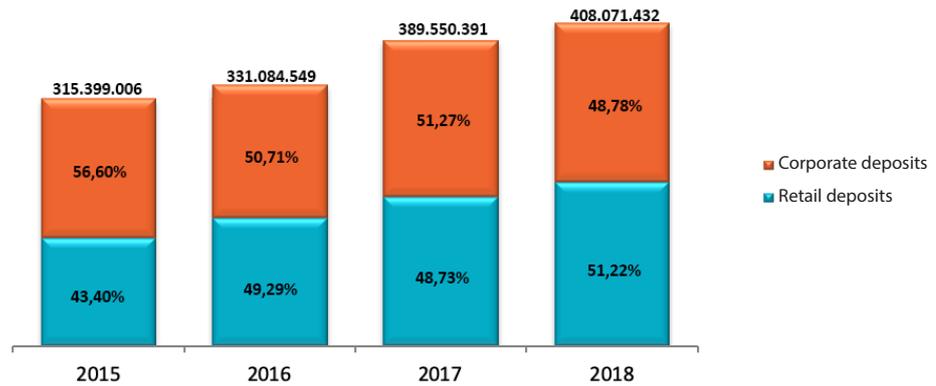


The increase in deposits resulted from the increase in the number of clients as well as the increase of confidence in the Bank. Thanks to all the attributes that characterize the Bank, which are, first and foremost, security, professionalism and quality of the offer, we are recognised as a trustworthy bank, thus continuing the positive trend of deposit growth.

With regard to the share of time and demand deposits in total deposits, the Bank maintained adequate structure of deposits. Time deposits accounted for 32.72% in total deposits, while demand deposits accounted for 67.28%.



The share of corporate deposits accounted for 48.78% of total deposits, while retail deposits stood at 51.22%, as shown in the following graph:



LOANS

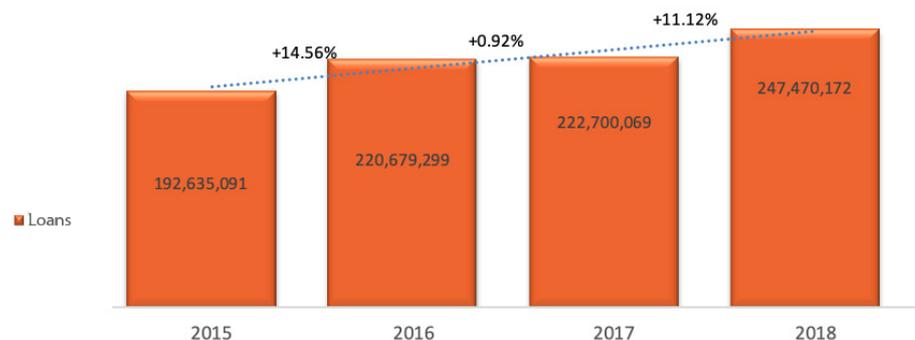
LOANS

In 2018, as well as in the previous years, the Bank granted loans to a large number of new clients. An ongoing support and further development of the existing clients was an imperative for the Bank and the main focus of the employees is always to anticipate the needs of the clients, optimise the structure of arrangements and tariffs for the existing clients.

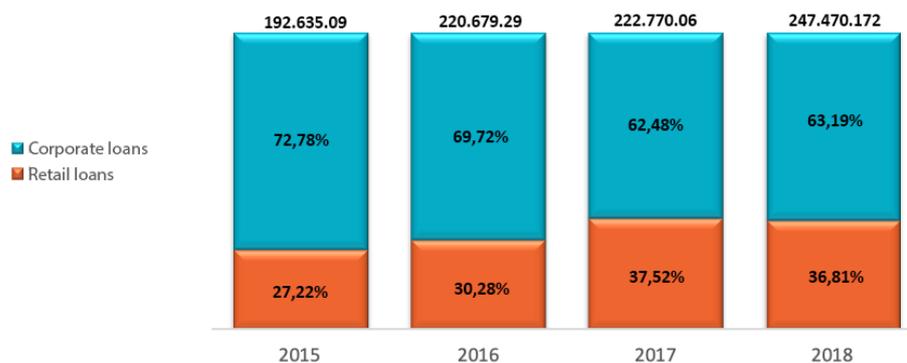
One of the distinctive features of the Bank is that, in addition to approving loans, it simultaneously provides advisory services to clients in order to improve their business operations and achieve better business results for both the Bank and its clients.

Despite the conservative policy the Bank has traditionally pursued in granting loans, total amount of loan portfolio increased by 11.12% compared to the previous year.

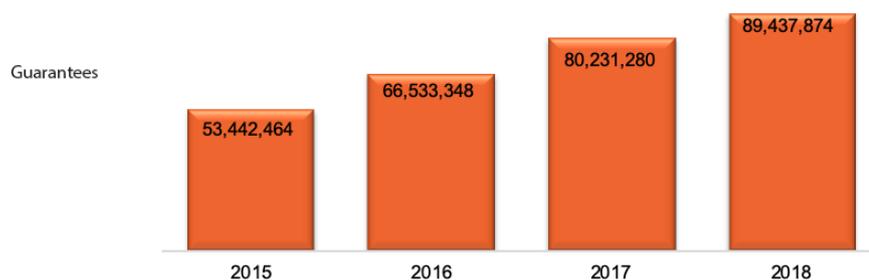
	Loans	Change in %
2015	192,635,091	0.00%
2016	220,679,299	14.56%
2017	222,700,069	0.92%
2018	247,470,172	11.12%



With regard to the structure of total loans, household loans accounted for 36.81%, while the share of corporate loans was 63.19% in total loan portfolio.



Overview of guarantees in 2018:



Y-o-y, guarantees increased by 11.48%.

The Bank has continued its successful cooperation with the Investment and Development Fund (IDF) in the area of lending under favourable conditions.

The Bank's range of services offered to corporate clients includes cash loans, revolving loans, loans for payment of liabilities to suppliers, loans for car purchase, loans for refinancing of debts with other banks, financing export receivables, for purchase of equipment, refurbishment of office space, preparation for tourist season, overdraft loans, factoring, as well as all types of guarantees.

The Bank also offers a wide spectrum of retail loans: cash loans, purpose-specific loans, student loans, car purchase loans, reconstruction and refurbishment loans, sailor loans, tourism loans, agriculture loans, overdraft loans, consumer instalment loans, etc. as well as all types of guarantees.

DEVELOPMENT OF NEW PRODUCTS AND SERVICES

In 2018, the Bank also maintained the expected continuity in launching new innovative products.

The most sophisticated NFC application **Moj novčanik** (My wallet) stands out among the new products, which has the possibility for Android mobile devices to set all Mastercard users in its mobile phone, and undisturbed payment at all contactless POS terminals. The application is characterised by the highest level of security, personalisation, easy and functional architecture of the application, and the like.

PAYMENT OPERATIONS

PAYMENT OPERATIONS

In 2018, all indicators defining the payment operations recorded growth. All payment operation plans that were set in the previous period were achieved, which proved the successfulness and efficiency of the Bank in the previous year.

Domestic Payment Operations

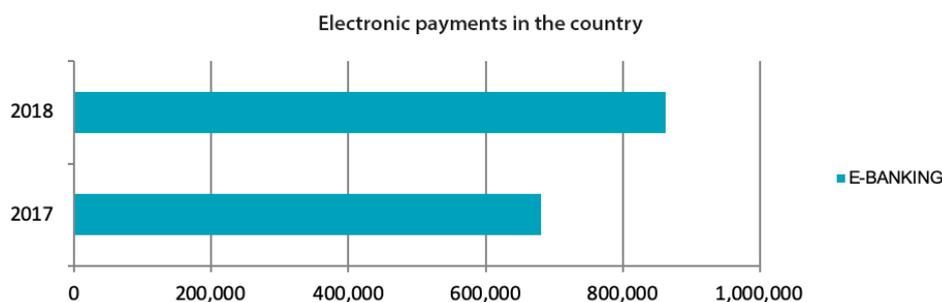
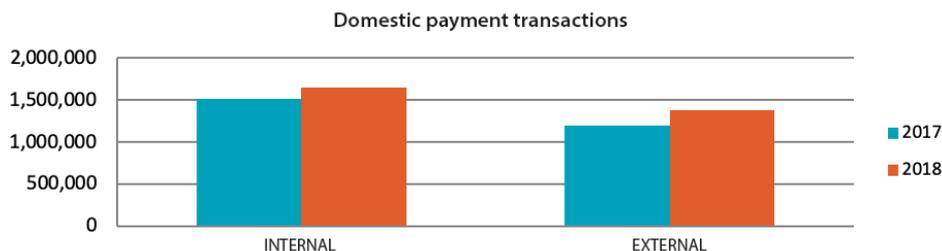
Overall domestic payment operations of the Bank recorded a growth in 2018.

Total number of transactions in the domestic payment operations recorded a y-o-y increase of 12%. Of this amount, a 9% y-o-y growth referred to internal transactions in the Bank. External transactions also saw a y-o-y increase of 16%.

With regard to the structure of external payment orders, the increase was recorded in both small payment orders (< 1,000 euros, increase of 13%) and large payment orders (>1,000 euros, increase of 21%).

Y-o-y, the number of inflows from other banks also increased by 10%.

A significant growth in the number of electronic (e-banking) transactions was also recorded, which indicates the increasing orientation of the clients towards electronic applications and the growing number of payments using electronic payment orders. The electronic transactions in domestic payment operations increased by 27% compared to the previous year.

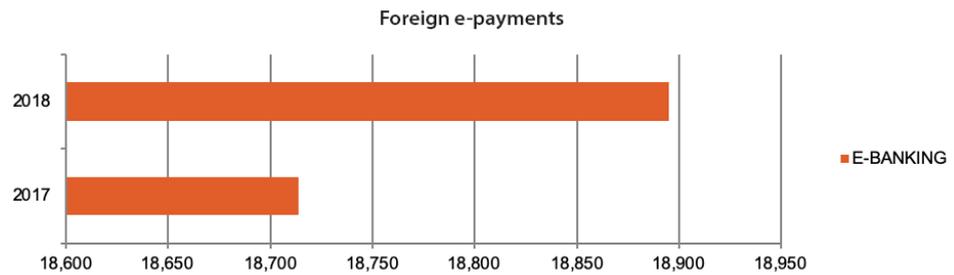


Foreign Payment Operations

The main features of the international payment operations in 2018 were as follows: an ongoing trend of high number of payments was maintained, as well as the growth in incoming payments and payments executed via e-banking, and other operations that represent an integral part of the foreign payment operations.

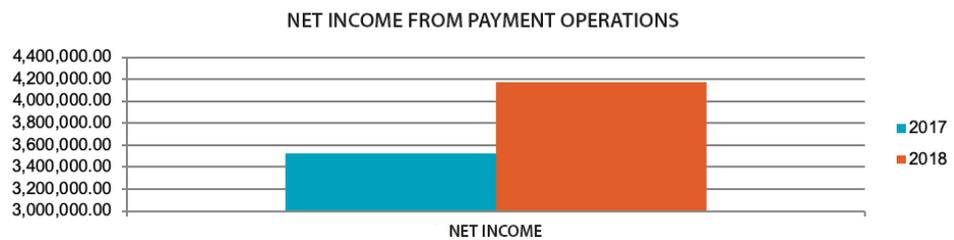
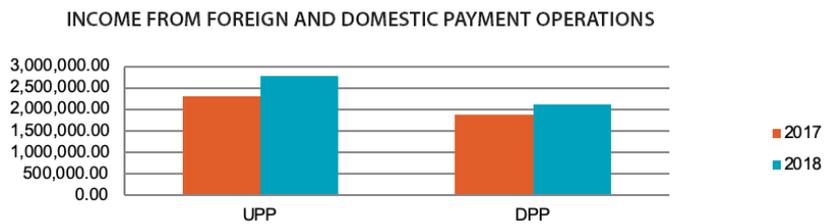
The Bank has long been recognised by foreign banks as an efficient and reliable partner.

The number of foreign payment transactions increased by 9% y-o-y. The number of foreign e-payments using the application HB-klik (e-banking) increased by 1%, y-o-y. The number of inflows grew by 24% compared to the previous year.



Total fees for the payment operations services grew y-o-y by 18%. Of this amount, income from domestic payment operations amounted to 21%, while foreign payment operations were 14%.

Net income from total payment operations grew by 19% compared to the previous year.



ASSET MANAGEMENT

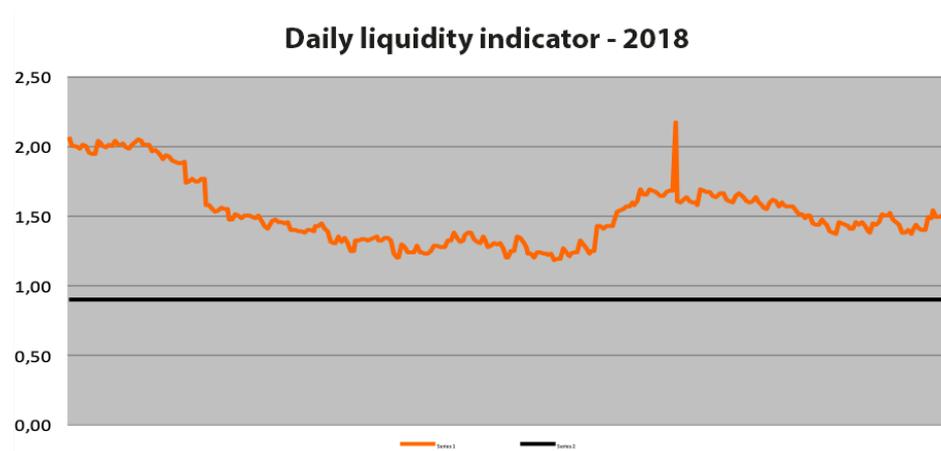
ASSET MANAGEMENT

Providing optimal liquidity is a basic requirement for safe and efficient operations of each bank. With the aim to maintain adequate liquid assets to total liabilities ratio, the Bank should provide the liquidity needed by applying rational assets and liabilities management.

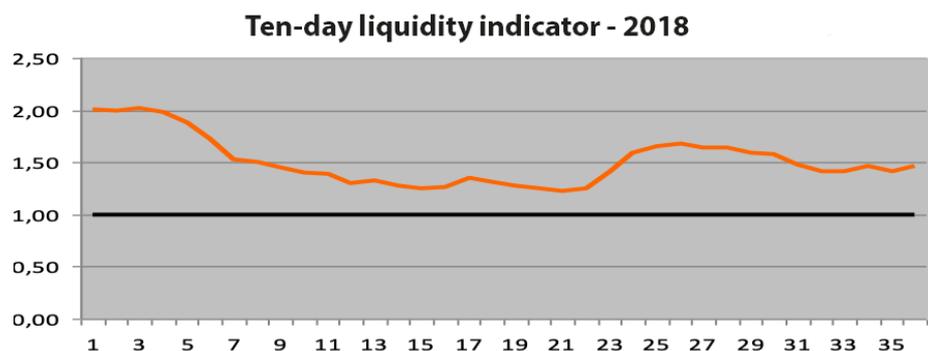
In 2018, the Bank also put emphasis on stabilising domestic sources of funding and expanding its client base, reducing short-term sources in favour of long-term sources of funding and taking new credit lines from foreign banks and international financial institutions.

The treasury back office operating as part of the Department for Financial Markets managed throughout 2018 to maintain the level of liquid assets and total liquid position of the Bank at the satisfactory level thanks to its rational liquidity management. In addition, the Office performed reconciled sources of funds with loans by daily, weekly, ten-day and monthly scheduling of available liquid assets. Adequate allocation of funds was performed through close cooperation with other departments and services in the Bank. This allowed the Bank to meet regularly its obligations towards creditors, as well as to accommodate client requests within the shortest terms possible.

The daily liquidity ratio, which is calculated using the methodology set by the Central Bank of Montenegro, was considerably above the statutory minimum of 0.90 throughout 2018.



Also, ten-day liquidity indicator was above the statutory minimum of 1,00 in 2018.



With the aim to manage liquidity within a period, the Bank regularly monitored indicators of the structural liquidity through maturity match of financial assets and liabilities, overview of maturity of large deposits, and by establishing a stable part of demand deposits using the internal model. The Bank maintained liquidity at the satisfactory levels.

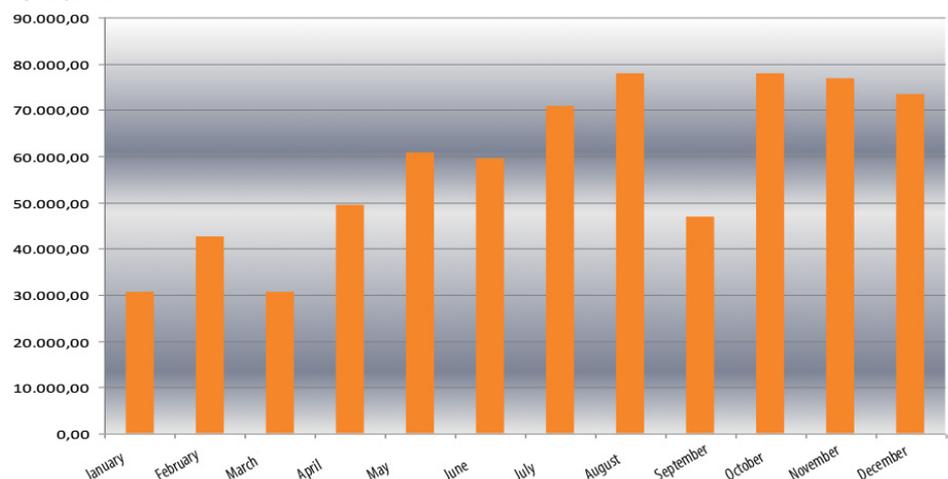
Given that 2018 saw a fall in interest rates on deposits of clients and the caution of clients in managing their own funds, it can be noted that the Bank was recognised even in these circumstances as one of the most reliable and most liquid banks in the banking system of Montenegro. This statement is supported by the data showing 2017 total deposits in the amount of 392.61 million euros, and 2018 total deposits in the amount of 409.09 million euros, which represented an increase of 4.19%. In addition to lending activity, surpluses of liquid funds were invested in marketable securities.

In 2018, the Bank actively participated in T-Bills auctions and made a satisfactory return. Also, through the activities of the Financial Markets Department, the Bank invested funds in securities both in Montenegro and region.

Large exchange rate fluctuations were recorded in 2018, particularly in currency pair EUR/USD, which has the highest impact on the exposure of the Bank to foreign exchange risk.



In such a circumstances, Treasury back office managed to achieve a remarkable result based on differences in exchange rates, which was the result of adequate foreign exchange risk management. Thus, at the end of 2018, total income from exchange rate differences amounted to 698 thousand euros, which significantly influenced the final financial result of the Bank.



Income from differences in exchange rates in 2018

INVESTMENT BANKING

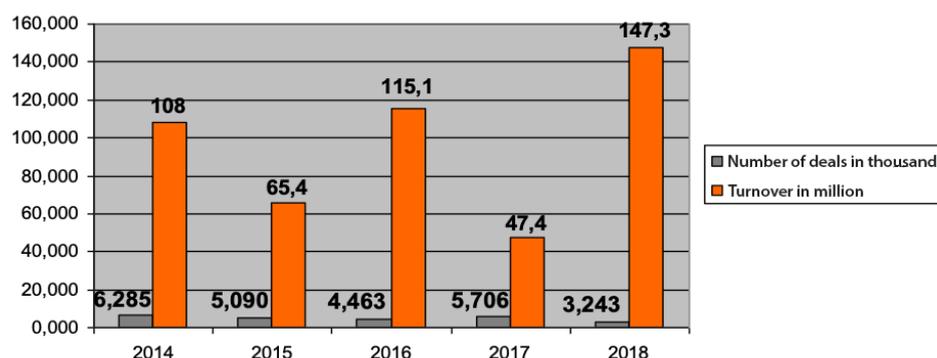
INVESTMENT BANKING

Montenegro Capital Market

In 2018, total turnover recorded at the Montenegro Stock Exchange amounted 147,355,442 euros, which was a y-o-y growth of 210%. This resulted from the block trades with the shares of Electricity Company of Montenegro which participated with about 82% (i.e. about 120 million euros) in this turnover. The trading volume declined by 43% and it can be said that the market was inactive.

In 2018, the Bank traded with shares and concluded 25 deals, and the turnover was made in the amount of 462 thousand euros. The turnover in subordinated bonds HBO1 was 551 thousand euros in 2018, and given the current market conditions, they showed good liquidity in secondary market.

MONEX 10 grew by 7.77% last year, and it was at 837.08 on the last trading day. On 12 November 2018, the Index peaked at 852.08 points, while its lowest value last year was recorded on 15 July being at 737.17 points. In 2018, MONEX recorded growth of 6.54%, and it stood at 10.840 percentage points on the last trading day.



BROKERAGE

In 2018, the Brokerage Division of Hipotekarna Banka made turnover of 58.74 million euros at the Montenegro Stock Exchange. The Bank kept the position of one of leading companies in the Montenegro Capital Market (it was ranked second measured by the achieved turnover).

Brokers of the Bank made turnover at the foreign market in the amount of 10,4 million euros.

TRADING WITH SHARES FOR THE ACCOUNT OF THE BANK

As at 31 December 2018, the Bank invested in equity securities 5.826 million euros. Its income from dividend was 58.55 thousand euros.

CUSTODY OPERATIONS

As at 31 December 2018, the Bank's clients held in custody the securities in the amount of 44.38 million euros. Therefore, the Bank remained one of the leaders in custody operations in Montenegro. Income of the Custody Division amounted to 112.91 thousand euros and, the business result of the Division amounted to 88 thousand euros.

RISK MANAGEMENT

RISK MANAGEMENT

Two departments are responsible for risk management in the Bank:

* Risk Management Department, which has two services, Service for Risk Assessment and Service for Managing Risk Loans, both being responsible for the assessment, identification, measurement and monitoring of risks

* Department for Control of Risk, which has a Service for the Control of Credit Risk, Service for the Control of Market and Liquidity Risks and Service for the Control of Operational Risk, and they are responsible for monitoring, control and reporting on risks

Special attention is paid to the policies and procedures related to risk management as well as the development of needed methodologies.

Both departments prepare monthly, quarterly and annual reports, and ALCO, Board of Directors and Credit Risk Committee are informed on all risk-related activities.

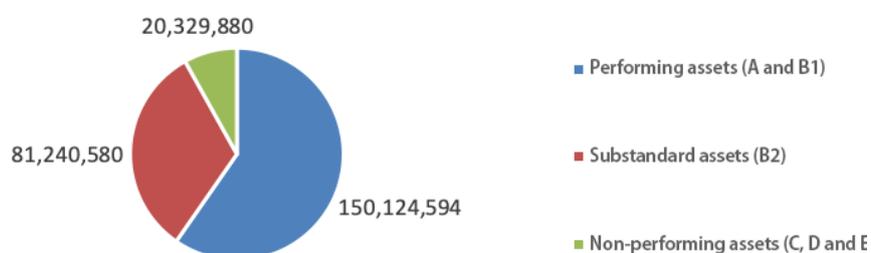
CREDIT RISK

Credit risk management is a key component of overall risk management system. Credit risk management is aimed at maximising the ratio between the risk and return of the Bank. In order to accomplish this objective, credit risk is managed at individual level (at the level of sub-account) within the Risk Management Department, and at the level of portfolio within the Department for Control of Risk.

In December 2018, Bank's loan portfolio increased by 24,768,883 euros y-o-y, and it amounted to 247,470,172 euros. In relative terms, the portfolio increased by 11.12%.

Bank's performing assets (A and B1) accounted for 60.28% of total portfolio, while substandard assets (B2) accounted for 31.52%, and non-performing assets (C, D and E) amounted to 8.20%.

Assets per quality - December 2018



The main indicators of credit risk were: default in repayment of loans, percentage of loan loss provisions, and share of non-performing assets in total portfolio (NPL%).

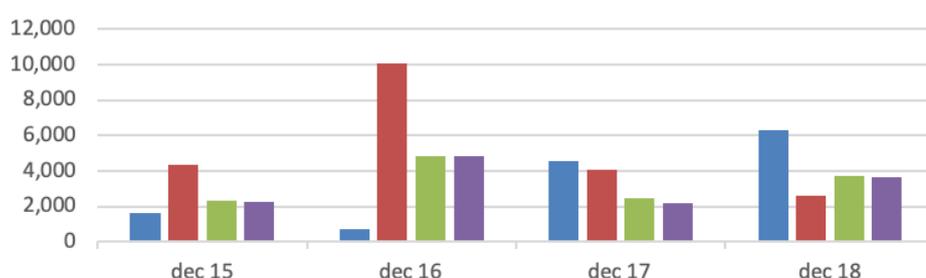
Default in repayment of loans:

* As at 31 December 2018, past due loans over 30 days amounted to

12,596,713 euros or 5.09% of total portfolio of the Bank, while as at 31 December 2017, the same loans amounted to 11,055,208 euros or 4.96% of total portfolio of the Bank.

* With regard to the past due loans over 90 days as at 31 December 2018, they amounted to 8,873,429 euros or 3.59% of total portfolio of the Bank, while as at 31 December 2017, they amounted to 8,610,333 euros or 3.87% of total portfolio of the Bank.

Receivables per past due sub-accounts



The percentage of loan loss provisions can be observed using the CBCG methodology and internal methodology of the Bank.

* According to the CBCG methodology, as at 31 December 2018, loan loss provisions made up 6.51% of the portfolio or 16,122,126 euros. When compared to end-2017, these provisions increased by 6.75% or 1,019,941 euros.

Portfolio / provisions according to the CBCG

	31.12.2017.	31.03.2018.	30.06.2018.	30.09.2018.	31.12.2018.
Portfolio	222.701.289	236.845.567	236.845.567	236.583.249	247.470.172
Provisions	15.102.186	16.276.629	16.276.629	15.411.017	16.122.126
Provisions (%)	6,78%	6,87%	6,87%	6,51%	6,51%

* According to the internal methodology, as at 31 December 2018, value adjustments for loans amounted to 12,485,129 euros or 5.05% of the portfolio. Y-o-y, the provisions increased by 3,855,343 euros or 45%.

	31.12.2017.	31.03.2018.	30.06.2018.	30.09.2018.	31.12.2018.
Portfolio	222.701.289	238.716.571	246.755.400	236.583.249	247.470.172
Provisions	8.629.786	11.032.186	11.249.677	10.415.127	12.485.129
Provisions (%)	3,88%	4,62%	4,56%	4,40%	5,05%

The share of non-performing assets (NPLs) in total portfolio is monitored on the basis of the clients' financial situation i.e. group and past due days (over 90 days past due).

According to the groups of clients' financial situation, as at end-December 2018, NPLs amounted to 20,297,486 euros or 8.20% portfolio, which represents an NPL decline of 28% compared to December 2017, when it amounted to 28,039,482 euros.

**SOLVENCY
RATIO**

As at 31 December 2018, solvency ratio was above the statutory limit (10%), and it amounted to 12.28%. Solvency ratio was the most important indicator of confidence in the Bank, and of the protection of depositors, creditors and business partners of the Bank.

Solvency ratio for 2018

