FINANCIAL STATEMENTS AS AT 31 DECEMBER 2018

BANCA SISTEMA
CONTEMPORARY BANK

Banca SISTEMA S.p.A.

DRAFT SEPARATE FINANCIAL STATEMENTS AT 31 DECEMBER 2018

BANCA SISTEMA

CONTENTS

DIRECTORS' REPORT
AT 31 DECEMBER 2018

COMPOSITION OF MANAGEMENT BODIES

Board of Directors

Chairperson	Ms.	Luitgard Spögler[1]
Deputy Chairperson	Mr.	Giovanni Puglisi[2]
CEO and General Manager	Mr.	Gianluca Garbi
Directors	Mr.	Daniele Pittatore *(Independent)*[3]
	Ms.	Carlotta De Franceschi *(Independent)*
	Ms.	Laura Ciambellotti *(Independent)*
	Mr.	Federico Ferro Luzzi *(Independent)*
	Mr.	Francesco Galietti *(Independent)*
	Mr.	Marco Giovannini *(Independent)*

Board of Statutory Auditors

Chairperson	Mr.	Massimo Conigliaro
Standing Auditors	Mr.	Biagio Verde
	Ms.	Lucia Abati[4]
Alternate Auditors	Mr.	Marco Armarolli[5]
	Ms.	Daniela D'Ignazio

Independent Auditors

KPMG S.p.A.

Manager in charge of financial reporting

Mr. Alexander Muz

[1] Meets the independence requirement pursuant to art. 147-ter, paragraph 4, and art. 148, paragraph 3 of Legislative Decree no. 58 of 24 February 1998, but it also does not meet the provisions of art. 3, application criteria 3.c.1.b and 3.c.2 of the Code of Conduct issued by Borsa Italiana.
[2] Meets the independence requirement pursuant to art. 147-ter, paragraph 4, and art. 148, paragraph 3 of Legislative Decree no. 58 of 24 February 1998, but it also does not meet the provisions of art. 3, application criteria 3.c.1.b and 3.c.2 of the Code of Conduct issued by Borsa Italiana.
[3] Director co-opted by the Board of Directors on 13 July 2018 replacing Mr. Pugelli who tendered his resignation from the position with effect from 30 June 2018.
[4] Appointed as a Standing Auditor at the Shareholders' Meeting on 14 December 2017 and shall remain in office until the end of the Board of Statutory Auditors' term.
[5] On 14 December 2017, following the appointment of the new Standing Auditor, he was once again appointed Alternate Auditor at the Shareholders' Meeting and shall remain in office until the end of the Board of Statutory Auditors' term.

COMPOSITION OF THE INTERNAL COMMITTEES

Internal Control and Risk Management Committee

Chairperson	Ms.	Laura Ciambellotti
Members	Ms.	Carlotta De Franceschi
	Mr.	Federico Ferro Luzzi
	Mr.	Daniele Pittatore[6]

Appointments Committee

Chairperson	Mr.	Federico Ferro Luzzi
Members	Mr.	Marco Giovannini
	Ms.	Luitgard Spögler

Remuneration Committee

Chairperson	Mr.	Giovanni Puglisi
Members	Mr.	Francesco Galietti
	Mr.	Marco Giovannini

Ethics Committee

Chairperson	Mr.	Giovanni Puglisi
Members	Ms.	Carlotta De Franceschi
	Mr.	Federico Ferro Luzzi[7]

Supervisory Body

Chairperson	Mr.	Massimo Conigliaro
Members	Mr.	Daniele Pittatore
	Mr.	Franco Pozzi

[6] On 21 September 2018, the Board of Directors appointed Mr. Daniele Pittatore (independent and non-executive director) as a new member of the Internal Control and Risk Management Committee to replace Ms. Luitgard Spögler, who will in any case be entitled to attend meetings without the possibility of voting.

[7] On 21 September 2018, the Board of Directors appointed Mr. Federico Ferro Luzzi (independent and non-executive director) as a new member of the Ethics Committee.

FINANCIAL HIGHLIGHTS AT 31 DECEMBER 2018

Statement of financial position data (€,000)

	31 Dec 2018	31 Dec 2017	
Total Assets	3,150,153	2,310,427	36.3%
Securities Portfolio	739,880	370,989	99.4%
Loans - Factoring	1,566,613	1,285,726	21.8%
Loans - Salary-backed loans and SME	679,589	556,061	22.2%
Funding - Banks and REPOs	875,016	733,156	19.3%
Funding - Term Deposits	958,193	447,093	114.3%
Funding - Current Accounts	660,582	510,349	29.4%

Income statement data (€,000)

	31 Dec 2018	31 Dec 2017	
Net interest income	74,746	70,809	5.6%
Net fee and commission income	15,257	10,667	43.0%
Total Income	91,272	82,652	10.4%
Personnel Expenses	(19,811)	(17,549)	12.9%
Other administrative expenses	(20,710)	(19,259)	7.5%
Pre-tax profit	42,700	39,767	7.4%

Performance Indicators

	31 Dec 2018	31 Dec 2017	
Cost/Income	45.8%	45.4%	0.7%
ROAE	19.3%	21.5%	-10.5%

SIGNIFICANT EVENTS FROM 1 JANUARY TO 31 DECEMBER 2018

On 8 February 2018, the Board of Directors approved the Remuneration Policies Document of the Banca Sistema Group for 2018. It also acknowledged the quarterly report by the Internal Control Department as at 31 December 2017 (Risk Reporting, Tableau de Bord of the Compliance Department and Tableau de Bord of the Internal Audit Department), the quarterly report on Related Party Transactions within the scope of the Master Resolution, and the annual Report of the Head of internal whistleblowing systems.

On 8 March 2018, the Board of Directors approved: (I) the "2017 Risks Department Annual Report", (II) the "2017 Compliance Department Annual Report", (III) the "2017 Anti-Money Laundering Department Annual Report", (IV) the "Compliance Department Annual Report on complaints received by the Bank", (V) the "Annual Report on the activities carried out by the Internal Audit Department during 2017", and (VI) the Activity Plan for 2017 related to the II Level Internal Control Departments (Risk, Compliance and Anti-Money laundering) and Internal Audit Department and the Periodic Report by the Supervisory Body concerning the application of the "Organisational, management and control model pursuant to Legislative Decree no. 231/2001". The Board of Directors also approved (I) the Report on Corporate Governance and Ownership Structure prepared in accordance with art. 123-Bis of Legislative Decree no. 58/1998 and the Remuneration Report pursuant to art. 123-Ter of Legislative Decree no. 58/1998, as well as (II) the document "IFRS 9 - Business Model Policy".

On 9 April 2018, following the authorisations granted by the Bank of Italy, two new branches dedicated exclusively to the collateralised lending business were opened in Naples and Palermo.

On 10 April, the Board of Directors of Banca Sistema approved the 2018-2020 Strategic Plan, which was presented to analysts and investors on 11 April 2018.

On 23 April 2018, the shareholders' meeting was held during which the Board of Directors' mandate was renewed with the appointment of nine members.

Following the renewal, the Board of Directors approved the appointment of Gianluca Garbi as CEO of the Bank, conferring on him necessary operational powers.

At the end of May, the placement of a senior bond issue was successfully completed. The placement in a club deal reserved for institutional investors that are not related parties, in the total amount of € 90 million, has a term of 3 years, with a fixed rate and an all-inclusive cost of 200 bps. The objective of the issue is consistent with the bank's strategy to diversify its sources of funding and to support the growth of the core business.

On 19 June 2018, the Bank completed the acquisition of a 19.90% stake in the share capital of ADV Finance S.p.A. ("ADV Finance"), a registered financial intermediary (under art. 106 of the Consolidated Banking Act) that since 2010 has offered in Italy, through agents and brokers, a complete range of services related to salary- and pension-backed personal loans (CQS/CQP). Subsequently, on 18 December 2018, it acquired from ADV Finance, 19.90% of the quota capital of the subsidiary Procredit S.r.l., a company specialising in services related to salary- and pension-backed personal loans (CQS/CQP).

On 22 June, the Board of Directors approved the start of market making activities and thus allocated € 40,000 to them for the purchase and disposal of treasury shares within the scope of the authorisation granted at the Shareholders' Meeting of 27 April 2017 and in accordance with the terms authorised by the Bank of Italy on 13 September 2017. The programme was suspended on 5 October 2018 to start the treasury share repurchase programme for the purpose of supporting the remuneration and incentive policies for key personnel for an overall amount not exceeding € 200,000, which was concluded on 12 October 2018, the day on which the market making activity programme resumed and which was terminated on 27 October 2018.

On 29 June 2018, notice was given that the shareholders Società di Gestione delle Partecipazioni in Banca Sistema S.r.l. (SGBS), Fondazione Cassa di Risparmio di Alessandria and Fondazione Sicilia, in anticipation of the imminent expiry date of the Shareholders' Agreement signed on 3 June 2015 along with Fondazione Pisa, having taken note of the intention expressed by Fondazione Pisa not to join the new Shareholders' Agreement, signed a new Shareholders' Agreement which came into effect on this date until 1 July 2020. The new Shareholders' Agreement reflects a shareholding of 38.41% in Banca Sistema's share capital.

Given the above, Claudio Pugelli, a non-executive and non-independent Director of Banca Sistema, tendered his resignation from the position with effect from 30 June.

An abstract of the new Shareholders' Agreement, which was drafted pursuant to article 129 of the Issuers' Regulation approved by Consob Resolution no. 11971/99, and essential information pursuant to article 130 of the Issuers' Regulation have been made available on the Parent's website www.bancasistema.it and on the website of the storage mechanism authorised by Consob www.1info.it in accordance with the legal terms.

On 28 September 2018, the Bank signed a binding agreement for the acquisition of 100% of Atlantide S.p.A., a registered financial intermediary (under art. 106 of the Consolidated Banking Act) and active in the granting of salary- and pension-backed personal loans (CQS/CQP) since 2010. Atlantide, headquartered in Bologna, has 23 employees and provides comprehensive CQS/CQP services throughout the country through a network of more than 30 agents. The agreement is in line with Banca Sistema's growth objectives and with the 2018-2020 Strategic Plan for CQS/CQP, a market in which Banca Sistema is already active through agreements with other intermediaries for the purchase of portfolios.

The value of the transaction is equal to the equity of Atlantide at 30 June 2018 plus goodwill of € 250 thousand; the agreement also includes a variable component to be paid upon achievement of certain objectives. All the proceeds resulting from the completion of the transaction will be used by Atlantide's current shareholders to buy Banca Sistema's shares on the open market, subject to a maintenance obligation of three years. The agreement is expected to be completed by the end of the first quarter of 2019 following the authorisation of the Supervisory Authority. The transaction had an impact of approximately 15 bps on Banca Sistema's CET1 ratio at 30 June 2018.

The transaction is structured so that, subsequent to authorisation by the Bank of Italy, the company will be merged into Banca Sistema pursuant to Article 2505 of the Italian Civil Code (so-called simplified merger). The merger will take effect on the first day of the month following the last of the planned filings with the Chamber of Commerce, while the tax effects will be backdated to 1 January 2019.

On 12 October 2018, work commenced on relocating to the new headquarters located in Largo Augusto 1/A, at the corner of Via Verziere 13, in Milan and were completed on 9 November 2018.

On 12 October 2018 ProntoPegno S.p.A. was incorporated, with Banca Sistema S.p.A. as sole shareholder. The registered office of the company is in Largo Augusto 1/A, Milan (at the corner of Via Verziere 13) and the share capital amounts to € 3,500,000. On 9 November 2018, the application was sent to the Bank of Italy for the registration of ProntoPegno S.p.A. in the Register referred to in Article 106 of Italian Legislative Decree no. 385/1993, in accordance with the provisions of Circular no. 288 of 3 April 2015. Once the authorisation to conduct business has been obtained, all the assets and liabilities relating to the collateralised loan business will be transferred to the company, in addition to the personnel dedicated to the management and development of the business.

On 8 November 2018, following the authorisation issued by the Bank of Italy, a new branch dedicated exclusively to the collateralised loan business was opened in the city of Rimini. This branch joins the branches in Milan, Rome, Pisa, Naples and Palermo.

On 7 November, Banca Sistema also acquired the portfolio of Credit Agricole, formerly Carim, a well-established collateralised lender based in Rimini. The transaction will accelerate growth and strengthen the presence of "ProntoPegno" throughout the area while promoting a service that has significant social value.

It should be noted that between October and December 2018, in accordance with banking and financial regulations, the Bank was subject to inspections by the Bank of Italy. The purpose of the inspections was to verify compliance with anti-money laundering legislation and the effectiveness of the organisational structures in reporting the AOER correctly and preventing the risks associated with violations of usury regulations. Upon completion of the inspections, the inspectors met with the Chairperson of the Board of Directors, the Chairperson of the Board of Statutory Auditors and the CEO, reporting to each of them, albeit informally, that the inspections did not reveal any significant weaknesses with respect to the effectiveness of the controls in place regarding the risks of money laundering, terrorism financing and usury, and that the departments under inspection had fully cooperated with them. The Bank has already implemented some of the recommendations made during the inspection, which are to be reported in the inspection report that is scheduled to be issued by the end of the first quarter of 2019.

THE MACROECONOMIC SCENARIO

In the last few months of 2018, the global economy continued to grow, although there were signs of cyclical deterioration in many advanced and emerging economies. The expansion which has taken place in the international economy is influenced by a number of risk factors: the repercussions stemming from the adverse outcome of trade negotiations between the United States and China, rising financial tensions in emerging countries, and the way in which the United Kingdom's exit from the European Union will be achieved. At the end of 2018, the United States continued to grow at a fairly robust rate and Japan has recovered after a marked contraction in output caused by natural disasters in the third quarter of the year.

The slowdown in economic activity in China that started at the beginning of the year continues despite the fiscal stimulus introduced by the government. In Brazil, macroeconomic conditions remain fragile, while in India cyclical expansion remains strong. At its meeting on 19 December, the Federal Reserve raised the target range for interest rates on federal funds by 25 basis points. The economic slowdown in the Euro Area continues: as shown in Economic Bulletin no. 1 2019 of 11 January 2019 issued by the Bank of Italy, GDP increased by 0.2%, a significant slowdown compared to previous periods (it had increased by 0.4% in the second quarter).

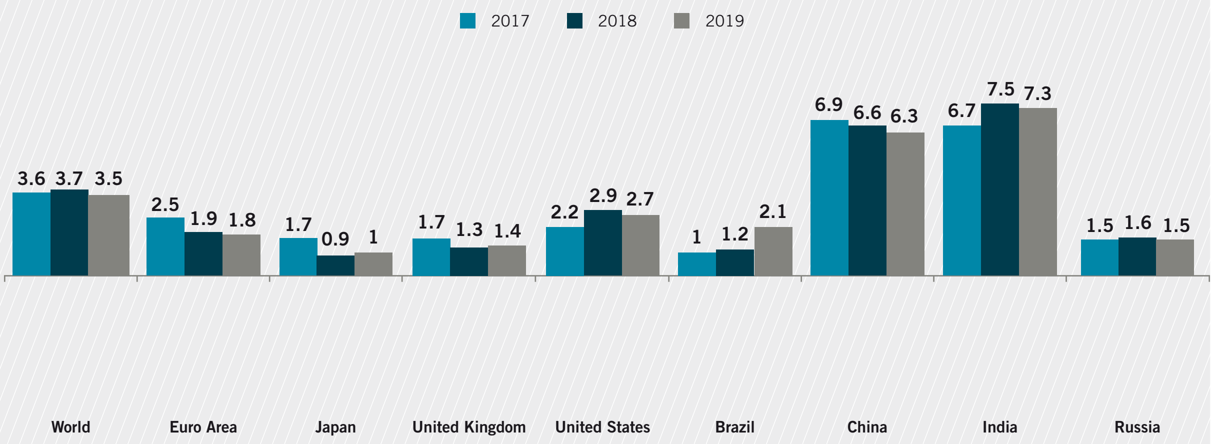
According to the estimates contained in the Bulletin, in the final months of the year industrial production fell more than expected. The €-coin indicator prepared by the Bank of Italy, which measures the underlying performance of the area's GDP, decreased, reaching the lowest level since the end of 2006 (0.42).

Inflation in December stood at 1.6%, down compared to previous months due to the slowdown in energy prices.

In the fourth quarter, yields on ten-year government bonds fell in all major economic areas. Lending to households and non-financial companies continues to grow in all major countries. In the final months of 2018, the Euro declined by 2% against the Dollar and its main trading partners, as expectations of a weakening of the common currency persist.

World macroeconomic scenario (GDP % change)

(Source OECD Economic Outlook, November 2018; Bank of Italy for world trade)



ITALY

In Italy there was a 0.1% drop in gross domestic product over the previous period, and according to estimates in the Economic Bulletin, GDP will continue to fall. The slowdown in activity was mainly due to the decline in investments and the slight drop in household spending.

Business confidence indicators have worsened. According to a survey carried out by the Bank of Italy, both the opinions on the general economic situation and those regarding the trend in demand have worsened.

Investments rose again in 2018 but were below the levels seen before the financial crisis. It is estimated that this growth will continue in 2019, although at a slower pace than in 2018.

The recovery in home sales continues while the construction sector has slowed. There was a slight decrease in household consumption in the closing months of 2018 (down 0.1% on the previous period), due to less than encouraging signs from the labour market. Disposable income net of inflation fell by 0.2% on the previous quarter, while the propensity to save continued to rise (8.1%). Italian household debt as a percentage of disposable income remained substantially unchanged and well below the average for the Euro Area (61.3%). Interest rates on new mortgages remained low (1.9% in October).

Exports picked up again after a sharp decline at the beginning of the year. The most substantial increase occurred mainly in the domestic markets of the European Union notwithstanding the sharp slowdown in sales to Germany. Increases were seen in the mechanical, electrical equipment and electronics sectors.

There was a slowdown in imports, mainly of means of transport, especially motor vehicles. In 2018, the current account surplus narrowed slightly compared to the previous year, but the decline in the trade surplus caused by increased spending for energy raw materials is offset by the growth in the primary income.

Purchases of foreign securities by residents amounted to € 51 billion, while purchases of Italian government bonds and Italian bank securities by non-resident investors decreased. Italian banks increased their foreign sourced net funding in the form of loans and deposits.

The number of hours worked continued to rise (+0.6% on the previous period), while the number of employed persons decreased, especially in the services to households and individuals sectors. The youth unemployment rate remained largely stable (32%).

Consumer price inflation fell to 1.2% in December as a result of the slowdown in energy prices. Core inflation remained low (0.5% in December) thanks mainly to a reduction in university tuition fees decided in the stability law for 2017, which slowed price growth in the early months of 2018. The slowdown in energy prices also led to lower producer price inflation for industrial products sold on domestic markets. Loans to non-financial companies have increased, particularly to firms in the manufacturing and service sectors, while loans to construction companies have decreased. The cost of credit remained very low. The impact of new non-performing loans on total loans granted by banking groups continued to decline (from 9.7% in the previous period to 9.4%), thanks to the implementation of plans to sell bad exposures. The return on equity, net of extraordinary income, increased to 6.1% compared to 4.4% in 2017.

Overall, the outlook described in the Economic Bulletin points to a slowdown in economic growth for 2019. The main risks to this outlook include overarching uncertainties and the possibility of a further rise in sovereign bond yields, a faster deterioration in private sector financing conditions and a further slowdown in firms' propensity to invest.

FACTORING

The Italian factoring market

According to preliminary sector data published by Assifact, in the year just ended the market recorded volume growth of 7.65%, well above the expectations of specialised observers and all the more significant if we consider that in June volumes were stable compared to the corresponding half of 2017. The acceleration in the second half of the year, thanks in part to high-value transactions carried out by some operators with retail debtors, made it possible to achieve a total turnover of over € 238 billion (14% of GDP). Without recourse factoring is by far the most common form used by the market accounting for 75% of total turnover, against 25% for with recourse transactions (for amounts outstanding, these percentages do not vary much: 73% against 27%), thereby confirming that the assigning customers prefer completing assignments by hedging the risk associated with the assigned debtors.

Receivables turnover remains at the same levels as last year due to the fact that average collection times remained substantially unchanged. Outstanding receivables (to be collected at 31 December 2018) totalled € 67.3 billion (+8.07%), while advances/consideration from assignments reached an impressive € 54.4 billion (+8.1%). Even the proportion of advances to outstanding receivables remained unchanged (80.81% compared to 80.84% in 2017), which allowed banks/intermediaries to maintain a conservative margin for any possible credit dilution risks.

Unlike the trend in bank loans, which was severely affected by the prolonged economic crisis that began in 2007, factoring did not experience the same repercussions in terms of its business, which, by contrast, continued to grow at a rapid pace (turnover steadily increased from € 120 billion in 2007 to the current € 238 billion), thus proving its resilience to negative economic cycles.

The capacity of the sector to support businesses even during the downward phase of the cycle is related to the operators' unique approach to managing risks, as evaluation is not limited to the party being financed, but mainly the quality of the receivables acquired and the solvency of the assigned debtors are also considered. The particular attention paid to the management of purchased or financed receivables and the constant monitoring of collections ensure that risk is kept at much lower levels than those of traditional bank loans.

The sector's low level of risk is also confirmed by the Assifact figures at 30 September 2018: gross non-performing loans amount to 6.33% of outstanding receivables (6.45% at the end of 2017), of which 1.69% related to past due exposures, 1.87% were unlikely to pay, and 2.78% were bad exposures (at the end of 2017 such exposures amounted to 3.04%). Net of adjustments, non-performing loans stood at 3.10%, considerably lower than those reported by commercial banks in their financing.

Factoring represents an important opportunity available to the business world - especially small and medium-sized enterprises - that provides access to essential sources of financing necessary for ensuring financial support for business continuity and growth.

The range of services offered (credit management, risk hedging and credit collection, just to name a few) and the excellent level of expertise attained over the years by factoring companies permit considerable simplification of supply relationships between the participants in the system despite the lack of structural changes in Italy.

Even large companies benefit considerably from factoring services: through without recourse factoring they are able to reduce working capital and improve their net financial position. They can also optimise the supply chain relationship with the various suppliers through Supply Chain Finance and reduce internal costs through the use of advanced technological platforms that banks/intermediaries can make available to them.

Through servicing, they also receive full support in managing relations with debtors - consider, for example, the Public Administration - thanks to the specific expertise and thorough monitoring guaranteed by the specialised operators.

SMEs represent 55% of assignor companies and, with regard to economic sectors, 29% are manufacturers, 11% are commercial enterprises and 9% are construction companies.

In the Italian market, one of the most developed not only in

Europe, but in the world, a significant share of turnover is made up of factored receivables due from the Public Administration with extremely long payment terms and complex bureaucratic procedures for recognising and reconciling the receivable.

According to estimates provided by Assifact, more than € 13 billion of outstanding receivables are due from Public Administration debtors, which represents 20% of all outstanding receivables. More than 40% of receivables are due from entities of the National Health Service, while the remaining 60% are receivables equally divided between those due from the Central Authorities and those due from Territorial Entities. The efforts made by the Government in recent years through the establishment of ad hoc funds aimed at rectifying the payment of certain, liquid and collectable pre-existing Public Administration debt, and the transposition of the EU regulation on late payments which exacerbated the amount of default interest for late payments beyond 60 days, have however led to only a slight reduction in payment times by the Public Administration, which today stand at just under 100 days, leading the European Commission to refer the Italian Government to the European Court for violating the directive. It should be noted that more than 55% of past due receivables from the Public Administration are over one year old.

In order to speed up the payment of the debts accumulated by the Public Administrations at 31 December 2018, the recent Budget Law allows the Territorial Entities and the National Health Service Companies to obtain treasury advances from Cassa Depositi e Prestiti at a variable rate (currently equal to 0.67%) against payment deductions. Unlike Decree Law 35 of 2013, under which non-recurring advances were used to reduce the stock of debt with repayment up to a maximum of 30 years and which effectively allowed for a reduction of accumulated debts by approximately € 40 billion, the new measure is unlikely to contribute to the reduction of the pre-existing stock, as the repayment of the advance must be made by 15 December 2019.

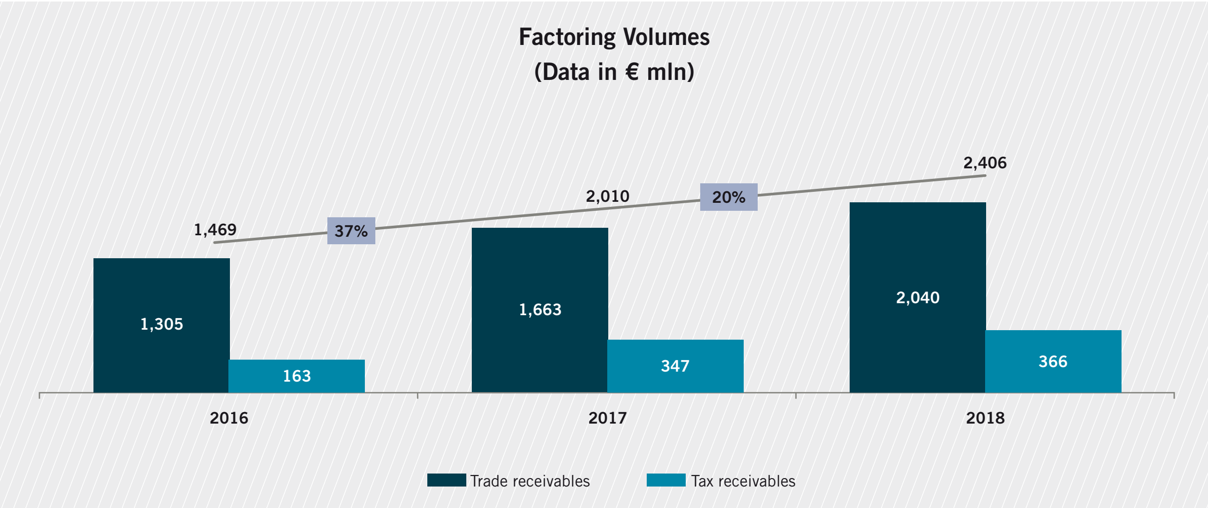
As to the relative effectiveness of the Late Payment Directive even in other EU countries, in the second half of 2018 the EU took action to monitor the EU countries and sent a questionnaire to the various stakeholders which aimed to identify possible new recommendations or suggestions.

The E.U.F.- European Federation for Factoring, bearing in mind the responses to the Assifact questionnaire, noted that a further tightening of the sanctions, which are already significant, would not lead to results different from those obtained so far due to the differences in bargaining power between assignors and large debtors who - if requested to pay default interest - would terminate the supply contract. It would be better to work through the various legal systems to eliminate the refusal to assign the receivables or to prevent the assigned debtors from not accepting the assignment, particularly where the assignors are SMEs, thus avoiding the effects that late payments would have on their working capital.

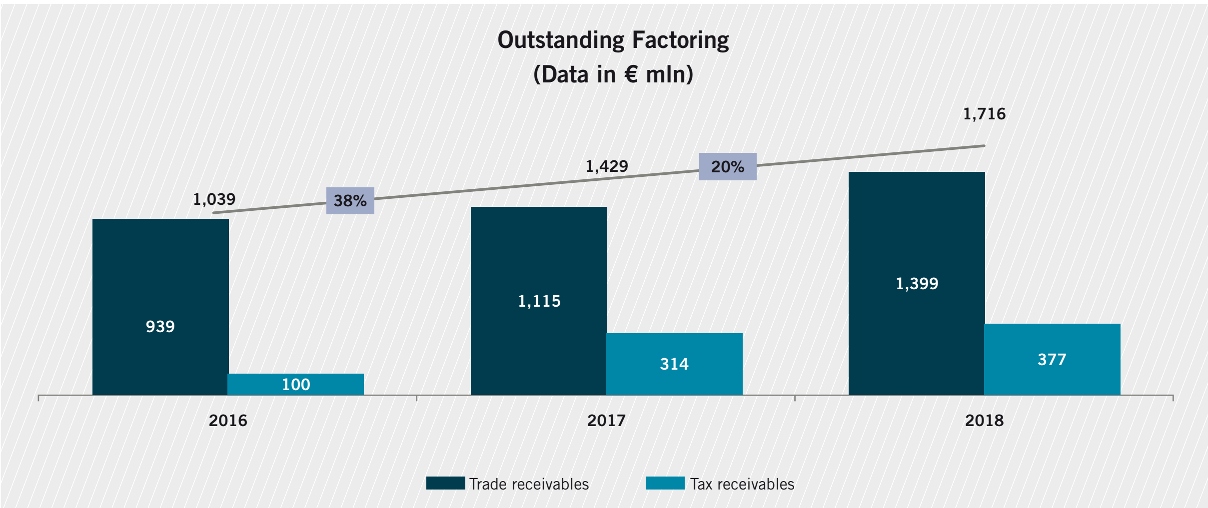
The projected decline in GDP, as evidenced over the last 10 years, is unlikely to affect the sector's performance as it will continue to play an important role in supporting businesses, even as commercial banks are struggling to increase their lending due to capital constraints.

Banca Sistema and factoring activities

Banca Sistema's total turnover in 2018 was € 2,406 million, up 20% on 2017, confirming its ability to continue growing year-on-year.

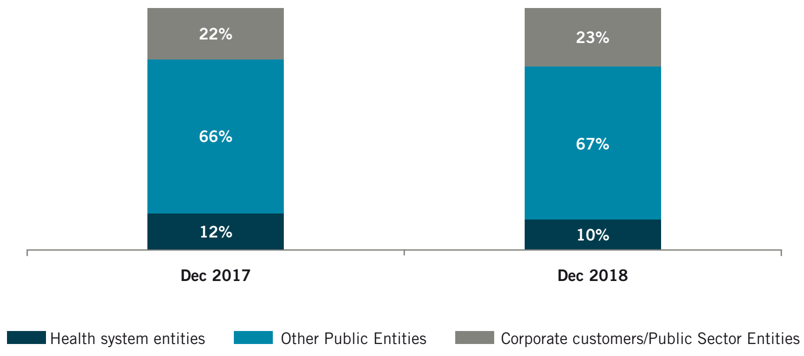


Outstanding loans as at 31 December 2018 amounted to € 1,716 million, up 20% on € 1,429 million at 31 December 2017 mainly due to increased volumes acquired in 2018 compared to collections during the same year.



The chart below shows the ratio of debtors to the total exposure in the outstanding loans and receivables portfolio at 31 December 2018 and 2017.

The Bank's core factoring business remains almost exclusively the Public Administration entities segment.



Turnover was generated through both its own internal commercial network, or through banks with which the Bank has entered into distribution agreements.

In 2018 the external networks accounted for 28% of total turnover. The following table shows the factoring turnover by product type:

PRODUCT (amounts in millions of Euro)	31.12.2018	31.12.2017	€ CHANGE	% CHANGE
Trade receivables	2,040	1,663	377	23%
of which, without recourse	*1,711*	*1,219*	*492*	*40%*
of which, with recourse	*329*	*444*	*(115)*	*-26%*
Tax receivables	366	347	19	5%
of which, without recourse	*353*	*339*	*14*	*4%*
of which, with recourse	*13*	*8*	*5*	*63%*
TOTAL	**2,406**	**2,010**	**396**	**20%**

In absolute terms, the growth in turnover derives mainly from the purchase of receivables from the public administration.

SALARY- AND PENSION-BACKED LOANS

Salary-backed loans (CQS) and Pension-backed loans (CQP)

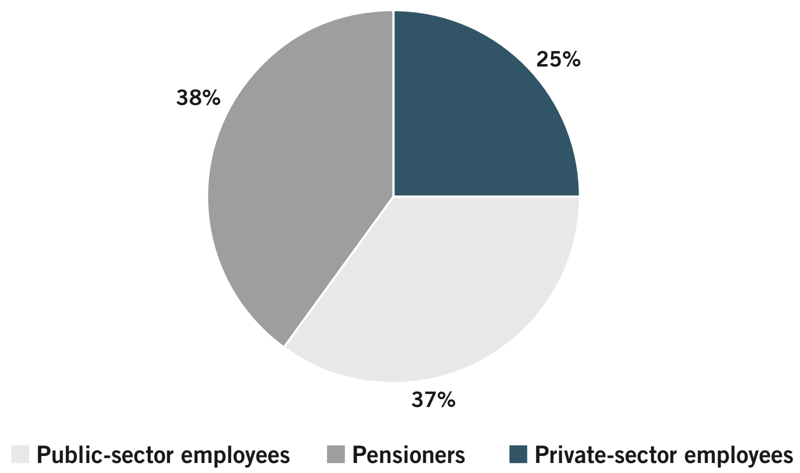
A salary- or pension-backed loan (CQS/CQP) is a consumer loan product that allows customers to allocate up to a fifth of their salaries or pensions to the payment of loan instalments. In 2018, the Bank acquired portfolios through agreements with specialist distributors in the sector.

The volumes acquired in 2018 amounted to € 212 million, including private-sector employees (25%), pensioners (38%) and public-sector employees (37%). Therefore, over 75% of the volumes refer to pensioners and employees of Public Administration, which remains the Bank's main debtor.

	31.12.2018	31.12.2017	€ CHANGE	% CHANGE
No. of applications	10,571	12,536	(1,965)	-16%
Volumes disbursed (millions of Euro)	212	258	(46)	-18%

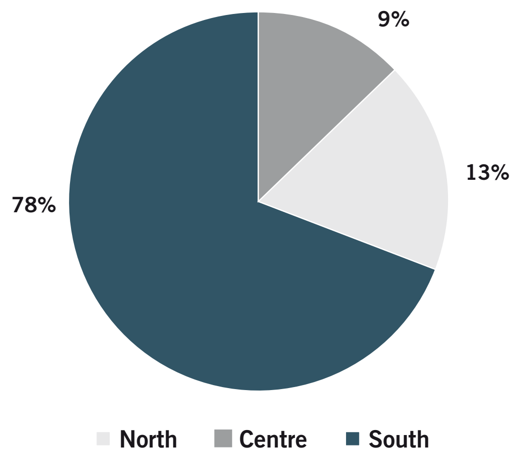
As inferred from the table, the amounts disbursed in 2018 are down slightly from what was disbursed in 2017.

CQ disbursed volumes - Breakdown



The geographical breakdown of the pension- and salary-backed loan portfolio is shown below:

CQ disbursed volumes - Breakdown by geographical area



FUNDING ACTIVITIES

Treasury portfolio

A treasury portfolio has been established in order to support liquidity commitments mainly through short-term investment in Italian government bonds.

The balance at 31 December 2018 increased compared to 31 December 2017 and was equal to a nominal € 735 million (compared to € 362.5 million at 31 December 2017). The increase in the treasury portfolio allowed for optimal management of the Treasury commitments which are increasingly characterised by a concentration of transactions in very specific periods.

In the first part of the year, the trend in the fair value of the securities portfolio was affected by the significant volatility of the markets associated with political uncertainties. During the fourth quarter, following the stabilisation of the Italian political situation, government bond yields and spreads between Italian and German bonds decreased.

At 31 December 2018, the nominal amount of securities in the HTCS (formerly AFS) portfolio amounts to € 300 million (compared to € 279 million as at 31 December 2017) with a duration of 1 year and 2 months (7.3 months in the previous year).

During 2018 the securities at amortised cost portfolio ("HTC" or "Held to Collect") was established again, made up entirely of Italian government securities. At 31 December, the HTC portfolio amounted to € 435 million with an average residual duration of 2 years and 2 months. The average duration of the total portfolio is 1 year and 9 months.

Wholesale funding

As at 31 December 2018, wholesale funding was about 41% of the total, mainly comprising bonds, inter-bank deposits and refinancing transactions with the ECB (51% as at 31 December 2017).

The 2018 issues of € 100 million of senior bonds maturing on 31 May 2021 and the reopening of the € 3 million subordinated loan maturing on 30 March 2027 have enabled a diversification of the sources of funding and an increase in their duration. The senior bond was issued at the end of May in a club deal reserved for institutional investors that are not related parties, for a total subscribed amount of € 90 million, a term of three years, with a fixed rate and an all-inclusive cost of 200 bps. This issue replaced the senior loan of € 75 million which expired in May.

The securitisation transactions of Quinto Sistema Sec. 2016 and Quinto Sistema Sec. 2017, completed with a partly-paid securities structure and "progressive growth of the securitised portfolio" (a "warehouse" structure), permitted an efficient and effective source of funding dedicated to the CQS portfolio. On 25 June 2018, the Quinto Sistema Sec. 2017 Senior securities (Class A) and Mezzanine securities (Class B1) of the salary- and pension-backed loan (CQ) securitisation transaction were given a rating by Moody's of Aa2 and Baa3, respectively (on 25 October downgraded to "Aa3" and "Ba1" respectively as a result of Moody's downgrading of the rating of the sovereign debt of the Italian Republic) and by DBRS (A-high and A-low, respectively) and were admitted to trading on the Luxembourg Stock Exchange. The Senior class securities can be used as collateral in Eurosystem refinancing transactions. Quinto Sistema Sec. 2017 is the second ABS transaction of salary- and pension-backed loans by Banca Sistema to be given a rating. The Quinto Sistema Sec. 2017 transaction later incorporated the loans portfolio from the first securitisation (whose securities have been fully reimbursed), thus bringing it to around € 400 million. After obtaining the rating, a ramp up period began, which allowed the transaction to reach approximately 440 million at the end of 2018 and which will end with an amount of € 508 million.

The transaction will allow Banca Sistema to continue to grow its salary-/pension-backed loan business, thus optimising its funding structure dedicated to this same segment.

The Bank also used the interbank deposit market both through the e-MID platform and through bilateral agreements with other banks. Existing bank deposits at 31 December 2018 totalled € 282 million. Such funding allows short-term treasury needs to be met by exploiting the moderate level of interest rates and enables the diversification of funding.

Retail funding

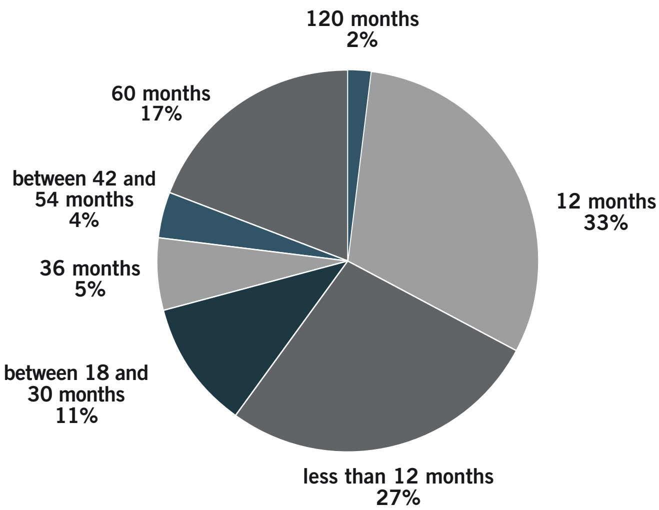
The funding policy of the banking division is strictly linked to changes in trade loans and market conditions.

Retail funding accounts for 59% of the total and is composed of the account SI Conto! Corrente and the product SI Conto! Deposito.

Total term deposits as at 31 December 2018 amounted to € 958 million, an increase of 114% compared to 31 December 2017. The above-mentioned amount also includes total term deposits of € 294 million (obtained with the help of partner platfor8s) held with entities resident in Germany, Austria and Spain (accounting for 31% of total deposit funding), an increase of € +169 million over the previous year.

The breakdown of funding by term is shown below. The average duration of the portfolio is 15 months.

Breakdown of deposit accounts as at 31 December 2018

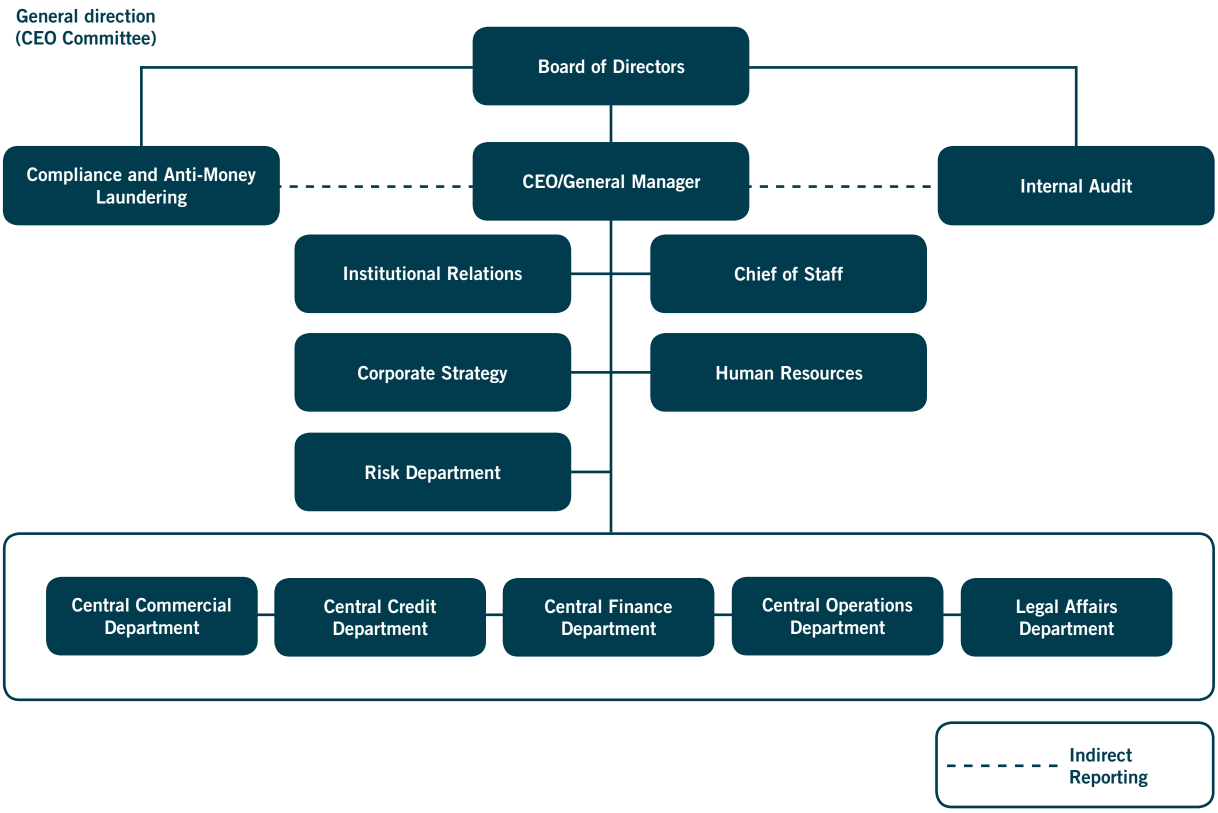


Current accounts decreased from 4,675 (as at 31 December 2017) to 4,492 as at 31 December 2018, while the current account balance at 31 December 2018 increased +29% on 2017 to € 657 million.

COMPOSITION AND ORGANISATIONAL STRUCTURE OF THE GROUP

Organisational chart

An updated organisational chart of Banca Sistema is shown below:



REGISTERED OFFICES AND BRANCHES OF THE BANCA SISTEMA GROUP

The Registered Offices and Branches of the Banca Sistema Group are as follows:

- Milan - Largo Augusto 1/A, at the corner of Via Verziere 13 (registered office and branch)
- Milan - Piazza Napoli, at the corner of Via Vespri Siciliani, 1 (collateralised loan branch)
- Rome - Via Romagna, 25 (bank and collateralised loan branch)
- Rome - Via Campania, 59 (Administrative office)
- Pisa - Galleria Chiti, 1 (bank and collateralised loan branch)
- Palermo - Via Bara all’Olivella 2 (administrative office)
- Palermo - Via Marco Polo 7 (collateralised loan branch)
- Naples - Via Verdi 35 (administrative office)
- Naples - Via Verdi 36 (collateralised loan branch)
- Rimini - Corso d’Augusto 68 (collateralised loan branch)
- Watford - (UK) CP House, Otterspool Way (Representative office)

HUMAN RESOURCES

As at 31 December 2018, the Bank had staff of 182, broken down by category as follows:

FTES	31.12.2018	31.12.2017
Senior managers	20	18
Middle managers (QD3 and QD4)	41	39
Other personnel	121	98
Total	**182**	**155**

During the year, 38 new resources joined the Group, mainly in the Factoring, Collateral and CQ commercial structures, in the departments that oversee the credit and collection process, in Compliance and Anti-Money Laundering, in Administration and Operations (14 replaced the same number of people who had left or were long-term absent and 24 to improve professional and managerial expertise).

During the year 11 employees left the Bank, of which 2 were senior managers and 2 were managers.

In addition, three senior managers were appointed respectively to the Legal Department, the Commercial Banking Department and the Risk Department, and five promoted to the manager category in General Management, Central Credit Department and Central Operations Department.

Over the course of the year the Bank realigned the organisational structure based on market changes and performance in order to support the achievement of its strategic objectives. The branches in Naples, Palermo and Rimini were opened, dedicated to collateralised lending and for which six specialised experts were hired.

During the year, various professional training courses were organised on issues relating to the Bank's regulatory scope, both with internal and external instructors. More specifically, training was provided on Privacy, Transparency, Legislative Decree 231 and Anti-Money Laundering, Mifid 2, Related Party Transactions and New Bankruptcy Law, with a total of 146 people participating. These programmes will continue during 2019 in order to complete the continuing professional development of the remaining employees.

The average age of Bank employees is 41 for men and 39 for women. The breakdown by gender remains essentially stable compared to 2017 with women accounting for 43% of the total.

INCOME STATEMENT RESULTS

INCOME STATEMENT (€,000)	2018	2017	€ Change	% Change
Net interest income	74,746	70,809	3,937	5.6%
Net fee and commission income	15,257	10,667	4,590	43.0%
Dividends and similar income	227	227	-	-
Net trading income (expense)	(125)	18	(143)	<100%
Gain from sales or repurchases of financial assets/liabilities	1,167	931	236	25.3%
Total income	**91,272**	**82,652**	**8,620**	**10.4%**
Net impairment losses on loans and receivables	(6,814)	(5,352)	(1,462)	27.3%
Net financial income	**84,458**	**77,300**	**7,158**	**9.3%**
Personnel expense	(19,811)	(17,549)	(2,262)	12.9%
Other administrative expenses	(20,710)	(19,259)	(1,451)	7.5%
Net accruals to provisions for risks and charges	(414)	(8)	(406)	>100%
Net impairment losses on property and equipment/intangible assets	(404)	(303)	(101)	33.3%
Other operating expense	(419)	(414)	(5)	1.2%
Operating costs	**(41,758)**	**(37,533)**	**(4,225)**	**11.3%**
Pre-tax profit from continuing operations	**42,700**	**39,767**	**2,933**	**7.4%**
Income taxes for the year	(14,629)	(12,207)	(2,422)	19.8%
Post- tax profit for the year	**28,071**	**27,560**	**511**	**1.9%**

The comparative figures represent a mere restatement of the statutory figures at 31 December 2017 in accordance with IFRS 9. Therefore, they do not represent the net amounts resulting from retrospective application of the aforementioned accounting standard and consequently are not perfectly comparable with each other.

Profit for 2018 amounted to € 28.1 million, an increase compared to the previous year, mainly due to an increase in total income that more than offset the normal growth in operating costs. In the third quarter of 2018, the expected rates of recovery of default interest on factoring and the related collection times used were updated in the light of the progressive consolidation of the historical data series; the adjustment of these estimates led to the recognition of higher interest income for 2018 of € 7.8 million, of which € 4.9 million attributable to previous years. The results for the previous year also benefited from the change in the estimate for the probability of collection of default interest which led to the recognition of higher interest income of € 9.6 million, of which € 3.7 related to prior years. Results in the prior year also benefited from a € 3.9 million release related to bad exposures with troubled local authorities and greater tax benefits which had a positive impact on lowering the tax rate.

NET INTEREST INCOME (€,000)	2018	2017	€ Change	% Change
Interest and similar income				
Loans and receivables portfolio	96,549	87,792	8,757	10.0%
Securities portfolio	258	203	55	27.1%
Other	1,404	521	883	>100%
Financial liabilities	1,679	1,777	(98)	-5.5%
Total interest income	**99,890**	**90,293**	**9,597**	**10.6%**
Interest and similar expense				
Due to banks	(2,536)	(1,603)	(933)	58.2%
Due to customers	(14,572)	(12,949)	(1,623)	12.5%
Securities issued	(6,992)	(3,809)	(3,183)	83.6%
Financial assets	(1,044)	(1,123)	79	-7.0%
Total interest expense	**(25,144)**	**(19,484)**	**(5,660)**	**29.0%**
Net interest income	**74,746**	**70,809**	**3,937**	**5.6%**

Net interest income was higher than the previous year, due to the contribution from the loans and receivables portfolio which more than offset the increase in interest expense which, in 2018, included the non-recurring interest expense component of € 0.8 million linked to the higher benefit provided by TLTRO II.

The total contribution of the factoring portfolio was € 75 million (equal to 78% of the entire loans and receivables portfolio), increasing by 6% over the previous year; when considering the commission component associated with the factoring business, the contribution increased by 10.4%. The component linked to default interest from legal action at 31 December 2018 was € 28.4 million (€ 26.8 million in 2017, excluding € 2.8 million related to the early termination of the guarantee agreement provided by the former shareholder of Beta Stepstone, the company acquired in 2016 and then merged into Banca Sistema the following year):

- of which € 18.1 million resulting from the actual recovery estimates (€ 7.8 million from the updated recovery estimates, of which € 4.9 million attributable to previous years: € 17.6 million in 2017, of which € 3.7 million from previous years);
- of which € 10.3 million (€ 9.2 million in 2017) coming from net collections during the year, i.e. the difference between the amount collected during the year, equal to € 19.2 million (€ 14.8 million in 2017) and what was recognised on an accruals basis in previous years.

The amount of the stock of default interest from legal actions accrued at 31 December 2018, relevant for the allocation model, was € 96 million (€ 92 million at the end of 2017) while the loans and receivables recognised in the financial statements amounted to € 42.5 million. The decrease in the stock compared to the € 100 million recognised in the third quarter of 2018 is attributable to collections from both debtors and, in part, from parties to whom some interest has been definitively assigned.

The positive impact on income was also driven by growth in interest on the salary- and pension-backed portfolios, which rose from € 13.1 million to € 19.6 million (an increase of 48% over the previous year), whereas interest declined on the SME portfolios, which contributed € 2.0 million to the total, following the strategic decision to discontinue this area of the business.

Beginning in 2018, the new financial statements require that the negative components of financial assets, for example securities, and the positive components of technical forms of funding be aggregated in the items interest expense and interest income respectively according to their sign (under the items “financial assets” and “financial liabilities”). As a result, financial liabilities include the interest income from funding through REPOs.

The “other" interest income mainly includes income generated from hot money transactions and interest generated by collateral-backed loan activities which contributed € 0.3 million.

The increase in the cost of funding compared to the previous year is closely related to the increase in average lending. In particular, there was an increase in interest on securities issued that was strictly related to the new bond issues, and therefore to higher stock compared to the previous year, which allowed for greater diversification in the forms of funding and a duration greater than the previous funding mix.

The cost of funding also includes reversal of the positive component coming from the previously expected rate of -40 bps on the amount resulting from participation in the TLTRO II auction (for € 123 million in June 2016), equal to € 0.8 million as previously recognised.

Financial assets at 31 December 2018 were largely composed of the negative yield on Italian government bonds and the above par acquisition of a loan portfolio consisting of collateral-backed loans.

NET FEE AND COMMISSION INCOME (€,000)	2018	2017	€ Change	% Change
Fee and commission income				
Collection activities	1,127	1,014	113	11.1%
Factoring activities	15,772	11,462	4,310	37.6%
Other	726	571	155	27.1%
Total fee and commission income	**17,625**	**13,047**	**4,578**	**35.1%**
Fee and commission expense				
Placement	(1,837)	(1,940)	103	-5.3%
Other	(531)	(440)	(91)	20.7%
Total fee and commission expense	**(2,368)**	**(2,380)**	**12**	**-0.5%**
Net fee and commission income	**15,257**	**10,667**	**4,590**	**43.0%**

Net fee and commission income of € 15.3 million increased by 43% due to the greater commissions from factoring. These should be considered together with interest income, since it makes no difference from a management point of view whether profit is recognised in the commissions and fees item or in interest in the without recourse factoring business.

Commissions on collection activities, related to the service of reconciliation of third-party invoices collected from Public Administration are in line with the previous year, while other fee and commission income, which primarily includes commissions and fees from collection and payment services, the keeping and management of current accounts, and fees related to the collateral-backed loan business, amounting to € 192 thousand, have increased.

The placement fees and commissions paid to third parties decreased slightly; they include the origination costs of factoring receivables of € 1,186 thousand (€ 1,405 thousand last year) while the remainder includes returns to third party intermediaries for the placement of the SI Conto! Deposito product on volumes placed in Germany, Austria and Spain.

Other commission expense includes commissions for trading third-party securities and for interbank collections and payment services.

PROFIT FROM THE SECURITIES PORTFOLIO (€,000)	2018	2017	€ Change	% Change
Net trading income (expense)				
Realised gains (losses)	(125)	18	(143)	<100%
Total	**(125)**	**18**	**(143)**	**<100%**
Gain from sales or repurchases				
Gains from HTCS portfolio debt instruments	1,167	931	236	25.3%
Total	**1,167**	**931**	**236**	**25.3%**
Total profit from the securities portfolio	**1,042**	**949**	**93**	**9.8%**

Net trading income (expense) is mainly generated by the market value of the Italian government bonds included in the trading portfolio that have suffered a decrease in fair value as a result of the continuing tensions in the financial markets. The short remaining duration of the securities in the trading portfolio sold during the fourth quarter of 2018 made it possible to recover the temporary loss from market valuation that had emerged at 30 September 2018. The gains generated by the proprietary HTCS portfolio made a greater contribution than in the previous year.

Impairment losses on loans and receivables at 31 December 2018 amounted to € 6.8 million and were up on the previous year, inasmuch as 2017 had been influenced by releases of € 3.9 million tied to bad exposures with troubled local authorities; net of these releases, these impairment losses are decreasing. On the other hand, while not significant, the new method resulting from the application of IFRS 9, which is based on an "expected loss" model compared to the previous "incurred loss" model, led to an increase in impairment losses on performing loans classified as stage 2. The loss rate at 31 December 2018 amounts to 33 bps.

PERSONNEL EXPENSE (€,000)	2018	2017	€ Change	% Change
Wages and salaries	(18,529)	(16,427)	(2,102)	12.8%
Social security contributions and other costs	(307)	(329)	22	-6.70%
Directors' and statutory auditors' remuneration	(975)	(793)	(182)	23.0%
Total	**(19,811)**	**(17,549)**	**(2,262)**	**12.9%**

The increase in personnel expense is mainly due to the increase in the average number of employees from 146 to 174, an increase in an additional cost component related to the variable portion and some new non-compete agreements executed.

OTHER ADMINISTRATIVE EXPENSES (€,000)	2018	2017	€ Change	% Change
IT expenses	(4,372)	(4,354)	(18)	0.4%
Consultancy	(3,696)	(3,150)	(546)	17.3%
Servicing and collection activities	(2,736)	(3,063)	327	-10.7%
Rent and related fees	(2,195)	(1,963)	(232)	11.8%
Indirect taxes and duties	(2,010)	(1,658)	(352)	21.2%
Resolution Fund	(942)	(807)	(135)	16.7%
Car hire and related fees	(858)	(863)	5	-0.6%
Expense reimbursement and entertainment	(726)	(697)	(29)	4.2%
Advertising	(568)	(284)	(284)	100.0%
Expenses related to management of the SPVs	(536)	(462)	(74)	16.0%
Insurance	(385)	(349)	(36)	10.3%
Other	(365)	(416)	51	-12.3%
Audit fees	(295)	(265)	(30)	11.3%
Membership fees	(265)	(262)	(3)	1.1%
Infoprovider expenses	(255)	(278)	23	-8.3%
Maintenance of movables and real properties	(235)	(112)	(123)	109.8%
Telephone and postage expenses	(175)	(177)	2	-1.1%
Stationery and printing	(96)	(99)	(3)	-3.0%
Total	**(20,710)**	**(19,259)**	**(1,451)**	**7.5%**

IT expenses, which represent the most significant cost, remained in line with the previous year despite the increase in business.

The increase in consulting expenses is mainly due to the costs incurred in 2018 for the assignment of the rating and admission to listing of the securities of the Quinto Sistema Sec. 2017 securitisation, which also included the merger of the previous Quinto Sistema Sec. 2016 securitisation into it.

The increase in indirect taxes and duties is mainly due to the increase in contributions paid for the enforceable injunctions deposited with Public Administration.

Contributions to the Resolution Fund, up again versus the previous year, amounted to € 942 thousand.

The Bank has never become a member of the Voluntary Deposit Guarantee Fund, but only of the mandatory fund. As such, the Bank did not contribute to the subscription of the subordinated bond issued by Carige.

Pro-forma total income

PRO-FORMA TOTAL INCOME (€,000)	2018	2017
Net interest income	74,746	70,809
Change in % expected recovery of default interest	7,746	(3,745)
Pro-forma net interest income	**82,492**	**67,064**
Net fee and commission income	15,257	10,667
Dividends and similar income	227	227
Net trading income (expense)	(125)	18
Gain from sales or repurchases of financial assets	1,167	931
Pro-forma total income	**99,018**	**78,907**

The figures for the years ended 31 December 2018 and 2017 set out above have been restated to emphasise and ensure the comparability of the accounting impact of the change in the estimate of the expected recovery of default interest.

In particular, total income has been restated as if the current probability of collection of default interest had also been applied in the previous years.

THE MAIN STATEMENT OF FINANCIAL POSITION AGGREGATES

The comments on the main aggregates on the asset side of the statement of financial position are shown below.

ASSETS (€,000)	31.12.2018	31.12.2017	€ Change	% Change
Cash and cash equivalents	288	161	127	78.9%
Financial assets measured at fair value through profit or loss		1,201	(1,201)	n.a.
Financial assets measured at fair value through other comprehensive income	304,469	285,610	18,859	6.6%
Financial assets measured at amortised cost	2,801,813	1,981,105	820,708	41.4%
a) loans and receivables with banks	56,694	35,809	20,885	58.3%
b1) loans and receivables with customers - loans	2,309,708	1,861,118	448,590	24.1%
b2) loans and receivables with customers - debt instruments	435,411	84,178	351,233	>100%
Equity investments	19,278	16,222	3,056	18.8%
Property and equipment	710	814	(104)	-12.8%
Intangible assets	1,788	1,790	(2)	-0.1%
Tax assets	7,626	10,083	(2,457)	-24.4%
Non-current assets held for sale and disposal groups	2,221	-	2,221	n.a.
Other assets	11,960	13,441	(1,481)	-11.0%
Total assets	**3,150,153**	**2,310,427**	**839,726**	**36.3%**

The comparative data represent a mere restatement of the statutory figures at 31 December 2017 in continuity with respect to the previously applicable accounting standard IAS 39. Therefore, they do not represent net amounts resulting from retrospective application of the new accounting standard IFRS 9. The reader is referred to the following paragraphs and notes to the financial statements for a description and presentation of the effects resulting from application of IFRS 9.

The year ended 31 December 2018 closed with total assets up 36.3% (at € 3.2 billion) on the end of 2017, mainly due to the effect of the increase in the portfolios of receivables with customers and the securities portfolio.

The government securities portfolio, which was included in the item Financial assets measured at fair value through profit or loss ("HTS"), was completely disposed of during the fourth quarter, thus recovering the temporary loss recognised until 30 September 2018.

The securities portfolio relating to Financial assets measured at fair value through other comprehensive income ("HTCS" or "Held to Collect and Sell") of the Bank is mainly comprised of Italian government bonds with an average remaining duration of about 1 year and 1.5 months (the average remaining duration at the end of 2017 was 7.3 months). This is consistent with the Bank investment policy. The government securities portfolio amounted to € 300 million at 31 December 2018 (€ 279 million at 31 December 2017). The associated valuation reserve was negative at the end of the year, amounting to € 1.5 million before the tax effect. In addition to government securities, the HTCS portfolio also includes 200 shares of the Bank of Italy, amounting to € 5 million and purchased in July 2015, and the Axactor Norway shares, which at 31 December 2018 had a break-even net fair value reserve, resulting in a year-end amount of € 1.2 million.

LOANS AND RECEIVABLES WITH CUSTOMERS (€,000)	31.12.2018	31.12.2017	€ Change	% Change
Factoring	1,566,613	1,285,726	280,887	21.8%
Salary-/pension-backed loans (CQS/CQP)	652,040	500,480	151,560	30.3%
Loans to SMEs	27,549	55,581	(28,032)	-50.4%
Current accounts	38,473	16,803	21,670	>100%
Pledge on receivables	6,428	1,366	5,062	>100%
Compensation and Guarantee Fund	17,413	865	16,548	>100%
Other loans and receivables	1,192	297	895	>100%
Total loans	**2,309,708**	**1,861,118**	**448,590**	**24.1%**
Securities	435,411	84,178	351,233	>100%
Total loans and receivables with customers	**2,745,119**	**1,945,296**	**799,823**	**41.1%**

The item loans and receivables with customers under Financial assets measured at amortised cost (hereinafter HTC, or "Hold to Collect"), is composed of loan receivables with customers and, beginning in 2018, the securities portfolios that were classified separately until 31 December 2017 in the line "held-to-maturity securities".

Outstanding loans for factoring receivables compared to the total in the item, excluding the amounts of the securities portfolio, were unchanged from the end of 2017 at 68%. Their absolute value grew as a result of turnover generated during the year which was up by 20% compared to last year to € 2,406 million (€ 2,010 million at 31 December 2017). Salary- and pension-backed loans grew in terms of their outstanding amount thanks to new loans, which fell by 18% compared to the previous year (the new volumes acquired during the year amounted to € 212 million), while government-backed loans to SMEs fell, which is in line with the strategic decision to discontinue this line of business.

At the end of 2016, the Bank began developing the collateralised loan business. Accordingly, in addition to the Milan, Rome and Pisa branches, the branches in Naples, Palermo and Rimini were opened. Outstanding volumes at 31 December 2018, totalling € 6.4 million, are the result of loans granted during the year of € 9.2 million, which includes the acquisition of three portfolios of third party receivables amounting to € 1.9 million.

The increase in exposure to the Compensation and Guarantee Fund is due to the increase in the number of repurchase agreements as well as to the increased volatility of the underlying securities.

Securities are composed entirely of Italian government securities with an average duration of 2 years and 2 months for an amount of € 435 million.

The following table shows the quality of receivables in the loans and receivables with customers item, excluding the securities positions.

STATUS	31.12.2017	31.03.2018	30.06.2018	30.09.2018	31.12.2018
Bad exposures	44,577	44,867	53,412	60,566	57,467
Unlikely to pay	24,061	37,621	30,765	31,305	87,189
Past due	74,690	76,626	89,355	97,263	80,507
Non-performing	**143,328**	**159,114**	**173,532**	**189,134**	**225,163**
Performing	**1,745,673**	**1,788,833**	**2,016,559**	**2,122,685**	**2,119,998**
Stage 2	-	73,131	67,260	101,813	106,473
Stage 1	-	1,715,702	1,949,299	2,020,872	2,013,525
Total loans and receivables with customers	**1,889,001**	**1,947,947**	**2,190,091**	**2,311,819**	**2,345,161**
Individual impairment losses	**22,293**	**23,413**	**26,629**	**27,662**	**29,169**
Collective impairment losses	**5,590**	**5,324**	**5,496**	**5,856**	**6,284**
Stage 2	-	454	437	569	579
Stage 1	-	4,870	5,059	5,287	5,705
Total impairment losses	**27,883**	**28,737**	**32,125**	**33,518**	**35,453**
Net exposure	**1,861,118**	**1,919,210**	**2,157,966**	**2,278,301**	**2,309,708**

The ratio of gross non-performing loans to the total portfolio went from 7.6% at 31 December 2017 to 9.6% at the end of 2018. The increase in the absolute value of non-performing loans compared to 31 December 2017 is mainly due to a new factoring position with a local authority: since local authorities are not subject to bankruptcy and knowing that the receivable will be collected in full, including default interest, there are doubts as to whether it is correct to classify it as non-performing. In-depth analyses are underway to understand whether substance should prevail over form. If the substance prevails, the receivables from troubled local authorities that are not subject to bankruptcy proceedings should no longer be included among non-performing loans. The amount of past due loans is attributed to factoring receivables without recourse from Public Administration and is considered normal for the sector and does not represent an issue in terms of credit quality and probability of collection.

Net bad exposures remained at moderate levels and amounted to 1.7% of total loans and receivables with customers, while the coverage ratio of non-performing loans was equal to 13%.

Equity investments include the acquisition for € 0.6 million of a 19.90% stake in the share capital of ADV Finance S.p.A. (“ADV Finance”), and 19.90% of its subsidiary Procredit S.r.l. for € 0.2 million, as well as LASS S.r.l., the Group's real estate company. During the fourth quarter, the 10% equity investment in Axactor Italy S.p.A. was reclassified under Non-current assets held for sale and disposal groups, following the Board of Directors' resolution of December 2018 to sell the same equity investment through the exercise of the put option provided for in the contract. The carrying amount, which according to the International Financial Reporting Standards is the lower of the carrying amount and the fair value, is € 2,221 thousand.

Other assets include amounts being processed after the end of the year and advance tax payments of approximately € 7.5 million.

Comments on the main aggregates on the liability side of the statement of financial position are shown below.

LIABILITIES AND EQUITY (€,000)	31.12.2018	31.12.2017	€ Change	% Change
Financial liabilities measured at amortised cost	2,902,240	2,083,435	818,805	39.3%
a) due to banks	695,197	517,533	177,664	34.3%
b) due to customers	1,902,056	1,284,132	617,924	48.1%
c) securities issued	304,987	281,770	23,217	8.2%
Tax liabilities	15,676	10,118	5,558	54.9%
Other liabilities	65,234	71,916	(6,682)	-9.3%
Post-employment benefits	2,402	2,172	230	10.6%
Provisions for risks and charges	9,221	6,698	2,523	37.7%
Valuation reserves	(1,131)	367	(1,498)	<100%
Reserves	118,988	98,659	20,329	20.6%
Share capital	9,651	9,651	-	-
Treasury shares (-)	(199)	(149)	(50)	33.6%
Profit for the year	28,071	27,560	511	1.9%
Total liabilities and equity	**3,150,153**	**2,310,427**	**839,726**	**36.3%**

The comparative data represent a mere restatement of the statutory figures at 31 December 2017 in continuity with respect to the previously applicable accounting standard IAS 39. Therefore, they do not represent net amounts resulting from retrospective application of the new accounting standard IFRS 9.

Wholesale funding, which represents about 41% (51% at 31 December 2017) of the total, rose in absolute terms from the end of 2017 following the increase in ECB deposits. The contribution of bond funding to total wholesale funding was 34.2% (36.5% at 31 December 2017).

DUE TO BANKS (€,000)	31.12.2018	31.12.2017	€ Change	% Change
Due to Central banks	412,850	192,064	220,786	>100%
Due to banks	282,347	325,469	(43,122)	-13.2%
Current accounts and demand deposits	*53*	*13,969*	*(13,916)*	*-99.6%*
Term deposits	*282,294*	*311,500*	*(29,206)*	*-9.4%*
Totale	**695,197**	**517,533**	**177,664**	**34.3%**

The total of the sub-item "Due to banks" increased by 34.3% compared to 31 December 2017 due to the increase in funding through refinancing with the ECB, whose underlying assets are primarily ABS from the salary- and pension-backed loans (CQS/CQP) securitisation.

DUE TO CUSTOMERS (€,000)	31.12.2018	31.12.2017	€ Change	% Change
Term deposits	958,193	447,093	511,100	>100%
Financing (repurchase agreements)	179,819	215,623	(35,804)	-16.6%
Current accounts	660,582	510,349	150,233	29.4%
Due to assignors	87,397	72,108	15,288	21.2%
Other payables	16,065	38,959	(22,894)	-58.8%
Total	**1,902,056**	**1,284,132**	**617,924**	**48.1%**

Customer deposits increased compared to the end of the year, mainly due to an increase in funding from term deposits and partly from current accounts. The year-end amount of term deposits increased by more than 100% compared to the end of 2017, reflecting net positive deposits (net of interest accrued) of € 469 million; gross deposits from the beginning of the year were € 1,071 million, against withdrawals caused mainly by non-renewals totalling € 603 million.

Due to customers also includes financing of € 16 million from Cassa Depositi e Prestiti obtained against collateral consisting solely of loans to SMEs by the Bank.

Due to assignors includes payables related to receivables acquired but not financed.

SECURITIES ISSUED (€,000)	31.12.2018	31.12.2017	€ Change	% Change
Bond - Tier I	8,017	8,017	-	-
Bond - Tier II	31,570	28,703	2,867	10.0%
Bonds - other	265,400	245,050	20,350	8.3%
Total	**304,987**	**281,770**	**23,217**	**8.2%**

The nominal amount of securities issued at 31 December 2018 is broken down as follows:

- Tier 1 subordinated loan of € 8 million, with no maturity (perpetual basis) and a fixed coupon until 18 December 2022 at 7%;
- Tier 2 subordinated loan of € 12 million, set to mature on 15 November 2022 and with a variable coupon equal to 6-month Euribor + 5.5%;
- Tier 2 subordinated loan of € 19.5 million, set to mature on 30 March 2027 and with a variable coupon equal to 6-month Euribor + 4.5%;
- Senior bonds (market placement) of € 175 million, set to mature on 13 October 2020 and with a fixed coupon of 1.75%;
- Senior bonds (private placement) of € 90 million, set to mature on 31 May 2021 and with a fixed coupon of 2%.

At the end of May a senior bond was successfully issued in a club deal reserved for institutional investors that are not related parties, for a total subscribed amount of € 90 million, a term of three years, with a fixed rate and an all-inclusive cost of 200 bps. This issue replaced the senior loan of € 75 million which expired in May.

The provision for risks and charges of € 9.2 million includes the estimated liabilities attributable to the Beta acquisition, the estimated portion of the bonus for the year, the deferred portion of the bonus accrued in previous years, and the update to the estimate related to the non-compete agreement. The provision also includes an estimate of the charges relating to legal actions within the framework of a lending transaction in which the end borrower is bankrupt, and the estimated charges for labour-related lawsuits and legal disputes.

Other liabilities mainly include payments received after the end of the year from the assigned debtors and which were still being allocated and items being processed during the days following year-end, as well as trade payables and tax liabilities.

CAPITAL ADEQUACY

Provisional information concerning the regulatory capital and capital adequacy of Banca Sistema is shown below.

OWN FUNDS (€,000) AND CAPITAL RATIOS	31.12.2018	31.12.2017
Common Equity Tier 1 (CET1)	**146,549**	**127,119**
ADDITIONAL TIER 1	8,000	8,000
Additional Tier 1 capital (T1)	**154,549**	**135,119**
TIER2	28,799	28,239
Total Own Funds (TC)	**183,348**	**163,358**
Total risk weighted assets	**1,308,721**	**1,049,315**
of which, credit risk	1,152,293	900,968
of which, operational risk	156,428	142,829
of which, market risk	-	2,402
of which, CVA	-	3,116
CET1	**11.2%**	**12.1%**
T1	**11.8%**	**12.9%**
TCR	**14.0%**	**15.6%**

Total own funds were € 183.3 million at 31 December 2018 and included the profit for the year, net of dividends estimated on the profit for the year which were equal to a pay-out of 25% of Banca Sistema's profit.

The increase in RWAs compared to 31 December 2017 was primarily due to the increase in loans, particularly salary- and pension-backed loans and non-performing loans.

Starting from 1 January 2019, as a result of the increase in the capital conservation buffer from 1.875% to 2.500%, the OCR (Overall Capital Requirement) for Banca Sistema is as follows:

- CET1 ratio of 7.750% + additional +0.75% above the minimum regulatory requirement;
- TIER1 ratio of 9.500% + additional +1.0% above the minimum regulatory requirement;
- Total capital ratio of 11.850% + additional +1.35% above the minimum regulatory requirement.

The additional ratios remained unchanged from those already communicated last year.

At the ECOFIN meeting of 4 December 2018, a number of amendments to EU Regulation no. 575/2013, better known as the "CRR", were approved, including the reduction of the risk capital weighting for salary- (CQS) and pension-backed (CQP) loans. The amendment reduces the weighting to 35% from the current 75% for salary- and pension-backed personal loans. The deadline for its entry into force has not yet been set, as it may be at the same time as its publication in the Official Journal or it may be postponed for a certain amount of time.

CAPITAL AND SHARES

Capital and ownership structure

The share capital of Banca Sistema is composed of 80,421,052 ordinary shares, for a total paid-in share capital of € 9,650,526.24. All outstanding shares have regular dividend entitlement from 1 January.

Based on evidence from the Shareholders' Register and more recent information available, as at 11 February 2019 the shareholders with stakes of more than 5%, the threshold above which Italian law (art. 120 of the Consolidated Finance Act) requires disclosure to the investee and Consob, were as follows:

SHAREHOLDERS	% HELD
SGBS S.r.l.	23.10%
Garbifin	0.51%
Fondazione Sicilia	7.40%
Fondazione Cassa di Risparmio di Alessandria	7.91%
Fondazione Pisa	7.61%
Market	*53.47%*

Treasury shares

At 31 December 2018, after the launch in 2018 of a plan for the repurchase of treasury shares designed to create a stock of securities to be used for the incentive plan for the Group's key personnel, the Bank held 104,661 shares (equal to 0.13% of the share capital).

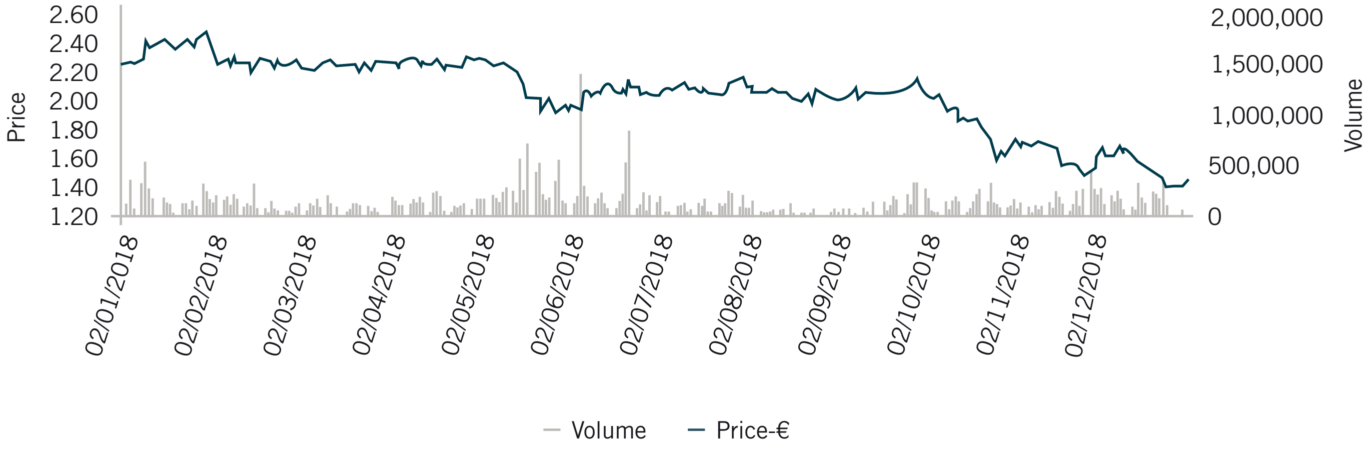
Stock performance

The shares of Banca Sistema are traded on the Mercato Telematico Azionario - Italian Equities Market (MTA) of the Italian Stock Exchange, STAR segment. The Banca Sistema stock is included in the following Italian Stock Exchange indices:

- FTSE Italia All-Share Capped;
- FTSE Italia All-Share;
- FTSE Italia STAR;
- FTSE Italia Servizi Finanziari;
- FTSE Italia Finanza;
- FTSE Italia Small Cap.

Investor Relations

During 2018, the Bank, in addition to the information provided through press releases and earnings conference calls with the market, also met with analysts and institutional investors, the latter both collectively and individually, for a total of around 150 investors (over 15% more than in 2017), also thanks to the participation in 16 events, including Conferences and Roadshows, in 8 European cities.



Source: Bloomberg

Reclassification reconciliation statement as at 31 December 2017

Below is a reconciliation statement between the approved financial statements at 31 December 2017, and the financial statements in accordance with the new Circular no. 262 from the Bank of Italy. Therefore, it does not represent net amounts resulting from retrospective application of the new accounting standard IFRS 9.

Statement of financial position - Liabilities	31.12.2017	Due to banks	Due to customers	Securities issued	Tax liabilities	Other liabilities	Post-employment benefits	Provisions for risks and charges	Equity	Total
Financial liabilities measured at amortised cost	2,083,434,873	-	-	-	-	-	-	-	-	**2,083,434,873**
a) due to banks	*517,532,691*	*517,532,691*	-	-	-	-	-	-	-	***517,532,691***
b) due to customers	*1,284,131,980*	-	*1,284,131,980*	-	-	-	-	-	-	***1,284,131,980***
c) securities issued	*281,770,202*	-	-	*281,770,202*	-	-	-	-	-	***281,770,202***
Tax liabilities	10,117,999	-	-	-	10,117,999	-	-	-	-	**10,117,999**
Other liabilities	71,916,098	-	-	-	-	71,916,098	-	-	-	**71,916,098**
Post-employment benefits	2,171,668	-	-	-	-	-	2,171,668	-	-	**2,171,668**
Provisions for risks and charges	6,698,378	-	-	-	-	-	-	6,698,378	-	**6,698,378**
Equity	136,087,543	-	-	-	-	-	-	-	136,087,543	**136,087,543**
Total liabilities and equity	**2,310,426,559**	**517,532,691**	**1,284,131,980**	**281,770,202**	**10,117,999**	**71,916,098**	**2,171,668**	**6,698,378**	**136,087,543**	**2,310,426,559**

Statement of financial position - Assets	31.12.2017	Cash and cash equivalents	Financial assets held for trading	Available-for-sale financial assets	Held-to-maturity investments	Loans and receivables with banks	Loans and receivables with customers	Equity investments	Property and equipment	Intangible assets	Tax assets	Other assets	Total
Cash and cash equivalents	160,897	160,897	-	-	-	-	-	-	-	-	-	-	160,897
Financial assets measured at fair value through profit or loss	1,201,206	-	1,201,206	-	-	-	-	-	-	-	-	-	1,201,206
Financial assets measured at fair value through other comprehensive income	285,609,813	-	-	285,609,813	-	-	-	-	-	-	-	-	285,609,813
Financial assets measured at amortised cost	1,981,105,317	-	-	-	-	-	-	-	-	-	-	-	1,981,105,317
a) loans and receivables with banks	35,808,941	-	-	-		35,808,941		-	-	-	-	-	35,808,941
b) loans and receivables with customers	1,945,296,376	-	-	-	84,177,932	-	1,861,118,444	-	-	-	-	-	1,945,296,376
Equity investments	16,221,580	-	-	-	-	-	-	16,221,580	-	-	-	-	16,221,580
Property and equipment	813,636	-	-	-	-	-	-	-	813,636	-	-	-	813,636
Intangible assets	1,789,816	-	-	-	-	-	-	-	-	1,789,816	-	-	1,789,816
Tax assets	10,083,293	-	-	-	-	-	-	-	-	-	10,083,293	-	10,083,293
Other assets	13,441,001	-	-	-	-	-	-	-	-	-	-	13,441,001	13,441,001
Total Assets	**2,310,426,559**	**160,897**	**1,201,206**	**285,609,813**	**84,177,932**	**35,808,941**	**1,861,118,444**	**16,221,580**	**813,636**	**1,789,816**	**10,083,293**	**13,441,001**	**2,310,426,559**

An equity reconciliation statement is shown below with a description of the impact from application of IFRS 9. Additional details are provided in the Accounting policies section.

Book equity at 31 December 2017 (IAS 39)	**136,088**
FTA reserve	**(224)**
Application of the new impairment model	**(224)**
Performing loans (stages 1 and 2)	(273)
Non-performing loans (stage 3)	-
Debt instruments	(61)
Tax effect	110
Classification and measurement effects	**527**
Adjustment of carrying amount of financial assets deriving from application of the Business Model as a balancing entry for the valuation reserve	787
Tax effect	(260)
Total effects of transition to IFRS 9	**303**
Book equity at 1 January 2018 (IFRS 9)	**136,391**

Application of the new impairment rules ("expected credit losses") has resulted in:

- Greater impairment losses on performing loans by € 334 thousand (€ 224 thousand net of the tax effect), substantially related to the portion of the performing portfolio in Stage 2, based on the defined stage allocation criteria, with the consequent need to calculate the expected loss for the entire residual lifetime of the financial assets;
- Greater impairment losses on performing securities by € 61 thousand (€ 50 thousand net of the tax effect), mainly related to inclusion in the calculation of expected losses of new parameters set by the standard.

No additional impairment losses have been recognised on non-performing loans.

The impact deriving from first-time adoption of IFRS 9 on the consolidated CET 1 ratios of the Group is 2 bps. Therefore, the Bank has decided to allocate this impact in full to Equity.

RISK MANAGEMENT AND SUPPORT CONTROL METHODS

With reference to the functioning of the "Risk Management System", the Bank has adopted a system based on four leading principles:

- suitable supervision by relevant bank bodies and departments;
- suitable policies and procedures to manage risks (both in terms of credit risk and the granting of loans);
- suitable methods and instruments to identify, monitor and manage risks, with suitable measuring techniques;
- thorough internal controls and independent audit.

The "Risk Management System" is monitored by the Risk Department, which ensures that capital adequacy and the degree of solvency with respect to its business are kept under constant control.

The Risk Department continuously analyses the Bank's operations to fully identify the risks the Bank is exposed to (risk map).

To reinforce its ability to manage corporate risks, the Bank has set up a Risk and ALM Committee, whose mission is to help the Bank define strategies, risk policies, and profitability and liquidity targets.

The Risk and ALM Committee continuously monitors relevant risks and any new or potential risks arising from changes in the working environment or Bank forward-looking operations.

Pursuant to the eleventh amendment of Bank of Italy Circular no. 285/13, within the framework of the Internal Control System (Part I, Section IV, Chapter 3, Subsection II, Paragraph 5) the Bank entrusted the Internal Control and Risk Management Committee with the task of coordinating the second and third level Control Departments; to that end, the Committee allows the integration and interaction between these Departments, encouraging cooperation, reducing overlaps and supervising operations.

With reference to the risk management framework, the Bank adopts an integrated reference framework both to identify its own risk appetite and for the internal process of determining capital adequacy. This system is the Risk Appetite Framework (RAF), designed to make sure that the growth and development aims of the Bank are compatible with capital and financial solidity.

The RAF comprises monitoring and alert mechanisms and related processes to take action in order to promptly intervene in the event of discrepancies with defined targets. The framework is subject to annual review based on the strategic guidelines and regulatory changes.

The ICAAP (the Internal Capital Adequacy Assessment Process) allows the Bank to conduct ongoing tests of its structure for determining risks and to update the related safeguards included in its RAF.

With regard to protecting against credit risk, along with the well-established second level controls and the periodic monitoring put in place by the Risk Management Department, a specific project has been implemented related to the introduction of the new IFRS 9 "Financial Instruments" which will be mandatory starting from 1 January 2018. This initiative enabled the determination of the qualitative and quantitative impact on the financial statements, and the identification and implementation of the necessary organisational, internal policy and applicable IT system changes.

Regarding the monitoring of credit risk, the Bank, with the goal of attaining greater operating synergies, has incorporated the Collection Department into the Underwriting Department, and renamed it Central Credit Department. This Department reports directly to the CEO.

It should also be noted that, in accordance with the obligations imposed by the applicable regulations, each year the Bank publishes its report (Pillar 3) on capital adequacy, risk exposure and the general characteristics of the systems for identifying, measuring and managing risks. The report is available on the website www.bancasistema.it in the Investor Relations section.

In order to measure "Pillar 1 risks", the Bank has adopted standard methods to calculate the capital requirements for Prudential Regulatory purposes. In order to evaluate "Pillar 2 risks", the Bank adopts - where possible - the methods set out in the Regulatory framework or those established by trade associations. If there are no such indications, standard market practices by operators working at a level of complexity and with operations comparable to those of the Bank are assessed.

OTHER INFORMATION

Report on corporate governance and ownership structure

Pursuant to art. 123-bis, paragraph 3 of Legislative Decree no. 58 dated 24 February 1998, a "Report on corporate governance and ownership structure" has been drawn up; the document - published jointly with the draft separate financial statements as at and for the year ended 31 December 2017 - is available in the "Governance" section of the Banca Sistema website (www.bancasistema.it).

Remuneration Report

Pursuant to section 84-quater, paragraph 1 of the Issuers' Regulation implementing Legislative Decree No. 58 dated 24 February 1998, a "Remuneration Report" has been drawn up; the document - published jointly with the draft separate financial statements as at and for the year ended 31 December 2017 - is available in the "Governance" section of the Banca Sistema website (www.bancasistema.it).

Research and Development Activities

No research and development activities were carried out in 2018.

RELATED PARTY TRANSACTIONS

Related party transactions including the relevant authorisation and disclosure procedures, are governed by the "Procedure governing related party transactions" approved by the Board of Directors and published on the internet site of Banca Sistema S.p.A. Transactions between Group companies and related parties were carried out in the interests of the Bank, including within the scope of ordinary operations; these transactions were carried out in accordance with market conditions and, in any event, based on mutual financial advantage and in compliance with all procedures.

ATYPICAL OR UNUSUAL TRANSACTIONS

During 2018, the Bank did not carry out atypical or unusual transactions, as defined in Consob Communication 6064293 dated 28 July 2006.

SIGNIFICANT EVENTS AFTER THE REPORTING DATE

On 9 January 2019, a put option was exercised that consists of the sale of all the shares of Axactor Italy that the parent Axactor AB is obliged to buy, as provided for in Article 3.5 of the existing shareholders' agreement, which is scheduled for 4 February 2019 for a price of € 2,399 thousand.

On 22 February 2019, the shareholders and quotaholders of Banca Sistema, Società di Gestione delle Partecipazioni in Banca Sistema S.r.l., Fondazione Sicilia and Fondazione Cassa di Risparmio di Alessandria, announced that they had determined that Article 3 (Board of Directors and Committees) and Article 5 (Consultation at the Shareholders' Meeting) of the Shareholders' Agreement, which became effective on 2 July 2018 and will expire on 1 July 2020, are not effective. The other provisions of the Agreement remain valid. These decisions do not affect the current composition of the Board of Directors, which will remain in office until it approves the financial statements as at and for the year ending 31 December 2020. An abstract of the Shareholders' Agreement, including the above amendments, which was drafted pursuant to article 129 of the Issuers' Regulation approved by Consob Resolution no. 11971/99, and essential information pursuant to article 130 of the Issuers' Regulation have been made available on the Parent's website www.bancasistema.it and on the storage mechanism authorised by Consob www.1info.it in accordance with the legal terms.

After the reporting date of these financial statements, there were no events worthy of mention which would have had an impact on the financial position, results of operations and cash flows of the Bank.

BUSINESS OUTLOOK AND MAIN RISKS AND UNCERTAINTIES

The 2018 financial year ended with continuing growth in volumes in the factoring sector and in terms of salary- and pension-backed loans.

In 2019, the Bank will continue to follow the guidelines set out in the business plan and will continue to evaluate options for non-organic growth in the Bank's core business areas.

PROPOSED ALLOCATION OF PROFIT FOR THE YEAR

Dear Shareholders,

The separate financial statements as at and for the year ended 31 December 2018, which we submit for your approval, show a profit for the year of € 28,070,559.59. We recommend allocating the profit for the year as follows:

- a dividend of € 6,996,631.52;
- the remainder of € 21,073,928.07 to retained earnings.

An allocation to the Legal Reserve was not made since the limits set out in Article 2430 of the Italian Civil Code were reached.

Milan, 1 March 2019

On behalf of the Board of Directors

The Chairperson

Luitgard Spögler

The CEO

Gianluca Garbi

SEPARATE FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION

(Amounts in Euros)

	Assets	31.12.2018	31.12.2017 (*)
10.	Cash and cash equivalents	288,431	160,897
20.	Financial assets measured at fair value through profit or loss	-	1,201,206
	a) financial assets held for trading	-	1,201,206
30.	Financial assets measured at fair value through other comprehensive income	304,469,478	285,609,813
40.	Financial assets measured at amortised cost	2,801,812,681	1,981,105,317
	a) loans and receivables with banks	56,694,080	35,808,941
	b) loans and receivables with customers	2,745,118,601	1,945,296,376
70.	Equity investments	19,278,011	16,221,580
80.	Property and equipment	709,928	813,636
90.	Intangible assets	1,788,397	1,789,816
	goodwill	1,785,760	1,785,760
100.	Tax assets	7,626,222	10,083,293
	a) current	-	3,471,483
	b) deferred	7,626,222	6,611,810
110.	Non-current assets held for sale and disposal groups	2,220,930	-
120.	Other assets	11,959,252	13,441,001
	Total assets	**3,150,153,330**	**2,310,426,559**

(*) Restatement of the net amounts of the separate financial statements at 31 December 2017 in compliance with the new Circular no. 262 issued by the Bank of Italy.

	Liabilities and equity	31.12.2018	31.12.2017 (*)
10.	Financial liabilities measured at amortised cost	2,902,239,596	2,083,434,873
	a) due to banks	695,196,627	517,532,691
	b) due to customers	1,902,056,238	1,284,131,980
	c) securities issued	304,986,731	281,770,202
60.	Tax liabilities	15,676,925	10,117,999
	a) current	3,445,454	-
	b) deferred	12,231,471	10,117,999
80.	Other liabilities	65,235,054	71,916,098
90.	Post-employment benefits	2,402,013	2,171,668
100.	Provisions for risks and charges:	9,221,203	6,698,378
	a) commitments and guarantees issued	7,326	-
	c) other provisions for risks and charges	9,213,877	6,698,378
110.	Valuation reserves	(1,131,458)	366,663
140.	Reserves	79,803,766	59,391,440
150.	Share premium	39,184,038	39,267,909
160.	Share capital	9,650,526	9,650,526
170.	Treasury shares (-)	(198,893)	(149,428)
180.	Profit for the year	28,070,560	27,560,433
	Total liabilities and equity	**3,150,153,330**	**2,310,426,559**

(*) Restatement of the net amounts of the separate financial statements at 31 December 2017 in compliance with the new Circular no. 262 issued by the Bank of Italy.

INCOME STATEMENT

(Amounts in Euros)

		2018	2017 (*)
10.	Interest and similar income	99,889,812	90,293,622
	of which interest income calculated with the effective interest method	98,210,888	89,303,685
20.	Interest and similar expense	(25,144,185)	(19,484,342)
30.	**Net interest income**	**74,745,627**	**70,809,280**
40.	Fee and commission income	17,625,263	13,047,029
50.	Fee and commission expense	(2,367,900)	(2,379,853)
60.	**Net fee and commission income**	**15,257,363**	**10,667,176**
70.	Dividends and similar income	226,667	226,667
80.	Net trading income (expense)	(124,809)	18,204
100.	Gain from sales or repurchases of:	1,167,196	930,565
	b) financial assets measured at fair value through other comprehensive income	1,167,196	930,565
120.	**Total income**	**91,272,044**	**82,651,891**
130.	Net impairment losses on:	(6,814,326)	(5,352,297)
	a) financial assets measured at amortised cost	(6,812,268)	(5,352,297)
	b) financial assets measured at fair value through other comprehensive income	(2,058)	-
150.	**Net financial income**	**84,457,718**	**77,299,594**
160.	Administrative expenses:	(40,521,280)	(36,808,119)
	a) personnel expense	(19,811,309)	(17,549,337)
	b) other administrative expenses	(20,709,971)	(19,258,782)
170.	Net accruals to provisions for risks and charges	(414,040)	(8,228)
	b) other net accruals	(414,040)	(8,228)
180.	Net impairment losses on property and equipment	(400,881)	(268,567)
190.	Net impairment losses on intangible assets	(3,250)	(34,043)
200.	Other operating expense	(418,294)	(412,740)
210.	**Operating costs**	**(41,757,745)**	**(37,531,697)**
260.	**Pre-tax profit from continuing operations**	**42,699,973**	**39,767,897**
270.	Income taxes	(14,629,413)	(12,207,464)
300.	**Profit for the year**	**28,070,560**	**27,560,433**

(*) Restatement of the net amounts of the interim financial report at 31 December 2017 in compliance with the new Circular no. 262 issued by the Bank of Italy.

STATEMENT OF COMPREHENSIVE INCOME

(Amounts in Euros)

		2018	2017
10.	**Profit for the year**	**28,070,560**	**27,560,433**
	Items, net of tax, that will not be reclassified subsequently to profit or loss	**-**	-
20.	Equity instruments designated at fair value through other comprehensive income	-	-
30.	Financial liabilities designated at fair value through profit or loss (changes in own credit rating)	-	-
40.	Hedging of equity instruments designated at fair value through other comprehensive income	-	-
50.	Property and equipment	-	-
60.	Intangible assets	-	-
70.	Defined benefit plans	39,019	(56,148)
80.	Non-current assets held for sale and disposal groups	-	-
90.	Share of valuation reserves of equity-accounted investments:	-	**-**
	Items, net of tax, that will be reclassified subsequently to profit or loss	**-**	-
100.	Hedges of foreign investments	-	-
110.	Exchange rate gains (losses)	-	-
120.	Cash flow hedges	-	-
130.	Hedging instruments (non-designated elements)	-	-
140.	Financial assets (other than equity instruments) measured at fair value through other comprehensive income	(2,064,140)	(94,853)
150.	Non-current assets held for sale and disposal groups	-	-
160.	Share of valuation reserves of equity-accounted investments:	-	-
170.	**Total other comprehensive expense, net of income tax**	**(2,025,121)**	**(151,001)**
180.	**Comprehensive income (Items 10+170)**	**26,045,439**	**27,409,432**

STATEMENT OF CHANGES IN EQUITY AS AT 31.12.2018

(Amounts in Euros)

				Allocation of prior year profit		Changes during the year								
							Transactions on equity							
	Balance at 31.12.2017	Change in opening balances	Balance at 1.1.2018	Reserves	Dividends and other allocations	Changes in reserves	Issue of new shares	Repurchase of treasury shares	Extraordinary dividend distribution	Change in equity instruments	Derivatives on treasury shares	Stock Options	Comprehensive income for 2018	**Equity at 31.12.2018**
Share capital:														
a) ordinary shares	**9,650,526**	-	9,650,526	-	-	-	-	-	-	-	-	-	-	**9,650,526**
b) other shares	**-**	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Share premium	**39,267,909**	-	39,267,909	-	-	(83,871)	-	-	-	-	-	-	-	**39,184,038**
Reserves	**59,391,440**	(223,650)	59,167,790	20,644,223	-	(8,247)	-	-	-	-	-	-	-	**79,803,766**
a) income-related	**60,201,614**	(223,650)	59,977,964	20,644,223	-	5,869	-	-	-	-	-	-	-	**80,628,056**
b) other	**(810,174)**	-	(810,174)	-	-	(14,116)	-	-	-	-	-	-	-	**(824,290)**
Valuation reserves	**366,663**	527,000	893,663	-	-	-	-	-	-	-	-	-	(2,025,121)	**(1,131,458)**
Equity instruments	**-**	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Treasury shares	**(149,428)**	-	(149,428)	-	-	(49,465)	-	-	-	-	-	-	-	**(198,893)**
Profit for the year	**27,560,433**	-	27,560,433	(20,644,223)	(6,916,210)	-	-	-	-	-	-	-	28,070,560	**28,070,560**
Equity	**136,087,543**	**303,350**	**136,390,893**	-	**(6,916,210)**	**(141,583)**	-	-	-	-	-	-	**26,045,439**	**155,378,539**

STATEMENT OF CHANGES IN EQUITY AS AT 31.12.2017

(Amounts in Euros)

				Allocation of prior year profit		Changes during the year								
							Transactions on equity							
	Balance at 31.12.2016	Change in opening balances	Balance at 1.1.2017	Reserves	Dividends and other allocations	Changes in reserves	Issue of new shares	Repurchase of treasury shares	Extraordinary dividend distribution	Change in equity instruments	Derivatives on treasury shares	Stock Options	Comprehensive income for 2017	**Patrimonio netto al 31.12.2017**
Share capital:														
a) ordinary shares	**9,650,526**	-	9,650,526	-	-	-	-	-	-	-	-	-	-	**9,650,526**
b) other shares	**-**	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Share premium	**39,351,779**	-	39,351,779	-	-	(83,870)	-	-	-	-	-	-	-	**39,267,909**
Reserves	**39,686,132**	-	39,686,132	18,369,013		1,336,295	-	-	-	-	-	-	-	**59,391,440**
a) income-related	**40,480,307**	-	40,480,307	18,369,013	-	1,352,294	-	-	-	-	-	-	-	**60,201,614**
b) other	**(794,175)**	-	(794,175)	-	-	(15,999)	-	-	-	-	-	-	-	**(810,174)**
Valuation reserves	**517,664**	-	517,664	-	-	-	-	-	-	-	-	-	(151,001)	**366,663**
Equity instruments	**-**	-	-	-	-	-	-	-	-	-	-	-	-	**-**
Treasury shares	**(52,476)**	-	(52,476)	-	-	52,476	-	(149,428)	-	-	-	-	-	**(149,428)**
Profit for the year	**24,481,013**	-	24,481,013	(18,369,013)	(6,112,000)	-	-	-	-	-	-	-	27,560,433	**27,560,433**
Equity	**113,634,638**	-	**113,634,638**	**-**	**(6,112,000)**	**1,304,901**	-	**(149,428)**	-	-	-	-	**27,409,432**	**136,087,543**

STATEMENT OF CASH FLOWS (direct method)

(Amounts in Euros)

	2018	2017
A. OPERATING ACTIVITIES		
1. Operations	**44,287,349**	**32,696,435**
▪ interest income collected	99,889,812	87,392,999
▪ interest expense paid	(25,144,185)	(16,583,720)
▪ dividends and similar income	226,667	226,667
▪ net fees and commissions	15,257,364	10,667,176
▪ personnel expense	(13,500,759)	(13,124,704)
▪ other expenses	(21,128,265)	(19,671,523)
▪ other income	-	-
▪ taxes and duties	(11,313,285)	(16,210,460)
▪ costs/income from discontinued operations, net of tax effect	-	-
2. Cash flows used for financial assets	**(845,378,424)**	**(312,651,152)**
▪ financial assets held for trading	1,076,397	(186,639)
▪ financial assets designated at fair value through profit or loss	-	-
▪ financial assets measured at fair value through profit or loss	-	-
▪ financial assets measured at fair value through other comprehensive income	(19,192,648)	145,922,484
▪ financial assets measured at amortised cost	(827,519,632)	(458,279,972)
▪ other assets	257,459	(107,025)
3. Cash flows generated by financial liabilities	**813,711,184**	**297,705,342**
▪ financial liabilities measured at amortised cost	818,804,723	278,136,529
▪ financial liabilities held for trading	-	-
▪ financial liabilities designated at fair value through profit or loss	-	-
▪ other liabilities	(5,093,539)	19,568,813
Net cash flows generated by operating activities	**12,620,109**	**17,750,625**
B. INVESTING ACTIVITIES		
1. Cash flows generated by	**-**	**-**
▪ sales of equity investments	-	-
▪ dividends from equity investments	-	-
▪ sales of property and equipment	-	-
▪ sales of intangible assets	-	-
▪ sales of business units	-	-
2. Cash flows used in	**(5,576,365)**	**(11,573,483)**
▪ purchases of equity investments	(5,277,361)	(11,300,064)
▪ purchases of property and equipment	(297,173)	(270,664)
▪ purchases of intangible assets	(1,831)	(2,755)
▪ purchases of business units	-	-
Net cash flows used in investing activities	**(5,576,365)**	**(11,573,483)**
C. FINANCING ACTIVITIES		
▪ issues/repurchases of treasury shares	-	-
▪ issues/repurchases of equity instruments	-	-
▪ dividend and other distributions	(6,916,210)	(6,112,000)
Net cash flows used in financing activities	**(6,916,210)**	**(6,112,000)**
NET CASH FLOWS FOR THE YEAR	**127,534**	**65,142**

RECONCILIATION

Cash and cash equivalents at the beginning of the year	160,897	95,755
Total net cash flows for the year	127,534	65,142
Cash and cash equivalents: effect of change in exchange rates	-	-
Cash and cash equivalents at the end of the year	288,431	160,897

NOTES TO THE SEPARATE FINANCIAL STATEMENTS

A.1 - GENERAL PART

SECTION 1 - Statement of compliance with International Financial Reporting Standards

The separate financial statements of Banca Sistema S.p.A. at 31 December 2018 were drawn up in accordance with International Financial Reporting Standards - called IFRS - issued by the International Accounting Standards Board (IASB) and interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and endorsed by the European Commission, as established by EU Regulation no. 1606 of 19 July 2002, adopted in Italy by art. 1 of Legislative Decree no. 38 of 28 February 2005 and considering the Bank of Italy Circular no. 262 of 22 December 2005[8] as subsequently updated, regarding the forms and rules for drafting the Financial Statements of banks.

The International Financial Reporting Standards are applied by referring to the "Framework for the Preparation and Presentation of Financial Statements" (Framework).

If there is no standard or interpretation that applies specifically to a transaction, other event or circumstance, the Board of Directors uses its judgement to develop and apply an accounting standard in order to provide disclosure that:

- is relevant to the purposes of the financial decisions made by the users;
- is reliable, so that the separate financial statements:
  - faithfully represent the capital/financial position, the profit or loss and the cash flows of the bank;
  - reflect the economic substance of transactions, other events and circumstances and not merely the legal form;
  - are neutral, i.e. devoid of prejudice;
  - are prudent;
  - are complete, with reference to all relevant aspects.

When exercising the aforementioned judgement, the Board of Directors of the Bank has made reference to and considered the applicability of the following sources, described in descending order of importance:

- the provisions and application guidelines contained in the Standards and Interpretations governing similar or related cases;
- the definitions, recognition criteria and measuring concepts for accounting for the assets, liabilities, revenue, and costs contained in the "Framework".

When expressing an opinion, the Board of Directors may also consider the most recent provisions issued by other bodies that rule on accounting standards that use a similar "Framework" in concept for developing accounting standards, other accounting literature and consolidated practices in the sector.

In accordance with Art. 5 of Legislative Decree no. 38 of 28 February 2005, if, in exceptional cases, the application of a provision imposed by the IFRS were incompatible with the true and fair representation of the financial position or results of operations, the provision would not apply. The justifications for any exceptions and their influence on the presentation of the financial position and results of operations would be explained in the Notes to the separate financial statements.

Any profits resulting from the exception would be recognised in a non-distributable reserve if they did not correspond to the recovered amount in the financial statements. However, no exceptions to the IFRS were applied. The separate financial statements were audited by KPMG S.p.A.

SECTION 2 - General basis of preparation

The financial statements are drawn up with clarity and give a true and fair view of the financial position, profit or loss, cash flows, and changes in equity and comprise the statement of financial position, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows and

[8] With the 5th update of Circular no. 262 published on 22 December 2017, the new provisions introduced by IFRS 9 and IFRS 1 were transposed. For the sake of completeness, it should be noted that, on 30 November 2018, the Bank of Italy published the 6th update of Circular no. 262. The update, which transposes the changes introduced by IFRS 16, will be effective for financial years ending on or after 31 December 2019.

the notes to the separate financial statements.

The separate financial statements are accompanied by the Director's Report on the Bank's performance.

If the information required by the IFRS and provisions contained in Circular no. 262 of 22 December 2005 and/or the subsequent updates issued by the Bank of Italy are not sufficient to give a true and fair view that is relevant, reliable, comparable and understandable, the notes to the separate financial statements provide the additional information required.

The general principles that underlie the drafting of the separate financial statements are set out below:

- the measurements are made considering that the bank will continue as a going concern guaranteed by the financial support of the Shareholders;
- costs and income are accounted for on an accruals basis;
- to ensure the comparability of the data and information in the separate financial statements and the notes to the separate financial statements, the methods of presentation and classification are kept constant over time unless they are changed to present the data more appropriately;
- each material class of similar items is presented separately in the statement of financial position and income statement; items of a dissimilar nature or function are presented separately unless they are considered immaterial;
- items that have nil balances at year end or for the financial year or for the previous year are not indicated in the statement of financial position or the income statement;
- if an asset or liability comes under several items in the statement of financial position, the notes to the separate financial statements make reference to the other items under which it is recognised if it is necessary for a better understanding of the separate financial statements;
- the items are not offset against one another unless it is expressly requested or allowed by an IFRS or an interpretation or the provisions of the aforementioned Circular no. 262 of 22 December 2005 as amended by the Bank of Italy;
- the separate financial statements are drafted by favouring substance over form and in accordance with the principle of materiality and significance of the information;
- comparative data for the previous financial year are presented for each statement of financial position and income statement item; if the items are not comparable to those of the previous year, they are adapted and the non-comparability and adjustment/or impossibility thereof are indicated and commented on in the notes to the separate financial statements;
- the layout recommended by the Bank of Italy was used with reference to the information reported in the notes to the separate financial statements; they were not presented if they were not applicable to the bank's business.

Within the scope of drawing up the separate financial statements in accordance with the IFRS, bank management must make assessments, estimates and assumptions that influence the amounts of the assets, liabilities, costs and income recognised during the year.

The use of estimates is essential to preparing the separate financial statements. In particular, the most significant use of estimates and assumptions in the separate financial statements can be attributed to:

- the valuation of loans and receivables with customers: the acquisition of performing receivables from companies that supply goods and services represents the Bank's main activity. Estimating the value of these receivables is a complex activity with a high degree of uncertainty and subjectivity. Their value is estimated by using models that include numerous quantitative and qualitative elements. These include the historical data for collections, expected cash flows and the related expected recovery times, the existence of indicators of possible impairment, the valuation of any guarantees, and the impact of risks associated with the sectors in which the Bank's customers operate;
- the valuation of default interest pursuant to Legislative Decree no. 231 of 9 October 2002 on performing receivables acquired without recourse: estimating the expected recovery percentages of

default interest is complex, with a high degree of uncertainty and subjectivity. Internally developed valuation models are used to determine these percentages, which take numerous qualitative and quantitative elements into consideration;
- the estimate related to the possible impairment losses on goodwill and equity investments recognised in the separate financial statements;
- the quantification and estimate made for recognising liabilities in the provision for risks and charges, the amount or timing of which are uncertain;
- the recoverability of deferred tax assets.

It should be noted that an estimate may be adjusted following a change in the circumstances upon which it was formed, or if there is new information or more experience. Any changes in estimates are applied prospectively and therefore will have an impact on the income statement for the year in which the change takes place.

Pursuant to the provisions of Art. 5 of Legislative Decree no. 38 of 28 February 2005, the separate financial statements use the Euro as the currency for accounting purposes. The separate financial statements are expressed in Euro. Unless otherwise stated, the notes to the separate financial statements are expressed in thousands of Euro.

The transition to financial reporting standard IFRS 9

Regulatory provisions

The new financial reporting standard IFRS 9, issued by the IASB in July 2014 and endorsed by the European Commission through Regulation no. 2067/2016, replaced IAS 39 effective as of 1 January 2018.

IFRS 9 has introduced significant changes, particularly in regard to the following aspects:
- Classification and measurement of financial instruments;
- Impairment;
- Hedge Accounting.

The new international financial reporting standard "IFRS 9 - Financial Instruments" (the "Standard"), in force since 1 January 2018, replaces accounting standard "IAS 39 - Financial Instruments: Recognition and Measurement" for the measurement and recognition of financial instruments.

The Standard imposes new rules for classifying financial assets in the following categories:
- Amortised Cost - "AC": this category implies use of the amortised cost measurement method;
- Fair Value through Other Comprehensive Income - "FVOCI": this classification entails measurement at fair value, with recognition of the changes in fair value in a special equity reserve. This reserve is transferred to profit or loss when the financial instrument is sold/redeemed;
- Fair Value through Profit or Loss - "FVTPL": this class governs the measurement of instruments at fair value, with recognition of changes in profit or loss. The FVTPL category is defined by the Standard as a residual category, in which the financial instruments that cannot be classified in the preceding categories are classified based on the Business Model or the results of the test on the characteristics of contractual cash flows (SPPI test).

The classification is then made according to the Business Model that the Bank has associated with each of the identified portfolios and the characteristics of the contractual cash flows of the financial instrument.

The classification and measurement of financial assets represented by loans and receivables and instruments are based on a two-step approach:
- association of the Business Model with the identified uniform portfolios, where the aggregation by uniform portfolios is determined at a level that reflects how groups of financial assets are managed together to achieve a particular business objective;
- analysis of the characteristics of the contractual cash flows of the instrument carried out on the individual assets at the origination date.

Thus, the Business Model represents the way in which the Bank manages its financial assets, i.e. with which it intends to realise the cash flows of the debt instruments. It reflects the way in which groups of financial assets are managed together to achieve a particular business objective. It does not depend on management intentions concerning an individual instrument but is decided at a higher level of aggregation.

The possible Business Models delineated by the

Standard are as follows:

- "Hold to collect (HTC)": this requires the realisation of contractually agreed cash flows. This Business Model is associated with assets that will presumably be held until maturity (IFRS 9 - B4.1.2C);
- "Hold to Collect and Sell (HTCS)": this calls for the realisation of cash flows as contractually agreed or through sale of the instrument. This Business Model is associated with assets that may be held until maturity, but also sold (IFRS 9 – B4.1.4);
- "Other": this calls for the realisation of cash flows through disposal of the instrument. This Business Model is associated with assets whose cash flows will be realised through trading (IFRS 9 - B4.1.5).

As regards impairment, the new financial reporting standard requires:

- the introduction of a model for expected loss on loans and debt instruments recognised at Amortised Cost or FVTOCI;
- inclusion of Irrevocable Commitments and Guarantees Issued in the scope;
- introduction of the 3-stage portfolio classification according to the deterioration of the credit risk, i.e. stage 1 for performing loans, stage 2 for under-performing loans, and stage 3 for non-performing loans;
- a calculation of expected credit losses ("ECLs") for either a "lifetime" or on a 12-month horizon according to the stage;
- the need to incorporate forward-looking information tied, among other things, to the developments in the macroeconomic scenario.

When calculating impairment losses on loans and receivables classified in stage 1, the expected loss in the first year is considered, while for the loans classified in stages 2 and 3, the expected losses are calculated on a lifetime basis.

Adoption of IFRS 9

In regard to the methods used to present the effects of first-time adoption of the Standard, the Bank has exercised the option envisaged in paragraph 7.2.15 of IFRS 9 and paragraphs E1 and E2 of IFRS 1 "First-Time Adoption of International Financial Reporting Standards". According to those rules – without prejudice to retrospective application of the new measurement and presentation rules prescribed by the Standard – there is no obligation to restate the comparative data in the financial statements on a uniform basis in the financial statements prepared upon first-time adoption of the new standard. According to the instructions given in the report accompanying issuance of Circular no. 262 "Bank financial statements: forms and drafting rules" - version 5 of 22 December 2017, the banks that claim exemption from the obligation to restate their comparative values will nonetheless have to include, in the first financial statements prepared pursuant to the update to Circular no. 262, a reconciliation statement showing the method used and provide a reconciliation between the data of the last approved financial statements and the first financial statements prepared in accordance with the new rules. Moreover, the form and contents of that disclosure will depend on the autonomous choices of the delegated corporate bodies.

The main areas of impact as previously defined are briefly examined as follows.

The effects of first-time adoption (FTA) of IFRS 9

Classification and measurement of financial instruments

Application of the new classification and measurement methods introduced by IFRS 9 has resulted in reclassification of the securities held in the HTM portfolio pursuant to IAS 39 among financial assets measured at amortised cost. No other effects deriving from definition of the business models and the SPPI test have been recognised.

Impairment

Application of the new impairment rules ("expected credit losses") has resulted in:

- greater impairment losses on performing loans by € 273 thousand (€ 183 thousand net of the tax effect), substantially related to the portion of the performing portfolio in Stage 2, based on the defined stage allocation criteria, with the consequent need to calculate the expected loss for the entire residual lifetime of the financial assets;

- greater impairment losses on performing securities by € 61 thousand (€ 41 thousand net of the tax effect), mainly related to inclusion in the calculation of expected losses of new parameters set by the standard.

No additional impairment losses have been recognised on non-performing loans.

Details are provided in the table below:

STATUS	31.12.2017	FTA	01.01.2018
Bad exposures	44,577	-	44,577
Unlikely to pay	24,061	-	24,061
Past due/overdrawn	74,690	-	74,690
Gross non-performing loans - Stage 3	**143,328**	-	**143,328**
Individual impairment losses	(22,293)	-	(22,293)
Total net non-performing loans	**121,035**	-	**121,035**
Gross performing loans	**1,745,673**	-	**1,745,673**
Performing - Stage 1	-	1,630,418	1,630,418
Performing - Stage 2	-	115,255	115,255
Collective impairment losses	**(5,590)**	**(241)**	**(5,831)**
of which Stage 1	(5,152)	(49)	(5,201)
of which Stage 2	(438)	(192)	(630)
Total net performing loans	**1,740,083**	**-**	**1,739,842**
Gross exposure on securities	363,025	-	363,025
Impairment losses on securities	-	(61)	(61)
Net exposure	**363,025**	**-**	**362,964**
Gross off-statement of financial position exposure	645	-	645
Impairment losses on endorsement credit	**-**	(23)	(23)
Net exposure	**645**	**-**	**622**
Gross exposure on loans and receivables with banks	-	-	-
Impairment losses on endorsement credit	-	(9)	(9)
Net exposure	**-**	**-**	**(9)**

The following tables show the reconciliation between the net balances on the statement of financial position at 31 December 2017 (under IAS 39) and the opening balances at 1 January 2018, which include the effect of first-time adoption of IFRS 9.

Reconciliation between the statement of financial position at 31 December 2017 (under IAS 39) and the statement of financial position at 1 January 2018 (IFRS 9).

STATEMENT OF FINANCIAL POSITION - ASSETS (Amounts in Euros)	31.03.2018	31.12.2017	Change in opening balances	01.01.2018
Cash and cash equivalents	198,839	160,897	-	160,897
Financial assets measured at fair value through profit or loss	843,591	1,201,206	-	1,201,206
Financial assets measured at fair value through other comprehensive income	453,500,917	285,609,813	84,903,608	370,513,421
Financial assets measured at amortised cost	2,075,748,467	1,981,105,317	(84,450,870)	1,896,654,447
a) loans and receivables with banks	*24,532,502*	*35,808,941*	-	*35,808,941*
b) loans and receivables with customers	*2,051,215,965*	*1,945,296,376*	*(84,450,870)*	*1,860,845,506*
Equity investments	16,371,354	16,221,580	-	16,221,580
Property and equipment	836,289	813,636	-	813,636
Intangible assets	1,788,235	1,789,816	-	1,789,816
Tax assets	8,129,968	10,083,293	110,505	10,193,798
Other assets	15,299,024	13,441,001	-	13,441,001
Total Assets	**2,572,716,684**	**2,310,426,559**	**563,243**	**2,310,989,802**

STATEMENT OF FINANCIAL POSITION - LIABILITIES (Amounts in Euros)	31.03.2018	31.12.2017	Change in opening balances	01.01.2018
Financial liabilities measured at amortised cost	2,326,279,707	2,083,434,873	-	2,083,434,873
a) due to banks	*566,194,371*	*517,532,691*	-	*517,532,691*
b) due to customers	*1,477,072,064*	*1,284,131,980*	-	*1,284,131,980*
c) securities issued	*283,013,272*	*281,770,202*	-	*281,770,202*
Financial liabilities held for trading	10,218,656	-	-	-
Tax liabilities	10,331,202	10,117,999	260,226	10,378,225
Other liabilities	76,212,229	71,916,098	-	71,916,098
Post-employment benefits	2,237,359	2,171,668	-	2,171,668
Provisions for risks and charges	6,862,512	6,698,378	-	6,698,378
Valuation reserves	214,082	366,663	526,667	893,330
Reserves	86,729,390	59,412,408	(223,650)	59,188,758
Share premium	39,246,941	39,246,941	-	39,246,941
Share capital	9,650,526	9,650,526	-	9,650,526
Treasury shares (-)	(145,671)	(149,428)	-	(149,428)
Profit for the period/year (+/-)	4,879,751	27,560,433	-	27,560,433
Total liabilities and equity	**2,572,716,684**	**2,310,426,559**	**563,243**	**2,310,989,802**

Finally, in the Statement of "Reconciliation between equity calculated under IAS 39 and equity calculated under IFRS 9", shown below, a quantitative disclosure is provided on the principal effects on Equity.

Book equity at 31 December 2017 (IAS 39)	**136,088**
FTA reserve	**(224)**
Application of the new impairment model	**(224)**
Performing loans (stages 1 and 2)	(273)
Non-performing loans (stage 3)	-
Debt instruments	(61)
Tax effect	110
Classification and measurement effects	**527**
Adjustment of carrying amount of financial assets deriving from application of the Business Model as a balancing entry for the valuation reserve	787
Tax effect	(260)
Total effects of transition to IFRS 9	**303**
Book equity at 1 January 2018 (IFRS 9)	**136,391**

The impact deriving from first-time adoption of IFRS 9 on the CET 1 ratio of Banca Sistema is 2 bps. Therefore, the Bank has decided to allocate this impact in full to Equity.

IFRS 15

With regard to the introduction of IFRS 15, the analyses carried out did not reveal any significant impact on the accounts.

IFRS 16

Effective from 1 January 2019, IFRS 16 “Leases” will replace the current IAS 17 “Leases”.

This standard introduces new accounting requirements for lessees (i.e. the user of the assets that are the object of the lease) which define a lease as a contract that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.

Under this new approach, starting on 1 January 2019, the right to use the leased asset will be recognised on the asset side of the statement of financial position, and the liability for future lease payments still to be paid to the lessor will be recognised on the liability side of the statement of financial position.

In addition, recognition in the income statement will also differ under this new method, whereby for lease payments previously recognised under administrative expenses, under IFRS 16 the depreciation of the “right-of-use” asset and interest expense on the lease liability will be recognised.

The economic impact does not change over the lease term, but is instead allocated differently over time. In 2018, the Bank carried out a special recognition project for all contracts so as to identify which were affected by the new accounting standard and the impact on the statement of financial position and income statement. From an information point of view, the external software house that supplies the Bank with accounting information systems has developed a system to handle the operations.

The analysis of the contracts revealed that there were impacts regarding property and company car leases. Property leases represent the most significant implementation impact area in terms of estimated rights of use.

The Bank's choices

The Bank has chosen to use the modified retrospective approach for the first-time application (FTA), which permits the recognition of the cumulative effect of applying the Standard at the date of initial application and excludes the restatement of comparative data from the financial statements prepared upon first-time adoption of IFRS 16. Therefore, the figures for 2019 will not be comparable for the valuation of the rights of use and the corresponding lease liability. Contracts with a residual duration of less than or equal to 12 months were excluded.

With reference to the duration of the lease, at the date of initial application the Group has decided to consider only the term of the contract, without considering renewals as reasonably certain, unless there are particular contractual clauses, facts or circumstances which indicate that additional renewals should be considered or that the lease should be terminated.

With regard to the discount rate, the Group has decided to use the average cost of funding.

The estimated impact on the opening balances following the application of IFRS 16 using the modified retrospective approach resulted in an increase in assets due to the recognition of the right of use of € 7 million, and an increase in financial liabilities (payable to the lessor) for the same amount. Consequently, there is no impact on equity since, following the decision to adopt the modified approach (option B), on first-time application the two amounts, assets and liabilities, are the same.

The increase in RWAs due to the recognition of the total estimated rights of use results in a negative impact on CET 1 of about 6 bps.

SECTION 3 - Subsequent events

With regard to IAS 10, after 31 December 2018, the reporting date of the separate financial statements, and up to 1 March 2019, the date when the separate financial statements were presented to the Board of Directors, no events occurred that would require any adjustments to the figures in the separate financial statements.

SECTION 4 - Other aspects

There are no significant aspects to note.

A.2 - INFORMATION ON THE MAIN ITEMS OF THE SEPARATE FINANCIAL STATEMENTS

Financial assets measured at fair value through profit or loss

Classification criteria

Financial assets other than those classified as Financial assets measured at fair value through other comprehensive income and Financial assets measured at amortised cost are classified in this category. In particular, this item includes:

- financial assets held for trading;
- equity instruments, except for the possibility of their being classified in the new category Financial assets measured at fair value through other comprehensive income, excluding the possibility of subsequent reclassification to profit or loss;
- the financial assets mandatorily measured at fair value, and which have not met the requirements to be measured at amortised cost;
- the financial assets that are not held under a Held to Collect (or "HTC") business model or as part of a mixed business model, whose aim is achieved by collecting the contractual cash flows of financial assets held in the Bank's portfolio or also through their sale, when this is an integral part of the strategy ("Held to Collect and Sell" business model);
- financial assets designated at fair value, i.e. financial assets that are defined as such upon initial recognition and when the conditions apply. For this type of financial assets, upon recognition an entity may irrevocably recognise a financial asset as measured at fair value through profit or loss only if this eliminates or significantly reduces a measurement inconsistency;
- derivative instruments, which shall be recognised as financial assets held for trading if their fair value is positive and as liabilities if their fair value is negative. Positive and negative values may be offset only for transactions executed with the same counterparty if the holder currently holds the right to offset the amounts recognised in the books and it is decided to settle the offset positions on a net basis. Derivatives also include those embedded in complex financial contracts - where the host contract is a financial liability which has been recognised separately.

Except for the equity instruments which cannot be reclassified, financial assets may be reclassified to other categories of financial assets only if the entity changes its own business model for management of the financial assets. In such cases, which are expected to be absolutely infrequent, the financial assets may be reclassified from those measured at fair value through profit or loss to one of the other two categories established by IFRS 9 (Financial assets measured at amortised cost or Financial assets measured at fair value through other comprehensive income). The transfer value is the fair value at the time of the reclassification and the effects of the reclassification apply prospectively from the reclassification date. In this case, the effective interest rate of the reclassified financial asset is determined based on its fair value at the reclassification date and that date is considered as the initial recognition date for the credit risk stage assignment for impairment purposes.

Recognition criteria

Initial recognition of financial assets occurs at the settlement date for debt instruments and equity instruments, at the disbursement date for loans and at the subscription date for derivative contracts.

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

Measurement and recognition criteria for income components

After initial recognition, the financial assets measured at fair value through profit or loss are recognised at fair value. The effects of the application of this measurement criterion are recognised in the income statement. For the determination of the fair value of financial instruments quoted on active markets, market quotations are used. If the market for a financial instrument is not active, standard practice estimation methods and measurement techniques are used which consider all the risk factors correlated to the instruments and that are based on market elements such as: measurement of quoted instruments with the same characteristics, calculation of discounted cash flows, option pricing models, recent comparable transactions, etc.. For equity and derivative instruments that have equity instruments as underlying assets, which are not quoted on an active market, the cost approach is used as the estimate of fair value only on a residual basis and in a small number of circumstances, i.e., when all the measurement methods referred to above cannot be applied, or when there are a wide range of possible measurements of fair value, in which cost represents the most significant estimate.

In particular, this item includes:

- debt instruments held for trading;
- equity instruments held for trading.

For more details on the methods of calculating the fair value please refer to the paragraph below "Criteria for determining the fair value of financial instruments".

Derecognition criteria

Financial assets are derecognised when the contractual rights on the cash flows deriving from the assets expire, or in the case of a transfer, when the same entails the substantial transfer of all risks and rewards related to the financial assets.

Financial assets measured at fair value through other comprehensive income (FVOCI)

Classification criteria

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

- financial assets that are held under a business model whose aim is achieved both through the collection of contractual cash flows and through sale (“Held to Collect and Sell” business model);
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (“SPPI Test” passed).

This item also includes equity instruments, not held for trading, for which the option was exercised upon initial recognition of their designation at fair value through other comprehensive income.

In particular, this item includes:

- debt instruments that can be attributed to a Held to Collect and Sell business model and that have passed the SPPI test;
- equity interests, that do not qualify as investments in subsidiaries, associates or joint ventures and are not held for trading, for which the option has been exercised of their designation at fair value through other comprehensive income.

Except for the equity instruments which cannot be reclassified, financial assets may be reclassified to other categories of financial assets only if the entity changes its own business model for management of the financial assets. In such cases, which are expected to be absolutely infrequent, the financial assets may be reclassified from those measured at fair value through other comprehensive income to one of the other two categories established by IFRS 9 (Financial assets measured at amortised cost or Financial assets measured at fair value through profit or loss). The transfer value is the fair value at the time of the reclassification and the effects of the reclassification apply prospectively from the reclassification date. In the event of reclassification from this category to the amortised cost category, the cumulative gain (loss) recognised in the valuation reserve is allocated as an adjustment to the fair value of the financial asset at the reclassification date. In the event of reclassification to the fair value through profit or loss category, the cumulative gain (loss) previously recognised in the valuation reserve is reclassified from equity to profit (loss).

Recognition criteria

Initial recognition of the financial assets is at the date of disbursement, based on their fair value including the transaction costs/income directly attributable to the acquisition of the financial instrument. Costs/income having the previously mentioned characteristics that will be repaid by the debtor or that can be considered as standard internal administrative costs are excluded.
The initial fair value of a financial instrument is usually the cost incurred for its acquisition.

Measurement and recognition criteria for income components

Following initial recognition, financial assets are measured at their fair value with any gains or losses resulting from a change in the fair value compared to the amortised cost recognised in a specific equity reserve recognised in the statement of comprehensive income up until said financial asset is derecognised or an impairment loss is recognised.
For more details on the methods of calculating the fair value please refer to paragraph 17.3 below "Criteria for determining the fair value of financial instruments".
Equity instruments, for which the choice has been made to classify them in this category, are measured at fair value and the amounts recognised in other comprehensive income cannot be subsequently transferred to profit or loss, not even if they are sold (the so-called OCI exemption). The only component related to these equity instruments that is recognised through profit or loss is their dividends.
Fair value is determined on the basis of the criteria already described for Financial assets measured at fair value through profit or loss.
For the equity instruments included in this category, which are not quoted on an active market, the cost approach is used as the estimate of fair value only on a residual basis and in a small number of circumstances, i.e., when all the measurement methods referred to above cannot be applied, or when there are a wide range of possible measurements of fair value, in which cost represents the most significant estimate.
Financial assets measured at fair value through other comprehensive income are subject to the verification of the significant increase in credit risk (impairment) required by IFRS 9, with the consequent recognition through profit or loss of an impairment loss to cover the expected losses.

Derecognition criteria

Financial assets are derecognised when the contractual rights on the cash flows deriving from the assets expire, or in the case of a transfer, when the same entails the substantial transfer of all risks and rewards related to the financial assets.

Financial assets measured at amortised cost

Classification criteria

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

- the financial asset is held under a business model whose objective is achieved through the collection of expected contractual cash flows (Held to Collect business model);

- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding ("SPPI Test" passed).

In particular, this item includes:

- loans and receivables with banks;
- loans and receivables with customers;
- debt instruments.

Except for the equity instruments which cannot be reclassified, financial assets may be reclassified to other categories of financial assets only if the entity changes its own business model for management of the financial assets. In such cases, which are expected to be absolutely infrequent, the financial assets may be reclassified from the amortised cost category to one of the other two categories established by IFRS 9 (Financial assets measured at fair value through other comprehensive income or Financial assets measured at fair value through profit or loss). The transfer value is the fair value at the time of the reclassification and the effects of the reclassification apply prospectively from the reclassification date. Gains and losses resulting from the difference between the amortised cost of a financial asset and its fair value are recognised through profit or loss in the event of reclassification to Financial assets measured at fair value through profit or loss and under equity, in the specific valuation reserve, in the event of reclassification to Financial assets measured at fair value through other comprehensive income.

Recognition criteria

Initial recognition of a receivable is at the date of disbursement based on its fair value including the costs/ income of the transaction directly attributable to the acquisition of the receivable.

Costs/income having the previously mentioned characteristics that will be repaid by the debtor or that can be considered as standard internal administrative costs are excluded.

The initial fair value of a financial instrument is usually equivalent to the amount granted or the cost incurred by the acquisition.

Measurement and recognition criteria for income components

Following initial recognition, loans and receivables with customers are stated at amortised cost, equal to the initial recognition amount reduced/increased by principal repayments, by impairment losses/gains and the amortisation - calculated on the basis of the effective interest rate - of the difference between the amount provided and that repayable at maturity, usually the cost/ income directly attributed to the individual loan.

The effective interest rate is the rate that discounts future payments estimated for the expected duration of the loan, in order to obtain the exact carrying amount at the time of initial recognition, which includes both the directly attributable transaction costs/income and all of the fees paid or received between the parties. This accounting method, based on financial logic, enables the economic effect of costs/income to be spread over the expected residual life of the receivable.

The measurement criteria are strictly connected with the stage to which the receivable is assigned, where stage 1 contains performing loans, stage 2 consists of under-performing loans, i.e. loans that have undergone a significant increase in credit risk ("significant deterioration") since the initial recognition of the instrument, and stage 3 consists of non-performing loans, i.e. the loans that show objective evidence of impairment.

The impairment losses recognised in profit or loss for the performing loans classified in stage 1 are calculated by considering an expected loss at one year, while for the performing loans in stage 2 they are calculated by considering the expected losses over the entire residual contractual lifetime of the asset (Lifetime Expected Loss).

The performing financial assets are measured according to probability of default (PD), loss given default (LGD) and exposure at default (EAD) parameters, derived from internal historic series. For impaired assets, the amount of the loss, to be recognised through profit or loss, is established based on individual measurement or determined according to uniform categories and, then, individually allocated to each position, and takes account of forward-looking information and possible alternative recovery scenarios. Impaired assets include financial instruments classified as bad exposures, unlikely-to-pay or past due/overdrawn by over ninety days according to the rules issued by the Bank of Italy, in line with the IFRS and EU Supervisory Regulations. The expected cash flows take into account the expected recovery times and the estimated realisable value of any guarantees. The original effective rate of each asset remains unchanged over time even if the relationship has been restructured with a variation of the contractual interest rate and even if the relationship, in practice, no longer bears contractual interest. If the reasons for impairment are no longer applicable following an event subsequent to the recognition of impairment, impairment gains are recognised in the income statement. The impairment gains may not in any case exceed the amortised cost that the financial instrument would have had in the absence of previous impairment losses. Impairment gains with time value effects are recognised in net interest income.

Derecognition criteria

Loans and receivables are derecognised from the separate financial statements when they are deemed totally unrecoverable or if transferred, when this entails the substantial transfer of all loan-related risks and rewards.

Hedging transactions

At the reporting date, the Bank had not made any "Hedging transactions".

Equity investments

Classification criteria

This category includes equity investments in subsidiaries, associates, and joint ventures by Banca Sistema.

Recognition criteria

Equity investments are recognised in the separate financial statements at purchase cost plus any related charges.

Measurement criteria

If there is evidence that an equity investment may be impaired, the recoverable value of said equity investment is estimated by considering the present value of future cash flows that the investment could generate, including the final disposal value of the investment and/ or other measurement elements. The amount of any impairment, calculated based on the difference between the carrying amount of the investment and its recoverable value is recognised in the income statement under "Gains (losses) on equity investments". If the reasons for impairment are removed following an event occurring after recognition of the impairment, impairment gains are recognised in the income statement under the same item as above to the extent of the previous impairment loss.

Derecognition criteria

Equity investments are derecognised from the separate financial statements when the contractual rights to cash flows deriving from the investment are lost or when the investment is transferred, with the substantial transfer of all related risks and rewards. Gains and losses on the sale of equity investments are charged to the income statement under the item "220 Gains (losses) on equity investments"; gains and losses on the sale of investments other than those measured at equity are charged to the income statement under the item "250 Gains (losses) on sales of investments".

Property and equipment

Classification criteria

This item includes assets for permanent use, held to generate income, to be leased, or for administrative purposes, such as land, operating property, investment property, technical installations, furniture and fittings and equipment of any nature and works of art.
They also include leasehold improvements to third party assets if they can be separated from the assets in question. If the above costs do not display functional or usefulness-related autonomy, but future economic benefits are expected from them, they are recognised under "other assets" and are depreciated over the shorter period between that of expected usefulness of the improvements in question and the residual duration of the lease. Depreciation is recognised under "Other operating income (expense)".

Property and equipment also include payments on account for the purchase and restructuring of assets not yet part of the production process and therefore not yet subject to depreciation.
"Operating" property and equipment are represented by assets held for the provision of services or for administrative purposes, while property and equipment held for "investment purposes" are those held to collect lease instalments and/or held for capital appreciation.

Recognition criteria

Property and equipment are initially recognised at cost, including all costs directly attributable to installation of the asset.
Extraordinary maintenance costs and costs for improvements leading to actual improvement of the asset, or an increase in the future benefits generated by the asset, are attributed to the reference assets, and are depreciated based on their residual useful life.

Measurement and recognition criteria for income components

Following initial recognition, "operating" property and equipment are recognised at cost, less accumulated depreciation, and any impairment losses, in line with the "cost model" illustrated in paragraph 30 of IAS 16. More specifically, property and equipment are systematically depreciated each year based on their estimated useful life, using the straight-line basis method apart from:

- land, regardless of whether this was purchased separately or was incorporated into the value of the building, which, insofar as it has an indefinite useful life, is not depreciated;
- works of art, which are not depreciated as their useful life cannot be estimated and their value typically appreciates over time;
- investment property which is recognised at fair value in accordance with IAS 40.

For assets acquired during the financial year, depreciation is calculated on a daily basis from the date of entry into use of the asset. For assets transferred and/or disposed of during the financial year, depreciation is calculated on a daily basis until the date of transfer and/or disposal.

At the end of each year, if there is any evidence that property or equipment that is not held for investment purposes may have suffered an impairment loss, a comparison is made between its carrying amount and its recoverable value, equal to the higher between the fair value, net of any costs to sell, and the related value in use of the asset, intended as the present value of future cash flows expected from the asset. Any impairment losses are recognised in the income statement under "net impairment losses on property and equipment".
If the reasons that led to recognition of the impairment loss cease to apply, an impairment gain is recognised that may not exceed the value that the asset would have had, net of depreciation calculated in the absence of previous impairment losses.
For investment property, which comes within the scope of application of IAS 40, the measurement is made at the market value determined using independent surveys and the changes in fair value are recognised in the income statement under the item "fair value gains (losses) on property, equipment and intangible assets".

Derecognition criteria

Property and equipment is derecognised from the statement of financial position upon disposal thereof or when the asset is permanently withdrawn from use and no future economic benefit is expected from its disposal.

Intangible assets

Classification criteria

This item includes non-monetary assets without physical substance that satisfy the following requirements:

- they can be identified;
- they can be monitored;
- they generate future economic benefits.

In the absence of one of the above characteristics, the expense of acquiring or generating the asset internally is recognised as a cost in the year in which it was incurred.
Intangible assets include software to be used over several years and other identifiable assets generated by legal or contractual rights.
Goodwill is also included under this item, representing

the positive difference between the acquisition cost and fair value of the assets and liabilities acquired as part of a business combination. Specifically, an intangible asset is recognised as goodwill when the positive difference between the fair value of the assets and liabilities acquired and the acquisition cost represents the future capacity of the equity investment to generate profit (goodwill). If this difference proves negative (badwill), or if the goodwill offers no justification of the capacity to generate future profit from the assets and liabilities acquired, it is recognised directly in the income statement.

Measurement criteria

Intangible assets are systematically amortised from the time of their input into the production process.
With reference to the goodwill, on an annual basis (or when impairment is detected), an assessment test is carried out on the adequacy of its carrying amount. For this purpose, the cash-generating unit to which the goodwill is attributed, is identified. The amount of any impairment is determined by the difference between the goodwill carrying amount and its recoverable value, if lower. This recoverable value is equal to the higher amount between the fair value of the cash-generating unit, net of any costs to sell, and its value in use. As stated above, any consequent impairment losses are recognised in the income statement.

Derecognition criteria

An intangible asset is derecognised from the statement of financial position at the time of its disposal and if there are no expected future economic benefits.

Non-current assets held for sale and disposal groups

Non-current assets or groups of assets for which a disposal process has been initiated and whose sale is considered highly probable are classified under "Non-current assets held for sale and disposal groups". These assets are measured at the lower of their carrying amount and their fair value, net of disposal costs, with the exception of certain types of assets (e.g. financial assets falling within the scope of IFRS 9) for which IFRS 5 specifically requires that the measurement criteria of the relevant accounting standard be applied. Income and expenses (net of the tax effect) relating to groups of assets being disposed of or recognised as such during the year, are shown in the income statement as a separate item.

Financial liabilities measured at amortised cost

Classification criteria

This item includes Due to banks, Due to customers and Securities issued.

Recognition criteria

These financial liabilities are initially recognised when the deposits are received or when the debt instruments are issued. Initial recognition is based on the fair value of the liabilities, increased by the costs/income of the transaction directly attributable to the acquisition of the financial instrument.
Costs/income having the previously mentioned characteristics that will be repaid by the creditor or that can be considered as standard internal administrative costs are excluded.
The initial fair value of a financial liability is usually equivalent to the amount collected.

Measurement and recognition criteria for income components

After the initial recognition, the previously mentioned financial liabilities are measured at amortised cost with the effective interest rate method.

Derecognition criteria

The above financial liabilities are derecognised from the statement of financial position when they expire or when they are extinguished. They are derecognised also in the event of repurchase, even temporary, of the previously-issued securities. Any difference between the carrying amount of the extinguished liability and the amount paid is recognised in the income statement, under “Gain (loss) from sales or repurchases of: financial liabilities”. If the Bank, subsequent to the repurchase, re-places its own securities on the market, said transaction is considered a new issue and the liability is recognised at the new placement price.

Financial liabilities held for trading

Classification and recognition criteria

In particular, this category of liabilities includes the liabilities originating from technical exposures deriving from security trading activities.

Financial instruments are recognised at the date of their subscription or issue at a value equal to their fair value, without including any transaction costs or income directly attributable to the instruments themselves.

Measurement and recognition criteria for income components

The financial instruments are measured at fair value with recognition of the measurement results in the income statement.

Derecognition criteria

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

Financial liabilities designated at fair value through profit or loss

At the reporting date, the Bank did not hold any "Financial liabilities designated at fair value through profit or loss".

Current and deferred taxes

Income taxes, calculated in compliance with prevailing tax regulations, are recognised in the income statement on an accruals basis, in accordance with the recognition in the separate financial statements of the costs and income that generated them, apart from those referring to the items recognised directly in equity, where the recognition of the tax is made to equity in order to be consistent.

Income taxes are provided for on the basis of a prudential estimate of the current and deferred taxes. More specifically, deferred taxes are determined on the basis of the temporary differences between the carrying amount of assets and liabilities and their tax bases. Deferred tax assets are recognised in the separate financial statements to the extent that it is probable that they will be recovered based on the Bank's ability to continue to generate positive taxable income. Deferred tax assets and liabilities are accounted for at equity level with open balances and without offsetting entries, recognising the former under "Tax assets" and the latter under "Tax liabilities". With respect to current taxes, at the level of individual taxes, advances paid are offset against the relevant tax charge, indicating the net balance under "current tax assets" or "current tax liabilities" depending on whether it is positive or negative.

Provisions for risks and charges

In line with the requirements of IAS 37, provisions for risks and charges cover liabilities, the amount or timing of which is uncertain, related to current obligations (legal or implicit), owing to a past event for which it is likely that financial resources will be used to fulfil the obligation, on condition that an estimate of the amount required to fulfil said obligation can be made at the reporting date. Where the temporary deferral in sustaining the charge is significant, and therefore the extent of the discounting will be significant, provisions are discounted at current market rates.

The provisions are reviewed at the reporting date of the annual financial statements and the interim financial statements and adjusted to reflect the current best estimate. These are recognised under their own items in the income statement in accordance with a cost classification approach based on the "nature" of the cost. Provisions related to future charges for employed personnel relating to the bonus system appear under "personnel expense".

The provisions that refer to risks and charges of a tax nature are reported as "income taxes", whereas the provisions connected to the risk of potential losses not directly chargeable to specific items in the income statement are recognised as "net accruals to provisions for risks and charges".

Other information

Post-employment benefits

According to the IFRIC, the post-employment benefits can be equated with a post-employment benefit of the "defined-benefit plan" type which, based on IAS 19, is to be calculated via actuarial methods. Consequentially, the end of the year measurement of the item in question is made based on the accrued benefits method using the Projected Unit Credit Method.

This method calls for the projection of the future payments based on historical, statistical, and probabilistic analysis, as well as in virtue of the adoption of appropriate demographic fundamentals. It allows the post-employment benefits vested at a certain date to be calculated actuarially, distributing the expense for all the years of estimated remaining employment of the existing workers, and no longer as an expense to be paid if the company ceases its activity on the reporting date.

The actuarial gains and losses, defined as the difference between the carrying amount of the liability and the present value of the obligation at year end, are recognised in equity.

An independent actuary assesses the post-employment benefits in compliance with the method indicated above.

Repurchase agreements

"Repurchase agreements" that oblige the party selling the relevant assets (for example securities) to repurchase them in the future and the "securities lending" transactions where the guarantee is represented by cash, are considered equivalent to swap transactions and, therefore, the amounts received and disbursed appear in the separate financial statements as payables and receivables. In particular, the previously mentioned "repurchase agreements" and "securities lending" transactions are recognised in the separate financial statements as payables for the spot price received, while those for investments are recognised as receivables for the spot price paid. Such transactions do not result in changes in the securities portfolio. Consistently, the cost of funds and the income from the investments, consisting of accrued dividends on the securities and of the difference between the spot price and the forward price thereof, are recognised for the accrual period under interest in the income statement.

Criteria for determining the fair value of financial instruments

Fair value is defined as "the price that would be collected for the sale of an asset or also that would be paid for the transfer of a liability in an orderly transaction between market participants", at a specific measurement date, excluding forced transactions. Underlying the definition of fair value in fact is the presumption that the company is in operation, and that it has no intention or need to liquidate, significantly reduce the volume of its assets, or engage in a transaction at unfavourable terms.

In the case of financial instruments listed in active markets, the fair value is determined based on the deal pricing (official price or other equivalent price on the last stock market trading day of the financial year of reference) of the most advantageous market to which the Group has access. For this purpose, a financial instrument is considered to be listed in an active market if the quoted prices are readily and regularly available from a price list, trader, intermediary, industrial sector, agencies that determine prices, or regulatory authority and said prices represent actual market transactions that regularly take place in normal dealings.

In the absence of an active market, the fair value is determined using measurement techniques generally accepted in financial practice, aimed at establishing what price the financial instrument would have had, on the valuation date, in a free exchange between knowledgeable and willing parties. Such measurement techniques require, in the hierarchical order in which they are presented, the use:

1. of the most recent NAV (Net Asset Value) published by the management investment company for the harmonised funds (UCITS - Undertakings for Collective Investment in Transferable Securities), the Hedge Funds and the SICAVs;
2. of the recent transaction prices observable in the markets;
3. of the price indications deducible from infoproviders (e.g., Bloomberg, Reuters);

4. of the fair value obtained from measurement models (for example, Discounting Cash Flow Analysis, Option Pricing Models) that estimate all the possible factors that influence the fair value of a financial instrument (cost of money, credit exposure, liquidity risk, volatility, foreign exchange rates, prepayment rates, etc.) based on data observable in the market, also with regards to similar instruments on the measurement date. If market data cannot be referenced for one or more risk factors, metrics internally determined on a historical-statistical basis are used. The measurement models are subject to periodic review to guarantee complete and constant reliability;
5. of the price indications provided by the counterparty issuer adjusted if necessary to take into account the counterparty and/or liquidity risk (for example, the price resolved on by the Board of Directors and/or the Shareholders for the shares of unlisted cooperative banks, the unit value communicated by the management investment company for the closed-end funds reserved to institutional investors or for other types of UCIs other than those cited in paragraph 1, the redemption value calculated in compliance with the issue regulation for the insurance contracts);
6. for the equity-linked instruments, where the measurement techniques pursuant to the previous paragraphs are not applicable: i) the value resulting from independent surveys if available; ii) the value corresponding to the portion of equity held resulting from the company's most recently approved financial statements; iii) the cost, adjusted if necessary to take into account significant reductions in value, where the fair value cannot be reliably determined.

Based on the foregoing considerations and in compliance with the IFRS, the Group classifies the measurements at fair value based on a hierarchy of levels that reflects the significance of the inputs used in the measurements. The following levels are noted:

- **Level 1** - prices (without adjustments) reported on an active market: the measurements of the financial instruments quoted on an active market based on quotations that can be understood from the market;
- **Level 2 -** the measurement is not based on prices of the same financial instrument subject to measurement, but on prices or credit spreads obtained from the official prices of essentially similar instruments in terms of risk factors, by using a given calculation method (pricing model).
  The use of this approach translates to the search for transactions present on active markets, relating to instruments that, in terms of risk factors, are comparable with the instrument subject to measurement.
  The calculation methods (pricing models) used in the comparable approach make it possible to reproduce the prices of financial instruments quoted on active markets (model calibration) without including discretional parameters - i.e. parameters whose value cannot be obtained from the prices of financial instruments present on active markets or cannot be fixed at levels as such to replicate prices present on active markets - which may influence the final valuation price in a decisive manner.
- **Level 3** - inputs that are not based on observable market data: the measurements of financial instruments not quoted on an active market, based on measurement techniques that use significant inputs that are not observable on the market, involving the adoption of estimates and assumptions by management (prices supplied by the issuing counterparty, taken from independent surveys, prices corresponding to the fraction of the equity held in the company or obtained using measurement models that do not use market data to estimate significant factors that condition the fair value of the financial instrument). This level includes measurements of financial instruments at cost price.

Business combinations

A business combination involves the combination of separate companies or business activities in a single party who has to draft the financial statements. A business combination may give rise to an investment relationship between the parent (acquirer) and the subsidiary (acquired). A combination may also provide for the acquisition of the net assets of another entity, including any goodwill, or the acquisition of another entity's capital (mergers and contributions). Based on the provisions of IFRS 3, business combinations must be accounted for by applying the acquisition method, which comprises the following phases:

- identification of the acquirer;
- determination of the cost of the business combination;
- allocation, on the acquisition date, of the business combination cost in terms of the assets acquired and the liabilities, and potential liabilities taken on.

More specifically, the cost of a business combination must be determined as the total fair value as at the date of exchange of the assets transferred, liabilities incurred or assumed, equity-linked instruments issued by the acquirer in exchange for control of the acquired company and all costs directly attributable to the business combination.

The acquisition date is the date on which control over the acquired company is actually obtained. If the acquisition is completed through a single transfer, the date of the transfer will be the acquisition date.

If the business combination is carried out through several transfers:

- the cost of the combination is the overall cost of the individual transactions
- the exchange date is the date of each exchange transaction (namely the date on which each investment is recognised in the acquiring company's financial statements), whereas the acquisition date is the one on which control is obtained over the acquired company.

The cost of a business combination is assigned by recognising the assets, liabilities and potential liabilities that are identifiable in the acquired company, at the relevant fair values at the date of acquisition.

The assets, liabilities and potential liabilities that can be identified in the acquired company are recognised separately on the acquisition date only if, on this date, they meet the following criteria:

- if an asset is not an intangible asset, it is probable that any future connected economic benefits will flow to the acquiring company and it is possible to assess its fair value reliably;
- if a liability is not a potential liability, it is probable that, in order to extinguish the obligation, investment in resources will be required to produce economic benefits and it is possible to assess the fair value reliably;
- in the case of an intangible asset or a potential liability, the relevant fair value may be assessed reliably.

The positive difference between the cost of the business combination and the acquiring company's profit sharing at the fair value net of the assets, liabilities and identifiable potential liabilities, must be accounted for as goodwill.

After the initial recognition, the goodwill acquired in a business combination is measured at the relevant cost and is submitted to an impairment test at least once a year.

If the difference is negative, a new measurement is made. This negative difference, if confirmed, is recognised immediately as income in the income statement.

A.3 - DISCLOSURE ON TRANSFERS BETWEEN PORTFOLIOS OF FINANCIAL ASSETS

A.3.1 Reclassified financial assets: change in business model, carrying amount and interest income

No financial instruments were transferred between portfolios.

A.3.2 Reclassified financial assets: change in business model, fair value and effects on comprehensive income

No financial assets were reclassified.

A.3.3 Reclassified financial assets: change in business model and effective interest rate

No financial assets held for trading were transferred.

A.4 - FAIR VALUE DISCLOSURE

QUALITATIVE DISCLOSURE

A.4.1 Fair value levels 2 and 3: valuation techniques and inputs used

Please refer to the accounting policies.

A.4.2 Processes and sensitivity of measurements

The carrying amount was assumed as a reasonable approximation of the fair value.

A.4.3 Fair value hierarchy

The following fair value hierarchy was used in order to prepare the separate financial statements:

- Level 1- Effective market quotes
- The valuation is the market price of said financial instrument subject to valuation, obtained on the basis of quotes expressed by an active market.
- Level 2 - Comparable Approach
- Level 3 - Mark-to-Model Approach

A.4.4 Other Information

The item is not applicable for the Bank.

QUANTITATIVE DISCLOSURE

A.4.5 Fair value hierarchy

A.4.5.1 Assets and liabilities measured at fair value on a recurring basis: breakdown by fair value level.

Financial assets/liabilities measured at fair value	31.12.2018			31.12.2017		
	L1	L2	L3	L1	L2	L3
1. Financial assets measured at fair value through profit or loss	-	-	-	1,201	-	-
a) financial assets held for trading	-	-	-	-	-	-
b) financial assets designated at fair value through profit or loss	-	-	-	-	-	-
c) other financial assets mandatorily measured at fair value through profit or loss	-	-	-	-	-	-
2. Financial assets measured at fair value through other comprehensive income	299,469	-	5,000	280,610	-	5,000
3. Hedging derivatives	-	-	-	-	-	-
4. Property and equipment	-	-	-	-	-	-
5. Intangible assets	-	-	-	-	-	-
TOTAL	**299,469**	**-**	**5,000**	**281,811**	**-**	**5,000**
1. Financial liabilities held for trading	-	-	-	-	-	-
2. Financial liabilities designated at fair value through profit or loss	-	-	-	-	-	-
3. Hedging derivatives	-	-	-	-	-	-
TOTAL	-	-	-	-	-	-

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

A.4.5.4 Assets and liabilities not measured at fair value or measured at fair value on a non-recurring basis:

breakdown by fair value level

Assets and liabilities not measured at fair value or measured at fair value on a non-recurring basis	31.12.2018				31.12.2017			
	CA	L1	L2	L3	CA	L1	L2	L3
1. Financial assets measured at amortised cost	2,801,813	435,482	-	2,366,331	1,981,105	84,178	-	1,896,927
2. Investment property	-	-	-	-	-	-	-	-
3. Non-current assets held for sale and disposal groups	2,221	-	-	-	-	-	-	-
TOTAL	**2,804,034**	**435,482**	**-**	**2,366,331**	**1,981,105**	**84,178**	**-**	**1,896,927**
1. Financial liabilities measured at amortised cost	2,902,240	-	-	2,902,240	2,083,435	-	-	2,083,435
2. Liabilities associated with disposal groups	-	-	-	-	-	-	-	-
TOTAL	**2,902,240**	**-**	**-**	**2,902,240**	**2,083,435**	**-**	**-**	**2,083,435**

Key:
CA = carrying amount
L1 = Level 1
L2 = Level 2
L3 = Level 3

A.5 DISCLOSURE CONCERNING "DAY ONE PROFIT/LOSS"

Nothing to report.

ASSETS

SECTION 1 - CASH AND CASH EQUIVALENTS - ITEM 10

1.1 Cash and cash equivalents: breakdown

	31.12.2018	31.12.2017
a. Cash	288	161
b. Demand deposits with Central Banks	-	-
TOTAL	**288**	**161**

SECTION 2 - FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS - ITEM 20

2.1 Financial assets held for trading: breakdown by product

	31.12.2018			31.12.2017		
	L1	L2	L3	L1	L2	L3
A. On-statement of financial position assets						
1. Debt instruments	-	-	-	-	-	-
1.1 Structured instruments	-	-	-	-	-	-
1.2 Other debt instruments	-	-	-	-	-	-
2. Equity instruments	-	-	-	1,201	-	-
3. OEIC units	-	-	-	-	-	-
4. Financing	-	-	-	-	-	-
4.1 Reverse repurchase agreements	-	-	-	-	-	-
4.2 Other	-	-	-	-	-	-
TOTAL A	-	-	-	**1,201**	-	-
B. Derivatives						
1. Financial derivatives	-	-	-	-	-	-
1.1 trading	-	-	-	-	-	-
1.2 associated with fair value option	-	-	-	-	-	-
1.3 other	-	-	-	-	-	-
2. Credit derivatives	-	-	-	-	-	-
2.1 trading	-	-	-	-	-	-
2.2 associated with fair value option	-	-	-	-	-	-
2.3 other	-	-	-	-	-	-
TOTAL B	**-**	**-**	**-**	**-**	**-**	**-**
TOTAL (A+B)		**-**	**-**	**1,201**	**-**	**-**

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

2.2 Financial assets held for trading: breakdown by debtor/issuer/counterparty

	31.12.2018	31.12.2017
A. ON-STATEMENT OF FINANCIAL POSITION ASSETS		
1. Debt instruments	-	-
a. Central Banks	-	-
b. Public administrations	-	-
c. Banks	-	-
d. Other financial companies	-	-
of which: insurance companies	-	-
e. Non-financial companies	-	-
2. Equity instruments	-	**1,201**
a. Banks	-	-
b. Other financial companies	-	-
of which: insurance companies	-	-
c. Non-financial companies	-	1,201
d. Other issuers	-	-
3. OEIC units	-	-
4. Financing	-	-
a. Central Banks	-	-
b. Public administrations	-	-
c. Banks	-	-
d. Other financial companies	-	-
of which: insurance companies	-	-
e. Non-financial companies	-	-
f. Households	-	-
TOTAL A	-	**1,201**
B. DERIVATIVES		
a. Central Counterparties	-	-
b. Other	-	-
TOTAL B	-	-
TOTAL (A+B)	-	**1,201**

SECTION 3 - FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME - ITEM 30

3.1 Financial assets measured at fair value through other comprehensive income: breakdown by product

	31.12.2018			31.12.2017		
	L1	L2	L3	L1	L2	L3
1. Debt instruments	**298,292**	-	**-**	**278,847**	-	**-**
1.1 Structured instruments	-	-	-	-	-	-
1.2 Other debt instruments	298,292	-	-	278,847	-	-
2. Equity instruments	**1,177**	-	**5,000**	**1,763**	-	**5,000**
3. Financing	-	-	-	**-**	-	-
Total	**299,469**	-	**5,000**	**280,610**	-	**5,000**

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

3.2 Financial assets measured at fair value through other comprehensive income: breakdown by debtor/issuer

	31.12.2018	31.12.2017
1. Debt instruments	**298,292**	**278,847**
a) Central Banks	-	**-**
b) Public administrations	298,292	278,847
c) Banks	-	-
d) Other financial companies	-	-
of which: insurance companies	-	-
e) Non-financial companies	-	-
2. Equity instruments	**6,177**	**6,763**
a) Banks	5,000	5,000
b) Other issuers:	1,177	1,763
- other financial companies	-	-
of which: insurance companies	-	-
- non-financial companies	1,177	1,763
- other	-	-
3. Financing	-	-
a) Central Banks	-	-
b) Public administrations	-	-
c) Banks	-	-
d) Other financial companies	-	-
of which: insurance companies	-	-
e) Non-financial companies	-	-
f) Households	**-**	**-**
Total	**304,469**	**285,610**

3.3 Financial assets measured at fair value through other comprehensive income: gross amount and total impairment losses

	Gross amount				Total impairment losses			Overall partial write-offs (*)
	First stage	of which instruments with low credit risk	Second stage	Third stage	First stage	Second stage	Third stage	
Debt instruments	298,341	-	-	-	49	-	-	-
Financing	-	-	-	-	-	-	-	-
Total at 31.12.2018	**298,341**	-	-	-	**49**	-	-	-
Total at 31.12.2017	**278,847**	-	-	-	-	-	-	-
of which: purchased or originated credit-impaired financial assets	X	X	-	-	X	-	-	-

SECTION 4 - FINANCIAL ASSETS MEASURED AT AMORTISED COST - ITEM 40

4.1 Financial assets measured at amortised cost: breakdown by product of the loans and receivables with banks

	31.12.2018						31.12.2017					
	Carrying amount			Fair Value			Carrying amount			Fair Value		
	First and second stage	Third stage	of which: purchased or originated credit-impaired	L1	L2	L3	First and second stage	Third stage	of which: purchased or originated credit-impaired	L1	L2	L3
A. Loans and receivables with Central Banks	**12,460**	**-**	**-**	-	-	**12,460**	**18,534**	**-**	**-**	-	-	**18,534**
1. Term deposits	-	-	-	X	X	X	-	-	-	X	X	X
2. Minimum reserve	12,437	-	-	X	X	X	18,534	-	-	X	X	X
3. Reverse repurchase agreements	-	-	-	X	X	X	-	-	-	X	X	X
4. Other	23	-	-	X	X	X	-	-	-	X	X	X
B. Loans and receivables with banks	**44,234**	**-**	**-**	**-**	**-**	**44,234**	**17,275**	**-**	**-**	**-**	**-**	**17,275**
1. Financing	44,234	-	-	-	-	44,234	17,275	-	-	-	-	17,275
1.1 Current accounts and demand deposits	24,046	-	-	X	X	X	17,252	-	-	X	X	X
1.2. Term deposits	**19,996**	**-**	**-**	**X**	**X**	**X**	**-**	**-**	**-**	**X**	**X**	X
1.3. Other financing:	192	-	-	X	X	X	23	-	-	X	X	X
- Reverse repurchase agreements	-	-	-	X	X	X	-	-	-	X	X	X
- Finance leases	-	-	-	X	X	X		-	-	X	X	X
- Other	192	-	-	X	X	X	23	-	-	X	X	X
2. Debt instruments	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
2.1 Structured instruments	-	-	-	-	-	-	-	-	-	-	-	-
2.2 Other debt instruments	-	-	-	-	-	-	-	-	-	-	-	-
Total	**56,694**	**-**	**-**	**-**	**-**	**56,694**	**35,809**	**-**	**-**	**-**	**-**	**35,809**

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

4.2 Financial assets measured at amortised cost: breakdown by product of the loans and receivables with customers

	31.12.2018						31.12.2017					
	Carrying amount			Fair Value			Carrying amount			Fair Value		
	First and second stage	Third stage	of which: purchased or originated credit-impaired	L1	L2	L3	First and second stage	Third stage	of which: purchased or originated credit-impaired	L1	L2	L3
1. Financing	**2,113,713**	**195,995**	**25,776**	-	-	**2,309,708**	**1,740,082**	**121,036**	**1,103**	**-**	-	**1,861,118**
1.1 Current accounts	38,536	70	-	X	X	X	17,237	57	-	X	X	X
1.2 Reverse repurchase agreements	-	-	-	X	X	X	-	-	-	X	X	X
1.3 Loans	27,602	8,470	-	X	X	X	54,768	1,993	-	X	X	X
1.4 Credit cards, personal loans and salary-backed loans	636,134	291	-	X	X	X	481,160	1	-	X	X	X
1.5. Finance leases	-	-	-	X	X	X	-	-	-	X	X	X
1.6 Factoring	974,942	176,942	25,776	X	X	X	837,181	102,815	1,103	X	X	X
1.7 Other financing	436,499	10,222	-	X	X	X	349,736	16,170	-	X	X	X
2. Debt instruments	**435,411**	**-**	**-**	**435,411**	**-**	**-**	**84,178**	**-**	**-**	**84,178**	**-**	-
2.1 Structured instruments	-	-	-	-	-	-	-	-	-	-	-	-
2.2 Other debt instruments	435,411	-	-	435,411	-	-	84,178	-	-	-	-	-
Total	**2,549,124**	**195,995**	**25,776**	**435,411**	**-**	**2,309,708**	**1,824,260**	**121,036**	**1,103**	**84,178**	**-**	**1,861,118**

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

Financing mainly includes the loans and receivables of companies that supply goods and services mainly to the Public Administration (ASL - local health authorities - and Territorial Entities) and receivables related to the pension and salary-backed loans segment.

Receivables for factoring and salary- and pension-backed loans (CQS-CQP), mainly classified under their own captions as well as under "Other financing", amount to € 1,567 million and € 652 million respectively.

Factoring receivables include default interest recognised on an accruals basis for € 42.5 million.

For classification purposes analyses are performed, some of which are complex, aimed at identifying positions which, subsequent to disbursement/acquisition, show evidence of possible impairment based on both internal information, associated with the performance of credit positions, and external information, associated with the specific sector in question.

Measuring loans and receivables with customers is an activity with a high degree of uncertainty and subjectivity involving the use of measurement models that take into account numerous quantitative and qualitative elements. These include the historical data for collections, expected cash flows and the related expected recovery times, the existence of indicators of possible impairment, the valuation of any guarantees, and the impact of risks associated with the sectors in which the Bank's customers operate.

Securities are composed entirely of Italian government securities with an average duration of 2 years and 2 months for an amount of € 435 million.

4.4 Financial assets measured at amortised cost: breakdown by debtor/issuer of the loans and receivables with customers

	31.12.2018			31.12.2017		
	First and second stage	Third stage	of which: purchased or originated credit-impaired	First and second stage	Third stage	of which: purchased or originated credit-impaired
1. Debt instruments	**435,411**	**-**	**-**	**84,178**	**-**	**-**
a) Public administrations	435,411	-	-	84,178	-	-
b) Other financial companies	-	-	-	-	-	-
of which: insurance companies	-	-	-	-	-	-
c) Non-financial companies	-	-	-	-	-	-
2. Financing to:	**2,113,713**	**195,995**	**25,776**	**1,740,082**	**121,036**	**1,103**
a) Public administrations	1,083,480	139,952	25,776	958,363	83,131	1,103
b) Other financial companies	43,429	1	-	7,578	13	-
of which: insurance companies	4	1	-	3	13	-
c) Non-financial companies	306,520	52,484	-	238,642	35,369	-
d) Households	680,284	3,558	-	535,499	2,523	-
Total	**2,549,124**	**195,995**	**25,776**	**1,824,260**	**121,036**	**1,103**

4.5 Financial assets measured at amortised cost: gross amount and total impairment losses

	Gross amount				Total impairment losses			
	First stage							
		of which instruments with low credit risk	Second stage	Third stage	First stage	Second stage	Third stage	Overall partial write-offs
Debt instruments	435,482	-	-	**-**	71	-	**-**	**-**
Financing	2,070,229	1,086,780	106,473	225,164	5,714	580	29,169	-
Total at 31.12.2018	**2,505,711**	**1,086,780**	**106,473**	**225,164**	**5,785**	**580**	**29,169**	**-**
of which: purchased or originated credit-impaired financial assets	X	X		26,062	X	**-**	286	-

SECTION 7 - EQUITY INVESTMENTS - ITEM 70

7.1 Equity investments: information on investment relationships

	Registered office	Interest %	% of votes available
A. Fully-controlled companies			
1. S.F. Trust Holdings Ltd	**London**	100%	100%
2. Largo Augusto Servizi e Sviluppo S.r.l.	**Milan**	100%	100%
3. ProntoPegno S.p.A.	**Milan**	100%	100%
C. Companies under significant influence			
1. ADV Finance S.p.A.	**Milan**	19.90%	19.90%
2. Procredit S.r.l.	**Milan**	19.90%	19.90%

Equity investments include the acquisition for € 0.6 million of a 19.90% stake in the share capital of ADV Finance S.p.A. ("ADV Finance"), and 19.90% of its subsidiary Procredit S.r.l. for € 0.2 million, as well as LASS S.r.l., the Group's real estate company. During the fourth quarter, the 10% equity investment in Axactor Italy S.p.A. was reclassified under Non-current assets held for sale and disposal groups, following the Board of Directors' resolution of December 2018 to sell the same equity investment through the exercise of the put option provided for in the contract. The carrying amount, which under the International Financial Reporting Standards is the lower of the carrying amount and the fair value, is € 2,221 thousand.

7.3 Significant equity investments: accounting information

	Cash and cash equivalents	Financial assets	Non-financial assets	Financial liabilities	Non-financial liabilities	Total income	Net interest income (expense)	Net impairment losses on property and equipment/intangible assets	Pre-tax loss from continuing operations	Post-tax loss from continuing operations	Profit (loss) on groups of assets held for sale after tax	Loss for the year	Other comprehensive income (expense), net of income tax	Comprehensive expense
A. Fully-controlled companies														
1. S.F. Trust Holdings Ltd	-	55	688	1,660	108	-	(67)	-	(212)	(212)	-	(212)	-	(212)
3. Largo Augusto Servizi e Sviluppo S.r.l.	-	-	28,423	13,627	647	-	(113)	-	(421)	(421)	-	(346)	-	(421)

7.4 Non-significant equity investments: accounting information

	Carrying amount of equity investments	Total assets	Total liabilities	Total income	Post-tax profit (loss) from continuing operations	Profit (loss) on groups of assets held for sale after tax	Profit (loss) for the year	Other comprehensive income (expense), net of income tax	Comprehensive income (expense)
C. Companies under significant influence									
1. ADV Finance S.p.A.	620	5,283	2,177	2,710	66	-	66	-	66
2 . Procredit Srl	158	727	194	306	(25)	-	(25)	-	(25)

Figures presented in accordance with the International Financial Reporting Standards.

7.5 Equity investments: changes

	31.12.2018	31.12.2017
A. Opening balance	**16,222**	**61,628**
B. Increases	**5,277**	**11,300**
B.1 Purchases	5,277	11,000
B.2 Impairment gains	-	-
B.3 Revaluations	-	-
B.4 Other increases	-	300
C. Decreases	**2,221**	**56,706**
C.1 Sales	-	-
C.2 Impairment losses	-	-
C.3 Write-offs	-	-
C.4 Other decreases	2,221	56,706
D. Closing balance	**19,278**	**16,222**
E. Total revaluations	**-**	**-**
F. Total impairment losses	**-**	**-**

The increases in Equity investments relate to the acquisition for € 0.6 million of a 19.90% stake in the share capital of ADV Finance S.p.A. ("ADV Finance"), and 19.90% of its subsidiary Procredit S.r.l. for € 0.2 million, in addition to the contribution of € 3.5 million for the incorporation of ProntoPegno, a company awaiting authorisation from the Bank of Italy to be entered in the Register referred to in Article 106 of Legislative Decree No. 385/1993. Once the authorisation to conduct business has been obtained, all the assets and liabilities relating to the collateralised loan business will be transferred to the company, in addition to the personnel dedicated to the management and development of the business. During the fourth quarter, the 10% equity investment in Axactor Italy S.p.A. was reclassified under Non-current assets held for sale and disposal groups, following the Board of Directors' resolution of December 2018 to sell the same equity investment through the exercise of the put option provided for in the contract. The carrying amount, which under the International Financial Reporting Standards is the lower of the carrying amount and the fair value, is € 2,221 thousand.

SECTION 8 - PROPERTY AND EQUIPMENT - ITEM 80

8.1 Operating property and equipment: breakdown of the assets measured at cost

	31.12.2018	31.12.2017
1. Owned	**710**	**814**
a) land	-	-
b) buildings	-	-
c) furniture	260	264
d) electronic equipment	421	525
e) other	29	25
2. Under finance lease	**-**	**-**
a) land	-	-
b) buildings	-	-
c) furniture	-	-
d) electronic equipment	-	-
e) other	-	-
TOTAL	**710**	**814**
of which: obtained from the enforcement of guarantees received	**-**	-

Property and equipment are recognised in the separate financial statements in accordance with the general acquisition cost criteria, including the related charges and any other expenses incurred to place the assets in conditions useful for the bank, in addition to indirect costs for the portion reasonably attributable to assets that refer to the costs incurred, as at the end of 2018.

Depreciation rates:

- Office furniture: 12%
- Furnishings: 15%
- Electronic machinery and miscellaneous equipment: 20%
- Assets less than Euro 516: 100%

8.6 Operating assets: changes

	Land	Buildings	Furniture	Electronic equipment	Other	Total
A. Gross opening balances	**-**	**-**	**1,162**	**1,744**	**70**	**2,976**
A.1 Total net impairment losses	-	-	898	1,219	45	2,162
A.2 Net opening balances	**-**	**-**	264	525	25	814
B. Increases	**-**	**-**	**51**	**231**	**20**	**302**
B.1 Purchases	-	-	51	231	20	302
B.2 Capitalised improvement costs	-	-	-	-	-	**-**
B.3 Impairment gains	-	-	-	-	-	**-**
B.4 Fair value gains recognised in	**-**	**-**	**-**	**-**	**-**	**-**
a. equity	-	-	-	-	-	**-**
b. profit or loss	-	-	-	-	-	**-**
B.5 Exchange rate gains	-	-	-	-	-	**-**
B.6 Transfers from investment property	-	-	-	-	-	**-**
B.7 Altre variazioni	-	-	-	-	-	**-**
C. Diminuzioni	**-**	**-**	**55**	**335**	**16**	**406**
C.1 Sales	-	-	2	1	-	3
C.2 Depreciation	-	-	53	331	16	400
C.3 Impairment losses recognised in	**-**	**-**	**-**	**-**	**-**	**-**
a. equity	-	-	-	-	-	**-**
b. profit or loss	-	-	-	-	-	**-**
C.4 Fair value losses recognised in	**-**	**-**	**-**	**-**	**-**	**-**
a. equity	-	-	-	-	-	**-**
b. profit or loss	-	-	-	-	-	**-**
C.5 Exchange rate losses	-	-	-	-	-	**-**
C.6 Transfers to:	**-**	**-**	**-**	**-**	**-**	**-**
a. investment property	-	-	-	-	-	**-**
b. non-current assets held for sale and disposal groups	-	-	-	-	-	**-**
C.7 Other decreases	-	-	-	3	-	3
D. Net closing balance	**-**	**-**	**260**	**421**	**29**	**710**
D.1 Total net impairment losses	-	-	953	1,554	61	2,568
D.2 Gross closing balance	**-**	**-**	1,213	1,975	90	3,278
E. Measurement at cost	**-**	**-**	**260**	**421**	**29**	**710**

SECTION 9 - INTANGIBLE ASSETS - ITEM 90

9.1 Intangible assets: breakdown by type of asset

	31.12.2018		31.12.2017	
	Finite useful life	Indefinite useful life	Finite useful life	Indefinite useful life
A.1 Goodwill	-	**1,786**	-	**1,786**
A.2 Other intangible assets	**2**	-	**4**	-
A.2.1 Assets measured at cost:	2	-	4	-
a. Internally developed assets	-	-	-	-
b. Other	2	-	4	-
A.2.2 Assets measured at fair value:	-	-	-	-
a. Internally developed assets	-	-	-	-
b. Other	-	-	-	-
TOTAL	**2**	**1,786**	**4**	**1,786**

The other intangible assets are recognised at purchase cost including related costs, and are systematically amortised over a period of 5 years. The item mainly refers to software.

The goodwill originates from the merger of the subsidiary Solvi S.r.l. which took place in 2013.

Subsequent to the merger, the former Solvi's assets were fully integrated with those of the Bank with the purpose of pursuing efficiencies both in terms of expected synergies with the other businesses and in terms of overall operating costs. Since the activities once performed by Solvi S.r.l. are now fully integrated and inseparable from the rest of Banca Sistema's operations, the Bank is not currently able to distinguish the expected cash flows of the merged entity from those of the Bank itself.

Therefore, in this specific case, the goodwill of € 1.8 million recognised in the separate financial statements is an asset that cannot be separated from the rest of the Bank.

In particular, the impairment test pursuant to IAS 36 requires that the recoverable value of goodwill be greater than its carrying amount in the separate financial statements; in detail, as provided for by paragraph 18 of IAS 36, the recoverable value has been defined as "the higher of the fair value of an asset or of a cash-generating unit less costs to sell and its value in use".

Specifically, the impairment test was conducted referring to the "Value in use" based on the flows indicated in the Bank's business plan in relation to the 2018-2020 period and to a forecast of expected cash flows for the 2021-2023 period, conservatively assuming an estimated growth rate of 1.5% on an annual basis.

The main parameters used for estimation purposes were as follows:

Risk Free Rate + country risk premium	2.9%
Equity Risk Premium	4.6%
Beta	1.3%
Cost of equity	9.0%
Growth rate "g"	1.5%

The estimated value in use obtained based on the parameters used and the growth assumptions is considerably greater than equity as at 31 December 2018. Furthermore, considering that the value in use was determined via estimates and assumptions that may introduce elements of uncertainty, sensitivity analyses -

as required by IFRS - were performed with the purpose of verifying the variations of the results previously obtained as a function of the basic assumptions and parameters. In particular, the quantitative exercise was completed by a stress test of the parameters related to the Bank's growth rate and the discount rate of the expected cash flows (quantified in an isolated or simultaneous movement of 50 bps), that confirmed the absence of impairment indicators, confirming a value in use once again significantly greater than the carrying amount of goodwill in the separate financial statements.

Considering all the above, with no qualitative trigger events that suggest a need for impairment having been identified, management deemed it appropriate not to recognise an impairment loss on goodwill recognised in the separate financial statements at 31 December 2018.

9.2 Intangible assets: changes

		Other intangible assets: internally developed		Other intangible assets: Other		
	Goodwill	Fin	Indef	Fin	Indef	Total
A. Opening balance	**1,786**	-	-	**3,103**	-	**4,889**
A.1 Total net impairment losses	-	-	-	3,099	-	3,099
A.2 Net opening balances	**1,786**	-	-	**4**	-	**1,790**
B. Increases	**-**	-	-	**1**	-	**1**
B.1 Purchases	-	-	-	1	-	1
B.2 Increases in internally developed assets	X	-	-	**-**	-	-
B.3 Impairment gains	X	-	-	**-**	-	-
B.4 Fair value gains recognised in:	-	-	-	**-**	-	-
- equity	X	-	-	**-**	-	-
- profit or loss	X	-	-	**-**	-	-
B.5 Exchange rate gains	-	-	-	**-**	-	-
B.6 Other increases	-	-	-	**-**	-	-
C. Decreases	**-**	-	-	**3**	-	**3**
C.1 Sales	-	-	-	-	-	-
C.2 Impairment losses	-	-	-	3	-	3
- Amortisation	X	-	-	3	-	3
- Impairment losses:	-	-	-	**-**	-	-
+ equity	X	-	-	**-**	-	-
+ profit or loss	-	-	-	**-**	-	-
C.3 Fair value losses recognised in:	-	-	-	**-**	-	-
- equity	X	-	-	**-**	-	-
- profit or loss	X	-	-	**-**	-	-
C.4 Transfers to disposal groups	-	-	-	**-**	-	-
C.5 Exchange rate losses	-	-	-	**-**	-	-
C.6 Other decreases	-	-	-	**-**	-	-
D. Net closing balance	**1,786**	-	-	**2**	-	**1,788**
D.1 Total net impairment losses	-	-	-	3,102	-	3,102
E. Gross closing balance	**1,786**	-	-	**3,104**	-	**4,890**
F. Measurement at cost	1,786	-	-	2	-	1,788

Key - Fin: finite useful life | Indef: indefinite useful life

Goodwill refers to the merger of the subsidiary Solvi S.r.l. which took place on 1 August 2013.

SECTION 10 - TAX ASSETS AND TAX LIABILITIES - ITEM 100 OF ASSETS AND ITEM 60 OF LIABILITIES

Below is the breakdown of the current tax assets and current tax liabilities

	31.12.2018	31.12.2017
Current tax assets	**9,086**	**12,308**
IRES prepayments	6,781	9,467
IRAP prepayments	2,278	2,811
Other	27	30
Current tax liabilities	**(12,531)**	**(8,837)**
Provision for IRES	(9,321)	(6,618)
Provision for IRAP	(3,210)	(2,219)
Provision for substitute tax	-	-
Total	**(3,445)**	**3,471**

10.1 Deferred tax assets: breakdown

	31.12.2018	31.12.2017
Deferred tax assets through profit or loss:	**6,716**	**6,198**
Impairment losses on loans	2,756	2,756
Non-recurring transactions	533	705
Other	3,427	2,737
Deferred tax assets through equity:	**910**	**414**
Non-recurring transactions	311	414
HTCS securities	504	-
Other	95	-
Total	**7,626**	**6,612**

10.2 Deferred tax liabilities: breakdown

	31.12.2018	31.12.2017
Deferred tax liabilities through profit or loss:	**12,222**	**9,829**
Uncollected default interest income	12,094	9,633
Other	128	196
Deferred tax liabilities through equity:	**9**	**289**
HTCS securities	9	289
Total	**12,231**	**10,118**

10.3 Changes in deferred tax assets (through profit or loss)

	31.12.2018	31.12.2017
1. Opening balance	**6,198**	**3,784**
2. Increases	**1,847**	**4,388**
2.1 Deferred tax assets recognised in the year	1,847	4,388
a. related to previous years	206	-
b. due to changes in accounting policies	-	-
c. impairment gains	-	-
d. other	1,641	1,170
e. business combination transactions	-	3,218
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	**1,329**	**1,974**
3.1 Deferred tax assets derecognised in the year	1,329	1,974
a. reversals	-	-
b. impairment due to non-recoverability	-	-
c. changes in accounting policies	-	-
d. other	1,329	1,974
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
a. conversion into tax assets pursuant to Law 214/2011	-	-
b. other	-	-
4. Closing balance	**6,716**	**6,198**

10.3 bis Change in deferred tax assets pursuant to Law 214/2011

	31.12.2018	31.12.2017
1. Opening balance	**3,429**	**2,373**
2. Increases	**-**	**1,362**
3. Decreases	**53**	**306**
3.1 Reversals	-	-
3.2 Conversions into tax assets	-	-
a) arising on loss for the year	-	-
b) arising on tax losses	-	-
3.3 Other decreases	53	306
4. Closing balance	**3,376**	**3,429**

10.4 Changes in deferred tax liabilities (through profit or loss)

	31.12.2018	31.12.2017
1. Opening balance	**9,829**	**3,234**
2. Increases	**5,802**	**7,934**
2.1 Deferred tax liabilities recognised in the year	5,802	7,934
a. related to previous years	-	-
b. due to changes in accounting policies	-	-
c. other	5,802	4,007
d. business combination transactions	-	3,927
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	**3,409**	**1,339**
3.1 Deferred tax liabilities derecognised in the year	3,409	1,339
a. reversals	-	-
b. due to changes in accounting policies	-	-
c. other	3,409	1,339
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
4. Closing balance	**12,222**	**9,829**

10.5 Change in deferred tax assets (through equity)

	31.12.2018	31.12.2017
1. Opening balance	**414**	**551**
2. Increases	**600**	**-**
2.1 Deferred tax assets recognised in the year	600	-
a. related to previous years	-	-
b. due to changes in accounting policies	-	-
c. other	600	-
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	**104**	**137**
3.1 Deferred tax assets derecognised in the year	104	137
a. reversals	-	-
b. impairment due to non-recoverability	-	-
c. due to changes in accounting policies	-	-
d. other	104	137
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
4. Closing balance	**910**	**414**

10.6 Change in deferred tax liabilities (through equity)

	31.12.2018	31.12.2017
1. Opening balance	**289**	**336**
2. Increases	**9**	**289**
2.1 Deferred tax liabilities recognised in the year	9	289
a. related to previous years	-	-
b. due to changes in accounting policies	-	-
c. other	9	289
2.2 New taxes or tax rate increases	-	-
2.3 Other increases	-	-
3. Decreases	**289**	**336**
3.1 Deferred tax liabilities derecognised in the year	289	336
a. reversals	-	-
b. due to changes in accounting policies	-	-
c. other	289	336
3.2 Tax rate reductions	-	-
3.3 Other decreases	-	-
4. Closing balance	**9**	**289**

SECTION 11 - NON-CURRENT ASSETS HELD FOR SALE AND DISPOSAL GROUPS AND ASSOCIATED LIABILITIES
ITEM 110 OF ASSETS AND ITEM 70 OF LIABILITIES

11.1 Non-current assets held for sale and disposal groups: breakdown by type of asset

	31.12.2018	31.12.2017
A. Assets held for sale	-	-
A.1 Financial assets	-	-
A.2 Equity investments	2,221	-
A.3 Property and equipment	-	-
of which: obtained from the enforcement of guarantees received	-	-
A.4 Intangible assets	-	-
A.5 Other non-current assets	-	-
TOTAL A	**2,221**	**-**
of which measured at cost	2,221	-
of which measured at fair value - level 1	-	-
of which measured at fair value - level 2	-	-
of which measured at fair value - level 3	2,221	-
B. Discontinued operations	-	-
B.1 Financial assets measured at fair value through profit or loss	-	-
- financial assets held for trading	-	-
- financial assets designated at fair value through profit or loss	-	-
- other financial assets mandatorily measured at fair value through profit or loss	-	-
B.2 Financial assets measured at fair value through other comprehensive income	-	-
B.3 Financial assets measured at amortised cost	-	-
B.4 Equity investments	-	-
B.5 Property and equipment	-	-
of which: obtained from the enforcement of guarantees received	-	-
B.6 Intangible assets	-	-
B.7 Other assets	-	-
TOTAL B	-	-
of which measured at cost	-	-
of which measured at fair value - level 1	-	-
of which measured at fair value - level 2	-	-
of which measured at fair value - level 3	-	-
C. Liabilities associated with assets held for sale	-	-
C.1 Payables	-	-
C.2 Securities	-	-
C.3 Other liabilities	-	-
TOTAL C	-	-
of which measured at cost	-	-
of which measured at fair value - level 1	-	-
of which measured at fair value - level 2	-	-
of which measured at fair value - level 3	-	-
D. Liabilities associated with discontinued operations	-	-
D.1 Financial liabilities measured at amortised cost	-	-
D.2 Financial liabilities held for trading	-	-
D.3 Financial liabilities designated at fair value through profit or loss	-	-
D.4 Provisions	-	-
D.5 Other liabilities	-	-
TOTAL D	-	-
of which measured at cost	-	-
of which measured at fair value - level 1	-	-
of which measured at fair value - level 2	-	-
of which measured at fair value - level 3	-	-

SECTION 12 - OTHER ASSETS - ITEM 120

12.1 Other assets: breakdown

	31.12.2018	31.12.2017
Tax advances	6,939	8,357
Prepayments not related to a specific item	1,711	630
Other	1,587	2,777
Work in progress	952	995
Trade receivables	610	473
Leasehold improvements	113	156
Security deposits	48	53
Total	**11,960**	**13,441**

The item is mainly composed of tax advances relative to virtual stamp duties and withholding taxes on interest expense. "Work in progress" predominantly relates to bank transfers allocated to their own items and set to zero in January 2019.

LIABILITIES

SECTION 1 - FINANCIAL LIABILITIES MEASURED AT AMORTISED COST - ITEM 10

1.1 Financial liabilities measured at amortised cost: breakdown by product of due to banks

	31.12.2018				31.12.2017			
	Carrying amount	Fair value			Carrying amount	Fair value		
		L1	L2	L3		L1	L2	L3
1. Due to Central banks	412,850	X	X	X	192,064	X	X	X
2. Due to banks	282,347	X	X	X	325,469	X	X	X
2.1 Current accounts and demand deposits	53	X	X	X	13,688	X	X	X
2.2 Term deposits	282,294	X	X	X	311,781	X	X	X
2.3 Financing	-	X	X	X	-	X	X	X
2.3.1 Repurchase agreements	-	X	X	X	-	X	X	X
2.3.2 Other	-	X	X	X	-	X	X	X
2.4 Commitments to repurchase own equity instruments	-	X	X	X	-	X	X	X
2.5 Other payables	-	X	X	X	-	X	X	X
TOTAL	**695,197**			**695,197**	**517,533**			**517,533**

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

1.2 Financial liabilities measured at amortised cost: breakdown by product of due to customers

	31.12.2018				31.12.2017			
	Carrying amount	Fair value			Carrying amount	Fair value		
		L1	L2	L3		L1	L2	L3
1. Current accounts and demand deposits	660,751	X	X	X	510,970	X	X	X
2. Term deposits	957,862	X	X	X	446,366	X	X	X
3. Financing	283,244	X	X	X	326,687	X	X	X
3.1 Repurchase agreements	179,819	X	X	X	215,624	X	X	X
3.2 Other	103,425	X	X	X	111,063	X	X	X
4. Commitments to repurchase own equity instruments	-	X	X	X	-	X	X	X
5. Other payables	199	X	X	X	109	X	X	X
TOTAL	**1,902,056**			**1,902,056**	**1,284,132**			**1,284,132**

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

1.3 Financial liabilities measured at amortised cost: breakdown by product of the securities issued

	31.12.2018				31.12.2017			
	Carrying amount	Fair value			Carrying amount	Fair value		
		L1	L2	L3		L1	L2	L3
A. Securities								
1. bonds	**304,987**	**-**	**-**	**304,987**	**281,770**	**-**	**-**	**281,770**
1.1 structured	-	-	-	-	-	-	-	-
1.2 other	304,987	-	-	304,987	281,770	-	-	281,770
2. other securities	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
2.1 structured	-	-	-	-	-	-	-	-
2.2 other	-	-	-	-	-	-	-	-
TOTAL	**304,987**	**-**	**-**	**304,987**	**281,770**	**-**	**-**	**281,770**

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

1.4 Breakdown of subordinated loans/securities

	Issuer	Type of issue	Coupon	Maturity date	Nominal amount	IFRS amount
Tier 1 Capital	Banca Sistema S.p.A.	Tier 1 subordinated loans with mixed rate	Until 17 June 2023, fixed rate at 7% From 18 June 2023, 6-month Euribor +5% variable rate	Perpetual	8,000	8,017
Tier 2 Capital	Banca Sistema S.p.A.	Subordinated ordinary loans (Tier 2)	6-month Euribor + 5.5%	15/11/2022	12,000	12,081
Tier 2 Capital	Banca Sistema S.p.A.	Subordinated ordinary loans (Tier 2)	6-month Euribor + 4.5%	30/03/2027	19,500	19,489
TOTAL					**39,500**	**39,587**

SECTION 6 - TAX LIABILITIES - ITEM 60

The breakdown as well as the change in the deferred tax liabilities were illustrated in Part B Section 10 of assets in these notes to the separate financial statements.

SECTION 8 - OTHER LIABILITIES - ITEM 80

8.1 Other liabilities: breakdown

	31.12.2018	31.12.2017
Payments received in the reconciliation phase	37,959	43,912
Tax liabilities with the Tax Authority and other tax authorities	9,121	10,261
Accrued expenses	6,043	3,411
Trade payables	5,767	5,591
Work in progress	4,760	7,176
Due to employees	797	735
Pension repayments	654	659
Due to group companies	92	107
Other	41	64
TOTAL	**65,234**	**71,916**

SECTION 9 - POST-EMPLOYMENT BENEFITS - ITEM 90

9.1 Post-employment benefits: changes

	31.12.2018	31.12.2017
A. Opening balance	**2,172**	**1,640**
B. Increases	**460**	**770**
B.1 Accruals	460	412
B.2 Other increases	-	358
C. Decreases	**230**	**238**
C.1 Payments	196	222
C.2 Other decreases	34	16
D. Closing balance	**2,402**	**2,172**
TOTAL	**2,402**	**2,172**

9.2 Other Information

The actuarial amount of post-employment benefits was calculated by an external actuary, who issued an appraisal.

The other decreases refer to the actuarial gain accounted for in 2018. The payments made refer to post-employment benefits paid in 2018.

The technical valuations were conducted on the basis of the assumptions described in the following table:

Annual discount rate	1.57%
Annual inflation rate	1.50%
Annual post-employment benefits increase rate	2.625%
Annual salary increase rate	1.00%

The discount rate used for determining the present value of the obligation was calculated, pursuant to IAS 19.83, from the Iboxx Corporate AA index with 10+ duration during the valuation month.

To this end, a choice was made to select the yield with a duration comparable to the duration of the set of workers subject to valuation.

SECTION 10 - PROVISIONS FOR RISKS AND CHARGES - ITEM 100

10.1 Provisions for risks and charges: breakdown

	31.12.2018	31.12.2017
1. Provisions for credit risk related to commitments and financial guarantees issued	7	-
2. Provisions for other commitments and other guarantees issued	-	-
3. Internal pension funds	-	-
4. Other provisions for risks and charges	9,214	6,698
4.1 legal and tax disputes	3,029	3,008
4.2 personnel expense	6,139	3,690
4.3 other	46	-
TOTAL	**9,221**	**6,698**

10.2 Provisions for risks and charges: changes

	Provisions for other commitments and other guarantees issued	Pension funds	Other provisions for risks and charges	**Total**
A. Opening balance	**-**	**-**	**6.698**	**6.698**
B. Increases	**22**	**-**	**4.482**	**4.504**
B.1 Accruals	-	-	4.314	4.314
B.2 Discounting	-	-	-	-
B.3 Changes due to discount rate changes	-	-	-	-
B.4 Other increases	22	-	168	190
C. Decreases	**15**	**-**	**1.966**	**1.981**
C.1 Utilisations	-	-	1.403	1.403
C.2 Changes due to discount rate changes	-	-	-	-
C.3 Other decreases	15	-	563	578
D. Closing balance	**7**	**-**	**9.214**	**9.221**

The provision for risks and charges of € 9.2 million includes the estimated liabilities attributable to the Beta acquisition, the estimated portion of the bonus for the year, the deferred portion of the bonus accrued in previous years, and the update to the estimate related to the non-compete agreement. The provision also includes an estimate of the charges relating to legal actions within the framework of a lending transaction in which the end borrower is bankrupt, and the estimated charges for labour-related lawsuits and legal disputes.

The other increases refer mainly to the actuarial loss for the NCA accounted for in 2018.

10.3 Provisions for credit risk related to commitments and financial guarantees issued

	Provisions for credit risk related to commitments and financial guarantees issued			
	First stage	Second stage	Third stage	**Total**
1. Commitments to disburse funds	-	-	-	-
2. Financial guarantees issued	7	-	-	7
Total	**7**	**-**	**-**	**7**

10.5 Internal defined benefit pension funds

Nothing to report.

10.6 Provisions for risks and charges - other provisions

	31.12.2018	31.12.2017
Legal and tax disputes	3,029	3,008
Personnel expense	6,139	3,690
Other	46	-
TOTAL	**9,214**	**6,698**

"Personnel expense" includes:

- the provisions made for variable remuneration to be paid to employees in subsequent years, for which the due date and/or amount are uncertain;
- an estimate of labour-related disputes;
- the amount resulting from the actuarial valuation of the non-compete agreement under IAS 19, as described below.

The calculation method can be summarised in the following steps:

- projection for each employee in service at the valuation date of the NCA that has already been accrued, and the future NCA portions that will be accrued up to an uncertain payment date;
- determination for each employee of the NCA payments that the Bank will have to make should the employee leave due to dismissal or retirement;
- discounting, at the valuation date, of each probable payment.

In particular, the annual discount rate used for determining the present value of the obligation was calculated, pursuant to IAS 19.83, from the Iboxx Corporate AA index with 10+ duration during the valuation month. To this end, a choice was made to select the yield with a duration comparable to the duration of the set of workers subject to valuation.

SECTION 12 - BANK EQUITY - ITEMS 110, 130, 140, 150, 160, 170 AND 180

12.1 "Share capital" and "Treasury shares": breakdown

The share capital of Banca Sistema is composed of 80,421,052 ordinary shares with a nominal amount of € 0.12 for a total paid-in share capital of € 9,651 thousand. All outstanding shares have regular dividend entitlement from 1 January. Based on evidence from the Shareholders' Register and more recent information available, as at 2 July 2015 the shareholders with stakes of more than 5%, the threshold above which Italian law (art. 120 of the Consolidated Finance Act) requires disclosure to the investee and Consob, were as follows:

SHAREHOLDERS	% HELD
SGBS	23.10%
Garbifin	0.51%
Fondazione Sicilia	7.40%
Fondazione Cassa di Risparmio di Alessandria	7.91%
Fondazione Pisa	7.61%
Market	*53.47%*

At 31 December 2018, after the launch in 2018 of a plan for the repurchase of treasury shares designed to create a stock of securities to be used for the incentive plan for the Group's key personnel, the Bank held 104,661 shares (equal to 0.13% of the share capital).

The breakdown of the bank's equity is shown below:

	31.12.2018	31.12.2017
1. Share capital	9,651	9,651
2. Share premium	39,184	39,268
3. Reserves	79,804	59,391
4. (Treasury shares)	(199)	(149)
5. Valuation reserves	(1,131)	367
6. Equity instruments	-	-
7. Profit for the year	28,071	27,560
TOTAL	**155,380**	**136,088**

For changes in reserves, please refer to the statement of changes in equity.

12.2 Share capital - Number of shares: changes

	Ordinary	Other
A. Opening balance	**80,421,052**	**-**
- fully paid-in	80,421,052	-
- not fully paid-in	-	-
A.1 Treasury shares (-)	70,000	-
A.2 Outstanding shares: opening balance	**80,351,052**	**-**
B. Increases	**69,515**	**-**
B.1 New issues	69,515	-
against consideration:	-	
- business combination transactions	-	-
- conversion of bonds	-	-
- exercise of warrants	-	-
- other	-	-
bond issues:	69,515	
- to employees	24,346	-
- to directors	45,169	-
- other	-	-
B.2 Sale of treasury shares	-	-
B.3 Other increases	-	-
C. Decreases	**104,176**	**-**
C.1 Cancellation	-	-
C.2 Repurchase of treasury shares	104,176	-
C.3 Disposal of equity investments	-	-
C.4 Other decreases	-	-
D. Outstanding shares: closing balance	**80,316,391**	**-**
D.1 Treasury shares (+)	104,661	-
D.2 Closing balance	80,421,052	-
- fully paid-in	80,421,052	-
- not fully paid-in	-	-

12.4 Income-related reserves: other information

In compliance with art. 2427(7 bis) of the Italian Civil Code, below is the detail of the equity items revealing the origin and possibility of use and distributability.

Natura	Amount as at 31.12.2018	Possible use	Available portion
A. Share capital	9,651	-	-
B. Equity-related reserves	-	-	-
Share premium reserve	39,184	A,B,C	-
Reserve to provide for losses	-	-	-
C. Income-related reserves:	-	-	-
Legal reserve	1,930	B	-
Valuation reserve	(1,131)	-	-
Negative goodwill	1,774	A,B,C	-
Retained earnings	76,948	A,B,C	-
Reserve for treasury shares	200	-	-
Reserve for future capital increase	-	-	-
D. Other reserves	(1,048)	-	-
Treasury shares	(199)	-	-
TOTAL	**127,309**	-	-
Profit for the year	28,071	-	-
TOTAL EQUITY	**155,380**	-	-
Undistributable portion	-	-	-
Distributable portion	-	-	-

Key
A: for share capital increase
B: to cover losses
C: for distribution to shareholders

OTHER INFORMATION

1. Commitments and financial guarantees issued (other than those designated at fair value)

	Nominal amount of commitments and financial guarantees issued				
	First stage	Second stage	Third stage	31.12.2018	31.12.2017
Commitments to disburse funds	**249,013**	**18,966**	**17,931**	**285,910**	**2,804**
a) Central Banks	-	-	-	-	-
b) Public administrations	-	-	-	-	-
c) Banks	-	-	-	-	2,159
d) Other financial companies	176,660	-	-	176,660	645
e) Non-financial companies	70,002	18,966	17,931	106,899	-
f) Households	2,351	-	-	2,351	-
Financial guarantees issued	**2,446**	**-**	**-**	**2,446**	-
a) Central Banks	-	-	-	-	-
b) Public administrations	-	-	-	-	-
c) Banks	2,446	-	-	2,446	-
d) Other financial companies	-	-	-	-	-
e) Non-financial companies	-	-	-	-	-
f) Households	-	-	-	-	-

The item “financial guarantees issued - banks” includes the commitments taken on with the interbank guarantee systems; the item “Irrevocable commitments to disburse funds” is related to the equivalent value of the securities to receive for transactions to be settled.

2. Other commitments and other guarantees issued

	Nominal amount	
	31.12.2018	31.12.2017
Other guarantees issued	**970**	**-**
of which: impaired	-	-
a) Central Banks	-	-
b) Public administrations	-	-
c) Banks	-	-
d) Other financial companies	-	-
e) Non-financial companies	900	-
f) Households	70	-
Other commitments	-	-
of which: impaired	-	-
a) Central Banks	-	-
b) Public administrations	-	-
c) Banks	-	-
d) Other financial companies	-	-
e) Non-financial companies	-	-
f) Households	-	-

3. Assets pledged as collateral for liabilities and commitments

	31.12.2018	31.12.2017
1. Financial assets measured at fair value through profit or loss	-	-
2. Financial assets measured at fair value through other comprehensive income	91,989	43,154
3. Financial assets measured at amortised cost	258,235	75,260
4. Property and equipment	-	-
of which: Property and equipment included among inventories	-	-

5. Management and trading on behalf of third parties

	Amount
1. Execution of orders on behalf of customers	**-**
a) purchases	-
1. settled	-
2. unsettled	-
b) sales	-
1. settled	-
2. unsettled	-
2. Individual asset management	**-**
3. Securities custody and administration	**1,378,087**
a) third-party securities held as part of depositary bank services (excluding asset management)	-
1. securities issued by the reporting entity	-
2. other securities	-
b) third-party securities on deposit (excluding asset management): other	67,276
1. securities issued by the reporting entity	3,857
2. other securities	63,419
c) third-party securities deposited with third parties	67,276
d) securities owned by the bank deposited with third parties	1,243,535
4. Other transactions	**-**

PART C - INFORMATION ON THE INCOME STATEMENT

SECTION 1 - INTEREST - ITEMS 10 AND 20

1.1. Interest and similar income: breakdown

	Debt instruments	Financing	Other transactions	2018	2017
1. Financial assets measured at fair value through profit or loss:	-	-	-	-	-
1.1 Financial assets held for trading	-	-	-	-	-
1.2 Financial assets designated at fair value through profit or loss	-	-	-	-	-
1.3 Other financial assets mandatorily measured at fair value through profit or loss	-	-	-	-	-
2. Financial assets measured at fair value through other comprehensive income	-	-	X	-	-
3. Financial assets measured at amortised cost:	258	97,953	-	98,211	89,303
3.1 Loans and receivables with banks	-	51	X	51	825
3.2 Loans and receivables with customers	258	97,902	X	98,160	88,478
4. Hedging derivatives	X	X	-	-	-
5. Other assets	X	X	-	-	-
6. Financial liabilities	X	X	X	1,679	990
TOTAL	**258**	**97,953**	**-**	**99,890**	**90,293**
of which: interest income on impaired financial assets	-	-	-	-	-

The main contribution came from interest income on the factoring portfolio of € 75 million (equal to 78% of the entire loans and receivables portfolio), increasing by 6% over the previous year. The component linked to default interest from legal action at 31 December 2018 was € 28.4 million (€ 26.8 million in 2017, excluding € 2.8 million related to the early termination of the guarantee agreement provided by the former shareholder of Beta Stepstone, the company acquired in 2016 and then merged into Banca Sistema the following year):

- of which € 18.1 million resulting from the actual recovery estimates (€ 7.8 million from the updated recovery estimates, of which € 4.9 million attributable to previous years: € 17.6 million at 31 December 2017, of which € 3.7 million from previous years);
- of which € 10.3 million (€ 9.2 million in 2017) coming from net collections during the year, i.e. the difference between the amount collected during the year, equal to € 19.2 million (€ 14.8 million in 2017) and that recognised on an accruals basis in previous years.

The other significant element of this item is attributable to interest on the salary- and pension-backed portfolios, which rose from € 13.2 million to € 19.6 million (an increase of 48% over the previous year), whereas interest declined on the SME portfolios, which contributed € 2.0 million to the total, following the strategic decision to discontinue this area of the business.

1.3 Interest and similar expense: breakdown

	Liabilities	Securities	Other transactions	2018	2017
1. Financial liabilities measured at amortised cost	17,108	6,992	-	24,100	18,361
1.1 Due to Central banks	786	X	X	786	-
1.2 Due to banks	1,750	X	X	1,750	1,603
1.3 Due to customers	14,572	X	X	14,572	12,949
1.4 Securities issued	X	6,992	X	6,992	3,809
2. Financial liabilities held for trading	-	-	-	-	-
3. Financial liabilities designated at fair value through profit or loss	-	-	-	-	-
4. Other liabilities and provisions	X	X	-	-	-
5. Hedging derivatives	X	X	-	-	-
6. Financial assets	X	X	X	1,044	1,123
TOTAL	**17,108**	**6,992**	**-**	**25,144**	**19,484**

Financial assets at 31 December 2018 were largely composed of the negative yield on Italian government bonds and the above par acquisition of a loan portfolio consisting of collateral-backed loans.

SECTION 2 - NET FEE AND COMMISSION INCOME - ITEMS 40 AND 50

2.1 Fee and commission income: breakdown

	2018	2017
a. guarantees given	18	13
b. credit derivatives	-	-
c. management, brokerage and consultancy services:	165	96
1. trading in financial instruments	-	-
2. foreign currency transactions	-	-
3. individual asset management	7	-
4. securities custody and administration	1	1
5. depositary services	-	-
6. placement of securities	97	49
7. order collection and transmission	60	46
8. consultancy services	-	-
8.1. on investments	-	-
8.2. on financial structure	-	-
9. distribution of third party services	-	-
9.1. asset management	-	-
9.1.1. individual	-	-
9.1.2. collective	-	-
9.2. insurance products	-	-
9.3. other products	-	-
d. collection and payment services	100	117
e. services for securitisations	-	-
f. services for factoring	15,772	11,462
g. tax collection services	-	-
h. management of multilateral trading facilities	-	-
i. keeping and management of current accounts	48	75
j. other services	1,522	1,284
TOTAL	**17,625**	**13,047**

2.2 Fee and commission income: distribution channels of products and services

	2018	2017
A) at its branches:	**104**	**49**
1. asset management	7	-
2. placement of securities	97	49
3. third-party services and products	-	-
B) off-premises:	**-**	**-**
1. asset management	-	-
2. distribution of securities	-	-
3. third-party services and products	-	-
C) other distribution channels:	**-**	**-**
1. asset management	-	-
2. distribution of securities	-	-
3. third-party services and products	-	-

2.3 Fee and commission expense: breakdown

	2018	2017
A) guarantees received	1	31
B) credit derivatives	-	-
C) management and brokerage services:	712	612
1. trading in financial instruments	61	60
2. foreign currency transactions	-	-
3. asset management	-	-
3.1 own portfolio	-	-
3.2 third party portfolios	-	-
4. securities custody and administration	-	17
5. placement of financial instruments		-
6. off-premises distribution of securities, products and services	651	535
D) collection and payment services	162	148
E) other services	1,493	1,589
Total	**2,368**	**2,380**

SECTION 3 - DIVIDENDS AND SIMILAR INCOME - ITEM 70

3.1 Dividends and similar income: breakdown

		2018		2017	
		dividends	similar income	dividends	similar income
A.	Financial assets held for trading	-	-	-	-
B.	Other financial assets mandatorily measured at fair value through profit or loss	-	-	-	-
C.	Financial assets measured at fair value through other comprehensive income	227	-	227	-
D.	Equity investments	-	-	-	-
	TOTAL	**227**	**-**	**227**	**-**

SECTION 4 - NET TRADING EXPENSE - ITEM 80

4.1 Net trading expense: breakdown

	Gains (A)	Trading income (B)	Losses (C)	Trading losses (D)	Net trading expense [(A+B) - (C+D)]
1. Financial assets held for trading	**-**	**77**	**-**	**(202)**	**(125)**
1.1 Debt instruments	-	30	-	(202)	**(172)**
1.2 Equity instruments	-	47	-	-	47
1.3 OEIC units	-	-	-	-	-
1.4 Financing	-	-	-	-	-
1.5 Other	-	-	-	-	-
2. Financial liabilities held for trading	**-**	**-**	**-**	**-**	**-**
2.1 Debt instruments	-	-	-	-	-
2.2 Payables	-	-	-	-	-
2.3 Other	-	-	-		-
3. Financial assets and liabilities: exchange rate losses	**X**	**X**	**X**	**X**	**-**
4. Derivatives	**-**	**-**	**-**	**-**	**-**
4.1 Financial derivatives:	-	-	-	-	-
On debt instruments and interest rates	-	-	-	-	-
On equity instruments and equity indexes	-	-	-	-	-
On currencies and gold	X	X	X	X	-
Other	-	-	-	-	-
4.2 Credit derivatives	-	-	-	-	-
of which: natural hedges connected to the fair value option	X	X	X	X	-
TOTAL	**-**	**77**	**-**	**(202)**	**(125)**

SECTION 6 - GAIN FROM SALES OR REPURCHASES - ITEM 100

6.1 Gain from sales or repurchases: breakdown

	2018			2017		
	Gain	Loss	Net gain	Gain	Loss	Net gain
A. Financial assets	**-**	**-**	**-**	**-**	**-**	**-**
1. Financial assets measured at amortised cost:	-	-	-	-	-	-
1.1 Loans and receivables with banks	-	-	-	-	-	-
1.2 Loans and receivables with customers	-	-	-	-	-	-
2. Financial assets measured at fair value through other comprehensive income	1,545	(378)	1,167	1,071	(140)	931
2.1 Debt instruments	1,545	(378)	1,167	1,071	(140)	931
2.2 Financing	-	-	-	-	-	-
TOTAL ASSETS (A)	**1,545**	**(378)**	**1,167**	**1,071**	**(140)**	**931**
B. Financial liabilities measured at amortised cost	**-**	**-**	**-**	**-**	**-**	**-**
1. Due to banks	-	-	-	-	-	-
2. Due to customers	-	-	-	-	-	-
3. Securities issued	-	-	-	-	-	-
TOTAL LIABILITIES (B)	**-**	**-**	**-**	**-**	**-**	**-**

SECTION 8 - NET IMPAIRMENT LOSSES DUE TO CREDIT RISK - ITEM 130

8.1 Net impairment losses due to credit risk related to financial assets measured at amortised cost: breakdown

	Impairment losses (1)			Impairment gains (2)		2018	2017
	First and second stage	Third stage		First and second stage	Third stage		
		write-offs	Other				
A. Loans and receivables with banks	**-**	**-**	**-**	**-**	**-**	**-**	**-**
- Financing	-	-	-	-	-	-	-
- Debt instruments	-	-	-	-	-	-	-
of which: purchased or originated credit-impaired loans and receivables	-	-	-	-	-	-	-
B. Loans and receivables with customers:	**1,915**	**-**	**6,176**	**(1,279)**	**-**	**6,812**	**5,352**
- Financing	1,858	-	6,176	(1,279)	-	6,755	5,352
- Debt instruments	57	-	-	-	-	57	-
of which: purchased or originated credit-impaired loans and receivables	-	-	-	-	-	-	-
Total	**1,915**	**-**	**6,176**	**(1,279)**	**-**	**6,812**	**5,352**

8.2 Net impairment losses due to credit risk related to financial assets measured at fair value through other comprehensive income: breakdown

	Impairment losses (1)			Impairment gains (2)		2018	2017
	First and second stage	Third stage		First and second stage	Third stage		
		write-offs	Other				
A. Debt instruments	**2**	**-**	**-**	**-**	**-**	**2**	**-**
B. Financing	**-**	-	-	-	-	**-**	-
- To customers	-	-	-	-	-	-	-
- To banks	-	-	-	-	-	-	-
of which: purchased or originated credit-impaired financial assets	-	-	-	-	-	-	-
Total	**2**	-	-	-	-	**2**	-

SECTION 10 - ADMINISTRATIVE EXPENSES - ITEM 160

10.1 Personnel expense: breakdown

	2018	2017
1) Employees	18,206	16,225
a) wages and salaries	10,957	10,020
b) social security charges	2,741	2,630
c) post-employment benefits	-	-
d) pension costs	-	-
e) accrual for post-employment benefits	676	613
f) accrual for pension and similar provisions:	-	-
- defined contribution plans	-	-
- defined benefit plans	-	-
g) payments to external supplementary pension funds:	307	329
- defined contribution plans	307	329
- defined benefit plans	-	-
h) costs of share-based payment plans	-	-
i) other employee benefits	3,525	2,633
2) Other personnel	413	330
3) Directors and statutory auditors	975	793
4) Retired personnel	-	-
5) Recovery of costs for employees of the Bank seconded to other entities	-	-
6) Reimbursement of costs for employees of other entities seconded to the Bank	217	201
TOTAL	**19,811**	**17,549**

10.2 Average number of employees by category

Personnel:

a) Senior managers:	21
b) Managers :	41
c) Remaining employees:	120

10.5 Other administrative expenses: breakdown

	2018	2017
IT expenses	4,372	4,354
Consultancy	3,696	3,150
Servicing and collection activities	2,736	3,063
Rent and related fees	2,195	1,963
Indirect taxes and duties	2,010	1,658
Resolution Fund	942	807
Car hire and related fees	858	863
Expense reimbursement and entertainment	726	697
Advertising	568	284
Expenses related to management of the SPVs	536	462
Insurance	385	349
Other	352	412
Audit fees	295	265
Membership fees	265	262
Infoprovider expenses	255	278
Maintenance of movables and real properties	235	112
Telephone and postage expenses	175	177
Stationery and printing	96	99
Discretionary payments	13	4
Total	**20,710**	**19,259**

IT expenses, which represent the most significant cost, remained in line with the previous year despite the increase in business.

The increase in consulting expenses is mainly due to the costs incurred in 2018 for the assignment of the rating and admission to listing of the securities of the Quinto Sistema Sec. 2017 securitisation, which also included the merger of the previous Quinto Sistema Sec. 2016 securitisation into it.

The increase in indirect taxes and duties is mainly due to the increase in contributions paid for the enforceable injunctions deposited with public administration.

Contributions to the Resolution Fund, up again versus the previous year, amounted to € 942 thousand.

SECTION 11 - NET ACCRUALS TO PROVISIONS FOR RISKS AND CHARGES - ITEM 170

11.3 Net accruals to other provisions for risks and charges: breakdown

	2018	2017
Provisions for risks and charges - other provisions and risks	(414)	(223)
Release of provisions for risks and charges	-	215
TOTAL	**(414)**	**(8)**

SECTION 12 - NET IMPAIRMENT LOSSES ON PROPERTY AND EQUIPMENT - ITEM 180

12.1 Net impairment losses on property and equipment: breakdown

	Depreciation (a)	Impairment losses (b)	Impairment gains (c)	**Carrying amount (a + b - c)**
A. Property and equipment				
A.1 Owned	401	-	-	401
▪ Operating assets	401	-	-	401
▪ Investment property	-	-	-	-
▪ Inventories	X	-	-	-
A.2 Acquired under finance lease	-	-	-	-
▪ Operating assets	-	-	-	-
▪ Investment property	-	-	-	-
TOTAL	**401**	**-**	**-**	**401**

SECTION 13 - NET IMPAIRMENT LOSSES ON INTANGIBLE ASSETS - ITEM 190

13.1 Net impairment losses on intangible assets: breakdown

	Amortisation (a)	Impairment losses (b)	Impairment gains (c)	**Carrying amount (a + b - c)**
A. Intangible assets				
A.1 Owned	3	-	-	3
▪ Developed internally	-	-	-	-
▪ Other	3	-	-	3
A.2 Acquired under finance lease	-	-	-	-
TOTAL	**3**	-	-	**3**

SECTION 14 - OTHER OPERATING EXPENSE - ITEM 200

14.1 Other operating expense: breakdown

	2018	2017
Amortisation of leasehold improvements	80	207
Other operating expense	735	515
TOTAL	**815**	**722**

14.2 Other operating income: breakdown

	2018	2017
Recoveries of expenses on current accounts and deposits for sundry taxes	265	231
Recoveries of sundry expenses	11	25
Other income	120	53
TOTAL	**396**	**309**

"Recoveries of expenses on current accounts and deposits for sundry taxes" include the amounts recovered from customers for the substitute tax on medium and long-term loans and for the stamp duty on current account and security statements of account.

SECTION 19 - INCOME TAXES - ITEM 270

19.1 Income taxes: breakdown

		2018	2017
1.	Current taxes (-)	(12,531)	(8,836)
2.	Changes in current taxes from previous years (+/-)	(223)	101
3.	Decrease in current taxes for the year (+)	-	-
3.bis	Decrease in current taxes for the year due to tax assets pursuant to Law no. 214/2011 (+)	-	-
4.	Changes in deferred tax assets (+/-)	518	(804)
5.	Changes in deferred tax liabilities (+/-)	(2,393)	(2,668)
6.	Tax expense for the year (-) (-1+/-2+3+/-4+/-5)	(14,629)	(12,207)

19.2 Reconciliation between theoretical and effective tax expense

IRES (CORPORATE INCOME TAX)	Taxable income	IRES (Corporate income tax)	%
Theoretical IRES expense	**42,700**	**(11,742)**	**27.50%**
Permanent increases	1,631	(448)	1.05%
Temporary increases	17,435	(4,795)	11.23%
Permanent decreases	(3,378)	929	-2.18%
Temporary decreases	(24,492)	6,735	-15.77%
Effective IRES expense	**33,896**	**(9,321)**	**21.83%**
IRAP (REGIONAL BUSINESS TAX)	Taxable income	IRAP (Regional business tax)	%
Theoretical IRAP expense	**42,700**	**(2,378)**	**5.57%**
Permanent increases	49,173	(2,739)	6.41%
Temporary increases	1,945	(108)	0.25%
Permanent decreases	(35,207)	1,961	-4.59%
Temporary decreases	974	54	0.13%
Effective IRAP expense	**57,637**	**(3,210)**	**7.52%**
▪ Other tax expense			
Total effective IRES and IRAP expense	**91,533**	**(12,531)**	**29.35%**

SECTION 21 - OTHER INFORMATION

Nothing to report.

SECTION 22 - EARNINGS PER SHARE

Earnings per share (EPS)	2018
Profit for the year (thousands of Euro)	28,071
Average number of outstanding shares	80,345,506
Basic earnings per share (in Euro)	0.349
Diluted earnings per share (in Euro)	0.349

EPS is calculated by dividing the profit attributable to holders of ordinary shares of Banca Sistema (numerator) by the weighted average number of ordinary shares (denominator) outstanding during the year.

PART D - OTHER COMPREHENSIVE INCOME

Breakdown of comprehensive income

		2018	2017
10.	**Profit for the year**	**28,070**	**27,560**
	Items, net of tax, that will not be reclassified subsequently to profit or loss	-	-
20.	Equity instruments designated at fair value through other comprehensive income:	-	-
	a) fair value gains (losses)	-	-
	b) transfers to other equity items	-	-
30.	Financial liabilities designated at fair value through profit or loss (changes in own credit rating):	-	-
	a) fair value gains (losses)	-	-
	b) transfers to other equity items	-	-
40.	Hedging of equity instruments designated at fair value through other comprehensive income:	-	-
	a) fair value gains (losses) - hedged item	-	-
	b) fair value gains (losses) - hedging instrument	-	-
50.	Property and equipment	-	-
60.	Intangible assets	-	-
70.	Defined benefit plans	39	(56)
80.	Non-current assets held for sale	-	-
90.	Share of valuation reserves of equity-accounted investments:	-	-
100.	Income taxes on items that will not be reclassified subsequently to profit or loss	-	-
	Items, net of tax, that will be reclassified subsequently to profit or loss	-	-
110.	Hedges of foreign investments:	-	-
	a) fair value gains (losses)	-	-
	b) reclassification to profit or loss	-	-
	c) other changes	-	-
120.	Exchange rate gains (losses):	-	-
	a) fair value gains (losses)	-	-
	b) reclassification to profit or loss	-	-
	c) other changes	-	-
130.	Cash flow hedges:	-	-
	a) fair value gains (losses)	-	-
	b) reclassification to profit or loss	-	-
	c) other changes	-	-
	of which: net position gains (losses)	-	-
140.	Hedging instruments (non-designated elements):	-	-
	a) fair value gains (losses)	-	-
	b) reclassification to profit or loss	-	-
	c) other changes	-	-

	2018	2017
150. Financial assets (other than equity instruments) measured at fair value through other comprehensive income:	(2,064)	(95)
a) fair value gains (losses)	(1,001)	174
b) reclassification to profit or loss	-	-
- impairment losses due to credit risk	49	-
- losses on sales	(585)	(268)
c) other changes	(527)	-
160. Non-current assets held for sale and disposal groups:	-	-
a) fair value gains (losses)	-	-
b) reclassification to profit or loss	-	-
c) other changes	-	-
170. Share of valuation reserves of equity-accounted investments:	-	-
a) fair value gains (losses)	-	-
b) reclassification to profit or loss	-	-
- impairment losses	-	-
- gains/losses on sales	-	-
c) other changes	-	-
180. Income taxes on items that will be reclassified subsequently to profit or loss	-	-
190. Total other comprehensive expense	**(2,025)**	**(151)**
200. Comprehensive income (10+190)	**26,045**	**27,409**

SECTION 1 - CREDIT RISK

QUALITATIVE DISCLOSURE

In order to manage the significant risks to which it is or could be exposed, Banca Sistema has set up a risk management system that reflects the characteristics, size and complexity of its operations.

In particular, this system hinges on four core principles:

- suitable supervision by relevant bank bodies and departments;
- satisfactory risk management policies and procedures;
- suitable methods and instruments to identify, monitor and manage risks, with suitable measuring techniques; thorough internal controls and independent reviews.

In order to reinforce its ability to manage corporate risks, the Bank established the Risk and ALM Committee - a committee independent of the Board of Directors, which supports the CEO in defining strategies, risk policies and profitability targets.

The Risk Committee continuously monitors the relevant risks and any new or potential risks arising from changes in the working environment or forward-looking operations.

With reference to the new regulation in matters of the operation of the internal control system, in accordance with the principle of collaboration between the control functions, the Internal Control and Risk Management Committee (a Board committee) was assigned the role of coordinating all the control functions.

The methods used to measure, assess and aggregate risks are approved by the Board of Directors, based on proposals from the Risk Department, subject to approval by the Risk Committee. In order to measure “Pillar 1 risks”, the Bank has adopted standard methods to calculate the capital requirements for Prudential Regulatory purposes. In order to evaluate non-measurable “Pillar 2 risks”, the Bank adopts - where possible - the methods stipulated under Supervisory regulations or those established by trade associations. If there are no such indications, standard market practices by operators working at a level of complexity and with operations comparable to those of the Bank are assessed.

With reference to the new provisions in matters of regulatory supervision (15th update of circular no. 263 - New regulations for the prudential supervision of banks), a series of obligations on risk management and control, including the Risk Appetite Framework (RAF) and the regulatory instructions defined by the Basel Committee were introduced. The Bank has tied the strategic objectives to the RAF. The key ratios and the respective levels were assessed and any revisions needed were made while defining the bank's annual objectives.

In particular, the RAF was designed with key objectives to verify that over time, the business grows and develops observing capital strength and liquidity obligations, implementing monitoring and alert mechanisms and related series of actions that allow prompt intervention in case of significant discrepancies.

The structure of the RAF is based on specific indicators so-called Key Risk Indicators (KRI) which measure the Bank's solvency in the following areas:

- Share capital;
- Liquidity;
- Quality of the loans and receivables portfolio;
- Profitability;
- Other specific risks the Bank is exposed to.

Target levels, consistent with the plan's defined values, the level I thresholds, defined as “warning” thresholds, that trigger discussion at Risk Management Committee level and subsequent communication to the Board of Directors and the level II thresholds, that require direct discussion in the Board of Director's meeting to determine the actions to be taken are associated with the various key indicators.

The level I and II thresholds are defined with scenarios of potential stress with respect to the plan's objectives and on dimensions having a clear impact for Banca Sistema.

Starting from 1 January 2014, the Bank used an integrated reference framework both to identify its own risk appetite and for the internal process entailing the determination of the capital adequacy (Internal Capital

Adequacy Assessment Process - ICAAP).

Furthermore, the Internal Capital Adequacy Assessment Process allows the Bank to comply with the public disclosure obligation, with appropriate tables, concerning its capital adequacy, risk exposure and the general characteristics of the management, control, and monitoring systems of the risks themselves (the so-called “third pillar”). As concerns this matter, the Bank fulfils the public disclosure requirements with the issuing of Circular no. 285 of 17 December 2013 “Prudential supervisory provisions for banks” in which the Bank of Italy transposed Directive 2013/36/EU (CRD IV) of 26 June 2013. This regulation, together with that contained in (EU) Regulation no. 575/2013 (the so-called “CRR”) incorporates the standards defined by the Basel Committee on Banking Supervision (the so-called “Basel III”).

1. General aspects

The prudential supervisory provisions, provide for the banks the possibility to determine the weighting coefficients for the calculation of the capital requirement with respect to credit exposure within the standardised approach based on the creditworthiness ratings issued by External Credit Assessment Institutions (ECAI) of the Bank of Italy.

Banca Sistema, as at 31 December 2018, uses the appraisal issued by the ECAI “DBRS”, for the exposures to Central Authorities, and Public Sector Institutions and Entities, whereas, as concerns the valuations related to the regulatory business segment, it uses the agency “Fitch Ratings Ltd”.

The identification of a reference ECAI does not represent in any way, in subject matter or in purposes, an assessment on the merit of the opinions made by the ECAI or a support of the methodologies used, for which the External Credit Assessment Institutions remain solely responsible.

The assessments issued by the rating agencies do not exhaust the creditworthiness assessment process that the Bank performs with regard to its customers; rather they represent a further contribution to define the information framework regarding the credit quality of the customer.

The satisfactory appraisal of the borrower’s creditworthiness, with regards to capital and income, and of the correct remuneration of the risk, are made based on documentation acquired by the Bank; the information acquired from the Bank of Italy Central Credit Bureau and from other infoproviders, both when decisions are made and during the subsequent monitoring, complete the informational framework.

For Banca Sistema, Credit risk is one of the Group’s main components of overall exposure; the composition of the credit portfolio predominantly consists of National Institutions of the Public Administration, such as local health authorities / Hospitals, Territorial entities (Regions, Provinces and Municipalities) and Ministries that, by definition, entail a very limited default risk.

The main components of Banca Sistema’s operations that generate credit risk are:

- Factoring activities (with and without recourse);
- Loans to SMEs (with guarantee from the National Guarantee Fund - FNG);
- Acquisition without recourse of salary-/pension-backed loans;
- Collateralised Lending (mainly secured by gold).

2. Credit Risk Management Policies

2.1 Organisational aspects

Banca Sistema’s organisational model provides that the preliminary credit assessment procedure be performed carefully in accordance with the decision-making powers reserved to the decision-making bodies.

In order to maintain high credit quality in its loan portfolio, the Bank, as the Parent, deemed it expedient to concentrate all phases related to the assumption and control of risk upon its internal structures, thus obtaining, through the specialisation of resources and the segregation of duties at each decision-making level, a degree of standardisation in the granting of credit and robust monitoring of the individual positions.

In light of the above, the Bank’s Underwriting Department, which reports to the Central Credit Department, performs the analyses for the granting of credit. The Department performs assessments focused on the separate analysis and extension of credit to counterparties (assignor, debtor) and on managing the related financial transactions. This takes place in all normal phases of the credit process, summarised as follows:

- "analysis and assessment": the gathering of quantitative and qualitative information from the counterparties under examination and within the system allows an opinion of the party's reliability to be obtained and is helpful in quantifying the proposed line of credit;
- "deliberation and formalisation": once the proposal has been deliberated upon, the contractual documentation to be signed by the counterparty is prepared;
- "monitoring the relationship": the continuous control of the counterparties benefiting from the credit allows any anomalies to be identified and consequentially prompt intervention.

Credit risk is mainly generated as a direct result of the definitive acquisition of credit from the customer company versus the insolvency of the assigned debtor. In particular, the credit risk generated by the factoring portfolio essentially consists of public entities.

With regard to each credit acquired, Banca Sistema performs, via the Out-of-Court Collection and Legal Collection Departments, both of which report to the Central Credit Department, activities described further on in order to verify the credit status, and whether or not there are any impediments to the payment of the invoices to be assigned, and the date scheduled for the payment thereof. Specifically, the structure endeavours:

- to verify that each credit is certain, liquid and collectable, i.e. there are no disputes or complaints and that there is no further request for clarification or information with regard to said credit and should there be any, that said requests are promptly satisfied;
- to verify that the debtor has received and recognised in its system the related deed of assignment, i.e. it is aware that the credit has been assigned to Banca Sistema;
- to verify that the debtor, where provided for by the assignment agreement and by the purchase offer, has formalised its acceptance of the assignment of the related credit or has not rejected it in accordance with law;
- to verify that the debtor has received all the documentation required to proceed with the payment (copy of invoice, orders, bills, transportation documents, etc.) and that it has recognised the corresponding debt in its system (existence of the credit);
- to verify c/o the local and/or regional institutions: the existence of specific allocations, available cash;
- to verify the payment status of the credits via meetings c/o the Public Administrations and/or debtor agencies, telephone contacts, emails, etc. in order to facilitate the ascertainment and the removal of any obstacles that could delay and/or impede payment.

With regard to the SME Loans product, beginning in February 2017, it was decided to exit this segment of the market as well as the run-off of prior exposures in the portfolio. On this basis, credit risk is associated with the inability of the two counterparties involved in the loan to honour their financial commitments, i.e.:

- the debtor (SME);
- the Guarantee Fund (the Government of Italy).

The type of loan follows the usual operating process concerning the preliminary assessment, the disbursement and the monitoring of the credit.

In particular, two separate due-diligence procedures are performed on this type of loan (one by the Bank and the other by Medio Credito Centrale, the so-called MCC) on the borrower of funds.

The debtor's insolvency risk is mitigated by direct (i.e. that referring to an individual exposure), explicit, unconditional and irrevocable guarantee by the Guarantee Fund, the sole Manager of which is "MCC".

As regards, instead, the acquisition of salary-/pension-backed loan portfolios, the credit risk is associated with the inability of the three counterparties involved in the loan process to honour their financial commitments, i.e.:

- the employer (ATC);
- the financial assigning company;
- the insurance company.

The insolvency risk of the employer (ATC) / debtor is generated in the following cases:

- default of employer (e.g.: bankruptcy);
- the debtor losing his job (e.g.: resignation/ dismissal of the debtor) or reduction of remuneration (e.g.:

redundancy fund);

- death of the debtor.

The risks described above are mitigated by the mandatory subscription of life and employment insurance policies. In detail:

- the employment risk policy fully covers any insolvency deriving from the reduction of the debtor's remuneration whereas, in case of default by the employer, the coverage is limited to the portion of the residual debt in excess of the post-employment benefits accrued;
- the life risk policy provides that the insurance company will intervene to cover the portion of the residual debt expiring subsequent to death; any instalments previously not settled remain instead incumbent upon by the heirs.

The Bank is subject to the insolvency risk of the insurance company in the event that a claim is made upon a loan. In order to mitigate this risk, the Bank requires that the outstanding credit portfolio be insured by several insurance companies observing the following terms:

- an individual company with no rating or with rating lower than Investment Grade may insure a maximum of 30% of the cases;
- an individual company of Investment Grade may insure a maximum of 40% of the cases.

The employer insolvency risk is generated in the event that a case is retroceded back to the employee, which must therefore, repay the credit to the Bank. The Framework Agreement initialled with the employer provides for the possibility of returning the credit in the cases of fraud on the part of the employer/debtor or in any case, of non-observance, on the part of the employer, of the criteria underwritten in the Framework Agreement.

As concerns the financial instruments held on its own account, the Bank performs security purchase transactions regarding Italian government debt, which are allocated based on the investment strategy, to the HTC, HTCS and HTS portfolios.

With reference to aforementioned transactions the Bank identified and selected specific IT applications to manage and monitor the treasury limits on the securities portfolio and to set up the second level controls.

The Treasury Department, operating within the limits allowed by the Board of Directors, conducts said transactions.

2.2 Management, measurement and control systems

The Bank sets effective Credit Risk Management as a strategic objective via instruments and processes integrated to ensure a correct credit management in all phases (processing, disbursement, monitoring and management, intervening on loans with credit quality problems).

By involving the various central structures of Banca Sistema and through the specialisation of the resources and the segregation of duties at each decision-making level, it seeks to guarantee a high degree of efficiency and standardisation in overseeing credit risk and monitoring the individual positions.

With specific reference to the monitoring of credit activities, the Bank, via the collection meetings, assesses and inspects the credit portfolio based upon the guidelines defined within the "collection policy".

The framework related to the above credit risk ex-post monitoring sets the objective of promptly identifying any anomalies and/or discontinuities and evaluating the persistence of risk profiles, in-line with the strategic indications provided.

The purchase activities of government securities classified among HTCS financial assets (formerly classified as available-for-sale) continued during 2018 in relation to the credit risk associated with the bond securities portfolios. Said financial assets, which in virtue of their classification fall within the perimeter of the "banking book" although outside of the bank's traditional investment activity, are sources of credit risk. This risk consists in the issuer's inability to redeem, upon maturity, all or part of the bonds subscribed.

The securities held by Banca Sistema consist exclusively of Italian government securities, with an average duration of less than two years for the overall portfolio.

Furthermore, the formation of a portfolio of highly liquid assets is also expedient for anticipating the trend of the prudential regulations in relation to the governance and management of liquidity risk.

As concerns counterparty risk, Banca Sistema's operations call for extremely prudent reverse repurchase and repurchase agreements being that Italian government securities are the predominant underlying instrument and the Compensation and Guarantee Fund is the predominant counterparty.

2.3 Methods of measuring expected losses

The general approach defined by IFRS 9 for estimating impairment is based on a process aimed at giving evidence of the deterioration of a financial instrument's credit quality from the date of initial recognition to the reporting date. The regulatory guidance on assigning loans and receivables to the various stages under the Standard ("staging" or "stage allocation") calls for the identification of significant changes in credit risk based on the changes in a counterparty's creditworthiness since initial recognition, the expected life of the financial asset and other forward-looking information that may affect credit risk.

Consistently with the provisions of IFRS 9, performing loans are therefore divided into two categories:

- Stage 1: this bucket contains assets that do not show signs of significant deterioration in credit quality. For this stage the expected one-year credit loss is calculated on a collective basis;
- Stage 2: this bucket contains assets that show signs of significant deterioration in credit quality from the date of initial recognition to the reporting date. The expected loss for this bucket must be calculated on a lifetime basis, i.e. over the entire duration of the instrument, on a collective basis.

2.4 Credit Risk mitigation techniques

It should be noted that, at the reporting date, the Bank did not implement any hedging of the credit portfolio.

As concerns credit and counterparty risk on the securities portfolio and on the repurchase agreements, risk mitigation is pursued by a careful management of the operational autonomy, establishing limits in terms of both responsibility and consistency and composition of the portfolio by type of securities.

3. Impaired loans

Banca Sistema defined its credit quality policy based on the provisions in the Bank of Italy Circular no. 272 (Accounts matrix), the main definitions of which are provided on the following pages.

The Supervisory Provisions for Banks assign to intermediaries specific obligations concerning the monitoring and classification of loans: "The obligations of the operating units in the monitoring phase of the loan granted must be deducible from the internal regulation. In particular, the terms and methods of action must be set in the event of anomalies. The criteria for measurement, management and classification of irregular loans, as well as the related responsible units, must be set through a resolution by the Board of Directors in which the methods for connecting these criteria with those required for the supervisory reports are indicated. The Board of Directors must be regularly informed on the performance of the irregular loans and the related recovery procedures".

According to the definitions in the above-mentioned Bank of Italy Circular, "impaired" financial assets are defined as those that lie within the "bad exposures", "unlikely to pay" or "past due and/or overdrawn exposures" categories.

Exposures whose anomalous situation is attributable to factors related to "country risk" are not included in "impaired" financial assets.

In particular, the following definitions apply:

Bad exposures

On- and off-statement of financial position exposures (loans, securities, derivatives, etc.) owed by a party in state of insolvency (even if not judicially ascertained) or in broadly similar situations, regardless of any loss forecast formulated by the Bank (cf. Art. 5 bankruptcy law). The definition therefore applies regardless of the existence of any collateral (real or private) provided as protection against the exposures.

This class also includes:

- the exposure to local institutions (municipalities and provinces) in state of financial difficulty for the portion subject to the applicable liquidation procedure;
- receivables acquired from third parties in which the main debtors are non-performing, regardless of the portfolio's accounting allocation.

Unlikely to pay

The classification in this category is first and foremost based on the Bank's judgement regarding the unlikelihood that, without having to resort to actions such as enforcing the guarantees, the debtor will completely (with regard to principal and/or interest) fulfil its credit obligations. This assessment is made independently of whether any sums (or instalments) are past due and not paid. It is therefore unnecessary to wait for explicit symptoms of irregularity (non-repayment) if there are elements that entail a situation of default risk on the part of the debtor (e.g. a crisis in the industrial sector in which the debtor operates). The set of on- and off-statement of financial position exposures to the same debtor in the above conditions is named "unlikely to pay", save that the conditions for classifying the debtor under bad exposures do not exist. The exposures to retail parties may be classified in the unlikely to pay category at the level of the individual transaction, provided that the Bank has assessed that the conditions for classifying the set of exposures to the same debtor in that category do not exist.

Past due and/or overdrawn exposures

These are understood to be the on-statement of financial position exposures at carrying amount and off-statement of financial position exposures (loans, securities, derivatives, etc.), other than those classified as bad exposures, unlikely to pay, that, on the reference date of the report, are past due or have been overdrawn by more than 90 days. In order to verify the continuity of the past due exposure in connection with factoring transactions, the following should be noted:

- for "with recourse" transactions, a past due exposure, other than one associated with the assignment of future receivables, becomes such only if both of the following conditions exist:
  - the amount of the advance is equal to, or greater than the total amount of receivables that are coming due;
  - at least one invoice has not been honoured (past due) by more than 90 days and the set of the past due invoices (including those by less than 90 days) exceeds 5% of the total receivables.
- for "without recourse" transactions, reference must be made to the invoice that is furthest past due for each assigned debtor.

In the calculation of the capital requirement for the credit and counterparty risk, Banca Sistema uses the standardised approach. This envisages that the exposures that lie within the portfolios related to "Central Authorities and Central Banks", "Territorial entities", and "Public sector institutions" and "Businesses", must apply the notion of past due and/or overdrawn exposures at the level of the debtor party.

The regulation requires that the debtor's total exposure be considered past due and/or overdrawn, on the reference date of the report, any time the 5% materiality level is exceeded.

Forborne exposures

Forborne exposures are defined as exposures that fall into the category "Non-performing exposures with forbearance measures" and "Forborne performing exposures" as defined by the International Technical Standard (ITS).

A forbearance measure represents a concession towards a debtor which faces or is about to face difficulties in fulfilling its financial obligations ("financial difficulties"); a "concession" indicates one of the following actions:

- an amendment of the previous terms and conditions of a contract which the debtor is considered unable to fulfil due to its financial difficulties, that would not have been granted if the debtor was not in financial difficulty;
- a total or partial refinancing of a problem loan that would not have been granted if the debtor was not in financial difficulty.

Art. 172 of the EBA ITS sets some situations which, if occurring, lead in any case to the presence of forbearance measures, i.e. when:

- an amended contract was classified as non-performing and would have been so in the absence of the amendment;
- the amendment made to the contract implies a partial or total cancellation of the debt;
- the intermediary approves the use of forbearance clauses incorporated in the contract for a debtor classified as non-performing or that would have been so without resorting to these clauses;
- at the same time or close to the additional granting of credit by the intermediary, the debtor makes payments

of principal or interest on another contract with the intermediary that was classified as non-performing or that would have been classified so in the absence of the refinancing.

According to these criteria, forbearance is presumed to have taken place when:

- the amended contract has totally or partially expired for more than 30 days (without being classified as non-performing) at least once during the three months before the amendment or it would have been so in the absence of the amendment;
- at the same time or near the time additional credit is granted by the intermediary, the debtor makes principal or interest payments on another contract with the intermediary that was classified as totally or partially past due by more than 30 days (without it being classified as non-performing) at least once during the three months previous to the amendment or it would have been had the amendment not been made;
- the intermediary approves the use of forbearance clauses incorporated in the contract for a debtor which has expired for more than 30 days or that would have been so without resorting to these clauses.

3.1 Management strategies and policies

The current regulatory framework requires impaired financial assets to be classified according to their criticality. More specifically, there are three categories: "bad exposures", "unlikely to pay" and "past due and/or overdrawn exposures".

- Bad exposures: exposures owed by a party in state of insolvency (even if not judicially ascertained) or in broadly similar situations, regardless of the loss forecasts formulated by the intermediary.
- Unlikely to pay: exposures for which the intermediary considers it unlikely that the debtor will fully meet its obligations without having to resort to actions such as the enforcement of guarantees, regardless of whether there are any past due and/or overdrawn amounts.
- Past due and/or overdrawn exposures: exposures, other than those classified as bad exposures or unlikely to pay, which have been continuously past due and/or overdrawn for more than 90 days.

Forborne exposures, which refer to exposures that are subject to renegotiation and/or refinancing due to the customer's financial difficulties (whether evident or developing), are also classified. These exposures may constitute a subset of non-performing loans (non-performing exposures with forbearance measures) and performing loans (forborne performing exposures). The management of these exposures, in compliance with the regulatory provisions regarding timing and classification methods, is supported by specific work processes and IT tools.

The Group has a policy that establishes criteria and methods for recognising impairment losses by standardising the rules that, depending on the type of non-performing loan and its original technical form, define the methods and processes used to determine expected losses. The management of non-performing exposures is assigned to a specific organisational unit, the Central Credit Department, which is responsible for identifying strategies for maximising collection on individual positions and establishing the impairment losses to be recognised for those positions through a formalised process.

The expected loss reflects a number of elements derived from various internal and external assessments of the financial condition of the main debtor and any guarantors. Expected losses are continuously monitored and compared to the changes in each position. The Risk Department oversees the collection of non-performing loans.

In order to maximise collections, the relevant departments identify the best strategy for managing non-performing exposures, which, based on the subjective characteristics of the individual counterparty/exposure and internal policies, may include amending the contractual terms (forbearance), establishing the methods for loan collection, or assigning the credit to third parties (either for individual exposures or for a group of positions with similar characteristics).

3.2 Write-offs

Non-performing exposures for which collection is not possible (whether in full or in part) are written off from the accounting records in compliance with the policies in force at the time and subject to approval by the Bank's Board of Directors.

3.3 Purchased or originated credit-impaired financial assets

In accordance with “IFRS 9 - Financial Instruments”, in some cases a financial asset is considered impaired at initial recognition because the credit risk is very high, and in the case of a purchase, it is acquired at a significant discount (compared to the original 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 among assets measured at amortised cost or at fair value through other comprehensive income, they are classified as "Purchased or Originated Credit-Impaired" (in short "POCI") and are subject to specific treatment. More specifically, impairment losses equal to the lifetime expected credit loss (ECL) are recognised from the date of initial recognition over the asset’s entire life. In light of the above, POCI financial assets are initially recognised in stage 3, although they may be subsequently reclassified to performing loans, in which case an expected loss equal to the lifetime ECL (stage 2) will continue to be recognised. A POCI financial asset is therefore classified as such in the expected credit loss (ECL) reporting and calculation processes.

4. Financial assets subject to commercial renegotiation and forborne exposures

In the event the debtor is experiencing financial difficulties, the contractual terms of the exposures may be amended in favour of the debtor in order to make repayment financially sustainable. Depending on the subjective characteristics of the exposure and the reasons behind the debtor's financial difficulties, the amendments may be short term (temporary suspension of the payment of the principal of a loan or extension of a maturity) or long term (extension of the duration of a loan, adjustment of the interest rate) and result in the exposure (both performing and non-performing) being classified as “forborne”. “Forborne” exposures are subject to specific provisions for classification in accordance with EBA ITS 2013-35, as transposed in the Group's credit policies. If the lending measures are applied to performing exposures, these are included in the group of stage 2 exposures. All exposures classified as “forborne” are included in specific monitoring processes by the relevant departments.

QUANTITATIVE DISCLOSURE

A. CREDIT QUALITY

A.1 Impaired and unimpaired loans: carrying amounts, impairment losses, performance and business breakdown

A.1.1 Breakdown of financial assets by portfolio and by credit quality (carrying amounts)

	Bad exposures	Unlikely to pay	Impaired past due exposures	Unimpaired past due exposures	Other unimpaired exposures	Total
1. Financial assets measured at amortised cost	39,017	77,912	79,066	265,500	2,340,318	2,801,813
2. Financial assets measured at fair value through other comprehensive income	-	-	-	-	298,292	298,292
3. Financial assets designated at fair value through profit or loss	-	-	-	-	-	-
4. Other financial assets mandatorily measured at fair value through profit or loss	-	-	-	-	-	-
5. Financial assets held for sale	-	-	-	-	-	-
Total at 31.12.2018	**39,017**	**77,912**	**79,066**	**265,500**	**2,638,610**	**3,100,105**
Total at 31.12.2017	**32,340**	**15,445**	**73,251**	**331,052**	**1,807,864**	**2,259,952**

A.1.2 Breakdown of financial assets by portfolio and by credit quality (gross amount and carrying amount)

	Impaired assets				Unimpaired assets			
	Gross amount	Total impairment losses	Net exposure	Overall partial write-offs (*)	Gross amount	Total impairment losses	Net exposure	Total (carrying amount)
1. Financial assets measured at amortised cost	225,163	29,169	195,994	-	2,612,185	6,366	2,605,819	2,801,813
2. Financial assets measured at fair value through other comprehensive income	-	-	-	-	298,341	49	298,292	298,292
3. Financial assets designated at fair value through profit or loss	-	-	-	-	X	X	-	-
4. Other financial assets mandatorily measured at fair value through profit or loss	-	-	-	-	X	X	-	-
5. Financial assets held for sale	-	-	-	-	-	-	-	-
Total at 31.12.2018	**225,163**	**29,169**	**195,994**	**-**	**2,910,526**	**6,415**	**2,904,111**	**3,100,105**
Total at 31.12.2017	**143,328**	**22,292**	**121,036**	**-**	**2,144,506**	**5,590**	**2,138,916**	**2,259,952**

A.1.3 Breakdown of financial assets by past due range (carrying amounts)

	First stage			Second stage			Third stage		
	From 1 day to 30 days	From more than 30 days to 90 days	More than 90 days	From 1 day to 30 days	From more than 30 days to 90 days	More than 90 days	From 1 day to 30 days	From more than 30 days to 90 days	More than 90 days
1. Financial assets measured at amortised cost	27,148	24,474	202,713	1,047	3,672	6,900	295	10,975	126,523
2. Financial assets measured at fair value through other comprehensive income	-	-	-	-	-	-	-	-	-
TOTAL at 31.12.2018	**27,148**	**24,474**	**202,713**	**1,047**	**3,672**	**6,900**	**295**	**10,975**	**126,523**
TOTAL at 31.12.2017	**40,196**	**80,393**	**210,462**	**-**	**-**	**-**	**934**	**3,427**	**74,940**

A.1.4 Financial assets, commitments to disburse funds and financial guarantees issued: changes in impaired positions and accruals to provisions

	Total impairment losses													Overall accruals to provisions on commitments to disburse funds and financial guarantees issued			Total
	Assets included in the first stage				Assets included in the second stage				Assets included in the third stage								
	Financial assets measured at amortised cost	Financial assets measured fair value through other comprehensive income	of which: individual impairment losses	of which: collective impairment losses	Financial assets measured at amortised cost	Financial assets measured at fair value through other comprehensive income	of which: individual impairment losses	of which: collective impairment losses	Financial assets measured at amortised cost	Financial assets measured at fair value through other comprehensive income	of which: individual impairment losses	of which: collective impairment losses	Of which: purchased or originated credit-impaired financial assets	First stage	Second stage	Third stage	
Opening balance	**5,590**	**-**	**-**	**5,590**	**-**	**-**	**-**	**-**	**22,292**	**-**	**22,292**	**-**	**571**	**-**	**-**	**-**	**27,882**
Increases in purchased or originated financial assets	53	-	20	32	-	-	-	-	164	-	164	-	216	-	-	-	217
Derecognition other than write-offs	4,133	-	3,013	1,120	5	-	-	5	26	-	26	-	-	-	-	-	4,164
Net impairment losses/gains due to credit risk (+/-)	(3,990)	49	(2,888)	(1,053)	575	-	-	575	6,687	-	6,648	40	(502)	-	-	-	3,321
Contract amendments without derecognition	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Changes in estimation method	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Write-offs	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Other changes	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Closing balance	**5,786**	**49**	**145**	**5,689**	**580**	**-**	**-**	**580**	**29,169**	**-**	**29,130**	**40**	**285**	**-**	**-**	**-**	**35,584**
Recoveries from collection on financial assets that have been written off	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Write-offs recognised directly through profit or loss	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

A.1.5 Financial assets, commitments to disburse funds and financial guarantees issued: transfers between different credit risk stages (gross amount and nominal amount)

	Gross amount / Nominal amount					
	Transfers between the first and second stage		Transfers between the second and third stage		Transfers between the first and third stage	
	From the first to the second stage	From the second to the first stage	From the second to the third stage	From the third to the second stage	From the first to the third stage	From the third to the first stage
1. Financial assets measured at amortised cost	92,292	472	4,253	861	156,920	5,909
2. Financial assets measured at fair value through other comprehensive income	-	-	-	-	-	-
3. Commitments to disburse funds and financial guarantees issued	16,661	634	145	1,952	15,286	-
TOTAL at 31.12.2018	**108,953**	**1,106**	**4,398**	**2,813**	**172,206**	**5,909**

A.1.6 On- and off-statement of financial position loans and receivables with banks: gross amounts and carrying amounts

	Gross amount		Total impairment losses and accruals to provisions	Carrying amount	Overall partial write-offs
	Impaired	Unimpaired			
A. ON-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES	-				
a) Bad exposures	-	X	-	-	-
of which: forborne exposures	-	X	-	-	-
b) Unlikely to pay	-	X	-	-	-
of which: forborne exposures	-	X	-	-	-
c) Impaired past due exposures	-	X	-	-	-
of which: forborne exposures	-	X	-	-	-
d) Unimpaired past due exposures	X	1	-	1	-
of which: forborne exposures	X	-	-	-	-
e) Other unimpaired exposures	X	56,702	9	56,693	-
of which: forborne exposures	X				
TOTAL A	-	**56,703**	**9**	**56,694**	**-**
B. OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES	-				
a) Impaired	-	X	-	-	-
b) Unimpaired	X	2,446	-	2,446	-
TOTAL B	-	**2,446**	**-**	**2,446**	**-**
TOTAL A+B	-	**59,149**	**9**	**59,140**	**-**

A.1.7 On- and off-statement of financial position loans and receivables with customers: gross amounts and carrying amounts

	Gross amount		Total impairment losses and accruals to provisions	Carrying amount	Overall partial write-offs
	Impaired	Unimpaired			
A. ON-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES					
a) Bad exposures	57,468	X	18,451	39,017	-
of which: forborne exposures		X			-
b) Unlikely to pay	87,188	X	9,277	77,912	-
of which: forborne exposures		X			-
c) Impaired past due exposures	80,508	X	1,442	79,066	-
of which: forborne exposures	1,434	X	15	1,419	-
d) Unimpaired past due exposures	X	266,322	823	265,499	-
of which: forborne exposures	X				
e) Other unimpaired exposures	X	2,587,500	5,583	2,581,917	-
of which: forborne exposures	X				
TOTAL A	**225,164**	**2,853,822**	**35,576**	**3,043,411**	**-**
B. OFF-STATEMENT OF FINANCIAL POSITION LOANS AND RECEIVABLES					
a) Impaired	17,931	X		17,931	-
b) Unimpaired	X	204,018	7	204,011	-
TOTAL B	**17,931**	**204,018**	**7**	**221,942**	**-**
TOTAL (A+B)	**243,095**	**3,057,840**	**35,583**	**3,265,353**	**-**

A.1.9 On-statement of financial position loans and receivables with customers: gross impaired positions

	Bad exposures	Unlikely to pay	Impaired past due exposures
A. Opening gross balance	**44,578**	**24,061**	**74,690**
- of which: positions transferred but not derecognised	-	-	-
B. Increases	**95,699**	**140,870**	**429,094**
B.1 transfers from performing loans	21,821	125,125	336,332
B.2 transfers from purchased or originated credit-impaired financial assets	5,007	-	709
B.3 transfers from other categories of impaired loans	32,779	15,416	6,117
B.4 contract amendments without derecognition	-	-	-
B.5 other increases	36,092	329	85,936
C. Decreases	**82,809**	**77,743**	**423,276**
C.1 transfers to performing loans	5,120	5	207,451
C.2 write-offs	3,888	-	-
C.3 collections	73,801	44,927	194,324
C.4 gains on sales	-	-	-
C.5 losses on sales	-	-	-
C.6 transfers to other categories of impaired loans	-	32,811	21,501
C.7 contract amendments without derecognition	-	-	-
C.8 other decreases	-	-	-
D. Closing gross balance	**57,468**	**87,188**	**80,508**
- of which: positions transferred but not derecognised	-	-	-

A.1.9bis On-statement of financial position loans and receivables with customers: breakdown of gross forborne exposures by credit quality

	Non-performing exposures with forbearance measures	Other forborne performing exposures
A. Opening gross balance	**-**	
- of which: positions transferred but not derecognised	**-**	
B. Increases	**1,465**	
B.1 transfers from performing exposures without forbearance measures	1,465	
B.2 transfers from forborne performing exposures	-	X
B.3 transfers from non-performing exposures with forbearance measures	X	
B.4 other increases	-	
C. Decreases	**31**	
C.1 transfers to performing exposures without forbearance measures	X	X
C.2 transfers to forborne performing exposures	-	
C.3 transfers to non-performing exposures with forbearance measures	X	
C.4 write-offs	-	
C.5 collections	31	
C.6 gains on sales	-	
C.7 losses on sales	-	
C.8 other decreases	-	
D. Closing gross balance	**1,434**	
- of which: positions transferred but not derecognised	**-**	

A.1.11 On-statement of financial position non-performing loans and receivables with customers: changes in impaired positions

	BAD EXPOSURES		UNLIKELY TO PAY		IMPAIRED PAST DUE EXPOSURES	
	Total	of which: forborne exposures	Total	of which: forborne exposures	Total	of which: forborne exposures
A. Opening total impairment losses	**12,237**		**8,616**		**1,439**	
- of which: positions transferred but not derecognised	-		-		-	
B. Increases	**11,238**		**8,252**		**3,432**	**15**
B.1 impairment losses on purchased or originated credit-impaired financial assets	164	X	-	X	-	X
B.2 other impairment losses	6,765		8,010		522	15
B.3 losses on sales	-		-		-	
B.4 transfers from other categories of impaired loans	4,119		41		2,664	
B.5 contract amendments without derecognition	-	X	-	X	-	X
B.6 other increases	190		201		246	
C. Decreases	**5,024**		**7,591**		**3,429**	
C.1 impairment gains	1,911		476		2,767	
C.2 impairment gains due to collections	2,082		461		469	
C.3 gains on sales	-		-		-	
C.4 write-offs	-		-		-	
C.5 transfers to other categories of impaired loans	104		6,654		67	
C.6 contract amendments without derecognition	-	X	-	X	-	X
C.7 other decreases	927		-		126	
D. Closing total impairment losses	**18,451**		**9,277**		**1,442**	**15**
- of which: positions transferred but not derecognised	**-**		**-**		**-**	

A.2 CLASSIFICATION OF FINANCIAL ASSETS, COMMITMENTS TO DISBURSE FUNDS AND FINANCIAL GUARANTEES ISSUED BASED ON EXTERNAL AND INTERNAL RATING

A.2.1 Breakdown of financial assets, commitments to disburse funds and financial guarantees issued by external rating class (gross amounts)

The risk categories for the external rating indicated in this table refer to the creditworthiness classes of the debtors/ guarantors pursuant to prudential requirements (cf. Circular no. 285 of 2013 "Regulations for the supervision of banks" and subsequent updates).

The Bank uses the standardised approach in accordance with the risk mapping of the rating agencies:

- "DBRS Ratings Limited", for exposures to: central authorities and central banks; supervised brokers; public sector institutions; territorial entities.

	External rating class							
	Class 1	Class 2	Class 3	Class 4	Class 5	Class 6	Without rating	**Total**
A. Financial assets measured at amortised cost	-	**2,196**	**435,482**	-	-	-	**2,834,551**	**2,822,229**
- First stage	-	-	435,482	-	-	-	2,055,618	2,491,100
- Second stage	-	-	-	-	-	-	106,473	106,473
- Third stage	-	2,196	-	-	-	-	222,460	224,656
B. Financial assets measured at fair value through other comprehensive income	-	-	**298,341**	-	-	-	-	**298,341**
- First stage	-	-	298,341	-	-	-	-	298,341
- Second stage	-	-	-	-	-	-	-	-
- Third stage	-	-	-	-	-	-	-	-
Total (A+B)	-	**2,196**	**733,823**	-	-	-	**2,384,551**	**3,120,570**
of which: purchased or originated credit-impaired financial assets	-	-	-	-	-	-	26,062	26,062
C. Commitments to disburse funds and financial guarantees issued	-	-	-	-	-	-	**282,870**	**282,870**
- First stage	-	-	-	-	-	-	245,973	245,973
- Second stage	-	-	-	-	-	-	18,966	18,966
- Third stage	-	-	-	-	-	-	17,931	17,931
Total C	-	-	-	-	-	-	**282,870**	**282,870**
Total (A + B + C)	-	**2,196**	**733,823**	-	-	-	**2,667,421**	**3,403,440**

of which long-term rating

Creditworthiness class	Risk weighting factors				ECAI
	Central authorities and central banks	Supervised brokers, public sector institutions and territorial entities	Multilateral development banks	Companies and other parties	DBRS Ratings Limited
1	0%	20%	20%	20%	from AAA to AAL
2	20%	50%	50%	50%	from AH to AL
3	50%	100%	50%	100%	from BBBH to BBBL
4	100%	100%	100%	100%	from BBH to BBL
5	100%	100%	100%	150%	from BH to BL
6	150%	150%	150%	150%	CCC

of which short-term ratings (for exposures to companies)

Creditworthiness class	Risk weighting factors	ECAI DBRS Ratings Limited
1	20%	R-1 (high), R-1 (middle), R-1 (low)
2	50%	R-1 (high), R-2 (middle), R-2 (low)
3	100%	R-3
4	150%	R-4, R-5
5	150%	
6	150%	

"Fitch Ratings", for exposures to companies and other parties.

of which long-term rating

Creditworthiness class	Risk weighting factors				ECAI
	Central authorities and central banks	Supervised brokers, public sector institutions and territorial entities	Multilateral development banks	Companies and other parties	Fitch Ratings
1	0%	20%	20%	20%	from AAA to AA-
2	20%	50%	50%	50%	from A+ to A-
3	50%	100%	50%	100%	from BBB+ to BBB-
4	100%	100%	100%	100%	from BB+ to BB-
5	100%	100%	100%	150%	from B+ to B-
6	150%	150%	150%	150%	CCC+ and lower

of which short-term ratings (for exposures to companies)

Creditworthiness class	Risk weighting factors	ECAI Fitch Ratings
1	20%	F1+, F1
2	50%	F2
3	100%	F3
from 4 to 6	150%	less than F3

A.3 Breakdown of guaranteed credit exposures by type of guarantee

A.3.2 Guaranteed on- and off-statement of financial position loans and receivables with customers

	Gross amount	Carrying amount	Collateral (1)				CLN	Personal guarantees (2)								Total (1)+(2)
								Credit derivatives				Endorsement credits				
								Other derivatives								
			Mortgaged estate	Properties under finance lease	Securities	Other collateral		Central Counterparties	Banks	Other financial companies	Other	Public administrations	Banks	Other financial companies	Other	
1. Guaranteed on-statement of financial position loans:	**744,217**	**732,093**	**-**	**-**	**23,029**	**640,797**	**-**	**-**	**-**	**-**	**-**	**21,660**	**-**	**12**	**45,287**	**730,785**
1.1 fully guaranteed	731,625	720,916	-	-	23,029	640,796	-	-	-	-	-	12,526	-	12	44,554	720,917
- of which impaired	7,351	5,661	-	-	-	499	-	-	-	-	-	3,342	-	-	1,820	5,661
1.2 partially guaranteed	12,592	11,177	-	-	-	1	-	-	-	-	-	9,134	-	-	733	9,868
- of which impaired	4,668	3,639	-	-	-	-	-	-	-	-	-	2,848	-	-	643	3,491
2. Guaranteed off-statement of financial position loans:	**33,218**	**33,212**	**-**	**-**	**949**	**300**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**27,938**	**29,187**
2.1 fully guaranteed	28,342	28,336	-	-	949	300	-	-	-	-	-	-	-	-	27,086	28,335
- of which impaired	1,506	1,506	-	-	-	-	-	-	-	-	-	-	-	-	1,506	1,506
2.2 partially guaranteed	4,876	4,876	-	-	-	-	-	-	-	-	-	-	-	-	852	852
- of which impaired	292	292	-	-	-	-	-	-	-	-	-	-	-	-	266	266

B. BREAKDOWN AND CONCENTRATION OF CREDIT EXPOSURES

B.1 Breakdown by business segment of on- and off-statement of financial position loans and receivables with customers

	Public administrations		Financial companies		Financial companies (of which: insurance companies)		Non-financial companies		Households	
	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment
A. On-statement of financial position loans and receivables										
A1. Bad exposures	28,522	2,365	-	-	-	-	10,339	15,504	155	582
- of which: forborne exposures										
A.2 Unlikely to pay	59,807	2,384	-	-	-	-	16,405	6,229	1,700	663
- of which: forborne exposures										
A.3 Impaired past due exposures	51,623	397	1	-	1	-	25,740	1,023	1,702	22
- of which: forborne exposures							1,419	15		
A.4 Unimpaired exposures	1,817,179	3,421	43,429	55	4	-	306,520	1,672	680,284	1,259
- of which: forborne exposures										
TOTAL (A)	**1,957,131**	**8,567**	**43,430**	**55**	**5**	**-**	**359,004**	**24,428**	**683,841**	**2,526**
B. Off-statement of financial position loans and receivables										
B.1 Impaired exposures	-	-	-	-	-	-	17,931	-	-	-
B.2 Unimpaired exposures	-	-	111,729	-	-	-	89,862	6	2,420	1
TOTAL (B)	**-**	**-**	**111,729**	**-**	**-**	**-**	**107,793**	**6**	**2,420**	**1**
Total (A+B) at 31.12.2018	**1,957,131**	**8,567**	**155,159**	**55**	**5**	**-**	**466,797**	**24,434**	**686,261**	**2,527**
Total (A+B) at 31.12.2017	**1,404,519**	**6,440**	**7,575**	**-**	**16**	**-**	**274,621**	**19,753**	**538,057**	**1,689**

B.2 Breakdown by geographical segment of on- and off-statement of financial position loans and receivables with customers

	ITALY		OTHER EUROPEAN COUNTRIES		AMERICA		ASIA		REST OF THE WORLD	
	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment
A. On-statement of financial position loans and receivables										
A.1 Bad exposures	39,017	18,451	-	-	-	-	-	-	-	-
A.2 Unlikely to pay	77,912	9,277	-	-	-	-	-	-	-	-
A.3 Impaired past due exposures	76,893	1,419	-	-	-	-	2,173	23	-	-
A.4 Unimpaired exposures	2,808,499	6,267	30,635	108	5,011	19	2,871	11	400	1
Total (A)	**3,002,321**	**35,414**	**30,635**	**108**	**5,011**	**19**	**5,044**	**34**	**400**	**1**
B. Off-statement of financial position loans and receivables										
B.1 Impaired exposures	17,931	-	-	-	-	-	-	-	-	-
B.2 Unimpaired exposures	200,584	7	3,427	-	-	-	-	-	-	-
Total (B)	**218,515**	**7**	**3,427**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Total (A+B) at 31.12.2018	**3,220,836**	**35,421**	**34,062**	**108**	**5,011**	**19**	**5,044**	**34**	**400**	**1**
Total (A+B) at 31.12.2017	**2,206,708**	**27,834**	**14,982**	**39**	**1,080**	**3**	**2,018**	**6**	**-**	**-**

B.3 Breakdown by geographical segment of on- and off-statement of financial position loans and receivables with banks

	ITALY		OTHER EUROPEAN COUNTRIES		AMERICA		ASIA		REST OF THE WORLD	
	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment	Net amount	Total impairment
A. On-statement of financial position loans and receivables										
A.1 Bad exposures	-	-	-	-	-	-	-	-	-	-
A.2 Unlikely to pay	-	-	-	-	-	-	-	-	-	-
A.3 Impaired past due exposures	-	-	-	-	-	-	-	-	-	-
A.4 Unimpaired exposures	56,694	9	-	-	-	-	-	-	-	-
Total (A)	**56,694**	**9**	-	-	-	-	-	-	-	-
B. Off-statement of financial position loans and receivables										
B.1 Impaired exposures	-	-	-	-	-	-	-	-	-	-
B.2 Unimpaired exposures	2,446	-	-	-	-	-	-	-	-	-
Total (B)	**2,446**	-	-	-	-	-	-	-	-	-
Total (A+B) at 31/12/2018	**59,140**	**9**	-	-	-	-	-	-	-	-
Total (A+B) at 31/12/2017	**37,968**	-	-	-	-	-	-	-	-	-

B.4 Large exposures

As at 31 December 2018, the Bank's large exposures are as follows:

a) Carrying amount € 1,760,427 (in thousands)

b) Weighted value € 200,240 (in thousands)

c) No. of positions 19.

E. TRANSFERS

A. Financial assets transferred and not derecognised

QUALITATIVE DISCLOSURE

The financial assets transferred and not derecognised refer predominantly to Italian government securities used for repurchase agreements. Said financial assets are classified in the separate financial statements among the available-for-sale financial assets, while the repurchase agreement loan is predominantly presented in due to customers. As a last resort the financial assets transferred and not derecognised comprise trade receivables used for loan transactions in the ECB (Abaco).

QUANTITATIVE DISCLOSURE

E.2 Financial assets transferred and recognised partially, and associated financial liabilities: carrying amount

	Entire amount of original assets before transfer	Carrying amount of partially recognised assets	of which impaired	Carrying amount of associated financial liabilities
A. Financial assets held for trading	-	-	X	-
1. Debt instruments	-	-	X	-
2. Equity instruments	-	-	X	-
3. Financing	-	-	X	-
4. Derivatives	-	-	X	-
B. Other financial assets mandatorily measured at fair value through profit or loss	-	-		-
1. Debt instruments	-	-		-
2. Equity instruments	-	-	X	-
3. Financing	-	-		-
C. Financial assets designated at fair value through profit or loss	-	-		-
1. Debt instruments	-	-		-
2. Financing	-	-		-
D. Financial assets measured at fair value through other comprehensive income	-	-		-
1. Debt instruments	-	-		-
2. Equity instruments	-	-		-
3. Financing	-	-	X	-
E. Financial assets measured at amortised cost	**455,905**	-		-
1. Debt instruments	-	-		-
2. Financing	455,905	-		-
Total at 31.12.2018	455,905	-		-
Total at 31.12.2017	**455,550**	-		**43,149**

F. MODELS FOR THE MEASUREMENT OF CREDIT RISK

SECTION 2 - MARKET RISK

Banca Sistema did not conduct trading activity on financial instruments. At 31 December 2018 asset positions, except for shares, included in the regulatory trading portfolio that may generate market risk are not recognised.

The existing limit system defines a careful and balanced management of the operational autonomy, establishing limits in terms of portfolio amounts and composition by type of security.

2.1 Interest rate risk and price risk - regulatory trading portfolio

The trading risk changed only following the trading of the only shares held in the portfolio; due to the size of the investment the price risk is limited.

2.2 Interest rate risk and price risk - Banking Book

QUALITATIVE DISCLOSURE

A. General aspects, management procedures and methods of measuring the interest rate risk and the price risk

Interest rate risk is defined as the risk that the financial assets/liabilities increase /decrease because of movements contrary to the interest rate curve. The Bank identified the sources that generate interest rate risk with reference to the credit processes and to the Bank's funding.

The exposure to interest rate risk on the banking book is calculated as provided for by current regulations, via the simplified regulatory approach (Cf. Circular no. 285/2013, Part One, Title III, Chapter 1, Schedule C); by using this method the Bank is able to monitor the impact of unexpected changes in market conditions on equity, thus identifying the related mitigation measures to be implemented.

In greater detail, the process of estimating the exposure to interest rate risk of the banking book provided by the simplified method is organised in the following phases:

- Determination of material currencies. "Material currencies" are considered those that represent a portion of total assets, or also of the banking book liabilities, greater than 5%. For the purposes of the methodology for calculating exposure to interest rate risk, the positions denominated in "material currencies" are considered individually, while the positions in "non-material currencies" are aggregated for the equivalent amount in Euro;
- Classification of the assets and liabilities in time buckets. 14 time buckets are defined. The fixed-rate assets and liabilities are classified based on their residual maturity, while those at floating-rates based on the interest rate renegotiation date. Specific classification rules are prescribed for specific assets and liabilities. With particular reference to the deposit and savings product "Si conto! Deposito", the Bank proceeded with the bucketisation that takes into account the implied redemption option;
- Weighting the net exposures of each bucket. The asset and liability positions are offset within each bucket, obtaining a net position. The net position by bucket is multiplied by the corresponding weighting factor obtained as the product between a hypothetical change of the rates and an approximation of the modified duration for the individual bucket;
- Sum of the weighted net exposures of the various buckets. The weighted exposures calculated for each bucket (sensitivity) are summed together. The net weighted exposure thus obtained approximates the change of the present value of the items, denominated in a certain currency, in the event of the assumed rate shock;
- Aggregation in the various currencies. The absolute values of the exposures regarding the individual "material currencies" and the aggregate of the "non-material currencies" are summed together, obtaining an amount that represents the change of the economic value of the Bank based on the assumed rate trends.

With reference to the Bank's financial assets, the main sources that generate interest rate risk are loans and receivables with customers and the bond securities portfolio. As concerns the financial liabilities, relevant instead are the customer deposits and savings activities via current accounts, the savings account, and the collections on the interbank market.

Given the foregoing submissions, it should be noted that:

- the interest rates applied to the factoring customers are at a fixed rate and can also be modified unilaterally by the Bank (in compliance with regulations in force and existing contracts);
- the average financial term of the bond securities portfolio is less than one year;
- the salary/pension-backed loan portfolio that contains fixed rate contracts is that with the longest duration, however on the reporting date this portfolio was small and it was not deemed necessary to enter into interest rate hedge transactions on said maturities;
- the REPO deposits c/o the Central Bank are of short duration (the maximum maturity is equal to 3 months);
- the customers' deposits on the deposit account product are at a fixed rate for the entire duration of the constraint, which can be unilaterally renegotiated by the Bank (in compliance with regulations in force and the existing contracts);
- the REPO and reverse REPO agreements are generally of short duration, without prejudice to different funding needs.

The Bank continuously monitors the main assets and liabilities subject to interest rate risk; furthermore, no hedging instruments were used as at the reporting date.

QUANTITATIVE DISCLOSURE

1. Banking book: Breakdown by residual term (by repricing date) of financial assets and liabilities

Currency of denomination: Euro

	On demand	Up to 3 months	From more than 3 months to 6 months	From more than 6 months up to 1 year	From more than 1 year up to 5 years	From more than 5 years up to 10 years	More than 10 years	Open term
1. Assets	**1,178,497**	**177,881**	**245,826**	**159,169**	**1,041,158**	**297,570**	**4**	**-**
1.1 Debt instruments	-	-	157,894	36,949	538,860	-	-	-
- with early repayment option	-	-	-	-	-	-	-	-
- other	-	-	157,894	36,949	538,860	-	-	-
1.2 Financing to banks	24,211	32,469	14	-	-	-	-	-
1.3 Financing to customers	1,154,286	145,412	87,918	122,220	502,298	297,570	4	-
- current accounts	38,603	-	-	-	-	2	-	-
- other financing	1,115,683	145,412	87,918	122,220	502,298	297,568	4	-
- with early repayment option	13,874	41,058	84,608	122,070	502,298	264,397	4	-
- other	1,101,809	104,354	3,310	150	-	33,171	-	-
2. Liabilities	**678,655**	**910,076**	**270,729**	**326,779**	**682,013**	**33,975**	**13**	**-**
2.1 Due to customers	678,307	378,588	190,631	326,779	293,763	33,975	13	-
- current accounts	678,108	184,313	183,028	311,428	241,646	20,078	13	-
- other payables	199	194,275	7,603	15,351	52,117	13,897	-	-
- with early repayment option	-	-	-	-	-	-	-	-
- other	199	194,275	7,603	15,351	52,117	13,897	-	-
2.2 Due to banks	348	511,999	60,000	-	122,850	-	-	-
- current accounts	-	-	-	-	-	-	-	-
- other payables	348	511,999	60,000	-	122,850	-	-	-
2.3 Debt instruments	-	19,489	20,098	-	265,400	-	-	-
- with early repayment option	-	19,489	12,081	-	265,400	-	-	-
- other	-	-	8,017	-	-	-	-	-
2.4 Other liabilities	-	-	-	-	-	-	-	-
- with early repayment option	-	-	-	-	-	-	-	-
- other	-	-	-	-	-	-	-	-
3. Financial derivatives	**-**	**74,752**	**66,483**	**2,316**	**3,316**	**-**	**-**	**-**
3.1 With underlying security	-	64,931	64,940	-	-	-	-	-
- Options	-	-	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-
- Other derivatives	-	64,931	64,940	-	-	-	-	-
+ long positions	-	-	64,940	-	-	-	-	-
+ short positions	-	64,931	-	-	-	-	-	-
3.2 Without underlying security	-	9,821	1,543	2,316	3,316	-	-	-
- Options	-	9,821	1,543	2,316	3,316	-	-	-
+ long positions	-	1,323	1,543	2,316	3,316	-	-	-
+ short positions	-	8,498	-	-	-	-	-	-
- Other derivatives	-	-	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-
4. Other off-statement of financial position transactions	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
+ long positions	-	-	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-	-	-

2.3 Currency risk

QUALITATIVE DISCLOSURE

A. General aspects, management processes and methods of measuring the currency risk

All items are in Euro, except for the security in the trading portfolio. The currency risk is limited due to the size of the investment.

QUANTITATIVE DISCLOSURE

1. Breakdown of assets, liabilities and derivatives by currency of denomination

	CURRENCIES					
	US DOLLARS	UK POUNDS	YEN	CANADIAN DOLLARS	SWISS FRANCS	OTHER CURRENCIES
A. Financial assets	**-**	**-**	**-**	**-**	**-**	**1,178**
A.1 Debt instruments	-	-	-	-	-	-
A.2 Equity instruments	-	-	-	-	-	1,178
A.3 Financing to banks	-	-	-	-	-	-
A.4 Financing to customers	-	-	-	-	-	-
A.5 Other financial assets	-	-	-	-	-	-
B. Other assets	**-**	**-**	**-**	**-**	**-**	**-**
C. Financial liabilities	**-**	**-**	**-**	**-**	**-**	**-**
C.1 Due to banks	-	-	-	-	-	-
C.2 Due to customers	-	-	-	-	-	-
C.3 Debt instruments	-	-	-	-	-	-
C.4 Other financial liabilities	-	-	-	-	-	-
D. Other liabilities	**-**	**-**	**-**	**-**	**-**	**-**
E. Financial derivatives	**-**	**-**	**-**	**-**	**-**	**-**
- Options	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-
- Other derivatives	-	-	-	-	-	-
+ long positions	-	-	-	-	-	-
+ short positions	-	-	-	-	-	-
Total assets	**-**	**-**	**-**	**-**	**-**	**1,178**
Total liabilities	**-**	**-**	**-**	**-**	**-**	**-**
Difference (+/-)	**-**	**-**	**-**	**-**	**-**	**1,178**

The amount refers to the Axactor shares held by the Bank partly in the Held to Collect and Sell (HTCS) portfolio. They are listed securities traded in Norwegian krone.

SECTION 3 - DERIVATIVES AND HEDGING POLICIES

3.1 Derivatives held for trading

A. Financial derivatives

At 31 December 2018 the Bank did not recognise any amount for this item.

B. Credit derivatives

At 31 December 2018 the Bank did not recognise any amount for this item.

3.2 Hedge Accounting

The Bank did not perform any such transactions in 2018.

3.3 Other disclosure of derivatives (held for trading and hedging)

At 31 December 2018 there were no such cases.

SECTION 4 - LIQUIDITY RISK

QUALITATIVE DISCLOSURE

A. General aspects, management processes and methods of measuring the liquidity risk

Liquidity risk is represented by the possibility that the Bank is unable to maintain its payment commitments due to the inability to procure funds or to the inability to sell assets on the market to manage the financial imbalance. It is also represented by the inability to procure adequate new financial resources, in terms of amount and cost, with respect to operational need/advisability, that forces the Bank to slow or stop the development of activity, or to incur excessive funding costs to deal with their commitments, with significant negative impacts on the profitability of its activity. The financial sources are represented by capital, funding from customers, the funds procured on the domestic and international interbank market as well from the Eurosystem. To monitor the effects of the intervention strategies and to limit the liquidity risk, the Bank identified a specific section dedicated to monitoring the liquidity risk in the Risk Appetite Framework (RAF).

Furthermore, in order to promptly detect and manage any difficulties in procuring the funds necessary to conduct its activity, every year, Banca Sistema, consistent with the prudential supervisory provisions, updates its liquidity policy and Contingency Funding Plan, i.e. the set of specific intervention strategies in case of liquidity stress, establishing procedures to procure funds in the event of an emergency.

This set of strategies is of fundamental importance to attenuate liquidity risk.

The aforesaid policy defines, in terms of liquidity risk, the objectives, the processes and the intervention strategies in case of liquidity stress, the organisational structures responsible for implementing the interventions, the risk indicators, the relevant calculation method and warning thresholds, and procedures to procure the funding sources that can be used in case of emergency.

In 2018, the Bank continued to pursue a particularly prudent financial policy aimed at funding stability. This approach allowed a balanced distribution between inflows from retail customer and corporate and institutional counterparties.

To date, the financial resources available are satisfactory for the current and forward-looking volumes of activity.

The Bank is continuously active ensuring a coherent business development, always in line with the composition of its financial resources.

In particular, Banca Sistema, prudentially, has constantly maintained a high quantity of securities and readily liquid assets to cover all of the deposits and savings products oriented towards the retail segment.

The Bank subscribed to all the securities issued by the securitisation vehicles Quinto Sistema Sec. 2017 and Atlantis SPV, the first in connection with the securitisation of a portfolio of salary- and pension-backed loans and payment deductions ("CQS loans”), and the second in connection with the securitisation of loans deriving from “uncontested" enforceable injunctions against Italian Public Administrations that are not in difficulty.

At 31 December 2018, the characteristics of the securities of the Quinto Sistema Sec. 2017 transaction were as follows.

Quinto Sistema Sec. 2017	ISIN	Amount as at 31/12	Rating (DBRS/Moody's)	Interest Rate	Maturity
Class A (senior)	IT0005246811	343,953,684	A-high / Aa3	0.40%	2034
Class B1 (mezzanine)	IT0005246837	42,745,256	A-low / Ba1	0.50%	2034
Class B2 (sub-mezzanine)	IT0005246845	53,327,792	n.a.	0.50%	2034
Class C (junior)	IT0005246852	2,137,262	n.a.	0.50%	2034
		442,163,994			

At 31 December 2018, the characteristics of the securities of the Atlantis SPV transaction were as follows.

Atlantis SPV	ISIN	Amount as at 31/12	Rating	Interest Rate	Maturity
Class A Notes (senior)	IT0005218802	17,501,570	n.a.	1.00%	2028
Class B Notes (junior)	IT0005218810	15,320,900	n.a.	5.00%	2028
		32,822,470			

QUANTITATIVE DISCLOSURE

1. Breakdown of financial assets and liabilities by remaining contractual term

	On demand	From more than 1 day to 7 days	From more than 7 days to 15 days	From more than 15 days to 1 month	From more than 1 month to 3 months	From more than 3 months to 6 months	From more than 6 months up to 1 year	From more than 1 year up to 5 years	Over 5 years	Open term
A. Assets	**1,145,697**	**159**	**151**	**23,229**	**72,983**	**262,197**	**187,609**	**1,075,017**	**274,231**	**12,437**
A.1 Government securities	-	-	-	-	-	158,296	37,338	540,000	-	-
A.2 Other debt instruments	-	-	-	-	-	-	-	-	-	-
A.3 OEIC units	-	-	-	-	-	-	-	-	-	-
A.4 Financing	1,145,697	159	151	23,229	72,983	103,901	150,271	535,017	274,231	12,437
- banks	24,213	-	-	36	20,001	15	-	-	-	12,437
- customers	1,121,484	159	151	23,193	52,982	103,886	150,271	535,017	274,231	-
B. Liabilities	**666,703**	**442,007**	**51,779**	**78,657**	**318,893**	**253,161**	**334,900**	**693,613**	**61,488**	**-**
B.1 Deposits and current accounts	666,504	29,041	51,762	68,053	257,793	244,030	314,554	241,646	20,091	-
- banks	348	25,000	35,000	34,499	127,500	60,000	-	-	-	-
- customers	666,156	4,041	16,762	33,554	130,293	184,030	314,554	241,646	20,091	-
B.2 Debt instruments	-	-	-	-	412	1,505	4,977	277,000	27,500	-
B.3 Other liabilities	199	412,966	17	10,604	60,688	7,626	15,369	174,967	13,897	-
C. Off-statement of financial position transactions	**143,595**	**64,931**	**-**	**-**	**300**	**65,000**	**-**	**611**	**25**	**-**
C.1 Financial derivatives with exchange of principal	-	64,931	-	-	-	65,000	-	-	-	-
- long positions	-	-	-	-	-	65,000	-	-	-	-
- short positions		64,931	-	-	-	-	-	-	-	-
C.2 Financial derivatives without exchange of principal	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.3 Deposits and financing to be received	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.4 Irrevocable commitments to disburse funds	141,122	-	-	-	-	-	-	-	-	-
- long positions	70,561	-	-	-	-	-	-	-	-	-
- short positions	70,561	-	-	-	-	-	-	-	-	-
C.5 Financial guarantees issued	2,473	-	-	-	300	-	-	611	25	-
C.6 Financial guarantees received	-	-	-	-	-	-	-	-	-	-
C.7 Credit derivatives with exchange of principal	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-
C.8 Credit derivatives without exchange of principal	-	-	-	-	-	-	-	-	-	-
- long positions	-	-	-	-	-	-	-	-	-	-
- short positions	-	-	-	-	-	-	-	-	-	-

With reference to the financial assets subject to “self-securitisation”, at the end of 2018, Banca Sistema has two securitisation transactions in place for which it subscribed to the set of securities issued.

QUALITATIVE DISCLOSURE

Operational risk is the risk of loss arising from inadequate or non-functioning internal processes, human resources or systems, or from external events. This type of risk includes - among other things - the ensuing losses from fraud, human errors, business disruption, unavailability of systems, breach of contract, and natural catastrophes. Operational risk, therefore, refers to other types of events that, under present conditions, would not be individually relevant if not analysed jointly and quantified for the entire risk category.

A. General aspects, management processes and methods of measuring operational risk

In order to calculate the internal capital generated by the operational risk, the Bank adopts the Basic Indicator Approach, which provides for the application of a regulatory coefficient (equal to 15%) to the three-year average of the relevant indicator defined in Article 316 of EU Regulation no. 575/2013 of 26 June 2013. The above-said indicator is given by the sum (with sign) of the following elements:

- interest and similar income;
- interest and similar expense;
- income on shares, quotas and other variable/fixed yield securities;
- income for commissions/fees;
- expense for commissions/fees;
- profit (loss) from financial transactions;
- other operating income.

Consistent with that provided for by the relevant legislation, the indicator is calculated gross of provisions and operating costs; also excluded from computation are:

- profits and losses on the sale of securities not included in the trading portfolio;
- income deriving from non-recurring or irregular items;
- income deriving from insurance.

As of 2014, the Bank measured the operational risk events via a qualitative performance indicator (IROR - Internal Risk Operational Ratio) defined within the operational risk management and control process (ORF - Operational Risk Framework). This calculation method allows a score to be defined between 1 and 5, inclusive (where 1 indicates a low risk level and 5 indicates a high risk level) for each event that generates an operational risk.

The Bank assesses and measures the level of the identified risk by also considering the controls and the mitigating actions implemented. This method requires a first assessment of the possible associated risks in terms of probability and impact (so-called “Gross risk level”) and a subsequent analysis of the existing controls (qualitative assessment on the effectiveness and efficiency of the controls) which could reduce the gross risk, on the basis of which specific risk levels (the so-called “Residual risk”) are determined. Finally, the residual risks are mapped on a predefined scoring grid, useful for the subsequent calculation of IROR via appropriate aggregation of the scores defined for the individual operational procedure.

Moreover, the Bank assesses the operational risk associated with the introduction of new products, activities, processes and relevant systems mitigating the onset of the operational risk via a preliminary evaluation of the risk profile.

The Bank places strong emphasis on possible ICT risks. The Information and Communication Technology (ICT) risk is the risk of incurring financial, reputational and market losses in relation to the use of information and communication technology. In the supplemented representation of the business risks, this type of risk is considered, in accordance with the specific aspects, among operational, reputational and strategic risks.

The Bank monitors the ICT risks based on the continuous information flows between the departments concerned defined in its IT security policies.

In order to conduct consistent and complete analyses with respect to the activities performed by the Bank’s other control departments, the results of the compliance risks audits conducted by the Compliance and Anti-Money Laundering Department were shared internally with the Risk Management and Compliance Department, the Internal Control and Risk Management Committee, as well as with the CEO. The Internal Audit Department also monitors the Bank's operations and processes to ensure they are properly carried out and assesses the overall effectiveness and efficiency of the internal control system put in place to oversee activities that are exposed to risks. Finally, as an additional protection against operational risk, the Bank has:

- insurance coverage on the operational risks deriving from actions of third parties or procured to third parties. In order to select the insurance coverage, the Bank initiated specific assessment activities, with the support of a primary market broker, to identify the best offers in terms of price/conditions proposed by several insurance undertakings;
- appropriate contractual riders to cover damages caused by infrastructure and service suppliers;
- a business continuity plan;
- the assessment of each operational procedure in effect, in order to define the controls implemented to protect against risk activities.

PART F - INFORMATION ON EQUITY

SECTION 1 - BANK EQUITY

A. QUALITATIVE DISCLOSURE

The objectives pursued in the Bank's equity management are inspired by the prudential supervisory provisions and are oriented towards maintaining adequate levels of capitalisation to take on risks typical to credit positions.

The income allocation policy aims to strengthen the Bank's capital with special emphasis on primary capital, to the prudent distribution of the operating results, and to guaranteeing a correct balance of the financial position.

B. QUANTITATIVE DISCLOSURE

B.1 Bank equity: breakdown

		31.12.2018	31.12.2017
1	Share capital	9,651	9,651
2	Share premium	39,184	39,268
3	Reserves	79,803	59,391
	- income-related	79,794	59,388
	a) legal	1,930	1,930
	b) established under the Articles of Association	-	-
	c) treasury shares	200	200
	d) other	77,664	57,258
	- other	9	3
3.bis	Equity instruments	-	-
4	Interim dividends (-)	-	-
5	(Treasury shares)	(199)	(149)
6	Valuation reserves	(1,131)	367
	- Equity instruments designated at fair value through other comprehensive income	19	412
	- Hedging of equity instruments designated at fair value through other comprehensive income	-	-
	- Financial assets (other than equity instruments) measured at fair value through other comprehensive income	(972)	173
	- Property and equipment	-	-
	- Intangible assets	-	-
	- Hedges of foreign investments	-	-
	- Cash flow hedges	-	-
	- Hedging instruments (non-designated elements)	-	-
	- Exchange rate gains (losses)	-	-
	- Non-current assets held for sale and disposal groups	-	-
	- Financial liabilities designated at fair value through profit or loss (changes in own credit rating)	-	-
	- Net actuarial losses on defined benefit pension plans	(178)	(218)
	- Shares of valuation reserves of equity-accounted investees	-	-
	- Special revaluation laws	-	-
7	Profit for the year	28,071	27,560
	TOTAL	**155,379**	**136,088**

B.2 Valuation reserves for financial assets measured at fair value through other comprehensive income: breakdown

	TOTAL AT 31.12.2018		TOTAL AT 31.12.2017	
	Positive reserve	Negative reserve	Positive reserve	Negative reserve
1. Debt instruments	-	972	173	-
2. Equity instruments	19	-	412	-
3. Financing	-	-	-	-
Total	**19**	**972**	**585**	-

B.3 Valuation reserves for financial assets measured at fair value through other comprehensive income: changes

	Debt instruments	Equity instruments	Financing
1. Opening balance	**173**	**412**	-
2. Increases	**639**	**280**	-
2.1 Fair value gains	-	77	-
2.2 Impairment losses due to credit risk	49	X	-
2.3 Reclassifications of negative reserves to profit or loss on sale	-	X	-
2.4 Transfers to other equity items (equity instruments)	-		-
2.5 Other increases	590	203	-
3. Decreases	**1,784**	**673**	-
3.1 Fair value losses	-	663	-
3.2 Impairment gains due to credit risk	-		-
3.3 Reclassifications of positive reserves to profit or loss: on sale	259	X	
2.4 Transfers to other equity items (equity instruments)	-		-
2.5 Other decreases	1,525	10	-
4. Closing balance	**(972)**	**19**	-

B.4 Valuation reserves related to defined benefit plans: changes

A. Opening balance	**(217)**
B. Increases	**54**
B.1 Actuarial gains	54
B.2 Other increases	-
C. Decreases	**15**
C.1 Actuarial losses	-
C.2 Other decreases	15
D. Closing balance	**(178)**
Total	**(178)**

2.1 Own funds

A. QUALITATIVE DISCLOSURE

Own funds, risk weighted assets and solvency ratios as at 31 December 2018 were determined based on the new regulation, harmonised for Banks, contained in the Directive 2013/36/EU (CRD IV) and in the Regulation (EU) 575/2013 (CRR) of 26 June 2013, that transpose in the European Union the standards defined by the Basel Committee on Banking Supervision (the so-called Basel 3 framework), and based upon the Circular of the Bank of Italy no. 285 and no. 286 (enacted in 2013), and the update of Circular no. 154.

The Banca Sistema Group has not availed itself of the option provided for by Article 473 bis of Regulation (EU) 575/2013 (CRR), which concerns the transitional measures aimed at mitigating the impact of the introduction of IFRS 9.

Own funds are characterised by a 3-tier structure:

1) Common Equity Tier 1 (CET1) capital

A) Common Equity Tier 1 (CET1) capital

This item includes:

- Fully paid-in capital of € 9.7 million;
- A share premium of € 39.2 million;
- Other reserves including undistributed profits of € 99.8 million.

In particular, this item includes a profit of € 21.1 million recognised in Own funds pursuant to article 26 of the CRR, net of foreseeable dividends pertaining to the Bank and of the other negative accumulated income statement components of € 1.1 million composed as follows:

- Actuarial reserve in accordance with the application of the new IAS 19 amounting to € 179 thousand;
- Reserves on financial assets measured at fair value through other comprehensive income for € 952 thousand;
- Negative component for treasury shares of € 244 thousand.

D) Items to be deducted from CET1

This item includes the following main aggregates:

- Goodwill and other intangible assets, equal to € 1.8 million;

2) Additional Tier 1 (AT1) capital

G) Additional Tier1 (AT1) capital including elements to be deducted and the effects of the transitional regime.

This item includes the security ISIN IT0004881444 issued by Banca Sistema as an innovative equity instrument with mixed rate amounting to € 8 million.

3) Tier 2 (T2) capital

M) Tier 2 (T2) capital including elements to be deducted and the effects of the transitional regime.

This item includes:

- the security ISIN IT0004869712 issued by Banca Sistema as an ordinary subordinated loan (Lower Tier 2) equal to € 12 million, considered in Tier 2 capital for € 9.3 million following application of the conservatively recognised amortisation described in Article 64 of Regulation 575/2013 starting from 2017;
- the security IT0005247397 issued by Banca Sistema as an ordinary subordinated loan (Tier 2) equal to € 19.5 million.

A. QUANTITATIVE DISCLOSURE

	31.12.2018
A. Common Equity Tier 1 (CET1) before application of prudential filters	**148,337**
of which CET 1 instruments covered by transitional measures	-
B. CET1 prudential filters (+/-)	-
C. CET1 including items to be deducted and the effects of the transitional regime (A+/-B)	**148,337**
D. Items to be deducted from CET1	**1,788**
E. Transitional regime - Impact on CET (+/-)	**-**
F. Total Common Equity Tier 1 (CET1) (C-D+/-E)	**146,549**
G. Additional Tier 1 (AT1) including items to be deducted and the effects of the transitional regime	**8,000**
of which AT1 instruments covered by transitional measures	**-**
H. Items to be deducted from AT1	**-**
I. Transitional regime - Impact on AT1 (+/-)	**-**
L. Total Additional Tier 1 (AT1) (G-H+/-I)	**8,000**
M. Tier 2 (T2) including items to be deducted and the effects of the transitional regime	**28,799**
of which T2 instruments covered by transitional measures	-
N. Items to be deducted from T2	-
O. Transitional regime - Impact on T2 (+/-)	-
P. Total Tier 2 (T2) (M-N+/-O)	**28,799**
Q. Total Own Funds (F+L+P)	**183,348**

2.2 Capital adequacy

A. QUALITATIVE DISCLOSURE

The Own funds totalled € 183 million, against risk-weighted assets of € 1,309 million, derived almost exclusively from credit risk.

As at 31 December 2018, Banca Sistema had a CET1 capital ratio equal to 11.2%, a Tier 1 capital ratio equal to 11.8% and a Total capital ratio of 14.0%.

B. QUANTITATIVE DISCLOSURE

	UNWEIGHTED AMOUNTS		WEIGHTED AMOUNTS/ REQUIREMENTS	
	31.12.2018	31.12.2017	31.12.2018	31.12.2017
A. EXPOSURES	-	-	-	-
A.1 Credit and counterparty risk	3,591,235	2,754,827	1,152,293	900,968
1. Standardised approach	3,591,235	2,754,827	1,152,293	900,968
2. Internal ratings based approach	-	-	-	-
2.1 Basic	-	-	-	-
2.2 Advanced	-	-	-	-
3. Securitisations	-	-	-	-
B. CAPITAL REQUIREMENTS			-	-
B.1 Credit and counterparty risk			92,183	72,077
B.2 Credit assessment adjustment risk			-	249
B.3 Settlement risk			-	-
B.4 Market risk			-	192
1. Standard approach			-	192
2. Internal models			-	-
3. Concentration risk			-	-
B.5 Operational risk			12,514	11,426
1. Basic indicator approach			12,514	11,426
2. Standardised approach			-	-
3. Advanced measurement approach			-	-
B.6 Other calculation elements			-	-
B.7 Total prudential requirements			104,698	83,945
C. EXPOSURES AND CAPITAL RATIOS			**1,308,721**	**1,049,315**
C.1 Risk-weighted assets			1,308,721	1,049,315
C.2 CET1 capital/risk-weighted assets (CET1 Capital Ratio)			11.2%	12.1%
C.3 Tier 1 capital/risk-weighted assets (Tier 1 Capital Ratio)			11.8%	12.9%
C.4 Total Own Funds/risk-weighted assets (Total Capital Ratio)			14.0%	15.6%

PART G - BUSINESS COMBINATIONS

Section 1 - Transactions performed in the year

No transactions to report.

Section 2 - Transactions performed after the end of the year

No transactions to report.

Section 3 - Retrospective adjustments

No transactions to report.

PART H - RELATED PARTY TRANSACTIONS

Related party transactions including the relevant authorisation and disclosure procedures, are governed by the "Procedure governing related party transactions" approved by the Board of Directors and published on the internet site of Banca Sistema S.p.A.

Transactions between Group companies and related parties were carried out in the interests of the Bank, including within the scope of ordinary operations; these transactions were carried out in accordance with market conditions and, in any event, on the basis of mutual financial advantage and in compliance with all procedures.

With respect to transactions with parties who exercise management and control functions in accordance with article 136 of the Consolidated Banking Act, it should be noted that they, where applicable, have been included in the Board of Directors' resolutions and received approval from the Board of Statutory Auditors, subject to compliance with the obligations provided under the Italian Civil Code with respect to matters relating to the conflict of interest of directors.

Pursuant to IAS 24, the related parties of Banca Sistema include:

- shareholders with significant influence;
- companies belonging to the banking Group;
- companies subject to significant influence;
- key management personnel;
- the close relatives of key management personnel and the companies controlled by (or connected with) such personnel or their close relatives.

DISCLOSURE ON THE REMUNERATION OF KEY MANAGEMENT PERSONNEL

The following data show the remuneration of key management personnel, as per IAS 24 and Bank of Italy Circular no. 262 of 22 December 2005 as subsequently updated, which requires the inclusion of the members of the Board of Statutory Auditors.

In thousands of Euro	BOARD OF DIRECTORS	BOARD OF STATUTORY AUDITORS	OTHER MANAGERS	2018
Remuneration to Board of Directors and Board of Statutory Auditors	1,550	88	-	**1,638**
Short-term benefits for employees	-	-	1,286	1,286
Post-employment benefits	60	-	96	156
Other long-term benefits	187	-	10	197
Termination benefits	-	-	-	-
Share-based payments	95	-	54	149
Total	**1,892**	**88**	**1,446**	**3,426**

DISCLOSURE ON RELATED PARTY TRANSACTIONS

The following table shows the assets, liabilities, guarantees and commitments as at 31 December 2018, differentiated by type of related party with an indication of the impact on each individual caption.

In thousands of Euro	SUBSIDIARIES	DIRECTORS, BOARD OF STATUTORY AUDITORS AND KEY MANAGEMENT PERSONNEL	OTHER RELATED PARTIES	% OF CAPTION
Loans and receivables with customers	38,694	220	69,641	4.0%
Due to customers	-	2,051	30,844	1.7%
Other liabilities	321	-	-	0.5%

The following table indicates the costs and income for 2018, differentiated by type of related party.

In thousands of Euro	SUBSIDIARIES	DIRECTORS, BOARD OF STATUTORY AUDITORS AND KEY MANAGEMENT PERSONNEL	OTHER RELATED PARTIES	% OF CAPTION
Interest income	500	-	176	0.7%
Interest expense	-	19	102	0.5%

The following table sets forth the details of each related party:

	AMOUNT (Thousands of Euro)	PERCENTAGE (%)
ASSETS	**108,334**	**3.44%**
Loans and receivables with customers		
Axactor Italy Spa	69,641	2.54%
Speciality Finance Trust Holdings Ltd	1,593	0.06%
Largo Augusto Servizi E Sviluppo Srl	37,100	1.35%
LIABILITIES	**7,373**	**0.23%**
Due to customers		
Soci - SGBS	2,257	0.12%
Soci - Fondazione CR Alessandria	2,052	0.11%
Soci - Fondazione Sicilia	1,817	0.10%
Adv Finance S.P.A.	927	0.05%
Other liabilities		
Speciality Finance Trust Holdings Ltd	91	0.14%
Largo Augusto Servizi E Sviluppo Srl	229	0.35%

	AMOUNT (Thousands of Euro)	PERCENTAGE (%)
INCOME	**675**	**0.68%**
Interest income		
Axactor Italy Spa	174	0.17%
Speciality Finance Trust Holdings Ltd	158	0.16%
Largo Augusto Servizi E Sviluppo Srl	342	0.34%
Adv Finance S.P.A.	1	-
COSTS	**26**	**0.10%**
Interest expense		
Soci - SGBS	5	0.02%
Soci - Fondazione Sicilia	6	0.02%
Soci - Fondazione CR Alessandria	14	0.06%
Adv Finance S.P.A.	1	0.01%

PART I - PAYMENT AGREEMENTS BASED ON OWN EQUITY INSTRUMENTS

QUALITATIVE DISCLOSURE

The Banca Sistema Group's 2017-2019 Stock Grant Plan prepared in accordance with article 114-bis of Legislative Decree no. 58/98 and article 84-bis of regulation no. 11971/99 approved by Consob on 14 May 1999 as amended, approved by the Board of Directors on 28 March 2017 and published on the Bank's website, establishes the means and rules for granting, assigning and the availability of the Bank's ordinary shares to key management personnel and other persons who fall under the category of "key personnel" who are granted a bonus for which - in accordance with the rules set out in the Remuneration Policies Document applicable for each year in question (the "Policy") - the deferral and subordination mechanisms upon achieving specific corporate and individual performance targets are defined.

In 2018, the variable component of remuneration will be paid as follows upon approval of the separate financial statements:

- for amounts less than € 20,000, the full amount is paid up-front, in cash;
- for amounts between € 20,000 and € 50,000, 50% of the variable remuneration is paid up-front in cash and the remaining 50% is deferred and paid in shares of the Bank at the end of the 3-year deferral period;
- for amounts greater than € 50,000, 60% of the variable remuneration is paid up-front (50% in cash and 50% in shares of the Bank) and the remaining 40% is deferred and paid at the end of the 3-year deferral period (50% in cash and 50% in shares of the Bank).

Please see Annex 2 to the 2017 Policy and the Information Document relating to the 2017-2019 Stock Grant Plan in the 'Governance' section of the website www.bancasistema.it regarding the calculation of the Bank shares to be assigned and the applicable provisions.

Disclosure of the fees paid to the independent auditors

Pursuant to the provisions of Art. 149 duodecies of the Consob Issuers' Regulations, the information regarding the fees paid to the independent auditors KPMG S.p.A. and to the companies included in the same network is reported below for the following services:

- Audit services that include:
- The audit of the annual accounts, for the purpose of expressing an opinion thereon;
- The audit of the interim accounts;
- Certification services that include tasks whereby the auditor evaluates a specific element, the determination of which is performed by another party who is responsible thereof, through appropriate criteria, in order to express a conclusion that provides the recipient party with a degree of confidence concerning said specific element;
- Tax advisory services;
- Other services.

The fees presented in the table, pertaining to 2018, are those contracted, including any index-linking (but do not include out-of-pocket expenses, any supervisory contribution and VAT).

They do not include, in accordance with the cited provision, the fees paid to any secondary auditors or to parties of the respective networks.

Type of services	Entity providing the service	Addressee	Remuneration
Audit of the separate financial statements and interim reports	KPMG S.p.A.	Banca Sistema S.p.A.	184

For the purposes of segment reporting as per IFRS 8, the income statement is broken down by segment as follows.

Breakdown by segment: income statement for 2018

Amounts in thousands of Euro	2018			
	Factoring	**Banking**	**Corporate**	**Consolidated total**
Net interest income (expense)	67,621	18,742	(11,617)	**74,746**
Net fee and commission income (expense)	15,713	603	(1,059)	**15,257**
Other costs/income	-	-	1,269	**1,269**
Total income (expense)	**83,334**	**19,345**	**(11,407)**	**91,272**
Net impairment losses on loans and receivables	(2,077)	(4,737)	-	**(6,814)**
Net financial income (expense)	**81,257**	**14,608**	**(11,407)**	**84,458**

Breakdown by segment: statement of financial position data as at 31 December 2018

Amounts in thousands of Euro	31.12.2018			
	Factoring	**Banking**	**Corporate**	**Consolidated total**
Financial assets (HTS and HTCS)	-	-	304,469	**304,469**
Loans and receivables with banks	-	-	56,694	**56,694**
Loans and receivables with customers	1,566,613	680,781	497,725	**2,745,119**
Due to banks	-	-	695,197	**695,197**
Due to customers	87,396	-	1,814,660	**1,902,056**

The Factoring division includes the business segment related to the origination of trade and tax receivables with and without recourse. In addition, the division includes the business segment related to the management and recovery of receivables on behalf of third parties.

The Banking segment includes the business segment related to the purchase of salary- and pension-backed loans (CQS/CQP) portfolios, collateralised loans, run-off portfolios related to guaranteed loans to small and medium-sized enterprises, and costs/income from assets under administration and the placement of third-party products. The Corporate segment includes activities related to the management of the Group's financial resources and costs/income in support of the business activities. Moreover, this segment includes all the consolidation entries, as well as all the interbank eliminations.

The secondary disclosure by geographical segment has been omitted as immaterial, since the customers are mainly concentrated in the domestic market.

STATEMENTS ON THE SEPARATE FINANCIAL STATEMENTS IN ACCORDANCE WITH ARTICLE 81-TER OF CONSOB REGULATION NO. 11971 OF 14 MAY 1999 AS AMENDED AND SUPPLEMENTED

1. The undersigned, Gianluca Garbi, in his capacity as CEO, and Alexander Muz, in his capacity as Manager in charge of financial reporting of Banca Sistema S.p.A., hereby state, having taken into account the provisions of Art. 154-bis, paragraphs 3 and 4, of Legislative Decree no. 58 of 24 February 1998:
   - the suitability as regards the characteristics of the bank and
   - the effective application of the administrative and accounting procedures for the drafting of the separate financial statements as at and for the year ended 31 December 2018.
2. The suitability and effective application of the administrative and accounting process for the drafting of the separate financial statements at 31 December 2018 was verified based on internally defined methods, in accordance with the provisions of the reference standards for the internal audit system generally accepted on an international level.
3. Moreover, the undersigned hereby state that:

   3.1 the separate financial statements:

   a) were drafted in accordance with the applicable International Financial Reporting Standards endorsed by the European Community, pursuant to regulation (EC) no. 1606/2002 of the European Parliament and of the Council of 19 July 2002;

   b) match the accounting books and records;

   c) are suitable for providing a true and fair view of the financial position, results of operations and cash flows of the issuer.

   3.2 The Directors' report includes a reliable analysis of business performance and results, as well as of the position of the issuer, together with a description of the main risks and uncertainties to which it is exposed.

Milan, 1 March 2019

Gianluca Garbi

Chief Executive Officer

Alexander Muz

Manager in charge of financial reporting

BOARD OF STATUTORY AUDITORS' REPORT

BANCA SISTEMA S.P.A.

* * *

BOARD OF STATUTORY AUDITORS' REPORT

TO THE SHAREHOLDERS' MEETING CALLED TO APPROVE

THE FINANCIAL STATEMENTS AT 31 DECEMBER 2018

IN ACCORDANCE WITH ARTICLE 153 OF LEGISLATIVE DECREE 58/1998 and ARTICLE 2429 OF THE ITALIAN CIVIL CODE

***

Part One: introduction

Dear Shareholders of Banca Sistema S.p.A. ("**Bank**"),

pursuant to Article 153 of Legislative Decree 58/1998 and Article 2429 of the Italian Civil Code, we give you this report on our supervisory activities during the calendar year (and, for the sake of completeness, on the most significant events occurring after the end of the year), and also make proposals concerning the financial statements and their approval.

This report has been approved by the whole board and by the legal deadline pursuant to law.

As required by law and the Articles of Association, we monitored compliance with the law, regulations, and Articles of Association during 2018, whose compliance we confirm. We also monitored the application of proper management methods, the adequacy and functioning of the organisational, management and accounting structure, and the other acts and aspects as envisaged by law.

We have examined the draft financial statements of Banca Sistema S.p.A. at 31 December 2018 (the "**Financial Statements**"), comprised of the Statement of Financial Position, the Income Statement, the Statement of Comprehensive Income, the Statement of Changes in Equity, the Statement of Cash Flows and the Notes to the Financial Statements, and is accompanied by the Directors' Report and complementary financial statements, showing a profit for the year of € 28,070,559.59.

After approving the draft financial statements on 1 March 2019, the Board of Directors sent us the reporting package by the statutory deadline.

Between the meeting dedicated to drafting the previous report on the financial statements and today, the current Board of Statutory Auditors held 17 meetings (including the meeting held to draft this report), and participated in all the meetings of the Board of Directors and the Internal Control and Risk Management Committee, as confirmed by the documents provided to you in the package prepared for this shareholders' meeting.

We shall provide you with detailed information in this report about all of our activities.

Part Two: monitoring legal compliance and compliance with the Articles of Association

In this part we report on the activities performed by the Board of Statutory Auditors pursuant to Article 2403 of the Italian Civil Code.

During the year, the Board of Statutory Auditors monitored compliance with the law, the memorandum of association and compliance with the principles of proper management. These activities adhere to the principles of conduct of the Board of Statutory Auditors of listed companies recommended by the National Board of Business Experts and Accountants.

In addition to its previously discussed meetings, the Board of Statutory Auditors participated in all meetings held in 2018 by the corporate bodies in compliance with the Articles of Association, the law and regulatory provisions that govern their proceedings. Therefore, we can reasonably assure that the adopted resolutions complied with the law and the Articles of Association, were not manifestly imprudent, reckless or potentially in conflict of interest or conflicting with the resolutions approved by the Shareholders' Meetings or such as might compromise the solidity of corporate assets.

In the course of performing its own duties at meetings, the Board of Statutory Auditors met periodically with the principal internal departments of the Company (risk, compliance, legal affairs, corporate affairs, internal control and audit system, underwriting). It examined the documents submitted to it and performed its own analyses and assessments, as summarised in its own minutes. These have not revealed any elements that might cast doubt on compliance with the law, the Articles of Association, and principles of proper management. It analysed the most important operating, financial and equity transactions, verifying their compliance with the law and the memorandum of association, finding that they were not manifestly imprudent or reckless and/or in potential conflict of interest and/or in conflict with the resolutions passed by the shareholders' meetings and/or prejudicial to the operating, asset and liability, and financial performance of the Bank. It also participated in work groups on specific matters. The Board of Statutory Auditors has approved all examined transactions as being consistent with the corporate interest.

The Board of Statutory Auditors acknowledges that the key information concerning the Bank's transactions with related parties has been provided during the Board of Directors meetings and in the Financial Statements. In this regard, the Board of Statutory Auditors deems it appropriate to call the shareholders' attention to the interpretation of the paragraphs in the Directors' Report and Notes to the Financial Statements where those events are described.

Among the significant events that occurred in 2018, we note:

- On 9 April 2018, following the authorisations granted by the Bank of Italy, two new branches dedicated exclusively to the collateralised lending business were opened in Naples and Palermo.
- On 10 April, the Board of Directors of Banca Sistema approved the 2018-2020 Strategic Plan, which was presented to analysts and investors on 11 April 2018.
- On 23 April 2018, the shareholders' meeting was held during which the Board of Directors' mandate was renewed with the appointment of nine members.
- Following the renewal, the Board of Directors approved the appointment of Gianluca Garbi as CEO of the Bank, conferring on him necessary operational powers.
- At the end of May 2018, the placement was completed for a senior bond issue. The placement in a club deal reserved for institutional investors that are not related parties, in the total amount of € 90 million, has a term of 3 years, with a fixed rate and an all-inclusive cost of 200 bps.
- On 19 June 2018, the Bank completed the acquisition of a 19.90% stake in the share capital of ADV Finance S.p.A. ("ADV Finance"), a registered financial intermediary (under art. 106 of the Consolidated Banking Act) that since 2010 has offered in Italy, through agents and brokers, a complete range of services related to salary- and pension-backed personal loans (CQS/CQP). Subsequently, on 18 December 2018, it acquired from ADV Finance, 19.90% of the quota capital of the subsidiary Procredit S.r.l., a company specialising in services related to salary- and pension-backed personal loans (CQS/CQP).
- On 22 June 2018, the Board of Directors approved the start of market making activities and thus allocated € 40,000 to it for the purchase and disposal of treasury shares within the scope of the authorisation granted at the Shareholders' Meeting of

27 April 2017 and in accordance with the terms authorised by the Bank of Italy on 13 September 2017. The programme was suspended on 5 October 2018 to start the treasury share repurchase programme for the purpose of supporting the remuneration and incentive policies for key personnel for an overall amount not exceeding € 200,000, which was concluded on 12 October 2018, the day on which the market making activity programme resumed and which was terminated on 27 October 2018.

- On 29 June 2018, notice was given that the shareholders Società di Gestione delle Partecipazioni in Banca Sistema S.r.l. (SGBS), Fondazione Cassa di Risparmio di Alessandria and Fondazione Sicilia, in anticipation of the imminent expiry date of the Shareholders' Agreement signed on 3 June 2015 along with Fondazione Pisa, having taken note of the intention expressed by Fondazione Pisa not to join the new Shareholders' Agreement, signed a new Shareholders' Agreement which came into effect on this date until 1 July 2020. The new Shareholders' Agreement reflects a shareholding of 38.41% in Banca Sistema's share capital.
- Given the above, Claudio Pugelli, a non-executive and non-independent Director of Banca Sistema, tendered his resignation from the position with effect from 30 June.
- On 13 July 2018, the Board of Directors co-opted a Director in the person of Mr. Daniele Pittatore.
- An abstract of the new Shareholders' Agreement, which was drafted pursuant to article 129 of the Issuers' Regulation approved by Consob Resolution no. 11971/99, and essential information pursuant to article 130 of the Issuers' Regulation have been made available on the Parent's website www.bancasistema.it and on the website of the storage mechanism authorised by Consob www.1info.it in accordance with the legal terms.
- On 28 September 2018, the Bank signed a binding agreement for the acquisition of 100% of Atlantide S.p.A., a registered financial intermediary (under art. 106 of the Consolidated Banking Act) and active in the granting of salary- and pension-backed personal loans (CQS/CQP) since 2010. The administrative procedure was completed on 12 March 2019 with the order of the Bank of Italy that authorised the acquisition of the entire shareholding and the subsequent merger pursuant to art. 2505 of the Italian Civil Code.
- During 2018, work was completed on the renovation of the building to be used for the new registered office and the transfer to Milan, Largo Augusto, 1/A at the corner of

Via Verziere, 13, which began on 12 October 2018, was completed on 9 November 2018.

- On 12 October 2018, the company ProntoPegno S.p.A. was incorporated, with Banca Sistema S.p.A. as sole shareholder. The registered office of the company is in Largo Augusto 1/A, Milan (at the corner of Via Verziere 13) and the share capital amounts to € 3,500,000.
- On 9 November 2018, the application was sent to the Bank of Italy for the registration of ProntoPegno S.p.A. in the Register referred to in Article 106 of Legislative Decree no. 385/1993, in accordance with the provisions of Circular no. 288 of 3 April 2015.
- On 8 November 2018, following the authorisation issued by the Bank of Italy, a new branch dedicated exclusively to the collateralised loan business was opened in the city of Rimini. This branch joins the branches in Milan, Rome, Pisa, Naples and Palermo.
- On 7 November, Banca Sistema also acquired the portfolio of Credit Agricole, formerly Carim, a collateralised lender based in Rimini.
- On 16 October 2018, the Bank was subject to inspections by the Bank of Italy, in accordance with the banking and financial regulations. The purpose of the inspections was to verify compliance with anti-money laundering legislation and the effectiveness of the organisational structures in reporting the AOER correctly and preventing the risks associated with violations of usury regulations. The inspections were completed on 14 December 2018 and the inspection report was notified on 1 March 2019. The inspections concluded with an assessment that was "partially favourable considering the adequacy of controls on the risks of money laundering, terrorist financing and usury, although there is room for improvement in a situation of growth in operating volumes and number of customers".
- The exchanges of correspondence and meetings between the Board of Statutory Auditors and the Bank of Italy officers concerning the clarifications requested by the Supervisory Authority as part of its ordinary control activities;
- The exchanges of correspondence with Consob concerning the clarifications requested as part of its ordinary control activities;
- The periodic exchanges of information with the independent auditors;
- The meeting with the Supervisory Body for the exchange of information;
- The meeting with the independent directors;
- The approval of the Remuneration Policies Document;

- The monitoring of business activities in accordance with the Risk Appetite Framework.

With regard to "significant events during the year", reference is also made to the Directors' Report.

The Board of Statutory Auditors issued the following opinions pursuant to law:

- Request for approval of non-audit services, requested by the Independent Auditors;
- Opinion on the appointment of the new Manager in charge of financial reporting, pursuant to Article 154-bis of Legislative Decree 58 of 24 February 1998.

On 23 April 2018, the Board of Statutory Auditors issued its Observations on the Bank's Restructuring Plan, as well as the report prepared by the Internal Audit Department on the controls carried out on the major outsourced departments, any deficiencies found and the consequent corrective measures adopted for the year 2017.

Finally, pursuant to Article 2408 of the Italian Civil Code, we declare that in 2018, no complaint from Shareholders or any other complaints were received, no wrongdoing or other significantly negative acts or omissions were reported by the Independent Auditors or others, that required reporting to the Bank of Italy.

Part Three: supervision of the financial statements

In this section we report on our control activities related to the preparation and drafting of the financial statements of Banca Sistema S.p.A. for the year ended 31 December 2018.

The Financial Statements have been drafted in accordance with the International Financial Reporting Standards (IAS/IFRS), as endorsed by the European Commission and transposed in Italy by Legislative Decree 38 of 28 February 2005, while also considering the instructions issued by the Bank of Italy with Circular 262 of 22 December 2005, as amended.

Pursuant to Legislative Decree 39/2010, the person or entity responsible for the independent audit of the accounts must give an opinion on the financial statements as to whether they comply with the laws and regulations governing their preparation and whether they give a true and fair view of the capital financial position, the cash flows and the profit and loss for the year. In this regard, KPMG S.p.A. ("KPMG") exchanged material information with the Board of

Statutory Auditors pursuant to Article 2409-septies and issued its own audit report on the financial statements at 31 December 2017 today. The report does not contain any objections or censures.

Therefore, the Board of Statutory Auditors assumes that the financial data correspond to the data resulting from the internal accounts, which are regularly kept in compliance with the principles set out in current regulations.

That said, the Board of Statutory Auditors has monitored activities to ensure that the general process of preparing and drafting the financial statements complies with current laws and regulations.

The Statement of Financial Position contained in the financial statements submitted for approval to the Shareholders' Meeting is summarised as follows (in thousands of Euro):

Assets…………………………………………………………………...3,150,153

Liabilities………..……………………………..2,994,775

Capital and reserves………………………………………………………… 127,307

Profit for the year………………………………………………………….28,071

The reclassified Income Statement shows the following, summary values (in Euro):

Total income………………………………………………………………..91,272,044

Net impairment losses on loans and receivables……………….....................(6,814,326)

Operating costs (administrative expenses and other income / expenses) …(40,939,574)

Net impairment losses on property and equipment/intangible assets…………(404,131)

Net accruals to provisions for risks and charges…………......………….........(414,040)

Pre-tax profit………………………………………………………………42,699,973

Income taxes………………………………………………………………(14,629,413)

Profit for the year………………………..………………………………...28,070,560

Part Four: relations with the independent auditor

Material information was exchanged during the year with representatives of the Independent Auditors, KPMG so that it could perform its duties during the periodic meetings held pursuant to Article 150 of the Consolidated Law on Finance. These did not reveal any critical and/or significant problems.

In compliance with Article 6, paragraph 2), letter a) of European Regulation 537/2014 and paragraph 6 of the international standard in auditing (ISA Italia) 260, KPMG has certified that, during the period between 1st of January 2018 and today's date, it found no situations compromising the independence of the Independent Auditors or causes for incompatibility.

KPMG has also informed the Board of Statutory Auditors that the independent audit carried out as at 31 December 2018 did not reveal significant shortcomings in the internal control system related to the financial reporting process that needed to be brought to the attention of the Board of Statutory Auditors.

There are no other engagements that have been awarded to the independent auditors and/or to entities belonging to its "network".

Part Five: Adherence to the Corporate Governance Code

The Bank adheres to the Corporate Governance Code of the Corporate Governance Committee for listed companies. Information about certain essential elements is provided as follows.

Internal Control Committee

Banca Sistema S.p.A. has its own Internal Control and Risk Management Committee, whose current members were appointed by the BoD on 24 May 2018. Mr. Franco Pozzi was nominated and appointed to head the Internal Control Committee. The Committee and the head of the Internal Control Committee meet periodically.

Other Committees

The Appointments Committee, the Remuneration Committee, and the Ethics Committee have been established.

Board of Directors

- The BoD supervises general operating performance, dedicating special attention to situations exhibiting conflicts of interest, giving special consideration to the information received from the CEO and the Internal Control and Risk Management Committee, by periodically comparing the results achieved with those planned.
- The BoD examines and approves transactions having a significant economic, asset and liability, and financial impact, especially in regard to related party transactions.
- The composition of the Board of Directors includes six independent directors.
- The Chairman of the Board of Directors meets the independence requirement pursuant to art. 147-ter, paragraph 4, and art. 148, paragraph 3 of Legislative Decree no. 58 of 24 February 1998, but it also does not meet the provisions of art. 3, criteria for application 3.c.1.b and 3.c.2 of the Self-regulation Corporate Governance Code issued by Borsa Italiana.
- The CEO makes periodic reports to the BoD on his activities in the course of exercising his delegated authority.
- The CEO provides adequate information about the related party transactions whose examination is not reserved to the BoD.

The number of BoD, Internal Control Committee, and all Board committee meetings, and the attendance by the members of the Board of Statutory Auditors are shown in the document "Report on Corporate Governance".

Part Six: disclosure pursuant to Consob Communication no. 1025564 / 2001

This section presents the information required under Consob Communication no. 1025564 of 6 April 2001, as amended. In certain cases, that information has already been reported in other paragraphs of this Report.

- The Company did not execute any atypical or unusual transactions with:
    - Group companies;
    - Related parties;
    - Third parties.

See also page 44 of the Financial Statements for more information in this regard.

- Significant transactions affecting the financial position, and assets and liabilities of the Bank were executed, and they have been illustrated in the financial statements.
- Ordinary / recurring transactions were executed with related parties, as described (with reference to them for reading) on page 44 and pages 179-181 of the Financial Statements. In this regard, we inform you that they have always been appropriate and in the Bank's interest.
- The directors have explicitly stated the company's interest in execution of the transactions in their report on operations.
- The organisational structure of the Bank was revised during 2018. The actions approved by the BoD and subsequently implemented to improve the organisational structure have been illustrated.
- The orders issued by the company to its subsidiaries pursuant to Article 114, paragraph 2 of the Consolidated Law on Finance are considered adequate.
- The Board of Statutory Auditors has exchanged the required information with the corporate bodies of the subsidiary L.A.S.S. s.r.l., with no significant issues having arisen.
- The organisational structure has been found to be adequate in regard to the matters under the responsibility of the Board of Statutory Auditors.
- The internal control system has been found adequate, just as has been the administrative and accounting system. This is deemed to give a reliable and fair presentation of operating events.
- Please refer to "Part Two" of this Report for other assessments, observations and comments.
- No omissions, wrongdoing or irregularities have been found during supervisory activity.
- It is not considered necessary to make proposals to the shareholders' meeting in regard to the financial statements and their approval, aside from those approved by the Board of Directors and transcribed in the "summary and conclusions".
- The Board of Statutory Auditors has not had to exercise its powers to call the shareholders' meeting or the BoD.
- Pursuant to paragraph 2, sub-paragraph 2 of the Consob Communication, the following details are noted:

- the transactions indicated in paragraph 2, sub-paragraph 2, in paragraph 2, sub-paragraph 2.1, and in paragraph 2, sub-paragraph 2.2 of Consob Communication no. 1025564 of 6 April 2001. No atypical and/or unusual transactions were executed, including intercompany transactions or related party transactions. Consequently, no additional description needs to be given in this regard;
- the transactions indicated in paragraph 2, sub-paragraph 2.3 of the Consob Communication: as previously mentioned, reference is made to the reading of pages 44, 179, 180 and 181 of the Financial Statements.

***

Summary and conclusions

Dear Shareholders of Banca Sistema S.p.A.,

on the basis of the foregoing report and given what has been brought to the attention of the Board of Statutory Auditors, and what has been confirmed by its periodic controls, it is believed that no reasons exist not to approve the draft financial statements of Banca Sistema at 31 December 2018, as drafted and proposed to you by the Board of Directors, and consequently approve the distribution of dividends.

The Board of Statutory Auditors has also taken note of and brings to your attention the contents of the report of the Independent Auditors KPMG, issued pursuant to Article 14 of Legislative Decree 39/2010 and Article 10 of EU Regulation no. 537 of 16 April 2014, which shows that the financial statements have been clearly written and give a true and fair view of the operating result, assets and liabilities, financial position and cash flows of the Bank, the “additional report” prepared in accordance with Article 11 of EU Regulation no. 537/2014, and the result of the exchanges of information with the Independent Auditors, who have confirmed their own independence, have not found material errors, believe that the books are properly kept, and confirm that there are no material aspects requiring a report to the governance bodies.

Consequently, and notwithstanding all the references to the individual paragraphs of the Financial Statements previously made in this Report, the Board of Statutory Auditors asks you to approve the proposal of the Board of Directors of Banca Sistema S.p.A., which is copied here:

"Dear Shareholders,

The financial statements for the period ended 31 December 2018, which we submit for your approval, show a profit of € 28,070,559.59.

We recommend the following distribution of profits:

- *a dividend of € 6,996,631.52;*
- *the remainder of € 21,073,928.07 to retained earnings.*

No provision to the Legal Reserve is made since the limits set out in Article 2430 of the Italian Civil Code have been reached".

***

Milan, 27 March 2019

Board of Statutory Auditors

Massimo Conigliaro	Lucia Abati	Biagio Verde
Chairman	*Standing Auditor*	*Standing Auditor*

INDEPENDENT AUDITORS' REPORT

KPMG S.p.A.
Revisione e organizzazione contabile
Via Vittor Pisani, 25
20124 MILANO MI
Telefono +39 02 6763.1
Email it-fmauditaly@kpmg.it
PEC kpmgspa@pec.kpmg.it

(Translation from the Italian original which remains the definitive version)

Independent auditors' report pursuant to article 14 of Legislative decree no. 39 of 27 January 2010 and article 10 of Regulation (EU) no. 537 of 16 April 2014

To the shareholders of
Banca Sistema S.p.A.

Report on the audit of the separate financial statements

Opinion

We have audited the separate financial statements of Banca Sistema S.p.A. (the "bank"), which comprise the statement of financial position as at 31 December 2018, the income statement and the statements of comprehensive income, changes in equity and cash flows for the year then ended and notes thereto, which include a summary of the significant accounting policies.

In our opinion, the separate financial statements give a true and fair view of the financial position of Banca Sistema S.p.A. as at 31 December 2018 and of its financial performance and cash flows for the year then ended in accordance with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05 and article 43 of Legislative decree no. 136/15.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISA Italia). Our responsibilities under those standards are further described in the "*Auditors' responsibilities for the audit of the separate financial statements*" section of our report. We are independent of the bank in accordance with the ethics and independence rules and standards applicable in Italy to audits of financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the separate financial statements of the current year. These matters were addressed in the context of our audit of the separate financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Classification and measurement of loans and receivables with customers recognised under financial assets measured at amortised cost

Notes to the separate financial statements "Part A - Accounting policies": section A.2. "Information on the main items of the separate financial statements": "Financial assets measured at amortised cost"

Notes to the separate financial statements "Part B - Information on the statement of financial position - Assets": section 4 "Financial assets measured at amortised cost"

Notes to the separate financial statements "Part C - Information on the income statement": section 8.1 "Net impairment losses due to credit risk related to financial assets measured at amortised cost: breakdown"

Notes to the separate financial statements "Part E - Information concerning risks and related hedging policies": Section 1 "Credit risk"

Key audit matter	Audit procedures addressing the key audit matter
Loans and receivables with customers at 31 December 2018 amount to €2,745 million, accounting for 87% of total assets. The bank's core business is the acquisition of performing receivables from companies that supply goods and services, mainly due from the public administration (the "factoring receivables"), and salary- or pension-backed loans (the "S/P-B loans"). At 31 December 2018, the factoring receivables and the S/P-B loans amount to €1,567 million and €652 million, respectively. Net impairment losses on loans and receivables with customers recognised in profit or loss during the year totalled €6.8 million. For classification purposes, the bank's directors make analyses that are sometimes complex in order to identify those positions that show evidence of impairment after disbursement and/or acquisition. To this end, they consider both internal information about the performance of exposures and external information about the reference sector and borrowers' overall exposure to banks. Measuring loans and receivables with customers is a complex activity, with a high degree of uncertainty and subjectivity, with	Our audit procedures included: — gaining an understanding of the banks' processes and IT environment in relation to the disbursement, acquisition, monitoring, classification and measurement of loans and receivables with customers; — assessing the design and implementation of controls and performing procedures to assess the operating effectiveness of material controls, especially in relation to the identification of exposures with indicators of impairment and the calculation of impairment losses; — analysing the classification criteria used for allocating loans and receivables with customers to the IFRS 9 categories (staging); — analysing the individual and collective impairment assessment policies and models used and checking the reasonableness of the main assumptions and variables included therein; we carried out these procedures with the assistance of experts of the KPMG network;

Key audit matter	Audit procedures addressing the key audit matter
respect to which the bank's directors apply valuation models that consider many quantitative and qualitative factors, including historical collection flows, expected cash flows and related estimated collection dates, the existence of any indicators of impairment, the borrower's estimated repayment ability, an assessment of any guarantees, the impact of macroeconomic variables, future scenarios and risks of the sectors in which the bank's customers operate. For the above reasons, we believe that the classification and measurement of loans and receivables with customers recognised under financial assets at amortised cost are a key audit matter.	— selecting a sample of exposures tested collectively, checking the application of the measurement models applied and checking that the impairment rates applied complied with those provided for in such models; — selecting a sample of exposures tested individually and checking the reasonableness of the indicators of impairment identified and of the assumptions about their recoverability, including considering the guarantees received; — analysing the significant changes in the financial asset categories and in the related impairment rates compared to the previous years' figures and discussing the results with the relevant internal departments; — assessing the appropriateness of the disclosures about loans and receivables with customers recognised under financial assets measured at amortised cost.

Recognition of default interest on performing loans and receivables with customers acquired without recourse pursuant to Legislative decree no. 231 of 9 October 2002

Notes to the separate financial statements "Part A - Accounting policies": section A.2. "Information on the main items of the separate financial statements"

Notes to the separate financial statements "Part C - Information on the income statement": section 1 "Interest"

Notes to the separate financial statements "Part E - Information concerning risks and related hedging policies": paragraph 1.1 "Credit risks"

Key audit matter	Audit procedures addressing the key audit matter
The bank's directors have recognised default interest accrued on performing loans and receivables with customers acquired without recourse and not yet collected pursuant to Legislative decree no. 231 of 9 October 2002 on an accruals basis ("default interest") since the separate financial statements at 31 December 2016. Default interest recognised on an accruals basis in 2018 amounts to €18.1 million and	Our audit procedures included: — gaining an understanding of the bank's processes and IT environment in relation to the estimation of default interest; — assessing the design and implementation of controls and procedures to assess the operating effectiveness of material controls, especially as regards the estimation of default interest;

Key audit matter	Audit procedures addressing the key audit matter
accounts for 18% of the bank's interest and similar income. The bank's directors estimate recoverable default interest using models based on historical recovery percentages and the actual collection times observed internally. These analyses are regularly updated following the progressive confirmation of the historical figures. The above estimate is highly uncertain and subjective and feeds the analysis models that consider many quantitative and qualitative factors, including historical collection flows, expected cash flows, the related actual collection times and the impact of risks of the sectors in which the bank's customers operate. For the above reasons, we believe that the recognition of default interest is a key audit matter.	— analysing the default interest estimation models used and checking the reasonableness of the main assumptions and variables included therein; we carried out these procedures with the assistance of experts of the KPMG network; — assessing the appropriateness of the disclosures about default interest.

Responsibilities of the bank's directors and board of statutory auditors ("Collegio Sindacale") for the separate financial statements

The directors are responsible for the preparation of separate financial statements that give a true and fair view in accordance with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38/05 and article 43 of Legislative decree no. 136/15 and, within the terms established by the Italian law, for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The directors are responsible for assessing the bank's ability to continue as a going concern and for the appropriate use of the going concern basis in the preparation of the separate financial statements and for the adequacy of the related disclosures. The use of this basis of accounting is appropriate unless the directors believe that the conditions for liquidating the bank or ceasing operations exist, or have no realistic alternative but to do so.

The *Collegio Sindacale* is responsible for overseeing, within the terms established by the Italian law, the bank's financial reporting process.

Auditors' responsibilities for the audit of the separate financial statements

Our objectives are to obtain reasonable assurance about whether the separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA Italia will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these separate financial statements.

As part of an audit in accordance with ISA Italia, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- identify and assess the risks of material misstatement of the separate financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the bank's internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors;
- conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the separate financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the bank to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the separate financial statements, including the disclosures, and whether the separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance, identified at the appropriate level required by ISA Italia, regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with the ethics and independence rules and standards applicable in Italy and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the separate financial statements of the current year and are, therefore, the key audit matters. We describe these matters in our auditors' report.

Other information required by article 10 of Regulation (EU) no. 537/14

On 27 April 2010, the bank's shareholders appointed us to perform the statutory audit of its separate and consolidated financial statements as at and for the years ending from 31 December 2010 to 31 December 2018.

We declare that we did not provide the prohibited non-audit services referred to in article 5.1 of Regulation (EU) no. 537/14 and that we remained independent of the bank in conducting the statutory audit.

We confirm that the opinion on the separate financial statements expressed herein is consistent with the additional report to the *Collegio Sindacale*, in its capacity as audit committee, prepared in accordance with article 11 of the Regulation mentioned above.

Report on other legal and regulatory requirements

Opinion pursuant to article 14.2.e) of Legislative decree no. 39/10 and article 123-bis.4 of Legislative decree no. 58/98

The bank's directors are responsible for the preparation of a report and a report on corporate governance and ownership structure at 31 December 2018 and for the consistency of such reports with the related separate financial statements and their compliance with the applicable law.

We have performed the procedures required by Standard on Auditing (SA Italia) 720B in order to express an opinion on the consistency of the directors' report and the specific information presented in the report on corporate governance and ownership structure indicated by article 123-bis.4 of Legislative decree no. 58/98 with the bank's separate financial statements at 31 February 2018 and their compliance with the applicable law and to state whether we have identified material misstatements.

In our opinion, the directors' report and the specific information presented in the report on corporate governance and ownership structure referred to above are consistent with the bank's separate financial statements at 31 December 2018 and have been prepared in compliance with the applicable law.

With reference to the above statement required by article 14.2.e) of Legislative decree no. 39/10, based on our knowledge and understanding of the entity and its environment obtained through our audit, we have nothing to report.

Milan, 27 March 2019

KPMG S.p.A.

(signed on the original)

Alberto Andreini
Director of Audit

FINANCIAL STATEMENTS AS AT 31 DECEMBER 2018

BANCA SISTEMA
CONTEMPORARY BANK