Siena, Rocca Salimbeni,
sede storica della Banca Monte dei Paschi di Siena

MPS
CAPITAL SERVICES

FINANCIAL STATEMENTS 2018

FINANCIAL STATEMENTS AT 31 DECEMBER 2018

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Company Profile

Name	**MPS CAPITAL SERVICES BANCA PER LE IMPRESE S.p.A.** "Monte dei Paschi di Siena" Banking Group
General Information	MPS Capital Services Banca per le Imprese SpA (MPSCS) is the Corporate & Investment Bank of the Monte dei Paschi di Siena Banking Group (MPS Group), specialised in financial support and advice to the Corporate, Public Bodies and Institutional segment. It is registered as a Joint Stock Company in the Florence Companies Register from 4 September 2007, with No. 00816350482, Registered in the Bank of Italy List of Banks with No. 4770, a subscriber to the Interbank Deposit Protection Fund and to the National Guarantee Fund. It is a signatory to the Banking and Financial Sector Code of Conduct. It also participates in the Banking and Financial Ombudsman (ABF) through the Bank of Italy, and the Financial Dispute Arbitrator (ACF) through CONSOB, and the Italian Bank Reconciliation Body. It is subject to the direction and coordination of Banca Monte dei Paschi di Siena SpA (BMPS). In particular the Bank is obliged to observe the rules that the Parent Company issues for the execution of the instructions provided by the Bank of Italy in the interest of the group's stability. The duration of the company is until 31 December 2050.
Year of constitution	**1954** as Mediocredito Regionale della Toscana
Share Capital	€ **1,669,516,282.10** fully paid-up.
Registered Offices	**Florence** - Via Pancaldo, 4 - 50127
General Management	**Florence** - Via Panciatichi, 48 - 50127 Telephone +39 055 2498.1 - Fax +39 055 240826 Website www.mpscapitalservices.it
Other General Management Offices	**Siena** - Viale G. Mazzini, 23 - 53100 Telephone +39 0577 209111 - Fax +39 0577 209100 **Rome** - Via Salaria, 231 (villino 2) - 00199 Telephone +39 06 42048325 - Fax +39 06 42016914 **Milan** - Via Ippolito Rosellini, 16 - 20124 Telephone +39 02 697 05571 - Fax +39 02 882 33205
Market Supervisory Structures	**Milan** - Via Ippolito Rosellini, 16 - 20124 Telephone +39 02 888 91941/30 - Fax +39 02 882 33206 (electronic channels, e-trade) Telephone +39 02 888 91945/43/31/28/24/21 Fax +39 02 882 33205 (Financial Institutions) Telephone +39 02 888 91934 - Fax +39 02 88233205 (Corporates) Ref. NORTH WEST Territorial Area

Siena - Viale G. Mazzini, 23-53100
Telephone +39 0577 537326 - Fax +39 0577 209505
(electronic channels, execution)
Telephone +39 0577 537150 - Fax +39 0577 209505 (Corporates)
Ref. TUSCANY Territorial Area
Telephone +39 0577 537151/56/62 - Fax +39 0577 209505
(Entities and Institutional Bodies)

Rome - Via Salaria, 231 (Villino 2) - 00199
Telephone +39 06 424 50714 - Fax +39 06 420 48337 (Corporates)
Ref. CENTRE AND SARDINIA Territorial Area, SOUTH AND SICILY Territorial Area

Padua - Piazzetta Turati, 2 (Torre Est) - 35131
Telephone +39 049 804 6106 - (Corporate)
Ref. NORTH EAST Territorial Area

Territorial Centres

North West

Milan (**head office**) - c/o Banca Monte dei Paschi di Siena
Largo Cairoli, 1 - 20123
Telephone +39 02 882 33210 - Fax +39 02 882 33233

Turin - c/o Banca Monte dei Paschi di Siena
Corso Filippo Turati, 43 - 10128
Telephone +39 011 192 17629 - Fax +39 055 240826

Mantua - c/o Banca Monte dei Paschi di Siena
Via Vittorio Emanuele II°, 30 - 46100
Telephone +39 049 699 2067

North East

Padua (head office) - c/o Banca Monte dei Paschi di Siena
Piazzetta Turati, 2 - 35131
Telephone +39 049 699 1513 - Fax +39 049 699 2195

Bologna - c/o Banca Monte dei Paschi di Siena
Viale della Repubblica, 23 - 40127
Telephone +39 049 6991659 - Fax +39 055 240826

Tuscany

Florence (head office)
Via Panciatichi 48 - 50127
Telephone +39 055 2498.111 - Fax +39 055 240826

Siena -Viale G. Mazzini, 23 - 53100
Telephone +39 0577 209111 - Fax +39 055 240826

Centre and Sardinia

Rome (head office)
Via Salaria (villino 2) 231 - 00199
Telephone +39 06 673 45313 - Fax +39 06 673 45330

Ancona - c/o Banca Monte dei Paschi di Siena
Via 1° Maggio, 70/d - 60131
Telephone +39 071 2912735 - Fax +39 055 240826

Perugia - c/o Banca Monte dei Paschi di Siena
Via Pietro Cestelini, 13 - 06135
Telephone +39 06 673 45313 - Fax +39 06 673 45330

South and Sicily

Naples (head office) - c/o Banca Monte dei Paschi di Siena
Via Cervantes de Savaedra, 55/14 - 80133
Telephone +39 081 778 5243 - Fax +39 055 240826

Bari - c/o Banca Monte dei Paschi di Siena
Via Nicolò Dall'Arca, 22 - 70121
Telephone +39 080 522 6244 - Fax +39 055 240826

Catania - c/o Banca Monte dei Paschi di Siena
Piazza della Repubblica, 32/38 - 95131
Telephone +39 081 778 5243 - Fax +39 055 240826

Other administrative offices

Rome c/o Banca Monte dei Paschi di Siena
Via Pedicino, 5 - 00156
Telephone +39 06 42048320 - Fax +39 06 42016914

Padua - c/o Banca Monte dei Paschi di Siena
Piazzetta Turati, 13 - 35131

Corporate Officers and Auditing Company

BOARD OF DIRECTORS

Chairperson	*Mario COMANA*
Deputy Chairperson	*Angelo BARBARULO*
Managing Director	*Giampiero BERGAMI*[1]
Director	*Paola DEMARTINI*
Director	*Lucia SAVARESE*
Director	*Riccardo TISCINI*
Director	*Vittorio CALVANICO*
Director	*Ilaria Maria DALLA RIVA*[2]
Director	*Renzo Filippo Riccardo QUAGLIANA*

BOARD OF STATUTORY AUDITORS

Chairperson	Graziano GALLO
Regular Auditor	Werther MONTANARI
Regular Auditor	Lara ZAMPIERO
Alternate Auditor	Marco TANINI

MANAGEMENT

General Manager	*Emanuele SCARNATI*

AUDITING COMPANY

ERNST & YOUNG S.P.A.
Via Po, 32
00198 ROME
VAT No. 00891231003

(1) On 1 January 2019, Mr Giampiero Bergami resigned from the position of Managing Director. At the moment, the position remains vacant.
(2) On 14 February 2019, Ms Ilaria Dalla Riva resigned from the BoD.

Ratings

The following ratings were assigned to the Bank by Moody's Investors Service Ltd for financial year 2018:

LONG-TERM DEPOSITS RATING: **B1**
SHORT-TERM DEPOSITS RATING: **Not Prime**
FINANCIAL STRENGTH RATING: **caa1**

with **stable** outlook.

The international ratings agency **Moody's** revised its assessment of creditworthiness for the Sovereign Entity Italy downwards by one notch, with a rating of **Baa3**, although with a stable outlook. Even in this context, the rating on the financial strength of the MPS Group and of the Bank remained unchanged at **caa1**. The rating on long-term deposits was confirmed at **B1**.
However, in its first 2019 "Credit Opinion", Moody's decided to change the Bank's outlook, taking it from **stable** to **negative**, thus aligning it with the Parent Company's outlook, which was downgraded at the end of 2018.

Shareholding Structure

Banca Monte dei Paschi di Siena controls the company with an equity investment equal to 99.993% as of 31 December 2018, as shown in the table below:

Shareholder	*Number of shares*	*Percentage*
Banca Monte dei Paschi di Siena SpA	802,495	99.993%
I.N.A.I.L.	23	0.003%
Other shareholders	33	0.004%
Total	**802,551**	**100.000%**

REPORT ON OPERATIONS

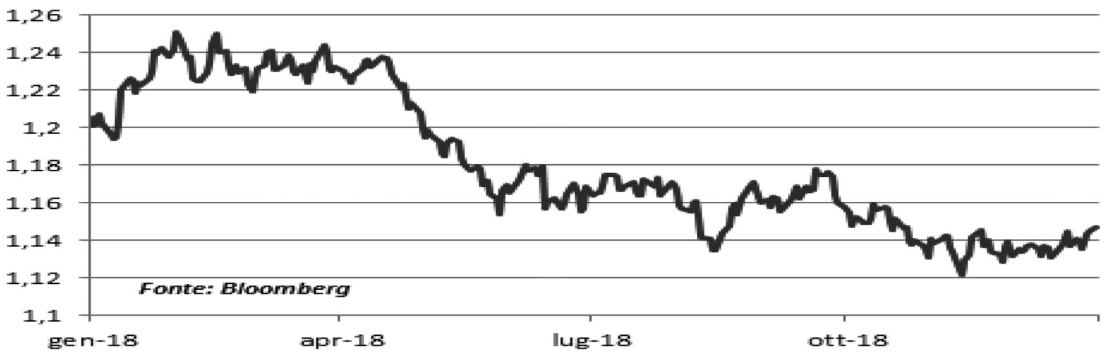
Reference Context

2018 was characterised by robust growth at the global level and by a limited rise in inflation. On the Central Banks front, while the ECB, the BoJ and the BoE continued to maintain an accommodating attitude, the Fed continued the process of normalising monetary policy raising the rates - with four rises during 2018 - up to 2.25%-2.50% and reducing its balance sheet (Quantitative Tightening). In December, the **ECB** terminated the securities purchasing programme (Quantitative Easing), stressing, however, that the rates will remain low at least up to next summer and, in any case, until the target on prices has been reached and that reinvestment of securities maturing will continue also after the rate rise. The macro data did not have a determining effect on the trend in government rates which was driven mainly by events of a political nature (trade war, Brexit, Italian crisis).

On the **macroeconomic front** for the IMF, the final figures for 2018 should show global GDP growth at 3.7% from the 3.8% of 2017. In the USA, growth should come out at 2.9% from the 2.2% of 2017 and in the Euro Area at 1.8% from 2.4%. **Inflation** did not rise as the market expected, owing mainly to a drop in the price of oil towards the end of the year. In the Euro Area, 2018 ended with total inflation at 1.7% (from 1.5% in 2017), remaining below the target of 2% and with core inflation at 1%. **On the rate front**, we saw a divergence between the German and the American ten-year rate (usually with related trends), such as to take the spread up to 280 bps. After a beginning of the year in harmony, starting from February we saw in fact a change of direction of the ten-year *Bund* rate, while the ten-year Treasury rate continued on its upward trend reaching around 3.25%, with marked flattening of the curve on 2-10 years (10 bps from the 78 bps reached in February). The movement of the US rates was determined by the launch of the tax reform at the beginning of the year, by the lower purchases by foreign investors (China and Japan above all) and by the unexpected aggressiveness of the Fed faced with particularly strong US growth. The trend came back down in the last months of the year owing to the exacerbation of the commercial tensions and the excessive aggressiveness of the Fed, which affected the sentiment. The **German ten-year** rate, apart from a brief spike to 0.8% at the beginning of the year, trended downwards for the whole of 2018, ending the year just above 0.20% in the face of an increase in political risks, the sharp drops in share prices and the deteriorating macro scenario. First the formation of the new government in Italy, then the clash with the EU on the new budget law pushed the **Italian ten-year** rate above 3.5% and the spread with Germany above 300 bps (from 123pb at the end of April). Also in this case, the trend came back down, when in the autumn an outline agreement was reached between the government and the European Commission.

On the **currency front**, 2018 saw generalised strength of the dollar, which rose against almost all currencies at the global level and in particular against those of the emerging area. After a beginning of the year marked by weakness, associated with fears of the twin deficits (in particular with the impact of the tax reform on the US deficit), the greenback began to regain strength at the moment in which operators came back to concentrating on the differences in growth and rates in a context of greater fears about a possible trade war with China. The rise was subsequently boosted by the continuation of the normalisation of monetary policy by the Fed and, in particular, with the acceleration of the pace of reduction of its balance sheet (Quantitative Tightening). Thus, the euro/dollar exchange rate, after pushing up at the beginning of the year to around 1.25, ended 2018 just below 1.15.

EURO/DOLLARO



With reference to the **equity markets**, 2018 was a difficult year, owing in particular to the high sales that affected the exchanges in the last quarter. In the **USA,** the main indices recorded new record highs during the year but the strong sell-off toward the end of 2018 reduced the increases. The S&P 500 index lost 6.2%, the NASDAQ 100 1% and the Dow Jones 5.6%. In **Europe**, the performance was much worse, with the Euro Stoxx back to its lowest since 2016, ending the year down 14.8%. Things went badly also on Piazza Affari where the FTSE MIB lost 16.2%, but the worst was the German Dax (-18.3%), which more than others suffered the Chinese slowdown and the threat of duties on cars. Additionally, in **Asia**, the situation was not much better with the Japanese Nikkei, which fell 12.1%, even though, during the year, it had reached the highest levels since 1991. The **emerging** index MSCI EM dropped 16.6%. However, not everything was negative in the emerging world because, in Brazil, the Bovespa gained 15% in the wake of the election of President Bolsonaro, and in India, the Sensex gained 5.9%. It was, however, a negative year for China, with the Shanghai Composite down 24.6%, at its lowest since 2014.

Significant Aspects of Operations

The "Business Units" (hereinafter BUs) were unchanged with respect to the previous year and serve as the basis of supervision and operational monitoring of the Bank's business. They are listed below:

"Ordinary Finance" BU
"Corporate Finance" BU
"Global Markets" BU
"Investment Banking" BU

"Ordinary Finance" BU

As regards the "Ordinary Finance" BU, both agreements and disbursements were less (respectively: -56.0% and -55.4%) than those achieved the previous year, due to the Bank's increasingly decisive strategic repositioning in terms of structured, extraordinary and project finance.

(amounts in millions of Euro)

Ordinary Finance	*Final figure at 31/12/2018*	*Final figure at 31/12/2017*	*Percentage changes*
Operations agreed	3.7	8.4	(56.0%)
Transactions disbursed	7.0	15.7	(55.4%)

As regards the Subsidised Finance segment, the Bank continued the activity of "Manager" of a number of the main national public incentives for productive activities on behalf of the Ministry for Economic Development, in particular: Sustainable Growth Fund and Guarantee Fund for SMEs.
The service of "Authorised Bank" was also launched by the Italian Ministry of Agricultural, Food, Forestry and Tourism Policies, in relation to the incentives for Supply Chain Contracts in the agricultural and agri-food sector.

"Corporate Finance" BU

During 2018, the activity of the Corporate Finance BU showed a trend marked by volumes of both agreements and disbursements in rapid expansion compared to the levels of the previous year, recording +83.0% for the former and +64.4% for the latter.
The strategy of concentrating the Bank's "operating focus" on structure and project finance remains, in practice, substantially unchanged as regards the activity related to the lending segment, through granting credit to companies and/or initiatives of particular interest and significance.
Actions aimed at optimising interaction with the Parent Company's commercial unit continued throughout the year, to the extent that it is still the priority channel for Corporate Finance operations both agreed (about 55% of the total) and disbursed (more than 63% of the total).

(amounts in millions of Euro)

Corporate Finance	*Final figure at 31/12/2018*	*Final figure at 31/12/2017*	*Percentage changes*
Transactions agreed	1,170.4	639.7	83.0%
Transactions disbursed	1,016.0	618.0	64.4%

A summary of the activities performed by the single departments into which the Corporate Finance BU is divided is presented below:

- **Project Financing** - In 2018 the Bank confirmed its positioning among the leading banks in Italy for loans in the sector of renewable energies and infrastructures on a project financing basis, and in the real estate sector with important actions catering mainly for qualified institutional customers (for example: Real Estate Funds).
  In consideration of their complexity, the structuring of loans needs medium-long finalisation times; consequently, the closings of the operations regarded both mandates acquired during the year and mandates acquired previously.
  We can note, with reference to financial year 2018, the following most significant operations:
    - financing of the significant investment plan promoted by Open Fiber - a partnership between CDP Equity and Enel - destined for the development of ultra-wideband fibre optics at the national level with the related infrastructures. The investment of a total of € 6,300 million, of significant importance for our country, is supported by public grants for approximately € 1,400 million, while the remaining € 4,900 million is chargeable to the private operator which entered into a loan divided into several cash and endorsement lines for a total of € 3,470 million in which the leading Italian and European banks participate (our cash portion: € 125 million);
    - bridge loan in favour of Arexpo, a hub set up for the transformation of the Expo Milano 2015 exhibition site into a science, health and innovation park. The financial loan was granted through a Temporary Grouping of Companies (TGC) set up under the terms of the Contracts Code with 3 other banks besides our own. The operation for a total amount of € 210 million (our share: 50 million) will be the subject of future consolidation in a medium/long-term action;
    - loan in favour of Fondo Opportunità Italia, a closed-end real estate fund, intended for retail customers managed by Torre SGR and listed on the Italian Stock Exchange in the MIV segment, owner of various commercial and executive investment properties in Bologna, Rome and Milan, and in a luxury outlet complex in the province of Florence. The loan, for a total of € 85 million, divided into several cash lines, was granted entirely by our bank and is for the purpose of enabling further acquisitions in prestigious properties (for executive use, hotels, shopping centres etc.) in the metropolitan areas of Milan and Rome;
    - refinancing of 5 contiguous photovoltaic plants, already connected to the national electricity grid, implemented through the establishment of 5 vehicle companies, controlled by the main British investor in the photovoltaic sector, Octopus Investments, for 63 MWp of power, located in the province of Viterbo. The loan operation, for a total of € 23 million entirely subscribed by our bank, was the first in Italy to be structured on the basis of market parity in the sector of renewable energies;
    - refinancing of a portfolio of photovoltaic plants originating from several industrial operators and acquired by a special purpose vehicle controlled by Tages Helios, a closed-end real estate fund aimed at professional investors, and Delos Power, created by the partnership between Tages Capital SGR and Renam S.r.l. These are plants located in various regions (Apulia, Sicily, Marche and Emilia Romagna) for approximately 140 MWp of power; the operation for a total of € 452 million (our share € 50.5 million) saw the participation of major national and international banks;
    - loan, entered into by the Tozzi Green Group, a leading Italian player in renewable energies, through its subsidiary Solarwind 2, for the creation of 2 wind farms consisting of a total of 15 wind turbines for 18 and 16.5 MW respectively, situated in the Municipalities of Butera (CL) and Siculiana (AG). The operation entirely financed by our bank amounts to a total of € 39.4 million;
    - loan for the completion of a latest-generation data center consisting of a 20,000 sq. m. module divided into sectors completed with equipment located in the province of Pavia. The pool project in which the Bank served as the Mandated Lead Arranger (MLA) amounts to a total of € 91 million (our share € 20 million) and was granted together with 2 other leading international banks.

- **Corporate Finance -** The loan granting activity regarded support to important operators of the Integrated Water Service (IWS), services to businesses (payment system; temporary work, transport), the industrial sector (building materials, electro-mechanical components, pharmaceuticals), shipping, tourism-accommodation, the real estate and construction sector and the media entertainment sector. In particular, among other things, assuming the role of MLA three important loan operations were completed in a pool with other banks, in support of concessionary companies of the IWS operating in the regions Lombardy (Padania Acque and Pavia Acque) and Tuscany (G.A.I.A.), in favour, as the only Lender, of a concessionary company of the IWS in the Sicily Region and in favour, through a loan operation in a pool with other banks, of TSH Bologna Propco (The Student Hotel group); a significant loan operation (in the role of MLA in a pool with other banks) in favour of a leading Italian company in the building sector and an operation, again in a pool with other banks assuming the role of MLA, in favour of a leading Local Public Transport company operating in the Lombardy Region.

- **Acquisition Financing** - Also during 2018 the Bank confirmed its competitive positioning in the activity of acquisitions & leveraged finance in the Mid-Corporate segment for operations distinguished by strong industrial connotations and important commercial impacts for the MPS Group.
  MPSCS in fact continued the activity of origination and structuring of acquisition operations in support of counterparties of leading standing, focusing on industrial integrations carried out by corporate operators and maintaining also a strong presence on the leverage market promoted by the main private equity operators in Italy.
  Among the most important operations organised and financed - as the MLA - we can note the following:
    - acquisition of Uteco Converting - a major Italian operator, market leader in the production and sale of printing machinery for flexible packaging applications - by the private equity operator Neuberger Berman Renaissance Partners (LBO);
    - acquisition of Calligaris - a well-known Italian brand operating in the design, production and distribution of home furniture for the medium/high market segment - by the private equity operator Alpha PE (LBO);
    - acquisition of Emmeti - a major Italian operator, market leader in the manufacture of automatic dosing machines, packaging and packing - by the private equity operator Xenon PE (LBO);
    - acquisition of part of the Total Erg group by API, a major Italian operator, leader in the production and sale of oil refining derivatives (Corporate Acquisition);
    - acquisition of the business unit related to paper processing services and production in central and south-eastern Europe of First Data Corporation by SIA, a major Italian operator, leader at the international level in the design, construction and management of infrastructures and technological services in support of financial institutions and corporate bodies (Corporate Acquisition);
    - acquisition of Aletti SGR and of part of the activities of management of the insurance reserves of the Poste group by Anima Holding in the context of its industrial plan of external growth (Corporate Acquisition).

"Global Markets" BU

During 2018, the activity with customers and that on the markets of the Global Markets and Sales and Financial Solutions Departments was affected, both in volumes and in the quality of flows, by several geopolitical events (Brexit, commercial tensions between the United States and China on the subject of customs duties, the Italian political situation) which, although in a context of robust global growth and a limited rise in inflation, considerably influenced the performance of the various asset classes, generating high volatility and a rise in yields of government securities, in particular Italian ones, with consequent reflections also on the credit spread compared to the other Euro area countries.
As a consequence of this, in the Government bond segment, during the year there was a gradual reduction in the proprietary portfolios trying to optimise the nominal amount of government securities held with the carry matured.

With reference to the activity of Italian Treasury Specialist also in 2018 the activity that in the last few years has brought our Bank into a position of absolute pre-eminence continued. This element made it possible, among other things, to perform also in 2018 important roles in primary syndicate operations as well as in the placing of the new BTP Italia.
The Lending segment, in a market characterised by great illiquidity and a widening of spreads, also recorded a drastic reduction in volumes, both on the markets and with customers. We can note instead the excellent result, in terms of acceptances, of the global voluntary public offering on structured paper launched by BMPS on class A asset-backed securities and class B asset-backed securities issued by Casaforte S.r.l.
With reference to Structuring activity there were good results on the placing of funds with structured investment strategy in commercial collaboration with Anima Asset Management. The production together with Axa MPS Financial of protected unit-linked products continued, and to this was added, during the first half of the year, the structuring of a different non-protected product range.
The increase in structured products placed had a positive effect on the Equity and Fixed Income segments, which benefited from a considerable increase in volumes on retail hedging. In addition, this activity led to important technological and process adjustments in the management of equity risks, in the segment for which, in a certainly difficult market context, excellent overall results were obtained from dynamic risk-warehousing.
The Sales & Financial Solutions Department continued to perform its activity of channelling flows coming from institutional and corporate customers to the entire array of the Bank's business lines. The greater constraints imposed by entry into force of the MiFID II Directive represented one of the factors that contributed to the contraction in terms of volumes, in relation to both institutional customers - with some exceptions related above all to the positive trend in Auctions - and corporate customers, with particular reference, as regards this customer segment, to exchange rate and commodity hedging. Remaining on the subject of corporate customers, it is worth noting the turnaround on interest rate hedging, which recorded an increase of more than 100% compared to the same period for the previous year, as a consequence of considerable growth in medium/long-term lending and the good result on exchange rates with a flexible term.

"Investment Banking" BU

As regards "Investment Banking" activity, among the transactions of greatest significance on the bond market during 2018, the Bank played the role of Joint Lead Manager Bookrunner in the following bond issues: Tier 2 issued by Banca MPS, with maturity at 10 years; BTP Italia 13th issue linked to Italian inflation; CDP Sustainability Bond at 5 years and two High Yield bonds issued by Nexi at both fixed and floating rates, for a total of € 2.2 billion. In addition, it took part as Dealer in two "tender offers" both on a BTP Italia and on a selected panel of CCTs and BTPs on behalf of the Italian Republic for a total of € 7 billion. In addition to these transactions, the Bank took part as Co-Lead Manager in the placing of a nominal BTP at 20 years, of two covered bonds issued by *Credit Agricole* Cariparma for a total of € 2 billion and of an issue of covered bonds of Commerzbank at 7 years for € 500 million.
As regards the equity market, in the same period, the Bank took part in the guarantee consortium in service of the capital increase of Anima Holding, with the role of Joint Global Coordinator and Joint Bookrunner.
The Bank continued to work as Nominated Advisor on behalf of Poligrafici Printing SpA, listed on Borsa Italiana's AIM Italia market.

Credit Aggregates

Commercial flows

In Italy, the macroeconomic scenario in 2018 showed a slowdown in the GDP growth rate, until it recorded a negative sign in the last few surveys, so with the prospect of a potentially recessive scenario that no longer seems capable of sustaining trends of lively expansion. The annual growth figure came out at less than 1%, much lower than the 1.5% recorded in 2017.

However, bucking the trend of negative signs coming from the macro-economic scenario, the Bank achieved commercial volumes up both from the point of view of applications presented and from that of transactions resolved, signed and disbursed, as can be seen from the tables presented below.

LOAN APPLICATIONS SUBMITTED

(amounts in millions of Euro)

	2018	*2017*	*Changes*	
			absolute	*%*
Number	172	176	(4)	(2.3)
Amount	2,181	1,264	917	72.5

LOANS APPROVED

(amounts in millions of Euro)

	2018	*2017*	*Changes*	
			absolute	*%*
Number	144	146	(2)	(1.4)
Amount	1,895	930	965	103.8

The following table shows the ratio between loans agreed (approved) and applications presented:

	2018	*2017*	*2016*	*2015*
Number	83.7%	83.0%	90.4%	89.4%
Amount	86.9%	73.6%	85.7%	98.9%

LOAN CONTRACTS SIGNED

(amounts in millions of Euro)

	2018	*2017*	*Changes*	
			absolute	*%*
Number	230	152	78	51.3
Amount	1,174	648	526	81.2

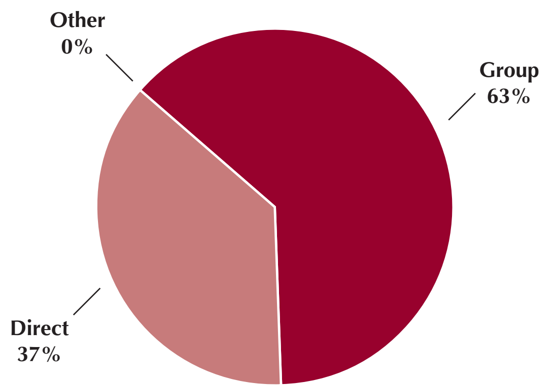
LOANS DISBURSED

(amounts in millions of Euro)

	2018	*2017*	*Changes*	
			absolute	*%*
Number	473	374	99	26.5
Amount	1,023	634	389	61.4

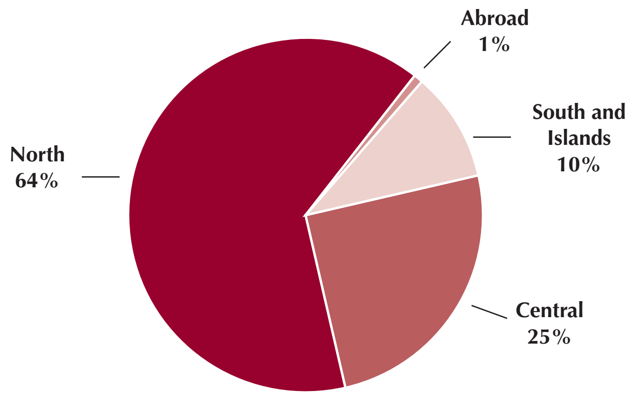
During financial year 2018, the Bank disbursed a total of € 1,023 million. We can note that, also contributing to this result, were disbursements linked to investments to be made over a multi-year period, in accordance with precise terms for implementation set at the time in the production development plans. In these cases, the disbursements are made in several tranches, according to the "state of progress" of the projects financed.
As can be seen from the chart below, 63% of the amounts disbursed during the year related to applications channelled by the Group's network, a percentage up compared to the previous year, when the "Group" channel accounted for 57%.

LOANS ISSUED 2018 - Breakdown by Channel



As regards the geographical distribution of the commercial flows, the next chart demonstrates that 89% of the amounts disbursed in the year were channelled to Northern and Central Italy. Comparing the 2018 figures with those of the previous year, it can be noted that the North's portion rose from 55% to 64%, while disbursements allocated to Central Italy remained substantially unchanged, going from 26% in 2017 to 25% in the year just ended. The South and the Islands decreased from the 15% of 2017 to 10% in financial year 2018, while foreign transactions became even more marginal, going down from 4% in 2017 to 1% today.

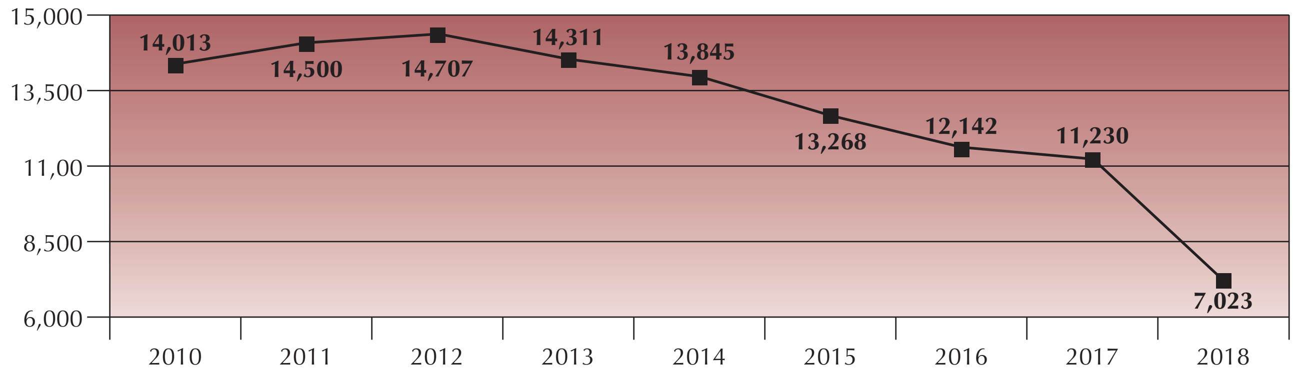
BREAKDOWN OF FINANCING DISBURSED 2018 - Geographical Breakdown



TOTAL LOANS

Loans to customers, determined according to operating criteria, at 31 December 2018 equalled € 7,023 million, down compared to the € 11,230 million recorded at the end of the previous year (-37.46% on an annual basis). The considerable drop in total loans to customers is attributable mostly to the sale of non-performing loans made in June 2018, of which more details are provided in another part of this Report.

TREND IN TOTAL LOANS
"Management" view



The reconciliation of the operating figure for customer loans at 31 December 2018, with the balance of the asset items 20.c "Financial assets obligatorily measured at fair value through profit or loss", 40.b "Financial assets measured at amortised cost - loans to customers" and 110. Non-current assets and groups of assets held for sale", in which customer loans are included, is presented below:

BALANCING BETWEEN "OPERATING" VIEW AND ACCOUNTING FIGURES
(amounts in millions of Euro)

Operating amount	**7,023**
Spreads on past-due derivatives (1)	(49)
Repurchase agreements with customers	3,395
Receivables for collateral paid in (2)	387
Valuation reserve on loans (3)	(1,499)
Other receivables and sundry items	634
Accounting amount (A020c + A040b + A110)	**9,891**

(1) Nominal value of spreads on past-due derivatives, recognised for accounting purposes under item A020a "Financial assets held for trading";
(2) Deposits for collateral paid not connected to financing activities and operationally attributable to "Global Markets" activity;
(3) Provisions related to loan exposures.

The table below shows the breakdown of loans to customers at amortised cost (item 40.b of Assets) by credit quality stages introduced by the accounting standard IFRS 9:

Customer loans at amortised cost	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Gross exposure	6,595,731	2,103,840	2,159,698	10,859,269
Value adjustments	(7,345)	(97,038)	(1,020,886)	(1,125,269)
Net exposure	6,588,386	2,006,802	1,138,812	9,734,000
Coverage ratio	0.11%	4.61%	47.27%	10.36%
% of total loans to customers at amortised cost	67.68%	20.62%	11.70%	100.00%

SALE OF BAD LOANS AND OTHER IMPAIRED EXPOSURES

With reference to initiatives taken to improve credit quality, the MPS Group Restructuring Plan, approved on 4 July 2017 by the European Commission, includes the disposal of almost all the existing bad loan portfolio at 31 December 2016 and the sale, by the end of 2019, of further exposures belonging to the portfolio of probable defaults (PDs), for a total exposure at the Group level of € 4.5 billion.
In relation to the sale of bad loans, in June 2018, following the sale of 95% of junior notes to the Italian Recovery Fund, the securitised portfolio was derecognised.[3] The economic impacts of the operation, for a total amount of €657 million of net write-downs booked to item 130 a) "Net value adjustments for impairment of loans", had been fully recognised in the financial statements for the year ended 31/12/2017.[1] The Bank presents, in the assets of the financial statements, securities deriving from the aforesaid securitisation for the following amounts:

- senior notes classified in item 40b) "financial assets measured at amortised cost - loans to customers" for € 581,177 thousand;
- mezzanine notes classified in item 20c) "financial assets obligatorily measured at fair value through profit or loss", for € 8,959 thousand;
- junior notes classified in item 20c) "financial assets obligatorily measured at fair value through profit or loss", for € 6,434 thousand.

In the previous year, the Bank had already launched the plan for the disposal of the portfolio of Probable Defaults (PDs), completing important transactions for the sale of receivables, and this activity continued in 2018 and will continue in the coming year, thanks also to the activity performed by a "dedicated team" which enabled the Bank to conclude sale contracts for approximately € 430 million. The overall programme was completed through competitive procedures, both for the sale of the receivables and for the selection of the lawyers.

(1) *With respect to the disclosure provided in the Report on Operations of the 2017 financial statements, we must specify that the conditions precedent laid down for the sale of the sub-portfolio related to exposures guaranteed by Fidi Toscana S.p.A. were also not fulfilled, and therefore these receivables (for an amount of approximately € 48 million at the Group level of which € 23.9 referable to the Bank) have remained in the Bank's Assets.*

Impaired exposures

The tables below show the distribution of impaired assets at 31 December 2018 by portfolio (amounts in thousands of Euro).

On-balance-sheet exposure	*Gross exposure*	*Specific adjustments*	*Net exposure*
Financial assets measured at amortised cost	2,159,698	(1,020,886)	1,138,812
Financial assets measured at fair value through other comprehensive income	3,850	(2,430)	1,420
Other financial assets obligatorily measured at fair value	228,590	(161,813)	66,777
Financial assets held for sale	110,712	(58,687)	52,025
Total	**2,502,850**	**(1,243,816)**	**1,259,034**
Total 31/12/2017(*)	**6,834,792**	**(4,308,469)**	**2,526,323**

(*) The Bank utilised the option not to redetermine, on a uniform basis, the comparative data of the year of first application of IFRS 9.

On-balance-sheet exposure	*Gross exposure*	*Specific adjustments*	*Net exposure*
Guarantees given	797	(626)	171
Commitments to disburse funds and other commitments	9,636		9,636
Total	**10,433**	**(626)**	**9,807**

Impaired assets are broken down by type below (amounts in thousands of euro):

Type of on-balance-sheet impaired assets	*Gross exposure*	*Specific adjustments*	*Net exposure*	*Net exposure 2017(*)*
Bad loans	1,146,169	(637,800)	508,369	1,394,751
Probable defaults	1,349,128	(605,048)	744,080	1,112,403
Impaired past-due exposures	7,553	(968)	6,585	19,169
Total	**2,502,850**	**(1,243,816)**	**1,259,034**	**2,526,323**

(*) The Bank utilised the option not to redetermine, on a uniform basis, the comparative data of the year of first application of IFRS 9.

With reference to the loan exposures to customers presented in table A.1.7 of the Notes to the Financial Statements, the balance of on-balance sheet impaired assets, net of value adjustments and discounting, came out at € 1,259 million. The decrease, compared to the amount at 31 December 2017 (€ 2,526 million), was € 1,267 million (-50.15%). This reduction was mostly attributable to the deconsolidation of the bad loan portfolio sold to the securitisation vehicle "Siena NPL 2018 S.r.l.".
Bad loans, mainly for the above reason, went down from € 1,395 million at 31 December 2017 to € 509 million at 31 December 2018 with a reduction of € 886 million (-63.51%). The average write-down of bad loans came out at

55.65% (70.86% at 31 December 2017). Gross and net bad loans represent 7.05% and 3.41%, respectively, of total gross and net exposures to customers shown in table A.1.7 in part E of the Notes to the Financial Statements (21.93% and 7.99% at 31 December 2017).

Probable defaults went from € 1,112 million at 31 December 2017 to € 744 million at 31 December 2018, a reduction of € 368 million (-33.09%). The average write-down of probable defaults came out at 44.85% (45.05% at 31 December 2017). Gross and net probable defaults represent 8.30% and 4.99%, respectively, of total gross and net exposures to customers shown in table A.1.7 in part E of the Notes to the Financial Statements (9.27% and 6.37% at the end of 2017). The reduction recorded was due mostly to the programme for the deleveraging of Unlikely-To-Pay (UTP) exposures implemented by the Group, which, in 2018, at the Bank level, entailed the sale of UTPs for a total Gross Book Value of € 430 million.

Impaired past-due loans went from € 19 million at 31 December 2017 to € 7 million at 31 December 2018, a reduction of € 12 million (-63.16%). The average write-down of past-due loans was 12.82% (20.42% at 31 December 2017). Gross and net past-due receivables represent 0.04% and 0.47% respectively of total gross and net exposures to customers shown in table A.1.7 of part E of the Notes to the Financial Statements (0.11% and 0.11% at the end of 2017).

A number of indicators that offer an overview of the Bank's credit quality are presented below. Unlike what is presented above, these have been calculated, with exclusive reference to the financial assets at amortised cost presented in the Assets under items 40b) "financial assets measured at amortised cost - loans to customers" and 110 "non-current assets and disposal groups held for sale".

Credit quality indices	*31/12/18 (%)*	*31/12/17(*) (%)*	*Changes*
Net impaired loans/Loans to customers	11.7	21.5	(9.8)
Gross NPL ratio (1)	22.3	42.4	(20.1)
Coverage of impaired loans (2)	49.7	63.0	(13.3)
Net non-performing loans/Loans to customers	4.8	11.9	(7.1)
Coverage of non-performing loans (2)	55.6	70.9	(15.3)
Net value adjustments on loans/Loans to customers (3)	-0.2	6.6	(6.8)
Texas Ratio (4)	102.4	121.7	(19.3)

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9.

Note:

(1) Gross NPL ratio: ratio between gross impaired loans to customers and gross loans to customers.

(2) Coverage: the coverage ratio on impaired loans and on bad loans is calculated as the ratio between the related provisions for impairment and the corresponding gross exposures.

(3) Net value adjustments on loans/Loans to customers (provisioning): this is the ratio between net value adjustments on loans and loans to customers.

(4) Texas Ratio: this is the ratio between gross impaired loans and the sum, as denominator, of tangible shareholders' equity (that is net of goodwill and other intangibles) and the provisions allocated to cover the impaired loans.

Deposits

The table below shows the breakdown of deposits (item 10 of Liabilities) by type and by operating segment at 31 December 2018, compared with the situation at the end of the previous year.

As regards lending activity, a contraction of loans and, consequently, of dedicated deposits was also recorded in 2018. The amount of existing deposits and loans payable with the Parent Company to deal with lending, at the end of the year, was in fact down by € 1,824 million and came out at € 6,208 million (€ 8,032 million at 31 December 2017) divided as follows: € 875 million on-demand and short-term (€ 829 million at 31 December 2017), and € 5,333 million medium- and long-term (€ 7,203 million at 31 December 2017).

Funding to cope with the typical activities of the "Global Markets" BU consists both of deposits made by the Parent Company and of repurchase agreements. In particular, short-term deposit-related financial assets held for trading amounted to € 418 million (€ 1,645 million at 31 December 2017), and those at long term amounted to € 577 million (not present at 31 December 2017).
The aggregate "Loans from the Parent Company for "Global Markets" activity - on demand and short term" includes also a time deposit of € 1,549 million (€ 1,375 million at 31 December 2017) made by the Parent Company to guarantee securities lending for its customers.
For comments on trading operations, please see the paragraph "Main financial aggregates" below.

(amounts in millions of Euro)

	31/12/2018	*31/12/2017*
Loans from the Parent Company for Lending activities:		
- on demand and short term	875	829
- medium and long term	5,333	7,203
Loans from the Parent Company for Global Markets activities:		
- on demand and short term	2,290	3,219
- medium and long term	677	100
Funding in repurchase agreements:	10,429	10,072
- of which with Parent Company	*5,482*	*3,221*
Subordinated bonds:	457	457
Other payables to Banks and Customers:	897	966
TOTAL	**20,958**	**22,846**

Main financial aggregates

The main trends that characterised the activity of the Global Markets BU in financial year 2018 are illustrated below:

- the volumes deriving from hedging of interest rate risk with corporate customers, followed by the Corporate Sales Office, were € 1,448 million compared to € 696 million in 2017, an increase of approximately 108% due to the growth in medium/long-term loans disbursed by the Group;
- the volume of interest rate derivatives with institutional counterparties was € 1,847 million (-24% compared to the previous year);
- the volume deriving from hedges of exchange rate risk with corporate customers totalled € 1,910 million, down by approximately 29% compared to 2017. This decrease was partially offset by growth in the volume generated by flexible term operations (+13% compared to the previous year);
- the volume of hedges on commodities with corporate customers totalled € 610 million, a decrease of 13% compared to 2017;
- the volumes deriving from repos decreased by 26% compared to the previous year;
- the volumes traded on the secondary credit market of securities with institutional customers - Over The Counter and via platforms - showed a decrease of approximately 40% compared to 2017 (€ 4,996 million compared to the € 8,339 million of the previous year);
- the volume deriving on the secondary market of government securities - OTC and via platforms - was € 26,242 million, compared to € 34,420 million in the previous year, with a decrease of approximately 24%, partially offset by the higher volumes observed at auctions, which reached € 4,403 million compared to € 2,490 million in the previous year;
- the volumes deriving from placing with institutional investors of primary market securities recorded a 45% decrease compared to 2017 (€ 3,456 million compared to € 6,250 million in the previous year). The comparison with respect to the previous year reflects less recourse to the primary market by the Parent Company.

(amounts in millions of Euro)

Product	*31/12/2018*	*31/12/2017*	*Changes %*
Customer desk interest rate hedging	1,448	696	108%
Institutional interest rate hedging	1,847	2,434	(24%)
Exchange rate hedging	1,910	2,680	(29%)
Commodity hedging	610	699	(13%)
Flexible term	2,095	1,857	13%
Flexible term institutional	26	3	n.a.
Institutional interest rate hedging	147	-	n.a.
Equity hedging	11	140	(92%)
Repos	4,208	5,679	(26%)
ETF	3	49	(93%)
Secondary Credit to institutional customers	4,996	8,339	(40%)
Secondary government securities to institutional customers	26,242	34,420	(24%)
Auctions	4,403	2,490	77%
Primary	3,456	6,250	(45%)
Total	**51,402**	**65,736**	**(22%)**

Note:

these are commercial volumes determined according to operating criteria, aimed at representing the trend of the volumes moved during the year.

Moving on to examine financial aggregates, it can be seen that, with respect to 2017, net amounts of securities held for trading increased by € 133,215 thousand. The increase in the segment of government securities was substantially offset by the reduction in securities of other issuers. In particular, we can note that, during 2018, the securities issued by the vehicle Casaforte S.r.l were sold for a market value of € 986,915 thousand as at 31 December 2017.

(amounts in thousands of Euro)

Trading portfolio	*31/12/2018*	*31/12/2017*	*Changes*	
long position in securities			*Absolute*	*%*
Government and public entity securities (*)	4,488,961	4,253,449	235,512	5.54%
Other	1,507,629	2,639,184	(1,131,555)	(42.88%)
Total securities	**5,996,590**	**6,892,633**	**(896,043)**	**(13.00%)**

(amounts in thousands of Euro)

Trading portfolio	*31/12/2018*	*31/12/2017*	*Changes*	
short position in securities			*Absolute*	*%*
Government and public entity securities (*)	(1,831,646)	(2,868,654)	1,037,008	(36.15%)
Other	(42,314)	(34,564)	(7,750)	22.42%
Total securities	**(1,873,960)**	**(2,903,218)**	**1,029,258**	**(35.45%)**

(amounts in thousands of Euro)

Trading portfolio	*31/12/2018*	*31/12/2017*	*Changes*	
net long position in securities			*Absolute*	*%*
Government and public entity securities (*)	2,657,315	1,384,795	1,272,520	91.89%
Other	1,465,315	2,604,620	(1,139,305)	(43.74%)
Total securities	**4,122,630**	**3,989,415**	**133,215**	**3.34%**

(*) For a detailed analysis of "Sovereign Risk", please see Part E, section 1 "Credit Risk" part A "Credit Quality", of the Notes to the Financial Statements.

The long net position in securities and, in general, the activity of Global Markets is financed for 90% (60% at the end of the previous year) through repurchase agreements. The residual amount is covered with short term deposits payable taken out with the parent company.

Repurchase agreements	*31/12/2018*	*31/12/2017*	*Changes*	
			Absolute	*%*
repurchase agreements	6,742,719	7,751,548	(1,008,829)	(13.01%)
reverse repurchase agreements	(10,428,713)	(10,071,942)	(356,771)	3.54%
Net repurchase agreements	**(3,685,994)**	**(2,320,394)**	**(1,365,600)**	**29.78%**

The other significant portion of Global Markets business is focused on trading in credit and financial derivatives.
As regards credit derivatives, from the comparison between the notional values at 31 December 2018 and those referred to the previous year, there emerges an increase in nominal terms of € 858 million, attributable substantially for € 442 million to protection sales on the Italian state and for € 367 million to derivatives on indices settled at the Central Counterparty ICE Clear Europe (ICE). Existing transactions are exclusively carried out with banking counterparties or with financial companies.

(nominal amounts in thousands of Euro)

Credit derivatives	*31/12/2018*	*31/12/2017*	*Changes*	
			Absolute	*%*
Protection purchases	802,952	622,608	180,345	28.97%
Protection sales	3,003,679	2,325,302	678,377	29.17%

Single-name credit derivatives mainly refer to government securities. For more details on the contraction of protection purchases with Sovereign underlyings, please see the analysis of “Sovereign Risk” presented in Part E, section 1 “Credit risk” part A “Credit Quality”, of the Notes to the Financial Statements.

Credit derivatives underlying single name	*Protection purchases %*	*Protection sales %*
Sovereign	95.56%	99.47%
Banking insurance	4.44%	0.53%

For additional quantitative information, please see Section 3.1 of Part E of the Notes to the Financial Statements.

As regards financial derivatives, below we offer a breakdown expressed both in notional and fair values:

(nominal amounts in thousands of Euro)

Financial derivatives	*31/12/2018*	*31/12/2017*	*Changes*	
			Absolute	*%*
Over the counter	381,358,712	272,292,490	109,066,222	40.05%
Central counterparties	43,080	350,155	(307,075)	(87.70%)
Total	**381,401,792**	**272,642,645**	**108,759,147**	**(51.47%)**

OTC financial derivatives are represented for 96.13% by instruments with underlying “debt securities and interest rates” (93.32% at 31 December 2017). Derivatives on Organised Markets were those taken out with Cassa di Compensazione e Garanzia (CC&G), with equity/stock indices as underlyings.
The carrying amounts at 31 December 2018 are presented below, compared with the previous year. Obviously, listed future-style agreements, whose marginalisations are included directly in the total treasury balances as offset entries in the income statement, are excluded.

(amounts in thousands of Euro)

Financial derivatives (fair value)	*31/12/2018*	*31/12/2017*	*Changes*	
			Absolute	*%*
Positive market value (item 20 of the Assets)	3,339,709	3,572,280	(232,571)	(6.51%)
Negative market value (item 40 of the Liabilities)	(1,537,614)	(1,866,804)	329,190	(17.63%)

We must stress that, in line with application of IAS 32, paragraph 42, both active and passive exposures with “direct”

central counterparties (only CC&G) and with "indirect" access (LCH - London Clearing House, ICE - ICE Clear Europe and central counterparties related to foreign markets which the Bank accesses through Merrill Lynch), are subject to offsetting and the net balance is hence shown in the financial statements. For more information on Clearing, please see section 2.1 in part B of the Notes and the comments found in paragraphs 5 and 6 of the "Other information" section in part B of the Notes to the Financial Statements.
OTC derivatives, which represent the largest proportion of total exposure, are almost exclusively traded with banks and financial companies.

For additional quantitative information on the breakdown of the fair values of OTC derivatives by counterparty and by underlying, please see Section 3.1 of Part E of the Notes to the Financial Statements. In particular, in the section referred to, the amount and type of OTC derivative contracts, whether subject to netting agreements or not, are illustrated. Note that almost all of the Bank's counterparties operate with netting agreements, which in most cases provide for the reciprocal provision of guarantees to mitigate risk deriving from net exposure.

Equity Investments

The amount of equity investments in stocks or those similar to equity securities, classified under balance sheet Assets at: 20 c. "financial assets obligatorily measured at fair value through profit or loss", 30. "financial assets measured at fair value through other comprehensive income" and 70. "Equity investments", amounted to € 24.8 million compared to € 62.2 million at 31 December 2017.
The change in the amount of the aggregate is mainly attributable to the write-down of € 35.7 million of the Parent Company's shares (acquired in 2017 following the conversion of the BMPS subordinated securities in the context of the so-called "burden sharing") and to other changes attributable to collections related to Silent Participation contracts for a total of € 1 million; sales for € 3.3 million which generated gains of € 3.2 million (of which € 3 million from Moncada Solar Equipment S.r.l. and € 0.2 million from the liquidation of Società Infrastrutture Toscane SpA); and write-downs for a total of € 0.6 million.

(amounts in thousands of Euro)

Company	*% Stake*	*Book value*
Investments in cinema productions		497
Other		931
20 c. Financial assets obligatorily measured at fair value through profit or loss		**1,428**
Parent Company shares		22,087
Other		506
30. Financial assets measured at fair value through other comprehensive income		**22,593**
Interporto Toscano Amerigo Vespucci S.p.A.	19.00%	0
Sviluppo Imprese Centro Italia S.G.R. S.p.A.	15.00%	779
Other		-
70. Equity investments		**779**
TOTAL		**24,801**

A few brief notes on the investee companies included in item 70 of Assets are presented below:

Interporto Toscano Amerigo Vespucci S.p.A. - Leghorn. This is a company responsible for the construction and management of the logistics centre located on the Guasticce plain, in the municipality of Collesalvetti (Leghorn). The majority of share capital is held by public entities and administrations (Tuscany Regional Authority, Provincial Authorities and local municipalities, Chambers of Commerce (CCIAA) of Leghorn and Pisa). The Bank holds approximately 19% of the capital and Banca Monte dei Paschi di Siena S.p.A. holds approximately 21.8% of the capital.

Sviluppo Imprese Centro Italia S.G.R. S.p.A. - Florence. The company manages four closed-end mutual funds, Fondo Centroinvest, Fondo Toscana Venture, Fondo Toscana Innovazione and Fondo Rilancio e Sviluppo.
the Bank holds 15% of the capital. The other shareholders of the asset management company are Fidi Toscana (31%), Cassa di Risparmio di Firenze S.p.A. (15%), Gepafin S.p.A. (14%), Cassa di Risparmio di San Miniato S.p.A. (10%), Banca Popolare di Vicenza (10%) and Unione Banche Italiane SpA (5%).

Income Statement and operating indicators

ECONOMIC AGGREGATES

The Bank closed the financial statements at 31 December 2018 with a profit of € 80.7 million. The main aggregates from the operating income statement are shown below compared with the figures for the previous year.

(Values in € millions)

Operating Income Statement	*2018*	*2017(*)*	*Absolute change*	*% Change*
Net profit (loss) from trading/valuation at fair value	-20.4	17.9	-38.3	-213.86%
Net hedging gains (losses)	0.0	0.0	0.0	
Gains (losses) from sale or repurchase	0.4	7.5	-7.0	-94.05%
Net gains (losses) on assets/liabilities carried at fair value	-14.7		-14.7	
Other revenues from financial operations	**-33.5**	**27.3**	**-60.8**	**-222.96%**
Other charges/other operating income	**1.1**	**-0.1**	**1.2**	**-1034.24%**
Total revenues	**113.3**	**117.7**	**-4.4**	**-3.74%**
Administrative expenses	-61.6	-68.1	6.6	-9.62%
- personnel costs	*-27.1*	*-28.3*	*1.2*	*-4.19%*
- Other administrative expenses	*-34.4*	*-39.8*	*5.4*	*-13.49%*
Net value adjustments on property, plant and equipment	-0.5	-0.9	0.5	-51.37%
Net value adjustments to intangible fixed assets	0.0	0.0	0.0	
Operating costs	**-62.0**	**-69.1**	**7.0**	**-10.18%**
Gross operating profit	**51.3**	**48.7**	**2.6**	**5.40%**
Net value adjustments for impairment	14.8	-838.4	853.2	-101.76%
- on loans	16.7	-781.2	797.9	-102.14%
- on other assets	-1.9	-57.2	55.3	-96.67%
Gains (losses) on contractual changes without cancellations	-4.5		-4.5	
Net operating profit (loss)	**61.6**	**-789.8**	**851.3**	**-107.80%**
DTA fee	-6.2	-6.2	0.0	0.00%
Commitments and guarantees given	2.5	10.6	-8.1	-76.11%
Other net provisions	-1.2	-5.9	4.6	-78.97%
Risks and charges related to SRG, DGS and similar	-17.9	-12.9	-5.0	38.45%
Restructuring charges	-1.8	-4.8	3.0	-62.57%
Gains (losses) on disposal of investments	0.0	0.0	0.0	
Profit (loss) before taxes	**37.1**	**-808.8**	**845.9**	**-104.58%**
Income taxes on current operations	43.6	175.9	-132.3	-75.20%
Profit (loss) for the year	**80.7**	**-632.9**	**713.6**	**-112.75%**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9.

Before commenting on the trend of the single items, we can illustrate the reasons for the most significant differences compared to the official income statement format:

- € 1.5 million is deducted from "other operating expenses/income" in relation to recoveries of expenses which are attributed operationally to "other administrative expenses";
- the costs related to early retirement of € 1.4 million were deducted from "personnel expenses". These costs were then transferred to the item "restructuring charges";
- "other administrative expenses" were reduced by the amounts of certain items included in specific items placed under Net operating profit/(loss) (DTA fee of € 6.2 million; SRF expenses of € 17.9 million);
- "restructuring expenses", as indicated above, include (i) the costs connected to the sale of bad loans in the context of the Siena NPL securitisation for € 0.4 million and (ii) the costs related to early retirement of personnel of € 1.4 million.

Net Interest Income recorded an increase of 46% compared to the previous year as a result of the optimisation of funding to cover lending operations following the sale of bad loan positions and, more generally, in the context of the management of structural liquidity.
The aggregate **Net Fee and Commission Income** showed a sharply improved result, going from a negative balance of € 2.3 million in 2017 to € 10.3 million in net revenue in 2018. This trend reflects positively both the low fees paid for activities to recover bad loans, as a result of the sale of these exposures to the vehicle Siena NPL S.l.r. (-€ 7 million in fee expense) and the good trend in fee income collected for arranging activities in the context of Loan Agency work (+€ 7 million).
The trend in **Other Revenues from Financial Management** shows a marked reduction compared to the previous year, of approximately € 61 million, mostly (-€ 38.3 million) attributable to the uncertainties connected with the domestic and international political/economic scenario illustrated in the paragraph "Significant Aspects of Operations" in relation to the "Global Markets" BU and, for the rest, deriving mainly from the write-downs of assets classified in the new financial item "financial assets obligatorily measured at fair value through profit or loss" (-€ 14.7 million) and from the lack of the contribution, in 2018, of the early settlement of fixed-rate liabilities made in the previous year (-€ 6.8 million).
As a result of the trend in these components, **Total Revenues** came out at approximately € 113.3 million, down by 3.74 % compared to the result of the previous year.
Operating costs, an aggregate which for management purposes includes, in addition to other operating costs in the strict sense, costs related to write-downs on property, plant and equipment and intangible assets while excluding certain items not directly pertaining to the operating management of the bank and are represented in specific items included under "net operating profit" (DTA fee, SRG contributions and similar, restructuring charges), saw a decrease of around € 7 million or 10.18%, compared to the previous year. Examining in detail the single components, we can note that other administrative expenses (OAEs) fell by approximately € 5.4 million compared to 2017 (-13.49%), owing essentially to lower legal expenses connected with the recovery of loans in dispute (as a result of the often-mentioned sale of the portfolio of bad loans), and that also personnel expenses, net of charges related to the early retirement of employees reclassified among "Restructuring charges", recorded a significant drop of approximately € 1.2 million (- 4.19%).
As a result of the trends just illustrated, there was a **Gross Operating Profit (EBIT)** of € 51.3 million, up by 5.4% compared to the previous year.
The cost of credit, limited to the effects recorded in item 130a., "Net value adjustments for credit risk of financial assets measured at amortised cost", was a positive € 16.7 million compared to net write-downs of € 781.2 million recorded in financial year 2017 to adjust the net value of bad loans to the selling price. We can note that in 2017 item 130b. "Net value adjustments for credit risk of financial assets measured at fair value through other comprehensive income" (formerly AFS) included impairment of € 58.9 million recorded on the Parent Company's shares deriving from the

conversion of subordinated securities in the context of the so-called "burden sharing". Overall, therefore, item 130 recorded a positive change of € 853.2 million which, considering also the € 4.5 million of losses due to contractual changes without cancellations, determined a **Net Operating Profit** of € 61.58 million compared to a loss of € 789.8 recorded in the previous year.
As highlighted above, certain items which are not strictly linked to the bank's "core" operations were presented separately under Net Operating Profit. In particular, these included: (i) costs related to the DTA fee of approximately € 6.2 million, unchanged compared to the previous year; (ii) net provisions for risks and charges of € 1.2 million (against € 5.9 million in 2017), almost entirely related to legal disputes currently pending; (iii) contributions to the Resolution Funds (SRF) of approximately € 17.9 million, up compared to the previous year owing to the call for an extraordinary contribution of approximately € 5 million; (iv) restructuring charges of € 1.8 million (against € 4.8 million in the previous year), of which € 1.4 million related to early retirement of employees in the context of the MPS Group restructuring plan.
Profit from continuing operations before taxes therefore came out at € 37,1 million, compared to € -808.8 million recognised in 2017.
The tax component generated a positive contribution of € 43.6 million (€ +175.9 in the previous year), attributable mainly:
- to the recognition, under the terms of paragraphs 1067 and 1068 of the Stability Law for 2019, of IRES and IRAP DTAs on 9/10 of the higher write-downs on loans recognised on FTA of IFRS9, the deductibility of which was deferred to the next 9 years. This component, net of the reversal of the IRAP credit of € 5.8 million recognised on FTA of IFRS9 against the aforesaid higher write-downs on loans, contributed positively for € 39,2 million;
- To the effect consequent to the probability test (i) on non-transformable DTAs due to temporary differences, written down by € 145 thousand; (ii) on DTAs recognised against the IRES surcharge at 3.5% on earlier tax losses, written down by € 9.1 million and (iii) on the IRES credit from the consolidator recognised against the conferment to the Parent Company of the said earlier losses, revalued by € 14.4 million.

The **Profit for the period**, benefiting from the positive contribution of the item related to taxes, came out at € 80.7 million compared to a loss of € 632.9 in 2017.

OPERATING INDICATORS

Below are the main profitability indices, calculated using the reclassified income statement:

Profitability indices (%)	31/12/2018	31/12/2017	% Changes
Net interest income / Operating revenues [(1)]	119.61	78.86	51.68
Net fees / Operating revenues [(1)]	9.06	(1.93)	
Cost/Income ratio [(2)]	54.73	58.66	(6.69)
R.O.E. [(3)]	6.65	(42.49)	
R.O.A. [(4)]	0.31	(2.18)	

Notes:
[(1)] *Operating revenues: equal to "total revenues" from operating management in the reclassified income statement.*
[(2)] *Cost/Income: the ratio between operating costs and "total revenues" in the reclassified income statement.*
[(3)] *Return On Equity: the ratio between the result for the period and the average of shareholders' equity (including gains/losses) at the end of the previous year and that of the year in question.*
[(4)] *Return On Assets: the ratio between the net result for the period and total assets at period end.*

Risk governance

The risk governance strategies are defined in keeping with the Group's business model, with the medium-term objectives of the Restructuring Plan and with the external constraints of a legislative and regulatory nature.
The policies regarding the assumption, management, hedging, monitoring and control of risks are defined by the Parent Company's Board of Directors. This Body, in particular, defines and approves periodically the strategic guidelines on the subject of risk governance and expresses quantitatively the overall level of risk propensity of the whole Group, in keeping with the annual budget and with the multi-year projections.
The Parent Company's Board of Directors defines the overall Risk Appetite Framework (RAF) for the Group and approves the Group Risk Appetite Statement (RAS) at least once a year. The Risk Control Unit is tasked in particular with carrying out the monitoring of the indicators, preparing a periodic report to the Board of Directors and activating the escalation/authorisation processes if a position goes over the limit.
The RAS is fundamental in terms of defining the Group's risk strategy. Risk objectives/constraints are identified and indicators for the business units/legal entities are also established. This process is known as Risk Appetite cascading down. This moves in the direction of increasing the Group's Risk Culture and making fully responsible all the relevant Organisational Units for observing and pursuing the risk appetite targets, as required by the legislation and suggested also by the best practices.
The overall RAF system is structured for the Group's main Business Units and Legal Entities, also in terms of operating limits on the various business segments, and formalised in governance policies and the various business risk management processes.
The Risk Appetite Process is structured in such a way as to be consistent with both the ICAAP and ILAAP processes and the Planning and Budget and Recovery processes in terms of governance, roles, responsibilities, metrics, stress test methods and monitoring of the key risk indicators.
The Group's risk governance is guaranteed in a centralised manner by the Board of Directors of the Parent Company, which is also responsible for supervising the updating and issuing of the policies and the main internal regulations, with a view to promoting and guaranteeing an ever-increasing and more capillary diffusion of risk culture at all levels of the organisational structure. Awareness of risks and correct knowledge and application of the internal processes and models overseeing these risks - primarily those validated for regulatory purposes - constitute the fundamental prerequisite for effective, healthy and prudent business management.
The incorporation in the remuneration and bonus policies for the personnel of the macro-indicators of risk and risk-adjusted performance, in keeping with the RAF, represents a further lever for promoting awareness of the appropriate behaviour by all resources and the growth of a healthy risk culture.
During 2018, internal initiatives continued, aimed at guaranteeing continuous compliance with national and international regulatory provisions. On the subject of risk management, the Group Directive on Management of the Model Risk was drawn up and the internal regulations on the subject of Product Oversight and Governance, Credit Risk Management, RAS and Recovery processes were updated.
Additionally, the sending of the ICAAP and ILAAP packages to the Regulatory was completed in line with the ECB's regulatory provisions on the "*Technical implementation of the EBA Guidelines on ICAAP/ILAAP information for SREP Purposes*".
initiatives also continued with the aim of strengthening the Group's Governance on the subject of risk reporting in the light of the indications of the Basel Committee on Banking Supervision (BCBS Paper no. 239).
On the subject of promoting the Risk Culture within the Group, as well as continuing with the initiatives aimed at the Boards (cycles of board induction on specific subjects) and with those of general training (on-line courses) aimed at all the personnel on the subject of risk management and mitigation and other targeted training actions in the classroom, during 2018, a "pilot" programme of induction of the main business units was conducted in support of the understanding of the risk propensity objectives indicated by the BoD in the RAS and of the related monitoring reporting.
The MPS Group is one of the Italian banks that are subject to the ECB's Single Supervisory Mechanism.

The equity position

The table below summarises the categories of risks to which the Bank is exposed and the level of capital ratios compared to the previous year.

Categories/Balances		*Unweighted amounts*		*Weighted amounts/ requirements*	
		31/12/2018	*31/12/2017*	*31/12/2018*	*31/12/2017*
A.	**RISK ASSETS**				
A.1	Credit and counterparty risk	**25,383,644**	**24,894,947**	**5,997,208**	**5,659,259**
	1. Standardised approach	18,484,139	14,165,451	1,661,022	1,833,446
	2. Internal ratings-based approach	6,884,112	10,729,496	4,305,701	3,825,813
	2.1 Basic				
	2.2 Advanced	6,884,112	10,729,496	4,305,701	3,825,813
	3. Securitisations	15,393		30,485	
B.	**REGULATORY CAPITAL REQUIREMENTS**				
B.1	Credit and counterparty risk			**479,777**	**453,105**
B.2	Credit valuation adjustment risk			**23,283**	**20,828**
B.3	Regulatory risk				
B.4	Market risks			**188,954**	**194,591**
	1. Standard approach			188,954	194,591
	2. Internal models				
	3. Concentration risk				
B.5	Operational risk			**45,367**	**56,574**
	1. Basic approach				
	2. Standardised approach				
	3. Advanced approach			45,367	56,574
B.6	Other calculation elements				
B.7	Total prudential requirements			**737,381**	**725,098**
C.	**RISK ASSETS AND SUPERVISORY RATIOS**				
C.1	Risk-weighted assets			**9,217,266**	**9,063,731**
C.2	Common Equity Tier 1/Risk-weighted assets (CET1 capital ratio)			**13.03%**	**13.74%**
C.3	Tier 1 Capital/Risk-weighted assets (Tier 1 capital ratio)			**13.03%**	**13.74%**
C.4	Total own funds/Risk-weighted assets (Total capital ratio)			**18.00%**	**18.87%**

NB: The amount of the risk-weighted assets as per item C.1 is determined as the product of the total prudential requirements (item B.7) and 12.5 (inverse of the minimum mandatory ratio of 8%).

The total risk-weighted assets (RWAs) at 31 December 2018 amounted to € 9,217,266 thousand, slightly up compared to the previous year, and were distributed as follows: 65.06% represented by credit and counterparty risk (62.49% at 31/12/2017), 25.63% by market risk (26.84% at 31/12/2017) 6.15% by operational risks (7.80% at 31/12/2017) and 3.16% by the risk of Credit Value Adjustment (2.87% at 31/12/2017).

The table presented below shows the Regulatory Capital at the end of 2018 as compared to the previous year:

(amounts in thousands of euro)

Categories/Balances	*31/12/2018*	*31/12/2017*	*Changes from 31/12/2017*	
			Absolute	*%*
Common Equity Tier 1 (CET1)	1,200,688	1,245,188	(44,500)	(3.57%)
Tier 1 (T1)	1,200,688	1,245,188	(44,500)	(3.57%)
Tier 2 (T2)	458,300	465,444	(7,144)	(1.53%)
OWN FUNDS	**1,658,988**	**1,710,632**	**(51,644)**	**(3.02%)**

Comparing Own Funds, of € 1,659 million (€ 1,711 million at 31/12/2017), to RWAs, the Common Equity Tier 1 ratio (Common Equity Tier 1 Capital/Risk-weighted assets) came out at 13.03% compared to a minimum regulatory level of 6.375%; the Tier 1 ratio (Total Tier 1 Capital/Risk-weighted assets) came out at 13.03% compared to a minimum regulatory level of 7.875%; while the Total Capital Ratio (Total Own Funds/Risk-weighted assets) was 18% compared to a minimum regulatory level of 9.875% (the minimum levels include the percentage of the capital conservation buffer, of 1.875%).

As required by the ninth recital of Regulation (EU) 2017/2395, disclosure is provided below of the level of Own Funds and of the capital ratios with and without application of the transitional arrangements applied to adjustments recorded on FTA of the accounting standard IFRS9.
In the event of non-application of the transitional arrangements, the amount of "full IFRS 9" CET1 and Regulatory Capital would be less than € 53 million, the CET1 ratio and the Tier 1 ratio would come out at 12.45% (-58 basis points), and the Total Capital Ratio at 17.42% (-58 basis points).

Human Resources

STAFF TREND

The Bank's staff at 31 December 2018 is shown in the tables presented below:

	(a) MPSCS employees	*(b) MPSCS employees at Group companies or subsidiaries*	*(c) Group company employees at MPSCS*	*Workforce (a-b+c)*
Executives	22	10	7	**19**
Managers	283	122	32	**193**
Professionals	201	98	15	**118**
Total	**506**	**230**	**54**	**330**

Work force	*31/12/2018*	*31/12/2017*	*Changes*	
Comparison 2018/2017			*Absolute*	*%*
Executives	19	19	(0)	0%
Managers	193	204	(11)	(5.39%)
Professionals	118	115	3	2.61%
Total	**330**	**338**	**(8)**	(4.79%)

The changes in the workforce in the year are presented below:

Workforce trend	*2018*	*2017*
Opening balance	**338**	**355**
Increases	**17**	**16**
due to hiring	5	8
due to ceased secondments to the Group	10	2
due to secondments from the Group	2	6
Decreases	**25**	**33**
due to resignations	8	5
due to access to the Solidarity Fund	2	14
due to secondments in the Group	15	14
Closing number	**330**	**338**

DISTRIBUTION BY AGE

The following information pertains to the workforce situation at 31 December 2018:

	Age group in years					*Average*
	up to 30	*30-40*	*41-50*	*over 50*	*Total*	*age*
Women	6	16	65	28	115	45.3
Men	6	28	89	92	215	48.28
Total 2018	**12**	**44**	**154**	**120**	**350**	**47.25**
Proportion:	*3.64%*	*13.33%*	*46.67%*	*36.36%*		

PERSONNEL TRAINING

The training activity for 2018, in keeping with the scheduled plans, was characterised by specialist and/or obligatory actions aimed at all categories of employees or at specific proficiencies (302 employees involved), structured as follows:

- training in business, legal and organisational matters hours 1,076.7
- training in compliance matters hours 571.3
- training in safety matters hours 534
- on-line and web session training hours 760

EMPLOYMENT AND TRADE UNION RELATIONS

The Bank favours a model of trade union relations oriented towards transparency, reciprocal respect and sense of responsibility in order to safeguard a corporate climate of positive collaboration and to promote an increasingly active involvement of the trade unions.

Organisational and Technological Trends

Financial year 2018 saw strategic technological and organisational developments, which were guided both by the introduction of new external regulations and the stabilisation projects for the Montepaschi Group.
Activities continued on implementing actions related to Directive 2014/65/EU (MiFID II) and Regulation (EU) 600/2014 (MiFIR).
In the context of the MPS Banking Group, the activities performed went mainly in two directions: Investor Protection—under the coordination of the Parent Company—and the aspects related to the financial markets under the coordination of MPS Capital Services with the crucial involvement of the Group’s Operational Consortium.
The persistence of a level of uncertainty about the methods of implementing the exit of Britain from the EU and the possible implications in a Hard Brexit scenario, originated the need to assess and take the necessary actions aimed at guaranteeing business continuity in a context in which the entities of the United Kingdom no longer have access to the European market. With the European Banking Authority (EBA), companies considered the options for extending existing entities or creating new ones within the EU, endowed with adequate capacities for management, governance, personnel and infrastructure. This was in order to overcome the ambiguities still existing around the nature of the possible restrictions in future relations between the United Kingdom and the EU (payments, rules for access to the Central Counterparties recognised by the EU, etc.). In the second half of the year in question the Bank - as part of a group project - launched the on-boarding activities with the market counterparties, in relation to the offices of the same identified within the EU.
Again remaining in the context regarding compliance with the standards, we can mention the evolutions of the world related to financial statement formalities as a result of entry into force from 1 January 2018 of the new international accounting standards (IFRS 9). The standard, which replaces the previous IAS39, brought significant changes in the measurement of all financial assets with consequent direct changes to the Group’s information collection processes and summary systems. 2018 also saw the implementation of Regulation (EU) 2016/867 (ECB - 2016/13) on the collection and transmission of granular data on lending and credit risk (ANACREDIT) to the Regulator. This implementation, carried out under the guidance and coordination of Banca Monte dei Paschi, saw a great involvement also of the responsible structures of the Group’s Operational Consortium.
As regards the processes in support of the control activities against money-laundering the analysis and implementation activities continued consequent to the introduction of the IV EU Money-Laundering Directive (Directive 2015/849 transposed by Italian Legislative Decree 90/2017). The application GIANOS 3D was also required to be made more efficient (with particular reference to the Finance segment). This application, making use of sophisticated algorithms in part based on a wide swathe of information available within the Group's IT system, provides better monitoring of customer risk profiles and supports periodic monitoring than required by the AML (Anti Money Laundering) regulations.
Other large-scale initiatives with a significant impact on the activities of the Bank and the Group were those referable to Non-Performing Loans (NPL), which consisted, on the one hand of the sale of bad loans as part of the so-called Valentine project (completed in June 2018 with the derecognition of the bad loans sold to the vehicle “Siena NPL S.r.l.”), and on the other, of the operating launch of the Sirio project, which aims to make more efficient the process of recovering some of the bad loans outsourcing their management.
On the organisational model, a series of actions were carried out with the aim of optimising the business units and rationalising those of support, so as to have an organisational structure capable of dealing as well as possible with both the demands coming from the market and the internal operating needs. All the necessary initiatives for the activation of the provisions of Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016, General Data Protection Regulation (GDPR) were also implemented, under the guidance of the Parent Company.

Internal Audit

The Internal Audit Office constitutes, within the Bank, the Internal Audit Unit, as defined in the section on the Internal Controls System of Bank of Italy Circular No. 285/2013 and subsequent amendments and additions.
The Internal Audit Unit, which reports directly to the Board of Directors (the Body with the Function of Strategic Supervision), has the task of independently verifying the regularity of operations and the trend in risks and of assessing the functioning of the overall internal control system, in order to pursue also the improvement of the effectiveness and efficiency of the organisation. It also provides advice to the other corporate units where a prior analysis, on the subject of legislation or development of planning activities is considered worthwhile, with the aim of improving the governance, risk management and control processes, in keeping with the evolution of the Bank, the Group and the external legislative framework, bringing to the attention of the Corporate Bodies the possible improvements.
The Internal Audit Unit, in keeping with the Group's organisational model, is an independent structure, free of hierarchical relationships with the managers of the operating structures. The structure of the Internal Control System (I.C.S.) and the regulation of the activity of the Internal Audit Unit, the contents of which must be compliant with the rules of the law and the Supervisory Authorities, are defined observing the guidance provided by the Parent Company's Internal Audit Unit and approved by the Bank's Board of Directors, which is responsible for the entire I.C.S..
The Unit operates, also, in coordination with the equivalent Unit of the Parent Company (the Chief Audit Executive Department), in observance of the "Auditing Standards of the Montepaschi Group" and of the related "Code of Conduct", in accordance with a specific Annual Audit Plan (agreed with the said Chief Audit Executive Department) approved by the Board of Directors, after examination by the Auditing Body (Board of Statutory Auditors). The Plan, in addition to establishing strategic objectives for multi-year activity to be carried out within three years, takes into account the need to carry out the audits provided for in specific external and/or internal prescriptions, the indications of the Board of Auditors, of the Oversight Committee pursuant to Italian Legislative Decree. 231/2001 and, if expressed and agreed, of the Bank's other Audit Units. Actions on significant components in the area of operations and corporate structures, on compliance with internal and external regulations, on subjects of a transversal nature or with a view to assurance of the Top Management and Auditing Bodies are obviously also planned, depending on the resources available.
For the performance of its tasks, the Unit may accede to all the corporate information, the outsourced activities and the Company's structures (on-site audits).
The Internal Audit Unit reports the activities carried out systematically through a Reporting System consistent with the provisions of the Auditing Standards and laws, describing the results of the audits performed, the process of analysis followed, the main critical issues that have emerged and the "grade" assigned to the action. Notes containing the criticisms and observations formulated are transmitted to the structures audited, ensuring that over time the anomalies found are removed (follow-up activity).
Quarterly reports on the work done are also prepared for the Top Management and Auditing Bodies, while the report relating to the assessment of the Internal Control System, including also an overall final report on the activities carried out, is presented to the Board of Directors on an annual basis. The Office also prepares specific reports for the Oversight Committee, pursuant to Italian Legislative Decree 231/2001, at least once a year, on the auditing activity carried out on current operations exposed to the "231 risk".
During financial year 2018, the Internal Audit Office carried out its duties according to the schedule found in the 2018 Audit Plan approved by the Board of Directors, performing also a number of unplanned actions on the basis of new needs that emerged and/or were requested by the top management bodies and the authorities.
In accordance with the pre-set objectives, the audit activities performed in financial year 2018 made it possible to ascertain the substantial regularity of the corporate operations. Areas for improvement found were considered such as not to significantly affect the Bank's overall risk profile. The Bank's Internal Control System is considered substantially adequate, in terms of both design (Control Design) and effective operation (Test of Effectiveness).

Compliance

In 2017, the Bank's Organisational Model for the Compliance Department was modified. In fact, in line with the recommendations received from the European Central Bank, the MPS Group implemented a specific plan to strengthen the Compliance Department which involved, among other things:

- centralising the Compliance Units of Italian subsidiaries within the parent company, which also involved MPS Capital Services S.p.A. To this end, in December 2017, the Bank's Board of Directors approved the *“Agreement on outsourcing the Compliance Units to the Parent Company*”;
- the elimination of the “Common Compliance Model”, through centralising operating activities within the Compliance Unit that had previously been entrusted to Specialist Compliance Offices, with the exclusion of those related to “Workplace Health and Safety and Environmental Protection” and “Tax Compliance”.

The work done by the Compliance Unit in 2018 had the main goal of completing the actions described in the 2018 Compliance Plan and implementing the main legislative changes within company regulations and processes.

Special attention was paid to monitoring activities and safeguards established relative to:

- *ICT Compliance* (Bank of Italy circular 285) and international combating of tax evasion (FATCA/CRS);
- Banking transparency, with the updating of the new release of internal regulatory documents on “*Provisions for the Transparency of Banking Transactions and Services*” which implemented the developments associated with Italian Legislative Decree 72/2016;
- Fighting usury, by adjusting control procedures to the progressive updates made to the Bank of Italy Supervisory Instructions;
- Protection of personal information (privacy) with participation in periodic SAL meetings on the “*Project to adjust to Regulation EU 2016/679 (GDPR)*” and the actions associated with the same;
- Investment services, including defining and carrying out actions necessary to comply with the PRIIPS Regulation, MiFID II Directive and MiFIR Regulation by January 2018.

With regard to Customer complaints, during the year, 13 claims were made regarding banking services, 6 of which relating to usury(none of these were accepted). The complaints, in fact, were found to be groundless because they derived from erroneous application by the customer of the default interest calculation. Of the remaining complaints, 4 regarded the validity of sureties (non-adjustment of the maximum amount guaranteed to the ISTAT indices) and 3 concerned insignificant matters.

Environmental Issues

During the year, activities to maintain the Environmental Management System (EMS) continued. This system is compliant with the new international standard of reference, ISO 14001:2015. The EMS includes management of the direct and indirect impacts of the Bank's activities. Direct impacts are linked to operations, and relate to consumption of paper, water and energy, and to the production of waste and greenhouse gases, while indirect impacts are attributable to activities of suppliers and customers, to the environmental risk of activities financed, to the improvement in ecological efficiency encouraged through specific financing and to polluting activities of suppliers or of the products purchased.
The new ISO standard also envisages maintaining an adequate level of training as well as increasingly significant involvement of top management, including the Board of Directors. Therefore, personnel responsible for the main aspects of the system were adequately trained and all staff are periodically made aware of various initiatives and receive specific update training courses.
As regards operational aspects related to Certification, in October/November 2018 internal audits were carried out in preparation for auditing by the external entity, at the offices in Florence, Rome, Padua and Milan.
In December 2018, the RINA Services Certification Agency carried out its usual annual visit to confirm certification. The field of application of the management system remained unchanged and includes loan disbursement, corporate finance and structured finance services, investment services and activities on the capital market, consultancy and services to the Public Administration for the concession of public subsidies.
The audit was completed positively with the notification of only two recommendations for improvement, which are currently being managed.

Relations with Group companies

Transactions carried out with the Parent Company Banca Monte dei Paschi di Siena and with the other MPS Group Companies were numerous and significant throughout the financial year. Part H "Transactions with Related Parties" in the Notes to the Financial Statements gives a breakdown of the existing relations with Group companies as of 31 December 2018. The most important aspects are commented on below.

Given that the guidance, control and support provided by the Parent Company over the Bank's operations was focused on the areas of planning and control, legal and compliance, corporate identity and oversight of relations with supervisory authorities, these relations were characterised by proactive, constant and constructive cooperation, in accordance with the guidelines (directives, policies, process regulations) issued by the Parent Company and promptly brought to the attention of the Bank's Board of Directors, which ensured they were implemented.

The outsourcing of specific activities to other MPS Group organisations and companies has enabled the Bank to continue upon its own path to maximise synergies and economies. Services outsourced to and financial transactions carried out with MPS Group counterparties, summarised below, are as a rule settled on the basis of ordinary market conditions regulated by dedicated agreements between the Parties (called Service Level Agreements - SLAs).

As regards relations with the Parent Company and its subsidiaries, the following is specifically noted:

- operations on the financial markets carried out as part of the Bank's strategic mission, set forth in detail in the paragraphs above;
- the agreement on the subject of regulating relations with other Group companies regarding the repurchase on the secondary market of innovative finance products designed by MPSCS and placed with customers through the Group's commercial networks;
- the granting of short and medium/long-term loans by Banca MPS aimed at funding the Bank's normal activity; all carried out in keeping with and observing the objectives and limits set by the Parent Company in the context of the centralised management of liquidity risk and interest-rate risk;
- non-performing loan recovery activities and the delegated management of the related expense items, entrusted to the Parent Company's Workout Area, and governed by specific SLAs;
- the presence of personnel seconded from the Parent Company and other Group entities to the Bank;
- the secondment of Bank employees to the Parent Company and its subsidiaries, including the Consorzio Operativo Gruppo MPS (MPS Group Operational Consortium);
- the centralised supervision of Risk Management by the Parent Company's Risks Department;
- the activities of monitoring advertising, communication and the image at the External Relations Area of Banca MPS;
- the centralised monitoring of the Compliance activity at the Parent Company's Compliance Area;
- technological supervision, maintenance and development of the IT system assigned to the MPS Group's Operational Consortium, with which a specific SLA has been defined;
- the Back Office and Middle Office administrative activities of the finance area centralised respectively at the Operations Department and at the Finance, Cash and Capital Management Area of the Parent Company;
- the purchases of goods and services in amounts exceeding the specific thresholds by Parent Company structures, in the function of the Centralised Group Procurement and Supplier Management Service;
- conferment to the Parent Company's CFO Department - Equity investments and Extraordinary Operations Area - Real Estate Investments and Disinvestments Staff of the activities connected to the disposal/sale of properties still owned by the Bank;
- conferment of the delegated management of the expense items of the real estate sector to the Parent Company's Real Estate Maintenance Service;
- the support provided by the Parent Company's Prevention, Protection and Environment Service, regarding workplace health and safety, as well as the sustainable development of the Bank's activities, with reference to the possible consequences in terms of the environment;
- the lease of premises owned by the Group.

Significant Events During 2018, Significant Subsequent Events and Business Outlook

No significant changes in the Bank's operations were noted during the year and also in the first few months of 2019 activities continued as in the past and in line with the current business plan.
On 1 January 2019 Mr Giampiero Bergami resigned from the position of Managing Director. At the moment, the position remains vacant.

Proposals to the Shareholders' Meeting

Dear Shareholders,

We ask that you approve the 2018 separate Financial Statements, comprising the balance sheet, the income statement, the statement of comprehensive income, the statement of changes in shareholders' equity with the related movements in reserves, the cash flow statement and the Notes to the Financial Statements, as well as the related attachments and Report on Operations, as a whole and in their individual items, as presented by the Board of Directors, and to allocate the profit recorded for the year of € 80,699,464.61 to reducing the loss carried forward from financial year 2017.

FINANCIAL STATEMENTS

Balance Sheet

	Assets	*31/12/2018*	*31/12/2017(*)*	*Changes*	
				Absolute	*%*
10.	Cash and cash equivalents	7	331	(324)	(97.89%)
20.	Financial assets measured at fair value through profit or loss	9,454,408,788	10,476,326,898	(1,021,918,110)	(9.75%)
	a) financial assets held for trading	9,350,369,189	*10,476,326,898*	*(1,125,957,709)*	*(10.75%)*
	b) financial assets designated at fair value				
	c) financial assets obligatorily measured at fair value	104,039,599		*104,039,599*	
30.	Financial assets measured at fair value through other comprehensive income	95,303,214	69,494,803	25,808,411	37.14%
40.	Financial assets measured at amortised cost	15,403,344,128	16,814,466,795	(1,411,122,667)	(8.39%)
	a) receivables from banks	5,669,343,391	6,054,189,381	(384,845,990)	(6.36%)
	b) receivables from customers	9,734,000,737	10,760,277,414	(1,026,276,677)	(9.54%)
70.	Equity investments	779,480	779,480		
80.	Property, plant and equipment	11,909,099	12,329,805	(420,706)	(3.41%)
100.	Tax assets	510,168,963	499,495,410	10,673,553	2.14%
	a) current	*331,333,529*	*306,811,332*	*24,522,197*	*7.99%*
	b) deferred	*178,835,434*	*192,684,078*	*(13,848,644)*	*(7.19%)*
110.	Non-current assets and disposal groups held for sale	52,745,788	979,941,993	(927,196,205)	(94.62%)
120.	Other assets	201,056,944	196,837,141	4,219,803	2.14%
	Total Assets	25,729,716,411	29,049,672,656	(3,319,956,245)	(11.43%)

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Balance Sheet

	Liabilities and Shareholders' Equity	*31/12/2018*	*31/12/2017(*)*	*Changes*	
				Absolute	*%*
10.	Financial liabilities measured at amortised cost	20,957,254,853	22,845,977,105	(1,888,722,252)	(8.27%)
	a) payables to banks	15,900,331,577	15,449,515,916	450,815,661	2.92%
	b) payables to customers	4,600,384,217	6,939,910,501	(2,339,526,284)	(33.71%)
	c) outstanding securities	456,539,059	456,550,688	(11,629)	0.00%
20.	Financial liabilities held for trading	3,467,476,962	4,804,233,426	(1,336,756,464)	(27.82%)
70.	Liabilities associated with assets held for sale	25,000		25,000	
80.	Other liabilities	70,480,464	59,805,338	10,675,126	17.85%
90.	Employee severance indemnities	2,525,691	2,603,223	(77,532)	(2.98%)
100.	Provisions for risks and charges:	30,458,513	30,843,817	(385,304)	(1.25%)
	a) commitments and guarantees given	2,409,694	3,062,859	(653,165)	*(21.33%)*
	b) pensions and similar obligations	*4,107,980*	4,602,326	(494,346)	*(10.74%)*
	c) other provisions for risks and charges	*23,940,839*	23,178,632	762,207	*3.29%*
110.	Valuation reserves	(141,440,938)	(2,241,702)	(139,199,236)	6209.53%
140.	Reserves	(407,279,881)	110,426,757	(517,706,638)	(468.82%)
150.	Share premiums		161,445,808	(161,445,808)	(100.00%)
160.	Capital	1,669,516,282	1,669,516,282		
180.	Profit (Loss) for the period	80,699,465	(632,937,398)	713,636,863	(112.75%)
	Total Liabilities and Shareholders' Equity	25,729,716,411	29,049,672,656	(3,319,956,245)	(11.43%)

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Income Statement

	Items	*31/12/2018*	*31/12/2017(*)*	*Changes*	
				Absolute	*%*
10.	Interest and similar income	303,094,889	309,645,662	(6,550,773)	(2.12%)
	of which: interest income calculated with				
	the effective interest rate method	*238,365,148*		161,527,893	
20.	Interest expense and similar charges	(167,471,906)	(217,550,370)	50,078,464	(23.02%)
30.	**Net interest income**	**135,622,983**	**92,095,292**	**43,527,691**	**47.26%**
40.	Fee income	45,650,326	43,194,534	2,455,792	5.69%
50.	Fee expense	(35,581,538)	(48,232,125)	12,650,587	(26.23%)
60.	**Net fee and commission income**	**10,068,788**	**(5,037,591)**	**15,106,379**	**(299.87%)**
70.	Dividends and similar income	1,129,901	1,885,405	(755,504)	(40.07%)
80.	Net trading gains (losses)	(20,356,117)	18,070,635	(38,426,752)	(212.65%)
90.	Net hedging gains (losses)				
100.	Gains (losses) on disposal or repurchase of:	445,304	8,421,173	(7,975,869)	(94.71%)
	a) financial assets measured at amortised cost	*(130,668)*	*8,511*	*(139,179)*	(1635.28%)
	b) financial assets measured at fair value through other comprehensive income	*575,972*	*1,587,539*	*(1,011,567)*	*(63.72%)*
	c) financial liabilities		*6,825,123*	*(6,825,123)*	*(100.00%)*
110.	Net gains/(losses) on financial assets and liabilities				
	measured at fair value through profit or loss	(14,517,721)	0	*(14,517,721)*	
	a) financial assets and liabilities designated				
	at fair value				
	b) other financial assets obligatorily				
	measured at fair value	*(14,517,721)*		*(14,517,721)*	
120.	**Operating income**	**112,393,138**	**115,434,914**	**(3,041,776)**	**(2.64%)**
130.	Net value adjustments for credit risk of:	14,552,146	(838,432,059)	852,984,205	(101.74%)
	a) financial assets measured at amortised cost	*16,458,532*	*(781,220,885)*	*797,679,417*	*(102.11%)*
	b) financial assets measured at fair value through other comprehensive income	*(1,906,386)*	*(57,211,174)*	*55,304,788*	*(96.67%)*
140.	Gains/(losses) on contractual changes without cancellations	(4,515,016)		(4,515,016)	
150.	**Net income from financial management**	**122,430,268**	**(722,997,145)**	**845,427,413**	**(116.93%)**
160.	Administrative expenses	(88,904,813)	(95,155,029)	6,250,216	(6.57%)
	a) personnel expenses	*(28,573,545)*	*(30,713,492)*	*2,139,947*	*(6.97%)*
	b) other administrative expenses	*(60,331,268)*	*(64,441,537)*	*4,110,269*	*(6.38%)*
170.	Net provisions for risks and charges	1,306,363	4,765,710	(3,459,347)	(72.59%)
	a) commitments and guarantees given	*2,540,363*	*10,634,116*	*(8,093,753)*	*(76.11%)*
	b) other net provisions	*(1,234,000)*	*(5,868,406)*	*4,634,406*	*(78.97%)*
180.	Net value adjustments on property, plant				
	and equipment	(452,487)	(930,505)	478,018	(51.37%)
200.	Other operating income/charges	2,690,098	6,369,103	(3,679,005)	(57.76%)
210.	**Operating costs**	**(85,360,839)**	**(84,950,721)**	**(410,118)**	**0.48%**
220.	Profit (loss) from equity investments		(900,667)	900,667	(100.00%)
260.	**Profit/(Loss) from continuing operations before tax**	**37,069,429**	**(808,848,533)**	**845,917,962**	**(104.58%)**
270.	Income taxes for the year on current operations	43,630,036	175,911,135	(132,281,099)	(75.20%)
300.	**Profit (Loss) for the period**	**80,699,465**	**(632,937,398)**	**713,636,863**	**(112.75%)**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Basic and Diluted Earnings per Share

	31/12/2018	*31/12/2017*
Basic earnings per share		
- of continuing operations	100.55369	(788.65692)
- of asset disposal groups held for sale		
Diluted earnings per share		
- of continuing operations	100.55369	(788.65692)
- of asset disposal groups held for sale		

Statement of Comprehensive Income

	Items	*31/12/2018*	*31/12/2017(*)*
10.	**Profit (Loss) for the period**	**80,699,465**	**(632,937,398)**
	Other income components after tax without transfer to income statement		
20.	Equity securities designated at fair value through other comprehensive income	(35,950,439)	
30.	Financial liabilities designated at fair value through profit or loss (changes in own creditworthiness)		
40.	Hedging of equity securities designated at fair value through other comprehensive income		
50.	Property, plant and equipment		
60.	Intangible assets		
70.	Defined benefit plans	32,888	67,344
80.	Non-current assets held for sale		
90.	Portion of equity investment revaluation reserves measured at equity		
	Other income components after tax with transfer to income statement		
100.	Foreign investment hedging		
110.	Exchange differences		
120.	Cash flow hedging		
130.	Hedging instruments (undesignated elements)		
140.	Financial assets (other than equity securities) measured at fair value through other comprehensive income	(1,871,583)	(147,112)
150.	Non-current assets and disposal groups held for sale		
160.	Portion of equity investment revaluation reserves measured at equity		
170.	**Total other income components net of taxes**	**(37,789,134)**	**(79,768)**
180.	**Comprehensive income (Item 10+170)**	**42,910,331**	**(633,017,166)**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Statement of Changes in Consolidated Shareholders' Equity 01/01/2018 - 31/12/2018

				Allocation of the result of the preceding financial year		*Changes for the period*								
						Changes in Reserves	*Shareholders' Equity transactions*							
	Balances as at 31/12/2017	*Changes in initial balances*	*Balances as at 01/01/2018*	*Reserves*	*Dividends and other allocations*		*Issue of new shares*	*Purchase of treasury shares*	*Extraordinary dividend distribution*	*Change in equity instruments*	*Derivates on treasury shares*	*Stock options*	*Comprehensive income 31/12/2018*	*Shareholders' equity at 31/12/2018*
Capital:	**1,669,516,282**		**1,669,516,282**											**1,669,516,282**
a) ordinary shares	***1,669,516,282***		***1,669,516,282***											**1,669,516,282**
b) other shares														
Share premiums	**161,445,808**		**161,445,808**	**(161,445,808)**										
Reserves:	**110,426,756**	***(46,215,048)***	**64,211,708**	**(471,491,590)**										**(407,279,882)**
a) profit	***76,641,913***	***(46,215,048)***	***30,426,865***	***(437,706,747)***										***(407,279,882)***
b) other	***33,784,843***		***33,784,843***	***(33,784,843)***										***0***
Valuation reserves	**(2,241,702)**	**(101,410,103)**	**(103,651,805)**										**(37,789,134)**	**(141,440,939)**
Equity instruments														
Treasury shares														
Profit (Loss) for the period	**(632,937,398)**		**(632,937,398)**	**632,937,398**									**80,699,465**	**80,699,465**
Shareholders' equity	**1,306,209,746**	**(147,625,151)**	**1,158,584,595**	**0**									**42,910,331**	**1,201,494,926**

Statement of Changes in Consolidated Shareholders' Equity 31/12/2016 - 31/12/2017

				Allocation of the result of the preceding financial year			*Changes for the period*							
							Shareholders' Equity transactions							
	Balances as at 31/12/2016	*Changes in initial balances*	*Balances as at 01/01/2017*	*Reserves*	*Dividends and other allocations*	*Changes in Reserves*	*Issue of new shares*	*Purchase of treasury shares*	*Extraordinary dividend distribution*	*Change in equity instruments*	*Derivates on treasury shares*	*Stock options*	*Comprehensive income 31/12/2017*	*Shareholders' equity at 31/12/2017*
Capital:	**829,304,239**		**829,304,239**				**840,212,043**							**1,669,516,282**
a) ordinary shares	***829,304,239***		***829,304,239***				***840,212,043***							**1,669,516,282**
b) other shares														
Share premiums	**875,214,055**		**875,214,055**	**(749,260,486)**		**(23,152,838)**	**58,645,077**							**161,445,808**
Reserves:	**107,686,272**		**107,686,272**	**(20,421,985)**		**23,162,469**								**110,426,756**
a) profit	***82,143,326***		***82,143,326***	***(5,511,044)***		***9,631***								***76,641,913***
b) other	***25,542,946***		***25,542,946***	***(14,910,941)***		***23,152,838***								***33,784,843***
Valuation reserves	**(2,161,933)**		**(2,161,933)**										**(79,769)**	**(2,241,702)**
Equity instruments														
Treasury shares														
Profit (Loss) for the period	**(769,682,471)**		**(769,682,471)**	**769,682,471**									**(632,937,398)**	**(632,937,398)**
Shareholders' equity	**1,040,360,162**		**1,040,360,162**	**0**		**9,631**	**898,857,120**						**(633,017,167)**	**1,306,209,746**

Cash Flow Statement (indirect method)

(amounts in Euro)

		31/12/2018	31/12/2017(*)
A.	**OPERATING ACTIVITIES**		
1.	**Operations**	**450,305,804**	**79,377,480**
	- result of the period (+/-)	80,699,465	(632,937,398)
	- capital gains/losses on financial assets held for trading and on other financial assets/liabilities measured at fair value through profit or loss	146,383,934	4,122,499
	- net value adjustments for credit risk	46,375,589	899,971,589
	- net value adjustments on property, plant and equipment and intangible assets	452,487	930,505
	- net provisions for risks and charges and other costs/revenues	530,056	5,930,972
	- tax, duties and tax credits not liquidated	(43,630,036)	(175,911,136)
	- net value adjustments of discontinued operations net of the tax effect		
	- other adjustments	219,494,309	(22,729,551)
2.	**Cash flows absorbed by financial assets:**	**2,817,350,094**	**8,194,805,590**
	- financial assets held for trading	996,973,444	1,686,133,438
	- financial assets designated at fair value		
	- other assets obligatorily measured at fair value	12,989,311	
	- financial assets measured at fair value through other comprehensive income	(217,284,213)	(58,106,098)
	- financial assets measured at amortised cost	2,022,512,160	6,704,733,262
	- other assets	2,159,392	(137,955,012)
3.	**Cash flows generated by financial liabilities:**	**(3,266,903,257)**	**(9,173,039,923)**
	- financial liabilities measured at amortised cost	(1,884,877,255)	(7,759,612,755)
	- financial liabilities held for trading	(1,333,684,071)	(1,573,201,886)
	- financial liabilities designated at fair value		
	- other liabilities	(48,341,931)	159,774,718
	Net cash flows absorbed/generated by operating activities	**752,641**	**(898,856,853)**
B.	**INVESTING ACTIVITIES**		
1.	**Cash flows generated by:**	**0**	**0**
	- sales of equity investments		
	- dividends from equity investments		
	- sales of property, plant and equipment		
	- sales of intangible assets		
	- sales of business units		
2.	**Cash flows absorbed by:**	**(752,965)**	**0**
	- purchases of equity investments		
	- purchases of property, plant and equipment	(752,965)	
	- purchases of intangible assets		
	- purchases of business units		
	Net cash flows absorbed/generated by investing activities	**(752,965)**	**0**
C.	**FUNDING ACTIVITIES**		
	issue/purchase of treasury shares		898,857,120
	issue/purchases of equity instruments		
	distribution of dividends and other purposes		
	Net cash flows absorbed/generated by funding activities	**0**	**898,857,120**
D	**(A+B+C) NET CASH FLOWS ABSORBED/GENERATED DURING THE PERIOD**	**(324)**	**267**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

The cash flow statement was prepared following the indirect method, whereby flows deriving from operating activities are represented by the profit/loss for the year rectified of effects due to operations of a non-monetary nature.

Reconciliation

Items	*31/12/2018*	*31/12/2017*
Cash and cash equivalents at the beginning of the period	331	64
Total net cash flows absorbed/generated during the period	(324)	267
Cash and cash equivalents: effect of changes in exchange rates		
Cash and cash equivalents at the end of the period	7	331

NOTES
TO THE
FINANCIAL
STATEMENTS

Part A
Accounting Policies

A.1 - GENERAL INFORMATION

Section 1 - STATEMENT OF COMPLIANCE WITH THE INTERNATIONAL ACCOUNTING STANDARDS

These separate Financial Statements, in application of Italian Legislative Decree No. 38 of 28 February 2005, have been drawn up according to the International Accounting Standards issued by the International Accounting Standards Board (IASB) and the related interpretations by the IFRS Interpretations Committee endorsed by the European Commission, as established by EU Regulation No. 1606 of 19 July 2002, and in force at 31 December 2018.
The international accounting principles were applied following the indications set forth in the "Framework for the preparation and presentation of financial statements" (the Framework).
In the absence of an accounting standard or interpretation specifically applicable to a transaction, other event or circumstance, the Company Management used its own judgement in developing and applying an accounting standard, in order to provide disclosure that is:
- significant for the purposes of financial decisions made by users of the financial statements;
- reliable, so that the financial statements:
  - provide a true representation of the financial position and equity, business performance and cash flows of the Bank;
  - reflect the economic substance of the transactions, other events and circumstances, and not merely their legal form;
  - are neutral, i.e. unbiased;
  - are prudent;
  - are complete, with reference to all significant aspects.

In exercising this judgement, the Company Management, after considering their applicability, referred to the following sources, in decreasing order of importance:
- the rules and application guidelines contained in the accounting standards and in the related interpretations dealing with similar or related cases;
- the definitions, recognition criteria, and measurement concepts in accounting for assets, liabilities, revenues and costs contained in the Framework.

In expressing judgements, the Company Management may also consider:
- the rules most recently issued by other entities responsible for establishing accounting standards, which use a conceptually similar framework in developing the accounting standards;
- other accounting literature;
- generally accepted practices in the sector.

In compliance with Article 5 of Italian Legislative Decree No. 38 of 28 February 2005, if, in exceptional cases, the application of a provision of the International Accounting Standards were to be incompatible with the true and accurate representation of the equity and financial situation and the economic result, this provision would not be applied. The Notes to the Financial Statements provide explanations for these derogations and their influence on the presentation of the equity/financial situation and the economic result.
In the financial statements, any profits deriving from such derogation would be recorded in a reserve which could be distributed only to the extent of the actual amount recovered.

Section 2 - GENERAL PRINCIPLES FOR PREPARATION OF THE FINANCIAL STATEMENTS

The separate Financial Statements have been prepared in accordance with the IAS/IFRS accounting standards issued by the International Accounting Standards Board (IASB) and the related interpretations issued by the IFRS Interpretations Committee (IFRIC), endorsed by the European Commission and subject to mandatory application in

2018, and in accordance with the assumptions indicated in the IASB Framework for the preparation and submission of financial statements. No exceptions were made to application of the IAS/IFRS accounting standards.
For an overview of the standards endorsed during 2018 or those endorsed in previous years, the application of which is provided for in financial year 2018 (or future years), please see “Section 4 - Other Information” below.
The communications of the Supervisory Bodies (Bank of Italy, CONSOB and ESMA) were also considered, if they were applicable, providing recommendations on the disclosure to be made in the Financial Statements on aspects of the greatest significance or on the accounting treatment of particular transactions.
The separate Financial Statements at 31 December 2018 were prepared on the basis of the provisions contained in Circular no. 262 of 22 December 2005 issued by the Bank of Italy “Banking Financial Statements: Formats and Rules for Compilation”, as amended by the fifth update of 22 December 2017.
The separate Financial Statements are made up of the balance sheet, the income statement, the statement of comprehensive income, the statement of changes in shareholders’ equity, the cash flow statement and the notes to the financial statements and are accompanied by the directors’ report on operations, on the economic results achieved and on the Bank’s financial situation and capital.
The Bank, controlled by the Parent Company Banca Monte dei Paschi di Siena S.p.A., which draws up consolidated financial statements compliant with the IAS/IFRS for public use, presents its own separate financial statements as its sole annual financial statements.
The Consolidated Financial Statements are drawn up by the Parent Company Banca Monte dei Paschi di Siena S.p.A. - with registered office in Piazza Salimbeni No. 3 - Siena, enrolled in the Banking Register and the Banking Groups Register with No. 5274 - and are made available to the public at the said registered office.
The Financial Statements have been prepared with clarity, and provide a true and accurate representation of the financial situation, equity and income of the year.
In the Notes to the Financial Statements, all of the information required by the international accounting standards and the provisions contained in Bank of Italy Circular no. 262 is provided, in addition to further non-obligatory information considered necessary to provide a true, correct, relevant, reliable, comparable and comprehensible representation.
The balance sheet, income statement and statement of comprehensive income consist of numbered items, sub-items (identified by letters), and by additional details (the “of which” of the items and sub-items). The items, sub-items and related details constitute the financial statement accounts.
The prior-year balance has also been reported for each item of the balance sheet, income statement and statement of comprehensive income. If the account balances are not comparable, the prior-year balances are adjusted. The lack of comparability and the restatement or the impossibility of restatement are noted and discussed in the Notes to the Financial Statements.

In consideration of first application of the standards IFRS 9 and IFRS 15, the related impacts of which were reflected through an adjustment of the balances of the opening shareholders’ equity at 1 January 2018, we can note that the MPS Group - and within it the Bank - utilised the option provided for in the aforementioned standards not to restate the comparative data. Therefore, the financial and economic balances of the previous year, as they were prepared with specific reference to financial instruments in accordance with the standard IAS 39 previously in force (that is with the accounting standards in force as of 31 December 2017 and used for the purposes of preparing the Financial Statements at the same date, to which you are referred), are not fully comparable with the new accounting categories and with the related measurement criteria introduced by the new standard. Taking into account that, at the moment the 5th update of Bank of Italy Circular no. 262 was issued, the Supervisory Body referred back to the competent corporate bodies the form and content of the disclosure related to the transition to IFRS 9, the MPS Group and, within it, the Bank, in order to bring the comparative data at 31 December 2017 in line with the new official formats provided for in the 5th update of Bank of Italy Circular 262 in force from 1 January 2018, made the following reclassifications, on a merely conventional basis and without changing the corresponding figures. As regards the balance sheet asset and liability items:

- item 20 "*Financial assets held for trading*" is reclassified to item 20 "*Financial assets measured at fair value through profit or loss*", sub-item a) "*Financial assets held for trading*";
- items 60 and 70 "*Receivables from banks*" and "*Receivables from customers*" are reclassified to item 40 "*Financial assets measured at amortised cost*", respectively to sub-items *a) and b)*;
- item 40 "*Financial assets available for sale*" is reclassified to item 30 "*Financial assets measured at fair value through other comprehensive income*";
- item 120 "*Other assets*", in relation to improvements of assets owned by third parties, was reclassified to item 80 "*Property, plant and equipment*";
- items 10, 20 and 30, respectively, "Payables to banks", "Payables to customers" and "Outstanding securities" are reclassified to item 10 "Financial liabilities measured at amortised cost", respectively to sub-items *a), b) and c)*;
- the balances related to item 100 "*Other liabilities*" were reallocated to the new item 100 "Provisions for risks and charges, sub-item *a) commitments and financial guarantees given*, not present in the 2017 statements".

With reference to the income statement:

- item 130 "*Net value adjustments for credit risk of*" now includes previous sub-items "*a) receivables*" in the new sub-item "*a) Financial assets measured at amortised cost*" and "*b) Financial assets available for sale*" in "b*) Financial assets measured at fair value through other comprehensive income*".
- item 130 "*Net value adjustments due to impairment of*" sub-item *d) "other financial transactions*" is reclassified to the new item 170 "*Net provisions for risks and charges*" sub-item "*a) commitments and guarantees given*".

At the same time the comparative balances at 31 December 2017, present in the tables of part B "*Information on the balance sheet*" and of part C "*Information on the income statement*" of the Notes to the Financial Statements, were stated according to the conventional reclassifications indicated above.

The section "Disclosure on first application of the standards IFRS 9 and IFRS 15" contains the reconciliation statements that illustrate in detail the reclassifications made between the items of the official formats previously in force and those of the new official formats provided for in Bank of Italy Circular no. 262.

Assets and liabilities and costs and revenues are not offset, except where allowed or required by the International Accounting Standards or the provisions of Bank of Italy Circular no. 262.
In the tables of the balance sheet, income statement and statement of comprehensive income items with a zero balance for the year and for the prior year are not presented. If an asset or liability can be booked to more than one balance sheet item, the Notes to the Financial Statements provide an explanation of its referability to accounts other than the account in which it is recognised, if necessary, for the purpose of understanding the financial statements.
Revenues are reported in the income statement, the statement of comprehensive income and the related section of the Notes to the Financial Statements without a +/- sign, while costs are indicated in brackets.
The statement of comprehensive income, starting from the profit (loss) for the year, presents the income components recognised against the valuation reserves, net of the related tax effect, in accordance with the international accounting standards. Comprehensive income is presented providing separate evidence of the income components which will not in future be recognised in the income statement and of those which, on the contrary, may subsequently be reclassified in the profit (loss) for the period if certain conditions are fulfilled.
The statement of changes in shareholders' equity shows the breakdown of and changes in shareholders' equity during the reporting and previous periods, divided into share capital (ordinary shares), capital and profit reserves, reserves from the valuation of accounting assets and liabilities, equity instruments and operating results. Treasury shares in the portfolio are recognised as a reduction of shareholders' equity.

The cash flow statement was prepared following the indirect method, whereby flows deriving from operating activities are represented by the income/loss for the year rectified by the effects of operations of a non-monetary nature. Cash flows are divided into those deriving from operating activities, those provided by investing activities and those produced by funding activities. In the statement, cash flows provided during the year are indicated without a sign, while those used are indicated in brackets.
In compliance with Article 5 of Italian Legislative Decree No. 38 of 28 February 2005, the financial statements have been prepared using the Euro as the functional currency. In particular, the balance sheet, the income statement, the statement of comprehensive income and the statements of changes in shareholders' equity are prepared in Euro units, whilst the Notes to the Financial Statements are in Euro thousands. Tables that do not contain any figures were omitted in the Notes to the Financial Statements.
The Financial statements have been drawn up with the view of the company as a going concern, in accordance with the accruals concept, observing the principles of the importance and significance of information, and of the prevalence of substance over form, as well as in order to favour consistency with future presentations.
Items with different natures or purposes have been presented separately, unless the related amounts were considered immaterial. When necessary, the amounts indicated in the Financial Statements were adjusted to reflect events subsequent to the reporting date which, pursuant to the standard IAS 10, involve the obligation of making an adjustment (adjusting events). Subsequent events that do not involve adjustments and that hence reflect circumstances that occurred after the reporting date (non-adjusting events) are disclosed in section 3 below when relevant and able to influence the economic decisions of users.

Disclosure on first application of the accounting standard IFRS 15 - Revenue from Contracts with Customers

EU Regulation no. 1905 of 22 September 2016 endorsed the new international accounting standard IFRS 15 "Revenue from Contracts with Customers", mandatorily applicable from 1 January 2018, with which a single framework of reference was introduced for the recognition of revenue deriving from contracts with customers, replacing the accounting standards IAS 18 "Revenue" and IAS 11 "Construction Contracts" and related interpretations (IFRIC 13, IFRIC 15, IFRIC 18, SIC 31).

The new standard proposes a model according to which an entity must recognise revenue so as to faithfully present the process of transferring goods and services to customers and in an amount that reflects the consideration to which the entity expects to be entitled in exchange for the goods or services provided. On this point, the standard provides for five steps:

1. identification of the contract, defined as an agreement (written or verbal) with commercial substance between two or more parties which creates in relation to the customer legally enforceable rights and obligations;
2. identification of the "performance obligations" contained in the contract;
3. determination of the price of the transaction as the consideration that the entity expects to be entitled to in exchange for the transfer of goods or the provision of services to the customer, in keeping with the techniques provided for in the Standard and depending on the presence of any financial components;
4. allocation of the transaction price to each "performance obligation" provided for in the contract;
5. recognition of the revenue when the obligation is settled, taking into consideration the fact that the services could be rendered not in one specific moment, but also over a period of time.

The services that entailed recognition in the income statement of fee and commission income were analysed, as the Bank does not have other kinds of revenue within the scope of IFRS 15, with the objective of checking the correct method of recognising revenue. In detail, the analysis focused on the "variable" revenue components and on those potentially subject to reversal, in particular those attributable to the activity of placing third-party products.

On the basis of the analyses performed, it emerged that the methods of recognising revenue introduced by the new accounting standard are in line with the accounting treatment previously in force.
The accounting standard IFRS 15 makes explicit the need to recognise a liability against the payments received but subject to possible reversal (so-called "refund liabilities"), but no fee and commission types falling within this category were noted.
As well as the quantitative impacts, the new standard requires greater disclosure on the nature, amount, timing and degree of uncertainty of revenue, as well as on the cash flows deriving from contracts with customers.

Disclosure on first application of the accounting standard IFRS 9- Financial Instruments

The legislative provisions

Regulation no. 2067 of 22 November 2016 endorsed the new international accounting standard IFRS 9 "Financial Instruments", mandatorily applicable from 1 January 2018, which governs the stages of classification and measurement, impairment and hedge accounting in relation to financial instruments, replacing the accounting standard IAS 39 "Financial Instruments: Recognition and Measurement".
IFRS 9 is structured in the three different areas of classification and measurement of financial instruments, impairment and hedge accounting.

Requirements for the classification and measurement of financial assets and liabilities according to IFRS 9

The standard IFRS 9 establishes that the classification of financial assets depends on the combination of the two following drivers:

1. Business Model of the entity: which reflects the objectives that the company management intends to pursue by holding financial assets. In detail:
   - "Held To Collect" (HTC), if the objective is to receive the contractual cash flows, keeping the financial instrument until maturity;
   - "Held to Collect and Sell" (HTC&S), if the financial assets are held with the objectives of receiving the contractual cash flows over the duration of the asset and of collecting the proceeds deriving from its sale;
   - "Other", if the objectives are different with respect to those described in the previous points, ascribable, for example, to the intention to receive cash flows through a trade ("Sell").
2. Contractual characteristics of the cash flows: according to whether the cash flows are based exclusively on principal and interest (so-called "Solely Payments of Principal and Interest", or SPPI) or whether, on the contrary, they depend also on other variables (for example, shares in profits, such as dividends, or repayment of the invested capital according to the financial performance of the issuer, etc.). The checks carried out in order to ascertain the contractual characteristics of the cash flows are indicated with the term "SPPI test".

On the basis of the combinations between the business model and the contractual characteristics of the cash flows, it is possible to identify the following accounting categories:

- financial assets measured at amortised cost: these include debt instruments (loans and securities) with business model "Held to Collect", the contractual terms of which are represented solely by payment of principal and interest (SPPI test passed);
- financial assets measured at fair value through other comprehensive income, with passage through the income statement of the measurement and realisation components: these include debt instruments (loans and securities)

with business model "Held to Collect and Sell", the contractual terms of which are represented solely by payment of principal and interest (SPPI test passed);
- financial assets measured at fair value through profit or loss: these include all assets held for trading, including derivative instruments not for hedging and, irrespective of the business model, assets that must be measured obligatorily at fair value because the cash flows do not represent solely payment of principal and interest (SPPI test not passed). These therefore include all equity securities, unless the entity chooses the irrevocable option of classifying them in the category of financial assets designated at fair value through other comprehensive income, with no passage through the income statement of the measurement and realisation components (with the exception of dividends which continue to be recognised in the income statement).

In addition to the categories illustrated above, there is the option to use the accounting category of financial assets designated at fair value through profit or loss; this option is irrevocable and is permitted only to eliminate or reduce significantly an inconsistency in the measurement or recognition that otherwise would result from measurement of the asset or liability or from the recognition of the related gains and losses on a different basis (so-called "accounting asymmetry").
In relation to the new classification rules based on the characteristics of the cash flows, IFRS 9 eliminates the rules on separating embedded derivatives from financial assets not measured at fair value through profit or loss.

With reference to financial liabilities, the new accounting standard IFRS 9 confirms the rules on classification and measurement provided for in IAS 39, on the basis of which the same are subject to measurement at amortised cost, with the exception of financial liabilities held for trading, including derivative liabilities, and financial liabilities for which the option of designation at fair value through profit or loss is taken.

In relation to this last type of liability, IFRS 9 states that changes in fair value associated with own creditworthiness must be recognised as a counter-entry of a specific shareholders' equity reserve, which will not be subject to subsequent "reversal" to the income statement, even if the liability is settled or extinguished.

If the changes in fair value associated with own creditworthiness create or amplify an accounting asymmetry, the entire change in fair value of the liability must be booked to the income statement.

IFRS 9 impairment methodology based on expected losses (ECLs)

On the basis of the standard IFRS 9, all financial assets not subject to measurement in the financial statements at fair value through profit or loss, represented by debt securities and loans, and off-balance-sheet exposures (commitments and guarantees given) must be made subject to the new impairment model based on expected losses (ECLs - Expected Credit Losses). The objective of the new approach is to guarantee quicker recognition of losses compared to the previous model of IAS 39, on the basis of which losses had to be recognised only in the presence of objective evidence that emerges after initial recognition of the asset (the so-called "incurred losses" model). In detail, the impairment model introduced by the accounting standard IFRS 9 is based on the concept of "forward-looking" measurement, that is on the notion of Expected Credit Loss, be it calculated at 12 months (stage 1) or for the entire residual life of the instrument (lifetime loss for stage 2 and stage 3). In particular, the model provides for the financial assets being classified in three distinct "stages" to which correspond different measurement criteria:
- Stage 1: to be measured on the basis of an estimate of expected loss having as reference a time horizon of one year. Stage 1 comprises performing financial assets for which no significant increase in credit risk has been observed compared to the date of initial recognition;

- Stage 2: to be measured on the basis of an estimate of expected loss having as reference a time horizon of the entire residual life of the financial asset. Stage 2 comprises financial assets which have suffered a significant increase in credit risk compared to the date of initial recognition;
- Stage 3: to be measured on the basis of an estimate of expected loss which assumes a probability of default of 100%. Stage 3 comprises financial assets considered impaired.

According to the Expected Credit Losses calculation model, the losses must be recorded not only making reference to the objective evidence of impairment already manifest at the reporting date, but also on the basis of the expectations of future impairment losses not yet evident, which must reflect:
- the probability of the occurrence of different scenarios;
- the effect of discounting through the use of the effective interest rate;
- historical experience and current and future measurements.

Hedge Accounting

With reference to hedge accounting, the new rules introduced by IFRS 9 have as their objective to guarantee greater alignment between the accounting presentation of hedges and the underlying operating logics (risk management); the said rules regard, however, the "macro-hedging" model for which an ad hoc and separate project with respect to IFRS 9 has been undertaken, although as of today this has not led to an accounting standard.

The MPS Group's choices

It is opportune to present a premise on the choices of a "general" nature made by the MPS Group on the subject of early application permitted by the standard, of recognising impacts deriving from application of the new impairment rules on own funds, according to the recent amendments introduced by the prudential regulations, and of presenting the comparative balances in the year of first application of the standard:
- the Group, if the regulatory conditions are fulfilled, decided to utilise the option of applying in advance, starting from financial year 2017, the new rules provided for in the standard IFRS 9 on the presentation of gains and losses on liabilities in the fair value option attributable to changes in own creditworthiness. The accounting treatment for the aforementioned liabilities involves the changes in fair value associated with own creditworthiness being recognised as a counter-entry of a specific shareholders' equity reserve ("Valuation reserves"), unless this treatment is such as create or amplify an accounting asymmetry in the economic result; in this last case the entire change in fair value of the liability must be booked to the income statement;
- with reference to the ways of presenting the effects of first application of the standard, the Group exercised the option provided for in paragraph 7.2.15 of IFRS 9 and in paragraph E1 and E2 of IFRS 1 "First-Time Adoption of International Financial Reporting Standards", according to which - without affecting the retrospective application of the new rules on measurement and presentation laid down by the standard - mandatory restatement on a uniform basis of the comparative data in the financial statements of first application of the new standard is not provided for. According to the indications contained in the document issuing the 5th update of Bank of Italy Circular 262 "Banking Financial Statements: Formats and Rules for Compilation", banks that make use of the exemption from the requirement of redetermining the comparative figures must, in any case, include, in the first financial statements drawn up on the basis of the new Circular 262, a reconciliation statement showing the methodology used and providing a reconciliation between the figures of the last financial statements approved and the first financial statements drawn up on the basis of the new provisions. The form and content of the disclosure are besides referred back to the competent corporate bodies.

Below is a brief examination of the main areas of impact of the new accounting standard as previously defined and of the main choices made in this regard by the MPS Group.

Classification and Measurement

On the basis of what is explained above, at the moment of transition to IFRS 9, the MPS Group therefore proceeded to define the classification of financial instruments on the basis of the new accounting categories provided for in IFRS 9 - taking into account the “business model” at 1 January 2018 and the characteristics of the contractual flows of the instrument at the date of origin of the same - and to carry out a new measurement of the same on the basis of the respective measurement criteria.

In defining the “business model”, at the level of both the Group and the single legal entity, all the relevant information was taken into consideration, including the historical data related to past sales, methods of measuring and reporting the performance of financial assets, methods of managing and measuring risks that can affect the performance of financial assets, and top management remuneration policies. Specific guidelines were therefore prepared with the aim of defining the business model of the Group and of its subsidiaries and any changes to it. For the portfolio of financial assets measured at amortised cost, considering that the objective of the business model is to collect the related cash flows, the criteria were defined for admissibility of sales on the occurrence of certain circumstances (such as a significant increase in credit risk or sales close to maturity) or in relation to the insignificance of the same in terms of amount or frequency.

As regards the SPPI test the Group’s methodological approach was defined and the target models, in terms of procedures and processes, were implemented for the performance of the test on all financial assets, represented by either debt securities or loans. In the context of the aforementioned methodological approach, the specific proceeding aimed at ascertaining the passing of the so-called “Benchmark Cash Flow Test” was defined. This test is necessary in the presence of financial instruments that have a modified time value of money, represented, by way of example, by a misalignment between the frequency with which the interest rate is fixed for payment of the respective instalment (fixing) and the reference rate (tenor).

The analyses that were carried out are illustrated below. They were done on the basis of a specific tool developed internally, based on a checklist of indicators aimed at ascertaining the passing of the SPPI test, rather than on the basis of information coming from external providers.

For the portfolio of debt securities in being at 31 December 2017 held with a Held to Collect rather than a Held to Collect and Sell business model the so-called SPPI test was performed, in order to verify the possibility of classifying the securities in question respectively in the accounting categories of “Financial assets measured at amortised cost” and “Financial assets measured at fair value through other comprehensive income”. The analyses carried out revealed that a very small percentage of debt instruments failed to pass the test, both as a number and as countervalue. These were represented by subordinated or structured securities, and they were therefore classified in the accounting category of “Other financial assets obligatorily measured at fair value through profit or loss”.

For financial instruments represented by loans in being at the date of FTA of IFRS9 (1/1/2018), a specific study was carried out on each position managed by the Corporate Finance Department while, for loans under the responsibility of the Credit Department, the work was done on two tracks, with a precise check on “particular” positions (loans in pools, IPRE positions, restructured loans, loans in foreign currencies) and with an analysis by uniform clusters on the remaining positions.

As regards new operations completed during 2018 a precise analysis of the single loan contracts was carried out. Assets represented by UCITS units were classified among "other financial assets obligatorily measured at fair value", also on the basis of the clarifications provided by the IFRIC, as will be better illustrated below. As regards equity securities held with the intention of a strategic investment, not having trading purposes and not classifiable as exclusive control, association or joint control, the instruments for which to take the option of designation at fair value through other comprehensive income were identified.

IFRS 9 impairment methodology based on expected losses (ECLs)

As regards the area of impairment:
- the methods were defined for measuring the evolution (or "tracking") of the credit quality of the positions present in the portfolios of financial assets measured at amortised cost and at fair value with a counter-entry to shareholders' equity;
- the parameters were defined for determining the significant increase in credit risk, for the purposes of correct allocation of performing exposures in stage 1 or stage 2. With reference, instead, to impaired exposures, the alignment of the definitions of accounting and regulatory default - already present today - makes it possible to consider identical the current logics for classification of exposures in the category of "impaired" ones with respect to the logics for classification of exposures in stage 3;
- the models were prepared, including the forward-looking information; these are to be used both for the purposes of stage assignment (lifetime PD) and for the purposes of calculating the expected credit loss at one year (to be applied to exposures in stage 1) and lifetime (to be applied to exposures in stage 2 and stage 3).

With reference to the "tracking" of the credit quality, a precise analysis was carried out of the credit quality of each single relationship (both in the form of nominal exposure and in credit form), for the purposes of identifying any "significant increase" in credit risk from the date of first recognition and the consequent need for classification in stage 2, and likewise, the conditions for re-entry into stage 1 from stage 2. The choice made involves, case by case and at every reporting date, a comparison - for "staging" purposes - between the credit quality of the financial instrument at the moment of measurement and that at the initial moment of disbursement or purchase. In relation to what is explained above, the elements that constitute the crucial principles to be taken into consideration for the purposes of the assessments on "transfers" between different stages are the following:
- a change (beyond certain thresholds) of lifetime probabilities of default with respect to the moment of initial recognition in the financial statements of the financial instrument. This is, therefore, an assessment carried out adopting a "relative" criterion, which represents the main "driver";
- any presence of a past-due amount which - without affecting the significance thresholds identified in the standard - has been such for at least 30 days. In the presence of this element, in other words, the credit risk of the exposure is assumed, unless proven otherwise, to be "significantly increased" and, therefore, the "transfer" to stage 2 is a consequence (if the exposure was previously included in stage 1);
- any presence of forbearance measures, which - again as an assumption - entail the classification of the exposures among those whose credit risk is "significantly increased" compared to initial recognition;
- some of the indicators of the credit monitoring systems, in particular, the reference is to the so-called "watch-lists", that is to credit monitoring systems which, on the basis of the current credit quality of the debtor counterparty, highlight performing exposures above a certain level of risk (operating perimeter High Risk and in Reclassification and debtors with negative EBITDA).

With particular reference to the relative quantitative criterion applicable to loan exposures in relation to customers, the MPS Group decided to assume as reference the change between the lifetime cumulative forward-looking probability of default (PD) recognised at the origination of the contractual relationship and the probability of default recognised at the measurement date. The development of the model entailed the identification of specific internal thresholds of change between the PD recognised at the origination of the contractual relationship and the PD recognised at the measurement date differentiated by counterparty, initial rating class and vintage. Exceeding the aforesaid thresholds constitutes an expression of a significant increase in credit risk and the single credit line is consequently transferred from stage 1 to stage 2. The comparison is based on uniform residual durations[5] and on uniform PD models, for example if the definition of default changes over time, the lifetime cumulative forward-looking PD at origination is redetermined to take into account this new definition of default. The cumulative PDs involved in the comparison are based on the same model used for ECL purposes (e.g., definition of PIT - Point in Time - Ratings, macroeconomic scenarios, expected life/contractual life). In order to obtain an unequivocal classification result, a cumulative PD is used, which results from the weighted average of the cumulative PDs calculated for the single prospective scenarios using as weights the probabilities of the scenarios. The significance threshold is determined, measuring historically, using quantile regression analysis by cluster as level of ratio, between lifetime cumulative forward-looking PD at the reporting date and that at the origination date, which can be considered predictive of transfer to NPE[6]. The threshold is determined so as to minimise the so-called false positives and false negatives and maximise the true positives and true negatives.

Some particular considerations are then valid for the so-called "staging" of the securities. Unlike receivables, for this type of exposure, sale and purchase transactions subsequent to the first purchase (made with reference to the same ISIN) can usually be considered part of the ordinary activity of managing the positions (with the consequent need to identify a methodology to be adopted to identify sales and refunds in order to determine the residual quantities of the single transactions with which to associate a credit quality/rating to the origination to be compared with that of the reporting date). In this context, it was decided that the use of the "first-in-first-out" or "FIFO" methodology (for the recognition in the income statement of the ECL recorded, in the case of sales and refunds) would contribute to more transparent management of the portfolio, also from the point of view of the front office operators, enabling, at the same time, continual updating of the assessment of creditworthiness on the basis of the new purchases.

Finally, for securities which at the date of transition to the new standard had an "investment grade" rating (or one of a similar quality) the so-called "low credit risk exemption" provided for in IFRS 9 itself was used. On the basis of this all exposures with these characteristics were identified as exposures at low credit risk and therefore to be considered in stage 1, irrespective of the precise measurement of the change in credit risk; this latter, therefore, is relevant for staging purposes only if the rating at the reporting date is sub-investment grade.

For these last the relative quantitative criterion is based on the change in lifetime cumulative forward-looking PD between reporting date and origination date greater than a given threshold. For corporate issuers the multi-annual PD curve is the corporate one estimated entirely by the Group; for government issues the multi-annual PD curve is the one prepared on the basis of the Moody's matrix of defaults at 1 year of government securities. The cumulative PDs subject to comparison are corrected according to the macroeconomic scenarios. In order to obtain an unequivocal classification result, a cumulative PD is used, which results from the weighted average of the cumulative PDs calculated for the single prospective scenarios using as weights the probabilities of the scenarios. Exposures are classified in stage 2 if the ratio between lifetime cumulative forward-looking PD at the reporting date compared to

(5) *Therefore, the assessment at 31/12/T of the significant increase in credit risk of a thirty-year loan disbursed on 31/12/T-5 is made comparing the lifetime cumulative forward-looking PDs on the residual life of 25 years.*
(6) *Transfer to NPE is measured on multi-year horizons.*

that at the origination date exceeds a given significance threshold equal, for both corporate securities and government ones, to that used for corporate exposures in the form of loans.

Once the allocation to the different credit risk stages has been defined, the expected losses (ECLs) are determined, at the level of single transaction or security tranche, starting from the IRB/operating models, based on the parameters of Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD), on which opportune corrective actions are carried out, so as to guarantee their compliance with the specific prescriptions of IFRS 9. Among these actions, we can note, in particular, the adoption of a Point in Time (PIT) PD against the Through the Cycle (TTC) PD used for Basel purposes, the estimate of multi-period PD and, if appropriate, of LGD to determine, where necessary, the expected loss for the entire residual life of the financial instrument, the removal from the calculation of the LGD of the component linked to the adverse economic cycle (the so-called Downturn), and the use, in the context of the discounting process, of the effective interest rate of the single positions.

The measurement of financial assets - both performing ones and those included in stage 3 - reflects, in addition, the best estimate of the effects of future conditions, first of all those of the economic context, on the basis of which the forward-looking PDs and LGDs are conditioned. With reference to the incorporation of this information in determining the impairment of a receivable, a useful indication was received from the IFRS Transition Resource Group for Impairment of Financial Instruments (ITG or TRG) which tackled, among other things, the following questions: (i) whether it is sufficient to use a single scenario, or it is necessary to incorporate a plurality of scenarios in when estimating impairment; (ii) if it is necessary to incorporate a plurality of scenarios, what methodology must be adopted for this purpose. With regard to the subject in (i), the TRG observed that, when there is a non-linear relationship between the macroeconomic variables and the impairment losses, a single macroeconomic scenario cannot represent the entire distribution of possible scenarios; therefore, the estimate of impairment must necessarily be based on a plurality of scenarios. With regard to the subject in (ii), the TRG noted that two methodologies can be used, alternatively:

a) estimate of losses in every scenario considered and calculation of the average of the losses thus obtained, weighted for the probabilities of occurrence of each scenario;
b) Estimate of the losses on the basis of the "most-likely" scenario and subsequent correction of the amount thus obtained through the application of an "add-on" (also called "overlay adjustment") to take into account the less-likely scenarios.

The information on the future macroeconomic scenarios in which the Group could find itself operating affect the situation of the debtors with reference both to the "riskiness" of migration of the exposures to lower quality classes (regarding therefore the "staging") and the recoverable amounts (regarding therefore the determination of the expected loss on the exposures).
From a methodological point of view, several possible alternative approaches were analysed in order to take these elements into consideration. With respect to the different alternatives considered, the MPS Group decided to adopt approach a), applied through the procedures described below:

- the forecast figures of macroeconomic factors considered relevant for the estimate of the Group's risk factors are considered with a time horizon of three years under different scenarios;
- These figures are used as inputs of opportune models, developed internally by the Group, in order to incorporate the macroeconomic and forward-looking information into the risk parameters, PD ("Satellite Model") and LGD (Sensitivity Analysis);
- the expected loss is calculated in relation to each scenario, considering the multi-period PDs and the LGD adjusted according to that specific scenario;
- starting from the expected losses related to each scenario, the expected loss was determined as the average of the related losses weighted for the probability of occurrence of each scenario.

This approach makes it possible to consider any non-linearities in the relationship between macroeconomic factors, risk parameters and expected loss.
The forecasts of the (forward-looking) macroeconomic indicators, provided by an external consultant of leading standing and reprocessed internally by the Research Unit, are quantified on the basis of three possible future scenarios, which consider the economic variables considered relevant (Italian GDP, interest rates, unemployment rate, price of commercial and residential properties, inflation, stock indices), with a future time horizon of three years to which are assigned the respective probabilities of occurrence, determined internally by the Group. In more detail, alongside the "baseline" scenario considered most probable, that is the forecast macroeconomic scenario on the basis of which the MPS Group develops its projections in relation to economic/financial and risk data along a short- and medium-term time horizon, a better (decidedly favourable) and worse (unfavourable) alternative scenario was prepared.

Particular considerations are valid for exposures classified in "stage 3" (those corresponding - as indicated above - to the current perimeter of impaired assets). As regards more specifically impaired receivables, we can note that, although in the presence of substantial equivalence of the definition of credit-impaired financial asset present in IFRS 9 with respect to the accounting standard previously in force, the methods of calculating the lifetime ECL entailed methodological effects also for the purposes of the assessments to be made in this segment, mainly in relation to:
• the inclusion of forward-looking information, namely that related to macroeconomic scenarios, estimates and recovery times, the probability of migration to worse classes, and those that can have an effect on the value of the collateral or on the expected duration of the related recovery;
• the consideration of alternative recovery scenarios, namely those of sale of the credit assets, in connection with possible sales of portions of the impaired portfolio, in relation to the corporate objectives of reducing non-performing assets, to which must be attributed a probability of realisation, to be considered in the context of the overall assessment.
As regards the inclusion of forward-looking information, we can note that, also in relation to impaired exposures, the same methodological framework is used as that for performing receivables: the same three macroeconomic scenarios are considered in the time horizon of the next three years, according to the methods indicated above. As we have already stated, the forward-looking scenario component is aimed at capturing the non-linearity of the relationship between the macroeconomic variables and the measurement of the ECL, through analysis of the forecasting uncertainty of the variables used to prepare the scenario.
Moving on to analyse the alternative recovery scenarios, we can note that the MPS Group, in relation to the objectives of reducing the stock of impaired receivables, included in the business plans, and to the commitments made to the Supervisory Bodies, with specific reference to the so-called NPL Strategy, considers the sale of certain portfolios as the strategy that can, in certain conditions, maximise the recovery of the cash flows, also in consideration of the recovery times.
Putting the sale scenario alongside the ordinary one of recovery through internal management responds therefore to the requests received from the Supervisory Authorities. The aforementioned change in strategy provided for in the new plan was taken into consideration on first application of IFRS 9, a standard which, as already noted, features significant innovations with respect to IAS 39. In addition to what has been explained, we can observe that the TRG - on the impairment of financial instruments - also confirmed that the cash flows coming from the sale of a receivable in default must be considered in the estimate of impairment losses on condition that:
• the sale of the receivable is one of the recovery methods that the entity expects to carry out;
• the entity has no legal or operational limitations that affect the ability to sell the receivable;
• the entity has reasonable and adequate information in support of the "disposal" scenario.

The TRG also observes that:
• in order to support the expectations of the entity on the assumption that sales to third parties represent a recovery

method in the case of default, both past conduct of the entity and future expectations must be assessed, and these latter may differ from the conduct previously observed;
- to determine the recoverable amount, the relevant market information on the trading prices of the receivables must be considered;
- the inclusion of the amounts recoverable through sale for the purposes of estimating the expected losses is applicable to financial instruments classified in all stages (1, 2 and 3); this is because, in measuring the expected losses, IFRS 9 requires consideration of all possible scenarios irrespective of the stage in which the receivable is classified.

This said, the Group reflected in the measurement of impaired receivables, according to the IFRS 9 impairment model, the different recovery strategies proposed so as to align them in a manner proportional to a probability of sale defined consistently with the Group NPL Plan.
With reference to receivables classified in stages 1 and 2, the Group assessed with probability zero the sale scenario as recovery strategy of the said receivables, given the fact that the sales provided for in the business plans must be considered as non-recurring in the context of the usual credit recovery methods, because they respond to the specific request of the Supervisory Authority to reduce the stock of impaired receivables and constitute therefore a qualifying restraint of the Restructuring Plan.

Consequently, for impaired receivables, the “ordinary”, scenario which involves a recovery strategy based on collecting the receivable typically through legal actions, mandates to recovery companies, realisation of the mortgage guarantees, was supplemented - as recovery strategy - also by the scenario of sale of the same receivable. In the light of this, for a defined perimeter of bad loans and probable defaults having the characteristics of transferability, in order to determine the total expected loss of the exposures, the recoverable values on the basis of the ordinary internal recovery process and the amounts recoverable from sale, estimated on the basis of massive transactions on analogous portfolios and single names carried out by the Group or of transactions carried out on the market over the last few years, were weighted according to the portion of portfolio destined for sale, provided for in the NPL Strategy, with respect to the total of the portfolio transferable.

The perimeter of transferable impaired receivables was determined including positions with a certain attraction on the market as a consequence both of the fact that other banks that have already carried out sale operations and of the presence of expressions of interest already received; and further positions consequent to assessments of convenience carried out by the Parent Company’s competent bodies (e.g. presence of widened bad loans positions or high danger rates).

In particular, the recoverable value of the transferable impaired receivables was quantified as the average value between (i) the “value in the case of sale” (fair value) and (ii) the “value in the case of collection”, assuming as weights for weighting, respectively, the percentage of transferable receivables that the management plans to sell, as defined in the “NPL plan” approved by the Board of Directors, and the percentage that it plans to keep in the portfolio. We can observe that the “value in the case of collection” was determined according to the ordinary logics followed by the Group for the impairment of bad loans and probable defaults, that is to say on the basis of an analytical measurement for exposures of more than a certain threshold (of € 500 thousand) and on the basis of an analytical-statistical measurement for the others. The analytical-statistical measurement of “below-threshold” exposures involves grouping them together in uniform clusters in terms of credit risk. As illustrated above, we can remind you that the measurement of the value in the case of sale was done through historical analyses carried out by the Group and through market benchmarks.

We can note, for completeness, that also as regards impairment a specific “IFRS9 Methodological Impairment Framework” document was prepared observing the rules of IFRS 9, and this was approved at the competent governance levels.

Hedge Accounting

On first application, the Group decided to avail itself of the “opt out” option, that is to avail itself of the possibility of continuing to manage the hedging operations according to the hedge accounting rules provided for in IAS 39, currently endorsed (in the “carve-out” version). This choice will be the subject of a new assessment for reporting subsequent to financial year 2018. At the moment the Bank does not have any hedging operations in place.

Governance of transition to the new standard

The first application of the new accounting standard IFRS 9 required significant implementations - in terms of processes, procedures, methodologies, IT systems - which were governed through the establishment, from financial year 2016, of a specific project led by the Manager of the Parent Company’s Administration and Financial Statements Area, assisted actively by the representatives of the Risks, Credit, Commercial, Organisation, IT, Finance, Planning and Control and Internal Audit units.
The main decisions on the project were taken by a Guidance Committee and an Operational Committee, made up of all the managers of the corporate units involved directly and indirectly in implementing the new rules.
The process of determining and reporting the value adjustments is governed by two sets of corporate regulations: IFRS9 Methodological Impairment Framework which, read together with the Group’s Accounting Rules, defines the metrics and algorithms for estimating the expected value losses.
The activities of determining the ECL on performing and non-performing loans were modified and supplemented in accordance with the Group’s current governance which sees the areas of the Chief Lending Officer and the Chief Risk Officer responsible respectively, the former for determining the analytical impairment losses on non-performing loans, the latter responsible for measuring, with statistical methods, the expected losses on performing loans and for further measurements on a non-analytical basis of non-performing loans (e.g. scenario add-on).
The activities of calculating expected losses involve, as the fundamental step, the definition of the expected scenarios; the definition of the basic assumptions is the responsibility of the Research unit. As we have said the CRO Area is responsible for developing and implementing the models necessary for calculating the losses on loans; these models and methods are then subject to validation by the Risk Systems Validation Service, a unit which is independent from both the Business structures and the model development and implementation structures. The Validation audit entailed a review of the documentation concerning the design and development of the models, the given validation, the re-performance of the calculations.
The process of classifying financial instruments was regulated through an update of the Group’s accounting policies approved by the Parent Company’s Board of Directors and adopted by the subsidiaries. These Rules define and describe the elements making up the various business models with which the MPS Group operates and, jointly with the method of performing the SPPI test described in the Group Accounting Rules, make it possible to determine the correct approach to measuring financial assets. The process rules define instead the processes, actions, conduct and controls of the organisational units involved in the process.
In particular, with reference to loans, we can note that the loan granting processes were supplemented (i) to manage the performance of the SPPI test, carried out on the basis of the method developed internally and implemented in the specific tool available to the business structures and (ii) to describe the business model associated with each loan granted.

Finally, the method for determining the fair value of loans (input data, models, etc.) was supplemented in the aforementioned document "IFRS9 Methodological Impairment Framework".

Transition to the accounting standards IFRS 9 and IFRS 15

As indicated in the paragraph General accounting principles, the Group and, within it, the Bank, chose to avail itself of the option, provided for in the standard IFRS 9, not to restate the comparative data of the financial statements of first application of IFRS 9. In order to bring the 2017 comparative data back into the context of the accounting items provided for in the new official formats of Circular 262 the necessary reallocations were carried out, without changing the amounts, on the basis of the criteria indicated below. The present section also illustrates the reconciliations of the accounting balances at 1 January 2018 as a result of application of the new classification and measurement rules laid down in IFRS 9.

Method of reallocating the comparative data of the accounting tables to take into account the 5th update of Bank of Italy Circular 262.

The comparative balances of 2017 of the balance sheet and income statement items were reallocated on the basis of the new IFRS 9 items introduced by the 5th update of Bank of Italy Circular 262, with the following conventions:

• financial - assets:
- item 20 *Financial assets held for trading* is reallocated to item 20 *Financial assets measured at fair value through profit or loss*, sub-item a) *Financial assets held for trading*;
- items 60 and 70 "*Receivables from banks*" and "*Receivables from customers*" are reclassified to item 40 "*Financial assets measured at amortised cost*", respectively to sub-items *a) and b)*;
- item 40 "*Financial assets available for sale*" is reclassified to item 30 "*Financial assets measured at fair value through other comprehensive income*";
- the balance related to improvements of assets owned by third parties was reallocated to item 80 *Property, plant and equipment*; in the 2017 statements it was classified under item 120 *Other assets*.

• financial - liabilities:
- items 10, 20 and 30, respectively, "*Payables to banks*", "*Payables to customers*" and "*Outstanding securities*" are reclassified to item 10 "*Financial liabilities measured at amortised cost*", respectively to sub-items *a), b)* and *c)*;
- the balances related to item 100 "*Other liabilities*" were reallocated to the new item 100 "Provisions for risks and charges, sub-item *a) commitments and financial guarantees given*, not present in the 2017 statements".

• economic:
- item 130 *Net value adjustments for credit risk of:* now includes previous sub-items "*a) receivables*" in the new sub-item "*a) Financial assets measured at amortised cost*" and "*b) Financial assets available for sale*" in "b*) Financial assets measured at fair value through other comprehensive income*;
- item 130 "*Net value adjustments due to impairment of*" sub-item "*d) other financial transactions*" is reclassified to the new item 170 "*Net provisions for risks and charges*" sub-item "*a) commitments and guarantees given*".

BALANCE SHEET - ASSETS

(figures in € thousands)

Asset items circ. 262 4th update	*31 12 2017*	*Reclassifications*	*31/12/2017(*)*		*Asset items circ. 262 5th update*
10 Cash and cash equivalents	-			10	Cash and cash equivalents
			10,476,327	20	Financial assets measured at fair value through profit or loss
20 Financial assets held for trading	10,476,327		*10,476,327*	*a)*	*financial assets held for trading;*
30 Financial assets designated at fair value			-	*b)*	*financial assets designated at fair value;*
			-	*c)*	*other financial assets obligatorily measured at fair value*
40 Financial assets available for sale	69,495		*69,495*	30	Financial assets measured at fair value through other comprehensive income
50 Financial assets held to maturity			16,814,467	40	Financial assets measured at amortised cost
60 Receivables from banks	6,054,189		*6,054,189*	*a)*	*receivables from banks*
70 Receivables from customers	10,760,278		*10,760,278*	*b)*	*receivables from customers*
80 Hedging derivatives			-	50	Hedging derivatives
90 Value adjustment of financial assets subject to macro hedging (+/-)			-	60	Value adjustment of financial assets subject to macro hedging (+/-)
100 Equity investments	779		779 -	70	Equity investments
110 Property, plant and equipment	12,329	1	12,330	80	Property, plant and equipment
120 Intangible assets *of which: goodwill*			- -	90	Intangible assets *of which: goodwill*
130 Tax assets *a) current* *b) deferred*	499,496 *306,812* *192,684*		499,496 *306,812* *192,684*	100	Tax assets *a) current* *b) deferred*
140 Non-current assets and disposal groups held for sale	979,942		979,942	110	Non-current assets and disposal groups held for sale
150 Other assets	196,838	(1)	196,837	120	Other assets
Total assets	**29,049,673**	**-**	**29,049,673**		**Total assets**

(*) *These are the comparative balances of 2017 of the balance sheet items reallocated to the new IFRS 9 items.*

BALANCE SHEET - LIABILITIES

(figures in € thousands)

Liabilities and shareholders' equity items circ. 262 4th update	*31/12/2017*	*Reclassifications*	*31/12/2017(*)*	*Liabilities and shareholders' equity items circ. 262 5th update*
			22,845,978	10 Financial liabilities measure at amortised cost
10 Payables to banks	15,449,516		*15,449,516*	*a) payables to banks*
20 Payables to customers	6,939,911		*6,939,911*	*b) payables to customer*
30 Outstanding securities	456,551		*456,551*	*c) outstanding securities*
40 Financial liabilities held for trading	4,804,233		4,804,233	20 Financial liabilities held for trading
50 Financial liabilities measured at fair value			-	30 Financial liabilities measured at fair value
60 Hedging derivatives			-	40 Hedging derivative
70 Value adjustment of financial liabilities subject to macro hedging (+/-)			-	50 Value adjustment of financial liabilities subject to macro hedging (+/-)
80 Tax liabilities	-		-	60 Tax liabilities
90 Liabilities associated with assets held for sale			-	70 Liabilities associated with assets held for sale
100 Other liabilities	62,868	(3,063)	59,805	80 Other liabilities
110 Employee severance indemnities	2,603		2,603	90 Employee severance indemnities
120 Provisions for risks and charges:	27,781	3,063	30,844	100 Provisions for risks and charges:
		3,063	*3,063*	*a) commitments and financial guarantees given*
a) pensions and similar obligations	*4,602*			*b) pensions and similar obligations*
b) other provisions	*23,179*		*23,179*	*c) other provisions for risks and charges*
130 Valuation reserves		*4,602*	(2,242)	110 Valuation reserves
140 Redeemable shares	-		-	120 Redeemable shares
150 Equity instruments	-		-	130 Equity instruments
160 Reserves	110,427		110,427	140 Reserves
170 Share premiums	161,446		161,446	150 Share premiums
180 Capital	1,669,516		1,669,516	160 Capital
190 Treasury shares (-)			-	170 Treasury shares (-)
200 Profit (Loss) for the period (+/-)	(632,937)		(632,937)	180 Profit (Loss) for the period (+/-)
Total Liabilities and Shareholders' Equity	**29,049,673**	**-**	**29,049,673**	**Total Liabilities and Shareholders' Equity**

(*) *These are the comparative balances of 2017 of the balance sheet items reallocated to the new IFRS 9 items.*

INCOME STATEMENT

(figures in € thousands)

	Income statement items circ. 262 4th update	*31/12/2017*	*Reclassifications*	*31/12/2017[*]*		*Income statement items circ.262 5th update*
10	Interest and similar income	309,645		309,645	10	Interest and similar income
20	Interest expense and similar charges	(217,550)		(217,550)	20	Interest expense and similar charges
30	**Net interest income**	**92,095**		**92,095**	30	**Net interest income**
40	Fee income	43,195		43,195	40	Fee income
50	Fee expense	(48,232)		(48,232)	50	Fee expense
60	**Net fee and commission income**	**(5,037)**		**(5,037)**	60	**Net fee and commission income**
70	Dividends and similar income	1,885		1,885	70	Dividends and similar income
80	Net trading gains (losses)	18,071		18,071	80	Net trading gains (losses)
100	Gain (loss) on disposal or repurchase of:	8,421		8,421	100	Gain (loss) on disposal or repurchase of:
	a) loans	*8*		*8*		*a) financial assets measured at amortised cost*
	b) financial assets available for sale	*1,588*		*1,588*		*b) financial assets measured at fair value through other comprehensive income*
	d) financial liabilities	*6,825*		*6,825*		*c) financial liabilities*
110	Net gains/(losses) on financial assets and liabilities measured at fair value			-	110	Net gains/(losses) on financial assets and liabilities measured at fair value through profit or loss
120	**Operating income**	**115,435**		**115,435**	**120**	**Operating income**
130	Net value adjustments due to impairment of:	(827,798)		(838,432)	130	Net value adjustments for credit risk of:
	a) loans	*(781,221)*		*(781,221)*		*a) financial assets measured at amortised cost*
	b) financial assets available for sale	*(57,211)*		*(57,211)*		*b) financial assets measured at fair value through other comprehensive income*
	d) other financial transactions	*10,634*	(10,634)		140	Gains/(losses) on contractual changes without cancellations
140	**Net income from financial management**	**(712,363)**		**(722,997)**	**150**	**Net income from financial management**
150	Administrative expenses:	(95,155)	-	(95,155)	160	Administrative expenses:
	a) personnel expenses	*(30,713)*		*(30,713)*		*a) personnel expenses*
	b) other administrative expenses	*(64,442)*		*(64,442)*		*b) other administrative expenses*
			10,634	4,766	170	Net provisions for risks and charges
			10,634	*10,634*		*a) for credit risk related to commitments and guarantees given*
160	Net provisions for risks and charges	(5,868)		*(5,868)*		*b) other net provisions*
170	Net value adjustments on property, plant and equipment	(930)		(930)	180	Net value adjustments on property, plant and equipment
190	Other operating income/charges	6,369		6,369	200	Other operating income/charges
200	**Operating costs**	**(95,584)**		**(84,950)**	**210**	**Operating costs**
210	Profit (loss) from equity investments	(901)		(901)	220	Profit (loss) from equity investments
250	**Profit (Loss) from continuing operations before tax**	**(808,848)**		**(808,848)**	**260**	**Profit (Loss) from continuing operations before tax**
260	Income taxes for the year on profit from continuing operations	175,911		175,911	270	Income taxes for the year on profit from continuing operations
290	**Profit (Loss) for the period**	**(632,937)**	**10,634**	**(632,937)**	**300**	**Profit (Loss) for the period**

[*] *These are the comparative balances of 2017 of the balance sheet items reallocated to the new IFRS 9 items.*

Impacts of transition at 1 January 2018 to the new accounting standards IFRS 9 and IFRS 15

The Reconciliation statements between the Balance Sheet at 31 December 2017 (pursuant to IAS 39), which incorporates the reclassifications determined by the new classifications rules provided for in IFRS 9, illustrated above, and the Balance Sheet at 1 January 2018 (IFRS 9) are presented below. In these statements the accounting balances at 31 December 2017 (amounts determined under the terms of IAS 39) are changed as a result of the application of the new measurement and impairment logics, in order to determine the IFRS 9-compliant opening balances.
The statements include both the impacts of the transition to the accounting standard IFRS 9 and some reclassifications provided for specifically in the 5th update of Circular 262.

BALANCE SHEET - ASSETS

(amounts in thousands euro)

BALANCE SHEET - Assets — amounts in thousands of euro

	Asset items - Bank of Italy Circ. 262 4th update	at 31/12/2017 BALANCES	IAS 2 reclassifications	Classifications	Measurement: other	Measurement: impairment	Tax effects	at 01/01/2018 BALANCES		Asset items - Bank of Italy Circ. 262 5th update	notes
10	Cash and cash equivalents	-							10	Cash and cash equivalents	
				144,677	(10,811)			10,610,193	20	Financial assets measured at fair value through profit or loss	
20	Financial assets held for trading	10,476,327		-				*10,476,327*		*a) financial assets held for trading;*	
30	Financial assets designated at fair value			-						*b) financial assets designated at fair value;*	
				144,677	(10,811)			*133,866*		*c) other financial assets obligatorily measured at fair value*	*a)*
40	Financial assets available for sale	69,495		(10,951)				*58,544*	30	Financial assets measured at fair value through other comprehensive income	*b)*
50	Financial assets held to maturity			(133,726)		(141,036)		*16,539,705*	40	Financial assets measured at amortised cost	*c)*
60	Loans to banks	6,054,189				(42)		*6,054,147*		a) loans to banks	
70	Loans to customers	10,760,278		(133,726)		(140,994)		*10,485,558*		b) loans to customers	
80	Hedging derivatives							-	50	Hedging derivatives	
90	Value adjustment of financial assets subject to macro hedging (+/-)							-	60	Value adjustment of financial assets subject to macro hedging (+/-)	
100	Equity investments	779						779	70	Equity investments	
								-			
110	Property, plant and equipment	12,329	1					12,330	80	Property, plant and equipment	*d)*
120	Intangible assets							-	90	Intangible assets	
130	Tax assets	499,496					6,395	505,891	100	Tax assets	*e)*
	a) current	*306,812*					*5,848*	*312,660*		*a) current*	
	b) prepaid	*192,684*					547	*193,231*		*b) prepaid*	
140	Non-current assets held for sale and discontinued operations	979,942						979,942	110	Non-current assets held for sale and discontinued operations	
150	Other assets	196,838	(1)				(286)	196,551	120	Other assets	*d)*
	Total Assets	29,049,673	-	-	10,811	141,036	6,109	28,903,935		Total Assets	

a) The impact of the classification under item "20 c) other financial assets obligatorily measured at fair value" was € 144,677 thousand and is attributable to:
   i. loans that failed the SPPI (Solely Payments of Principal and Interest) test of € 133,726 thousand. The reasons for failing the SPPI test are attributable to restructuring processes with repayment methods subject to liquidity events and/or waivers "now for then";
   ii. other instruments that failed the SPPI test of € 10,951 thousand: mainly UCITS units, participatory financial instruments and other equity securities, other than shares, of insignificant amounts.

In addition, the consequent recognition of the loans in question at fair value, instead of at amortised cost, entailed a total decrease of € 10,811 thousand (cf. the column measurement - other) in the value of the reclassified loans.

b) The decrease of € 10,951 thousand was due to reclassification to item "20 c) other financial assets obligatorily measured at fair value" of financial instruments such as UCITS units which failed the SPPI test and equity securities other than shares (see the previous point).

c) "Financial assets measured at amortised cost" decreased by € 133,726 thousand owing to the reclassification to item "20 c) other financial assets obligatorily measured at fair value" of loans which failed the SPPI test (see comment on letter a). As regards instead the effect of the introduction of the new impairment model, there was a negative impact of € 140,994 thousand on loans to customers. For receivables from banks the impact was a negative € 42 thousand.

d) The 5th update of Bank of Italy Circular 262 specifies that "Property, plant and equipment" includes also the inventories of property, plant and equipment governed by IAS 2: these were therefore reclassified from "Other assets" to "Property, plant and equipment" inventories of goods for € 1 thousand.

e) The impacts on the item "Tax assets" were mainly due to the component "a) current". In particular, the increase of € 5,848 thousand is attributable to the reduction of current IRAP taxes as a result of higher write-downs on loans, fully deductible, carried out on FTA.

BALANCE SHEET - LIABILITIES

(amounts in thousands euro)

	Liabilities and shareholders' equity items - Bank of Italy Circ. 262 IAS 39	BALANCES at 31/12/2017	Reclassifications	Classifications	Measurement: other	Measurement: impairment	Tax effects	BALANCES at 01/01/2018		Liabilities and shareholders' equity items - Bank of Italy circ. 262 5th update	notes
								22,845,978	10	Financial liabilities measured at amortised cost	
10	Due to banks	15,449,516						*15,449,516*		a) due to banks	
20	Due to customers	6,939,911						*6,939,911*		b) due to customers	
30	Outstanding securities	456,551						*456,551*		c) outstanding securities	
40	Financial liabilities held for trading	4,804,233						*4,804,233*	20	Financial liabilities held for trading	
50	Financial liabilities at fair value							-	30	Financial liabilities at fair value	
60	Hedging derivatives							-	40	Hedging derivatives	
70	Value adjustments to financial liabilities subject to macro hedging (+/-)							-	50	Value adjustment of financial liabilities subject to macro hedging (+/-)	
80	Tax liabilities	-						-	60	Tax liabilities	
	a) current							-		*a) current*	
	b) deferred							-		*b) deferred*	
90	Liabilities associated with assets held for sale							-	70	Liabilities associated with assets held for sale	
100	Other liabilities	62,868	(3,063)					59,805	80	Other liabilities	a)
110	Employee severance indemnities	2,603						2,603	90	Employee severance indemnities	
120	Provisions for risks and charges:	27,781	3,063			1,887		32,731	100	Provisions for risks and charges:	b)
			3,063			1,887		*4,950*		*a) commitments and financial guarantees given*	
	a) pensions and similar obligations	4,602						*4,602*		*b) pensions and similar obligations*	
	b) other provisions	23,179						*23,179*		*c) other provisions for risks and charges*	
130	Valuation reserves	(2,242)		(237)		(101,174)		(103,653)	110	Valuation reserves	c)
140	Refundable shares	-						-	120	Refundable shares	
150	Equity instruments	-						-	130	Equity instruments	
160	Reserves	110,427		237	(10,811)	(41,749)	6,109	64,213	140	Reserves	d)
170	Share premiums	161,446						161,446	150	Share premiums	
180	Capital	1,669,516						1,669,516	160	Capital	
190	Treasury shares (-)							-	170	Treasury shares (-)	
200	Profit (Loss) for the period (+/-)	(632,937)						(632,937)	180	Profit (Loss) for the period (+/-)	
	Total Liabilities and Shareholders' Equity	**29,049,673**			**10,811**	**141,036**	**6,109**	**28,903,935**		**Total Liabilities and Shareholders' Equity**	

Details are provided below with the aim of reconciling, by type of financial instrument, the accounting categories of financial assets at 31 December 2017 (IAS 39 values) with the accounting categories of financial assets at 1 January 2018 (IFRS 9 values) according to the requirements of IFRS 7.42O:

(amounts in thousands euro)

	Asset items - Bank of Italy Circ. 262 4th update	BALANCES at 31/12/2017	Debt securities	UCITS	Loans	Equity securities	BALANCES at 01/01/2018		Asset items - Bank of Italy Circ. 262 5th update
				8,021	122,915		10,610,193	20	Financial assets measured at fair value through profit or loss
20	Financial assets held for trading	10,476,327		-			*10,476,327*		*a) financial assets held for trading;*
30	Financial assets designated at fair value			-					*b) financial assets designated at fair value;*
				8,021	122,915	2,930	*133,866*		*c) other financial assets obligatorily measured at fair value*
40	Financial assets available for sale	69,495		(8,021)		(2,930)	*58,544*	30	Financial assets measured at fair value through other comprehensive income
50				-		-	16,539,705	40	Financial assets measured at amortised cost
60	Loans to banks	6,054,189			(42)		*6,054,147*		a) loans to banks
70	Loans to customers	10,760,278			(274,720)		*10,485,558*		b) loans to customers

a) Provisions for risks related to commitments to disburse and to financial guarantees given, subject to the measurement rules of IFRS 9, are accounted for in the new item "100a) Provisions for risks and charges: commitments and financial guarantees given". Provisions for risks on commitments and guarantees, of € 3,063 thousand, previously presented among "Other liabilities" were therefore reclassified to this new sub-item.

b) Item "100 Provisions for risks and charges", as well as the reclassification of € 3,063 thousand pursuant to the previous point, is also affected by € 1,887 thousand of higher write-downs on commitments to disburse funds and guarantees given, as a result of application of the IFRS 9 model.

c) Item "110 Valuation reserves" suffered a negative impact of € 101,411 thousand, almost completely attributable to the elimination of IAS 39 write-downs on equity securities in the OCI option[1].

d) The negative impact, of a total of € 46,214 thousand, on item "140 Reserves" is attributable, in brief, to the following cases:
   - € -142,923 thousand before tax for application of the new impairment model, of which:
     - ◊ € -49.5 million for performing on-balance-sheet loan exposures due mainly to the inclusion of the lifetime expected losses on non-impaired assets classified in stage 2, as a consequence of the significant increase in the credit risk of the debtor with respect to that existing at the moment of first recognition of the receivable in the financial statements;
     - ◊ € -91.5 million for impaired on-balance-sheet loan exposures, due mainly to the inclusion of the scenario of sale of those portfolios for which disposal is expected;
     - ◊ € -1.9 million for off-balance-sheet exposures related to commitments to disburse funds and guarantees given;
   - € -10,811 thousand as a result of measurement at fair value deriving from the reclassification of receivables from "financial assets measured at amortised cost" to "other financial assets obligatorily measured at fair value" as a result of failing the SPPI test.
   - +€ 101,411 thousand as reclassification of net valuation reserves (of equity securities for € 35 thousand and UCITS of € 200 thousand) and, for € 101,174 thousand, as counter-entry to the elimination of IAS 39 write-downs on equity securities in the OCI option (cf. letter c);
   - +€ 6,109 of tax effects (in particular the counter-entry to profit reserves of FTA of IRAP taxation described in letter e) of the comments on the Balance Sheet - Assets.

[1] *At the moment of initial recognition the entity can choose irrevocably to present in other comprehensive income the subsequent changes in fair value of the investment in an equity instrument that comes within the scope of application of IFRS 9 which is neither held for trading nor a potential consideration recognised by a purchaser in a business combination to which IFRS 3 applies.*

The increase recognised in IFRS 9 adjusting provisions on transition at 1 January 2018 is ascribable to the new provisions on the subject of impairment (higher Expected Credit Losses - ECLs) on cash and endorsement exposures. A reconciliation of gross exposures and adjusting provisions on the portfolios subject to impairment is presented below:

RECONCILIATION GROSS EXPOSURES AND IAS 39 - IFRS9 PROVISIONS (REF. IFRS 7 SECT. 42P)

(amounts in thousands of euro)

	IAS 39 Item 40 - Financial assets available for sale Item 60 - Due from banks Item 70 - Loans to customers Item 140 - Financial assets	*Different presentation overdue interest receivable (Bank of Italy Cir. 262)*	*Reclassification of IAS 39 items 60 - Loans to banks and 70 Loans to customers to IFRS 9 item 20 Assets measured at fair value through profit or loss*	*Differences between IAS 39 value adjustments and IFRS 9 value adjustments*	*IFRS9 Item 30 - Financial assets measured at fair value through other comprehensive income Item 40 - Financial assets Amortised cost Item 120 - Non-current assets held for sale and discontinued operations*
Gross loan exposures					
- Non-impaired on-balance sheet exposures	15,342,079	(18)	(6,689)		15,335,372
Stage 1					*13,161,946*
Stage 2					*2,173,426*
- Impaired on-balance sheet exposures	6,834,792	(510,966)	(288,957)		6,034,869
Stage 3					6,034,869
Total on-balance-sheet exposures	**22,176,871**	**(510,984)**	**(295,646)**		**21,370,241**
- Non-impaired off-balance sheet exposures	5,157,645				5,157,645
Stage 1					*5,091,754*
Stage 2					*65,891*
- Impaired off-balance sheet exposures	39,059				39,059
Stage 3					39,059
Total off-balance sheet exposures	**5,196,704**				**5,196,704**
Value adjustments					
- Adjustments to non-impaired on-balance-sheet exposures	73,993	(17)	(41)	49,535	123,470
Stage 1				(11,309)	*5,693*
Stage 2				60,844	*117,777*
- Adjustments to impaired on-balance-sheet exposures	4,308,469	(510,966)	(161,873)	91,475	3,727,105
Stage 3					*3,727,105*
Total Adjustments to on-balance-sheet exposures	**4,382,462**	**(510,983)**	**(161,914)**	**141,010**	**3,850,575**
- Adjustments to non-impaired off-balance sheet exposures	1,512			762	2,274
Stage 1				(83)	215
Stage 2				845	2,059
- Adjustments to impaired off-balance sheet exposures	1,550			1,125	2,675
Stage 3				*1,125*	2,675
Total Adjustments to off-balance sheet exposures	**3,062**			**1,887**	**4,949**
Net loan exposures					
- Non-impaired on-balance sheet exposures	15,268,086		(6,648)	(49,535)	15,211,903
Stage 1					*13,156,254*
Stage 2					*2,055,649*
- Impaired on-balance sheet exposures	2,526,323		(127,084)	(91,476)	2,307,763
Stage 3					2,307,763
Total on-balance-sheet exposures	**17,794,409**		**(133,732)**	**(141,011)**	**17,519,666**
- Non-impaired off-balance sheet exposures	5,156,133			(762)	5,155,371
Stage 1				83	5,091,539
Stage 2				(845)	63,832
- Impaired off-balance sheet exposures	37,508			(1,125)	36,383
Stage 3				(1,125)	36,383
Total off-balance sheet exposures	**5,193,641**			**(1,887)**	**5,191,754**

A reconciliation between Shareholders' Equity at 31 December 2017 and Shareholders' Equity at 1 January 2018 after the transition to IFRS 9 is provided below, detailing the column "Changes in opening balances" of the Statement of Changes in Shareholders' Equity (cf. "Financial Statements"). The effects on Shareholder's equity amounted to € 147,625 thousand, of which - € 153,735 thousand as total impact of the new IFRS 9 impairment model.

(amounts in thousands of euro)

		Classification and Measurement				Impairment										
	Shareholders' equity at 31/12/2017	Business model change	SPPI test failure	Reserve reclassification		Measurement of loans at amortised cost		Measurement of securities at amortised cost		Commitments to disburse funds and guarantees given	Reserve reclassification on financial assets measured at fair value through other comprehensive income		IFRS 15 effects on Shareholders' equity	Tax effects	Total adjustments to Shareholders' equity at 01/01/2018	Shareholders' equity at 01/01/2018
				Valuation reserves	Profit reserves	Performing	Non-performing	Performing	Non-performing		Valuation reserves	Profit reserves				
Shareholders' equity	1,306,210		-10,811	-101,410	101,410	-49,543		-91,493		-1,887				6,109	-147,625	1,158,585

Section 3 - EVENTS AFTER THE REPORTING PERIOD

IAS 10, "Events after the Reporting Period" expressly governs the treatment to be applied to favourable or unfavourable events occurring between the reporting date and the date on which the Board of Directors authorises the financial statements for publication. The standard distinguishes between events requiring an adjustment to accounting data and events which do not require adjustment but necessitate the provision of disclosure should the events be significant or important. There has been nothing significant to report.

Section 4 - OTHER INFORMATION

Going concern

These financial statements have been drawn up considering appropriate the assumption of the Bank's continuation as a going concern.
With regard to the indications provided within the scope of Document no. 4 of 3 March 2010 issued jointly by Bank of Italy, CONSOB and IVASS, as updated, the Bank has the reasonable expectation of continuing with its operating existence in a foreseeable future and, therefore, it has prepared the Financial Statements in view of its continuation as a going concern.

List of IAS/IFRS international accounting standards and related SIC/IFRIC interpretations whose application is mandatory as from the 2018 financial statements

The standard IFRS 15 **"Revenue from Contracts with Customers"**, published by the IASB on 18 May 2014 and endorsed by the European Commission with Regulation no. 2016/1905 of 22 September 2016 and subsequent clarifications endorsed on 31 October 2017 with Regulation no. 2017/1987, replaces the previous standards on revenue: IAS 11 "Construction Contracts", IAS 18 "Revenue", IFRIC 13 "Customer Loyalty Programmes", IFRIC 15 "Agreements for the Construction of Real Estate", IFRIC 18 "Transfers of Assets from Customers" and SIC 31 "Revenue - Barter Transactions Involving Advertising Services".
The standard applies obligatorily starting from the first day of the first financial year beginning on 1 January 2018 or later.
The standard IFRS9 "**Financial Instruments**", issued by the IASB on 24 July 2014, governs the stages of classification and measurement of financial instruments, and the related impairment process and replaces the previous accounting standard IAS 39 "Financial Instruments: Recognition and Measurement". Macro hedging is not regulated under this standard; for this the IASB has decided to undertake an autonomous project.
The document was endorsed by the European Commission on 22 September 2016, with Regulation No. 2016/2067 and applies obligatorily starting from the first day of the first financial year beginning on 1 January 2018 or later.
On 12 September 2016, the IASB published the amendment to IFRS 4 **"Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts"**, later endorsed by the European Commission with Regulation no. 2017/1988 on 9 November 2017. The changes have as their objective to resolve, for companies that provide insurance, the problems associated with the application of the standard IFRS 9, before the implementation of the standard (IFRS 17) which will replace IFRS 4 on insurance contracts.
Specifically, this amendment introduced a series of changes, which allow:

- entities that issue insurance contracts, to recognise in the statement of comprehensive income (i.e. the OCI statement), instead of in the income statement, the effects deriving from the volatility that could arise in the

moment in which an entity applies IFRS 9 before applying the new standard IFRS 4 ("overlay approach").
- entities whose business consists predominantly of insurance, to make use of a temporary exemption from applying IFRS 9 initially up to 2021. Entities that defer application of IFRS 9 will continue to apply the current standard IAS 39 ("deferral approach").

The amendments apply as of 1 January 2018.
We can also note that on 14 November 2018 the IASB decided to defer the application of IFRS 17 by a year, from 2021 to 2022, extending also the possibility of extending, to 2022, the temporary exemption from application of the standard IFRS 9 granted to insurance companies. The deferment proposed will in any case be subject to public consultation, planned for 2019.
In addition, the following apply from 1 January 2018:
- the Amendments pursuant to the document "**Annual Improvements to IFRS Standards 2014-2016 Cycle",** endorsed by the European Commission with Regulation (EU) 2018/182 of 7 February 2018, which regard:
  - IAS 28 "Investments in Associates and Joint Ventures";
  - IFRS 1 "First-time Adoption of International Financial Reporting Standards";
  - IFRS 12 "Disclosure of Interests in Other Entities";

- the Amendments to IFRS 2 "**Classification and Measurement of Share-based Payment Transactions**", endorsed by the European Commission with Regulation (EU) 2018/289 of 26 February 2018, which provides some clarifications in relation to the following aspects:
  - the effects of vesting conditions on the measurement of a cash-settled share-based payment;
  - the classification of share-based payment transactions characterised by net settlement for tax purposes;
  - the recognition of a modification of the terms and conditions of a share-based payment, which changes the classification of the transaction from cash-settled to equity-settled;

- the Amendments to IAS 40 "**Investment Property: *Transfers of Investment Property"*,** endorsed by the European Commission with Regulation 2018/400 of 14 March 2018. The amendments clarify the moment of transfer of an asset from/to the category of "investment property", identified as a "change in use";

- IFRIC *Interpretation 22* "***Foreign Currency Transactions and Advance Consideration"***, endorsed by the European Commission with Regulation 2018/519 of 28 March 2018, which clarifies the accounting for transactions that include the receipt or payment of advance consideration in a foreign currency.

With the exception of first application of the accounting standards IFRS 9 and IFRS 15 for which please see the specific section "Disclosure on first application of the accounting standards IFRS 9 - Financial Instruments and IFRS 15 - Revenue from Contracts with Customers", the other amendments or interpretations did not have a significant impact on the Bank's financial and economic situation.

IAS/IFRS international accounting standards and related SIC/IFRIC interpretations endorsed by the European Commission, whose mandatory application is subsequent to 31 December 2018

On 13 January 2016 the IASB published the new standard IFRS 16 "***Leases***", which replaces the standard IAS 17 - Leases, and the interpretations IFRIC 4 - "Determining Whether an Arrangement contains a Lease", SIC 15 - "Operating Leases—Incentives" and SIC 27 - "Evaluating the Substance of Transactions Involving the Legal Form of a Lease".
The objective of IFRS 16 is to ensure that lessees and lessors provide relevant information in ways that faithfully represent the transactions. The information therefore provides to users of the financial statements the elements for assessing the effect of the lease on the entity's financial and equity situation, economic result and cash flows.

The new standard provides a new definition of lease and introduces a criterion based on control (right of use) in the use of an asset to distinguish leasing contracts from contracts for services, identifying as discriminants: identification of the asset, the lessor's right not to replace the same, the right to obtain substantially all the economic benefits deriving from use of the asset and the right to manage the use of the asset underlying the contract.

The transactions excluded from the scope of application of the standard include, in particular:
- intellectual property licences granted by the lessor under the terms of IFRS 15 "Revenue from Contracts with Customers";
- the rights held by the lessee on the basis of licence agreements under the terms of IAS 38 "Intangible Assets".

The standard also acknowledges the possibility of applying certain exceptions to recognition (practical expedients):
- For short term leases, with contractual term of 12 months or less;
- for leases in which the underlying is a low-value asset.

More specifically, according to the definition of IFRS 16 a leasing contract is a contract that conveys to the lessee the right to control the use of an identified asset (underlying) for a set period of time in exchange for consideration.
The two conditions necessary for the existence of a leasing contract are:
- the existence of an identified and physically distinct asset;
- the right to control the use of the asset which is made explicit in the lessee's right to obtain substantially all the economic benefits deriving from use of the asset during the period of use and in the right to manage the use of the asset, establishing how and for what purpose it is used, along the entire period of use. There must not therefore be a substantial right of replacement by the lessor.

The definition of "lease contracts" includes, besides leasing contracts in the strict sense, also, for example, rental and hire contracts for a consideration.
For a contract that contains a lease component and additional non-lease components, (such as the lease of an asset and the provision of a maintenance service), the standard prescribes accounting for each lease component separately with respect to the non-lease components. The consideration payable must therefore be allocated to the different components on the basis of the related stand-alone prices, following the logic of IFRS 15 envisaged for service contracts. As a practical expedient, a lessee may in any case elect, by class of underlying asset, not to separate non-lease components from lease components and to account for all components as a lease.
The most significant changes introduced by the standard regard the lessee, for whom or which a single accounting model is defined, with no distinction between operating lease and finance lease, with impact both on the income statement and in the balance sheet.
All leasing contracts originate in fact for the lessee accounting respectively in liabilities and assets of the balance sheet of:
- a lease liability, equal to the present value of the future payments determined using the discount rate defined at the commencement of the leasing contract;
- a right of use on the asset (hereinafter RoU), equal to the lease liability plus any initial direct costs, the estimate for dismantling and net of incentives.

The lessee must measure the asset consisting of the RoU applying the cost model. The income statement will be impacted essentially for the portion of depreciation of the right of use, recognised among operating expenses, and for interest accrued on the lease liability, recognised in net interest income.
The distinction between operating lease and finance lease remains for the lessor, for which the approach of IFRS 16 does not introduce substantial changes with respect to IAS 17, other than greater disclosure.
The standard was endorsed by the European Commission on 9 November 2017 with Regulation no. 2017/1986 and applies as of 1 January 2019. Early application is allowed for entities that already apply IFRS 15.
As regards first application of the standard, full or modified retrospective application is permitted. The full retrospective option provides for applying IFRS 16 for 2018 recording the impact on shareholders' equity at 1 January 2018 as if

IFRS 16 had always been applied, through a restatement of the comparative data. The modified retrospective option involves instead:

- for 2018 application of IAS 17 without the need for restatement of the comparative data;
- For 2019 application of IFRS 16 with impact on shareholders' equity at 1 January 2019 (under the item reserves) of the cumulative effect of the new standard at the date of first application of only contracts in being at that date and indication of the impacts deriving from first application of the standard in the Notes to the Statements.

The Group chose to apply the modified retrospective option which does not provide for restatement of the comparative data of 2018. The quantitative effects estimated on first application of the standard at 1 January 2019 are insignificant compared to both total assets/liabilities and CET1.

On 7 June 2017, the IASB published **IFRIC 23 "Uncertainty over Income Tax Treatments"**, which clarifies how to apply requirements for recognition and measurement of IAS 12 when there is uncertainty about which treatment to apply to income taxes.
In these circumstances, for the purposes of recognising and measuring current and deferred tax assets and liabilities in application of IAS 12, taxable profits/loss, taxable bases, unused tax losses, unused tax credits and fiscal taxes are determined on the basis of the interpretation provided in IFRIC 23.
The entity is required to use its judgement to determine whether an uncertain tax treatment should be considered independently or jointly with other tax treatments around which there is uncertainty. The decision should be based on an approach which best guarantees the resolution of the uncertainty.
The entity must also consider whether the relevant tax authority, in the context of examining the data communicated, can accept the application of the tax treatment or group of tax treatments proposed by the entity.
If it is considered likely that a given tax treatment will be accepted, the entity must determine the taxable income, taxable bases, unused tax losses, unused tax credits or tax rates in line with the tax treatment included in the tax return.
If, on the other hand, it is held improbable that it will be accepted, it must reflect the effects of this uncertainty when determining the tax components, using one of the following methods:

- the "most likely amount", identifying the most likely amount within a range of possible results;
- the expected value, based on the weighted sum of probable values within a range of possible values.

The decision must fall upon the method offering the greatest guarantees of resolving the uncertainty.
Additionally, the entity must revise its judgements and estimates if facts and circumstances should change.
IFRIC 23 was endorsed by the European Commission on 24 October 2018 with Regulation no. 2018/1595 and applies as of 1 January 2019. Early application is allowed.

On 12 October 2017 the IASB published **Amendments to IFRS 9: *Prepayment Features with Negative Compensation"***. The amendments are aimed at clarifying the classification of particular prepayable financial assets when IFRS 9 is applied. Specifically:

- for financial assets they allow measurement at amortised cost or, depending on the business model, at fair value through other comprehensive income, also of loans which, in the case of prepayment, involve payment by the lender (negative compensation payment);
- for financial liabilities at amortised cost they contain a clarification related to accounting for a modification that does not result in derecognition. In these cases, it is envisaged that, at the date of the modification, the adjustment to the amortised cost of the financial liability, calculated as the difference between original contractual cash flows and modified cash flows discounted at the effective interest rate, must be recognised in the income statement.

The amendments were endorsed by the European Commission on 26 March 2018 with Regulation no. 2018/498 and apply as of 1 January 2019; early application is allowed.

IAS/IFRS international accounting standards and related SIC/IFRIC interpretations published by the IASB and still awaiting European Commission endorsement

On 18 May 2017, the IASB issued **IFRS 17 "Insurance Contracts"** which establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts within the context of the standard.
The objective of IFRS 17 is to ensure that significant information which faithfully represents the contracts is provided as a basis for users of the financial statements to evaluate their effects on the financial performance and cash flows of the entity. On 14 November 2018 the IASB decided to defer application of IFRS 17 by one year, that is starting from 1 January 2022 or later years. The deferment proposed is still awaiting endorsement by the European Commission.
For the Group's operations direct impacts are not foreseen, because neither the Parent Company nor the subsidiaries do insurance business.
On 12 October 2017 the IASB issued the document **"Amendments to IAS 28: Long-term Interests in Associates and Joint Ventures".** The document, the endorsement process of which is still in progress, clarifies that IFRS 9 must be applied to long-term receivables from an associate or joint venture which, substantially, are part of the net investment in the associate or joint venture (for which the entity does not use the equity method).
The changes apply from 1 January 2019 but early application is allowed.

On 12 December 2017 the IASB published the "**Annual Improvements to IFRS Standards 2015-2017 Cycle**", which include amendments to IAS 12 "Income Taxes", IAS 23 "Borrowing Costs", IFRS 3 "Business Combinations" and IFRS 11 "Joint Arrangements". Specifically:

- the amendments to IAS 12 clarify that impacts on taxes on income from dividends (as in the case of distribution of profits) must be recognised in the income statement irrespective of how the taxes originate;
- the amendments to IAS 23 clarify that if a specific loan continues to exist after the corresponding asset is ready for use or sale, this loan is then included in the provisions considered when calculating the capitalisation rate in relation to general loans;
- the amendments to IFRS 3 clarify that when an entity obtains control over a business, which was formerly a joint operation, it must redetermine the equity investment held in the said business;
- the amendments to IFRS 11 clarify that when an entity obtains joint control over a business, which was previously a joint operation, the entity does not need to redetermine the equity investment held in the said business.

The amendments apply as of 1 January 2019. Early application is allowed.
On 7 February 2018 the IASB published **"Amendments to IAS 19: Plan Amendment, Curtailment or Settlement"** which finalises certain specific issues submitted to the IFRIC in 2015, related to determination of the service cost and of net interest in the case of remeasurement of the plan. The amendments are effective as of 1 January 2019 or later.
On 28 March 2018, the IASB published a revised version of the "**Conceptual Framework**". In particular, the definitions of asset and liability were revised and new guidance was provided on measurement, derecognition, presentation and disclosure. The new Conceptual Framework does not constitute however a substantial revision of the original document. The IASB concentrated on topics that were not yet covered or that showed evident regulatory shortcomings. The amendments come into force on 1 January 2020. Early application is allowed.
On 22 October 2018 the IASB issued **"Amendments to IFRS 3: Definition of a Business"** with the objective of resolving the difficulties that arise when an entity determines whether it has acquired a business or a group of assets. In particular, the document:

- clarifies that to be considered a business, a set of activities and assets purchased must include at least an input and process that contribute significantly to the ability to produce outputs;
- eliminates the assessment of the ability of the market operators to replace missing inputs or processes to continue to produce outputs;
- introduces guidelines and illustrative examples to help entities to assess whether a substantial process has been

acquired;
- Narrows the definitions of business and of outputs, focusing on goods and services provided to customers and eliminating the reference to the ability to reduce costs;
- introduces an optional concentration test, which makes it possible to simplify the assessment of the eventuality that a set of activities and assets acquired does not constitute a business.

The amendments are effective for business combinations for which the acquisition date is in force or subsequent to the beginning of the first annual period of reference starting from 1 January 2020 or later.

On 31 October 2018 the IASB published "Amendments to IAS 1 "Presentation of Financial Statements" and to IAS 8 **"**Accounting Standards, Changes in Accounting Estimates and Errors**",** which clarifies the definition of materiality, aligning it to that used in the Conceptual Framework of the IASs. According to the IASB, information is material if its omission, falsification or ambiguity could reasonably influence the decisions of users of the financial statements. The amendments are effective as of 1 January 2020 or later. Early application is allowed.

A.2 - PRINCIPAL FINANCIAL STATEMENT AGGREGATES

Section 1 - ACCOUNTING STANDARDS

The accounting standards adopted with reference to the principal asset and liability items for the preparation of the Consolidated Financial Statements at 31 December 2018 are described below. The presentation is made with reference to the stages of recognition, classification, measurement and derecognition of the different Asset and Liability items, and to the recognition criteria of revenue components.

1) FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS (FVTPL) CLASSIFICATION CRITERIA

a) classification criteria

Financial assets other than those classified among “Financial assets measured at fair value through other comprehensive income” and among “Financial assets measured at amortised cost” are classified in this category. They include:

- debt securities and loans that are included in an Other/Trading business model (not attributable therefore to the business models “Held to Collect” or “Held to Collect and Sell”) or that do not pass the SPPI test;
- equity instruments - not classifiable as in subsidiaries, associates and joint ventures - held for trading purposes or for which the option was not taken, on initial recognition, for designation at fair value through other comprehensive income;
- UCITS units;
- derivative contracts, accounted for among financial assets held for trading, which are presented as assets if the fair value is positive and as liabilities if the fair value is negative.

With reference to the latter it is possible to offset the positive and negative current values deriving from transactions carried out with the same counterparty only if the entity has the legal right to offset the amounts recognised in the accounts and intends to proceed with settlement on a net basis of the positions subject to offsetting.

More detailed information is provided below on the three sub-items that make up the category in question, represented by: “a) Financial assets held for trading”, “b) Financial assets designated at fair value”; “c) Other financial assets obligatorily measured at fair value”.

- a) Financial assets held for trading

  A financial asset is classified as held for trading if it is managed with the objective of realising cash flows through the sale of the same, because:
  - it has been acquired or borne mainly in order to sell it or repurchase it soon;
  - it is part of a portfolio of identified financial instruments that are managed uniformly and for which the existence is proven of a recent and effective strategy aimed at obtaining a profit in the short term;
  - it is a derivative (with the exception of derivatives that constitute a financial guarantee contract or that represent designated and effective hedging instruments).

- b) Financial assets designated at fair value

  A financial asset may be designated at fair value irrevocably at the moment of initial recognition, only when this designation makes it possible to eliminate or reduce significantly an “accounting mismatch”. At the moment this category is not used by the Bank;

- c) Other Financial assets obligatorily measured at fair value

  Other financial assets obligatorily measured at fair value represent a residual category and include:
  - debt securities, loans and receivables when i) the related contractual flows do not represent solely payment of principal and interest on the residual principal (- SPPI test not passed), or ii) are not held in the context of a business model the objective of which is to hold assets with the aim of collecting the contractual cash flows ("Held to Collect" business model) or the objective of which is achieved both through collecting the contractual cash flows and through the sale of financial assets ("Held to Collect and Sell" business model);
  - equity securities held with purposes other than trading for which the option of classification at fair value through other comprehensive income has not been taken.

According to the general rules laid down in IFRS 9 on the subject of reclassification of financial assets (with the exception of equity securities, for which no reclassification is permitted), reclassifications to other categories of financial assets are not permitted except when the entity changes its business model for managing financial assets. In these cases, which are expected to be extremely infrequent, financial assets can be reclassified from the category measured at fair value through profit or loss to one of the other two categories provided for in IFRS 9 (Financial assets measured at amortised cost or Financial assets measured at fair value through other comprehensive income). The transfer value is represented by the fair value at the moment of reclassification and the effects of the reclassification operate prospectively starting from the reclassification date. In this case, the effective interest rate of the reclassified financial asset is determined on the basis of its fair value at the reclassification date and this date is considered as date of initial recognition for allocation in the different stages of credit risk (stage assignment) for the purposes of impairment.
For more information on the classification criteria of financial instruments please see the paragraph "Classification criteria of financial assets".

b) recognition criteria
For debt and equity securities initial recognition occurs at the settlement date. For loans and receivables recognition in the financial statements occurs at the disbursement date. For derivatives at the subscription date.
At the moment of initial recognition, financial assets measured at fair value through profit or loss are recognised at their fair value, which generally corresponds to the price paid, without considering the transaction costs or income directly attributable to the instrument itself, which are instead booked directly to the income statement.

c) measurement criteria
After initial recognition, financial assets measured at fair value through profit or loss are carried at fair value, recording changes as counter-entries in the income statement.
To determine the fair value of financial instruments quoted on active markets, market prices are used. In the absence of an active market, commonly adopted estimation methods and measurement models are used; these take into account all the risk factors related to the instruments and are based on data observable on the market such as: measurement of listed instruments that have analogous characteristics, discounted cash flow calculations, models for determining option prices, figures observed in recent comparable transactions, etc.. For equity securities and derivative instruments that regard equity securities, not quoted on an active market, the cost criterion is used as an estimate of fair value only residually and limited to a few circumstances, that is in the case of non-applicability of all the aforementioned measurement methods, or in the presence of a wide range of possible measurements of fair value, in the context of which cost represents the most significant estimate.
For more information on the criteria for determining fair value, please see Section "A.4 Disclosure on Fair Value" in Part A of the Notes to the Consolidated Financial Statements.

d) income recognition criteria

Gains and losses deriving from changes in the fair value of financial assets held for trading are recognised in the income statement under the item "80 - Net gains (losses) on trading activity". Gains and losses of "financial assets designated at fair value" and of "other financial assets obligatorily measured at fair value", including the result of measurement at fair value of these assets and liabilities, are recognised in the income statement under the item "110 - Net gains (losses) on other financial assets and liabilities measured at fair value through profit or loss", respectively in the sub-items "a) financial assets and liabilities designated at fair value;" "b) other financial assets obligatorily at fair value through profit or loss".

e) derecognition criteria

Financial assets are derecognised i) when the contractual rights to the cash flows deriving from the assets expire, ii) when the sale of the asset entails the substantial transfer of all the related risks and benefits.

2) FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME (FVTOCI)

a) classification criteria

The present category includes:
- financial assets represented by debt instruments, managed in the context of a "Held to collect and sell" business model[8], the contractual flows of which represent solely payment of principal and interest (SPPI test passed);
- financial assets represented by equity instruments, held in the context of a business model other than trading, for which, at the moment of initial recognition, the option of recognising in other comprehensive income the changes in fair value subsequent to initial recognition in the financial statements (OCI election) has been taken irrevocably.

In particular, this item includes:
- debt securities that are attributable to a "Held to Collect and Sell" business model and that have passed the SPPI test;
- equity interests, not classifiable as in subsidiaries, associates and joint ventures, which are held for trading purposes, for which the option was taken for designation at fair value through other comprehensive income;
- loans that are attributable to a "Held to Collect and Sell" business model and that have passed the SPPI test. These cases are not present in the Bank.

According to the general rules laid down in IFRS 9 on the subject of reclassification of financial assets (with the exception of equity securities, for which no reclassification is permitted), reclassifications to other categories of financial assets are not permitted except when the entity changes its business model for managing financial assets. In these cases, which are expected to be extremely infrequent, financial assets can be reclassified from the category measured at fair value through other comprehensive income to one of the other two categories provided for in IFRS 9 (Financial assets measured at amortised cost or Financial assets measured at fair value through profit or loss). The transfer value is represented by the fair value at the moment of reclassification and the effects of the reclassification operate prospectively starting from the reclassification date. In the event of reclassification from the category in question to that of amortised cost, the cumulative gain (loss) recognised in the valuation reserve is taken to adjust the fair value of the financial asset at the reclassification date. In the event instead of reclassification to the category of fair value through profit or loss, the cumulative gain (loss) previously recognised in the valuation reserve is reclassified from shareholders' equity to profit (loss) for the period.

(8) *The Held to Collect & Sell Business Model includes financial instruments held in the context of a business model the objective of which is achieved both through collecting the cash flows and through the sale of the said instruments.*

For more information on the classification criteria of financial instruments please see the paragraph "Classification criteria of financial assets".

b) recognition criteria

Financial assets are initially recorded at the settlement date for debt and capital securities, and at the disbursement date for loans.
At the moment of initial recognition, they are accounted for at their fair value, which normally corresponds to the price paid, inclusive of the transaction costs or income directly attributable to the instruments.

c) measurement criteria

Financial assets represented by debt instruments, after initial recognition, continue to be measured at fair value, with recognition in the income statement of the interest (on the basis of the effective interest rate method), of the expected credit losses (for more details please see the paragraph "Impairment" in the present section) and of any exchange rate effect. Changes in fair value, net of expected credit losses, are allocated to a specific shareholders' equity reserve net of the related tax effect (item "120. Valuation reserves"). At the moment of total or partial disposal, cumulative gain or loss in the valuation reserve is recognised, wholly or in part, in the Income Statement.
Financial assets represented by equity instruments, after initial recognition, continue to be measured at fair value with allocation of the changes in a specific shareholders' equity reserve net of the related tax effect (item "110. Valuation reserves"). The amount recognised as a counter-entry of shareholders' equity (Statement of Comprehensive Income) must not subsequently be transferred to the income statement, not even in the event of sale. In his case, it is reclassified to another shareholders' equity item (item "140. Reserves"). In addition, no write-down in the income statement is envisaged for these assets because they are not subjected to any impairment process. The only component referable to the equity securities in question which is recognised in the income statement is represented by the related dividends.
For the equity securities included in this category, not listed in an active market, the cost criterion is used as an estimate of fair value only residually and limited to a few circumstances, that is in the case of non-applicability of all the aforementioned measurement methods, or in the presence of a wide range of possible measurements of fair value, in the context of which cost represents the most significant estimate.
For more information on the criteria for determining fair value, please see Section "A.4 Disclosure on Fair Value" in Part A of the Notes to the Consolidated Financial Statements.

Financial assets measured at fair value through other comprehensive income - in the form of both debt securities and receivables - are subject to verification of the significant increase in credit risk (impairment) provided for in IFRS 9, as are assets at amortised cost, with consequent recognition in the income statement of a write-down to cover the expected losses. In brief, on instruments classified in stage 1 (that is on financial assets at the origination date, if unimpaired, and on instruments for which no significant increase in credit risk has occurred with respect to the date of initial recognition) an expected loss at one year is accounted for, at the date of initial recognition and at each subsequent reporting date. Instead, for instruments classified in stage 2 (performing, for which a significant increase in credit risk has occurred with respect to the date of initial recognition) and in stage 3 (impaired exposures) an expected loss for the entire residual life of the financial instrument financial is accounted for. Vice versa equity securities are not subjected to the impairment process.
For more details please see point 16) "Use of estimates and assumptions in preparing the statutory financial statements" below - paragraph "Methods of determining the impairment of IFRS 9 financial instruments".

d) income recognition criteria

As regards financial assets represented by debt instruments:

- the expected credit losses recognised in the period are accounted for in item "130 - Net value adjustments for credit risk of: b) financial assets measured at fair value through other comprehensive income"; the same applies for recoveries of some or all of the write-downs carried out in previous years;
- at the moment of derecognition, the valuations accumulated in the specific shareholders' equity reserve are transferred to the income statement under item "100 - Gains/losses on disposal/repurchase of: b) financial assets measured at fair value through other comprehensive income".

As regards financial assets represented by equity instruments, for which the so-called "OCI election" option has been taken, only the dividends are recognised in the income statement (item "70. Dividends and similar income"). Changes in fair value subsequent to initial recognition are recognised in a specific valuation reserve in shareholders' equity (item "110. Valuation reserves"); in the case of derecognition of the asset, the cumulative balance of this reserve is not transferred to the income statement but is reclassified among the profit reserves of shareholders' equity (item "140. Reserves").

e) derecognition criteria
Financial assets are derecognised i) when the contractual rights to the cash flows deriving from the assets expire, ii) when the sale of the asset entails the substantial transfer of all the related risks and benefits.

3) FINANCIAL ASSETS MEASURED AT AMORTISED COST

a) classification criteria
The present category includes financial assets represented by debt instruments, managed in the context of a "Held to collect" business model[9], the contractual flows of which represent solely payment of principal and interest (SPPI test passed).
The portfolio of financial assets measured at amortised cost includes the entire receivables portfolio (of the different types, including repurchase agreements, entered into with both banks and customers), managed in the context of a "Held to collect" business model, net of receivables that do not pass the SPPI test and that are consequently classified in the portfolio of financial assets obligatorily measured at fair value.
This category also includes debt securities managed in the context of the "Held to collect" business model and operating receivables connected with the provision of financial activities and services as defined by the C.L.B. and the C.L.F. (for example for distribution of financial products and servicing activities).
According to the general rules laid down in IFRS 9 on the subject of reclassification of financial assets, reclassifications to other categories of financial assets are not permitted except when the entity changes its business model for managing financial assets. In these cases, which are expected to be extremely infrequent, financial assets can be reclassified from the category measured at amortised cost to one of the other two categories provided for in 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 represented by the fair value at the moment of reclassification and the effects of the reclassification operate prospectively starting from the reclassification date. The gains or losses resulting from the difference between the amortised cost of the financial asset and the related fair value are recognised in the income statement in the case of reclassification among Financial assets measured at fair value through profit or loss and at equity, in the specific valuation reserve, in the case of reclassification among Financial assets measured at fair value through other comprehensive income.

(9) The Held to Collect Business Model includes financial instruments held in the context of a business model the objective of which is to hold the same with the aim of collecting the cash flows.

For more information on the classification criteria of financial instruments please see the paragraph “Classification criteria of financial assets”.

b) recognition criteria

Financial assets are initially recognised at the settlement date for debt securities, and at the disbursement date in the case of loans; we can distinguish in this item:
- loans to banks;
- loans to customers.

The initial amount is quantified on the basis of the fair value of the financial instrument, normally equal to the amount disbursed including costs/income directly attributable to the individual instrument, which can be defined from the beginning of the transaction, even if settled subsequently. Costs that have the aforementioned characteristics but are reimbursed by the debtor counterparty or which can be classified as normal internal administrative expenses are excluded.

Repurchase agreements with obligation to repurchase are recognised as loan transactions for the spot amount received.

c) income measurement and recognition criteria

After initial recognition financial assets booked to the present category are measured at amortised cost which determines the recognition of interest on the basis of the *pro rata temporis* effective interest rate criterion along the term of the loan. This interest is presented in item “10. Interest and similar income”.

The gross book value is equal to the value on first recognition, decreased/increased:
- by repayments of principal;
- by amortisation - calculated with the effective interest rate method - of the difference between the amount disbursed and that repayable on maturity, attributable typically to the costs/income allocated directly to the single loan;
- by gains/losses on contractual changes without cancellation recognised in the income statement in item “140. Gains/losses on contractual changes without cancellations”.

The amortised cost method is not used for short-term loans, for which the effect of application of the discounting logic is negligible. The same measurement criterion is adopted for loans with undefined maturity date or which are valid until revoked.

For more details on the amortised cost please see point 15) - letter b) “Other significant accounting treatments” - paragraph “amortised cost”.

The book value of financial assets at amortised cost is adjusted in order to take into account any provisions to cover expected credit losses. At each annual or interim reporting date the said assets are in fact subjected to an impairment test with the objective of estimating the expected losses in value related to credit risk (so-called “ECLs - Expected Credit Losses”). The said losses are recognised in the income statement under item “130. Net value adjustments for credit risk”. Total or partial recoveries of write-downs carried out in previous years are treated in the same way.

In more detail, the impairment model, as better indicated in point 16) “Use of estimates and assumptions in preparing the statutory financial statements” below - paragraph “Methods of determining the impairment of IFRS 9 financial instruments”, provides for the classification of assets in three distinct “stages” (stage 1, stage 2, stage 3), according to the evolution of the creditworthiness of the debtor, to which correspond different criteria for measuring the expected losses:

- stage 1: this comprises non-impaired (performing) financial assets for which no significant deterioration of credit risk has been observed with respect to the date of initial recognition or the credit risk of which is considered low. The impairment is based on the estimate of expected loss using as reference a time horizon of one year (expected loss that results from default events on the financial asset that are considered possible within one year from the reference date);

- stage 2: this comprises non-impaired (performing) financial assets which have suffered a significant deterioration of credit risk with respect to the initial recognition. The impairment is commensurate to the estimate of expected loss having as reference a time horizon of the entire residual life of the financial asset;
- stage 3: represented by impaired financial assets (100% probability of default), to be measured on the basis of an estimate of the expected loss along the whole life of the instrument.

For performing assets the expected losses are determined according to a collective process based on certain risk parameters represented by Probability of Default (PD), Loss Given Default (LGD) and Exposure At Default (EAD), deriving from the internal models for calculating regulatory credit risk opportunely adjusted to take into account the specific requirements laid down in the accounting standards.

For impaired assets, that is for assets for which besides a significant increase in credit risk objective evidence of impairment has been found, the impairment losses are quantified on the basis of a measurement process - analytic or flat-rate on the basis of uniform risk categories - aimed at determining the present value of the forecast recoverable future flows, discounted on the basis of the original effective interest rate.

The category of impaired assets includes exposures to which has been attributed the status of bad loan, probable default or past-due/over-the-limit for more than 90 days according to the definitions established by the current supervisory regulations (Bank of Italy Circular no. 272 "Accounts Matrix") and referred to in Bank of Italy Circular no. 262, as they were considered consistent with the accounting rules provided for in IFRS 9 in terms of objective evidence of impairment.

The forecast cash flows take into account the expectations in terms of recovery times and estimated net realisable value of any guarantees.

For fixed-rate positions, the original effective rate used for discounting the forecast recovery flows, determined as illustrated above, remains unchanged over time even if a change is made to the contractual rate attributable to financial difficulties of the debtor.

For floating interest rate positions, the rate used for discounting the flows is subject to updating in relation to the indexing parameters (for example Euribor), keeping instead constant the spread originally fixed.

The original value of the financial assets is restored in subsequent years, in the event of an improvement in the credit quality of the exposure with respect to the level that entailed the previous write-down. The write-back is recognised in the income statement under the same item (130. Net value adjustments for credit risk) and, in any case, may not exceed the amortised cost that the asset would have had in the absence of previous write-downs.

For details of the impairment model please see what is explained in point 16) "Use of estimates and assumptions in preparing the statutory financial statements" below - paragraph "Methods of determining the impairment of IFRS 9 financial instruments".

Finally, for impaired exposures the interest accruing is calculated on the basis of the amortised cost, that is on the basis of the value of the exposure - determined on the basis of the effective interest rate - adjusted by the expected losses. For impaired exposures that do not accrue contractual interest, such as bad loans, the said interest corresponds to the write-backs connected with discounting of the recovery forecasts, as a result of the simple passing of time.

d) derecognition criteria

Financial assets are derecognised if one of the following cases occurs:

- the contractual rights to the cash flows deriving from the same have expired;
- the financial asset is sold with substantial transfer of all the risks and benefits deriving from ownership of the same;
- if it is not possible to ascertain the substantial transfer of the risks and benefits, the financial asset is derecognised when no type of control is kept over the same;
- the entity keeps the contractual right to receive the cash flows deriving from the same, but at the same time assumes a contractual obligation to pay the same flows to a third party (pass through arrangements) without delay and only for the amount of those received;

- the asset is subject to a change that can be classified as "substantial", as described in more detail in the paragraph "Renegotiations".

As regards impaired financial assets, the derecognition can occur following acknowledgement of the irrecoverability of the exposure and the consequent conclusion of the recovery process (definitive derecognition), and entails the reduction of the nominal value and gross book value of the receivable. These cases occur in the presence of settlement agreements signed with the debtor that entail a reduction of the receivable (full and final settlement agreements) or in the presence of specific situations, such as:

- a definitive judgement has been handed down which declares extinguished some or all of the receivable;
- Closure of the arrangement or enforcement procedure in relation to both the debtor and the guarantors;
- conclusion of all possible actions in and out of court for recovery of the receivable;
- Completion of a mortgage restriction on an asset in guarantee, with consequent derecognition of the receivable guaranteed by the mortgage subject to restriction, in the absence of further specific guarantees or further feasible actions for recovery of the exposure.

These specific situations may entail total or partial derecognition of the exposure but do not necessarily imply a waiver of the legal right to recover the receivable.
In addition, for impaired financial assets, the derecognition may occur after they have been written off, following acknowledgement of the non-existence of reasonable expectations of recovery, even though actions aimed at their recovery continue. The said write-off is carried out in the year in which the receivable, or part of it, is considered non-recoverable - even without closure of the legal procedure - and may occur before the legal actions brought against the debtor and the guarantors for recovery of the receivable have been definitively concluded. It does not imply the waiver of the legal right to recover the receivable and is carried out if the lending documentation contains reasonable financial information from which the impossibility of the debtor to repay the amount of the debt emerges. In this case the gross nominal value of the receivable remains unchanged, but the gross book value is reduced by an amount equal to the write-off, which may be referred to the entire exposure or to a portion of the same. The amount written off cannot be written back subsequently following an improvement in the recovery forecasts, but only following recoveries involving collection.
Lastly, for the financial assets in question the derecognition may also occur following reclassification to the categories of "Financial assets measured at fair value through other comprehensive income" and "Financial assets measured at fair value through profit or loss"; for more details please see the classification criteria presented above.
In the event of derecognition, the difference between the book value of the asset at the derecognition date and the price received, including any assets received net of any liabilities assumed, must be accounted for in the income statement, under the item "100. a) Gains (losses) on disposal or repurchase of: financial assets measured at amortised cost" in the case of sale and, in all other cases, under the item "130. Net value adjustments for credit risk".

4. HEDGING OPERATIONS

The Group availed itself of the possibility, provided for on first application of IFRS 9, to continue to use fully on the subject of "hedge accounting" the provisions of the international accounting standard IAS 39 (in the carved out version endorsed by the European Commission) for all types of hedging (for both micro- and macro-hedges). The Bank does not have hedging transactions in place.

a) classification - hedging type
Risk hedging transactions are aimed at neutralising potential losses recognisable on a certain financial instrument or on a group of financial instruments, attributable to a certain risk, if that particular risk effectively manifests itself. The following types of hedging are envisaged:

- hedging of fair value, which has the objective of hedging the exposure to a change in the fair value of an accounting item attributable to a particular risk. It includes also macro-hedges of fair value with the objective of reducing the oscillations of fair value, attributable to interest rate risk, of a cash amount, deriving from a portfolio of financial assets and liabilities (including "core deposits"). Net amounts deriving from the balancing of assets and liabilities cannot be the subject of macro-hedging;
- cash flow hedging, which has the objective of hedging exposure to changes in future cash flows attributable to specific risks associated with accounting items or to a highly probable planned transaction;
- foreign investment hedging, which aims at hedging the risks of an investment in a foreign operation in foreign currency.

At the level of the consolidated financial statements, the designation of the derivative as a hedging instrument is possible only if it was entered into in relation to a counterparty external to the Group. Results attributable to internal transactions carried out between different Group entities are eliminated.
For a derivative instrument to be designated as for hedging there must exist formalised documentation of the relationship between the hedged instrument and the hedging instrument and this relationship must be effective at the moment in which the hedging begins and, prospectively, during the whole life of the same. In addition, the hedging transaction must be attributable to a predefined risk management strategy and must be in keeping with the risk management policies adopted.

b) recognition criteria
Hedging derivative instruments are initially recognised at fair value at the date on which the contract is signed.

c) measurement and income recognition criteria
Hedging derivatives are measured at fair value. Specifically:
- In the case of fair value hedging, the change in fair value of the hedged element is recognised, together with the change in fair value of the hedging instrument, under item "90 - Net gains (losses) on hedging activities" of the income statement. Any difference, which represents the partial ineffectiveness of the hedging, constitutes its net economic effect. In the case of interruption of the hedging relationship, the hedged instrument, if it is not derecognised reacquires the original measurement criterion of the class it belongs to. More specifically for instruments measured at amortised cost the cumulative write-downs/write-backs recognised as a result of changes in fair value of the risk hedged are recognised in the income statement among interest income and expenses along the residual life of the hedged element, on the basis of the effective interest rate. Instead if on interruption of the hedging there is also derecognition of the hedged element (for example sale or prepayment), the portion of fair value not yet amortised is allocated immediately to the income statement under the item "Net gains (losses) on hedging activities". As regards fair value macro hedging transactions, the changes in fair value with reference to the hedged risk of the assets and liabilities being hedged are recognised in the balance sheet, respectively, under item "60 Value adjustment of financial assets subject to macro hedging" or "50 Value adjustment of financial liabilities subject to macro hedging". In the case of interruption of a fair value macro hedging relationship, the cumulative write-downs/write-backs recognised in the balance sheet items indicated above are recognised in the income statement among interest income and expenses along the residual duration of the original hedging relationships, after verification of the existence of the basic conditions;
- in the case of cash flow hedging, the changes in fair value of the derivative are recognised in shareholder's equity in a specific reserve (under the item "110 Valuation reserves") for the effective portion of the hedging, while the changes in fair value of the hedging instrument not offset by the change in the cash flows of the hedged transaction are recognised in the income statement under item "90 - Net gains (losses) on hedging activities". If the cash flow hedging is no longer considered effective, or the hedging relationship has ended, any portion in the reserve is transferred to the income statement when the hedged object, still in being, generates its effects in the income

statement. However, if the hedged instrument is derecognised, expires or is extinguished, the reserve is transferred fully to the income statement at the time the hedged element is derecognised;
• foreign investment hedges are accounted for using the same method as for cash flow hedges.

Hedging effectiveness depends on the degree to which the changes in fair value of the instrument hedged or the related expected cash flows are offset by those of the hedging instrument. Consequently, the effectiveness is measured by comparing these changes, taking into account the intended goal of the company at the time the hedge was established.
A hedge is effective when the changes in the fair value (or cash flows) of the hedging financial instrument almost completely neutralise (within the limits established by the range 80-125%) the changes in the hedged instrument, for the risk element being hedged against.
The effectiveness of the hedge is assessed at the end of each year, using:
• prospective tests, which justify application of hedge accounting, as they demonstrate its expected effectiveness;
• retrospective tests, which highlight the degree of hedging effectiveness achieved during the related period.
Derivative instruments which are considered for hedging from an economic point of view as they are operationally connected to financial liabilities designated at fair value (Fair Value Options) are classified among trading derivatives; the related spreads or positive and negative margins matured up to the reporting date, in accordance with their hedging function, are recognised among interest income and expenses, while gains and losses from measurement are recognised under item “110 - Net gains (losses) on financial assets and liabilities measured at fair value” of the income statement.

d) derecognition criteria
If the checks do not confirm the effectiveness of the hedging, both retrospectively and prospectively, the hedge accounting is interrupted according to what has been explained above.
In addition, the hedging relationship ceases when:
• the derivative expires, is extinguished or exercised;
• the hedged element is sold, expires or is repaid;
• it is no longer highly likely that the hedged future transaction will be carried out.
The hedging derivative contract, if it has not expired or been extinguished, is reclassified among financial assets held for trading, while the financial instrument being hedged, if it has not been sold or repaid, goes back to being measured according to the criterion of the class it originally belonged to.

5) EQUITY INVESTMENTS

a) classification criteria
The item includes interests held in subsidiaries, associates or joint ventures, which are accounted for on the basis of the equity method.
Companies that are not controlled but in which notable influence is exercised are considered associates. It is presumed that the company exercises notable influence in all cases in which it holds at least 20% of the voting rights (including “potential” voting rights) and, irrespective of the stake held, if there exists the power to participate in operating and financial decisions of the investees, in virtue of particular legal ties, such as shareholders' agreements, with the purpose, for participants in the agreement, to ensure representation in the management bodies and to safeguard uniformity in management guidance, without, however, having control over them.
Entities in which the control is shared between the Bank and one or more other operators on the basis of contractual agreements, on the basis of which the unanimous consent of all parties that share the control is necessary for taking decisions are considered joint ventures.

b) recognition criteria

The initial recognition of financial assets classified in the present category occurs on the settlement date, for an amount equal to the cost, including any goodwill paid on acquisition, which is therefore not the subject of autonomous and separate recognition.

c) measurement and income recognition criteria

The measurement criterion adopted for equity investments in subsidiaries and associates and in joint ventures is cost. At each annual or interim reporting date, any objective evidence that the equity investment has undergone impairment is assessed.

When a parent company relinquishes control over an investee company but nonetheless continues to hold a minority interest in the company, it must measure the retained interest on the balance sheet at fair value and allocate any gains or losses deriving from the loss of control to the income statement.

If evidence exists that the value of any equity investment may have undergone impairment, steps are taken to estimate the recoverable value of the equity investment represented by the higher amount between the fair value net of costs to sell and the value in use. Value in use is equal to the current value of the future cash flows which the investment may generate, including its final disposal value.

If the recovery value is lower than the book value, the related difference is stated in the income statement under item 220 “Gains/(losses) from equity investments”. On the other hand, if the reasons for the impairment cease to exist following an event which occurs after recognition of the impairment, write-backs are made with booking to the income statement under the same item 220 as above.

d) derecognition criteria

Equity investments are eliminated when the contractual rights over the cash flows deriving from the assets expire or when the financial assets are sold, essentially transferring all the related risks and benefits. In the presence of a situation that determines the loss of the notable influence or joint control, any residual equity investment is reclassified to the portfolios of IFRS9 financial assets.

6) PROPERTY, PLANT AND EQUIPMENT

a) classification criteria

Property, plant and equipment items include land, properties used for business purposes, investment properties, plant, furniture and furnishings, all kinds of equipment and works of art.

Those held by the Group and used in the production or provision of services or for administrative purposes are defined as instrumental property (classified as “property, plant and equipment used in the business” and recognised according to IAS 16) while those held by the Group in order to collected rents and/or held for appreciation of the invested capital are defined as investment property (classified as “property, plant and equipment used for investment” and follow the rules provided for in IAS 40).

The item also includes property, plant and equipment classified on the basis of IAS 2 - Inventories, related mainly to items acquired with a view to adding value to the investment, perhaps through restoration or renovation work, with the explicit intent of selling them in the immediate future in the context of the normal performance of the business, including assets deriving from the activity of enforcement of guarantees received or from purchase at auction.

In addition, property, plant and equipment includes assets connected with finance lease contracts which have come back into the company’s possession following the termination of the contracts and closure at the same time as the original lending position. This item also includes, if there are any, assets used under financial lease agreements, even if the legal ownership of the same remains with the lessor, improvements and incremental costs incurred on third party assets relating to property, plant and equipment which can be identified and separated from which future economic benefits are expected.

b) recognition criteria

Property, plant and equipment items are initially recognised at cost, which comprises both the purchase price and all the possible related charges directly attributable to the purchase and commissioning of the asset.

Extraordinary maintenance costs which involve an increase in the future economic benefits are booked as an increase in the value of the assets, while ordinary maintenance costs are recorded in the income statement.

In the case of properties withdrawn following closure of the original lending position (so-called "*datio in solutum*"), the recognition is made at the lower between the value of the gross receivable recognised at the moment of return of the asset and:

- the "market value" resulting from a specific appraisal, if their classification among "assets held for sale" is not foreseeable in a short-term time horizon;
- the "readily realisable value" taken from a specific appraisal, which adjusts the "market value" with the prospect of a sale in a very short time, if at the termination date the subsequent allocation among "assets held for sale" is known;
- at the price being negotiated, if at the moment of initial recognition there are concrete negotiations for the sale, demonstrated by commitments assumed by the parties involved in the negotiation.

With regard to properties, the components referring to land and buildings represent separate assets for accounting purposes and, in virtue of the application of the approach by components, are recognised separately at the time of acquisition. The division between the value of the land and the value of the building is made on the basis of appraisals by independent experts.

c) income measurement and recognition criteria

Property, plant and equipment, including properties not used for business purposes and with the exception of those governed by the rules of IAS 2, are measured at cost, less any accumulated depreciation and impairment losses.

The fixed assets are systematically depreciated over their useful lives, adopting the straight-line basis as the depreciation method, with the exception of land and works of art which have an indefinite useful life and cannot be depreciated.

The useful life of property, plant and equipment subject to depreciation is periodically verified; in case of adjustment of the initial estimate, the related depreciation rate is changed accordingly. The specific sections of the Notes to the Financial Statements show the depreciation rate and the consequent expected useful life of the main asset categories.

At each annual or interim reporting date, the presence of any signs of impairment - meaning indications which demonstrate that an asset may have undergone a loss in value - must be checked.

In the event of the presence of the said signs, the book value of the asset is compared to its recoverable value, i.e. the greater of the fair value, net of any costs to sell, and the related value in use of the asset, understood as the present value of the future flows originated by the asset. Any write-downs are recognised in the income statement under item "180 Net value adjustments on property, plant and equipment". Periodic depreciation is recorded in the same item.

If the reasons which led to the recognition of the impairment loss cease to exist, a write-back is made. This must not exceed the value that the asset would have had, net of the depreciation calculated in the absence of prior impairment.

The properties to which IAS 2 applies are measured in the same way as inventories and therefore at the lower between the cost of accounting recognition and the net realisable value, represented by the estimated selling price less the estimated costs for completion and the other costs necessary to make the sale. Any impairment losses, if they become manifest, are recognised in the income statement under item "180 Net value adjustments on property, plant and equipment". This category is not subject to periodic depreciation.

d) derecognition criteria

Property, plant and equipment is derecognised at the time of disposal or when the assets are permanently withdrawn from use and future economic benefits are not expected from their disposal. The capital gains and capital losses deriving from disinvestment or disposal of property, plant and equipment are determined as the difference between the net selling price and the book value of the asset and are recognised in the income statement at the same date on which they are derecognised.

7) INTANGIBLE ASSETS

a) classification criteria
Intangible assets are non-monetary assets, which are identifiable and lacking a physical presence, held to be used over the long-term or indefinitely.

b) recognition criteria
They are recognised at cost, as adjusted by any related charges, only if it is probable that the future economic benefits attributable to the assets will arise and if the cost of the assets can be reliably determined. Otherwise, the cost of the intangible assets is recorded in the income statement in the period in which it was incurred.
Goodwill is recognised among assets when it derives from a business combination transaction in accordance with the calculation approach envisaged by the accounting standard IFRS 3, as the residual excess between the cost incurred in total for the transaction and the net fair value of the assets and liabilities acquired constituting companies or business units.
If the cost incurred is instead lower than the fair value of the assets and liabilities acquired, the negative difference (badwill) is booked directly to the income statement.
The Bank does not hold intangible assets.

c) income measurement and recognition criteria
The cost of intangible fixed assets with defined useful life is amortised on a straight-line basis over the related useful life. If the useful life is indefinite, the asset is not amortised, but merely subjected to a periodic check of the adequacy of the value recorded for the fixed assets in the financial statements. Intangible assets deriving from software developed internally or acquired from third parties are amortized on a straight-line basis as from the completion and commissioning of the application on the basis of the related useful life. Intangible assets representing relations with customers, which can be recognised at the time of business combinations, are amortised at constant rates.
At each annual or interim reporting date, in the presence of evidence of impairment, steps are taken to estimate the recoverable value of the assets. The amount of the impairment loss, recorded in the income statement, is equal to the difference between the book value of the assets and the recoverable value.
Recorded goodwill is not amortised but subject to periodic checks on its book value, carried out annually or more frequently in the presence of signs of an impairment in value. To this end, the cash generating units to which the goodwill is to be allocated are identified. This unit represents the minimum level at which goodwill is monitored for internal management purposes and must not be larger than the operating segment determined in accordance with the standard IFRS 8.
The amount of any impairment is determined on the basis of the difference between the initial recognition value of the goodwill and its recoverable value, if lower. This recoverable value equates to the fair value of the cash generating unit, net of any cost to sell, or the related value in use, represented by the current value of the estimated cash flows for the periods of operation of the cash generating unit, and deriving from its disposal at the end of its useful life, whichever amount is the higher. The consequent value adjustments are recognised in the income statement under item "190 Value adjustments on intangible assets". Periodic depreciation is recorded in the same item. As regards goodwill, recognition of any subsequent write-backs is not permitted.

d) derecognition criteria
Intangible fixed assets are derecognised from the balance sheet at the time of disposal and if future economic benefits are not expected from the same.

8) NON-CURRENT ASSETS AND ASSET/LIABILITY GROUPS HELD FOR SALE CLASSIFICATION CRITERIA

a) classification criteria
These are classified in the asset item "110 Non-current assets and disposal groups held for sale" - and in the liability item "70 Liabilities associated with assets held for sale" - non-current assets/liabilities and asset/liability groups for which their book value will presumably be recovered through sale instead of with continuing use.
To be classified in the aforesaid item, the assets or liabilities (or disposal group) must be immediately available for sale and active and concrete plans must be noted such as to lead to believing their disposal highly likely in the near future.

b) measurement and income recognition criteria
After initial recognition, the assets and groups of non-current assets held for sale, with the related liabilities, are measured at the lower between the book value and the fair value net of costs to sell, with the exception of some types of assets - attributable, for example, to all financial instruments falling within the scope of application of IFRS 9 - for which IFRS 5 states specifically that the measurement criteria of the accounting standard of reference must be applied. At moment of classification of a non-current asset among non-current assets held for sale, any amortisation process is interrupted.
Valuation reserves related to non-current assets held for sale and, recognised as counter-entries to changes in value significant for this purpose, are shown in the statement of comprehensive income.
Income and expenses related to asset and liability groups held for sale, net of the tax effect, are presented in the income statement under the item "290 Gain (Loss) on discontinued operations, net of taxes". Gains and losses attributable to individual assets held for sale are recognised in the most suitable income statement item.
In the case of discontinued operations, it is also necessary to present the same economic disclosure again in a separate entry, also for the previous periods presented in the financial statements, reclassifying the income statements accordingly.

c) derecognition criteria
Non-current assets and asset/liability groups held for sale are derecognised on disposal.

9) CURRENT AND DEFERRED TAXATION

a) recognition criteria
The effects relating to current and deferred taxes calculated in observance of national tax legislation are recorded on an accruals basis, in line with the methods for recording the costs and revenues which have generated them in the financial statements, applying current tax rates.
Income taxes are recorded in the income statement, with the exception of those relating to items booked or credited directly to shareholders' equity.
The provision for income taxes is determined on the basis of a prudent forecast of the current, prepaid and deferred tax liability.
In particular current taxation includes the net balance between current liabilities for the year and the current tax assets with respect to the Tax Authorities represented by advances, credits deriving from previous tax returns and other tax credits for withholdings made. Current assets also include tax credits a rebate of which has been requested

from the competent Tax Authorities. Tax assets transferred to secure own payables also remain recorded in this item.
Deferred tax assets and liabilities are determined on the basis of the timing differences - without time-limits - between the value assigned to an asset or a liability according to statutory criteria and the corresponding values adopted for tax purposes applying the so-called balance sheet liability method.
Deferred tax assets determined on the basis of temporary deductible differences are recognised in the financial statements to the extent that their recovery is probable. This probability is determined through a probability test, on the basis of the Bank's ability to continuously generate positive taxable income or, as a result of exercising the option related to “Tax consolidation”, that of all of participating companies.
For a description of the specific methods with which the probability test is conducted please see the Notes to the present Consolidated Financial Statements, paragraph 11.8 of Section 11
- Part B - Notes to the Balance Sheet.
The probability of recovering deferred tax assets related to goodwill, other intangible assets and write-downs of receivables (so-called transformable DTAs), must be considered automatically fulfilled as a result of the legal provisions which contemplate their transformation into tax credit in the presence of losses for the period according to civil and/or tax legislation.
In particular, art. 2 - paragraphs 55 and following - of Italian Law Decree no. 225 of 29 December 2010 (as amended) states that:

- in the presence of a statutory loss for the period, prepaid taxes (IRES and IRAP) related to goodwill, other intangible assets and write-downs of receivables can be transformed into tax credit for a portion equal to the ratio between the statutory loss and accounting shareholders’ equity gross of the loss itself. The transformation takes effect as of the date of approval, on the part of the shareholders’ meeting, of the separate financial statements on which the loss is posted.
- in the presence of a tax loss for the period (that is, for IRAP purposes, of negative value of production), the deferred tax assets related to deductions referred to goodwill, other intangible assets and write-downs of receivables, which have contributed to formation of the aforesaid tax loss (that is of the negative value of production) are transformed into tax credit. The said transformation takes effect as of the date of the presentation of the tax return related to the financial year in which the loss is recorded.

As a result of the provisions contained in Italian Law Decree no. 83 of 27 June 2015, transformable DTAs ceased to increase starting from 2016. Specifically:

1. for deferred tax assets related to goodwill and other intangible assets newly recognised in the financial statements from 2016 onwards exclusion from the rules pursuant to art. 2 - paragraphs 55 and following - of Italian Law Decree 225/2010 was provided for;
2. for deferred tax assets related to write-downs of receivables, from 2016 onwards the accounting condition for the related recognition has ceased as these write-downs have become entirely deductible in the year they are accounted for. We can note that the budget law for 2019 (Italian Law no. 148 of 30 December 2018) recently made an exception to the full deductibility of write-downs on receivables with reference to those recognised (in 2018 for the Bank) on first application of IFRS 9, exclusively following the adoption of the recognition model of provisions to cover expected losses (ECLs), providing for the deductibility (IRES and IRAP) of the same in constant instalments over 10 years. It was, however, expressly clarified that the related DTAs consequently recognised, although they are referred to write-downs on loans to customers, do not come within those transformable into tax credit pursuant to Italian Law Decree 225/2010.

We can note, in addition, that the MPS Group and, within it the Bank, exercised the irrevocable option pursuant to Italian Law Decree no. 59 of 3 May 2016 (as amended) to keep the right to transform into tax credit the DTAs related to goodwill, other intangible assets and write-downs and losses on receivables; consequently, the related annual fee to be paid with reference to each of the years starting from 2016 and subsequently is payable, if the conditions are met

annually, up to 2030. Deferred taxes on tax losses not used are recognised on the basis of the same criteria envisaged for the recognition of deferred taxes on deductible temporary differences: they are therefore recognised only to the extent to which their recovery is likely, on the basis of the ability to generate positive taxable incomes in the future. As the existence of unused tax losses can be a symptom of difficulty in achieving positive taxable incomes in the future, IAS 12 states that, in the presence of losses made in recent periods, suitable evidence must be provided to support the existence of such income in the future. In addition, we can note that the current Italian tax legislation allows unlimited carrying forward over time of IRES tax losses (Art. 84 paragraph 1 of the Consolidated Income Tax Law); consequently, verification of the existence of future taxable earnings against which to use these losses is not subject to time limits.
Deferred tax assets and liabilities are calculated using the tax rates expected at the date of payment of the temporary differences, on the basis of the measures existing at the reporting date. Any changes in the tax rates or fiscal legislation, issued or communicated after the reporting date and before the date of authorisation for publication, which have a significant effect on deferred tax assets and liabilities are treated as events that occurred after the reporting date that do not entail adjustment under the terms of IAS 10, with consequent disclosure in the notes to the statements.
Prepaid and deferred taxes are recognised at the capital level by offsetting at the level of the same tax.

b) classification and measurement criteria
The deferred tax assets and liabilities recognised are measured systematically to take account of any changes made to legislation or tax rates. Any expenses that could derive from assessments already notified, or in any case from disputes in being with the tax authorities, are instead recognised under the item “Net provisions for risks and charges”.
In relation to the Tax Consolidation between the Parent Company and the subsidiaries that have accepted it contracts were signed that regulate the offsetting flows in relation to transfers of tax profits and losses. These flows are determined applying the IRES rate in force to the tax losses of the companies involved. For companies that transfer tax losses, the offsetting flow, calculated as above, is paid by the consolidating to the consolidated company when, and in the amount of which, the same consolidated company transfers to the tax consolidation, in tax periods subsequent to that in which the loss was made, positive taxable income. Offsetting flows determined in this way can be recognised as credits and debits relative to the companies participating in tax consolidation, classified among other assets and other liabilities, as a counter-entry to item “270 - Income taxes for the year from continuing operations”.

c) income recognition criteria
If the deferred tax assets and liabilities refer to components that have affected the income statement the counter-entry is represented by income taxes. In cases where deferred tax assets and liabilities concern transactions which have directly affected shareholders’ equity without influencing the income statement, for example measurements of financial instruments available for sale or cash flow hedging derivatives, the same are recorded as a counter-entry to shareholders’ equity, affecting the specific reserves when envisaged.

10) FINANCIAL LIABILITIES MEASURED AT AMORTISED COST

a) classification criteria
Item 10 “Financial liabilities measured at amortised cost” comprises the sub-items “a) payables to banks”, “b) payables to customers” and “c) outstanding securities” and consist of the various forms of funding, both interbank and in relation to customers and deposits made through certificates of deposits and bonds in issue, net of any repurchases.
Among outstanding securities are classified all securities not subject to “natural” hedging with derivatives, which are classified among liabilities measured at fair value.
Also included are payables recognised by the lessee in the context of any finance leasing operations entered into, and repurchase agreements for funding and securities lent receiving a guarantee in cash that comes within the full

availability of the lender. Lastly, the item includes operating payables connected with the provision of financial services as defined in the Consolidated Law on Banking and the Consolidated Law on Finance.

b) recognition criteria

Initial recognition of these financial liabilities occurs at the moment of receiving the amounts collected or of issue of the debt securities and is done on the basis of the fair value of the liabilities, which is normally equivalent to the amount collected or the issue price, increased by any additional costs/revenues directly attributable to the single funding operation or issue and not refunded by the creditor counterparty. Internal administrative costs are excluded. Repurchase agreements with obligation to repurchase are recognised as funding transactions for the spot amount received.
With regard to structured instruments, if there are the requirements envisaged by the standard IFRS 9 for separate recognition of embedded derivatives, these latter are separated from the host contract and recognised at fair value as assets or liabilities held for trading. The host contract is instead recognised at amortised cost.

c) income measurement and recognition criteria

After initial recognition, financial liabilities issued, net of any redemptions and/or repurchases, are measured at the amortised cost with the effective interest rate method. Short term liabilities, when the time factor is negligible, are excepted and remain recognised for the amount collected. Interest is charged to the income statement under item 20 "Interest and similar expenses".
We can note, in addition, that funding instruments that are the subject of an effective hedging relationship are measured on the basis of the rules laid down for hedging transactions.

d) derecognition criteria

Financial liabilities are derecognised when they have matured or been discharged. Derecognition also takes place when previously issued securities are repurchased. The difference between the book value of the liability and the amount paid to purchase it is recorded in the income statement under item 100 "Gains (losses) on disposal or repurchase of c) financial liabilities". The re-placing of own securities on the market subsequent to their repurchase is considered a new issue with recognition at the new placement price, with no effect on the income statement.
In compliance with the provisions of the standard IAS 32, the potential commitment to purchase treasury shares due to the issue of put options is represented in the financial statements as a financial liability with a reduction in shareholders' equity for the present value of the contractually set repayment amount as a direct counter-entry. At the end of financial year 2018 there were no put options sold on the Bank's treasury shares.

11. FINANCIAL LIABILITIES HELD FOR TRADING

a) classification criteria

This item comprises:
- financial liabilities issued with the intention of repurchasing them in the near future;
- liabilities that are part of a portfolio of financial instruments managed jointly for which there is a proven strategy aimed at achieving profits in the near future;
- derivative contracts with a negative fair value not designated as hedging instruments, including those embedded in complex financial instruments that have been separated from liabilities measured at cost amortised cost and those connected to assets/liabilities designated at fair value through profit or loss.

Also included are liabilities that originate from technical overdrafts generated by securities trading activity.

b) recognition criteria

Financial liabilities are initially recognised on the settlement date for on-balance-sheet liabilities, while derivative

contracts are recognised on the date they are signed.
At the moment of initial recognition financial liabilities held for trading are measured at their fair value, which generally corresponds to the amount collected, without considering the transaction costs or income directly attributable to the instrument itself, which are booked directly to the income statement.

c) measurement criteria
After initial recognition financial liabilities held for trading are carried at fair value, recording changes as offsetting entries in the income statement.
Please see section "A.4.3 Fair value hierarchy" in the present Part A, below, for a description of the criteria used to determine the fair value of financial instruments.

d) income recognition criteria
Gains and losses deriving from changes in the fair value of financial liabilities and/or from the sale of the same are recognised in the income statement item "80 - Net gains (losses) on trading activities", including those related to derivative liabilities connected with the Fair Value Option.

e) derecognition criteria
Financial liabilities are derecognised when the contractual rights to the related cash flows expire or when the financial liabilities are sold with substantial transfer of all the risks and benefits deriving from ownership of the same.

12) FINANCIAL LIABILITIES DESIGNATED AT FAIR VALUE
This portfolio is not used by the bank.

13) PROVISIONS FOR RISKS AND CHARGES

Provisions for risks and charges: commitments and guarantees given
The sub-item in question comprises provisions for credit risk covering commitments to disburse funds and guarantees given that come within the scope of application of the rules on impairment under the terms of IFRS 9, as is laid down for "Financial assets measured at amortised cost" and for "Financial assets measured at fair value through other comprehensive income". For details of the impairment model please see what is explained in point 16) "Use of estimates and assumptions in preparing the statutory financial statements" below - paragraph "Methods of determining the impairment of financial assets".
In addition, the sub-item also includes provisions for risks and charges set aside to cover other types of commitments and guarantees given which, owing to their specific features, do not come within the scope of application of the impairment rules under the terms of IFRS 9.

Provisions for risks and charges: pensions and similar obligations
The sub-item "Provisions for risks and charges: b) pensions and similar obligations" includes the provisions recorded on the basis of IAS 19 "Employee benefits" for the purpose of making good the technical deficit of the supplementary defined-benefit pension funds. Pension plans are divided up into the two categories with defined benefits and defined contributions. While for defined contribution plans the liability of the company is established in advance, for defined benefit plans the liability is estimated and must take into account any insufficiency in contributions or in return on the assets in which these contributions have been invested. For defined benefit pension plans, the determination of the actuarial values required by the application of the aforementioned standard is carried out by an independent

actuary, using the Projected Unit Credit Method. The actuarial gains and losses, defined as the difference between the book value of the liability and the present value of the commitments at the end of the period, are recognised for the entire amount in the statement of comprehensive income, in the item "Valuation reserves". For more details please see paragraph 15 "Other information" below, letter a) "Content of other significant accounting items" - paragraph "Provisions for severance indemnity and other employee benefits".

Provisions for risks and charges: other provisions for risks and charges

The sub-item "- Provisions for risks and charges: c) other provisions for risks and charges" comprises the amounts set aside to cover the estimated outlays for legal or implicit obligations deriving from past events. These outlays may be of a contractual nature, such as allocations for the incentive system for personnel and for early retirement incentives, indemnities provided for in contractual clauses on the occurrence of certain events, or involving compensation and/or restitution, such as those to cover estimated losses on litigation, including le actions for revocation, estimated outgoings to settle customer complaints for securities broking activities, disputes concerning taxation.

Provisions for risks and charges consist of liabilities of an uncertain amount or maturity and are recognised in the financial statements if:

- there is a current (legal or implied) obligation as a result of a past event;
- it will probably be necessary to use resources able to produce economic benefits to meet the obligation; and
- the amount of the probable future outgoing can be estimated reliably.

The amount recognised as provisions represents the best estimate of the financial outgoing necessary to fulfil the obligation existing at the reporting date and reflects the risks and uncertainties inherent in the facts and circumstances examined. If the time factor is significant, the provisions are discounted to the present using the current market rates. The provisions and the discounting effect are recognised in the income statement in item "170. Net provisions for risks and charges", as is the increase in the provisions as a result of the passing of time. Provisions set aside are re-examined at each reporting date and adjusted to reflect the best current estimate. When the use of resources, intended to produce economic benefits to fulfil the obligation, becomes improbable, or when the obligation is extinguished, the provisions are reversed.

In addition, each provision is used only to cover outgoings for which it was originally set aside.

No provision is made for liabilities which are merely potential and not probable, but disclosure is in any case provided in the Notes to the Financial Statements, unless the likelihood of using resources is remote or the phenomenon is not significant.

14) FOREIGN CURRENCY TRANSACTIONS

a) recognition criteria

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

b) income classification, measurement, derecognition and recognition criteria

At the end of every financial year or interim period foreign currency items are measured as follows:

- cash items are converted at the exchange rate in force on the balance sheet date;
- non-cash items are carried at their historical cost converted at the exchange rate in force on the date of the transaction;
- non-cash items designated at fair value are converted at the exchange rate in force on the balance sheet date.

The exchange differences which derive from the settlement of monetary elements or from the conversion of monetary

elements at rates other than for initial conversion, or conversion of the previous financial statements, are recorded in the income statement of the period in which they arise.
When a gain or a loss relating to a non-monetary element is recorded under shareholders' equity, the exchange difference relating to this element is also stated under equity. By contrast, when a gain or a loss is recognised in the income statement, the related exchange difference is also recorded in the income statement.

15) OTHER INFORMATION

a) Content of other significant accounting items
The content of other significant accounting items is described below.

■ Other assets and other liabilities
In item 120 of Assets "Other assets" and 80 of the Liabilities "Other liabilities" the assets and liabilities not attributable to the other balance sheet items are recognised. These are referable mainly to:
- items in transit;
- receivables and payables connected with the supply of goods or non-financial services and accrued income and expenses other than those that are capitalised on the pertinent financial assets/liabilities, including those deriving from contracts with customers under the terms of IFRS 15;
- any inventories of goods according to the definition of the standard IAS 2, with exclusion of those classified as inventories of property, plant and equipment;
- payment agreements that that must be classified as payables under IFRS 2;
- credit/debit positions deriving from the tax consolidation system;
- tax credit and debit items other than those recognised in item "100. Tax assets" and "60. Tax liabilities";
- capital gains/capital losses deriving from measurement of transactions in regular way securities not yet settled;
- improvements and incremental expenses paid on third party properties other than those recorded in item "80 Property plant, and equipment", as they are not identifiable and separable on their own.

The costs indicated in the last point are posted in item "120 Other assets" because as a result of the lease agreement the user company has control over the assets and may draw future economic benefits from them. These costs are recorded in the income statement under item "200 -Other operating income/charges" according to the shorter period between the one in which the improvements and incremental expenses can be used and the residual validity of the agreement, including the period of renewal, if there is evidence in this sense.

■ Severance indemnities and other employee benefits.
Severance indemnities for the personnel are classified, under the terms of IAS 19, as "post-employment benefits". Following the complementary pension reform pursuant to Italian Legislative Decree no. 252 of 5 December 2005, new rules were introduced for severance indemnities accrued starting from 1 January 2007, which are relevant for the related accounting treatment. In particular for companies with on average at least 50 employees during 2006, the portions of severance indemnities for personnel accrued starting from 1 January 2007 are classified in the accounts as a "defined contribution plan" both in the case of option by the employee for a complementary pension, and in the case of allocation to the Treasury Fund at the INPS; the expense, accounted for among personnel expenses, is limited to the contribution established by the rule provided for in the Italian Civil Code, without applying any actuarial methodology.
Otherwise, provisions for severance indemnities accrued as of 31 December 2006 continue to be classified in the accounts as a "defined benefit plan". In general, "post-employment plans" - which include, besides Provisions for severance indemnities, the Pension funds - are divided into two categories, "defined benefit" and "defined contribution", on the basis of the related characteristics.

In particular, for defined contribution plans the cost is represented by contributions accrued in the period, given that the company has only the obligation to pay the contributions fixed on a contractual basis to a fund and consequently does not have any legal or implicit obligation to pay, besides paying the contribution, further amounts if the fund does not have sufficient assets to pay all the benefits to the employees.
For defined benefit plans, the actuarial and investment risk, that is the risk of any insufficiency of contributions or of an insufficient return on the assets in which the contributions are invested, is borne by the company. The liability is determined by an independent actuary according to the actuarial "Projected Unit Credit" method. On the basis of the said method it is necessary to forecast future outgoings on the basis of demographic and financial assumptions, to be discounted to take into account the time that will pass before the effective payment and to be re-proportioned on the basis of the ratio between the years of service matured and the estimated theoretical seniority at the moment is disbursement of the benefit. For discounting purposes, the rate used is determined with reference to the market return of bonds of leading companies taking into account the average residual duration of the liability, weighted on the basis of the percentage of the amount paid and advanced, for each maturity, with respect to the total to be paid and advanced up to the final settlement of the entire obligation.
The actuarial value of the liability thus determined must then be adjusted by the fair value of any assets serving the plan (net liability/asset). The actuarial gains and losses that arise as a result of adjustments of the previous actuarial assumptions formulated, following the experience effectively noted or owing to changes in the said actuarial assumptions, entail a remeasurement of the net liability and are allocated as a counter-entry to a shareholders' equity reserve (item "110 Valuation reserves") and, therefore, subject to presentation in the "Statement of Comprehensive Income". The change in the liability consequent to a modification or a reduction of a plan is recognised in the income statement as a gain or loss. More specifically, changes occur when a new plan is introduced, rather than when an existing plan is modified or withdrawn. There is instead a reduction in the presence of a significant negative change in the number of employees included in the plan, for example in the case of plans for the reduction of surplus personnel (access to the Solidarity Fund).

The "Projected Unit Credit" method, described above, is followed also for measuring the long-term benefits, such as "seniority bonuses" in favour of employees. Unlike what is described for "defined-benefit plans", the actuarial gains and losses connected with the measurement of the long-term benefits are recognised immediately in the income statement.

■ **Valuation reserves**

The present item includes valuation reserves related to equity securities designated at fair value through other comprehensive income, to financial assets (other than equity securities) measured at fair value through other comprehensive income, to actuarial gains (losses) on defined benefit pension plans, and, more generally with respect to the cases of interest to the Bank, to foreign investment hedging, to cash flow hedging, to exchange differences from translation, to "single assets" and asset groups held for sale, to the portion of valuation reserves of equity investments measured at shareholders' equity, to gains/losses connected with the change in own creditworthiness in relation to liabilities in fair value options. Also included are revaluation reserves recognised in application of special revaluation laws, even if they are subject to tax "redemption".

■ **Share capital and Treasury shares**

Item 160. "Share capital" includes the amount of shares outstanding net of the amount of any capital subscribed but not yet paid up at the reporting date. The item is shown gross of any treasury shares held by the Bank. These latter, if present, are recognised in their own item as a negative component of shareholders' equity.

b) Other significant accounting treatments

■ **Revenue from Contracts with Customers (IFRS 15)**

Revenues are gross flows of economic benefits that have occurred during the accounting period in the form of a fee

for the obligation to transfer to customers a vast range of goods and services the come within the ordinary business.
The standard IFRS 15 "Revenue from Contracts with Customers" introduces a new model for recognising revenue deriving from contractual obligations with customers, which is based on the concept of transfer of control and not only, therefore, on the concept of transfer of the risks and benefits.
First of all, the revenue from contracts with customers is recognised in the financial statements only if the contract from which it derives is identifiable, that is:
- the parties have approved the contract and have committed themselves to executing it;
- the rights and obligations of the parties are clearly identifiable in the contract;
- the terms related to payment for the goods and services transferred can be identified;
- the contract has commercial substance, in the sense that it impacts the entity's cash flows;
- collection of the consideration is considered likely in exchange for transfer of the goods and provision of the services. This measurement must consider only the customer's ability and intention to pay the amount of the consideration payable.

After the consideration of the contract has been allocated to the single obligations deriving from the same, the revenue is recognised in the income statement when the customer obtains control over the goods or services promised (that is when the related performance obligation can be considered fulfilled) and this may occur:
- in a certain instant in time (for example, when the entity fulfils the performance obligation, transferring to the customer the good or service promised - at a point in time);
- Along a period of time (for example, as the entity gradually fulfils the performance obligation transferring to the customer the good or service promised - over time).

For the purposes of determining the revenue to be recognised, the consideration is defined as the amount to which the entity expects to have the right in exchange for transfer of the goods and services and may include fixed amounts, variable amounts or both. In detail, the consideration of the contract may vary following reductions, discounts, refunds, incentives, performance bonuses or other similar elements. The variability of the consideration may also depend on the occurrence or non-occurrence of a future event (as in the case of a commission linked to performance targets).
The methods suggested by IFRS 15 for estimating the variable part of the remuneration are:
- the expected value method, that is the weighted sum of the amounts in a range of possible considerations (for example, the company has a high number of contracts with similar characteristics);
- the most likely amount method, that is the most likely amount in a range of possible considerations (for example, the company receives a performance bonus or otherwise).

In the presence of variable considerations, the revenue is recognised in the income statement if it is possible to estimate the revenue reliably and only if it is highly likely that this consideration will not subsequently have to be reversed from the income statement, wholly or in a significant part. In the event of strong prevalence of factors of uncertainty linked to the nature of the consideration, the same will be recognised only at the moment in which this uncertainty is resolved. In any case, the estimated part of the transaction price must be updated at the end of each reporting period. In determining the price, the presence of financial components must be considered, if significant.
In the case of commercial agreements the provide payment to the entity of variable non-cash considerations, linked to the achievement of specific targets spendable in the provision of services rendered by the commercial partner, the Bank recognises this revenue in the income statement of the period in which they accrue, for an amount not more than the fair value of the services effectively rendered by the partner.
If the entity receives from the customer a consideration which provides for repayment, to the customer itself, wholly or in part, the revenue obtained, a liability must be recognised (the so-called "refund liabilities") against the forecast future refunds. This may occur, for example, when the customer has a right of withdrawal on the good or in the contract a so-called claw back clause is provided. This principle applies also to loyalty programmes. The liability for future refunds is equal to the amount of the consideration received (or receivable) to which it is expected not to have

a right (that is amounts not included in the transaction price). The liability for future refunds (and the corresponding change in the transaction price and, consequently, the liability deriving from the contract) must be updated to the date of closure of each reporting period to take into account the changes in circumstances.
In relation to the Bank's operations, the aforementioned particular cases were not recognised.
Finally, the costs related to attainment and fulfilment of contracts with customers are recognised in the income statement in the periods in which the corresponding revenue is accounted for; costs that do not have a direct association with revenue are booked immediately to the income statement.

■ Revenues and costs related to financial instruments
With reference to income and expenses related to financial assets/liabilities we must specify that:

a) interest is recognised *pro-rata temporis* on the basis of the contractual interest rate or of the effective interest rate in case of application of amortised cost; the negative income components accrued on financial assets are recognised under item "20. Interest and similar expense"; the positive economic components accrued on financial liabilities are recognised under item "10. Interest and similar income". The item interest income (or interest expense) also includes the spreads or margins, positive (or negative), accrued up to the reporting date, related to financial derivative contracts:
   - Hedging assets and liabilities that generate interest;
   - Classified in the Balance Sheet in the trading book, but operationally connected to financial assets and/or liabilities measured at fair value (fair value options);
   - connected operationally with assets and liabilities classified in the trading book and which provide for settlement of spreads or margins at several due dates;
b) default interest is recorded in the income statement solely at the time it is effectively collected;
c) dividends are recognised in the income statement at the moment in which their distribution is resolved and therefore the right to receive the related payment matures;
d) fees for revenues from services are recognised, on the basis of the existence of contractual agreements, in the period in which the services themselves were provided. Fees considered in amortised cost for the purposes of determining the effective interest rate, are recognised among interest;
e) gains and losses consequent to first recognition at fair value, determined by the difference between the transaction price and the fair value of the instrument, are recognised in the income statement when the transaction is recorded if the fair value can be determined with reference to parameters or recent transactions observable on the same market where the instrument is traded; otherwise, they are distributed over time, taking into account the duration and nature of the instrument;
f) gains and losses deriving from the sale of financial instruments are recognised in the income statement at the moment of completion of the sale, with related transfer of the risks and benefits, on the basis of the difference between the consideration received and the book value of the instruments themselves.

■ Share-based payments
These are payments to employees, as consideration of the work done, settled with equity instruments, that consist, for example, of assigning:

- rights to subscribe paid capital increases (stock options);
- rights to receive shares on achieving certain targets.

In consideration of the difficulties of directly estimating the fair value of the work services received as a counter-entry of the assignment of shares, it is possible to measure the value of the services received, indirectly, making reference to the fair value of the equity instruments, at date of their assignment. The fair value of the payments settled with the issue of shares is recognised, on the basis of the criterion of accrual of the service provided, in the income statement item “160. a) Personnel expenses” as a counter-entry to an increase in item “140. Reserves”. In particular, when the shares assigned are not immediately “usable” by the employee, but will be when the employee has completed a specific period of service, the company recognises the cost as consideration for the service rendered along the period of maturation of the said conditions (“vesting period”).

■ **Amortised cost**

The amortised cost of a financial asset or liability is the value at which it has been measured on initial recognition net of repayments of principal, increased or decreased by total amortisation calculated using the effective interest rate method, on the differences between the initial value and net of any permanent impairment.
The effective interest rate is the rate that makes the present value of a financial asset or liability equal to the contractual flow of the future payments in cash or received up to maturity or at the later date of recalculation of the price. For the calculation of the current value, the effective interest rate is applied to the flow of the future collections or payments estimated over the entire useful life of the financial asset or liability - or a shorter period in the presence of certain circumstances (for example the review of the market rates).
Subsequent to initial recognition, the amortised cost makes it possible to allocate revenues and costs decreasing or increasing the instruments over the entire estimated life of the same via the amortisation process. The determination of the amortised cost differs according to whether the financial assets/liabilities being measured are fixed or floating rate. With regard to fixed-rate instruments, the future cash flows are quantified on the basis of the interest rate noted over the duration of the loan. For floating-rate financial assets/liabilities, whose variability is not known in advance (because, for example, it is linked to an index), the cash flows are determined on the basis of the last known rate. As of every rate review date, steps are taken to recalculate the repayment plan and the effective rate of return over the entire useful life of the instruments, in other words to maturity. The adjustment is recognised as a cost or as income in the income statement.
Measurement at amortised cost is carried out for financial assets measured at amortised cost and for those measured at fair value through other comprehensive income; and for financial liabilities measured at amortised cost.
Financial assets and liabilities traded at market conditions are initially recognised at their fair value, which normally corresponds to the amount disbursed or paid including, for instruments measured at amortised cost, the transaction costs and fees directly attributable.
Internal or external marginal costs and income attributable to the issue, acquisition or disposal of a financial instrument and not rechargeable to the customer are considered transaction costs. These costs/fees, which must be directly ascribable to the individual financial asset or liability, affect the original effective return and render the effective interest rate associated with the transaction different from the contractual interest rate. Costs/income related indistinctly to several transactions and the components related to events that may occur during the life of the financial instrument, but which are not certain at the moment of the initial definition, such as fees for retrocession, for non-use, for early settlement, are excluded.

The costs that the Bank has to bear irrespective of the transaction (for example, administrative, stationery, communication costs), those which, although they are specifically attributable to the transaction, come within the normal loan management practice (for example, activities aimed at disbursement of the loan), ad fees for services received following performance of structured finance activity that would, in any case, by received irrespective of the subsequent financing of the operation (such as facility and arrangement fees) are also not considered.
With particular reference to receivables, commissions paid to distribution channel (agents, consultants, mediators) and fees paid for advice/assistance for the organisation and/or participation in syndicated loans are considered costs attributable to the financial instruments while revenue considered in the calculation of amortised cost are those of participation in syndicated operations and brokerage fees connected to commissions recognised by brokerage companies.

As regards securities not measured at fair value through profit or loss, fees for contracts with brokers operating on Italian equity markets, those disbursed to intermediaries operating on foreign equity and bond markets defined on the basis of fee tables are considered transaction costs.
For securities issued, fees for the placing of bond loans paid to third parties, the fees paid to stock exchanges and fees paid to independent auditors for the activity performed in relation to the single issue are considered in the amortised cost calculation, while fees paid to rating agencies, legal and consultancy/auditing expenses and expenses for the annual updating of prospectuses, costs for the use of indices and fees that originate during the life of the bond loan issued are not considered related to amortised cost.

With respect to the general approach the effective interest rate must be calculated differently for financial instruments measured at amortised cost or at fair value through other comprehensive income, purchased or originated, which at the moment of their first recognition are already credit impaired (so-called PCI or OCI).
The criterion of measurement at amortised cost does not apply for hedged financial assets/liabilities for which recognition of changes in fair value related to the risks hedged in the Income Statement is provided for. The financial instrument is however newly measured at amortised cost in the case of cessation of the hedging, the moment starting from which changes in fair value previously recognised are amortised, calculating a new effective interest rate which considers the value of the receivable adjusted by the fair value of the part hedged, up to expiry of the hedging originally provided for. In addition, as already noted in the paragraphs on financial assets and liabilities measured at amortised cost, measurement at amortised cost does not apply for financial assets/liabilities whose brief duration leads to believing negligible the economic effect of discounting for receivables without a defined maturity or until revoked.

■ Purchased and originated credit-impaired(POCI) assets

These are instruments for which the credit risk is very high and which, in the case of purchase, are purchased at a considerably discounted value with respect to the value of initial disbursement. For this reason, they are considered already credit-impaired at the moment of first recognition in the financial statements. These assets are classified, according to the business model with which the asset is managed, in item "30. Financial assets measured at fair value through other comprehensive income" or in item "40. Financial assets measured at amortised cost".
Among POCI assets there are two different kinds:

- impaired instruments or loan portfolios purchased on the market (Purchased Credit Impaired - "PCI");
- loans disbursed by the Group to customers distinguished by very high credit risk (Originated Credit Impaired - "OCI").

Impaired financial assets purchased through business combinations under the terms of IFRS 3 come within the scope of application of IFRS9 PCI assets.
We must specify that these financial assets are initially recognised in stage 3, without prejudice to the possibility of reclassifying them among performing receivables (stage 2), on which, therefore, an expected loss will continue to be recognised according to an impairment model based on lifetime ECLs, as illustrated below.
With reference to the criteria of initial recognition, measurement and derecognition please see what is illustrated in correspondence with the asset items in which they can be classified, subject to what is specified below, with reference to the methods of determining amortised cost and impairment.
In detail, amortised cost and, consequently, interest income are calculated considering a credit-adjusted effective interest rate or CEIR. As regards determination of the effective interest rate, the aforementioned credit adjustment consists of considering in the estimate of the future cash flows also the expected credit losses along the entire residual duration of the asset. For the purposes of calculating the CEIR the Bank uses the contractual cash flows net of the expected losses.
In addition, the assets in question involve a particular treatment also as regards the impairment process, because they are always subject to determination of an expected loss along the life of the financial instrument (lifetime ECL).

After initial recognition, the gain or loss deriving from any change in the expected losses along the whole life of the loan with respect to the initial losses must therefore be recognised in the income statement. For these assets it is therefore not possible for the calculation of the expected losses to occur taking as a reference a time horizon of one year.

■ **Renegotiations**

In some cases, during the life of financial assets and in particular of loans, the original contractual conditions are subject to subsequent amendment with the agreement of the parties to the contract. When, during the life of an instrument, the contractual clauses are amended (both when the amendment is formalised through the signing of a new contract and through an amendment to an existing contract) it is necessary to check whether the original asset must continue to be recognised in the financial statements or whether, on the contrary, the original instrument must be subject to derecognition from the financial statements and a new financial instrument must be recognised.

In general, the changes to a financial asset lead to derecognition of the same and to recognition of a new asset when they are "substantial". The assessment of the "substantiality" of the change is carried out considering only qualitative elements. In particular, renegotiations are considered substantial if they introduce specific objective elements that affect the characteristics and/or the cash flows of the financial instrument (such as, a change in the currency of denomination, the introduction of indexing to equity or commodity parameters) in consideration of the significant impact expected on the original cash flows or which are made in relation to customers that do not present financial difficulties, with the objective of adjusting the onerousness of the contract to the current market conditions. In this latter case, we must specify that if the bank did not permit renegotiation of the contractual conditions, the customer would have the possibility of obtaining finance from another intermediary with consequent loss for the bank of the revenue flows provided for in the renegotiated contract; in other words, in the face of a renegotiation of a commercial nature, it is considered that for the bank there is no loss to be recognised in the income statement consequent to realignment to the best current market conditions for its customers. On the contrary, in the presence of renegotiations considered non-substantial the gross value is redetermined through calculation of the present value of the cash flows consequent to the renegotiation, on the basis of the original interest rate of the exposure existing before the renegotiation. The difference between this gross value and the gross book value prior to the change is recognised in the income statement as a gain or loss on contractual changes without cancellations (so-called "modification accounting"). The case of non-substantial renegotiations includes modifications granted to counterparties with financial difficulties (granting of forbearance measures) attributable to the bank's attempt to maximise the recovery of the original exposure, the risks and benefits of which continue, however, to be held by the bank. Modifications that introduce into the contract substantial objective elements capable in themselves of entailing the derecognition of the financial asset, as illustrated above, are an exception.

■ **Accounting treatment of contributions to deposit guarantee systems and resolution mechanisms**

Italian Legislative Decrees 180 and 181 of 2015 transposed into Italian legislation Directive 2014/59/EU, the Banking Resolution and Recovery Directive ("BRRD"), which provides for the establishment of resolution funds. These funds are endowed, among other things, by:

a) contributions paid by banks on an annual basis, aimed at reaching the target level of fund endowment set by the legislation;
b) extraordinary contributions paid by banks if the ordinary contributions are insufficient to cover the interventions decided in the context of resolution.

Both types of contributions come within the scope of application of the interpretation IFRIC 21 "Levies", because these contribution obligations derive from legislative provisions. On the basis of this interpretation a liability must be recognised on occurrence of the "obligating event" that creates the payment obligation. The counter-entry of this liability is represented by Income Statement item 160 "Administrative expenses b) other administrative expenses", as the conditions are not fulfilled either for recognition of an intangible asset under the terms of the accounting standard

IAS 38 "Intangible Assets", or for recognition of an asset for advance payment. The same treatment is reserved for the "*ex ante*" contributions paid to the Interbank Deposit Protection Fund in the context of Directive 2014/49/EU "Deposit Guarantee Schemes" (DGS), contributions that the Bank does not pay because it does not have a "contributive base".

c) Other aspects

■ **The classification criteria for financial assets**

The classification of financial assets in the three categories provided for in the standard depends on two criteria, or drivers, of classification: the Business Model with which the financial instruments are managed and contractual characteristics of the cash flows of the financial assets (or SPPI Test).

The combined provisions of the aforementioned two drivers leads to the classification of the financial assets, according to what is highlighted below:

- Financial assets measured at amortised cost: assets that pass the SPPI test and fall within the Held To Collect (HTC) business model;
- Financial assets measured at fair value through other comprehensive income (FVOCI): assets that pass the SPPI test and fall within the Held To Collect and Sell (HTCS) business model;
- Financial assets measured at fair value through profit or loss (FVTPL): this is a residual category, which includes financial instruments which are not classifiable in the previous categories on the basis of what has emerged from the business model test or from the test on the characteristics of the contractual flows (SPPI test not passed).

■ ***Business model***

As regards the business model, IFRS 9 identifies three cases in relation to methods with which cash flows and sales of financial assets are managed.

- Held to Collect (HTC): this is a business model the objective of which is achieved through the collection of contractual cash flows of the financial assets included in the portfolios associated with it. Inclusion of a portfolio of financial assets in this business model does not necessarily entail the impossibility of selling the instruments even if it is necessary to consider the frequency, the value and the timing of sales in previous years, the reason for the sales and expectations with regard to future sales;
- Held to Collect and Sell (HTCS): this is a mixed business model, the objective of which is achieved through the collection of the contractual cash flows of the financial assets in the portfolio and (also) through sales activity which is an integral part of the strategy. Both activities (collection of contractual flows and sale) are indispensable for achievement of the objective of the business model. Therefore, sales are more frequent and significant compared to an HTC business model and are an integral part of the strategies pursued;
- Others/Trading: this is a residual category which includes both financial assets held for trading purposes and financial assets managed with a business model not attributable to the previous categories (Held to Collect and Held to Collect and Sell). In general, this classification applies to a portfolio of financial assets, the management and performance of which are assessed on the basis of its fair value.

The business model reflects the methods with which the financial assets are managed to generate cash flows for the benefit of the entity and is defined by the top management through opportune involvement of the business structures. It is observed considering the methods of managing financial assets and, as a consequence, the extent to which the cash flows of the portfolio derive either from the collection of contractual flows, or from sale of the financial assets or from both these events.

The measurement is not made on the basis of scenarios which, based on reasonable forecasts of the entity, are not likely to occur, such as the so-called "worst case" or "stress case" scenarios. For example, if the entity plans to sell a certain portfolio of financial assets only in a "stress case" scenario, this scenario does not affect the assessment of the entity's business model for these assets if this scenario, on the basis of reasonable forecasts of the entity, is not destined to occur.

The business model does not depend on the intentions that the management has with reference to a single financial instrument, but makes reference to the methods with which groups of financial assets are managed for the purposes of achieving a certain business objective.

In brief, the business model:
- reflects the methods with which financial assets are managed to generate cash flows;
- is defined by the top management, through the opportune involvement of the business structures;
- must be observable considering the methods of managing of financial assets.

In carrying out the assessment of the business model all relevant factors available at the assessment date. The aforementioned evidence includes the strategy, the risks and their management, the remuneration policies, the reporting and the amount of the sale. In the analysis of the business model it is essential for the elements studies to show consistency with each other and in particular for them to be consistent with respect to the strategy pursued. The evidence of activities not in line with the strategy must be analysed and adequately justified.
For Held to Collect portfolios, the Group defined the thresholds of permissibility of the sales that do not affect the classification (frequent but not significant, individually and in aggregate, or infrequent also if of a significant amount) and, at the same time, the parameters were established to identify sales consistent with this business model as they are attributable to an increase in credit risk.
More in detail, in the context of an HTC business model sales are permitted in the case of an increase in credit risk (or when these are sales of impaired loans or securities classified in stage 2), when made in proximity to the maturity and finally when they are frequent but not significant in terms of value or infrequent also if significant in terms of value.
In order to determine these aspects, the thresholds of frequency and significance were defined:
- frequency is defined as the percentage ratio between the number of positions sold (ISIN or ratios) during the observation period and the total of positions in the portfolio present at the beginning of the observation period (and is considered equal to zero if the number of securities at the beginning of the period is less than a certain amount);
- significance is defined as the percentage ratio between the nominal value of sales and the total nominal value of instruments in the portfolio present at the beginning of the observation period.

In cases of observance at the same time of both thresholds of frequency and significance in terms of single sale, a further assessment in terms of aggregate amount of sales is provided for in order to confirm the consistency of the HTC business model.

■ SPPI test

The other criterion to be used to determine whether a financial asset must be classified among financial instruments measured at amortised cost or at FVOCI - besides the analysis of the business model presented above - states that the related cash flows must consist exclusively of payment or repayment of principal and interest. To this end IFRS 9 states that a test, known in fact as “SPPI” (solely payments of principal and interest) must be carried out, for the purpose of checking that the remuneration of a certain financial instrument, debt securities and loans, is linked exclusively to payment of interest and to repayment of principal.
A debt instrument that does not pass the SPPI test must always be measured at FVTPL and classified in the sub-item “other financial assets obligatorily measured at fair value”.
For the purposes of the analysis, IFRS 9 proposes a definition of the terms principal and interest as follows:
- principal is understood as the fair value of the financial asset at the moment of its initial recognition;
- interest is the consideration for the time value of money, for the credit risk associated with the principal in a certain period of time, for other risks and costs associated with the basic risks of a loan operation and for the profit margin.

In basic lending arrangements, the value of interest must depend exclusively on the time value of money and on the credit risk associated with the principal amount in a certain period of time. Each time the contractual terms introduce

other elements, it is no longer possible to consider that asset as a generator exclusively of cash flows in terms of principal and interest. This could happen, for example, when the cash flows come from so-called non-recourse financial assets. The cash flows of the aforesaid financial assets may not consist of payment solely of interest and repayment of principal, because the remuneration is linked to specific business activities. On this point the holder of the asset is obliged to assess, through the so-called look-through approach, whether its own instruments pass or fail the SPPI test. For example, when the entity holds the non-recourse financial assets, the cash flows of which depend on the performance of a financial element of the issuer (for example net income), then the possibility of measurement at amortised cost or FVOCI must be excluded.
In addition, when the contractual cash flows depend on characteristics such as changes in equity or commodity prices, the related financial instruments cannot pass the SPPI test, given that they introduce an exposure to risk or volatility not related to the basic lending arrangements.
IFRS 9 in addition specifies that all financial instruments that undergo the so-called "financial leverage effect", cannot be considered generators of flows of principal and interest, because leverage has the power to increase the volatility of the cash flows. This case includes swaps, options, forwards and all derivative contracts.
IFRS 9 defines two cases in which the time value of money can be considered modified, that is when the relationship between the passing if time and the interest rate is considered imperfect. A case occurs when the interest rate of the asset is redetermined periodically, but the frequency of this redetermination the frequency of the payment does not correspond to the nature of the interest rate. This occurs for example in the case of monthly payments of floating interest, and at the beginning of each month the interest rate is determined as the Euribor at 1 year: the monthly interest rate is determined with reference to interest calculated annually, and therefore for a different time period. In these cases, the accounting standard introduces the need to make a comparison between the cash flows deriving from the entity's own financial asset and those deriving from a financial asset considered identical for credit risk and duration, but for which the monthly interest is calculated on the basis of the monthly Euribor. The other case of non-perfect correspondence between the passing of time and the time value of money occurs when the interest rate of the asset is redetermined periodically on the basis of an average of particular short- or medium/long-term interest rates. This happens, for example, when a financial asset provides for payment of interest every three months, based on the average of the three-month Euribor interest rate in the quarter prior to that to which the interest refers.
Therefore, in these cases, the entity must analyse whether, despite the change in the time value of money, the financial asset generates only cash flows in terms of principal and interest. The objective of this analysis is to check how different the non-discounted contractual cash flows would be if there were not the change in the time value of money (the so-called benchmark cash flow test).
The presence of contractual clauses that can modify the periodicity or the amount of the contractual cash flows must be considered to assess whether these flows meet the requirements to be considered SPPI (for example prepayment options, possibility of deferring the contractually expected cash flows, instruments with embedded derivatives, subordinated options, etcetera).
However, as provided for in IFRS 9, a characteristic of the contractual cash flows does not affect the classification of the financial asset if it can only have a *de minimis* effect on the contractual cash flows of the financial assets (in each financial year and cumulatively). In the same way, if a characteristic of the cash flows is not realistic (not genuine), or if it affects the contractual cash flows of the instrument only on the occurrence of an extremely rare event, very unusual and very improbable, it does not affect the classification of the financial assets
In the case of instruments subordinated to another instrument (e.g. guaranteed debt securities), the related cash flows are connected to the nominal value of the principal or interest of the main instrument. The holder of the instrument has the power to exercise the right of pre-emption also in the case of bankruptcy of the debtor. These instruments come within those that do not pass the SPPI test.
As regards contractually-linked instruments, reference is made to instruments with which an entity gives a certain priority to payment of the cash flows. The order of priority depends on the credit risk assigned to each category of creditor, called

"tranche". The characteristics that an investment, belonging to a certain tranche, must have in order to be considered a generator of cash flows represented exclusively by payment of interest and repayment of principal are the following:

- The underlying assets must contain one or more financial assets which produce cash flows made up solely of payment of interest and repayment of principal. In addition, the presence of supporting financial instruments, such as derivatives, is permitted only if they have the function of reducing the volatility of the related cash flows;
- The exposure to credit risk related to certain tranche must be equal to or less than the exposure to the risk attributable to the underlying financial instruments.

For the purposes of performing the SPPI test, for operations in debt securities the MPS Group avails itself of the services provided by an info-provider. Only if the securities are not managed by the info-provider, the test is carried out manually through the use of a proprietary tool based on a methodology developed internally (decision-making trees). To perform the SPPI test in the context of the loan granting processes a proprietary tool based on a methodology developed internally (decision-making trees) was developed. In particular, given the significant different characteristics, a differentiated management is envisaged for products attributable to a contractual standard (typically retail loan portfolio) and tailor-made financing (typically corporate loan portfolio). For standard products, the SPPI test is performed on structuring the contractual standard, through the "Product Approval" process and the result of the test is extended to all the single relationships attributable to the same product in the catalogue. Instead for tailor-made products, SPPI test is performed for each new credit line/relationship submitted to the decision-making body through the use of the proprietary tool. The decision-making trees - included in the proprietary tool - were prepared internally (for both debt securities and loans) and capture the possible non-SPPI-compliant characteristics.

16) USE OF ESTIMATES AND ASSUMPTIONS IN PREPARING THE FINANCIAL STATEMENTS

The accounting estimates required to apply the accounting standards may have significant effects on the amounts recorded in the balance sheet and in the income statement, as well as on information about contingent assets and liabilities reported in the financial statements. Processing those estimates requires using the information available and making subjective evaluations. For their very nature, the estimates and assumptions used may vary from year to year and, as such, it cannot be excluded that in future years the current values posted on the financial statements may differ, even significantly, as the subjective assessments used alter. These estimates and evaluations are therefore difficult to make and inevitably bring some uncertainty, even in stable macroeconomic conditions.

The main cases for which the use of subjective evaluation by the Company Management is required are:

a) quantification of losses for impairment of loans and, in general, of the other financial assets;
b) assessment of the congruity of the value of equity investments and of other non-financial assets (goodwill, property, plant and equipment and intangible assets);
c) use of measurement models to recognise the fair value of financial instruments not quoted on active markets;
d) the estimate and assumptions on the recoverability of deferred tax assets;
e) the estimate of the liabilities deriving from the defined-benefit company pension funds;
f) quantification of provisions for risks and charges of a legal and fiscal nature.

For some of the cases listed above it is possible to identify the main factors that are the subject of estimates by the Bank and the Group and that therefore contribute to determine the book value of assets and liabilities.

In brief, we can note that:

a) for allocation to the three credit risk stages provided for in IFRS 9 of loans and debt securities classified among Financial assets at amortised cost and Financial assets at fair value through other comprehensive income and the calculation of the related expected losses, the main estimates regard:
    - determination of the parameters of significant increase in credit risk, based essentially on models for measuring probabilities of default (PDs) on origination of the financial assets and at the reporting date;

- the inclusion of forward-looking factors, also of a macroeconomic type, for determination of PD, EAD and LGD;
- for determination of the estimates of future cash flows deriving from impaired receivables, certain elements are taken into consideration: the expected recovery times, the estimated realisable value of any guarantees, the costs that it is believed will be borne for recovery of the loan exposure and, finally, the probability of sale for positions for which there is a disposal plan;

b) for the determination of the fair value of financial instruments not quoted on active markets, if it is necessary to use parameters not observable on the market, the main estimates regard, on the one hand, the development of future cash flows (or also income flows, in the case of equity securities), possibly dependent on future events, on the other, the level of certain parameters in input not quoted on active markets;

c) for the quantification of pension funds and for similar obligations the present value of obligations is subject to estimates, taking into account the flows, opportunely discounted, deriving from the historical and statistical analyses and analyses of the demographic curve;

d) for quantification of provisions for risks and charges, the amount of outlays necessary for fulfilment of the obligations is subject to estimates, if possible, taking into account the effective probability of having to use resources;

e) for determination of the items related to deferred taxes the probability of an effective future payment of taxes (taxable temporary differences) is estimated together with the degree of reasonable certainty - if any - of future taxable amounts at the moment in which the tax deductibility will become manifest (deductible temporary differences).

For points a) and b) please see the respective paragraphs “Methods of determining the impairment of IFRS 9 financial instruments” and “Methods of determining the impairment of other non-financial assets” below, and, in particular as regards point b), paragraph A.4.3 “Fair value hierarchy”. In the context of the single sections of the notes to the balance sheet and income statement where the single contents of the individual accounting items are detailed, the actual technical and conceptual solutions adopted by the Bank and the Group are then analysed and discussed in depth. As regards point e) please see section 10 of the assets of the Notes to the Financial Statements “Tax assets and tax liabilities”, for the cases pursuant to points c) and d) please see section 10.5 of the liabilities of the Notes to the Financial Statements “Defined-benefit company pension funds” and section 5. Operational Risks of part E of the Notes to the Financial Statements.

■ Methods of determining the impairment of IFRS 9 financial instruments

At each reporting date, under the terms of IFRS 9, financial assets other than those measured at fair value through profit or loss are subjected to an impairment test, with the aim of estimating the expected impairment losses due to credit risk (so-called ECLs - expected credit losses). In particular the perimeter to be subjected to impairment tests comprises:

- “Financial assets measured at amortised cost”;
- “Financial assets measured at fair value through other comprehensive income” other than equity securities;
- commitments to disburse funds and guarantees given which are not measured at fair value through profit or loss; and
- trade receivables or assets deriving from contracts that result from transactions falling within the scope of application of IFRS 15.

According to the Expected Credit Losses calculation model, introduced by IFRS 9, the losses must be recorded not only making reference to the objective evidence of impairment already manifest at the measurement date, but also on the basis of the expectation of future impairment losses that have not yet occurred. This concept represents in fact an innovation with respect to that of incurred loss on which the previous impairment model was based.

In particular, the ECL model involves the aforementioned instruments being classified in three distinct “stages”, according to their absolute or relative credit quality with respect to initial disbursement, to which correspond different criteria for measuring the expected losses. In detail:

- stage 1: this comprises performing exposures which have not suffered a significant change in credit risk with respect to the initial recognition. The value adjustments correspond to the expected losses associated with the occurrence of default in the 12 months following the reporting date;
- stage 2: this comprises performing exposures whose creditworthiness is affected by a significant change in credit risk, but for which the losses are not yet observable. The adjustments are calculated considering the loss along all the residual lifetime of the instrument;
- stage 3: this comprises all impaired receivables, that is non-performing exposures which present objective evidence of impairment and which must be written down using the concept of lifetime expected loss.[10]

An exception to the above is represented by financial assets considered as impaired right from their acquisition or origin (so-called "POCI - Purchased or Originated Credit Impaired"), for the treatment of which please see what has already been illustrated in the previous paragraph on this subject.

For the MPS Group and, within it, for the Bank, the perimeter of exposures classified in stage 3 corresponds to that of impaired exposures, identified on the basis of the definitions established by the supervisory regulations (Bank of Italy Circular no. 272 "Accounts Matrix") and referred to in Bank of Italy Circular no. 262 "Banking Financial Statements: Formats and Rules for Compilation", because they are considered consistent with the accounting rules provided for in the IAS/IFRS accounting standards, in terms of objective evidence of impairment. On the basis of the aforementioned circulars, the perimeter of impaired exposures corresponds to the aggregate "Non-Performing Exposures", defined by Regulation (EU) 2015/227 which endorsed the EBA ITS "Implementing Technical Standards (ITS) on Supervisory Reporting on Forbearance and Non- Performing Exposures" (EBA/ITS/2013/03/rev1 24/7/2014).

In detail, the aforementioned circulars identify the following categories of impaired assets:

- Bad loans: the set of on- and off-balance sheet exposures in relation to a customer in a state of insolvency (even if not legally ascertained) or in substantially equivalent situations, irrespective of any loss forecasts formulated by the bank;
- Probable defaults (or "unlikely to pay"): these represent on- and off-balance-sheet exposures, for which the conditions are not fulfilled for classification of the debtors among bad loans and for which it is considered unlikely that, without recourse to actions such as enforcement of the guarantees, the debtors will comply fully (in principal and/or interest) with their loan obligations. This assessment is made irrespectively of the presence of any amounts (or instalments) past-due and unpaid. Classification among probable defaults is not necessarily linked to the explicit presence of anomalies, such as non-payment, but is linked to the existence of elements indicating a situation of risk of non-fulfilment by the debtor (for example, a crisis of the industrial sector in which the debtor operates);
- Impaired past-due and/or over-the-limit exposures: on-balance-sheet exposures, other than those classified among bad debts or probable defaults, which, at the reporting date, present a past-due and/or over-the-limit position for more than 90 days, according to the significance thresholds provided for in the aforementioned regulations. For the MPS Group impaired past-due and/or over-the-limit exposures are determined making reference to the position of the individual debtor.

In addition, the Bank of Italy regulations, in line with the EBA standards, introduced the definition of "Forborne Exposures". These in particular are exposures the benefit from measures of forbearance, which consist of concessions

(10) *The assessment is statistical for positions with a balance of less than € 0.5 mln and analytical, carried out by the managers, for positions above this threshold.*

in relation to debtors, in terms of modification and/or refinancing of a pre-existing loan, exclusively owing to, or to prevent, a condition of financial difficulty that could have negative effects on their ability to fulfil the contractual commitments originally assumed and which would not have been granted to other debtors with analogous risk profiles not in financial difficulty. These concession must be identified at the level of the single credit line and may regard exposures of debtors classified both in performing status and in non-performing (impaired) status. For exposures with forbearance measures classified among probable defaults, return among performing exposures can occur only after at least one year has passed since the moment of the concession (so-called "cure period") and all the other conditions provided for in paragraph 157 of the EBA ITS have been met.
In any case, renegotiated exposures must not be considered forborne when the debtor is not in a situation of financial difficulty (renegotiations carried out for commercial reasons).

■ **Loss of value of performing financial assets**
For performing financial assets, that is for assets not considered impaired it is necessary to assess, at level of the single relationship, the presence of a significant deterioration of credit risk, by comparing the credit risk associated with the financial instrument at the moment of measurement and that at the initial moment of disbursement or acquisition. This comparison is made assuming as a reference both quantitative and qualitative criteria. The consequences of this check, from the point of view of classification (or, more properly, of staging) and measurement, are the following:
- if these indicators exist, the financial asset goes into stage 2. The assessment, in this case, in keeping with the provisions of the international accounting standards and even in the absence of a manifest loss of value, provides for the recognition of value adjustments equal to the expected losses along the entire residual life of the financial instrument. These adjustments are revised at each subsequent reporting date both to check periodically the congruity with respect to the estimate of loss constantly updated, and to take into account - if the indicators of a "significantly increased" credit risk cease - the changed forecast horizon for calculating the expected loss;
- if these indicators do not exist, the financial asset goes into stage 1. The assessment, in this case, in keeping with the provisions of the international accounting standards and even in the absence of manifest loss of value, provides for the recognition of expected losses, for the specific the financial instrument, during the next twelve months. These adjustments are revised at each subsequent reporting date both to check periodically the congruity with respect to the estimate of loss constantly updated, and to take into account - if indicators of a "significantly increased" credit risk arise - the changed forecast horizon for calculating the expected loss.

As regards the assessment of financial assets and, in particular, the identification of the existence of a "significant increase" in credit risk (a necessary and sufficient condition for classification of the asset being assessed in stage 2), the elements which under the terms of the standard and its operational declination carried out by the MPS Group constitute the principal determinants to be taken into consideration are the following:
- relative quantitative criteria, based on statistical observations, considered expression of a significant increase in credit risk that has occurred over time;
- absolute qualitative criteria, represented by the identification of trigger events or by exceeding absolute thresholds in the context of the credit monitoring process. They include:
  - all exposures affected by forbearance measures that present this attribute still active, irrespective of the regularity or otherwise of the probation period in progress;
  - exposures classified in the High Risk and Requalification operating portfolios;
  - customers with negative EBITDA;
- backstop indicators, that is credit "delinquency" factors, the manifestation of which leads to presume that a significant increase in credit risk has occurred, unless there is contrary evidence. As an assumption, the MPS Group believes that the credit risk of the exposure must be considered significantly increased in the presence of an amount past due/over the limit for a period of more than 30 days, without affecting application of the thresholds of

significance provided for in the supervisory regulations. With particular reference to the relative quantitative criterion applicable to loan exposures in relation to customers, the MPS Group decided to assume as reference the change between the lifetime cumulative forward-looking probability of default (PD) recognised at the origination of the contractual relationship and the probability of default recognised at the measurement date. The development of the model entailed the identification of specific internal thresholds of change between the PD recognised at the origination of the contractual relationship and the PD recognised at the measurement date differentiated by counterparty, initial rating class and vintage. Exceeding the aforesaid thresholds constitutes an expression of a significant increase in credit risk and the single credit line is consequently transferred from stage 1 to stage 2. The comparison is based on uniform residual durations[11] and on uniform PD models, for example if the definition of default changes over time, the lifetime cumulative forward-looking PD at origination is redetermined to take into account this new definition of default. The cumulative PDs involved in the comparison are based on the same model used for ECL purposes (e.g.: definition of PIT - Point in Time - PD, macroeconomic scenarios, expected life/contractual life). In order to obtain an unequivocal classification result, a cumulative PD is used, which results from the weighted average of the cumulative PDs calculated for the single prospective scenarios using as weights the probabilities of the scenarios. The significance threshold is determined, measuring historically, using quantile regression analysis by cluster as level of ratio, between lifetime cumulative forward-looking PD at the reporting date and that at the origination date, which can be considered predictive of transfer to NPE[12]. The threshold is determined so as to minimise the so-called false positives and false negatives and maximise the true positives and true negatives. As regards debt securities that do not have an investment grade rating the relative quantitative criterion is based on the change in lifetime cumulative forward-looking PD between reporting date and origination date greater than a given threshold. For corporate issuers the multi-annual PD curve is the corporate one estimated entirely by the Group; for government issues the multi-annual PD curve is the one prepared on the basis of the Moody's matrix of defaults at 1 year of government securities. The cumulative PDs involved in the comparison are based on the same model used for ECL purposes (e.g.: definition of PIT - Point in Time - PD and macroeconomic scenarios). In order to obtain an unequivocal classification result, a cumulative PD is used, which results from the weighted average of the cumulative PDs calculated for the single prospective scenarios using as weights the probabilities of the scenarios. Exposures are classified in stage 2 if the ratio between lifetime cumulative forward-looking PD at the reporting date compared to that at the origination date exceeds a given significance threshold equal, for both corporate securities and government ones, to that used for corporate exposures in the form of loans. Debt securities which at the reporting date have an investment grade rating, mainly attributable to government securities, are classified in stage 1 because for this case, and only for it, the MPS Group availed itself of the "Low Credit Risk Exemption". This exemption consists of the practical expedient of not performing the test related to significant deterioration of the credit risk, in the presence of exposures whose credit risk is considered low. This exemption is applied to securities that, at the measurement date, have an investment grade rating level, in full conformity with the provisions of the accounting standard IFRS 9. In addition, considering the presence of several purchase transactions involving the same fungible security (ISIN), it became necessary to identify a methodology for identifying the tranches sold in order to determine the residual quantities with which to associate the credit quality at the date of initial recognition to be compared with that at the measurement date. In this regard it was considered suitable to use the FIFO (First In - First Out) methodology because it enables more transparent management of the portfolio, also from the operational point of view (front office), permitting, at the same time, continual updating of the assessment of creditworthiness on the basis of the new purchases.

(11) *Therefore, the assessment at 31/12/T of the significant increase in credit risk of a thirty-year loan disbursed on 31/12/T-5 is made comparing the lifetime cumulative forwardlooking PDs on the residual life of 25 years.*

(12) *Transfer to NPE is measured on multiyear horizons.*

In general, the criterion for transfer between stages is symmetrical. In particular, an improvement of the credit risk such as to remove the conditions that have led to the significant increase in the same entails the re-attribution of the financial instrument from stage 2 to stage 1. In this case the entity redetermines the value adjustment on a time horizon of twelve months instead of as previously recognised over the lifetime, recognising, consequently, in the income statement a write-back.

Once the allocation of the exposures to the different credit risk stages has been defined, the expected losses (ECLs) are determined, at the level of single transaction or security tranche, starting from the IRB/Operating models, based on the parameters of Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD), on which specific adaptations are carried out, so as to guarantee their compliance with the specific prescriptions of IFRS 9, given the different requirements and purposes of the accounting regulations with respect to the prudential regulations.

For PD, LGD and EAD the following definitions apply:
- PD (Probability of Default): probability of migrating from the performing status to that of impaired receivable over a time horizon of one year. In the models consistent with the supervisory provisions, the PD factor is typically quantified through the rating. In the MPS Group the PD values derive from the internal rating models, if available, supplemented by external assessments or by average of segment/portfolio data;
- LGD (Loss Given Default): percentage loss in the event of default. In the models consistent with the supervisory provisions this is quantified through the historical experience of discounted recoveries on files classified as non-performing loans;
- EAD (Exposure At Default) or credit equivalent: amount of the exposure at the moment of default.

As already noted above, to be able to observe the provisions of IFRS 9 it became necessary to take specific actions to adjust the above factor, among which we can note in particular:
- adoption of a Point in Time (PIT) PD against the Through the Cycle (TTC) PD used for Basel purposes;
- removal from LGD of a number of additional components, namely indirect costs (non-recurring costs) and the component linked to the adverse economic cycle (so-called “down turn”); and to reflect the most current recovery rates (PIT), the expectations for future (forward-looking) trends and the inclusion of any recovery fees in the case of recovery entrusted to third parties;
- use of multi-period PDs and, if necessary, LGDs, in order to determine the expected loss per for the entire residual life of the financial instrument (stages 2 and 3);
- use, in the context of the process of discounting expected future cash flows, of the effective interest rate of the single operation, unlike what is provided for in the regulatory models, in which the single cash flows are discounted using discounting rates determined in accordance with the prudential regulations.

In relation to the multi-period EAD, in line with the provisions of IFRS 9, the MPS Group makes reference to plans at amortised cost, irrespective of the related measurement methods (amortised cost or fair value through other comprehensive income). For commitments to disburse funds and guarantees given (off-balance-sheet exposures), the EAD is, instead, assumed to be equal to the nominal value weighted for a specific credit conversion factor (CCF).
The forecasts of the (forward-looking) macroeconomic indicators, provided by an external consultant of leading standing and reprocessed internally by the Research Unit, are quantified on the basis of three possible future scenarios, which consider the economic variables considered relevant (Italian GDP, interest rates, unemployment rate, price of commercial and residential properties, inflation, stock indices), with a future time horizon of three years to which are assigned the respective probabilities of occurrence, determined internally by the Group. In more detail, alongside the “baseline” scenario considered most probable, that is the forecast macroeconomic scenario on the basis of which the MPS Group develops its projections in relation to economic/financial and risk data along a short- and medium-term

time horizon, a better (decidedly favourable) and worse (unfavourable) alternative scenario was prepared.
starting from the expected loss related to each scenario, the expected loss was determined as the average of the related losses weighted for the probability of occurrence of each scenario. This approach makes it possible to consider any non-linearities in the relationship between macroeconomic factors, risk parameters and expected loss.
Lastly, for the estimate of the lifetime expected losses, the time horizon of reference is represented by the contractual maturity date; for instruments without maturity, the estimate of expected losses makes reference to a time horizon estimated through a behavioural model for product on demand and made equal to one year with respect to the reporting date in the other cases.

■ Loss of value of non-performing financial assets

As illustrated above, for impaired financial assets, with which is associated a probability of default of 100%, the amount of write-downs for expected losses related to each receivable is equal to the difference between the book value of the same at the moment of measurement (amortised cost) and the present value of the expected future cash flows, this latter calculated using the original effective interest rate (or a proxy of it if unavailable). The cash flows are estimated on the basis of the forecasts of expected recovery along the entire lifetime of the asset, taking into account the estimated realisable value net of any guarantees.
In order to estimate the future cash flows and the related collection times, the receivables in question of a significant unitary amount are the subject of an analytical measurement process. For some uniform categories of impaired receivables of an insignificant unitary amount, the measurement processes involve loss forecasts based on flat rate/statistical calculation methods, to be attributed in an analytical manner to each position. The perimeter of exposures subjected to a flat rate/statistical measurement process, that is on the basis of statistical grids of operating LGD, differentiated according to the segment and length of time in the risk status ("vintage"), is represented:

- by the bad loans and probable defaults with exposures less than or equal to an established significance threshold of € 500 thousand;
- by the set of "past-due" impaired exposures irrespective of the significance threshold of the exposure. These in particular are receivables that present continual over-the-limit positions or delayed payments, identified automatically by the MPS Group's IT procedures, according to the aforementioned rules of the Supervisory Body.

Determining the impairment loss presupposes the measurement of the future cash flows that it is believed the debtor will be able to produce and that will be destined also to service the financial debt. This estimate must be made on the basis of two alternative approaches:

- scenario of the business continuing (so-called "Going Concern Approach"): the operating cash flows of the debtor (or of the effective guarantor) continue to be produced, and are used to repay the financial debts contracted, on the basis of the repayment schedules provided for. The going concern assumption does not exclude any realisation of guarantees, but only to the extent to which this may happen without prejudice to the debtor's ability to generate future cash flows. The "going concern" method is applied also to cases in which recoverability of the exposure is based on any sale of assets by the debtor or on extraordinary operations;
- scenario of the business closing down (so-called "Gone Concern Approach"): applicable in cases in which it is believed that the debtor's cash flows are destined to cease. This is a scenario whose application could possibly regard positions for which classification as bad is provided for. In this context, assuming that actions of the shareholders and/or extraordinary debt rescheduling operations in contexts of a turnaround are not reasonably feasible, recovery of the receivable is based substantially on the value of the guarantees that back the receivable and, subordinately, on the realisable value of the capital asset, taking into account the insolvency assets and any reasons for pre-emption.

With reference to exposures classified as bad and probable default, the quantification of the expected losses includes forward-looking elements related to specific scenarios of sale, where the Group's NPL Strategy envisages that the said exposures may be recovered also through their sale on the market.

Consequently, the estimate of the expected losses of transferable exposures is variable according to, not only the forecast of flows recoverable through the internal management activity (workout), but also to the forecast of flows recoverable through possible sale of the same on the market (so-called "multi-scenario" approach). This arrangement is consistent with what is provided for in the ITG paper of 11 December 2015 "Inclusion of cash flows expected from the sale on default of a loan in the measurement of expected credit losses". In particular with the exposures in question are associated two different estimates of the cash flows that the MPS Group expects to receive:

- the first determined assuming as a reference the scenario of recovery from the debtor on the basis of the internal activity, according to the ordinary measurement guidelines followed by the Group illustrated above (so-called hold scenario);
- the second calculated assuming as a reference the scenario of recovery through sale of the receivable to third parties (so-called sale scenario).

To each of the two scenarios is assigned a probability of occurrence which is higher for clusters more subject to sale procedures on the basis of historical evidence and/or expectations (e.g. formalised NPL reduction plans). The expected loss of the exposures in question is therefore equal to the weighted average for the probabilities assigned to the two scenarios of the estimates of the recoverable cash flows in the two scenarios (hold and sale).

The selling values and the probability of sale therefore represent the two key elements for the definition of the expected loss. To this end the MPS Group carried out an analysis of the historical series of sales (past events) on the same portfolios and certain considerations on the future sale strategies.

The Restructuring Plan approved during 2017 by the European Commission envisages that in the four years 2018-2021 the MPS Group will carry out a strong action to reduce the exposure classified in default, to be implement though sale operations.

This programme represents a qualifying constraint of the Restructuring Plan in view of which the Group, in order to accelerate the process of reducing impaired loans as explicitly requested by the Supervisory Authority, stated that it was willing to bear higher costs with respect to the ordinary recovery scenario, which will continue in parallel on the portfolios of impaired loans not affected and on those of non-impaired loans (stage 1 and 2) with the priority objective of optimising the economic/financial profiles of the workout activity.

On the basis of these considerations, the accounting model of impairment of only impaired loans for the Group provides for differentiated application for:

- receivables subject to the ordinary recovery process: application of the existing accounting policies, revised to take into account the changes introduced by IFRS 9, including in particular the forward-looking and commission component (as a consequence of the outsourcing of the process of recovery on the Sirio platform, managed by Juliet SpA);
- receivables that come within the sale programme: measurement carried out with ordinary policy plus any add-on in order to adjust the portfolios to the estimated sale value.

To determine the add-on the Group considers the following elements:

- selection of the portfolios subject to presumable sale. The perimeter includes positions with a certain attraction on the market as a consequence both of the fact that other banks that have already carried out sale operations and of the presence of expressions of interest already received; and further positions consequent to assessments of convenience carried out by the Parent Company's competent bodies (e.g. presence of widened bad loans positions or a high danger rate);
- probability of sale: the probability of sale was assumed as 80% for all portfolios subject in the past to massive sales. The congruence of this estimate is proven by the fact that the finalisation of the sale of a portfolio, for example of bad loans, depends exclusively on the gap between the Group's expectations and the best offer received: as the expectations are linked to the market prices, the probability of success was quantified in a high threshold given an insignificant expected gap. For loans classified among probable defaults, the probability of sale was determined starting from the success rate observed by the Non-Performing Loan Department as regards the operations contracted and effectively concluded over the last few years, opportunely increased to take into account of the most binding context in which the planned sales programme provided for in the Restructuring Plan is carried out;

- selling prices: the selling prices used are derived from massive transactions on analogous portfolios and single names carried out by the Group or from transactions carried out on the market over the last few years.

■ Method of determining impairment losses of other non-financial assets

Property, plant and equipment and intangible assets with defined useful life are subjected to impairment testing if there is an indication that the book value of the asset can no longer be recovered. The recoverable value is determined with reference to the fair value of the property, plant and equipment or intangible asset net of disposal costs or to the value in use if it can be determined and if it exceeds fair value.

■ Correction of errors

Correction of errors is governed by IAS 8 (Accounting standards, changes in accounting estimates and errors). Based on this standard, errors may be committed in relation to the recognition, measurement, presentation or disclosure of elements in the financial statements.
When the errors are identified in the period in which they were committed they are corrected before publication of the financial statements is authorised.
Material errors identified in years subsequent to those in which they were committed are corrected, where determinable, modifying the comparative information presented in the financial statements of the year in which the errors were identified. In particular, material errors committed in previous periods must be corrected in the first financial statements authorised for publication after their discovery; the correction must be made recalculating retrospectively the comparative amounts of the period in which the error has occurred or, if the error occurred in a period that precedes the periods presented in the financial statements, recalculating the opening balances of assets, liabilities and equity of the first comparative period presented.

Obligations of transparency in the context of rules on public disbursements

Italian Law no. 124/2017 “Annual Law for the Market and Competition” introduced (art. 1, paragraphs from 125 to 129) new measures aimed at ensuring transparency in the system of public disbursements, in the wider context of the set of rules designed to ensure transparency in financial relationships between public bodies and other parties, in part of European origin, in part Italian.

The measure introduces obligations of transparency also for parties that receive public disbursements, stating that companies that have received subsidies, grants, remunerated appointments and in any case economic advantages of any kind from public administrations and other similar bodies must - starting from financial year 2018 - give an indication of the amounts received in the Notes to the Separate Financial Statements and in the Notes to any Consolidated Financial Statements .
Non-observance of the obligation of publication entails the return of the amounts received to the disbursing bodies.

Italian Law Decree no. 135/2018, converted into Italian Law 12/2019, established that for state aid and the *de minimis* aid contained in the National State Aid Register, registration of the individual aid amounts in the system, must take account of the obligations of publication placed on beneficiary companies provided for in article 1, paragraph 125, second sentence, of Italian Law no. 124 of 4 August 2017, on condition that the existence of aid covered by the obligation of publication in the National State Aid Register is declared in the Notes to the Financial Statements.

On the basis of the above, we can note that, at the reporting date of the present financial statements, in the National State Aid Register, in the section Transparency: “Individual Aid Amounts”, there are no contributions received by the Bank for 2018. For more details, please see the following link:
https://www.rna.gov.it/sites/PortaleRNA/it_IT/trasparenza.

A.3 - DISCLOSURE ON TRANSFERS BETWEEN FINANCIAL ASSET PORTFOLIOS

The Bank did not make any transfer between portfolios of financial assets either in previous years or in the current year.

A.4 - FAIR VALUE DISCLOSURE

QUALITATIVE INFORMATION

Below is the disclosure regarding the measurement techniques and inputs used for measurements related to assets and liabilities measured at fair value in the balance sheet on a recurring and non-recurring basis (the latter are essentially assets held for sale under the terms of IFRS 5).

A.4.1a Fair value level 2: measurement techniques and input used

	Fair value 31/12/2018									
Items	*Financial assets held for trading*	*Financial assets obligatorily measured at fair value*	*Financial assets measured at fair value through other comprehensive income*	*Hedging derivatives*	*Financial liabilities held for trading*	*Financial liabilities designated at fair value*	*Hedging derivatives*	***Types***	***Measurement technique***	***Input used***
Debt securities	984,907	8,959	-	X	-	-	X	Bonds	Discounted Cash Flow	Rates curve, CDS Curve, Yield, Inflation Curve
								Structured Bonds	Discounted Cash Flow	Rates curve, CDS curve, Yield Inflation curve + parameters necessary to value the optional component
								Bonds	Market price	Market price
Equitiy securities	23	305	-					Equity investments	Net Asset Adjusted	Carrying Amount Assets/Liabilities
									Discount cash flow	Share prices, sectore beta, risk free rate
								Shares/Equity investments	Market price	Market prices, recent transactions, appraisals, operator reports
UCITS units	-	10,543						Provisions/PE	Market price	Market prices, recent transactions, appraisals, operator reports
Loans/Payables	-	-	-		597				Accrual	Interest rates on transactions
Financial	3,280,376				1,537,614		-	IR/Asset/Currency Swaps	Discounted Cash Flow	Rate curve, CDS curve, yield, inflation curve, exchange rates, rate correlation
								Equity swaps	Discounted Cash Flow	Share prices, rate curve, exchange rates
								Forex Singlename Plain	Option Pricing Model	Rate curve, exchange rates, Forex volatility
								Forex Singlename Exotic	Option Pricing Model	Rate curve, exchange rates, Forex volatility (surface)
								Equity Singlename Plain	Option Pricing Model	Rate curve, share prices, exchange rates, equity volatility
								Equity Singlename Exotic	Option Pricing Model	Rate curve, share prices, exchange rates, equity volatility (surface), model parameters
								Equity Multiname Plain	Option Pricing Model	Rate curve, share prices, exchange rates, equity volatility Quanto correlations, equity/equity correlations
								Equity Multiname Exotic	Option Pricing Model	Rate curve, share prices, exchange rates, equity volatility (surface), model parameters, quanto correlations, equity/equity correlations
								Plain Rate	Option Pricing Model	Rate curve, inflation curve, bond prices, exchange rates, rate volatility, rate correlations
								Foreign currency transactions	Market price	Market price, Swap Point
Credit derivatives	14,070				55,903			Default swaps	Discounted Cash Flow	CDS curve, rates curve
Total assets	**4,279,377**		**19,807**	**-**						
Total liabilities					**1,594,114**	**-**	**-**			

A.4.1b Fair value level 3: measurement techniques and inputs used

Items	*Fair value 31/12/2018*										
	Financial assets held for trading	*Financial assets obligatorily measured at fair value*	*Financial assets measured at fair value through other comprehensive income*	*Hedging derivatives*	*Financial liabilities held for trading*	*Financial liabilities designated at fair value*	*Hedging derivatives*	***Types***	***Measurement technique***	***Non-observable input***	***Range (weighted average)***
Debt securities	2,523	6,434		X	-	-	X	Bonds Junior Tranche NPL Securitisation	Discounted Cash Flow SPV Assets/Liabilities	Yield SPV Assets Value	1.3% - 5.5% 594 €/mln
Equity securities	-	1,124	506	X	X	X	X	Equity investments	Cost/Shareholders' Equity	Fair value asset	0-0.6 €/mln
Units in collective investment undertakings		2,588	X	X	X	X	X	Reserved Closed-End Real Estate Fund	Adjusted NAV	FV active components	2.6 €/mln
Loans		74,087						Loans Loans Loans Loans	Discounted cash flow Discounted cash flow Discounted cash flow Discounted cash flow	NPE Spread LGD PD PE Spread	4.16% - 4.34% 8.47% - 18.5% 0.46% - 45% 0.01% - 1.44%
Total assets	**2,523**	**10,146**	**506**	**-**	**X**	**X**	**X**				
Total liabilities	**X**	**X**	**X**	**X**	**-**	**-**	**-**				

A.4.2 Measurement processes and sensitivity

In the category “Debt securities” of “Financial assets obligatorily measured at fair value”, the position related to the junior tranche of the Siena NPL securitisation, of approximately € 6 million at nominal value, was measured on the basis of the value determined using estimates of the assets and liabilities of the issuer vehicle. It is estimated that the expected fluctuation of these aggregates may have an impact on the value of the Notes of approximately € -0.46 million.
As regards “Debt securities” allocated to the item “Financial assets held for trading” (€ 2.5 million) these are bonds measured with the Discounted Cash Flow method where the non-observable parameter is the overall return of the security. For each percentage point of return, the change in value is estimated at around € 0.28 million.
Equity securities measured at fair value amounted to approximately € 1.6 million, of which € 0.5 million through other comprehensive income and € 1.1 million obligatorily measured at fair value. These are, in both cases, securities measured at cost/equity and representing all equity investments at fair value for which it was not possible to define measurement according to a market-based model.
UCITS units, measured on the basis of an adjusted NAV, are related for € 2.3 million to the position in the Reserved Closed-End Real Estate Fund Rainbow acquired by way of “datio in solutum” in the context of a loan restructuring operation.
The category “Loans” includes receivables (€ 74.1 mln) measured obligatorily at fair value because they did not pass the so-called SPPI test that is the related contractual flows do not involve solely repayment of principal and payment of interest on the principal to be repaid, both in virtue of clauses originally provided for in the contract and following subsequent amendments. The fair value is measured using the Discounted Cash Flow approach applied differently according to whether these are performing or non-performing loans: in the first case the contractual flows are discounted with a Risk-Adjusted curve that incorporates the risks regarding the cost of credit, the cost of funding and the cost of capital; in the second case the recoverable value is discounted applying a spread in order to include the risks related to any sale on the market. The unobservable parameters are Probability of Default (PD), Loss Given Default (LGD) and the distinct spread for performing and non-performing assets. A change in these parameters, respectively of 5%-10%, -1%-1%, would determine an impact on the fair value of approximately € -4 million.

A.4.3 Fair value hierarchy

In determining the fair value of a financial instrument, IFRS 13 establishes a hierarchy of criteria based on the source, type and quality of the information used in the calculation. This classification has the objective of establishing a hierarchy in terms of the reliability of the fair value as a function of the degree of discretion applied by the companies, giving priority to the use of parameters than can be observed on the market which reflect the assumptions that market participants would use in pricing the said assets/liabilities. The objective of the hierarchy is also to increase the consistency and comparability of fair value measurements.
Below we illustrate the three different measurement levels envisaged by the amendment in question, the choice of which is not optional, as the levels indicated must be applied in hierarchical order:
Level 1 (effective market quotes)
In this level, the input consists of prices quoted (not modified) on active markets for instruments for identical assets and liabilities, which can be accessed as of the measurement date.
Level 2 (comparable approach)
This level includes instruments which, for the purposes of measurement, prices quoted on active markets for similar assets or liabilities are used, or prices calculated using measurement techniques where all the significant input is based on parameters that can be observed on the market, directly or indirectly. An input is observable when it reflects

the same assumptions used by market participants, based on market data provided by sources that are independent of the appraiser.

Level 3 (mark-to-model approach)

This level, instead, is used when measurement techniques where at least one significant input is based on non-observable parameters are made use of to calculate the prices.

To determine the methods of classifying assets in fair value Level 1, the Bank, in line with the policies of the Parent Company, used the presence of regulated markets for some categories financial instruments. In any case, classification in an active market requires the meeting of given requirements established ad hoc for each type of financial instrument. In particular equity securities and bonds (with the exception of plain vanilla government securities issued in hard currency and government securities from the G10 and Spain, for which it was held that the significance test was not necessary to carry out for the prices given the breadth and depth of the markets on which they are listed) are subject to periodic tests in order to verify the presence of various elements such as the bid-ask spread, the presence of numerous price contributors, the absence of listings that remain unchanged over time which demonstrate sufficient liquidity to make it possible to classify them in Level 1. Specifically, listed derivatives, exchange rates and Units in collective investment undertakings (limited to SICAVs and mutual investment funds) are considered as level 1.

All other financial instruments (OTC derivatives, Hedge Funds, Private Equity Funds, equity investment structures valued at fair value) and the same instruments that do not pass the liquidity and price significance tests are inserted in Level 2, as a rule.

If certain instruments have peculiarities that make it possible to measure them only with the assistance of measurement models that make use of unobservable market data input and/or entity specific assumptions, they are classified in Level 3.

The measurement method defined for an instrument is adopted and then kept over time, modified only following significant changes in market conditions or the subjective conditions of the issuer of the financial instrument. The Group's policy is that any movement of a given financial instrument between Levels 1 and 2 must be motivated by changed conditions, either improving or worsening, of the liquidity or price significance which determine whether or not the periodic tests are passed. Movement to and from Level 3, on the other hand, may depend on changes in the observability of the unknown parameters, as well as the adoption of different measurement techniques (models, replicas, etc.). It must be stressed that, in relation to item 20 c) "Financial assets obligatorily measured at fair value" and 30 "Financial assets measured at fair value through other comprehensive income", the amounts shown among Level 3 equity securities are referable to shareholding associations for cinema credit and to equity interests that are included in this fair value level when they are measured at adjusted cost, irrespective of measurements based on market parameters.

QUANTITATIVE INFORMATION

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 levels

Assets / liabilities measured at fair value	*31/12/2018*			*31/12/2017*		
	Level 1	*Level 2*	*Level 3*	*Level 1*	*Level 2*	*Level 3*
1. Financial assets measured at fair value through profit or loss						
a) financial assets held for trading	5,068,469	4,279,377	2,523	5,121,217	5,352,067	3,042
b) financial assets designated at fair value						
c) other financial assets obligatorily measured at fair value		19,807	84,232			
2. Financial assets measured at fair value through other comprehensive income	94,797		506	57,806	5,739	5,950
3. Hedging derivatives						
4. Property, plant and equipment						
5. Intangible assets						
Total	**5,163,266**	**4,299,184**	**87,261**	**5,179,023**	**5,357,806**	**8,992**
1. Financial liabilities held for trading	1,873,363	1,594,114		2,901,366	1,902,867	
2. Financial liabilities designated at fair value						
3. Hedging derivatives						
Total	**1,873,363**	**1,594,114**	**0**	**2,901,366**	**1,902,867**	**0**

The amounts at 31/12/2018 of financial assets measured at fair value of fair value level 1, include, for a total amount of approximately € 40 million, financial instruments that at the end of the previous year were classified as level 2. The change in level regarded bonds (also of the Group) and was due essentially to an improvement in the liquidity conditions of the said securities (measured in terms of bid-ask spread of the quoted price) which, according to the provisions of the group policy on the subject of measuring financial instruments, enabled this reclassification.
The values at 31/12/2018 of financial assets held for trading at fair value level 2, include, for a total amount of approximately € 137 million, financial instruments that at the end of the previous year were classified as level 1. The change in level regarded bonds (mainly of the Group) and was due essentially to a worsening in the liquidity conditions of the said securities (measured in terms of bid-ask spread of the quoted price) which, according to the provisions of the group policy on the subject of measuring financial instruments, determined this reclassification.
In keeping with the accounting standard IFRS 13, the Bank calculates the value adjustment of OTC derivatives to take account of the creditworthiness of the individual counterparties. This corrective, known as Credit Value Adjustment (CVA), is estimated for all positions in OTC derivatives with non-collateralised commercial and institutional counterparties and with counterparties with which Collateral Support Annex (CSA) contracts outside of market standards have been signed.
The method is based on calculating the operating expected loss associated with the rating of the counterparty and estimated on the duration of the position. The exposure includes the component of future credit variation represented by the add-ons.
In the calculation of the CVA "risk premium" probability measurements are used in order to incorporate the

expectations of the market coming from the CDS quotations, together with the historical information available internally.
The value of the CVA at 31/12/2018 totalled approximately € 17.7 million (€ 20 million at 31/12/2017), with an effect on the income statement of the year of approximately € 2.3 million, due essentially to a decrease in positions subject to correction and marginally also to an improvement of the composition of the portfolio in lending terms.
In a specular manner and on the same perimeter the Bank calculates the adjustment of the value of OTC derivatives to take account of its own creditworthiness, that is Debit Value Adjustment (DVA). At the end of the year the value of the DVA totalled approximately € 1.9 million (€ 1 million at 31/12/2017), with a positive effect on the income statement of € 1 million, essentially due to the worsening of the Group's creditworthiness.

A.4.5.2 Yearly changes in assets measured at fair value (level 3) on a recurring basis

			Financial assets designated at fair value through profit or loss						
		Total	*Financial assets held for trading*	*Financial assets designated at fair value*	*Financial assets obligatorily measured at fair value*	*Financial assets measured at fair value through other comprehensive income*	*Hedging derivatives*	*Property, plant and equipment*	*Intangible assets*
1.	**Opening balances (*)**	**131,169**	**3,042**		**128,127**	**738**			
2.	**Increases**	**34,497**	**371**		**34,126**	**38**			
2.1	Purchases	**6,309**	309		6,000				
2.2	Income allocated to:	**13,010**	62		12,948				
2.2.1	Income statement		62		12,948				
	- of which capital gains	***12,746***	*2*		*12,744*				
2.2.2	Shareholders' equity					38			
2.3	Transfers from other levels	**0**							
2.4	Other increases	**15,178**			15,178				
3.	**Decreases**	**78,911**	**890**		**78,021**	**270**			
3.1	Sales	**33,268**	4		33,264				
3.2	Redemptions	**14,997**	750		14,247				
3.3	Losses allocated to:				30,510				
3.3.1	Income statement	**30,646**	136		30,510				
	- of which capital losses	***30,184***	*136*		*30,048*				
3.3.2	Shareholders' equity					270			
3.4	Transfers to other levels								
3.5	Other decreases	**0**							
4.	**Closing balances**	**86,755**	**2,523**		**84,232**	**506**			

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

A.4.5.3 Annual changes in liabilities measured at fair value on a recurring basis (level 3)

No liability measured at fair value on a recurring basis of level 3 was present at the beginning and the end of financial year 2018.

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 levels

				Financial statements at 31/12/2018
Assets/Liabilities not measured at fair value or measured at fair value on a non-recurring basis	*Book value*	*Fair value Level 1*	*Fair value Level 2*	*Fair value Level 3*
1. Financial assets measured at amortised cost	15,403,344		9,698,199	5,937,162
2. Property, plant and equipment held for investment purposes	10,981			12,962
3. Non-current assets and disposal groups held for sale	52,746			
Total	**15,467,071**		**9,698,199**	**5,950,124**
1. Financial liabilities measured at amortised cost	20,957,255		20,711,211	
2. Liabilities associated with assets held for sale	25			25
Total	**20,957,280**		**20,711,211**	**25**

				Financial statements at 31/12/2017
Assets/Liabilities not measured at fair value or measured at fair value on a non-recurring basis	*Book value*	*Fair value Level 1*	*Fair value Level 2*	*Fair value Level 3*
1. Financial assets measured at amortised cost	16,814,467	0	10,620,619	6,489,930
2. Property, plant and equipment held for investment purposes	12,147			14,147
3. Non-current assets and disposal groups held for sale	979,942			979,942
Total	**17,806,556**		**10,620,619**	**7,484,019**
1. Financial liabilities measured at amortised cost	22,845,977	0	22,891,757	0
2. Liabilities associated with assets held for sale				
Total	**22,845,977**		**22,891,757**	

As regards impaired loans, classified in level 3 of the fair value hierarchy, it is assumed that the carrying amount represents a reasonable approximation of the fair value. This assumption derives from the circumstance that the calculation of fair value is affected mainly by recovery expectations, the result of a subjective valuation by the manager; the discounting back rate applied is the contractual one, because the low liquidity and competitiveness of the market of impaired loans does not allow the recognition of the observable market premiums.
In the same way we can note that the fair value of non-impaired loans, also mostly classified in level 3, is based on models that use mainly non-observable inputs (e.g.: internal risk parameters).
For these reasons and owing to the absence of a secondary market, the fair value recognised in the financial statements for the sole purposes of disclosure could also be significantly different from the prices of any sales.

A.5 Disclosure on the so-called “day one profit/loss”

The fair value of financial instruments, in situations of non-active market, is determined using an evaluation technique, as indicated in IAS 39, paragraphs AG74-AG79. The same standard also prescribes that the best proof of the fair value of an instrument is represented at the time of the initial recognition by the price of the transaction (i.e. the fair value of the consideration paid or received), unless the conditions per IAS 39, Paragraph AG 76 are fulfilled.
The potential consequence, accentuated in determined market situations and for particularly complex and illiquid products, is the manifestation of a difference between the fair value of the financial asset or liability at initial recognition and the amount that would have been determined at the same date using the chosen evaluation technique.
The difference, income/expense, must be recognised on first measurement after “initial recognition”: this “phenomenon” is known as “day one profit/loss”.
This concept does not include the profits deriving from the characteristic intermediation of the investment banks if arbitrage between different markets and products, in the presence of contained, book entry risk positions, leads to the formation of a trading margin aimed at remunerating the intermediary for the service rendered and for the assumption of financial and credit risks.
During the year, there were no cases to be reported and handled according to the above criteria.

Part B
Notes to the Balance Sheet

ASSETS

SECTION 1 - CASH AND CASH EQUIVALENTS - ITEM 10

1.1 Cash and cash equivalents: breakdown

	31/12/2018	*31/12/2017*
a. Cash in hand	-	-
b. Demand deposits with Central Banks		
Total	**0**	**0**

Cash on hand at 31/12/2018 amounted to € 6.96 (€ 330.87 at 31/12/2017)

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

2.1 Financial assets held for trading: breakdown by type

Items/Balances	*31/12/2018*			*31/12/2017*		
	Level 1	*Level 2*	*Level 3*	*Level 1*	*Level 2*	*Level 3*
A. Cash assets						
1. Debt securities	4,942,127	984,907	2,523	4,930,951	1,871,824	3,042
1.1 Structured securities	*3,571*	*125,127*		*14,668*	*110,601*	
1.2 Other debt securities	*4,938,556*	*859,780*	*2,523*	*4,916,283*	*1,761,223*	*3,042*
2. Equity securities	20,765	23		24,992	99	
3. UCITS Units	46,245			61,723		
4. Loans						
4.1 Repurchase agreements						
4.2 Other						
Total A	**5,009,137**	**984,930**	**2,523**	**5,017,666**	**1,871,923**	**3,042**
B. Derivative instruments						
1. Financial derivatives:	59,332	3,280,376		103,551	3,468,729	
1.1 for trading	*59,332*	*3,280,376*		*103,551*	*3,468,729*	
1.2 associated with the fair value option						
1.3 other						
2. Credit derivatives		14,070			11,415	
2.1 for trading		*14,070*			*11,415*	
2.2 associated with the fair value option						
2.3 other						
Total B	**59,332**	**3,294,446**		**103,551**	**3,480,144**	
Total (A+B)	**5,068,469**	**4,279,376**	**2,523**	**5,121,217**	**5,352,067**	**3,042**

Note:

"Debt securities - 1.2 Other debt securities" include securities associated with securitisation transactions, senior for € 215,014 thousand (€ 1,068,273 thousand at 31/12/2017), mezzanine for € 86,600 thousand (€ 187,922 thousand at 31/12/2017) and junior for € 72,120 thousand (€ 4,066 thousand at 31/12/2017). The reduction in the segments of senior and mezzanine notes is attributable essentially to the sale of securities of the Casaforte securitisation.

The sub-item "Financial derivatives - 1.1 held for trading" includes the fair value of OTC derivative contracts signed with corporate customers which present an evident low credit quality for a net amount of € 346 thousand (€ 412 thousand al 31/12/2017).

In application of IAS32 para. 42, level 1 derivatives quoted on regulated markets were offset for € 54,607 thousand (€ 82,449 at 31/12/2017) as well as OTC level 2 regulated derivatives settled through the Central Counterparty London Clearing House (LCH) for € 1,271,296 thousand (€ 1,028,498 at 31/12/2017) and level 2 credit derivatives settled at the Central Counterparty ICE Clear Europe (ICE) for € 526 thousand (no offsetting at 31/12/2017). The Bank has "indirect" access to the Clearing of OTC derivatives through the Clearing Members.

2.1.a Detail of debt instruments: structured instruments

Structured debt securities	*31/12/2018*	*31/12/2017*
- Index Linked	78,915	50,238
- Reverse convertible		
- Convertible	628	1,827
- Credit linked notes		
- Equity Linked	12,266	17,144
- Step-up, Step-down		
- Dual Currency		
- Drop Lock		
- Target redemption notes		
- Cap Floaters	24,348	1,600
- Reverse Floaters	2,443	9,167
- Corridors		
- Commodities		36,439
- Fund Linked	9,998	8,619
- Inflation		
- Others	100	236
Total	**128,698**	**125,270**

2.1.b Analysis of debt securities: subordinated assets

Items / Balances	*31/12/2018*	*31/12/2017*
1. Debt securities	**203,621**	**308,694**
1.1 structured securities	14,800	14,921
1.2 other debt securities	188,821	293,773
2. Loans		
Total	**203,621**	**308,694**

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

Items / Balances	*31/12/2018*	*31/12/2017*
A. CASH ASSETS		
1. **Debt securities**	**5,929,557**	**6,805,818**
a) Central Banks		
b) Public administrations	4,488,961	4,253,449
c) Banks	927,533	1,103,328
d) Other financial companies	459,400	1,338,184
of which insurance companies	*6,707*	*28,169*
e) Non-financial companies	53,663	110,857
2. **Equity securities**	**20,788**	**25,092**
a) Banks	140	10,942
b) Other financial companies	1,042	1,071
of which insurance companies	*336*	*958*
c) Non-financial companies	19,606	13,079
d) Other issuers		
3. **UCITS units**	**46,245**	**61,723**
4. **Loans**		
a) Central Banks		
b) Public administrations		
c) Banks		
d) Other financial companies		
of which insurance companies		
e) Non-financial companies		
f) Households		
Total A	**5,996,590**	**6,892,633**
B. DERIVATIVE INSTRUMENTS		
a) Central Counterparties	0	n.a.
b) Other	3,353,779	n.a.
Total B	**3,353,779**	**3,583,695**
Total (A+B)	**9,350,369**	**10,476,328**

2.2.a U.C.I.T.S. units: breakdown by main categories

Categories/Balances	*31/12/2018*	*31/12/2017*
a. Stock		
b. Bonds	422	50,578
c. Balanced		
d. Hedge Funds		
e. Private Equity		
f. Real estate		
g. Exchange Traded Funds (ETFs)	45,823	11,145
h. Other		
Total	**46,245**	**61,723**

2.2.b analysis of equity securities issued by parties classified under non-performing loan or probable default status

Nothing to report at 31.12.2018

2.3 Financial assets designated at fair value: breakdown by type

The Bank holds no financial instruments classified within this category.

2.4 Financial assets designated at fair value: breakdown by debtor/issuer

The Bank holds no financial instruments classified within this category.

2.5 Other financial assets obligatorily measured at fair value: breakdown by type

Items/Balances	*31/12/2018*			*31/12/2017*		
	Level 1	*Level 2*	*Level 3*	*Level 1*	*Level 2*	*Level 3*
1. Debt securities		8,959	6,434			
1.1 Structured securities		8,959	6,434			
1.2 Other debt securities						
2. Equity securities		305	1,124			
3. UCITS units		10,543	2,588			
4. Loans			74,087			
4.1 Repurchase agreements						
4.2 Other			*74,087*			
Total		**19,807**	**84,233**			

Note:
"Other debt securities" includes mezzanine notes (for € 8,959 thousand) and junior notes (€ 6,434 thousand) deriving from the "Siena NPL" securitisation.
The introduction of the accounting standard IFRS 9 made the data non-comparable relative to the previous year, therefore the column related to 2017 was not filled in.

2.6 Other financial assets obligatorily measured at fair value: breakdown by debtors/issuers

Items/Balances	*31/12/2018*	*31/12/2017*
A. CASH ASSETS		
1. **Equity securities**	**1,429**	**0**
of which: banks		
of which: other financial companies		
of which: non-financial companies	1,429	
2. **Debt securities**	**15,393**	**0**
a) Central Banks		
b) Public administrations		
c) Banks		
d) Other financial companies	15,393	
of which insurance companies		
e) Non-financial companies		
3. **UCITS Units**	**13,130**	
4. **Loans**	**74,087**	
a) Central Banks		
b) Public administrations		
c) Banks		
d) Other financial companies	6,329	
of which insurance companies		
e) Non-financial companies	64,892	
f) Households	2,866	
Total	**104,039**	**0**

Note:

The introduction of the accounting standard IFRS 9 made the data non-comparable relative to the previous year, therefore the column related to 2017 was not filled in.

2.6.a U.C.I.T.S. units: breakdown by main categories

Categories/Balances	*31/12/2018*	*31/12/2017*
a. Stock		
b. Bonds	6,731	
c. Balanced		
d. Hedge Funds		
e. Private Equity		
f. Real estate	6,399	
g. Other		
Total	**13,130**	**0**

Note:
The introduction of the accounting standard IFRS 9 made the data non-comparable relative to the previous year, therefore the column related to 2017 was not filled in.

2.6.B Equity securities issued by parties classified as non-performing or in probable default status

	Historical cost	*Accumulated capital losses*	*Carrying Amount*	*Capital losses ascertained in the year*
Non-performing	207	207		
Probable defaults	13,617	12,991	626	418
Total	**13,824**	**13,198**	**626**	**418**

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 type

Items/Balances	*31/12/2018*			*31/12/2017(*)*		
	Level 1	*Level 2*	*Level 3*	*Level 1*	*Level 2*	*Level 3*
1. Debt securities	72,710				5,433	2,588
1.1 Structured securities						
1.2 Other debt securities	72,710				*5,433*	*2,588*
2. Equity securities	22,087		506	57,806	306	3,362
3. Loans						
Total	**94,797**		**506**	**57,806**	**5,739**	**5,950**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Note:
in the comparative data "UCITS units" were included in "Other debt securities".

3.2 Financial assets measured at fair value through other comprehensive income: breakdown by debtors/issuers

Items/Balances	*31/12/2018*	*31/12/2017(*)*
A. CASH ASSETS		
1. **Debt securities**	**72,710**	**8,021**
a) Central Banks		
b) Public administrations		
c) Banks	60,214	
d) Other financial companies	1,045	8,021
of which insurance companies		
e) Non-financial companies	11,451	
2. **Equity securities**	**22,593**	**61,474**
a) Banks	22,125	57,806
b) Other financial companies		
of which insurance companies		
c) Non-financial companies	468	3,668
d) Other issuers		
3. **Loans**		
a) Central Banks		
b) Public administrations		
c) Banks		
d) Other financial companies		
of which insurance companies		
e) Non-financial companies		
f) Households		
Total A	**95,303**	**69,495**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Note:
in the comparative data "UCITS units" were included in "Other financial companies".

3.2.a Details of equity securities issued by parties classified as non-performing or in probable default status

	Historical cost	*Cumulative write-downs*	*Carrying Amount*	*Adjustments ascertained in the year*
Non-performing			0	
Probable defaults	42,077	(42,077)	0	
- Fenice Holding S.p.A.	*42,077*	*(42,077)*	*0*	
Total	**42,077**	**(42,077)**	**0**	

3.3 Financial assets measured at fair value through other comprehensive income: gross value and total value adjustments

	Gross value				*Total value adjustments*			
	First stage							
	Total	*of which instruments with low credit risk*	*Second stage*	*Third stage*	*First stage*	*Second stage*	*Third stage*	*Total partial write-offs*
Debt securities	71,310	60,216		3,850	20		2,430	
Loans								
Total 31/12/2018	**71,310**	**60,216**	**0**	**3,850**	**20**	**0**	**2,430**	**0**
Total 31/12/2017 (*)	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**0**
Of which purchased or originated impaired financial assets								

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

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

4.1 Financial assets measured at amortised cost: breakdown by type of receivables from banks

Type of transaction / Balances	*Carrying Amount*			*Fair Value*		
	First and second stage	*Third stage*	*of which: purchased or originated impaired*	*Level 1*	*Level 2*	*Level 3*
A. Due from Central Banks						
1. Fixed-term deposits						
2. Compulsory reserve						
3. Repurchase agreements						
4. Other						
B. Due from banks	**5,669,343**	**0**			**5,715,130**	
1. Loans	5,669,343				5,715,130	
1.1 Current accounts and demand deposits	1,734,448					
1.2 Fixed-term deposits	330,324					
1.3. Other loans:	3,604,571	0				
- Reverse repurchase agreements	*3,347,790*					
- Financial lease						
- Others	*256,781*					
2. Debt securities						
2.1 Structured securities						
2.2 Other debt securities						
Total	**5,669,343**	**0**				

4.2 Financial assets measured at amortised cost: breakdown by type of receivables from customers

Figures at 31/12/2018

Type of transaction / Balances	*Carrying Amount*			*Fair Value*		
	First and second stage	*Third stage*	*of which: purchased or originated impaired*	*Level 1*	*Level 2*	*Level 3*
1. Loans	**8,014,012**	**1,138,812**	**1,319**		**3,405,671**	**5,937,162**
1.1. Current accounts	2					
1.2. Reverse repurchase agreements	3,394,929					
1.3. Loans	4,177,887	1,137,517	1,319			
1.4. Credit cards, personal						
Loans and loans secured						
over wages and salaries	2,763					
1.5. Financial leasing						
1.6. Factoring						
1.7. Other loans	438,431	1,295				
of which:						
operating loans	*5,698*	*188*				
2. Debt securities	**581,177**	**0**	**0**		**577,399**	
2.1 Structured securities						
2.2. Other debt securities	581,177				577,399	
Total	**8,595,189**	**1,138,812**	**1,319**			

Notes:

item 2.2 "Other debt securities" includes the Senior notes deriving from the "Siena NPL" securitisation. Line "1.7 Other loans" shows the balances of operating loans in the scope of IFRS 15, for which the performance obligation has been fulfilled at the reporting date of these financial statements and which will be settled during the coming months. These loans were subject to impairment tests.

"Loans to customers" include, for insignificant amounts, loans disbursed with funds made available by the State and by other public bodies, with assumption of partial or total risk by the Bank. These funds are managed in the context of the agreements signed by the MPS Group with Cassa Depositi e Prestiti (hereinafter CDP), in direct cooperation with the ABI. In particular the Bank and the Group signed up to the agreements structured by the ABI and CDP in support of businesses. These operations are aimed at facilitating the disbursement of credit, depending on the cases, to small and medium-sized enterprises and/or to medium-sized enterprises substantially to ensure the financial coverage of expenses related to investments and/or linked to needs to increase the working capital and for the purchase or leasing of instrumental assets. Loans disbursed to SMEs by the Bank - with duration of more than 12 months - and the related contractual conditions - released from CDP funding - are the subject of autonomous negotiation between the parties involved. The loans to the final beneficiaries are obligatorily transferred in guarantee to CDP. The funding received from CDP is intermediated by the Parent Company.

Figures at 31/12/2017(*)

Type of transaction / Balances	*Carrying Amount*			*Fair Value*		
	First and second stage	*Third stage*	*of which: purchased or originated impaired*	*Level 1*	*Level 2*	*Level 3*
1. Loans	**9,188,104**	**1,572,173**	**0**		4,566,430	6,489,930
1.1. Current accounts	9					
1.2. Reverse repurchase agreements	4,400,099					
1.3. Loans	4,273,113	1,568,638				
1.4. Credit cards, personal Loans and loans secured over wages and salaries	2,981	17				
1.5. Financial leasing						
1.6. Factoring						
1.7. Other loans	511,902	3,518				
2. Debt securities	**0**	**0**	**0**			
2.1 Structured securities						
2.2. Other debt securities						
Total	**9,188,104**	**1,572,173**	**0**		**4,566,430**	**6,489,930**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

4.3 Financial leasing

There are no existing agreements.

4.4 Financial assets measured at amortised cost: breakdown by debtors/issuers of loans to customers

Type of transaction / Balances	*31/12/2018*			*31/12/2017(*)*		
	First and second stage	*Third stage*	*of which: purchased or originated impaired*	*First and second stage*	*Third stage*	*of which: purchase or originated impaired*
1. Debt securities:	**581,177**					
a) Public administrations						
b) Other financial companies	581,177					
of which:						
Insurance companies						
c) Non-financial companies						
2. Loans to:	**8,014,011**	**1,138,812**	**1,319**	**9,188,104**	**1,572,173**	
a) Public administrations	29,219			14,663	641	
b) Other financial companies	3,760,311	42,446	1,094	5,210,819	53,679	
of which:						
Insurance companies						
c) Non-financial companies	4,006,630	909,351	225	3,860,409	1,495,097	
d) Households	*217,851*	*187,015*		*102,213*	*22,756*	
Total	**8,595,188**	**1,138,812**	**1,319**	**9,188,104**	**1,572,173**	

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

4.5 Financial assets measured at amortised cost: gross value and total value adjustments

	Gross value				*Total value adjustments*			
	First stage							
	Total	*of which instruments with low credit risk*	*Second stage*	*Third stage*	*First stage*	*Second stage*	*Third stage*	*Total partial write-offs*
Debt securities	**581,434**	**581,434**		**34**	**256**		**34**	
Loans	**11,608,603**		**2,179,506**	**2,159,664**	**7,710**	**97,045**	**1,020,852**	**102,725**
Total 31/12/2018	**12,190,037**	**581,434**	**2,179,506**	**2,159,698**	**7,966**	**97,045**	**1,020,886**	**102,725**
of which purchased or originated impaired financial assets				*3,197*			*1,878*	
Total 31/12/2017 (*)				3,106,625			(1,534,452)	

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

SECTION 5 - HEDGING DERIVATIVES - ITEM 50

There were no transactions for this accounting item.

SECTION 6 - VALUE ADJUSTMENTS TO FINANCIAL ASSETS SUBJECT TO MACRO-HEDGING - ITEM 60

There were no transactions for this accounting item.

SECTION 7 - EQUITY INVESTMENTS - ITEM 70

7.1 Equity investments: information on investment relationships

Name	*Registered Offices*	*Operating office*	*stake of equity investment %*	*Available votes %*	*Carrying Amount*	*Fair value*
A. Full subsidiaries						
B. Subsidiaries under joint control						
C. Companies subject to significant influence				779		
1. Immobiliare Centro Milano S.p.A.	Milan	Milan	33.333	33.333	0	
2. Terme di Chianciano S.p.A.	Chianciano T.	Chianciano T.	26.807	26.807	0	
3. Interporto Toscano A. Vespucci S.p.A.	Collesalvetti	Collesalvetti	19.001	19.001	0	
4. Sviluppo Imprese Centro Italia S.p.A.	Florence	Florence	15.000	15.000	779	
Total (A+B+C)					**779**	

The fair value of equity investments is not indicated because the securities in the portfolio are not listed.

7.2 Significant equity investments: book value, fair value and dividends received

Name	*Carrying Amount*	*Fair value*	*Dividends received*
A. Full subsidiaries			
B. Subsidiaries under joint control			
C. Companies subject to significant influence	**779**		
1. Immobiliare Centro Milano S.p.A.	0		-
2. Terme di Chianciano S.p.A.	0		-
3. Interporto Toscano A. Vespucci S.p.A.	0		-
4. Sviluppo Imprese Centro Italia S.p.A.	779		-
Total (A+B+C)	**779**		

7.2.a Details of equity securities issued by parties classified as non-performing or in probable default status

	Historical cost	*Cumulative write-downs*	*Carrying amount*	*Adjustments ascertained in the year*
Probable defaults				
- Immobiliare Centro Milano S.p.A.	40	(40)		
- Terme di Chianciano S.p.A.	2,010	(2,010)		
- Interporto Toscano A. Vespucci S.p.A.	8,369	(8,369)		
Total	**10,419**	**(10,419)**	**0**	**0**

Note:
The total book value of these securities is € 2.26.

7.3 Significant equity investments: accounting information

Name	*Cash and cash equivalents*	*Financial assets*	*Non-financial assets*	*Financial liabilities*	*Non-financial liabilities*	*Total revenue*	*Net interest income*	*Adjustments and value writ-ebacks on property, plant and equipment and intangible assets*	*Profit (Loss) from current operations before tax*	*Profit (Loss) from current operations net of taxes*	*Gain (Loss) on discontinued operations, net of taxation*	*Profit (loss) for the period (1)*	*Other income components net of taxes (2)*	*Comprehensive income (3)=(1)+ (2)*
A. Full subsidiaries														
B. Subsidiaries under joint control														
C. Companies subject to significant influence														
1. Sviluppo Imprese Centro Italia S.p.A.		4,149	4,721		456	983			(1,134)	(1,141)	-	(1,141)	-	(1,141)

Note:

The figures refer to the financial statements at 31/12/2017, the latest approved.

Sviluppo Imprese Centro Italia S.G.R. S.p.A. was classified among companies subject to significant influence, although in the presence of an interest of less than 20% of the share capital because the Bank has the power to take part in determining the financial and management policies by indicating a name for the company's Board of Directors.

7.4 Non-significant equity investments: accounting information

Name	*Carrying amount of the equity investments*	*Total assets*	*Total liabilities*	*Total revenues*	*Profit (Loss) from current operations net to taxes*	*Gain (Loss) on discontinued operations, net of taxation*	*Profit (Loss) for the period (1)*	*Other income components net of taxes (2)*	*Comprehensive income (3) = (1) + (2)*
A. Full subsidiaries									
B. Subsidiaries under joint control									
C. Companies subject to significant influence									
1. Immobiliare Centro Milano S.p.A.		203	461	-	(388)	-	(388)	-	(388)
2. Terme di Chianciano S.p.A.		12,598	8,104	6,088	(1,032)	-	(1,032)	-	(1,032)
3. Interporto Toscano A. Vespucci S.p.A.		133,451	114,634	6,091	204		204		204

Note:
The figures refer to the financial statements at 31.12. 2017, the latest approved.

7.5 Equity investments: annual changes

		31/12/2018	*31/12/2017*
A.	**Opening balances**	**779**	**1,680**
B.	**Increases**		
	B1. Purchases		
	B2. Write-backs		
	B3. Revaluations		
	B4. Other changes		
C.	**Decreases**		**901**
	C1. Sales		
	C2. Value adjustments		901
	C3. Other changes		
D.	**Closing balances**	**779**	**779**
E.	**Total revaluations**		
F.	**Total adjustments**	10,419	10,419

7.6 Commitments relating to equity interests in subsidiaries under joint control

At the reporting date, there were no equity investments in joint ventures.

7.7 Commitments relating to equity investments in companies under significant influence

At the reporting date, there were no commitments relating to equity investments in companies under significant influence.

7.8 Significant restrictions

There are no significant restrictions to report.

7.9 Other information

Nothing to report.

SECTION 8 - PROPERTY, PLANT AND EQUIPMENT - ITEM 80

8.1 Property, plant and equipment for use in business: breakdown of assets measured at cost

Assets / Balances	*31/12/2018*	*31/12/2017*
1. Company owned	**178**	**181**
a) land	6	6
b) buildings	9	9
c) furniture	7	10
d) electronic systems		
e) other	156	156
2. Assets acquired under financial leases		
a) land		
b) buildings		
c) furniture		
d) electronic systems		
e) other		
Total	**178**	**181**
of which: obtained through enforcement of guarantees received		

8.2 Property, plant and equipment held for investment purposes: breakdown of assets measured at cost

		Total 31/12/2018		
Assets / Balances	*Carrying Amount*	*Fair value*		
		Level 1	*Level 2*	*Level 3*
1. Company owned	**10,982**			**12,963**
a) land	8,905			8,169
b) buildings	2,077			4,794
2. Assets acquired under financial leases				
a) land				
b) buildings				
Total	**10,982**			**12,963**
of which: obtained through enforcement of guarantees received				

		Total 31/12/2017		
Assets / Balances	*Carrying Amount*	*Fair value*		
		Level 1	*Level 2*	*Level 3*
1. Company owned	**12,149**			**14,147**
a) land	9,684			8,817
b) buildings	2,465			5,330
2. Assets acquired under financial leases				
a) land				
b) buildings				
Total	**12,149**			**14,147**
of which: obtained through enforcement of guarantees received				

8.3 Property, plant and equipment used for business: breakdown of revalued assets

There were no revalued property, plant or equipment items used for business.

8.4 Property, plant and equipment held for investment purposes: breakdown of assets carried at fair value

There are no property, plant and equipment items held for investment purposes carried at fair value.

8.5 Inventories of property, plant and equipment governed by IAS 2: breakdown

Assets / Balances	*31/12/2018*
1. Inventories of assets obtained through enforcement of guarantees received	**750**
a) land	
b) buildings	750
c) furniture	
d) electronic systems	
e) other	
2. Other inventories of property, plant and equipment	
Total	**750**
of which: measured at fair value net of costs to sell	

8.6 Property, plant and equipment used for business: annual changes

		Land	*Buildings*	*Furniture*	*Electronic equipment*	*Other*	*Total*
A.	**Opening balances - gross**	**6**	**34**	**1,236**	**446**	**189**	**1,911**
A.1	Total value reductions - net		24	1,226	446	33	1,729
A.2	**Net opening balances**	**6**	**10**	**10**	**0**	**156**	**182**
B.	**Increases:**			**3**			**3**
B.1.	Purchases			3			3
B.2	Capitalised improvement costs						
B.3	Write-backs						
B.4	Positive fair value changes						
	booked to:						
	a) shareholders' equity						
	b) income statement						
B.5	Exchange gains						
B.6	Transfer from investment property						
B.7	Other changes						
C.	**Decreases:**		**1**	**6**			**7**
C.1	Sales						
C.2	Depreciation		1	6			7
C.3	Write-downs for impairment						
	booked to:						
	a) shareholders' equity						
	b) income statement						
C.4	Negative fair value changes booked to:						
	a) shareholders' equity						
	b) income statement						
C.5	Exchange losses						
C.6	Transfers to:						
	a) property, plant and equipment held for investment purposes						
	b) discontinued operations						
C.7	Other changes						
D.	**Net closing balances**	**6**	**9**	**7**	**0**	**156**	**178**
D.1	Total net value reductions		25	1,232	446	33	1,736
D.2	**Gross closing balances**	**6**	**34**	**1,239**	**446**	**189**	**1,914**
E.	Measured at cost	7	29	7		156	199

Note:

the item "other" regards furnishings not subject to amortisation (in particular works of art).

8.7 Property, plant and equipment held for investment purposes: annual changes

		Land	*Buildings*	*Total*
A.	**Opening balances**	**9,684**	**2,463**	**12,147**
B.	**Increases:**			
B.1.	Purchases			0
B.2	Capitalised improvement costs			
B.4	Positive fair value changes			
B.3	Write-backs			
B.5	Exchange gains			
B.6	Transfers from properties used for business			
B.7	Other changes			
C.	**Decreases:**	**780**	**386**	***1,166***
C.1	Sales			
C.2	Depreciation		166	166
C.3	Negative fair value changes			
C.4	Write-downs for impairment	280		280
C.5	Exchange losses			
C.6	Transfers to other asset portfolios:	500	220	720
	a) properties used for business			
	b) non-current assets held for sale	*500*	*220*	*720*
C.7	Other changes			
D.	**Closing balances**	**8,904**	**2,077**	**10,981**
E.	Fair value measurement	**8,169**	**4,793**	**12,962**

8.8 Inventories of property, plant and equipment governed by IAS 2: annual changes

	Inventories of property, plant and equipment obtained through enforcement of guarantees received						
	Land	*Buildings*	*Furniture*	*Electronic equipment*	*Other*	*Other inventories of property, plant and equipment*	*Total*
A. Opening balances							
B. Increases		**750**					**750**
B.1. Purchases		750					750
B.2 Write-backs							
B.3 Exchange gains							
B.4 Other changes							
C. Decreases							
C.1 Sales							
C.2 Value adjustments due to impairment							
C.3 Exchange gains							
C.4 Other changes							
D. Closing balances		**750**					**750**

8.9 Commitments for the purchase of property, plant and equipment (IAS 16/74.c)

As of the reporting date, there were no commitments undertaken to purchase property, plant and equipment.

8.10 Property, plant and equipment: useful life

Main categories of Property, plant and equipment	*years*
Land and works of art	Indefinite
Buildings	33
Furniture	8
Electronic and ordinary office machines	5
Electronic data processing equipment	4
Vehicles	4
Telephones	5

Statement of revaluations made (Article 10 of Italian Law No. 72/83)

Properties	*L.576/75*	*L.72/83*	*L. 408/90*	*L. 413/91*	*L. 342/00*	*L. 266/06*
Florence - via Scialoia, 47			180		336	237
Florence - piazza D'Azeglio, 22	230	840	2,745	1,175	336	1,857
Florence - piazza D'Azeglio, 26		319	173	4,638	1,109	3,670
Florence - via della Mattonaia						97
Florence - piazza Stazione (car park)					14	3
Total	**230**	**1,159**	**3,098**	**5,813**	**1,795**	**5,864**

SECTION 9 - INTANGIBLE ASSETS - ITEM 90

There were no transactions for this accounting item.

SECTION 10 - TAX ASSETS AND LIABILITIES - ASSET ITEM 100 AND LIABILITY ITEM 60

Current taxes

Current taxes include the estimated payable for current liabilities or liabilities referring to transactions from previous years. Current tax assets and liabilities are shown in their net balance in the respective balance sheet items following the offset carried out at the level of the said tax.

Current tax assets amounted to € 331,334 thousand and include for € 313,184 thousand the tax credit under Italian Law 214/11 and for € 20,153 thousand the IRAP credit offset with payables of the same nature for € 2,003 thousand. As a result of the adhesion to the national tax consolidation system under the terms of Art. 117 ff. of the Consolidated Act on Income Tax as a consolidated company, the Bank determines, in the presence of a taxable profit, the tax charges for which it is liable and the corresponding IRES taxable income is transferred to the Parent Company MPS, which, as the consolidating company, after consolidating the taxable amounts coming under the scope of consolidation, will pay any tax due to the tax authorities. In financial year 2018, IRES taxable income and surcharge was entirely offset with the AEG subsidy (of the year and in part of previous years) and with earlier losses (with reference to the IRES surcharge); consequently, current taxes were not recognised. In addition, the results of the probability test determined a revaluation of € 14,408 thousand of the tax credit to the Consolidator, which is € 180,622 thousand.

On the IRAP side, as a result of the deduction of the write-downs of loans accounted for and not deducted in the period 2008-2012 following the sale of loans entitled “Valentine”, which occurred in financial year 2018, no provisions accruing to the year were set aside. The amount shown in “current taxes” (€ 5,848 thousand) represents the closure in the income statement of IRAP taxation recognised on first application of IFRS 9, with a counter-entry in shareholder’s equity, on value adjustments on receivables.

With respect to IRES, the debit and credit positions are posted respectively among “Other assets” and “Other liabilities”.

Deferred tax assets and liabilities

Deferred taxation is measured with the “balance sheet liability method” specified in IAS 12 in accordance with the specifications prescribed by the Bank of Italy. This method takes account of the tax effect connected with temporary differences between the carrying value of assets and liabilities and their fiscal value, which lead to taxable or deductible amounts in future periods. For these purposes, “taxable temporary differences” are those which in future periods will determine taxable amounts and “deductible temporary differences” are those which in future periods will determine deductible amounts.

Deferred tax assets and liabilities are calculated applying the tax rates established by the provisions of current laws to the taxable temporary differences in relation to which there is the probability that the taxes will actually have to be paid and to the deductible temporary differences for which there exists reasonable certainty of recovery.

During the year deferred tax assets were recognised for IRES and IRAP respectively for € 37,582 thousand and € 7,612 thousand in relation to the rules introduced by the 2019 Italian Budget Law which set the deduction at 10 years (starting from 2018) of value adjustments on loans that emerged on first application of IFRS 9 (art. 1, paragraphs 1067-1069, Italian Law no. 145/2018). This positive effect on income statement item 270 was in part neutralised, as stated above, by reversal to the same income statement item of the credit for IRAP recognised on FTA with reference to the aforementioned write-down of receivables.

In addition, the probability test made necessary a write-down of deferred tax assets related to the IRES surcharge and to other temporary differences, respectively, of € 9,094 and 145 thousand.

Prepaid and deferred taxes are shown as the net balance of the respective balance sheet item, subsequent to offsetting at the same tax level and for each financial year, taking into account when payment is expected to fall due. Consequently, at 31 December 2018 deferred tax liabilities were completely offset with deferred tax assets.

10.1 Deferred tax assets: breakdown

Deferred tax assets, gross of offsetting against deferred tax liabilities, essentially derive from costs deductible in different periods from the one in which they were recorded in the financial statements and they refer to IRES for € 159,430 thousand and to IRAP for € 19,489 thousand.
The recognition of prepaid tax assets was made after verifying the existence of future taxable income (through the so-called Probability test). The write-downs (or write-backs of previous write-downs) made on the basis of the probability test are accounted for overall as a counter-entry of the income statement item taxes; in the tables of the present section, however, the non-recognisable portion of DTAs is attributed with a proportional criterion also to the DTAs originally recognised as a counter-item of shareholders' equity. For more information on the subject please see paragraph 10.7 "Other information" below.
Specifically:

- the sub-item "loans" represents the total amount of the value adjustments on loans exceeding the portion allowed for deduction for IRES and IRAP purposes and to be carried forward to future financial years, as well as provisions for documentary credit. In particular, this sub-item include, for an amount of € 45,194 thousand, the deferred tax assets which were recognisable in relation to nine tenths of the value adjustments to receivables from customers accounted for on first adoption of IFRS 9, the deduction of which was provided for in ten constant instalments (from 2018 to 2027) in paragraphs 1067-1069 of Italian Law no. 145 of 30/12/2018 (2019 Budget Law).
- the item "AEG tax credit" represents the residual amount of the subsidy related to financial years 2016 and 2017, which will be recovered in future years;
- "tax losses" for € 31,184 thousand, net of write-downs carried out due to the probability test and to the use of the same in order to reduce to zero the taxable income of financial year 2018, refer to financial years 2016 and 2017 and will be recovered if there is taxable income in future years;
- the item "other" refers to allocations for legal disputes and liabilities connected to external events.

Items / Balances	*31/12/2018* *Deffered tax assets counter-entry IS IRES*	*Deffered tax assets counter-entry SE IRES*	*Deffered tax assets counter-entry IS IRAP*	*Deffered tax assets counter-entry SE IRAP*	*Total*	*31/12/2017* *Total*
Receivables (including securitisations)	116,741		19,422		**136,163**	**135,069**
- of which It. Law 214/2011	*78,605*		*11,810*		***90,415***	***134,226***
Other financial instruments	4,403		1		**4,404**	
Goodwill						
Deferred charges						
Property, plant and equipment	326		66		**392**	**304**
- of which It. Law 214/2011						
Entertaining expenses						
Personnel-related costs	84	336			**420**	**463**
AEG tax credit	8,669				**8,669**	**19,464**
Tax losses	21,588				**21,588**	**31,184**
- of which It. Law 214/2011						
Reserves for valuation of financial instruments		728			**728**	
Other	6,555				**6,555**	**6,374**
Deferred tax assets - gross	**158,366**	**1,064**	**19,489**		**178,919**	**192,858**
Offsetting against deferred tax liabilities	**(55)**		**(30)**		**(85)**	**(174)**
Deferred tax assets - net	**158,311**	**1,064**	**19,459**	**0**	**178,834**	**192,684**

10.2 Deferred tax liabilities: breakdown

Deferred tax liabilities refer to IRES for € 55 thousand and to IRAP for € 30 thousand and are entirely recognised as a counter-entry of the income statement (in 2017, € 72 thousand recognised as a counter-entry of the income statement and € 102 thousand recognised as a counter-entry of shareholders' equity).
The main taxable temporary differences which caused deferred taxes to be recognised are related to the sub-item "Financial instruments", in particular to valuation gains recorded on equity investments in collective investment undertakings and equity investments and to the sub-item "Property, plant and equipment and intangible assets" as a result of a higher civil-law value with respect to the fiscal value of the same.

Items / Balances		*31/12/2018*				*31/12/2017*
	Deffered tax assets counter-entry IS IRES	*Deffered tax assets counter-entry SE IRES*	*Deffered tax assets counter-entry IS IRAP*	*Deffered tax assets counter-entry SE IRAP*	*Total*	*Total*
Capital gains to be collected						
Goodwill						
Property, plant and equipment and intangible assets	55		11		**66**	**72**
Financial instruments			19		**19**	
Personnel-related costs						
Reserves for valuation of financial instruments					**0**	**102**
Other						
Deferred tax liabilities - gross	**55**	**0**	**30**	**0**	**85**	**174**
Offsetting against deferred tax assets	**(55)**		**(30)**		**(85)**	**(174)**
Net deferred tax liabilities	**0**	**0**	**0**	**0**	**0**	**0**

10.3 Change in deferred tax assets (as counter-entry to the income statement)

The table shows all deferred tax assets to be absorbed in subsequent years as counter-entries to the income statement. Among the main "deferred tax assets recognised in the period" we can note those generated by the deferment of deduction in 10 years of the value adjustments that emerged on first application of IFRS 9 (€ 45,194 thousand), those deriving from non-deduction of negative components from measurement of "other financial assets obligatorily measured at fair value" recognised under income statement item 110/b, (€ 4,409 thousand) and from taxed provisions set aside in period of € 1,672 thousand (€ 3,054 thousand). "Deferred tax assets cancelled during the year", under item "reversals" refer mainly to portions used in the period referred to AEG 2016 and 2017 portions (for the part necessary to reduce to zero the IRES taxable base and IRES surcharge, € 4,744 thousand), to provisions for risks and charges and to endorsement loans (respectively € 933 thousand and € 1,228 thousand); the item "write-downs of non-recoverable items" represents the results of the aforementioned probability test described above, while "other decreases" include the use of deferred tax assets for transformation into tax credit under the terms of Italian Law 214/2011 (€ 43,811 thousand), besides the transformation of ACE deferred tax assets in IRAP tax credit of € 5,721 thousand (cf. table 13.3.1).

		31/12/2018	*31/12/2017*
1.	**Opening balance (*)**	**192,952**	**291,321**
2.	**Increases**	**51,599**	**18,067**
2.1	Prepaid taxes recorded in the year	51,599	17,987
	a) relating to prior years		
	b) due to changes in accounting policies	*0*	
	c) write-backs		*7,813*
	d) other	*51,599*	*10,174*
2.2	New taxes or increase in tax rates		
2.3	Other increases		80
3.	**Decreases**	**66,696**	**116,900**
3.1	Prepaid taxes cancelled during the year	17,163	5,305
	a) reversals	*7,924*	*5,305*
	b) written down as now considered unrecoverable	*9,239*	
	c) change in accounting policies		
	d) other		
3.2	Reductions in tax rates		
3.3	Other decreases	49,533	111,595
	a) transformation into tax credit as per law No. 214/2011	*43,812*	*111,595*
	b) other	*5,721*	
4.	**Closing balance**	**177,855**	**192,488**

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

"Changes in the year presented in the present table - balancing between closing and opening balances - reconciles with what is shown in the income statement table 19.1 "Income taxes for the year on profit from continuing operations: breakdown" in the line 'change in deferred tax assets' considering that:

- the amount of € 43.8 mln, relates to the transformation of deferred tax assets into tax credit under the terms of Italian Law no. 214/2011;
- the amount of € 5.7 mln, related to the conversion of the AEG surplus into IRAP credit, although it is shown in the present table as a decrease did not have as a counter-item the income statement item taxes but "current tax assets."

10.3bis Change in deferred tax assets pursuant to Italian Law 214/2011 (as a counter-entry to the income statement)

	IRES	*IRAP*	*Total 31/12/2018*	*Total 31/12/2017*
1. Opening balance (*)	**116,694**	**17,533**	**134,227**	**245,821**
2. Increases				
3. Decreases	**38,089**	**5,723**	**43,812**	**111,595**
3.1 Reversals				
3.2 Transformation into tax credit	38,089	5,723	**43,812**	**111,595**
a) deriving from losses of the period	*38,089*	*5,723*	*43,812*	*99,304*
b) deriving from tax losses				*12,291*
3.3 Other decreases				
4. Closing balance	**78,605**	**11,810**	**90,415**	**134,226**

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

Note:
These are deferred tax assets potentially transformable into tax credits, on the occurrence of a loss in the period and/or a tax loss on the basis of the provisions of Italian Law 214/2011.

10.4 Change in deferred taxes (as counter-entry to the income statement)

The table shows all deferred tax liabilities to be absorbed in subsequent years as counter-entries to the income statement.

	31/12/2018	*31/12/2017*
1. Opening balance	**72**	**110**
2. Increases	**20**	
2.1 Deferred tax liabilities recorded in the year	20	
a) relating to prior years		
b) due to changes in accounting policies	*20*	
c) other		
2.2 New taxes or increase in tax rates		
2.3 Other increases		
3. Decreases	**7**	**38**
3.1 Deferred taxes cancelled during the year	7	38
a) reversals	*7*	*38*
b) due to changes in accounting policies		
c) other		
3.2 Reductions in tax rates		
3.3 Other decreases		
4. Closing balance	**85**	**72**

10.5 Change in deferred taxes (as counter-entry to shareholders' equity)

Deferred tax assets as a counter-entry in shareholders' equity refer to the measurement of debt securities in OCI and to the discounting reserve for the defined-benefit pension fund.

	31/12/2018	*31/12/2017*
1. Opening balance	**369**	**220**
2. Increases	**864**	**17,900**
2.1 Deferred tax liabilities recorded in the year	864	17,696
a) relating to prior years		
b) due to changes in accounting policies		
c) other	*864*	*17,696*
2.2 New taxes or increase in tax rates		
2.3 Other increases		204
3. Decreases	**169**	**17,751**
3.1 Deferred taxes cancelled during the year	169	17,751
a) reversals	*168*	*17,751*
b) written down as now considered unrecoverable	*1*	
c) due to changes in accounting standards		
d) other		
3.2 Reductions in tax rates		
3.3 Other decreases		
4. Closing balance	**1,064**	**369**

10.6 Change in deferred taxes (as counter-entry to shareholders' equity)

	31/12/2018	31/12/2017
1. Opening balance	**102**	**36**
2. Increases	**163**	**171**
2.1 Deferred tax liabilities recorded in the year	163	171
a) relating to prior years		
b) due to changes in accounting policies		
c) other	*163*	*171*
2.2 New taxes or increase in tax rates		
2.3 Other increases		
3. Decreases	**265**	**105**
3.1 Deferred taxes cancelled during the year	265	105
a) reversals	*163*	*105*
b) due to changes in accounting policies		
c) other	*102*	
3.2 Reductions in tax rates		
3.3 Other decreases		
4. Closing balance	**0**	**102**

10.7 Other information

Probability test

The recognition of deferred tax assets was made after verifying the existence of sufficient future taxable income to reabsorb the same (the so-called Probability test).
This test took into account the different rules provided for in the Italian tax legislation that have an impact on the measurement in question, in particular:
- art. 2, paragraphs 55-59, of Italian Law Decree 29/12/2010 n. 225 (converted, with amendments, by Law 10 of 26/2/2011) which requires financial intermediaries, in the case of a statutory loss and/or tax loss, to transform DTAs (IRES and IREP) to tax credits, relative to goodwill, other intangible fixed assets and write-downs on loans;
- art. 84 paragraph 1 of the Consolidated Income Tax Law, which permits IRES tax losses to be carried forward with no time limits;
- art. 1, paragraph 4, of Italian Law Decree no. 201 of 06/12/2011 (converted, with amendments, into Italian Law no. 214 of 22/12/2011) which states that the unused AEG surplus can be carried forward with no time limits, or, alternatively, converted into tax credit to be used to offset the IRAP payable in 5 annual instalments;
- paragraphs from 61 to 66 of the Stability Law for 2016 (Italian Law No. 208 of 28 December 2015) which cut the IRES rate from 27.5% to 24% and introduced at the same time an IRES surcharge, of 3.5%, for lending and financial institutions.

We can note that the assessments of the probability test carried out in the 2018 financial statements were state impacted in very significantly by a number of measures introduced by art. 1 of Italian Law no. 145 of 30/12/2018 (2019 Budget Law). In particular, we refer to:
1. abrogation of the ACE (paragraph 1080);
2. the deduction in 10 constant instalments from 2018 to 2027 of the value adjustments on receivables from customers accounted for on first adoption of IFRS 9 (paragraphs 1067-1069).

The abrogation of the AEG, with effect from 2019, determined an increase in future taxable income with respect to the scenario previously in force enabling in this way greater absorption of earlier tax losses. From the accounting point of view, this translated essentially into a partial write-back of DTAs on tax losses not recognised in previous years.
The payment in instalments of the deduction of value adjustments on receivables from customers that emerged on FTA of IFRS 9 had an opposite effect with respect to the abrogation of the AEG. This was because nine tenths of this negative income component, which in the scenario previously in force (assumed for the purposes of the assessments of the probability test in the financial statements at 31.12.2017 and in the three subsequent quarterly reports) contributed to the formation of a tax loss for 2018 with non-recognisable DTAs, determined a reduction in positive future taxable incomes that enabled the absorption of earlier tax losses. From the accounting point of view, this entailed a write-down of DTAs for tax losses recognised in previous years and of DTAs recognised in 2018 on nine tenths of the negative component that emerged on FTA.

For completeness, the Budget Law for 2019 introduced measures that affected the Bank, however with marginal effects for the purpose of the assessments of the probability test. In particular, reference is made to deferment of the deduction of write-downs and losses on loans envisaged for 2018, according to the payment in instalments provided for in Italian Law Decree 83/2015 (10% of total non-deducted write-downs at 31/12/2015), with deferment to 2026 (paragraphs 1056 and 1065).

Besides by the aforementioned legislative amendments, the assessments of the probability test at 31 December 2018 were negatively affected also the revision downwards of the income prospects of the MPS Group, with respect to the

scenario included in the Restructuring Plan approved by the European Commission on 4 July 2017 which was used in the corresponding assessments for the financial statements al 31 December 2017 and the subsequent quarterly reports.
From the methodological point of view, the Probability test was thus carried out following the steps specified below.
The DTAs related to write-downs on loans (so-called "qualified" DTAs) were excluded from the total amount of the DTAs for which the existence of future sufficient taxable income must be verified.
This was because the aforementioned Art. 2, paragraphs 55-59, of Italian Law Decree 225/2010 made certain the recovery of this tale type of DTA, for both IRES and IRAP purposes, irrespective of the presence of future taxable income.
In fact, the law states that, if the taxable income of the financial year in which the rebate of the qualified DTAs is not sufficient for their re-absorption, the consequent tax loss will be transformable into tax credit which can alternatively be: i) used to offset, with no time limits, the various levies ordinarily payable by the Bank, or ii) requested as a rebate or iii) transferred to third parties. In addition, qualified DTAs can be transformed into tax credit, in advance with respect to the natural maturity, in the event of a civil-law loss for the period, voluntary liquidation or being made subject to bankruptcy proceedings.
In other words, for qualified DTAs the probability test must be understood as automatically passed; this is confirmed also by the joint Bank of Italy, CONSOB and ISVAP document No. 5 of 15/05/2012.
For DTAs other than qualified ones the year in which they are expected to be rebated was identified (or estimated when not certain).
The taxable incomes of future years were therefore estimated, on the basis of the forecast evolution of the Bank's income statements most recently approved by the Board of Directors. The taxable incomes were forecast for the purposes of the probability test applying a discount factor to the prospective economic results (so-called Risk-adjusted profits approach); this factor, used in a composite way, discounts future incomes to a growing extent to reflect their uncertainty. The discount factor is calculated by taking into account observable market parameters. We can note that this methodological approach was introduced during 2016; for more information on the reasons that led to this methodological evolution of the probability test please see the Notes to the Financial Statements of the Bank for financial year 2016 (Part B - Assets, para. 13.7).
The taxable incomes were forecast:
- at domestic tax consolidation level, for the IRES Probability test, since for the payment of this tax the Bank uses the method set forth in Arts 117 et seq. of the TUIR;
- at individual level, for additional IRES;
- at individual level, for IRAP.

The results of the probability test determined the following results:
- revaluation of € 14,408 thousand of tax credit to the consolidator;
- write-down of deferred tax assets related to the IRES surcharge of € 9,094 thousand;
- write-down of deferred tax assets related to other temporary differences of € 145 thousand.

As a result of the aforesaid measurement the Bank presented at 31 December 2018 DTAs not recognised in the Balance Sheet assets for a total of € 32,242 thousand (€ 22,950 thousand at 31 December 2017, € 23,005 thousand at FTA of IFRS 9)
This amount constitutes for the Bank a contingent asset, not subject to a time-limit according to the current tax legislation, the recognisability of which in the Balance Sheet assets will be assessed at future reporting dates according to the income prospects of the Bank and of the Group.

10.7.1 Current tax assets

Items / Balances	*31/12/2018*	*31/12/2017*
1. IRES advances		
2. IRAP advances		9,799
3. IRAP receivables		4,633
4. Other receivables and withholdings	333,337	294,382
Current tax assets - gross	**333,337**	**308,814**
Offsetting against current tax liabilities	2,003	(2,003)
Current tax assets - net	**331,334**	**306,811**

Note:
for IRES advances, please see Notes to the Financial Statements - Part B, Assets "Section 12 - Other assets".

10.7.2 Current tax liabilities

Items / Balances	*31/12/2018*		*31/12/2017*	
	taxation to shareholders' equity	*taxation to income statement*	*taxation to shareholders' equity*	*taxation to income statement*
1. IRES payables				
2. IRAP payables				
3. Other amounts due for current income taxes		2,003		2,003
Amounts due for current taxes - gross		**2,003**		**2,003**
Offsetting against current tax assets		(2,003)		(2,003)
Amounts due for current taxes - net		**0**		**0**

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

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

		31/12/2018	31/12/2017
A.	**Assets held for sale**		
A.1	Financial assets	52,025	979,942
A.2	Equity investments		
A.3	Property, plant and equipment	720	
	of which: obtained through enforcement of guarantees received		
A.4	Intangible assets		
A.5	Other non-current assets		
	Total A	**52,745**	**979,942**
of which valued at cost		**720**	**979,942**
of which valued at fair value level 1			
of which valued at fair value level 2			
of which valued at fair value level 3		**52,025**	
B.	**Discontinued operating activities**		
B.1	Financial assets measured at fair value through profit or loss		
	- financial assets held for trading		
	- financial assets designated at fair value		
	- other financial assets obligatorily measured at fair value		
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, plant and equipment		
	of which: obtained through enforcement of guarantees received		
B.6	Intangible assets		
B.7	Other assets		
	Total B		
of which valued at cost			
of which valued at fair value level 1			
of which valued at fair value level 2			
of which valued at fair value level 3			
C.	**Liabilities associated with assets held for sale**		
C.1	Payables		
C.2	Securities		
C.3	Other liabilities	**25**	
	Total C		
of which valued at cost			
of which valued at fair value level 1			
of which valued at fair value level 2			
of which valued at fair value level 3		**25**	
D.	**Liabilities associated with discontinued operating activities**		
D.1	Financial liabilities measured at amortised cost		
D.2	Financial liabilities held for trading		
D.3	Financial liabilities designated at fair value		
D.4	Funds		
D.5	Other liabilities		
	Total D		
of which valued at cost			
of which valued at fair value level 1			
of which valued at fair value level 2			
of which valued at fair value level 3			

11.2 Other information

Nothing to report.

SECTION 12 - OTHER ASSETS - ITEM 120

12.1 Other assets: breakdown

Type of transaction / Balances	*31/12/2018*	*31/12/2017*
1. Amounts due from the tax authorities and similar	1,847	2,264
2. Items being processed	2,232	6,171
3. Amounts receivable associated with the supply of goods and services	85	834
4. Improvement and incremental costs on third party assets	13	
5. Accrued income not attributable to own items	4,833	6,922
6. Prepaid expenses not attributable to own items	6,134	5,664
7. Receivable from consolidating entity for tax consolidation system	180,622	166,383
8. Receivables for reimbursement to personnel seconded with third parties	928	4,756
9. Measurement of securities to be settled ("regular way")	799	1,271
10.Other	3,564	2,572
Total	**201,057**	**196,837**

Note:
the sub-item "Amounts due from the tax authorities and similar" include credits due from foreign tax authorities equal to € 725 thousand (€ 813 in 2017).
The sub-item "Amounts due from the consolidating company" includes receivables for a total of € 2,144 thousand (€ 2,105 thousand at 31 December 2017) related to higher IRES taxes paid as a result of non-deduction of IRAP under the terms of art. 6 of Italian Law Decree no. 185/2010 and Italian Law Decree 16/2012.

LIABILITIES

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

1.1 Financial liabilities measured at amortised cost: breakdown by type of payables to banks

Type of transaction / Balances	*31/12/2018*	*31/12/2017(*)*
1. Due to Central Banks		
2. Due to banks	**15,900,332**	**15,449,516**
2.1 Current accounts and demand deposits	322,845	206,859
2.2 Fixed-term deposits	8,611,859	10,941,792
2.3 Loans	6,573,446	3,884,258
2.3.1 Repurchase agreements	*6,165,741*	*3,506,391*
2.3.2 Other	*407,705*	*377,867*
2.4 Amounts due for commitments to repurchase own equity instruments		
2.5 Other amounts payable	392,182	416,607
Total	**15,900,332**	**15,449,516**
Fair value - level 1		
Fair value - level 2	**15,900,332**	**15,449,516**
Fair value - level 3		
Total fair value	**15,900,332**	**15,449,516**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Note:
The sub-item "Due to banks - 2.5 Other amounts payable" includes collaterals received against operations in OTC and listed derivatives and in repurchase agreements (these last by way of additional marginalisations) on the basis of the agreements made between the parties (CSAs for OTC derivatives, GMRAs for repurchase agreements).
In relation to the disclosure on fair value, we can note that most of the deposits involve an early repayment on demand option. As a consequence, it was decided to quantify the related fair value as equal to the carrying amount, excluding changes which occurred in the Bank's creditworthiness subsequent to the date the individual relationships were begun.

1.2 Financial liabilities measured at amortised cost: breakdown by type of payables to customers

Type of transaction / Balances	*31/12/2018*	*31/12/2017(*)*
1. Current accounts and demand deposits		
2. Fixed-term deposits	3,163	3,158
3. Loans	4,280,895	6,596,423
3.1 Repurchase agreements	*4,262,972*	*6,565,551*
3.2 Other	*17,923*	*30,872*
4. Amounts due for commitments to repurchase own equity instruments		
5. Other amounts payable	316,326	340,329
Total	**4,600,384**	**6,939,910**
Fair value - level 1		
Fair value - level 2	**4,600,384**	**6,939,910**
Fair value - level 3		
Total fair value	**4,600,384**	**6,939,910**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Note:
Sub-item "5. Other amounts payable" includes collaterals received from institutional counterparties against operations in OTC and listed derivatives and in repurchase agreements (these last by way of additional marginalisations) on the basis of the agreements made between the parties (CSAs for OTC derivatives, GMRAs for repurchase agreements).

1.3 Financial liabilities measured at amortised cost: breakdown by type of securities outstanding

Type of security /Balances	*31/12/2018*				*31/12/2017(*)*			
	Carrying Amount	*Fair value*			*Carrying Amount*	*Fair Value*		
		Level 1	*Level 2*	*Level 3*		*Level 1*	*Level 2*	*Level 3*
A. Securities								
1. bonds	456,539		210,495		456,551		502,331	
1.1 structured								
1.2 other	*456,539*		*210,495*		*456,551*		*502,331*	
2. other securities								
2.1 structured								
2.2 other								
Total	**456,539**		**210,495**		**456,551**		**502,331**	

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Note:
the 2018 carrying amount includes € 6.530 thousand in interest accrued as of the reporting date (compared to € 6,526 thousand in 2017).

1.4 Details of subordinated debts/securities

No subordinated debts in relation to banks or customers are recorded in the financial statements.

The subordinated securities in issue are the following:

Name of security	*Currency*	*date of issue*	*maturity*	*interest rate*	*Carrying Amount 31/12/2018*	*31/12/2017*
1. IT0004809601 MPSCS-TV 12/22	Euro	30/03/2012	30/03/2022	variable	50,475	50,476
2. IT0005003451 MPSCS-TV 14/24	Euro	14/03/2014	14/03/2024	variable	253,225	253,232
3. IT0005041709 MPSCS-TV 14/24	Euro	31/07/2014	31/07/2024	variable	152,836	152,843
					456,536	**456,551**

Main characteristics of the subordinated securities in being at 31/12/2018:

1. Lower Tier II subordinated domestic bond issue, repayment of which will be in a single instalment at maturity; early repayment is not possible;
2. Tier II subordinated domestic bond issue, repayment of which will be in a single instalment at maturity; early repayment is not possible;
3. Tier II subordinated domestic bond issue, repayment of which will be in a single instalment at maturity; early repayment is not possible.

The subordination clauses state that, if the Bank is liquidated, the loans will be reimbursed only after all other creditors not equally subordinated have been repaid. The Bank may freely acquire on the market portions of the loans for no more than 10% of their value. Higher amounts shall be subject to prior approval by the Bank of Italy.

No portions of these securities were held in the receivable portfolio, at both reference dates.

1.5 Details of structured debts

No structured debts in relation to customers are recorded in the financial statements.

1.6 Payables for financial leasing

There is no liability for financial leases recorded in the financial statements.

SECTION 2 - FINANCIAL LIABILITIES HELD FOR TRADING - ITEM 20

2.1 Financial liabilities held for trading: breakdown by type

Type of transaction / Balances	*Total 31/12/2018*				
	Par value or notional value	*Fair value*			
		Level 1	*Level 2*	*Level 3*	*Fair value(*)*
A. Cash liabilities					
1. Due to banks	1,446,932	1,573,188	134		1,573,322
2. Due to customers	304,883	300,175	463		300,638
3. Debt securities					
3.1 Bonds					
3.1.1 Structured					
3.1.2 Other bonds					
3.2 Other securities					
3.1.1 Structured					
3.1.2 Other					
Total A	**1,751,815**	**1,873,363**	**597**		**1,873,960**
B. Derivative instruments					
1. Financial derivatives			1,537,614		
1.1 For trading			*1,537,614*		
1.2 Associated with the fair value option					
1.3 Other					
2. Credit derivatives			55,903		
2.1 For trading			*55,903*		
2.2 Associated with the fair value option					
2.3 Other					
Total B			**1,593,517**		
Total (A+B)		**1,873,363**	**1,594,114**		

(*) *fair value calculated by excluding the changes in value due to the change in the creditworthiness of the issuer since the issue date.*

Note:
The amounts shown in lines "1. Due to banks" and "2. Due to customers" are mainly correlated with those in lines "1. Debt securities" and "4. Loans" in table 2.1 of the assets "Financial assets held for trading." We also note that the sub-items "Due to banks" and "Due to customers", as above, include technical overdrafts. The same are measured at fair value consistently with the standards applied to "long" positions.
The sub-item "Financial derivatives - 1.1 held for trading" includes the fair value of OTC derivative contracts signed with corporate customers which present an evident low credit quality for a net amount of € 346 thousand (€ 412 thousand al 31/12/2017).
In application of IAS32 para. 42, level 1 derivatives quoted on regulated markets were offset for € 54,607 thousand (€ 82,449 at 31/12/2017) as well as OTC level 2 regulated derivatives settled through the Central Counterparty London Clearing House (LCH) for € 1,271,296 thousand (€ 1,028,498 at 31/12/2017) and level 2 credit derivatives settled at the Central Counterparty ICE Clear Europe (ICE) for € 526 thousand (no offsetting at 31/12/2017). The Bank has "indirect" access to the Clearing of OTC derivatives through the Clearing Members.

Type of transaction / Balances	*Total 31/12/2017*				
	Par value or notional value	*Fair value*			
		Level 1	*Level 2*	*Level 3*	*Fair value(*)*
A. Cash liabilities					
1. Due to banks	931,754	1,002,677	1,852		1,004,529
2. Due to customers	1,701,715	1,898,689			1,898,689
3. Debt securities					
3.1 Bonds					
3.1.1 Structured					
3.1.2 Other bonds					
3.2 Other securities					
3.1.1 Structured					
3.1.2 Other					
Total A	**2,633,469**	**2,901,366**	**1,852**		**2,903,218**
B. Derivative instruments					
1. Financial derivatives			1,866,804		
1.1 For trading			*1,866,804*		
1.2 Associated with the fair value option					
1.3 Other					
2. Credit derivatives			34,211		
2.1 For trading			*34,211*		
2.2 Associated with the fair value option					
2.3 Other					
Total B			**1,901,015**		
Total (A+B)		**2,901,366**	**1,902,867**		

(*) *fair value calculated by excluding the changes in value due to the change in the creditworthiness of the issuer since the issue date.*

3. Details of "Financial liabilities held for trading": subordinated liabilities

There are no subordinated liabilities.

4. Details of "Financial liabilities held for trading": structured debts

There are no structured debts.

SECTION 3 - FINANCIAL LIABILITIES DESIGNATED AT FAIR VALUE - ITEM 30

No positions have been classified in this category.

3.1 Financial liabilities designated at fair value: breakdown by type

No positions have been classified in this category

SECTION 4 - HEDGING DERIVATIVES - ITEM 40

There were no transactions for this accounting item.

4.1 Hedging derivatives: breakdown by type of hedge and hierarchical levels

There were no transactions for this accounting item

SECTION 5 - VALUE ADJUSTMENTS TO FINANCIAL LIABILITIES SUBJECT TO MACRO-HEDGING - ITEM 50

There were no transactions for this accounting item.

SECTION 6 - TAX LIABILITIES - ITEM 60

6.1 Current tax liabilities

Details of current tax liabilities are provided in the Notes to the Financial Statements Part B - Assets - Section 10 "*Tax assets and tax liabilities*".

6.2 Deferred tax liabilities

Details of deferred tax liabilities are provided in the Notes to the Financial Statements Part B - Assets - Section 10 "*Tax assets and tax liabilities*".

SECTION 7 - LIABILITIES ASSOCIATED WITH ASSETS HELD FOR SALE - ITEM 70

None of the Bank's liabilities are classified in this category.

SECTION 8 - OTHER LIABILITIES - ITEM 80

8.1 Other liabilities: breakdown

Type of transaction / Balances	*31/12/2018*	*31/12/2017*
1. Taxes due to the tax authorities and similar	3,647	2,383
2. Amounts due to social security and welfare institutions	1,576	1,584
3. Amounts due to the Parent Company for tax consolidation		
4. Sums available to customers	1,866	2,332
5. Other amounts due to employees	3,228	5,411
6. Items being processed	41,477	17,475
7. Amounts payable associated with the payment		
of supplies of goods and services	15,261	22,264
8. Payables for reimbursement of cost of personnel seconded to Bank	1,289	1,397
9. Deferred income not attributable to own items	123	743
10. Accrued liabilities not attributable to own items	18	13
11. Measurement of securities to be settled ("regular way")	337	3,715
12. Other	1,658	2,488
Total	**70,480**	**59,805**

Note:
sub-item 6. "Items being processed" includes mainly invoices not yet received.

SECTION 9 - EMPLOYEE SEVERANCE INDEMNITY - ITEM 90

9.1 Employee severance indemnity: annual changes

		31/12/2018	31/12/2017
A.	**Opening balances**	**2,603**	**3,112**
B.	**Increases**	**29**	**42**
B.2	Provision for the year	22	41
B.3	Other increases	7	1
C	**Decreases**	**107**	**551**
C.1	Liquidations carried out	50	500
C.2	Other decreases	57	51
D.	**Closing balances**	**2,525**	**2,603**

Following the supplementary welfare reform pursuant to Italian Legislative Decree No. 252 of 5 December 2005, the portions of severance indemnity accrued as from 1 January 2007 are, at the discretion of the employee, assigned to supplementary welfare plans or transferred to the Treasury Funds managed by INPS (National Institute of Social Insurance). The said portions do not appear in the table of movements.

Below, the amount subject to the prudential filter is shown, recognised according to the indications issued by the Bank of Italy regarding the determination of regulatory capital.

		31/12/2018	31/12/2017
a)	Value of net liability for defined benefits on the basis of the new IAS 19	2,525	2,603
b)	Value of net liability for defined benefits on the basis of the approach used in the 31/12/2012 financial statements	2,127	1,752
c)	**Difference between the two values (a-b)**	**398**	**851**
d)	Tax effect on the difference	109	234
e)	**Net difference to be added as a prudential filter to supervisory capital**	**289**	**617**

9.2 Other information

9.2.a Changes during the year for defined benefit liabilities. Severance indemnities

Items / Balances	*A (-) Plan assets*	*B(+) Current DBO value*	*C(+) Asset ceiling*	*D=A+B+C Net liabilities/ assets for defined benefits*
Opening balances		**2,603**		**2,603**
Welfare cost relating to current work services				
Interest income/expense		22		22
Revaluation of net liabilities/assets for defined benefits:		(50)		(50)
Yield of plan assets net of interest				
Actuarial gains/losses deriving from changes in demographic assumptions		*7*		*7*
Actuarial gains/losses deriving from past experience		*(13)*		*(13)*
Actuarial gains/losses deriving from changes in financial assumptions		*(44)*		*(44)*
Changes in the effect of limitations on the availability of a net asset for defined benefit plans				
Welfare cost relating to past employment service and/or regulatory gains/losses				
Exchange differences				
Contributions:		(50)		(50)
Paid by the employer				
Paid by employees				
Payments made by the plan		*(50)*		*(50)*
Effects of business combinations and disposals				
Effect of reductions in fund				
Effect of discharges on fund				
Other changes				
Closing balances		**2,525**		**2,525**

9.2.b Main actuarial hypotheses used

Main actuarial hypotheses / Percentages	*31/12/2018*	*31/12/2017*
1. Average discounting back rate (*)	0.9846%	0.7915%
2. Average future inflation rate	1.50005%	1.5000%
Annual inflation rate	2.6300%	2.6300%

(*) for the purposes of calculating the discounting back of gains/losses, the Bank uses the BFV EUR Composite (AA) curve at the measurement date. This curve refers to a basket of securities issued by corporate issuers with an "AA" rating.

9.2.c Analysis of DBO sensitivity to changes in the main actuarial hypotheses

Actuarial hypotheses	*Change in the value of the bond*	*% change in the bond*
Average discounting back rate		
25 bp increase	(54)	(2.1357%)
25 bp decrease	44	1.7596%
Average future inflation rate		
25 bp increase	25	0.9923%
25 bp decrease	(36)	(1.4149%)

9.2.2 Amount of liabilities pursuant to Article 2424-bis of the Italian Civil Code

Under the terms of Article 2424-bis of the Italian Civil Code, the statutory liability accrued at year end for the employee severance indemnity was € 2,269 thousand (€ 2,263 thousand at 31 December 2017).

SECTION 10 - PROVISIONS FOR RISKS AND CHARGES - ITEM 100

10.1 Provisions for risks and charges: breakdown

Items / Balances	31/12/2018	31/12/2017(*)
1. Provisions for credit risk related to commitments and guarantees given	2,409	3,063
2. Provisions for other commitments and other guarantees given		
3. Company pension funds	4,108	4,602
4. Other provisions for risks and charges:	23,941	23,179
4.1 legal disputes	*19,702*	*19,167*
4.2 personnel expenses	*1,794*	
4.3 other	*2,445*	*4,012*
Total	**30,458**	**30,844**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Note:
the sub-item "Other provisions for risks and charges: 2.1 legal disputes" includes allocations for liabilities deemed likely in relation to miscellaneous ordinary cases with customers and for actions for revocation, accounting for 88% and 12%, respectively, of the total shown in the table (82% and 18% at 31 December 2017).

10.2 Provisions for risks and charges: annual changes

	Provisions for other commitments and other guarantees given	*Pension funds*	*Other provisions for risks and charges*	*Total*
A. Opening balances		**4,602**	**23,179**	**27,781**
B. Increases		**163**	**4,634**	**4,797**
B.1 Provision for the year			4,634	4,634
B.2 Changes due to the passage of time		20		20
B.3 Changes due to discount rate changes				
B.4 Other increases		143		143
C. Decreases		**657**	**3,872**	**4,529**
C.1 Uses in the year		515	2,266	2,781
C.2 Changes due to discount rate changes				
C.3 Other changes		142	1,606	1,748
D. Closing balances		**4,108**	**23,941**	**28,049**

10.2a Other provisions for risks and charges: details of annual changes

	Legal disputes	*Personnel expenses*	*Other*	*Total*
A. Opening balances	**19,167**		**4,012**	**23,179**
B. Increases	**2,160**	**1,794**	**680**	**4,634**
B.1 Provision for the year	2,160	1,794	680	4,634
B.2 Changes due to the passage of time				
B.3 Changes due to discount rate changes				
B.4 Other increases				
C. Decreases	**1,625**		**2,247**	**3,872**
C.1 Uses in the year	19		2,247	2,266
C.2 Changes due to discount rate changes				
C.3 Other changes	1,606			1,606
D. Closing balances	**19,702**	**1,794**	**2,445**	**23,941**

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

		First stage	*Second stage*	*Third stage*	*Total*
1.	Irrevocable commitments to grant finance	247	907		1,154
2.	Financial guarantees given	142	487	626	1,255
	Total	**389**	**1,394**	**626**	**2,409**

10.4 Provisions for other commitments and other guarantees given

There were no provisions for other commitments and other guarantees given.

10.5 Defined-benefit company pension funds

10.5.1 Illustration of the features of the funds and of the related risks

Determination of the actuarial values, required by the application of IAS 19 “Employee Benefits” for defined-benefit complementary pension funds, is carried out by an independent actuary, using the “projected unit credit” method, as described in more detail in Part A of the Notes to the Financial Statements, Accounting Policies.

The internal defined benefit funds for which the Bank is jointly responsible are the following:
Defined benefit pension fund, of a supplementary or additional type, reserved for the personnel of the former Mediocredito Toscano and the former Istituto Nazionale di Credito Agrario already retired as of 1 January 1999 and personnel in service hired before 27 April 1993 who have expressed the desire to remain in said section. The provision for which the Bank is solely responsible is determined on the basis of the mathematical reserve calculated by an independent actuary at the end of each financial year.
“Defined contribution” pension fund, extended to all the Bank’s personnel, with separate assets but not a separate legal standing.
For more details, please refer to the statements of accounts for pension funds attached to the Notes to the Financial Statements.

10.5.2 Changes during the year in net defined benefit liabilities (assets) and in refund rights

Items / Balances	*31/12/2018*		*31/12/2017*	
	Internal plans	*External plans*	*Internal plans*	*External plans*
Opening balances	**4,602**		**5,036**	
Increases	**163**		**91**	
Welfare cost relating to current work services				
Borrowing costs	20		21	
Members contributions to plan				
Actuarial losses	143		70	
Exchange losses				
Welfare cost relating to past employment services				
Other changes				
Decreases	**657**		**525**	
Indemnities paid	515		518	
Welfare cost relating to past employment services				
Actuarial gains	142		7	
Exchange gains				
Effect of reductions in fund				
Effect of discharges on fund				
Other changes				
Closing balances	**4,108**		**4,602**	

10.5.2.a Changes in the year in defined-benefit net liabilities (assets)

Items / Balances	*A (-) Plan assets*	*B(+) Current DBO value*	*C(+) Asset ceiling*	*D=A+B+C Net liabilities/ assets for defined benefits*
Opening balances		**4,602**		**4,602**
Welfare cost relating to current work services				
Interest income/expense		20		20
Revaluation of net liabilities/assets for defined benefits:		1		1
Yield of plan assets net of interest				
Actuarial gains/losses deriving from changes in demographic assumptions		*(92)*		*(92)*
Actuarial gains/losses deriving from changes in financial assumptions		*(50)*		*(50)*
Actuarial gains/losses deriving from past experience		*143*		*143*
Changes in the effect of limitations on the availability of a net asset for defined benefit plans				
Welfare cost relating to past employment service and/or regulatory gains/losses				
Exchange differences				
Contributions:		(515)		(515)
Paid by the employer				
Paid by employees				
Payments made by the plan		*(515)*		*(515)*
Effects of business combinations and disposals				
Effect of reductions in fund				
Effect of discharges on fund				
Other changes				
Closing balances		**4,108**		**4,108**

10.5.3 Information about the fair value of the plan assets

The assets of the defined-benefit pension funds are invested in the Bank's assets; no specific assets have been classified as plan assets. As a consequence, it is not possible to provide precise information about the fair value of the plan assets.

10.5.4 Description of the main actuarial hypotheses

Main actuarial hypotheses / Percentages	*31/12/2018*	*31/12/2017*
1. Average annual discounting rate *(*)*	0.9846%	0.7915%
2. Average annual salary increase rate (*)	n.a.	n.a.
3. Average annual future inflation rate	1.5000%	1.5000%

(*) for the purposes of calculating the discounting back of gains/losses, the Bank uses the BFV EUR Composite (AA) curve at the measurement date. This curve refers to a basket of securities issued by corporate issuers with an "AA" rating.

10.5.5 Information on amounts, time frames, and uncertainties for financial flows

Below we provide the estimated uses in the coming years:

FUTURE PAYMENTS

Year	*2019*	*2020*	*2021*	*2022*	*2023*
Cash flow	473	443	411	378	344

OTHER INFORMATION

Main actuarial hypotheses / Percentages	*31/12/2018*	*31/12/2017*
Number of active employees	-	-
Number of pensioners	37	38
Service Cost 2016	-	-
Residual average length in years	5.81	6.25

10.5.5.a Analysis of DBO sensitivity to changes in the main actuarial hypotheses

Actuarial hypotheses	*Change in the value of the bond*	*% change in the bond*
Average annual discounting back rate		
DBO + 0.25% discounting	65	1.5915%
DBO - 0.25% discounting	(63)	(1.5292%)
Average annual future inflation rate		
DBO + 0.25% inflation rate	(46)	(1.1191%)
DBO - 0.25% inflation rate	50	1.2070%

10.5.6 Plans related to more than one employer

There are no plans related to more than one employer.

10.5.7 Defined benefit plans that share the risks between entities under joint control

No plans with this feature exist.

10.6 Provisions for risks and charges- other provisions

Items/Balances	*31/12/2018*	*31/12/2017*
1. Legal disputes	19,702	19,167
- revocatory actions	2,430	3,530
- other legal disputes	17,272	15,637
2. Personnel expenses	1,794	
- seniority bonuses		
- LPO VAP incentive system		
- employment dispute		
- voluntary retirement	*1,794*	
- other benefits from termination of the employment relationship, other than the liability		
- other		
3. Other	2,445	4,012
- contracts for a consideration		
- tax risks		
- expenses for misappropriation		
- risks connected with sundry items		
- complaints and out-of-court agreements		
- estimates of fees accruing for recovery of receivables		
- estimates of fees accruing for legal disputes		
- other	2,445	4,012
Total	**23,941**	**23,179**

SECTION 11 - REFUNDABLE SHARES - ITEM 120

There were no transactions for this accounting item.

SECTION 12 - THE BANK'S SHAREHOLDERS' EQUITY - ITEMS 110, 130, 140, 150, 160, 170 AND 180

The Bank's shareholders' equity has the following composition:

Items / Balances	*31/12/2018*	*31/12/2017*
1. Capital	1,669,516	1,669,516
2. Share premiums		161,446
3. Reserves	(407,280)	110,427
4. (Treasury shares)		
5. Valuation reserves	(141,441)	(2,242)
6. Equity instruments		
7. Profit (Loss) for the year	80,699	(632,937)
Total	**1,201,494**	**1,306,210**

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

12.1.a Share capital: breakdown

Items/Balances	*Number of shares*	*Unexpressed unit par value*	*Capital*
a) ordinary shares (fully paid-up)	802,551	*2,080.26*	1,669,516,282

On 18 August 2017 the Bank's Extraordinary Shareholders' Meeting resolved, inter alia, to eliminate the par value of the ordinary shares; consequently, the so-called "unexpressed par value" is indicated; this is obtained dividing the amount of the share capital by the number of shares outstanding at the reporting date.

12.1.b Treasury shares: breakdown

As of the balance sheet date, the Bank did not hold any treasury shares.

12.2 Capital - number of shares: annual changes

No change during the year.

12.3 Capital: other information

The share capital is fully subscribed and paid in.

12.4 Profit reserves: other information

Profit reserves, constituted in accordance with the Italian Code, with the articles of association or in relation to specific resolutions passed by the Shareholders' Meeting as to the allocation of the income for the loss, have the purpose of strengthening the Bank's capital. During 2018 the available profit reserves were completely used to cover part of the 2017 loss. For further details please see table 12.6.2. below.

Items / Balances	*31/12/2018*	*31/12/2017*
Legal reserve		41,323
Reserve of parent company shares		34,653
Statutory reserve		
Reserve ex art. 13 Lgs. Decree 124/93		
Extraordinary reserve		
Other reserves	(407,280)	666
Total	**(407,280)**	**76,642**

12.5 Equity instruments: breakdown and annual changes

There were no transactions for this accounting item.

12.6 Other information

12.6.1 Valuation reserves

12.6.1.1 Valuation reserves: breakdown

Items / Components	*31/12/2018*	*31/12/2017*
1. Financial assets measured at fair value through other comprehensive income	(139,706)	338
2. Property, plant and equipment		
3. Intangible assets		
4. Foreign investment hedging		
5. Cash flow hedging		
6. Exchange differences		
7. Non-current assets and disposal groups held for sale		
8. Special revaluation laws		
9. Employee severance indemnities	(1,207)	(1,257)
10.Company pension funds	(1,910)	(1,910)
11.Tax effect	1,382	587
Total	**(141,441)**	**(2,242)**

12.6.1.2 Valuation reserves: annual changes

	Financial assets designated at fair value	*Employee severance indemnities*	*Company pension funds*	*Tax effect*	*Total*
A. Opening balances (*)	**(101,174)**	**(1,257)**	**(1,910)**	**689**	**(103,652)**
B. Increases	**2,488**	**57**	**143**	**(58)**	**2,630**
B.1 Fair value increases	38				38
B.2 Other changes	2,450	57	143	(58)	2,592
C. Decreases	**41,020**	**7**	**143**	**(751)**	**40,419**
C.1 Fair value decreases	41,020			(710)	40,310
C.2 Other changes		7	143	(41)	109
D. Closing balances	**(139,706)**	**(1,207)**	**(1,910)**	**1,382**	**(141,441)**

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph “Transition to the accounting standards IFRS 9 and IFRS 15”.

12.6.1.3 Valuation reserves relating to financial assets measured at fair value through other comprehensive income: breakdown (before tax effects)

Assets / Balances	*31/12/2018*		*31/12/2017*	
	Positive reserve	*Negative reserve*	*Positive reserve*	*Negative reserve*
1. Debt securities		2,581		
2. Equity securities		137,125	39	
3. UCITS Units			414	115
4. Loans				
Total	**0**	**139,706**	**453**	**115**

Note:
For the measurement criteria used to determine the market value of this security please see paragraph A.4.2 Measurement processes and sensitivity.

12.6.1.5 Valuation reserves relating to financial assets measured at fair value through other comprehensive income: annual changes (before tax effects)

		Debt securities	*Equity securities*	*UCITS Units*	*Loans*
1.	**Opening balances (*)**		**(101,174)**		
2.	**Positive changes**	**2,450**	**38**		
2.1	Fair value increases		38		
2.2	Transfer to income statement of negative reserves	2,450	0		
	- due to impairment	*2,450*			
	- due to conversion				
2.3	Other changes				
3.	**Negative changes**	**5,032**	**35,989**		
3.1	Reductions of *fair value*	5,032	35,989		
3.2	Transfer to income statement of positive reserves		0		
	- due to conversion				
3.3	Other changes				
4.	**Closing balances**	**(2,582)**	**(137,125)**	**0**	

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

12.6.2 The Bank's capital: availability and possibility of distribution of the various items

	Amount	Possibility of utilisation (*)	Available portion	Summary of uses made in previous three years: for coverage of losses	Summary of uses made in previous three years: for other reasons
Capital	**1,669,516**				
Capital reserves				948,770	
Profit reserves:	(407,280)			81,488	
- Profit reserves FTA 2013 IAS 19	666				
- Reserves from FTA IFRS 9	(46,215)				
- Retained losses	(361,731)				
Other reserves subject to deferred taxation				10,632	
Valuation reserves	(141,441)				
Total reserves	**(548,721)**			**1,040,890**	
Profit for 2018	**80,699**				
Total Equity	**1,201,494**				

(*) Key:
A for share capital increases; B for coverage of losses; C for distribution to shareholders

Note:
"Retained losses" indicate the loss for financial year 2017 for the residual portion not covered by the reserves.
Utilisations were made in 2017 to cover 2016 losses (for € 769,683 thousand) and in 2018 to cover part of the 2017 losses (for € 271,207 thousand) using the available reserves.

OTHER INFORMATION

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

	a) Nominal value of commitments and financial guarantees given			*31/12/2018*
	First stage	*Second stage*	*Third stage*	
1. Irrevocable commitments to grant finance	**6,433,628**	**143,163**	**9,636**	**6,586,427**
a) Central banks				
b) Public administrations				
c) Banks	69,178			**69,178**
d) Other financial companies	6,068,629	18,387		**6,087,016**
e) Non-financial companies	295,642	124,776	9,445	**429,863**
f) Households	179		191	**370**
2. Financial guarantees given	**69,152**	**18,886**	**797**	**88,835**
a) Central banks				
b) Public administrations				
c) Banks	8,969			**8,969**
d) Other financial companies	2,747			**2,747**
e) Non-financial companies	57,436	18,886	797	**77,119**
f) Households				

2. Other commitments and other guarantees given

	31/12/2018
1. Other guarantees given	**1,048,686**
of which: impaired	
a) Central banks	
b) Public administrations	
c) Banks	1,048,686
d) Other financial companies	
e) Non-financial companies	
f) Households	
2. Other commitments	**1,628,467**
of which: impaired	
a) Central banks	
b) Public administrations	1,265,492
c) Banks	131,837
d) Other financial companies	230,633
e) Non-financial companies	505
f) Households	

3. Assets lodged as collateral for the Bank's liabilities and commitments

Portfolios	*31/12/2018*	*31/12/2017*
1. Financial assets measured at fair value through profit or loss	4,889,919	4,841,727
2. Financial assets measured at fair value through other comprehensive income	60,691	
3. Financial assets measured at amortised cost	1,655,648	697,223
4. Property, plant and equipment		
of which: *property, plant and equipment that constitutes inventories*		

Note:
these are mainly assets used as collateral for repurchase agreements, securities lending and derivatives.

4. Information on operating leases

Items / Balances	*31/12/2018*	*31/12/2017*
- Within 1 year	1,838	360
- Between 1 and 5 years	6,105	483
- Beyond 5 years	15,744	-

5. Management and brokerage on behalf of third parties

Type of services	*31/12/2018*	*31/12/2017*
1. Execution of order on customers' behalf		
a) Purchases	6,629,754	5,773,654
1. Settled	*6,612,092*	*5,730,169*
2. Not settled	*17,662*	*43,485*
b) Sales	6,205,195	6,380,059
1. Settled	*6,203,222*	*6,351,458*
2. Not settled	*1,973*	*28,601*
2. Portfolio management		
a) Individual		
b) Collective		
3. Custody and administration of securities		
a) Third party securities deposited with the Bank associated with its role as custodian bank (excluding asset management)		
1. Securities issued by the bank which draws up the financial statement		
2. Other securities		
b) Third party securities on deposit (excluding asset management): other	7,236,274	7,936,145
1. Securities issued by the bank which draws up the financial statement		
2. Other securities	*7,236,274*	*7,936,145*
c) Third party securities deposited with third parties	7,236,274	7,870,672
d) Bank's securities deposited with third parties	6,810,408	6,602,475
4. Other transactions	5,144,296	1,540,138

Note:
The amounts indicated in point 3 "Custody and administration of securities" represent the par value of the securities.
The sub-items "third party securities" include € 807,535 thousand as collateral received to guarantee derivative and repurchase agreements payable exposures (€ 659,817 thousand in 2017), as well as securities received for repurchase and securities lending operations receivable for a nominal value of € 6,302,241 thousand (€ 6,932,453 thousand at 31 December 2017). The aggregate had a total fair value of € 7,660,121 thousand (€ 8,465,142 at 31 December 2017).
The "Other transactions" indicated at point 4, represent the volumes of placement activities with or without guarantees.

6. Financial assets subject to netting in the financial statements, or subject to outline netting or similar agreements

Technical forms	*Gross amount of financial assets (a)*	*Amount of financial liabilities netted in the financial statements (b)*	*Net amount of financial assets recognised in the financial statements (c=a-b)*	*Correlated amounts not subject to netting in the financial statements*		***Net amount 31/12/2018*** *(f=c-d-e)*	***Net amount 31/12/2017***
				Financial instruments (d)	*Cash deposits received as guarantees (e)*		
1. Derivatives	4,590,708	1,325,904	3,264,804	1,397,439	1,465,872	**401,493**	**383,017**
2. Repurchase agreements	6,742,719		6,742,719	6,639,480		**103,239**	**80,822**
3. Securities lending							
4. Other							
Total 31/12/2018	**11,333,427**	**1,325,904**	**10,007,523**	**8,036,919**	**1,465,872**	**504,732**	
Total 31/12/2017	**12,307,035**	**1,110,947**	**11,196,088**	**9,355,155**	**1,377,094**		**463,839**

Note:

The assets indicated in the table above are measured in accordance with the criteria outlined in the relevant accounting standards, i.e. in Part A.2, Section 1: 1) Financial assets measured at fair value through profit or loss (FVTPL) and 3) Financial assets measured at amortised cost.

The amounts related to derivatives refer to: i) derivatives quoted on regulated markets; ii) OTC financial derivatives settled at the Central Counterparties LCH London Clearing House and ICE Clear Europe, through Clearings Members; iii) OTC derivatives entered into with institutional counterparties settled by ISDA, MNA and CSA.

The amounts related to repurchase agreements refer to transactions settled, respectively, through GMRA and GMSLA collateralisation agreements.

The amounts shown in column "c" correspond to those presented in the Balance Sheet Assets under Item 20. "Financial assets measured at fair value through profit or loss - a) Financial assets held for trading" as regards derivatives and, as regards repurchase agreements, under item 40. "Financial assets measured at amortised cost".

Description of netting rights subject to netting framework agreements or similar agreements, including cases in which the criteria envisaged in section 42 of IAS 32 are not met.

Operations regarding derivatives listed on regulated markets have the characteristics referred to in the amendment to IAS 32 for offsetting financial assets and liabilities, in that the Bank has a current and unconditional right, which can be exercised during the normal course of business and also in the cause of default, insolvency or bankruptcy of the counterpart, to offset the financial asset or liability (IAS 32 §AG38B), whether the intention is to settle the amount on a net basis or to make use of the asset while simultaneously eliminating the liability (IAS 32 §AG38E).

With reference to OTC financial derivatives settled with the Central Counterparties LCH and ICE, the relation between the Bank and the Clearing Members is governed by an ISDA MNA and CSA contract in which, unlike what occurs in the context of the agreements envisaged with the other counterparties, the application of a "Multiple Transaction Payment Netting" clause is envisaged, defined under article 2(c) of the 2002 ISDA MNA. Activation of the Multiple Transaction Payment Netting option involves:

- *settlement on a net basis on a daily or infra-daily basis;*
- *the execution of a single transfer of funds for each regulated currency inclusive of exchanges of contractual flows, any amounts to be paid in the case of early termination and payments/deposits related to the initial and variation margin (collateral).*

In the event of default of a Clearing Member the Bank can choose whether to transfer the positions to another Clearing Member or have the existing positions liquidated; in any case the netting mechanism provided for in the ISDA MNA is applied.

This type of transaction also has the characteristics envisaged in the amendment to IAS 32 (see previous point).

OTC derivatives entered into with institutional counterparties are governed by ISDA MNA and CSA contracts. The contractual clauses for these operations allow for offset adjustment of the financial assets and liabilities in question only in the case in which certain events occur, while the possibility of offsetting during the course of normal business being excluded. With the exception of the agreements stipulated with the Clearing Members of the CCP, no agreements exist with institutional counterparties that envisage the application of the Multiple Transaction Payment Netting clause.

Therefore, this type does not have the characteristics necessary for netting in the financial statements, as regulated by the amendment to IAS 32.
Repurchase agreements and securities borrowing and lending are all governed by the following agreements, developed with an eye to mitigating credit risk:
• Global Master Repurchase Agreement (GMRA) for repurchase agreements;
• Global Master Securities Lending Agreement (GMSLA) for securities lending.
On the basis of the analysis carried out, with particular reference to the contractual rules relating to the settlement of cash flows, no cases were identified that envisage settlement on a net basis of daily or infra-daily cash flows, during the normal course of business. Therefore, the requirements referred to in the amendment to IAS 32 for relative netting in the financial statements are not met.

7. Financial liabilities subject to netting in the financial statements, or subject to outline netting or similar agreements

Technical forms	*Gross amount of financial liabilities (a)*	*Amount of financial assets netted in the financial statements (b)*	*Net amount of financial liabilities recognised in the financial statements (c=a-b)*	*Correlated amounts not subject to netting in the financial statements*		***Net amount 31/12/2018*** *(f=c-d-e)*	***Net amount 31/12/2017***
				Financial instruments (d)	*Cash deposits received as guarantees (e)*		
1. Derivatives	2,879,490	1,325,904	1,553,586	1,381,627	147,751	**24,208**	**10,768**
2. Repurchase agreements	10,428,713		10,428,713	10,426,854		**1,859**	
3. Securities lending							
4. Other							
Total 31/12/2018	**13,308,203**	**1,325,904**	**11,982,299**	**11,808,481**	**147,751**	**26,067**	
Total 31/12/2017	**13,079,686**	**1,110,947**	**11,968,739**	**11,828,984**	**128,987**		**10,768**

Note:
The liabilities indicated in the table above are measured in accordance with the criteria outlined in the relevant accounting standards, i.e. in Part A.2, Section 1: 10) Financial liabilities at amortised cost and 11) Financial liabilities held for trading.
The amounts shown in column "c" correspond to those presented in the Balance Sheet Liabilities under Item 10. "Financial liabilities measured at amortised cost", in relation to repurchase agreements, and 20. "Financial liabilities held for trading", as regards derivatives.
In relation to the disclosure for netting rights, please refer to the information provided at the bottom of table "5. Financial assets subject to netting in the financial statements, or subject to outline netting or similar agreements" above.

8. Securities lending transactions

Securities lending transactions, as for similar repurchase agreement transactions, are carried out mostly to hedge against similar and specular transactions. They are also carried out to hedge against short positions on securities (known as technical overdrafts, representing, in terms of volumes, mainly sales of government securities) taken on by the trading desks for strategies focused on short/medium-term maturities.
Overall, we can note dynamic and complex management of the Global Markets portfolios, regarding both investments and funding, as can be seen from the figures involved: the amount of the securities lending transactions, at 31 December 2018, came out at € 1,582.6 million (compared to € 1,647 million at 31 December 2017). These transactions, aimed at acquiring available securities to be used for funding operations or to cover technical overdrafts, were for the most part carried out with the parent company (which, in turn, borrows these securities from its customers) and involved Italian government securities for approximately 88% of the total.
Considering together the securities lending and repurchase agreement transactions, the total net funding position, correlated with financing of net long positions in securities, was € 3,686 million.

9. Disclosure on jointly-controlled companies

Nothing to report.

Part C
Notes to the Income Statement

SECTION 1 - INTEREST - ITEMS 10 AND 20

1.1 Interest and other income: breakdown

Items / Technical forms	*Debt securities*	*Loans*	*Other transactions*	***Total 31/12/18***	***Total 31/12/17***
1. Financial assets measured at fair value through profit or loss:	64,066	625		**64,691**	**59,128**
1.1 Financial assets held for trading	*62,843*			**62,843**	**59,128**
1.2 Financial assets designated at fair value					
1.3 Other financial assets obligatorily measured at fair value	*1,223*	*625*		**1,848**	
2. Financial assets measured at fair value through other comprehensive income	1,658			**1,658**	**608**
3. Financial assets measured at amortised cost	5,352	156,176		**161,528**	**249,871**
3.1 Receivables from banks		*23,423*		**23,423**	**53,064**
3.2 Receivables from customers	*5,352*	*132,753*		**138,105**	**196,807**
4. Hedging derivatives				**0**	
5. Other assets			38	**38**	**38**
6. Financial liabilities				**75,179**	
Total	**71,076**	**156,801**	**38**	**303,094**	**309,645**
of which: interest income on impaired financial assets	321	35,794		**36,115**	

1.1.a Interest income on impaired assets

Items / Technical types	*Total*	*of wich forborne exposure*
a) Bad loans	14,026	4,400
b) Probable defaults	21,923	17,948
c) Impaired past-due exposures	166	1
Total	**36,115**	**22,349**

1.2 Interest and similar income: other information

	31/12/2018	*31/12/2017*
1. Interest income on foreign currency financial assets	12,912	11,703
2. Interest income on financial lease transactions	-	-

1.3 Interest expense and similar charges: breakdown

Items / Technical forms	*Payables*	*Securities*	*Other transactions*	***Total 31/12/18***	***Total 31/12/17***
1. Financial liabilities measured at amortised cost	(98,812)	(19,461)		**(118,273)**	**(217,203)**
1.1 Payables to central banks					
1.2 Payables to banks	(98,208)			**(98,208)**	**(159,579)**
1.3 Payables to customers	(604)			**(604)**	**(38,038)**
1.4 Outstanding securities		(19,461)		**(19,461)**	**(19,586)**
2. Financial liabilities held for trading	(78)			**(78)**	**(347)**
3. Financial liabilities designated at fair value					
4. Other liabilities and provisions					
5. Hedging derivatives					
6. Financial assets				**(49,121)**	
Total	**(98,890)**	**(19,461)**		**(167,472)**	**(217,550)**

1.4 Interest expense and similar charges: other information

	31/12/2018	*31/12/2017*
1. Interest expense on foreign currency liabilities	(8,330)	(6,203)
2. Interest expense on liabilities for financial lease transactions	-	-

1.5 Spreads relating to hedging transactions

During the last two financial years, no hedging operations were carried out.

SECTION 2 - FEES - ITEMS 40 AND 50

2.1 Fee income: breakdown

Type of services / Balances	31/12/2018	31/12/2017
a) guarantees given	1,612	1,351
b) credit derivatives		
c) asset management, brokerage and consultancy services:	16,908	13,738
1. financial instrument trading		
2. foreign exchange trading		
3. portfolio management		
3.1. individual		
3.2 collective		
4. custody and administration of securities		
5. custodian bank		
6. placing of securities	*14,774*	*11,899*
7. order reception and transmission	*2,134*	*1,839*
8. advisory services		
8.1 on investments		
8.2 on financial structure		
9. distribution of third-party services		
9.1. portfolio management		
9.1.1. individual		
9.1.2. collective		
9.2. insurance products		
9.3. other products		
d) collection and payment services		
e) servicing for securitisation transactions		
f) factoring services		
g) tax collection and State lottery services		
h) management of multilateral trading systems		
i) holding and managing current accounts		
j) other services	27,130	28,106
Total	**45,650**	**43,195**

Note:
in relation to the sub-item "c) 6. securities placement", 23 placing operations with/without guarantee were handled by the Bank.
In relation to the disclosure required by IFRS 15 please refer to the information provided in Part A, Section 2, para. 15) Other information. We can specify in this regard that fee income is normally recognised in the accounts at point in time, with the exception of that booked to sub-item "a) guarantees given" and for approximately 34% of that booked to sub-item "j) other services", which are received over time. As regards the latter this income consists, in particular, of:

- *fees for the work done for the Management of the SME Guarantee Fund, for € 1,403 thousand;*
- *fees chargeable to customers for the delayed use of amounts agreed to be disbursed mainly referable to corporate finance (in particular project financing) operations, for an amount of € 3,882 thousand (it is contractually provided for that, if the funds are not drawn down completely within a certain date, the customers periodically pay these fees, normally calculated applying a percentage of the credit spread on the amount not drawn down);*

- *agency fees for an amount € 2,965 thousand. These fees are paid by customers for the role played by the Bank as lead manager / agent of loans in pools, for the administrative work related to sending and collecting instalments, to retrocession of collections pro-rata to the participants, to managing arrears but also and above all for the work of monitoring the covenants, annual analysis of accounting indices, etc..*

2.1.a Fee income: breakdown of fees for other services

Type of services / Balances	*31/12/2018*	*31/12/2017*
a) for early repayment/termination of loans and mortgage loans	585	1,246
b) fees for advisory services	16,462	12,232
c) fees for services	2,624	4,328
d) fees for securities lending	132	82
e) other	7,327	10,218
Total	**27,130**	**28,106**

Note:
The detail "e) other" refers mainly to enquiry and secretarial fees, fees for non or late use of the line granted, disinvestment charges and agency fees.

2.2 Fee income: distribution channels for products and services

Channels / Balances	*31/12/2018*	*31/12/2017*
a) **at Bank branches:**		
1. asset management		
2. placing of securities		
3. third-party services and products		
b) **door-to-door sales:**		
1. asset management		
2. placing of securities		
3. third-party services and products		
c) **other distribution channels:**		
1. asset management		
2. placing of securities	14,774	11,899
3. third-party services and products		

2.3 Fee expense: breakdown

Services / Balances	*31/12/2018*	*31/12/2017*
a) guarantees received	(112)	(197)
b) credit derivatives		
c) management and brokerage services:	(27,516)	(24,526)
1. financial instrument trading	*(18,027)*	*(20,414)*
2. foreign exchange trading	*(2)*	*(1)*
3. asset management:		
3.1. treasury portfolio		
3.2. portfolio of third parties		
4. custody and administration of securities	*(1,806)*	*(1,478)*
5. placing of financial instruments	*(7,681)*	*(2,633)*
6. external marketing of financial instruments, products and services		
d) collection and payment services	(10)	(11)
e) other services	(7,943)	(23,498)
Total	**(35,581)**	**(48,232)**

2.3.a Fee expense: breakdown of fees for other services

Type of services / Balances	*31/12/2018*	*31/12/2017*
a) presentation of loan applications	(4,424)	(4,292)
b) handling of non-performing loans	(1,505)	(12,775)
c) fees for securities lending	(142)	(87)
d) other	(1,871)	(6,344)
Total	**(7,942)**	**(23,498)**

SECTION 3 - DIVIDENDS AND SIMILAR INCOME - ITEM 70

3.1 Dividends and similar income: breakdown

Items / Income	*31/12/2018*		*31/12/2017*	
	Dividends	*Similar income*	*Dividends*	*Similar income*
A. Financial assets held for trading	723	407	1,573	303
B. Other financial assets obligatorily measured at fair value				
C. Financial assets measured at fair value through other comprehensive income			9	
D. Equity investments				
Total	**723**	**407**	**1,582**	**303**

Note:
In the comparative data the dividends of "Financial assets available for sale" were reallocated to item "C . Financial assets measured at fair value through other comprehensive income.

SECTION 4 - NET INCOME FROM TRADING ACTIVITIES - ITEM 80

4.1 Net income from trading activities: breakdown

Transactions / Income components	*Capital gains (A)*	*Trading gains (B)*	*Capital losses (C)*	*Trading losses (D)*	*Net profit (Loss) (A+B-C-D) 31/12/18*	*Net profit (Loss) (A+B-C-D) 31/12/17*
1. Financial assets held for trading						
1.1 Debt securities	30,598	89,939	(50,947)	(143,395)	**(73,805)**	**(12,581)**
1.2 Equity securities	464	2,820	(2,330)	(1,052)	**(98)**	**(1,205)**
1.3 UCITS Units	405	5,502	(1,621)	(9,078)	**(4,792)**	**(584)**
1.4 Loans						
1.5 Other						
2. Financial liabilities held for trading						
2.1 Debt securities	24,756	90,851	(20,963)	(15,973)	**78,671**	**33,427**
2.3 Payables						
2.2 Other	938	1,306	(3)	(67)	**2,174**	**544**
3. Financial assets and liabilities:						
- exchange differences					**6,281**	**(9,199)**
4. Derivative instruments						
4.1. Financial derivatives:						
- on debt securities and interest rates	589,783	2,039,105	(447,040)	(2,223,508)	**(41,660)**	**(18,576)**
- on equity securities and share indices	82,338	637,387	(54,530)	(640,192)	**25,003**	**18,537**
- on foreign currencies and gold					**23,471**	**18,453**
- other	29,759	166,376	(23,395)	(181,264)	**(8,524)**	**3,219**
4.2 Credit derivatives	7,994	181,901	(37,292)	(179,679)	**(27,076)**	**(13,964)**
of which: natural hedging connected with the fair value option						
Total	**767,035**	**3,215,187**	**(638,121)**	**(3,394,208)**	**(20,355)**	**18,071**

4.1.a Write-downs and trading losses attributable to assets of evident low credit quality

Transactions/Income components	*Write-downs*	*Trading losses*
Debt securities	661	148
Equity securities		
Derivatives	2,609	295
Other		
Total	**3,270**	**443**

SECTION 5 - NET INCOME FROM HEDGING ACTIVITIES - ITEM 90

During the last two financial years, no hedging operations were carried out.

SECTION 6 - PROFIT (LOSS) ON SALE/REPURCHASE - ITEM 100

6.1 Profit (Loss) on sale/repurchase: breakdown

Items / Income components	*31/12/2018*			*31/12/2017(*)*		
	Gains	*Losses*	*Net profit (Loss)*	*Gains*	*Losses*	*Net profit (Loss)*
Financial assets						
1. Financial assets measured at amortised cost	2,949	(3,080)	(131)	15,862	(15,854)	8
1.1 Receivables from banks					(188)	(188)
1.2 Receivables from customers	2,949	(3,080)	(131)	15,862	(15,666)	196
2. Financial assets measured at fair value through other comprehensive income	576		576	1,753	(165)	1,588
2.1 Debt securities	*576*		*576*	*1,753*	*(165)*	*1,588*
2.2 Loans						
Total assets	**3,525**	**(3,080)**	**445**	**17,615**	**(16,019)**	**1,596**
Financial liabilities measured at amortised cost						
1. Due to banks				6,825		6,825
2. Due to customers						
3. Outstanding securities						
Total liabilities				**6,825**		**6,825**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

SECTION 7 - NET GAINS (LOSSES) ON OTHER FINANCIAL ASSETS AND LIABILITIES MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS - ITEM 110

7.1 Net change in value of other financial assets and liabilities measured at fair value through profit or loss: breakdown of financial assets and liabilities designated at fair value

There were no transactions for this accounting item.

7.1.a Change in FV from own creditworthiness on FVO liabilities

There were no transactions for this accounting item.

7.2 Net change in value of other financial assets and liabilities measured at fair value through profit or loss: breakdown of other financial assets obligatorily measured at fair value

Transactions/Income components	*Capital gains (A)*	*Gains on disposal (B)*	*Capital losses (C)*	*Losses on disposal (D)*	*Net gains (losses) (A+B-C-D)*
1. Financial assets	12,744	3,204	(30,003)	(462)	**(14,517)**
1.1 Debt securities			(467)		**(467)**
1.2 Equity securities	10	3,204	(768)		**2,446**
1.3 UCITS Units			(2)		**(2)**
1.4 Loans	12,734		(28,766)	(462)	**(16,494)**
2. Financial assets in foreign currencies:					
Exchange differences					
Total	**12,744**	**3,204**	**(30,003)**	**(462)**	**(14,517)**

SECTION 8 - NET VALUE ADJUSTMENTS DUE TO CREDIT RISK - ITEM 130

8.1 Net value adjustments due to credit risk in relation to financial assets measured at amortised cost: breakdown

Transactions / Income components	*Value adjustments*			*Write-backs*		*Total*	
		Third stage					
	First and second stage	*Write-off*	*Other*	*First and second stage*	*Third stage*	*31/12/2018*	*31/12/2017(*)*
A. Receivables from Banks	(559)	0	0			(559)	(16)
- Loans	(559)					(559)	(16)
- Debt Securities							
B. Loans to customers	(256)	(317)	(224,135)	19,300	222,426	17,018	*(781,205)*
- Loans		*(317)*	(224,135)	19,300	222,426	17,274	(781,213)
- Debt Securities	(256)					(256)	8
of which purchased or originated credit impaired			*(360)*		*643*	283	
Total	(815)	(317)	(224,135)	19,300	222,426	16,459	(781,221)

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Nota:
Expected losses referable to operating loans in the scope of application of IFRS 15 are of an insignificant amount.

8.2 Net value adjustments due to credit risk in relation to financial assets measured at fair value through other comprehensive income: breakdown

Transactions / Income components	Value adjustments			Write-backs		Total	
		Third stage					
	First and second stage	Write-off	Other	First and second stage	Third stage	31/12/2018	31/12/2017(*)
A. Debt securities	(20)		(1,886)			(1,906)	(57,211)
B. Loans							
- To customers							
- To banks							
of which purchased or originated impaired financial assets							
Total	**(20)**		**(1,886)**			**(1,906)**	**(57,211)**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Nota:
in the comparative data "Equity securities" are included in "Debt securities"

SECTION 9 - GAINS/LOSSES ON CONTRACTUAL CHANGES WITHOUT CANCELLATIONS- ITEM 140

9.1 Gains (losses) on contractual changes: breakdown

Items/Income components	*31/12/2018*		
	Gains	*Losses*	*Net profit (Loss)*
1. Financial assets measured at amortised cost	443	(4,958)	(4,515)
2. Financial assets measured at fair value through other comprehensive income			
Total	**443**	**(4,958)**	**(4,515)**

SECTION 10 - ADMINISTRATIVE EXPENSES - ITEM 160

10.1 Personnel expense: breakdown

Type of cost /Values	*31/12/2018*	*31/12/2017*
1. Employees	**(40,795)**	**(42,387)**
a) wages and salaries	(28,775)	(29,185)
b) social security contributions	(7,611)	(7,772)
c) retirement indemnities	(1,168)	(1,190)
d) other pension costs		
e) provision for personnel severance indemnities	(22)	(41)
f) provision for pensions and similar obligations:	(445)	(453)
- defined contribution	*(425)*	*(432)*
- defined benefit	*(20)*	*(21)*
g) payments to external supplementary welfare funds		
- defined contribution		
- defined benefit		
h) costs deriving from payment agreements based on Parent Company equity instruments (stock granting)		
i) other employee benefits	(2,774)	(3,746)
2. Other working personnel		
3. Directors and Statutory Auditors	**(428)**	**(401)**
4. Retired personnel	**(33)**	**(32)**
5. Recovered expenses for employees seconded at other companies	**17,344**	**17,373**
6. Expense reimbursements for third party employees seconded at the Bank	**(4,661)**	**(5,266)**
Total	**(28,573)**	**(30,713)**

Nota:
The fees paid to Directors and Statutory Auditors, shown before contributions and tax expenses, are divided as follows: € 320 thousand to Directors (€ 282 thousand in 2017) and € 108 thousand to Statutory Auditors (€ 119 thousand in 2017).

10.2 Average number of employees by category

Employee categories / Average number	*31/12/2018*	*31/12/2017*
Employees	**319**	**339**
a) executives	21	20
b) managers	193	206
c) other personnel	105	113
Other personnel		
Total	**319**	**339**

10.3 Defined-benefit company pension funds: costs and revenue

Items / Balances	*31/12/2018*		
	Defined-benefit company pension funds		*Severance indemnities*
	Internal plans	*External plans*	
Interest income/expense	(20)		(22)
- welfare cost relating to current employment services			
- welfare cost relating to past employment services			
Gain/loss from discharge of fund			
Total	**(20)**		**(22)**

10.3.a Contributions to the Plan which the Bank estimates it will pay out in the next year

Items / Balances	*31/12/2018*	
	Defined-benefit company pension funds	*Severance indemnities*
1. Contributions to the Plan which the Bank estimates it will pay out in the next year	(25)	(25)

10.4 Other employee benefits

Nothing to report.

10.5 Other administrative expenses: breakdown

Items/Balances	*31/12/2018*	*31/12/2017*
1. substitute tax	(11)	-
2. municipal property tax	(104)	(103)
3. stamp duty	(469)	(1,076)
4. fee for DTAs	(6,165)	(6,165)
5. other taxation	(77)	(149)
6. rental of bank properties	(2,803)	(2,802)
7. fees for outside professionals	(3,304)	(11,962)
8. maintenance of furnishings and property used for business purposes	(484)	(620)
9. postal	(45)	(51)
10. telephone	(110)	(88)
11. advertising		
12. sundry rents and leasing	(6,816)	(7,316)
13. information and inquiries		(6)
14. transport	(189)	(216)
15. electricity, heating and water	(6)	(6)
16. surveillance	(4)	(4)
17. reimbursement of staff vehicle and travel costs	(275)	(310)
18. other staff costs	(860)	(971)
19. contracts for cleaning of premises	(150)	(163)
20 rental of data transmission lines	(54)	(54)
21. printed matter, stationery and consumables	(23)	(23)
22. insurance policies	(65)	(19)
23. services outsourced to Group companies	(16,514)	(17,021)
24. membership fees	(524)	(458)
25. entertaining expenses	(49)	(47)
26. subscriptions to publications	(14)	(16)
27. contributions to Resolution Funds and Deposit Guarantee Systems	(17,851)	(12,897)
28. sundry	(3,365)	(1,898)
Total	**(60,331)**	**(64,441)**

The decrease in “Other administrative expenses” is mostly attributable to the significant drop in fees for external professionals following the sale of non-performing loans completed on 22/6/2018 (€ -8,658 thousand), a decrease in part offset by the increase in contributions paid to the Resolution Fund (€ + 4,959 thousand).

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

11.1 Net Provisions for credit risk related to commitments to grant finance and financial guarantees given: breakdown

	First stage	*Second stage*	*Third stage*	*31/12/18*	*31/12/17 (*)*
Financial guarantees given	**791**	**874**	**947**	**2,612**	**10,634**
- provisions for the year	(15)		(346)	(361)	(817)
- write-backs	806	874	1,293	2,973	11,451
Irrevocable commitments to grant finance	**(152)**	**(907)**	**987**	**(72)**	
- provisions for the year	(248)	(907)		(1,155)	
- write-backs	96		987	1,083	
Total	**639**	**(33)**	**1,934**	**2,540**	**10,634**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

11.3 Net other provisions for risks and charges: breakdown

	31/12/2018			*31/12/2017*		
	Personnel expenses	*Legal disputes*	*Other*	*Personnel expenses*	*Legal disputes*	*Other*
1. Provisions for the year		(2,160)	(680)		(7,094)	
2. Write-backs		1,606			1,226	
Total		**(554)**	**(680)**		**(5,868)**	**0**

SECTION 12 - NET VALUE ADJUSTMENTS/WRITEBACKS ON PROPERTY, PLANT AND EQUIPMENT - ITEM 180

12.1 Net value adjustments on property, plant and equipment: breakdown

Assets / Income components	*Depreciation (A)*	*Value adjustments due to impairment (B)*	*Write-backs (C)*	*Net profit (loss) (A+B-C)*	
				31/12/18	*31/12/17*
A. Property, plant and equipment					
A.1 Owned by the Bank	(172)	(280)		(452)	(931)
- For business use	*(6)*			*(6)*	*(18)*
- For investment	*(166)*	*(280)*		*(446)*	*(913)*
- Inventories				*0*	
A.2 Acquired under financial lease					
- For business use					
- For investment					
Total	**(172)**	**(280)**		**(452)**	**(931)**

SECTION 13 - NET VALUE ADJUSTMENTS/WRITEBACKS ON INTANGIBLE ASSETS - ITEM 190

There were no transactions for this accounting item.

SECTION 14 - OTHER OPERATING INCOME/CHARGES - ITEM 200

14.1 Other operating charges: breakdown

Items / Balances	31/12/2018	31/12/2017
1. Amounts not receivable not attributable to own items	(2)	(42)
2. Out-of-period expense not attributable to own items	(13)	(25)
3. Depreciation of leasehold improvement costs classified among “Other assets”		()
4. Settlements paid for litigation	(307)	(1,032)
5. Other	(22)	(7)
Total	**(344)**	**(1,106)**

14.2 Other operating income: breakdown

Items / Balances	31/12/2018	31/12/2017
1. Amounts not payable not attributable to own items	16	
2. Out-of-period income not attributable to own items	52	8
3. Rental income from investment properties		
4. Other costs charged back	1,698	5,713
5. Other	1,267	1,754
Total	**3,033**	**7,475**

SECTION 15 - PROFIT (LOSS) FROM EQUITY INVESTMENTS - ITEM 220

15.1 Profit (loss) from equity investments: breakdown

Income components / Balances	*31/12/2018*	*31/12/2017*
A. Income		
1. Revaluations		
2. Gains on disposal		
3. Write-backs		
4. Other income		
B. Charges	**0**	**901**
1. Write-downs		
2. Value adjustments due to impairment		901
3. Losses on disposal		
4. Other charges		
Net profit (Loss)	**0**	**901**

Notes:
The value adjustment due to impairment recorded in 2017 is from measurement of the equity investment in Interporto Toscano A. Vespucci S.p.A.

SECTION 16 - NET RESULT FROM PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS AT FAIR VALUE - ITEM 230

There were no transactions for this accounting item.

SECTION 17 - VALUE ADJUSTMENTS TO GOODWILL - ITEM 240

There were no transactions for this accounting item.

SECTION 18 - GAINS (LOSSES) ON DISPOSAL OF INVESTMENTS - ITEM 250

There were no transactions for this accounting item.

SECTION 19 - INCOME TAXES FOR THE YEAR ON PROFIT FROM CURRENT OPERATIONS - ITEM 270

19.1 Income taxes for the year on profit from current operations: breakdown

	Components / Balances	*31/12/2018*	*31/12/2017*
1.	Current taxes (-)	(5,848)	163,191
	Current taxes, consolidated	14,408	
2.	Changes in current taxes for previous years (+/-)	629	
3.	Reduction in current taxes for the year (+)		
3.bis	Reduction in current taxes for the year for tax credits pursuant to Italian Law no. 214/2011 (+)		111,594
4.	Change in deferred tax assets (+/-)	34,434	(98,913)
5.	Change in deferred tax liabilities (+/-)	7	39
6.	**Taxes for the year (-)**	**43,630**	**175,911**

Note:
Financial year 2018.
Current IRES and IRAP taxes were not recognised because the two taxable bases were reduced to zero as a result, respectively, of the deduction of earlier tax losses and of the ACE portions accrued in financial years 2016 and 2017 (as regards IRES), as a result of the deduction of value adjustments on receivables accounted for and not deducted in the period 2008-2012 following the sale of receivables entitled "Valentine" (for IRAP).
The result of the probability test is recognised under the item "income for tax consolidation"; this determined a revaluation of the credit from the consolidator referred to the 2016 and 2017 tax losses.
The "change in deferred tax assets", as already described in the comment on table 13.3, comprises mainly the recognition of deferred tax assets on the deduction in the next nine financial years of the value adjustments on receivables that emerged on first application of IFRS 9, as well as the results of the probability test which entailed a write-down of deferred tax assets in relation to the IRES surcharge and to other temporary differences respectively for € 9,094 and 145 thousand.

Financial year 2017.
The tax loss led to the non-recognition of provisions for current taxes. In the presence of an IRES or IRAP tax loss the aggregate does not present provisions for current taxes. The "change in prepaid taxes" as already described in table 13.3, mainly includes recognition of prepaid taxes on non-transformable tax losses for € 26,206 thousand, the ACE subsidy of € 6,024 thousand and taxed provisions for risks and charges for € 3,054 thousand.
We can note that the probability test entailed the write-down from item 260:
- *of the income recognised on the tax loss of € 16,512 thousand;*
- *the increase in deferred tax assets relative to non-transformable tax losses for € 18,394 thousand.*

19.2 Reconciliation between the theoretical tax charge and the actual tax charge in the financial statements

IRES

Items / Balances	*31/12/2018*		*31/12/2017*	
	Amount	*%*	*Amount*	*%*
A. Profit (Loss) on current operations, before taxes	37,069		(808,849)	
B. Profit (Loss) on asset disposal groups held for sale before taxes				
Profit (Loss) before taxes (A+B)	**37,069**		**(808,849)**	
Theoretical tax charge - IRES taxes with application of the nominal rate	**10,194**	**27.50%**	**(222,433)**	**27.50%**
- Non-deductible interest expense				
- Exempt dividends			(2)	
- Capital gains and revaluations on exempt equity investments	(840)		(261)	
- Impairment on exempt equity investments	211		16,888	
- Non-deductible administrative expenses	351		492	
- Non-deductible contingencies	540		711	
- Tax losses for which recovery is not expected	(14,408)		16,512	
- AEG Deduction	(4,863)		(6,025)	
- Value adjustments for deferred taxes from previous years			18,393	
- Changes in current IRES taxes for previous years				
- Other permanent differences	(41,085)		(219)	
Total permanent differences	**(60,094)**		**46,489**	
- Value adjustments for deferred taxes from previous years	8,680			
- Changes in current IRES taxes for previous years	(629)			
IRAP in income statement	**(1,781)**			
IRES taxation to income statement	**(43,630)**		**(175,944)**	
of which:				
- Income taxes for the year from current operations	(43,630)		(175,944)	
- Income taxes for the year of asset disposal groups held for sale				

IRAP

Items / Balances	*31/12/2018*		*31/12/2017*	
	Amount	*%*	*Amount*	*%*
A. Profit (Loss) on current operations, before taxes	37,069		(808,849)	
B. Profit (Loss) on asset disposal groups held for sale before taxes				
Profit (Loss) before taxes (A+B)	**37,069**		**(808,849)**	
Theoretical tax charge - IRAP taxes with application of the nominal rate	**1,724**	**4.65%**	**(37,611)**	**4.65%**
- Non-deductible interest expense				
- Net value adjustments on receivables			2,660	
- Gains/losses on contractual changes without cancellations	210			
- Net value adjustments for other financial transactions			494	
- Personnel expenses	41		53	
- Allocations to provision for risks and charges	(61)		203	
- Losses on equity investments			42	
- Lump sum recovery of administrative expenses	280		300	
- Sundry non-deductible administrative expenses	48		74	
- Lump sum recovery of amortisation/depreciation	21		43	
- Other non-significant operating income/charges	(52)		(50)	
- Other increases	4,882			
- Dividends excluded	(17)		(51)	
- Tax rate increases implemented by regions			(6,714)	
- Non-reportability of tax loss			40,760	
- 2008-2012 adjustments on loans subject to disposal				
- Other decreases	(8,563)		(170)	
Total permanent differences	**(3,211)**		**37,644**	
- Tax rate increases implemented by regions	(294)			
IRAP taxation to income statement	**(1,781)**		**33**	
of which:				
- Income taxes for the year from current operations	(1,781)		33	
- Income taxes for the year of asset disposal groups held for sale				

SECTION 20 - GAIN (LOSS) ON DISCONTINUED OPERATIONS, NET OF TAXES - ITEM 290

There were no transactions for this accounting item.

SECTION 21 - OTHER INFORMATION

Nothing to report.

SECTION 22 - EARNINGS PER SHARE

22.1 Average number of ordinary shares in diluted capital

(number of shares)

Items / Balances	31/12/2018	31/12/2017
1. Weighted average of ordinary shares outstanding (+)	802,551	802,551
2. Diluting effect deriving from put options sold (+)		
3. Diluting effect deriving from ordinary shares to be assigned as the result of share-based payments		
4. Diluting effect deriving from convertible liabilities (+)		
Weighted average of ordinary shares outstanding for diluted earnings per share	**802,551**	**802,551**

22.2 Other information

22.2.a Reconciliation of profit (loss) for the period - basic earnings per share numerator

(amounts in Euro)

Items / Balances	31/12/2018	31/12/2017
1. Net profit (Loss)	80,699,465	(632,937,398)
2. Profit (loss) attributable to other categories of shares		
Net profit (loss) attributable to ordinary shares - basic earnings per share numerator	**80,699,465**	**(632,937,398)**

21.2.b Net profit (loss) reconciliation - diluted earnings per share numerator

(amounts in Euro)

Items / Balances	31/12/2018	31/12/2017
1. Net profit (Loss)	80,699,465	(632,937,398)
2. Profit (loss) attributable to other categories of shares		
3. Interest expense on convertible instruments (+)		
4. Others (+/-)		
Net profit attributable to ordinary shares - diluted earnings per share numerator	**80,699,465**	**(632,937,398)**

21.2.c Basic and diluted earnings per share

(amounts in Euro)

Items / Balances	31/12/2018	31/12/2017
1. Basic earnings per share	100.554	(788.657)
2. Diluted earnings per share	100.554	(788.657)

Part D
Comprehensive Income

ANALYTICAL STATEMENT OF COMPREHENSIVE INCOME

	Items	*31/12/2018*	*31/12/2017*
10.	**Profit (Loss) for the period**	**80,699**	**(632,938)**
	Other income components without transfer to income statement	**(35,917)**	**67**
20.	Equity securities designated at fair value through other comprehensive income:	(35,950)	
	a) fair value change	(35,950)	
	b) transfers to other shareholders' equity components		
30.	Financial liabilities designated at fair value through profit or loss (changes in own creditworthiness)		
	a) fair value change		
	b) transfers to other shareholders' equity components		
40.	Hedging of equity securities designated at fair value through other comprehensive income:		
	a) fair value change (hedged instrument)		
	b) fair value change (hedging instrument)		
50.	Property, plant and equipment		
60.	Intangible assets		
70.	Defined benefit plans	50	(13)
80.	Non-current assets and disposal groups held for sale		
90.	Portion of equity investment valuation reserves measured at equity		
100.	Income tax expense related to other comprehensive income without transfer to income statement	(17)	80
	Other comprehensive income with transfer to income statement	**(1,872)**	**(147)**
110.	Foreign investment hedging:		
	a) fair value changes		
	b) transfer to income statement		
	c) other changes		
120.	Exchange differences:		
	a) fair value changes		
	b) transfer to income statement		
	c) other changes		
130.	Cash flow hedging:		
	a) fair value changes		
	b) transfer to income statement		
	c) other changes of which: result of net positions		
140.	Hedging instruments (undesignated elements):		
	a) changes in value		
	b) transfer to income statement		
	c) other changes		
150.	Financial assets (other than equity securities) measured at fair value through other comprehensive income:	(2,582)	(26)
	a) fair value changes	(5,032)	(59,715)
	b) transfer to income statement	2,450	59,689
	- adjustments for credit risk	*2,450*	*60,511*

	- gains/losses on disposal		*(822)*
	c) other changes		
160.	Non-current assets held for sale and discontinued operations:		
	a) fair value changes		
	b) transfer to income statement		
	c) other changes		
170.	Portion of equity investment valuation reserves measured at equity		
	a) fair value changes		
	b) transfer to income statement		
	- writedowns for impairment		
	- gains/losses on disposal		
	c) other changes		
180.	Income tax expense related to other comprehensive income with transfer to income statement	710	(121)
190.	**Total other income components**	**(37,789)**	**(80)**
200.	**Comprehensive income (Item 10+190)**	**42,910**	**(633,018)**

Part E
Information on Risks and Related Hedging Policies

Introduction

The organisational model on which the Internal Controls System is based provides for outsourcing to the Parent Company of the Risk Management Unit, in observance of the specific rules laid down in the corporate policy on the subject of outsourcing of the corporate auditing units within the banking Group and in a specific SLA signed with the Parent Company. Therefore, the Bank's Board of Directors, in keeping with the provisions laid down by the Supervisory Authorities and with the consent of the Board of Statutory Auditors, assigned responsibility for the unit to the Parent Company's *pro-tempore* Chief Risk Officer.

The internal contact point for the Risk Management activities is identified as the Manager of the AML and Risk Contact Point Unit for the Bank, responsible for:

- guaranteeing a constant connection between the Bank and the outsourced Risk Management unit;
- providing his or her support to the outsourced Risk Management unit;
- reporting to the Risk Management unit, on the basis of the available information, particular events or situations capable of modifying the risks generated by the Bank.

The organisation of the MPS Group's risk governance, the related processes and the key units involved are illustrated briefly below. An estimate of the Bank's Total Internal Capital at 31 December 2018 is also provided.

For more information on Risk Governance and the risk culture in the bank please see the Report on Operations.

Risk governance system

The risk governance system adopted by the Group features a clear distinction of roles and responsibilities between the first, second and third level control functions.

The policies regarding the assumption, management, hedging, monitoring and control of risks are defined by the Parent Company's statutory bodies. Specifically:

- the Board of Directors of the Parent Company defines and approves the strategic guidelines and risk governance policies and, at least once a year, expresses in numeric terms, the Group's total level of risk appetite;
- the Board of Statutory Auditors and the Risks Committee assess the level of efficiency and adequacy of the internal control system, specifically regarding control of risks;
- the Managing Director/General Manager guarantees compliance with the risk policies and procedures;
- the Director assigned responsibility for the internal control and risk management system, established in accordance with the Code of Conduct for Listed Companies, is responsible for establishing and maintaining an effective system of internal control and risk management.

In order to support efficiency and flexibility in the decision-making process and to smooth interaction between the various corporate departments involved, specific Management Committees exist, which are responsible for risks:

- the Risk Management Committee establishes the risk management policies, assesses the Group's risk appetite, in accordance with the annual and multi-annual targets for value creation for the Group and verifies and monitors overall observance of the limits assigned to the various levels of operations; evaluates, at a comprehensive level and at the level of individual companies, the risk profile achieved and hence capital consumption;
- the Finance and Liquidity Committee formulates the principles and strategic guidelines for proprietary finance; resolves and puts forward proposals regarding exposure to interest rate risk and liquidity in the banking book and to define capital management actions;
- the Credit and Credit Policies Committee expresses guidelines regarding lending processes and an opinion on credit policies at least once per year, verifying commercial sustainability and compliance with the Risk Appetite, and approves the corporate "Credit Assessment" policies at least once a year. In addition, it has the responsibility, on

the basis of the delegated powers, to resolve on the subject of loan disbursement and loan management and problem assets.

In the context of the Internal Control System, the Chief Audit Executive Department carries out third level controls, while the Chief Risk Officer Department and the Compliance Area are responsible for second level controls and the Business Control Units (BCUs) for the first level controls. In more detail:

- the Chief Audit Executive Department carries out independent and objective assurance and advisory activities aimed on one hand to check, also with on-site tests, the regularity of operations and risk performance and, on the other hand, to assess the functionality of the overall internal control system, also in order to pursue the improvement of the effectiveness and efficiency of the organisation. It also plays the role of Internal Secondary Supervisor with the objective of focussing on the main characteristics of the prudential supervision process adopted by the European supervisory authorities and the guidelines/priorities that it outlines on occasion, in order to evaluate the Group's positioning with respect to the expectations of the Single supervisory mechanism;
- the Chief Risk Officer Department, reporting directly to the Board of Directors and reporting functionally to the Managing Director, includes the risk management unit, the anti-money laundering unit and the internal validation unit. The Department is therefore responsible for:
  - guaranteeing the overall functioning of the risk management system;
  - participating in defining the performance check on the Risk Appetite Framework (RAF), besides guaranteeing the consistency with the RAF of the most significant operations;
  - verifying capital adequacy in the context of the ICAAP process and the adequacy of liquidity in the context of the ILAAP process;
  - monitoring the indicators of the Recovery Plan;
  - ensuring the necessary reporting to the Group's decision-making bodies and top management.
  - guaranteeing proper and adequate auditing activity to Group companies that have outsourced the relevant corporate unit.
  - defining strategic policies on the credit portfolio;
  - performing the anti-money laundering function provided for by the Law and that of internal validation of the risk management models;
  - guaranteeing proper and adequate auditing activity to Group companies that have outsourced the relevant corporate unit.
  - overseeing in a centralised manner the management of relations and the moments of verification with the Supervisory Authorities, coordinating and monitoring the planning of the commitments assumed and the main lines of evolution of the European regulatory context.
  - checking and validating continuously the reliability of the results of the risk measurement systems and the maintenance of their consistency with the legislative prescriptions

In particular, within the Chief Risk Officer Department, the structures of the risk control unit are:

- the Financial Risk Officer Area. This defines the integrated methods for assessing and analysing risks and ensures that they are constantly monitored, verifying their consistency with the Risk Appetite and observance of the threshold defined in terms of adequacy with respect to the capital and liquidity reserves, and participating in the definition of any mitigation actions required. It collaborates in the preparation, drafting and monitoring of the Recovery Plan. It supervises the evolution of the proprietary financial risk measurement and control system, in line with internal and regulatory standards. It guarantees management risk reporting for company bodies and top management.
- the Lending Risk Officer Area. this supervises the evolution of the credit risk measurement system, in line with internal and regulatory standards, both in terms of statistical models and analytical and process measurements, monitoring measurement of the credit risk relative portfolio quality down to the single name level. They perform

second level controls on Group credit exposures.
- the Operating Risk Officer Area. this supervises the evolution of the risk measurement and control system associated with the operational execution of the Group's business model (including operational risk, reputational risk, business model risk and risks associated with customer portfolios);

• the Compliance Area performs the function of controlling conformity with the laws for the Banking Parent Company. The unit has the direct responsibility for managing the risks related to breaches of the most significant laws in bank-customer relations and reports periodically to the top management bodies and to the supervisory authorities on the overall compliance status of the Bank’s systems and operations. The Compliance Unit reports directly to the Managing Director;
• the peripheral BCUs, located at the subsidiary banks or the main business areas, implement compliance checks on operations and represent the first level of organisational control of operations within the more general Internal Control System.

While observing the autonomy and independence requirements of each participating unit, the Committee for Coordination of the Units also operates with auditing tasks. The Committee has the aim of promoting and sharing operating and methodological aspects to identify possible synergies in the auditing activities by the second and third level Units, coordinating the methods and timing on the subject of planning and reporting to the Corporate Bodies and of planning initiatives connected with the Internal Control System, sharing the areas for improvement highlighted by all the Units with auditing tasks and by the Supervisory Authorities.

Autonomy and independence requirements of the Risk Control Unit
The Parent Company’s Risk Control Unit is headed by the Chief Risk Officer (CRO).
Autonomy and independence are ensured by direct reporting with the Collegial Body with strategic supervision functions (the Board of Directors), and only functionally with the Management (Managing Director/General Manager). It has direct access to the control body (Board of Statutory Auditors), and can communicate with it continuously without restrictions or liaisons. The CRO also has the right at its discretion to take part in the meetings of the Risks Committee to intervene or propose discussions on specific matters.
In particular the Manager of the Parent Company’s Chief Risk Officer is appointed/dismissed by the Board of Directors, on the proposal of the Risks Committee, making use of the contribution of the Appointments Committee, after consulting the Board of Statutory Auditors.
The determination of the remuneration of the Parent Company’s Chief Risk Officer is resolved by the Board of Directors, on the proposal of the Remuneration Committee, acquiring the opinion of the Risks Committee, after consulting the Board of Statutory Auditors.

Activities related to the International Supervisory Legislation
First pillar: since 2008, the Group has used internal models validated by the Bank of Italy to assess and manage credit risks (AIRB - Advanced Internal Rating Based) and operational risks (AMA - Advanced Measurement Approach). Over time, in agreement with the Supervisory Authority, these models have been further developed and their scope of application has been extended to Group entities not included in the initial validation perimeter.

Second pillar: in the year in particular the initiatives continued aimed at guaranteeing compliance with the new Supervisory Review and Evaluation Process (SREP) framework and at improving further the self-assessment processes regarding the Group’s capital and Liquidity adequacy (ICAAP - Internal Capital Adequacy Assessment Process and ILAAP - Internal Liquidity Adequacy Assessment Process) of which obligatory disclosure is provided to the Supervisors.

During 2018, the overall internal framework of reference for determining the Group's risk appetite developed further (the Risk Appetite Framework - RAF). The Group was also involved in various projects aimed at improving the management systems for various risks.
Third pillar: the related Market Disclosure is released quarterly on the Group's website, at www.mps.it/investors and is updated continuously in compliance with the regulatory developments on the subject.

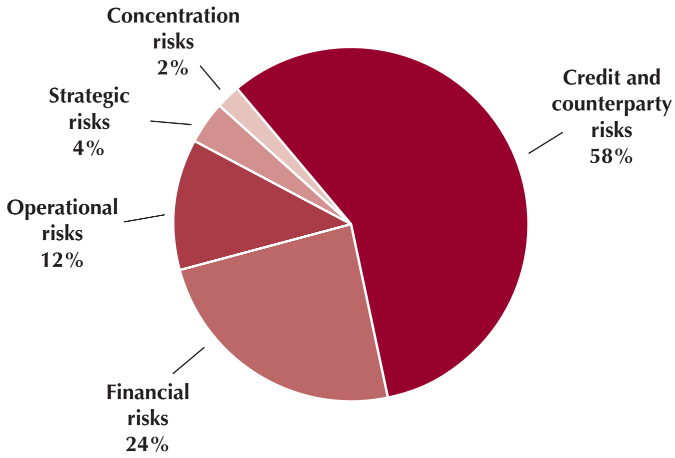
Analysis of Internal Capital
The Total Internal Capital (or Total Absorbed Internal Capital) is the minimum operational amount of capital required to cover economic losses due to unexpected events generated by simultaneous exposure to various types of risk.

The main types of risk to which the Group and, within it, the Bank is exposed during its normal business activities, can be schematically classified as follows:
• credit risk;
• market risk;
• operational risk;
• Banking Book interest rate risk;
• counterparty risk;
• property risk;
• issuer risk;
• concentration risk;
• equity investment portfolio risk;
• business/strategic risk
• liquidity risk;
• reputational risk.
The Total Internal Capital is quantified based on all the above types of risks, with the exception of liquidity risk and of reputational risk, which instead are mitigated through policies and organisational processes.
Protection is also put in place against the risks inherent in investment products/services designed for the Group's customers, both to protect the customers and to prevent potential impact on the Group's reputation.

Measurement models:
The Financial Risk Officer Area quantifies Internal Capital (in terms of Internal RWA equivalent) on a regular basis in relation to each risk type and periodically reports to the Risk Management Committee and the Top Management in the context of the informational flows prepared by the Chief Risk Officer Department.
The approach used for quantifying the risks-to-capital, to which the Group and, within it, the Bank is exposed, is what in the literature is called Pillar 1 Plus. This approach entails that, to the Pillar 1 requirements for Credit and Counterparty Risk (which already include the requirements related to Issuer Risk on the Banking Book (BB), Equity Investment Risk, Property Risk) and for Operational Risk, are added the requirements calculated using internal models related to Market Risks of both the Trading Book and the Banking Book and Banking Book Interest Rate Risk (Financial Risks), Concentration Risk and Business/Strategic Risk.

The Total Internal Capital is calculated without considering the inter-risk diversification, directly adding together therefore the contributions of internal capital for the individual risks (Building Block Approach). This approach tends to assimilate the indications present in the SREP (Supervisory Review and Evaluation Process) Guidelines published by the EBA.

TOTAL INTERNAL CAPITAL
MPS CAPITAL SERVICES - 31.12.2018



The MPS Group also continually manages and quantifies Liquidity Risk (risks-to-liquidity, as defined in the SREP Guidelines) using internal methodologies and policies of an organisational nature.

SECTION 1 - CREDIT RISK

QUALITATIVE INFORMATION

1. General aspects

The Bank, in the context of its strategic priorities set by the Parent Company's Business Plan, continues to pursue the improvement of the quality of its loan portfolio with the objective of limiting the cost of credit.
The Parent Company's Chief Lending Officer Department defines annually, with possible revision every six months, the strategic guidelines related to the loan portfolio, both at the Group level and at the level of the single subsidiaries. The Group's lending is managed with a view to risk oversight and taking advantage of opportunities for growth. The lending policies and management systems developed aim to make use of trend-related information at the level of the individual relationship, and are characterised by deep awareness and strategic management of the position (credit culture).
The main elements that contribute to the definition of the lending policy can be summarised briefly as:
- internal rating system;
- sectoral classification;
- geographical area of location;
- service models usable (retail, corporate e private).

Already back in 2008, the MPS Group received from the Bank of Italy the authorisation for the use of the advanced internal approaches for determining the capital requirements against credit risk (AIRB - Advanced Internal Rating Based approach). The Bank uses the internal estimates of the probability of default (PD) and the loss given default (LGD) for the loan portfolio, relating to the exposures towards businesses.
The internal PD, LGD and EAD models for measuring credit risk represent one of the main elements of assessment for all the Group's structures involved in the lending industry.
To make the valuation of the legal-economic links objective and unequivocal, within the MPS Group, a customised process entitled "Associated Customer Groups" is now operational; it makes it possible to establish and up-date the mapping of the afore-mentioned links by means of the application of automatic process rules which handled the objective data which can be gathered from internal and external official sources.

2. Credit risk management policies

2.1. Organisational aspects

2.1.1 Organisational aspects: banking book

The Bank carries out medium- and long-term lending related to extraordinary enterprise finance and corporate finance, in all its technical forms, directed at the growth of the manufacturing and production sectors. In some cases, a subsidised loan is arranged, although only in a remaining few cases since public aid is limited to a few research and industrialisation projects.
New finance operations are also agreed in the context of agreements for the restructuring of pre-existing debts.

Evaluation of creditworthiness, to supervise the risk assumed, is carried out both through an analysis of the repayment sources on the basis of income and cash production capacity (former, current and prospective), and as a function of the specific features of the project financed (competitive positioning, management quality, quality and quantity of equity and financial resources available, and equity capacity of the shareholders). Generally, real guarantees are acquired (mortgages, privileges, liens) and/or unsecured guarantees (sureties, letters of patronage) in order to mitigate risk and reduce capital absorption.
Loans are classified in categories of different risk intensity on which the lending decision autonomy limits of the lower level delegated bodies are parametrised. These limits are increased or decreased depending on the rating attributed to the counterparty. The Bank, in fact, assesses its customers through the system of ratings attributed by the Parent Company.
In relation to the process of attributing the project rating (activated in May 2009) for the "Specialised Lending" operations specifically identified as IPRE (Income Producing Real Estate), Project Finance or Object Finance, we can note that the Bank of Italy authorised the Monte dei Paschi di Siena Group to use the Regulatory Classification approach (the so-called "Slotting Criteria") for specialised lending with exposure of € 5 million or more. Transactions for an amount of less than € 5 million are instead assessed according to the ordinary process and reported with the standard method.

The lending activity also involves granting credit lines for derivative transactions, aimed at limiting the exposure of the contracting parties (Corporate customers) to market risks (interest and exchange rates and commodities).

The General Management of the Bank, in keeping with the guidance issued by the Chief Lending Officer Department of the Parent Company, establishes the criteria and methods for monitoring the portfolio, on an on-going basis making the best possible use of information about the credit facility positions, which is made available within the banking Group.
As a result of the introduction of the new general principles contained in the 7th update of Bank of Italy Circular 272, the Bank transposed the new Policy on the subject of Loan classification and measurement (cf. paragraph 3. Impaired loan exposures) below.
At the organisational structure level, the Loan Division carries out the activity described above with the Bank's competent organisations, represented by:

- Loan Department Staff which, besides the task of supporting the other structures of the Department itself, is responsible for:
  - coordinating the loan monitoring activity, according to the principles contained in the "Group Policy on Loan Classification and Measurement";
  - performing rating review activities for the Bank's exclusive customers and requesting reviews from the competent Parent Company structures for shared customers;
  - monitoring the project rating review activity;
- Credit Assessment Office, responsible for the activities summarised below:
  - assessing the creditworthiness of institutional and financial counterparties for the concession of specific credit lines;
  - assessing the creditworthiness of corporate counterparties for the concession of credit lines of a financial nature;
  - deciding the project rating, through validation of the "Specialized Lending" questionnaire with related periodical rating reviews. The decisions are completed by validating the specific section of the BI-PEF application (Banca Impresa Pratica Elettronica di Fido - Corporate Bank Electronic Credit File) inserted into the enquiry model in use;
  - preparing technical opinions, by the Proposals Review and Loans Sector, for all new loan proposals and changes in already approved credit operations, investigated by various functions in the Credit Department, with decision-making powers external to the Corporate Finance Department;

- deciding on loan proposals falling under its powers and proposing them, also for those received from other Departments, to higher bodies;
• Performing Portfolio Management Office which performs the following activities:
• assessing all the proposed changes related to ordinary finance operations in amortisation, as well as monitoring the correct classification of the performing positions according to the principles contained in the "Group Policy on Loan Classification and Measurement";
• examining applications for loans from employees;
• monitoring the guarantees backing loan operations;
• coordinating the activity of updating of the valuation of properties acquired as collateral;
• following, in relation to the activities performed in the context of the Lending Department, the operating formalities connected with combating money-laundering and the Bank's reference point on the subject of the General Customer Database;
• Non-Performing Portfolio Management Office, responsible for monitoring anomalous credit according to the principles contained in the "Group Policy on Loan Classification and Measurement", undertakes the most opportune initiatives in the related management as better specified below.

The above topics are analytically regulated by specific corporate standards.

2.1.2 Organisational aspects: trading book

The assessment of market counterparties for transactions involving financial instruments carried out by the Global Markets Department, is the responsibility of the Credit Assessment Office - Counterparty Assessment Service. Usually, market counterparties are regulated intermediaries, such as banks, EMIs (Electronic Money Institutions), investment firms, financial firms (pursuant to Art. 107 of the Consolidated Finance Act), AMCs, SICAVs, Italian and foreign-law Funds, insurance companies, as well as territorial, governmental and supranational agencies; some of these economic entities have a rating attributed by important international agencies.
The acceptance process requires a resolution by the Parent Company MPS regarding the "country risk" assigned to the Bank which, in compliance with this limit, independently approves credit lines. The Counterparty Assessment Service is tasked with carrying out all stages of the lending process through the applicant business units, from collecting the necessary documentation to the initial investigation review from the assessment of creditworthiness to the loan proposal.
The credit granted is of a dynamic nature, that is it can be used up to the total limit for operations of a financial nature, in its various technical forms and among the various companies related to a single Group, if not otherwise indicated at the moment of acceptance. In order to absorb the total counterparty risk, the Parent Company's Risk Management Unit identifies the calculation algorithms differentiated in relation to the different financial nature of the operations.
The Counterparty Assessment Service, also on the basis of the operating needs expressed by the Front Office units, periodically reviews and revises the creditworthiness of the borrower counterparties. If anomalous situations emerge, the Service proceeds with an extraordinary revision of the position and/or, if necessary, immediately applies an appropriate reduction in its amount. Each revision is immediately notified to the involved corporate functions.
Every six months the Counterparty Assessment Service produces a report for the Board of Directors concerning exposure to counterparty risk, indicating i) the trend of the credit line/utilisation ratio, the risk concentration, the guarantees and the quality of the risk; ii) the record of overdrafts related to the credit lines granted, together with comments on the causes and nature of the overdrafts; iii) the counterparties provided with credit lines and the record of pre-lending investigations, the situation of collaterals and of the country risk.
The Parent Company MPS is informed with updates on loans granted to counterparties and the related utilisations, by feeding a dedicated application (Zeta limit), in accordance with the directives issued by the same.

Regarding operational controls, the Counterparty Assessment Service oversees compliance with the total credit limit granted and assures the correct distribution of uses dynamically; it makes the checks on the exact allocation of the credit granted and on the record of its use; it monitors daily the over-the-limit positions - in terms of amount and duration - reporting the irregularities noted to the top management and the Internal Audit Office.
Monitoring takes place through the Murex3 application, which is able to reflect the effects of the transactions made, in real time. The operating limits granted and the utilisations referred to individual market counterparties are analysed using the MLC extension of the Murex3 application.

2.2 Management, measurement and control systems

The statistical models aimed at creating the Internal Rating Model and the attribution processes obtained, already back in 2008, the authorisation of the Supervisory Authority for calculating the capital requirements with the Advanced IRB (AIRB) System.
The prudential regulations require the Group and the Bank to adopt credit risk measures necessary for calculating Regulatory Capital (AIRB approach): Probability of Default (PD), Loss Given Default (LGD) and Exposure At Default (EAD). The “Probability of Default”, expressed by the rating, represents the ability to fulfil the commitments assumed over the time horizon of one year. The rating presupposes, therefore, a probabilistic approach to risk assessment, measures the quality of the portfolio from a predictive viewpoint entering into the daily credit assessment, credit management and pricing processes, into the provision methodologies and into the reporting to the management.
The regulatory endowment of the risk parameters has enabled the Group and the Bank to obtain important operating benefits in terms of both greater accuracy of forecast estimates related to credit, and greater control of lending aggregates: on the basis of the risk parameters, in fact, the Group - also for the Bank - sets up the process of annual planning of the figures related to lending items, arriving at accurate and sustainable estimates regarding the composition of the loan portfolio, the probable default and bad loan flows and the amount of adjustments. The sustainability of the estimates is ensured by arranging concrete actions on the loan portfolio, which are discussed with the subsidiaries and implemented in collaboration with them.

All the lending processes use the counterparty rating as decision-making driver and are designed according to the specific features of the different customer segments, in order to optimise the use of the resources invested in the management/monitoring of credit and to achieve the right balance between commercial thrust and effectiveness of the credit management. The internal ratings system, which at the Group level involves the Corporate and Retail portfolios, arises from the development of statistical models specialised for the type of customer aimed at attributing a solvency grade both for prospective counterparties (first disbursement models based on financial and socio-demographic information, and information coming from external databases) and for already existing counterparties (for which behavioural models that use internal performance data have been used).
In order to increase the levels of efficiency in the management of the Internal Rating, the internal Rating Agencies located around the country have become the only reference point for any business unit on the subject of Ratings. The role of the Agencies enables greater interaction with the Network so as to make more effective the assistance activity, generate better synergy and enable a more effective transfer of knowledge.
The prudential supervisory rules for banks, in line with the indications of the Basel Committee guidelines and the best practices, envisage that credit institutions carry out appropriate stress testing.
The Parent Company units responsible conduct stress tests regularly on all risk factors. Stress tests make it possible to assess the ability of the Group and of the Bank to absorb sizeable potential losses upon the occurrence of extreme but plausible market events, in order to identify the measures to take to reduce the risk profile and preserve the capital.

Stress tests are developed on the basis of historical and discretionary scenarios:

- historical scenarios: shocks are hypothesized for a combination of risk factors observed in the past, which continue to have a certain degree of relevance and repeatability;
- discretionary scenarios: shocks are hypothesized for a combination of risk factors that could occur in the near future, in relation to the foreseeable environmental, social and economic context. The discretionary stress scenarios currently examined are simple (only one risk factor changes) and joint (several risk factors change simultaneously). Simple discretionary scenarios are calibrated to hit independently one category of risk factors at a time, hypothesising that the shocks will not propagate to the other factors. Joint discretionary scenarios instead are aimed at evaluating the impact of global shocks that simultaneously hit all types of risk factors.

The MPS Group's methodological approach to stress tests is based on the identification of the main risk factors, with the objective being the selection of events and combinations of events (scenarios) that highlight special vulnerabilities at the Group level. To this end, specific stress test plans have been established regarding the First Pillar risks (credit, market and operating) which were then combined - together with a given stress designed ad hoc with the other risk factors - in an overall Second Pillar stress test, aimed at determining the potential impact on the Group, in the context of the ICAAP process.
Specifically, as regards Credit Risk, the MPS Group has defined a regressive macro-economic model to estimate changes in Probabilities of Default (PDs), as a function of the main credit drivers.
Initially, the credit drivers that explain variations in PD in a significant manner are identified. Then, on the basis of the regressive model, disturbances in the credit drivers are estimated, in line with the current and prospective economic situation. This shock to the credit drivers determines the change in the PDs of the credit portfolio, triggering the simulation of a hypothetical downgrading of counterparties, with the consequent variation of risk in terms of Expected Loss, Unexpected Loss and the entry of new defaults.
The results of the stress tests are brought to the attention of Top Management and the Parent Company's Board of Directors. This latter body formally examines them in the context of the approval of the Annual ICAAP Report, with an eye to self-assessing the current and prospective capital adequacy of the MPS Group.

2.3 Methods of measuring expected losses

Analysis of the credit risk is carried out internally for operating purposes by means of the Loan Portfolio Model developed internally by the Parent Company; as analytical output it produces the classic risk measurements of the Expected Loss and Unexpected Loss, both operating (diversified intra-risk, with a time frame of one year and a confidence interval calibrated to the target rating of the Group itself) and regulatory. The inputs are numerous: probability of default (PD), obtained using validated and non-validated models, operating and regulatory loss given default (LGD) rates, number and type of guarantees that back the single lending relationships, regulatory and operating Credit Conversion Factors (CCFs) on the basis of which, respectively, the regulatory and operating EAD (Exposure At Default) is estimated.
The internal PD, LGD, and EAD models for credit risk measurement represent one of the main assessment elements used for all the Group structures involved in the credit industry, both central (Risk Management, Credit Department, CFO, General Management, Risk Committee, Board of Directors) and peripheral (Ratings Agencies and Account Managers). Currently the Group is authorised to use Advanced Internal Rating-Based (AIRB) systems for the determination of capital requirements in the face of credit risk for business portfolios and exposures to retail customers of the Parent Company, of MPS Capital Services, and of MPS Leasing & Factoring, and is awaiting validation for these counterparties of the EAD parameter and the roll-out of the domestic NBFI portfolio.

To develop the internal rating systems, rigorous advanced statistical methods have been used, in compliance with the requirements envisaged in the supervisory regulations. At the same time, models have been selected so that the results

obtained are in line with the historical experience of the Bank and the Group in credit management. Finally, in order to optimise proper use of the new instruments, the rating models have been shared in a top-down manner - from Risk Management down to the individual customer managers. In the loss rate model estimate, internal evidence related to capital flows, recoveries, and expense effectively recorded for past non-performing loans have been used. The results obtained from the model are subsequently compared with that observed by the Credit Recovery Area which, within the Parent Company's Credit Department, is dedicated to managing and recovering non-performing loans.
The main features of the advanced rating systems are illustrated below:

- the rating for all validated regulatory portfolios is calculated using a counterparty approach, in line with management practices that envisage credit risk assessment, both during disbursement and monitoring stages, at the level of the individual borrower;
- the rating is based on a Group logic: each individual counterparty is attributed a single rating at the banking Group level, on the foundation of the information set relative to all the lending Banks within the AIRB perimeter. The LGD is distinct for the different companies, due to the variation in the products disbursed and the type of customers to which they are offered;
- segmentation of the rating models has been defined so as to make the individual model clusters align with the commercial logics, credit process logics and the regulatory portfolios envisaged by law;
- the final ratings determination varies by counterparty type. The credit process involves a level of study proportional to the risk associated with the counterparty: the assessment of loans granted has a complex articulated structure for medium-large corporate counterparties, with larger exposure and concentration risks, and a simplified structure for Small Business - SB - and Retail customers;
- in line with the process, the final rating for SME and LC companies is determined through a combination of several components: statistical rating, qualitative rating, override faculty, and evaluation of the economic group to which it belongs; for SB and Retail counterparties, instead, the rating is determined solely on the basis of the statistical component;
- the rating has an internal validity of 12 months and is normally reviewed once a year, except in the case of rating reviews that follow highly structured and codified rules or that are brought forward on the initiative of the account manager or following serious impairment of the counterparty.
- the LGD rate refers to economic losses recorded and not only accounting losses; for this reason, costs incurred during the recovery process and the time factor are also included in the estimate stage;
- the loss given default (LGD) rate is distinct for the various types of financing and the attribution occurs at the level of the individual operations; it is differentiated by geographical area, as different recovery rates have been encountered, over time and currently, between Northern and Central Italy and the South and Islands;
- the loss rate estimate on positions with default status other than non-performing loans is carried out using Cure Rates. For counterparties with a probable default and past-due impaired administrative status percentages of return to performing have been determined and are used to adjust the LGD rate estimated starting from disputed cases.

The MPS Group has adopted a single Master Scale for all types of exposures: this allows all the structures involved in managing credit to have an immediate comparison of the risk associated with various counterparties or portfolios. In addition, the probability of default (PD) for internal rating classes are mapped to the external Standard & Poor's rating scale to make internal risk assessments comparable to those available on the financial market.

Activities to develop and monitor the rating systems are assigned to Risk Management and subjected to control on the part of the units responsible for Internal Validation and Internal Auditing.
The Bank used the PD, LGD and EAD parameters, estimated for regulatory purposes for the calculation of Risk-Weighted Assets, also for other operational purposes and internal management. In effect, these constitute the foundation for calculation for the various systems of measurement and monitoring, specifically:

- for measurement of economic capital in the face of credit risk;

- for the process of calculating risk-adjusted performance and measuring value creation;
- for risk-adjusted pricing processes;
- for credit destination processes;
- in all credit processes (disbursement, review, management and continuation) which have been engineered within the PEF application (Electronic Credit File), in the context of which the counterparty rating is the result of a process which evaluates all the economic, financial, performance and qualitative information related to the customers with which credit risk exists in a transparent, structured and uniform process.

To be able to observe the provisions of IFRS 9 it became necessary to take specific actions to adjust the above parameters, among which we can note in particular:
- adoption of a Point in Time (PIT) PD against the Through the Cycle (TTC) PD used for Basel purposes;
- removal from LGD of a number of additional components, namely indirect costs (non-recurring costs) and from the component linked to the adverse economic cycle (so-called “down turn”); and to reflect the most current recovery rates (PIT), the expectations on the future (forward-looking) trends and the inclusion of any recovery fees in the case of recovery entrusted to third parties;
- use of multi-period PDs and, if necessary, LGDs, in order to determine the expected loss per for the entire residual life of the financial instrument (stages 2 and 3);
- use, in the context of the process of discounting expected future cash flows, of the effective interest rate of the single operation, unlike what is provided for in the regulatory models, in which the single cash flows are discounted using discounting rates determined in accordance with the prudential regulations.

For further details on the methods of determining impairment losses on loans in the context of IFRS 9 please see the paragraph “Methods of determining the impairment of IFRS 9 financial instruments” in part A “Accounting Policies” of the present Notes to the Financial Statements.

2.4 Credit risk mitigation techniques

The MPS Group makes use of a system for managing credit risk attenuation techniques (CRM model) which oversees the entire process of acquiring, assessing, controlling and creating the Credit Risk Mitigation instruments used.
This management system is structured so as to guarantee observance of the regulatory, legal and organisational requirements laid down in the Supervisory Measures for applying the credit risk mitigation rules. The admissibility requirements are both of a general nature, as they are valid for all CRM techniques, and of a specific nature for each technique.
The general requirements, aimed at ensuring the legal certainty and effectiveness of the guarantees are ensured in respect of the following significant elements:
- the binding nature of the legal commitment between the parties and the enforceability in court;
- the ability to be documented, the unenforceability of the instrument with third parties in all jurisdictions relevant for the purposes of establishment and enforcement;
- the timeframe for enforcement in the case of non-fulfilment;
- the respect for organisational requirements.

Regarding the respect for organisational requirements, attenuation of the risk is ensured:
- by the presence of an IT system that supports each stage in the life cycle of the guarantee (acquisition, assessment, management, revaluation, enforcement);
- by the formulation of guarantee management policies (principles, methods, processes), which are regulated and available to all users.

The Bank does not apply processes for netting credit risk exposures with items of the opposite sign in the on-balance-sheet or "off-balance-sheet" contexts, as regards the commercial portfolio. It adopts instead policies to reduce the counterparty risk with institutional counterparties, signing netting agreements according to the ISDA (International Swaps and Derivatives Association)/ISMA (International Securities Market Association) standards and the related collateral agreements, for derivatives (CSAs, Credit Support Annexes), for repos (GMRAs: Global Master Repurchase Agreements) and, finally for securities lending operations (GMSLAs: Global Master Securities Lending Agreements).
The main credit protection forms of a real type used by the Bank are pledges and mortgages on properties but other types are also present (insurance policies, guarantee funds). On occasion the exposures are also backed by unsecured guarantees, mainly provided by private individuals (sureties) but also by companies (sureties and binding letters of patronage).
The Bank has provided itself with a single process for the acquisition of real guarantees, which at the same time is a working tool and expression of the management policies. Management of guarantees is begun following the decision to grant the loan and the process is divided into several stages:

- acquisition (also multiple): in this stage, controls are carried out (formal and regarding the amount) to ensure that the guarantees proposed during the decision-making stage match those provided;
- adjustment/variation/correction: makes it possible to modify the features of the guarantee without interrupting credit protection;
- querying: makes it possible to learn the current figures and historical evolution of the guarantees received;
- termination/cancellation.

If monitoring measures regarding real guarantees indicate operational anomalies during the acquisition stage or possible inadequacies/losses of the values received as liens, events provided for in the credit monitoring policy are activated that aim to update the credit risk assessment.
The disbursement of credit with the acquisition of guarantees is subject to specific control measures, which are differentiated by the guarantee type, applied at the time of disbursement and during monitoring. Overall the Bank, to protect loans, accepts the various instruments summarised below:

- sureties (including omnibus sureties and unsecured guarantees provided by third party subjects);
- endorsements;
- surety policies;
- letters of comfort/binding letters of patronage;
- independent guarantee contracts;
- assumptions;
- unsecured guarantees under foreign law;
  - credit derivatives:
  - credit default swaps;
  - total return swaps;
  - credit linked notes.

The main guarantors are indicated below:

- Sovereign States and Central Banks;
- entities in the public sector and regional entities;
- multilateral development banks;
- regulated intermediaries;
- guarantee bodies (joint facilities);
- companies and private individuals.

As already mentioned in the introduction, in the case of relations with market counterparties for operations in financial instruments (repurchase agreements, securities trading and lending, forex, and financial and credit derivatives), the

Bank uses (bilateral) netting agreements which allow, in the case of default, for offsetting within its own operating sphere of all the existing credit and debit positions.
To optimise the credit risk management and mitigation, the Bank adopts the following protocols: ISDA (with CSAs for derivatives), GMSLA (Global Master Securities Lending Agreements for securities lending) and GMRA (Global Master Repurchase Agreements for repurchase agreements). At the end of 2018, 100% of uses of derivatives are for counterparties with whom an ISDA Master Agreement exists, of which 99.8% are also supported by collateral agreements (CSAs).
Another risk mitigation technique used by the Bank during 2018 is indirect adhesion to the "SwapClear" service, through the brokers Barclays Bank PLC, Merrill Lynch International and Morgan Stanley & Co. International PLC. This is a clearing activity (performed by LCH.Clearnet Ltd for the professional inter-bank market) for the more standardised types of OTC derivative agreements (such as plain vanilla IRS), whereby individual transactions are centralised with the clearer, through the legal mechanism of novation. This "circuit" not only entails an initial margin, but also the liquidation of a daily variation margin on individual transactions, deriving from automatic netting of mutual credit and debit positions, to which is added the indirect adhesion to the credit derivative clearing service operated by ICE CLEAR Ltd through the clearing broker Merrill Lynch International and Barclays Bank PLC. The possibility of making use of the "SwapClear" service directly is still being examined.

3. Impaired loan exposures

3.1 Strategies and management policies

Impaired financial assets include loans which, following the occurrence of events after their disbursement, show objective evidence of a possible loss of value.
The activity of managing, monitoring and controlling impaired receivables, with the exception of non-performing loans, of which only the administrative part is followed, is entrusted to the Non-Performing Portfolio Management Office.
Management of impaired loans begins on the first signs of impairment supported by among other things a specific procedure that makes it possible to intercept the parameters identified for default detection so as to submit the single most critical positions to the examination of the managers to assess a possible reclassification.
For the classification of impaired exposures in the various categories (bad loans, Probable Defaults, impaired past-due) reference is made to the regulations issued by the Bank of Italy, supplemented by internal rules that govern the transfer of loans to the various categories. In particular the classification occurs automatically as regards loans that are past-due and/or over-the-limit for more than 90 days, while the transfer to Probable Default and to Bad Loan occurs following specific checks and assessments submitted for the decisions of the Bodies included in the decision-making chain according to a process designed to guarantee the correct classification of the loan.
In the context of managing all the impaired positions that are not bad, the Non-Performing Portfolio Management Office has the objective of recovering the arrears and bringing the position back to performing status. On this point, on the basis of the analysis of each individual position and joining up with the other Group banks as regards shared positions, it makes the decisions considered most opportune, both with regard to the recovery times and methods and in relation to the classification of said position and the assessment of the related receivable in observance of the current policy.
The return of "impaired loans" to performing status takes place in various ways according to the classification category:
- for the category "impaired past-due and/or over-the-limit" the simple payment of the arrears exceeding 90 days is sufficient;
- for the category "Probable Default", besides payment of the arrears, the cessation of any subjective conditions must also be verified, with particular reference to the customer's state of financial difficulty, which had determined this

classification; in this last case the monitoring of forborne non-performing concessions begins; this provides for a cure period of 12 months during which the customer must necessarily remain classified as a Probable Default; after this period, in the event of regular payments and provided that at least one instalment of principal has been paid, the customer can come back to the "performing" status and the forborne position is transformed into performing under probation, but remains still under observation for a further 24 months. In the case of a shared customer, the removal from the "Probable Default" classification must be agreed with the other Group Banks.

- for the category "bad loan", a return to performing status is possible if, in addition to payment of the arrears (in addition to any payments due in the very near future), the following conditions are met:
    i. absence of enforcement procedures and reports of dispute to the Risk Authority;
    ii. the overcoming of the economic/financial difficulties which led to the classification;

As regards positions classified as "bad loans" we can note that following the recent organisational restructuring implemented by the Parent Company, which regarded mainly a substantial revision of the Credit Recovery Area and the activation of the credit recovery platform outsourced to the company Juliet S.p.A. ("SIRIO" project), currently the recovery activities are entrusted in part to the Credit Recovery Area which handles the management of positions that present profiles of particular delicacy (for example positions held by employees, related parties, presence of legal actions/cases brought against the bank etc.) and to the company Juliet S.p.A. for the remaining positions.
The two structures make use of the administrative support of the Bad Loan Administration Sector of the NPPM Office as regards accounting registrations. The office is in any case responsible for checking the correct assessment of the loans and the passing of the related resolutions including returns to "performing" status which must be analysed and proposed to the Bank.
The analysis and management of "impaired assets" includes obviously also the estimate of the write-downs of the nominal values of the receivables (doubtful outcomes and discounting according to the criteria identified in application of the IAS/IFRS accounting standards) for all non-performing customers "above the threshold" of € 500 thousand according to what is laid down in the group's policy.
For a review of the activities carried out in 2018, please see the section "Loan aggregates - impaired exposures" in the Report on Operations.

3.2 Write-offs

Total and/or partial write-offs are accounted for when it is ascertained that the loan is uncollectable or when there are no realistic prospects of recovery. It is assumed that the conditions on which a non-realistic assessment of recoverability is based, in the face of which it is considered opportune to abandon the interruption of the limitation period, mature when arrangement, bankruptcy, execution and also hereditary procedures have come to an end, at the same time as the absence of jointly-responsible parties or guarantors to foreclose, but also in cases of documented ascertainment of non-pursuability/non-convenient pursuability of the debtors/guarantors and finally on conclusion of out-of-court arrangements.
The control process with the aim of identifying the absence of realistic recovery prospects is focused on counterparties with a level of coverage of more than 95%, and a seniority of transfer to bad status of more than 3 years.
The case in question did not involve the Bank.

3.3 Purchased or originated impaired financial assets

The subject of the description is the internal systems of identification, measurement, management and control of credit risk with reference to POCI positions, with an indication, among other things, of the methodologies adopted

for their classification into uniform portfolios.
As far as Originated Credit Impaired (OCI) relationships are concerned, against a gross exposure at the beginning of the year of € 4.7 million, following the collection during 2018 of approximately € 1.6 million of a position classified as Probable Default, the amount at 31 December 2018 of gross exposure of the type of loan in question was € 3.2 million attributable to three customers of which one classified as bad and two as Probable Default; of these latter two, one which was over the limit at 31 December 2018 was regularised at the beginning of 2019.
As regards the adjustment methods, for all positions of this kind, the scenario of enforcing guarantees was used.
There were no relationships of the Purchased Credit Impaired (PCI) type.

4. Financial assets subject to commercial renegotiation and forborne exposures

The lever of the forbearance measure is activated if the onset of a critical financial situation is noted, and this is such as to have an impact on the counterparty's available income making it unable to fulfil its financial commitments.
Verification of the impacts of the financial difficulty with respect to the debt is crucial for identifying a sustainable forbearance measure, which is agreed only if it is considered that these impacts can be overcome through recourse to forbearance measures.
At the moment of forbearance, it is crucial to assess the degree of the customer's financial difficulty (serious or not) to determine the type of measure (suspension of payments or simple rescheduling of the debt) and to ensure that the measure is credibly aimed at resolving the customer's difficulty.
To achieve this objective, in the corporate world it is indispensable not to carry out only an analysis of the historical data but to examine and assess thoroughly the forecast data and the company's medium/long-term strategies.
From an operational point of view the Bank's orientation is to reschedule the customer's commitments so as to them compatible with the aforementioned items of information and to proceed instead to suspend payments only in cases of a drop in employment or other symptoms of serious financial difficulty of the company.
The stock of performing forbearance measures at the beginning of the year of € 747 million, for approximately 20.6% was classified as NPE; on the other hand, the said stock translated in 46% of cases into coming out of the probation period without default events.
As of 31 December 2018, the stock of forborne performing positions was € 333 million.
The stock of forborne non-performing positions, at the beginning of the year of € 2,679 million recorded during 2018 reductions following the return of some positions to performing status, sales and full and final settlement measures, coming out at the end of the year at € 1,692 million. The existing stock at the end of 2018 is characterised mostly by positions in restructuring, which are the subject of specialist monitoring in the context of plans resolved and/or awaiting approval. The residual component (not in restructuring) has high over-the-limit rates and the operating objective is to check that there are the conditions for granting further forbearance measures or, alternatively, for adopting full and final settlement measures.
During 2018 exposures in the order of approximately 4.5% of the initial stock of forborne non performing exposures were remedied (that is readmitted to performing).
During financial year 2018 the production of new forbearance measures generated a net cost recognised in item 140. "Gains/losses on contractual changes without cancellations" of the income statement, calculated as delta fair value between forecast cash flows before and after the forbearance measure, of € 4.5 million.

QUANTITATIVE INFORMATION

A. CREDIT QUALITY

A.1 Impaired and non-impaired loan exposures: amounts, value adjustments, trend and economic distribution

A.1.1 Breakdown of financial assets by portfolio and credit quality (book values)

Portfolios/Quality	*Bad loans*	*Probable defaults*	*Impaired past-due exposures*	*Non-impaired past-due exposures*	*Other non-impaired assets*	***Total***
1. Financial assets measured at amortised cost	471,172	661,055	6,585	30,210	14,234,322	**15,403,344**
2. Financial assets measured at fair value through other comprehensive income		1,420			71,290	**72,710**
3. Financial assets designated at fair value						**0**
4. Other financial assets obligatorily measured at fair value	37,197	29,580		134	22,569	**89,480**
5. Financial assets held for sale		52,025				**52,025**
Total 31/12/2018	**508,369**	**744,080**	**6,585**	**30,344**	**14,328,181**	**15,617,559**
Total 31/12/2017 (*)	**1,394,751**	**1,112,403**	**19,169**	**53,037**	**15,215,048**	**17,794,408**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

A.1.1.a Analysis of forborne loan exposures by portfolio and credit quality (carrying amount)

Portfolios/Quality	*Bad loans*	*Probable defaults*	*Impaired past-due exposures*	*Non-impaired past-due exposures*	*Other non-impaired assets*	***Total***
1. Financial assets measured at amortised cost	192,952	573,463	24	11,013	293,283	**1,070,735**
2. Financial assets measured at fair value through other comprehensive income						
3. Financial assets designated at fair value						
4. Other financial assets obligatorily measured at fair value	37,197	29,580			1,196	**67,973**
5. Financial assets held for sale		41,054				**41,054**
Total 31/12/2018	**230,149**	**644,097**	**24**	**11,013**	**294,479**	**1,179,762**
Total 31/12/2017 (*)	**413,286**	**945,908**	**5,591**	**22,294**	**697,093**	**2,084,172**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

A.1.1.b Analysis of non-impaired loan exposures: seniority of past-due positions

Portfolios/Quality	*Past due up to 3 months*	*Past due from over 3 months up to 6 months*	*Past due from over 6 months up to 1 year*	*Past due for over 1 year*	*Not past due*	***Total***
1. Financial assets measured at amortised cost	19,224	8,815	2,171		14,204,112	**14,234,322**
2. Financial assets measured at fair value through other comprehensive income					71,290	**71,290**
3. Financial assets designated at fair value						**0**
4. Other financial assets obligatorily measured at fair value		134		22,435	**22,569**	
5. Financial assets held for sale						
Total 31/12/2018	**19,224**	**8,815**	**2,305**	**0**	**14,297,837**	**14,328,181**
Total 31/12/2017 (*)	**24,930**	**13,135**	**14,972**		**15,215,048**	**15,268,085**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

A.1.2 Breakdown of financial assets by portfolio and credit quality (gross and net amounts)

Portfolio / Quality	*Impaired*				*Non-impaired*			**Total**
	Gross exposure	*Total value adjustments*	*Net exposure*	*Total partial write-offs*	*Gross exposure*	*Total value adjustments*	*Net exposure*	***Total (net exposure)***
1. Financial assets measured at amortised cost	2,159,698	(1,020,886)	1,138,812	102,725	14,369,543	(105,011)	14,264,532	**15,403,344**
2. Financial assets measured at fair value through other comprehensive income	3,850	(2,430)	1,420		71,310	(20)	71,290	**72,710**
3. Financial assets designated at fair value								
4. Other financial assets obligatorily measured at fair value	228,590	(161,813)	66,777				22,703	**89,480**
5. Financial assets held for sale	110,712	(58,687)	52,025					**52,025**
Total 31/12/2018	**2,502,850**	**(1,243,816)**	**1,259,034**	**102,725**	**14,440,853**	**(105,031)**	**14,358,525**	**15,617,559**
Total 31/12/2017 (*)	**6,834,792**	**(4,308,469)**	**2,526,323**		**15,342,079**	**(73,993)**	**15,268,086**	**25,414,768**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

Notes:
The exposure related to creditors which have presented an application for "blank" arrangement amounted to € 10,564 thousand (net exposure) divided among 9 customers.
The exposure related to creditors which have presented an application for arrangement "as an ongoing concern" amounted to € 383 thousand (net exposure) for only one customer.
Partial write-offs carried out by the Bank during the year on impaired financial assets totalled € 33,010 thousand (€ 34,455 thousand in 2017 - net of receivables for default interest).

A.1.2.a Analysis of financial assets held for trading and hedging derivatives

Portfolios / Quality	*Assets of evident low credit quality*		*Other assets*
	Accumulated capital losses	*Net exposures*	*Net exposures*
1. Financial assets held for trading	47,664	769	9,282,567
2. Hedging derivatives			
Total 31/12/2018	**47,664**	**769**	**9,282,567**
Total 31/12/2017(*)	**50,398**	**498**	**10,389,014**

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

A.1.2.c Impaired financial assets purchased

There were no impaired financial assets purchased in the portfolio.

A.1.3 Breakdown of financial assets by past-due band (book values)

Portfolios/risk stages	*First stage*			*Second stage*			*Third stage*		
	From 1 day to 30 days	*From over 30 days up to 90 days*	*Over 90 days*	*From 1 day to 30 days*	*From over 30 days up to 90 days*	*Over 90 days*	*From 1 day to 30 days*	*From over 30 days up to 90 days*	*Over 90 days*
1. Financial assets measured at amortised cost	1,319			3,133	14,773	10,986	2,179	16,152	796,527
2. Financial assets measured at fair value through other comprehensive income									
Total 31/12/2018	**1,319**			**3,133**	**14,773**	**10,986**	**2,179**	**16,152**	**796,527**

A.1.4 Financial assets, commitments to grant finance and financial guarantees given: trend of total value adjustments and total provisions

Total value adjustments

Reasons/risk stages	*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 at fair value through other comprehensive income*	*of which: individual write-downs*	*of which: collective write-downs*	*Financial assets measured at amortised cost*	*Financial assets measured at fair value through other comprehensive income*	*of which: individual write-downs*	*of which: collective write-downs*	*Financial assets measured at amortised cost*	*Financial assets measured at fair value through other comprehensive income*	*of which: individual write-downs*	*of which: collective write-downs*	*of which purchased or originated impaired financial assets*	***Total***
Opening balance of overall value adjustments (*)	**5,691**			**5,691**	**117,805**			**117,805**	**1,366,544**		**1,282,128**	**84,415**	**2,201**	**1,490,040**
Increases due to purchased or originated financial assets	3,426	20		3,446	10,006			10,006						**13,432**
Derecognitions other than write-offs	(1,059)			(1,059)	(7,174)			(7,174)	(267,225)		(267,022)	(203)	(678)	**(275,458)**
Net value adjustments for credit risk (+/-)	(15,914)			(15,914)	2,459			2,459	15,930	2,430	62,363	(44,003)	355	**2,475**
Contractual changes without cancellations									4,407		4,359	48		**4,407**
Changes in the estimation methodology														**0**
Write-offs not recognised directly in the income statement									(32,970)		(32,825)	(145)		**(32,970)**
Other changes	15,823			15,823	(26,051)			(26,051)	(65,800)		(97,676)	31,877		**(76,028)**
Closing balance of overall value adjustments	**7,967**	**20**	**0**	**7,987**	**97,045**	**0**	**0**	**97,045**	**1,020,886**	**2,430**	**951,327**	**71,989**	**1,878**	**1,125,898**
Recoveries due to collection on financial assets written off									**111**		**(111)**			**111**
Write-offs recognised directly in the income statement									**(165)**		**165**			**(165)**

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

Total provisions on commitments to grant finance and financial guarantees given

Reasons / risk stages	*First Stage*	*Second Stage*	*Third Stage*	*Total*
Opening balance of overall value adjustments	**91**	**2,183**	**2,675**	
Increases due to purchased or originated financial assets	364	1,342	541	
Derecognitions other than write-offs	(35)	(95)	(2,124)	
Net value adjustments for credit risk (+/-)	(31)	(2,036)	(466)	
Contractual changes without cancellations				
Changes in the estimation methodology				
Write-offs not recognised directly in the income statement				
Other changes				
Closing balance of overall value adjustments	**389**	**1,394**	**626**	
Recoveries due to collection on financial assets written off				
Write-offs recognised directly in the income statement				

A.1.5 Financial assets, commitments to grant finance and financial guarantees given: transfers among the different credit risk stages (gross and nominal amounts)

Portfolios / risk stages	***Gross amounts/nominal amount***					
	Transfers between first stage and second stage		*Transfers between second stage and third stage*		*Transfers between first stage and third stage*	
	From first stage to second stage	*From second stage to first stage*	*From second stage to third stage*	*From third stage to second stage*	*From first stage to third stage*	*From third stage to first stage*
1. Financial assets measured at amortised cost	300,548	476,955	199,368	124,476	29,026	625
2. Financial assets measured at fair value through other comprehensive income						
3. Commitments to grant finance and financial guarantees given	7,563	82,285	4,502	120		
Total 31/12/2018	**308,111**	**559,240**	**203,870**	**124,596**	**29,026**	**625**

A.1.6 On- and off-balance-sheet exposure to banks: gross and net amounts

Types of exposures/amounts	*Gross exposure*		*Total value adjustments and total provisions*	*Net exposure*	*Total partial write-offs*
	Impaired	*Non-impaired*			
A. On-balance-sheet loan exposures					
a) Bad loans					
of which: forborne exposures					
b) Probable defaults					
of which: forborne exposures					
c) Impaired past-due exposures					
of which: forborne exposures					
d) Non-impaired past-due exposures					
of which: forborne exposures					
e) Other non-impaired exposures		6,657,721	(630)	6,657,091	
of which: forborne exposures					
Total A		**6,657,721**	**(630)**	**6,657,091**	
B. Off-balance-sheet loan exposures					
a) Impaired					
b) Non-impaired		2,001,413	(1)	2,001,412	
Total B		**2,001,413**	**(1)**	**2,001,412**	
Total A+B		**8,659,134**	**(631)**	**8,658,503**	

A.1.7 On- and off-balance-sheet loan exposures to customers: gross and net amounts

Types of exposures/amounts	*Gross exposure*		*Total value adjustments and total provisions*	*Net exposure*	*Total partial write-offs*
	Impaired	*Non-impaired*			
A. On-balance-sheet loan exposures					
a) Bad loans	1,146,169		(637,800)	508,369	**102,725**
of which: forborne exposures	*526,883*		*(296,734)*	*230,149*	***3,372***
b) Probable defaults	1,349,128		(605,048)	744,080	
of which: forborne exposures	*1,165,505*		*(521,408)*	*644,097*	
c) Impaired past-due exposures	7,553		(968)	6,585	
of which: forborne exposures	*27*		*(3)*	*24*	
d) Non-impaired past-due exposures		32,072	(1,728)	30,344	
of which: forborne exposures		*11,983*	*(970)*	*11,013*	
e) Other non-impaired exposures		13,703,321	(102,673)	13,600,648	
of which: forborne exposures		*321,567*	*(27,087)*	*294,480*	
Total A	**2,502,850**	**13,735,393**	**(1,348,217)**	**14,890,026**	**102,725**
B. Off-balance-sheet loan exposures					
a) Impaired	10,433		(626)	9,807	
e) Non-impaired		12,664,643	(47,983)	12,616,660	**446**
Total B	**10,433**	**12,664,643**	**(48,609)**	**12,626,467**	
Total A+B	**2,513,283**	**26,400,036**	**(1,396,826)**	**27,516,493**	**103,171**

A.1.8 On-balance-sheet loan exposures to banks: trend of gross impaired exposures

No on-balance-sheet loan exposure to banks was classified among impaired exposures in either the financial statements at 31 December 2018 or the financial statements at 31 December 2017.

A.1.8bis On-balance-sheet loan exposures to banks: trend of gross forborne exposures broken down by credit quality

No on-balance-sheet loan exposure to banks was classified among impaired exposures in either the financial statements at 31 December 2018 or the financial statements at 31 December 2017.

A.1.9 On-balance-sheet loan exposures to customers: trend of gross impaired exposures

	Reasons / Categories	*Bad loans*	*Probable defaults*	*Impaired past-due exposures*
A.	**Opening gross exposure (*)**	**4,318,404**	**1,981,697**	**23,776**
	- of which: exposures sold but not derecognised			
B.	**Increases**	**176,640**	**288,990**	**7,444**
B.1	transfers from non-impaired exposures	5,603	219,393	7,297
B.2	transfers from purchased or originated impaired financial assets			
B.3	transfers from other categories of impaired exposures	150,356	12,476	
B.4	contractual changes without cancellations		316	
B.5	other increases	20,681	56,805	147
C.	**Decreases**	**3,348,874**	**921,560**	**23,667**
C.1	transfers to non-impaired exposures	2,788	119,367	12,003
C.2	write-offs	145	32,855	
C.3	collections	88,221	143,476	1,707
C.4	disposals	903,821	164,577	
C.5	losses on disposal		3,542	
C.6	transfers to other categories of impaired exposures	3,125	150,015	9,692
C.8	contractual changes without cancellations		4,700	
C.9	other decreases	2,350,774	303,028	265
D.	**Gross closing balance**	**1,146,170**	**1,349,127**	**7,553**
	- of which: exposures sold but not derecognised	*99,531*		

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph “Transition to the accounting standards IFRS 9 and IFRS 15”.

A.1.9bis On-balance-sheet loan exposures to customers: trend of gross forborne exposures broken down by credit quality

	Reasons / Quality	*Forborne exposures: impaired*	*Forborne exposures: non-impaired*
A.	**Opening gross exposure (*)**	**2,679,438**	**747,529**
	- of which: exposures sold but not derecognised	107,343	
B.	**Increases**	**330,973**	**187,858**
B.1	transfers from non-forborne non-impaired exposures	35,761	39,865
B.2	transfers from forborne non-impaired exposures	154,073	
B.3	transfers from impaired forborne exposures		119,403
B.4	other increases	141,139	28,590
C.	**Decreases**	**1,317,995**	**601,837**
C.1	transfers to non-forborne non-impaired exposures		343,424
C.2	transfers to forborne non-impaired exposures	119,403	
C.3	transfers to impaired forborne exposures		154,073
C.4	write-offs	32,883	
C.5	collections	155,780	51,003
C.6	disposals	355,503	
C.7	losses on disposal	3,240	
C.8	other decreases	651,186	53,337
D.	**Gross closing balance**	**1,692,416**	**333,550**
	- of which: exposures sold but not derecognised	*99,531*	

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

Note:
impaired credit exposures at 31/12/2017 which during the course of 2018 were subject to forbearance measures totalled € 82,798 thousand.

A.1.10 On-balance-sheet impaired loan exposures to banks: trend of total value adjustments

No on-balance-sheet loan exposure to banks was classified among impaired exposures in either the financial statements at 31 December 2018 or the financial statements at 31 December 2017.

A.1.11 On-balance-sheet loan exposures to customers: trend of total value adjustments

Reasons / Categories	Bad loans		Probable defaults		Impaired past-due exposures	
	Total	of which: forborne exposures	Total	of which: forborne exposures	Total	of which: forborne exposures
A. Opening balance of overall value adjustments (*)	**2,925,915**	**581,936**	**969,939**	**822,209**	**4,392**	**2,049**
- of which: exposures sold but not derecognised	53,769	53,769				
B. Increases	**158,179**	**101,319**	**218,443**	**232,572**	**956**	**587**
B.1 value adjustments on purchased or originated impaired financial assets	**6**		**353**			
B.2 other value adjustments	83,813	38,981	173,598	146,786	728	2
B.3 losses on disposal			3,542	3,240		
B.4 transfers from other categories of impaired exposures	72,509	61,090	1,902	810		
B.5 contractual changes without cancellations			4,700		23	
B.6 other increases	1,851	1,248	34,348	81,736	205	585
C. Decreases	**2,446,294**	**386,521**	**583,334**	**533,373**	**4,380**	**2,633**
C.1 write-backs from valuation	73,032	23,047	143,402	127,002	2,638	2,080
C.2 write-backs from collection	21,340	4,781	23,307	19,821		
C.3 gains on disposal	1,237	1,237	1,712	1,712		
C.4 write-offs	11,597	1,018	65,839	65,230	265	
C.5 transfers to other categories of impaired exposures	453	257	72,480	64,301	1,477	553
C.6 contractual changes without cancellations			317			
C.7 other decreases	2,338,635	356,181	276,277	255,307		
D. Final total value adjustments	**637,800**	**296,734**	**605,048**	**521,408**	**968**	**3**
- of which: exposures sold but not derecognised	*62,335*	*62,335*				

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

EXPOSURE TO SOVEREIGN RISK

As contemplated by the international accounting standards (in particular IAS 1 and IFRS7) related to disclosures on exposures to sovereign credit risk (such as issuers of debt securities, counterparties of OTC derivative contracts, reference entities of credit derivatives and financial guarantees), details of the Bank's exposures at 31 December 2018 are provided.

Overall, exposure to sovereign credit risk, in net nominal values, amounted to € 4,894 million (€ 3,151 million at 31 December 2017) and for € 4,890 million is represented by the long net position with the Republic of Italy (€ 3,139 million at 31 December 2017) and for € 4 million by a long net position with the rest of the world (long net position of € 12 million at 31 December 2017).

The exposures indicated in the following table, including the interest accrued at the end of the year, include the short positions of the HFT portfolio. For credit derivatives the net amount (long or short) of the notional values underlying protection purchases and sales is given. The column "total exposure" shows the net total asset/liabilities, at nominal value, related to the single countries and included in the assets at the end of every year. Any derivative contracts listed on regulated markets are excluded since the economic effects of these are directly posted as an offsetting entry in the cash and cash equivalents, as a result of the settlement of the changes in the margins on a daily basis.

Exposure to sovereign risk

Country	Debt securities							Loans			Credit derivatives	31/12/2018
	Financial assets measured at fair value through profit or loss		Financial assets measured at fair value through other comprehensive income		Financial assets measured at amortised cost			Financial assets measured at amortised cost			Financial assets measured at fair value through profit or loss	Total
	Nominal	Market value book value	Nominal	Market value book value	Nominal	Market value	Carrying Amount	Nominal	Market value	Book/nominal value	Nominal	Nominal
Argentina	202	(8)										202
Austria	64	66										64
Belgium												0
Bosnia and Herzeg.	9	2										9
Brazil												0
Canada												0
Croatia												0
Philippines												0
France	30	35									3,000	3,030
Germany	2,898	3,121										2,898
Greece	(57)	(48)										(57)
Ireland												0
Italy	2,660,338	2,648,840						29,254	29,254	29,254	2,200,478	4,890,070
Lithuania												0
Netherlands												0
Poland												0
Portugal												0
United Kingdom	1	1										1
Romania												0
Russia												0
Spain	1,400	1,590									(3,200)	(1,800)
United States	5	5										5
Turkey	1	1										1
Hungary												0
Venezuela												0
TOTAL	**2,664,891**	**2,653,605**	**0**	**0**	**0**	**0**	**0**	**29,254**	**29,254**	**29,254**	**2,200,278**	**4,894,423**

OTHER INFORMATION

Credit derivatives in Italy	*31/12/2018*	*31/12/2017*
Protection purchases		
- Nominal	138,733	138,338
- Positive fair value	7,196	4,588
- Negative fair value	32	119
Protection sales		
- Nominal	2,339,212	1,897,867
- Positive fair value		
- Negative fair value	49,548	22,981

A.2 Classification of financial assets, commitments to grant finance and financial guarantees given on the basis of external and internal ratings

A.2.1 Breakdown of financial assets, commitments to grant finance and financial guarantees given: by external rating classes (gross amounts)

	External rating classes							
Non-impaired	*AAA/AA- Class 1*	*A+/A- Class 2*	*BBB+/BBB- Class 3*	*BB+/BB- Class 4*	*B+/B- Class 5*	*Lower than B- Class 6*	*Unrated*	*Total*
A. Financial assets measured at amortised cost	12,285	722,752	443,662	34	4,543,304		10,807,205	**16,529,242**
- First stage	*12,285*	*647,666*	*126,648*	*34*	*4,543,304*		*6,860,101*	***12,190,038***
- Second stage		*75,086*	*317,014*				*1,787,406*	***2,179,506***
- Third stage							*2,159,698*	***2,159,698***
B. Financial assets measured at fair value through other comprehensive income	60,216	0	0	11,094	0	3,850	0	**75,160**
- First stage	*60,216*			*11,094*				***71,310***
- Second stage								***0***
- Third stage						*3,850*		***3,850***
Total (A+B)	72,501	722,752	443,662	11,128	4,543,304	3,850	10,807,205	**16,604,402**
of which purchased or originated impaired financial assets							*3,197*	***3,197***
C. Commitments to grant finance and financial guarantees given	0	0	0	0	29,871	0	6,645,392	**6,675,263**
- First stage					29,871		6,472,909	**6,502,780**
- Second stage							162,050	***162,050***
- Third stage							10,433	***10,433***
Total (C)	0	0	0	0	29,871	0	6,645,392	**6,675,263**
Total (A+B+C)	72,501	722,752	443,662	11,128	4,573,175	3,850	17,452,597	**23,279,665**

The external rating classes adopted to fill out the table are those used by Standard & Poor's.
In the presence of multiple assigned external ratings, the criteria adopted to select the rating are those prescribed by the Bank of Italy (in the presence of two ratings, the worse one is used, in the presence of three or more assigned ratings, the second-best is selected).
To assure that the information is significant, transcoding tables were used to convert the classification provided by the different rating companies to the one adopted by Standard & Poor's.

A.2.2 Breakdown of financial assets, commitments to grant finance and financial guarantees given: by internal rating classes (gross amounts)

Non-impaired	External rating classes								
	High quality	*Good quality*	*Quality sufficient*	*Mediocre quality*	*Quality weak*	*Default*	*Group administrative default*	*Unrated*	*Total*
A. Financial assets measured at amortised cost	181,826	1,163,308	2,234,227	1,456,983	192,175	2,128,464	17,578	9,154,680	**16,529,241**
- First stage	*181,493*	*811,109*	*1,787,602*	*425,518*				*8,984,315*	***12,190,037***
- Second stage	*333*	*352,199*	*441,359*	*1,005,531*	*192,175*		*17,578*	*170,331*	***2,179,506***
- Third stage			*5,266*	*25,934*		*2,128,464*		*34*	***2,159,698***
B. Financial assets measured at fair value through other comprehensive income	0	2,204	1,186	0	0	3,850	0	67,920	**75,160**
- First stage		*2,204*	*1,186*					*67,920*	***71,310***
- Second stage									***0***
- Third stage						*3,850*			***3,850***
Total (A+B)	181,826	1,165,512	2,235,413	1,456,983	192,175	2,132,314	17,578	9,222,600	**16,604,401**
of which purchased or originated impaired financial assets						*3,197*			***3,197***
C. Commitments to grant finance and financial guarantees given	51,027	84,277	226,318	173,485	13,029	10,433	0	6,116,695	**6,675,264**
- First stage	41,825	83,114	185,720	85,250				6,106,872	**6,502,781**
- Second stage	9,202	1,163	40,598	88,235	13,029			9,823	***162,050***
- Third stage						10,433			***10,433***
Total (C)	51,027	84,277	226,318	173,485	13,029	10,433	0	6,116,695	**6,675,264**
Total (A+B+C)	232,853	1,249,789	2,461,731	1,630,468	205,204	2,142,747	17,578	15,339,295	**23,279,665**

The table describes the breakdown of the Bank's customer by risk classes attributed according to the rating assigned by internal models. For this purpose, only exposures (counterparties) whose internal rating is periodically determined (Corporate and Private customers) without any transcoding from official rating to internal rating concerning instead sectors such as "banks", "non-banking financial institutions" and "Governments and Government Agencies". Based on this caveat, therefore, the positions referred to these latter segments - while provided with official ratings - were also indicated as "unrated" in the internal rating models.

A.3 Distribution of guaranteed loan exposures by type of guarantee

A.3.1 Guaranteed on- and off-balance-sheet loan exposures to banks

			Secured guarantees (1)				*Unsecured guarantees (2)*									
							Credit derivatives					*Endorsement credits*				
								Other derivatives								
	Exposure gross	*Exposure net*	*Real estate - mortgages*	*Fixed assets held under financial leases*	*Securities*	*Other secured guarantees*	*Credit linked notes*	*Central counterparties*	*Banks*	*Other financial companies*	*Others*	*Public administrations*	*Banks*	*Other financial companies*	*Others*	***Total (1) + (2)***
1. Guaranteed on-balance-sheet loan exposures	**3,348,202**	**3,347,790**			**3,255,485**											**3,255,485**
1.1 fully secured	**3,348,202**	3,347,790			3,255,485											**3,255,485**
- of which impaired																
1.2 partially secured																
- of which impaired																
2. Guaranteed "off-balance sheet" loan exposures	**423,169**	**423,169**			**50,632**	**350,943**										**401,575**
2.1 fully secured	**159,104**	159,104			50,632	108,472										**159,104**
- of which impaired																
2.2 partially secured	**264,065**	264,065				242,471										**242,471**
- of which impaired																

Exposures guaranteed by securities are represented by loan operations such as repos, with the exchange of cash collateral with counterparty's full availability.
Secure guarantees backing "off book" exposures refer to the net counterparty risk, i.e. determined on the basis of the netting agreements defined according to the ISDA directives, and guaranteed by collateral acquired according to the methods specified in the CSA agreements stipulated between the parties. These guarantees are recognised at fair value estimated at the reporting date, or when this information is lacking, at the contractual value of the same.

A.3.2 Guaranteed on- and off-balance-sheet loan exposure to customers

			Secured guarantees (1)				*Unsecured guarantees (2)*									
							Credit derivatives					*Endorsement credits*				
								Other derivatives								
	Exposure gross	*Exposure net*	*Real estate - mortgages*	*Fixed assets held under financial leases*	*Securities*	*Other secured guarantees*	*Credit linked notes*	*Central counterparties*	*Banks*	*Other financial companies*	*Others*	*Public administrations*	*Banks*	*Other financial companies*	*Others*	***Total (1) + (2)***
1. Guaranteed on-balance-sheet loan exposures	**9,073,739**	**7,856,048**	**2,917,946**		**3,661,388**	**493,825**					**6,862**	**1,898**	**7,222**	**150,060**		**7,239,201**
1.1 fully secured	7,661,579	6,866,008	2,721,944		3,571,772	415,866					6,805	1,599	3,253	101,038		**6,822,277**
- of which impaired	*1,768,379*	*1,028,579*	*937,079*		*17,457*	*33,944*						*851*	*1,796*	*37,401*		***1,028,528***
1.2 partially secured	1,412,160	990,040	196,002		89,616	77,959					57	299	3,969	49,022		**416,924**
- of which impaired	*587,373*	*190,100*	*144,288*		*5,190*	*3,655*					*57*	*62*	*2,949*	*1,818*		***158,019***
2. Guaranteed "off-balance-sheet" loan exposures	**7,340,084**	**7,339,705**	**27,897**		**5,987,511**	**1,159,057**								**47,890**		**7,222,355**
2.1 fully secured	6,896,776	6,896,479	25,637		5,984,897	843,354								28,831		**6,882,719**
- of which impaired	*9,488*	*9,488*	*4,391*											*5,096*		***9,487***
2.2 partially secured	443,308	443,226	2,260		2,614	315,703							1,923	19,059		**341,559**
- of which impaired																***0***

Exposures guaranteed by securities are represented by loan operations such as repos, with the exchange of cash collateral with counterparty's full availability.

Secure guarantees backing "off book" exposures refer to the net counterparty risk, i.e. determined on the basis of the netting agreements defined according to the ISDA directives, and guaranteed by collateral acquired according to the methods specified in the CSA agreements stipulated between the parties. These guarantees are recognised at fair value estimated at the reporting date, or when this information is lacking, at the contractual value of the same.

A.4 Financial and non-financial assets obtained through enforcement of guarantees received

Type of transaction / Balances	*Loan exposure written off*	*Gross value*	*Total value adjustments*	*Carrying amount*	
					of which: obtained during the year
A. Property, plant and equipment	750	750		750	750
A.1 Used in the business					
A.2 For investment purposes					
A.3 Inventories	750	750		750	750
B. Equity securities and debt securities					
C. Other assets					
D. Non-current assets and disposal groups held for sale					
D.1 Property, plant and equipment					
D.2 Other assets					
Total 31/12/2018	**750**	**750**		**750**	**750**

B. DISTRIBUTION AND CONCENTRATION OF LOAN EXPOSURES

B.1 Sectoral distribution of on- and off-balance-sheet loan exposures to customers

B.1.1 Sectoral distribution of loan exposures: on-balance-sheet to customers

Counterparties / Exposures	*Bad loans*		*Probable defaults*		*Impaired past-due exposures*		*Non-impaired exposures*			
	Total	*of which forborne exposures*	*Total*	*of which forborne exposures*	*Total*	*of which forborne exposures*	*Total*	*of which forborne exposures*	***Total 31/12/18***	***Total 21/12/17***
Public administrations										
- Net exposure							4,518,180	*866*	**4,518,180**	**4,268,754**
- Total value adjustments							(35)	*(6)*	**(35)**	**(349)**
Financial companies										
- Net exposure	**2,264**	*801*	**66,672**	*65,701*			4,817,326	*10,565*	**4,886,262**	**6,617,373**
- Total value adjustments	(5,763)	*(5,139)*	(64,381)	*(62,310)*			(5,056)	*(533)*	**(75,200)**	**(157,378)**
of which: insurance companies										
- Net exposure							*6,707*		***6,707***	***28,169***
- Total value adjustments										
Non-financial companies										
- Net exposure	372,913	*195,454*	622,715	*539,207*	3,022		4,075,271	*270,337*	**5,073,921**	**6,382,448**
- Total value adjustments	(508,598)	*(274,752)*	(519,889)	*(443,670)*	(462)		(95,672)	*(25,546)*	**(1,124,621)**	**(4,152,717)**
Households										
- Net exposure	133,192	*33,893*	54,692	*40,188*	3,563	***24***	220,215	*23,723*	**411,662**	**145,966**
- Total value adjustments	(123,439)	*(16,483)*	(20,777)	*(15,428)*	(506)	***(3)***	(3,638)	*(1,972)*	**(148,360)**	**(71,992)**

B.1.2 Sectoral distribution of loan exposures: "off-balance-sheet" to customers

Counterparties / Exposures	*Impaired exposures*	*Non-impaired exposures*	*Total 31/12/18*	*Total 31/12/17*
Public administrations				
- Net exposure		4,660,141	**4,660,141**	**2,490,295**
- Total value adjustments			**0**	
Financial companies				
- Net exposure		7,351,851	**7,351,851**	**1,758,372**
- Total value adjustments		(985)	**(985)**	**(625)**
of which insurance companies				
- Net exposures		1	**1**	**354**
- Total value adjustments			**0**	
Non-financial companies				
- Net exposure	9,615	593,653	**603,268**	**607,951**
- Total value adjustments	(626)	(46,289)	**(46,915)**	**(52,228)**
Households				
- Net exposures	191	179	**370**	**256**
- Total value adjustments		(709)	**(709)**	

The above data may differ from the quantitative information indicated in table A.1.7 above "On- and off-balance-sheet loan exposures to customers: gross and net amounts" for the total of exposures connected with the counterparty risk related to operations for the lending or borrowing of securities or goods.

B.2 Geographical distribution of on- and "off-balance sheet" loan exposures to customers

B.2.1 Geographical distribution of loan exposures: on-balance sheet to customers

Counterparties / Exposures	*Bad loans*	*Probable defaults*	*Impaired past-due exposures*	*Non-impaired exposures*	*Total 31/12/18*	*Total 31/12/17 (*)*
Italy						
- Net exposure	506,611	733,046	6,585	13,201,611	**14,447,853**	**17,000,230**
- Total value adjustments	(630,067)	(598,728)	(968)	(104,313)	**(1,334,076)**	**(4,366,643)**
Other European countries						
- Net exposure	1,758	11,034		414,852	**427,644**	**433,639**
- Total value adjustments	(7,734)	(6,319)		(89)	**(14,142)**	**(15,730)**
America						
- Net exposure				12,504	**12,504**	**8,014**
- Total value adjustments						**(63)**
Asia						
- Net exposure				2,024	**2,024**	**819**
- Total value adjustments						
Rest of world						
- Net exposure					**0**	**6**
- Total value adjustments						

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

B.2.2 Geographical distribution of loan exposures: "off-balance-sheet" to customers

Geographical area / Exposures	*Impaired exposures*	*Non-impaired exposures*	*Total 31/12/18*	*Total 31/12/17*
Italy				
- Net exposure	9,807	10,985,420	**10,995,227**	**3,681,966**
- Total value adjustments	(626)	(47,727)	**(48,353)**	**(52,527)**
Other European countries				
- Net exposure		1,584,347	**1,584,347**	**1,142,190**
- Total value adjustments		(257)	**(257)**	**(327)**
America				
- Net exposure		36,058	**36,058**	**33,071**
- Total value adjustments				
Asia				
- Net exposure				
- Total value adjustments				
Rest of world				
- Net exposure				
- Total value adjustments				

The above data may differ from the quantitative information indicated in table A.1.7 above "On- and off-balance-sheet loan exposures to customers: gross and net amounts" for the total of exposures connected with the counterparty risk related to operations for the lending or borrowing of securities or goods.

B.3 Geographical distribution of on- and "off-balance-sheet" loan exposures to banks

B.3.1 Geographical distribution of loan exposures: on-balance-sheet to banks

Geographic area / Exposures	*Bad loans*	*Probable defaults*	*Impaired past-due exposures*	*Non-impaired exposures*	*Total 31/12/18*	*Total 31/12/17 (*)*
Italy						
- Net exposure				6,157,359	**6,157,359**	**6,682,454**
- Total value adjustments				(621)	**(621)**	**(6)**
Other European countries						
- Net exposure				428,002	**428,002**	**406,918**
- Total value adjustments				(8)	**(8)**	**(20)**
America						
- Net exposure				21,174	**21,174**	**16,006**
- Total value adjustments						
Asia						
- Net exposure						
- Total value adjustments						
Rest of world						
- Net exposure				50,554	**50,554**	**52,139**
- Total value adjustments				(2)	**(2)**	

(*) The Bank utilised the option not to redetermine on a uniform basis the comparative data of the year of first application of IFRS 9; therefore, the figures for financial year 2017, determined according to the IAS 39 criteria, are not fully comparable.

B.3.2 Geographical distribution of exposures: "off-balance-sheet" loan exposures to banks (carrying amount)

Geographical area / Exposures	*Impaired exposures*	*Non-impaired exposures*	*Total 31/12/18*	*Total 31/12/17*
Italy				
- Net exposure		1,423,458	**1,423,458**	**1,935,057**
- Total value adjustments		(1)	**(1)**	
Other European countries				
- Net exposure		138,983	**138,983**	**209,046**
- Total value adjustments				
America				
- Net exposure		191,065	**191,065**	**178,750**
- Total value adjustments				
Asia				
- Net exposure				
- Total value adjustments				
Rest of world				
- Net exposure				
- Total value adjustments				

The above data may differ from the quantitative information indicated in table A.1.6 above "On- and off-balance-sheet loan exposures to banks: gross and net amounts" for the total of exposures connected with the counterparty risk related to operations for the lending or borrowing of securities or goods.

B.4 Significant exposures

	31/12/2018	*31/12/2017*
a) amount (carrying amount)	41,997,036	27,518,747
b) amount (weighted value)	1,024,954	1,220,318
c) number	-	-

The Supervisory Regulations define a position as a “large exposure” on the basis of the unweighted exposure for credit risk. A position is considered a “large exposure” if of an amount equal to or greater than 10% of the regulatory capital.
As provided for in the aforementioned regulations, exposures in Government Securities were also considered.
No positions exceed the risk concentration limit.

C. SECURITISATION TRANSACTIONS

QUALITATIVE INFORMATION

The Bank acts as investor as well as market maker. The internal organisational structure which oversees these operations is the Credit Trading Desk. Its main objective involves providing liquidity and pricing for the transactions carried out by the MPS Group and support, again in terms of pricing, both to the Parent Company and to customers that have invested in the securitisations. For such purposes, ongoing and structured analysis is used on the underlying flows of these transactions principally attributable to residential mortgage loans and consumer credit disbursement activities.
For deals originating outside the MPS Group, the Desk's activity is oriented to seizing the various opportunities that the market offers, in order to maximise the income returns of the portfolios as an investor in this segment also and mainly in the light of the operations carried out by the Central Bank following approval of the purchase programme on this Asset Class. The process for assessing and measuring the risks connected to the positions temporarily held is centralised at the Risk Management Area of the Parent Company MPS within the scope of market risk measurement. Activities for controlling and mitigating risks are mainly carried out via the study and daily analysis of the underlying flows, all by the use of advanced models.
During 2018, operations were carried out via trading on the secondary market. The amount held in the trading book (item 20a of the Assets "Financial assets held for trading") was € 374 million (€ 1,260 million at 31 December 2017) with a preponderant exposure on the senior part of the capital structure. Senior securities are also present in the portfolio at amortised cost (for € 581 million), as well as mezzanine and junior securities in the portfolio at obligatory FV (for a total of € 15.3 million), recognised following the derecognition of bad loans carried out in June 2018 as part of the securitisation transaction involving the Group's bad loans.
The Bank holds only on-balance-sheet exposures and has not issued either guarantees or credit lines to securitisation vehicles.

QUANTITATIVE INFORMATION

C.1 Exposures deriving from the main "own" securitisation transactions divided by type of asset securitised and type of exposure

Type of underlying assets/Exposure	On-balance-sheet exposures					
	Senior		*Mezzanine*		*Junior*	
	Carrying Amount	*Value Adjustments/ write-backs*	*Carrying Amount*	*Value Adjustments/ write-backs*	*Carrying Amount*	*Value Adjustments write-backs*
A. Completely derecognised						
- non-performing loans	581,177		8,959	(165)	6,433	310
C. Not derecognised from the financial statements						
- mortgage loans			6,470	(541)	2,767	(232)
- ship finance			8,827	(2,714)	16,514	(5,078)
Total 31/12/2018	**581,177**		**24,256**	**(3,420)**	**25,714**	**(5,000)**
Total 31/12/2017					**114,247**	

There are no exposures either as guarantees given or as credit lines.

C.2 Exposures deriving from the main "third party" securitisation transactions divided by type of asset securitised and type of exposure

Type of underlying assets/Exposure	On-balance-sheet exposures					
	Senior		*Mezzanine*		*Junior*	
	Carrying Amount	*Value Adjustments/ write-backs*	*Carrying Amount*	*Value Adjustments/ write-backs*	*Carrying Amount Amount*	*Value Adjustments write-backs*
- Other assets	-	-	6,598	10	356	(2)
- Consumer credit	29,990	(163)	21,905	(85)	35,801	(81)
- Non-performing loans	22,308	(51)	1,252	(1)		
- Non-residential mortgage loans	28,884	(73)	21,302	(31)	5,025	(17)
- Residential mortgage loans	133,832	(864)	35,542	(278)	30,938	(153)
Total 31/12/2018	**215,014**	**(1,151)**	**86,599**	**(385)**	**72,120**	**(253)**
Total 31/12/2017	**1,068,273**	**(216)**	**187,922**	**1,547**	**4,066**	**(13)**

There are no exposures either as guarantees given or as credit lines.

C.3 Special purpose vehicle for securitisation

Name of securitisation / Name of special purpose vehicle	*Registered Offices*	*Consolidation*	*Assets*			*Liabilities*		
			Receivables	*Debt securities*	*Other*	*Senior*	*Mezzanine*	*Junior*
2017 Popolare Bari RMBS S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	614,161		16,349	464,059	58,264	92,516
A-Best Fifteen S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	977,712		49,000	911,000	73,000	31,000
Argo Mortgage 2 S.r.l.	Via Cassa di Risparmio, 15 Genoa	NO	51,960			0	22,610	29,350
Arrow CMBS 2018 - 1	3 George's Dock IFSC Dublin 1	NO	292,743			154,800	137,900	400
Berica ABS 3 S.r.l.	Via Battaglione Framarin, 18 Vicenza	NO	524,786		11,575	255,710	93,900	115,012
BP Mortgages S.r.l.	Via Gustavo Fara, 26 Milan	NO	166,226		17,373	58,757	25,300	47,100
Casaforte S.r.l.	Via E.Duse, 53 Rome	YES	1,220,912		31,177	1,063,804		188,285
Citizen Irish Auto Receivables Trust 2017 Dac	3 George's Dock IFSC Dublin 1	NO	65,582		1,582	36,634	17,400	7,900
Cordusio RMBS Securitisation S.r.l. - Series 2006	Piazzetta Monte, 1 Verona	NO	225,881		2,544	90,743	141,700	10,688
Deco 2014-Tulip Dac	George's Quay Dublin 2	NO	97,215			27,422	52,872	5
Deco 2015-Harp Limited Dac	George's Quay Dublin 2	NO	38,451			0	20,075	18,281
Dilosk RMBS 1 Dac	16 Hume Street Dublin 2	NO	125,961		1,029	80,590	35,000	10,300
European Residential Loan Securitisation 2017-PL1 Dac	125 Old Broad Street London, EC2N 1AR	NO	618,960		12,534	247,606	367,825	100
European Residential Loan Securitisation 2018 - 1 Dac	Canada Square, Canary Wharf London, E14 5LB	NO	339,729		1,373	194,481	45,390	95,478
Fastnet Securities 12 Dac	3 George's Dock IFSC Dublin 1	NO	419,836		11,221	320,310	52,000	62,200
F-E Mortgages S.r.l.	Piazzetta Monte, 1 Verona	NO	103,269			14,683	59,000	7,630
Fino 1 Securitisation S.r.l.	Viale Luigi Majno, 45 Milano	NO	739,000		32,500	636,298	69,640	50,311
First Swiss Mobility 2017 1 Ag	Bellerivestrasse 201, 8008 Zurich	NO	292,839			237,199	14,642	13,133
Grand Canal Securities 2 Dac	Kilmore House, Park Lane Dublin 1	NO	479,777		6,112	198,661	67,809	218,961
Intesa Sec.3 S.r.l.	Via Monte di Pietà, 8 Milan	NO	155,079		45,000	0	72,900	72,900
Madeleine SPV S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	27,730		3,164	0	14,188	17,522
Marche M6 S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	1,086,265		34,010	585,741	0	496,566
Pietra Nera Uno S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	403,810			210,000	173,600	20,210
Quarzo S.r.l.	Via Galleria Del Corso, 2 Milan	NO	899,987		3,735	747,000		153,000
Rural Hipotecario IX Fondo de Titulización de Activos	Lagasca,120 Madrid	NO	419,809		15,255	381,198	39,558	8,415
Sestante Finance S.r.l.	Via G. Negri, 10 Milan	NO	101,054			48,140	30,530	30,547
Siena Mortagages 10-7 S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	YES	1,672,044		197,173	840,154	817,600	211,463
Siena Npl 2018 S.r.l.	Via Piemonte, 38 Rome	NO	4,171,871			2,752,431	847,600	565,000
Storm 2016-I B.V.	Prins Bernhardplein 200 Amsterdam, 1097 JB	NO	1,449,897		24,635	1,360,306	95,000	0
Tagus Sociedade de Titularizacao de Creditos S.A.	Rua Castilho, 20 Lisbon	NO	1,320,899		11,830	1,161,267	16,127	50,572
Taurus 2018-1 IT S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	341,654			224,297	117,387	
Towers CQ S.r.l.	Via A.Pestalozza, 12/14 Milan	NO	505,073		13,673	288,649	87,100	114,488
Voba n.5 S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	237,551		3,390	0	124,520	89,450
Voba n.7 S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	691,157		13,196	428,849	150,000	121,319
Norma Spv S.r.l.	Via V.Alfieri, 1 Conegliano (TV)	NO	494,291		106	8,674	164,820	320,902
TOTAL			**21,373,171**		**599,536**	**14,029,462**	**4,105,257**	**3,271,004**

(*) The liabilities do not show the remaining items different from the financial instruments issued, including the accumulated profits (losses) for the year.

With reference to the consolidated securitisations, we can inform you that:
- Siena Mortgages 10-7 Srl is a securitisation transaction carried out in 2010. The transaction took the form of the sale by BMPS to the vehicle of a portfolio of performing residential mortgage loans for approximately € 3.5 billion. The Parent Company did not derecognise the underlying receivables, because it maintained substantially all the risks and

benefits associated with ownership of the receivables transferred;

- Casaforte is a securitisation transaction carried out in 2010, which took the form of the sale to the special purpose vehicle "Casaforte Srl" of the receivable originating from the mortgage loan granted to the consortium 'Perimetro Gestione Proprietà Immobiliari'. The residual debt at 31/12/2018 amounted to € 1,220.9 million. In December 2013 the bank completed the full repurchase of the PGPI 2010 financial equity instruments and the related class Z Securities for an amount of approximately € 70 million. As a result of these purchases the bank gained control over the company, with consequent consolidation of the same in the financial statements.
  In the context of the "2017-2021 Restructuring Plan", approved by the Board of Directors of BMPS on 26 June 2017 and by the European Commission on 4 July 2017, and of the commitments made to the Directorate General for Competition the European Commission contained in it, in 2018 a second stage of restructuring of the "Chianti Classico" operation was launched; this involves the merger of "Perimetro Gestione Proprietà Immobiliari" and the early unwinding of the securitisation. To be able to proceed with these activities giving investors the possibility of an early exit from the investment, on 29 October 2018 Banca MPS launched a public offering at a premium on the securities placed at the time with third-party investors. As a result of the public offering, Banca MPS came to hold 97.59% of the Class A notes and 99.81% of the Class B notes. At the end of 2018, following the public offering and the further repurchases of securities made at the request of customers, € 35 mln of Casaforte Class A Notes are still placed with investors. These are recognised in the item "10 Financial liabilities measured at amortised cost c) outstanding securities" in the liabilities of the consolidated balance sheet.

C.4 Special purpose vehicles for securitisation (non-consolidated)

Accounting item / Type of structured entity	*Financial assets held for trading*	*Financial assets obligatorily measured at fair value*	*Financial assets measured at amortised cost*	*Total assets (A)*	*Financial liabilities held for trading*	*Total liabilities (B)*	*Net book value (C=A-B)*	*Maximum exposure to risk of loss (D)*	*Difference between exposure to risk of loss and carrying amount (E=D-C)*
2017 Popolare Bari RMBS S.r.l.	38,941	0	0	38,941		0	38,941	38,941	0
A-Best Fifteen S.r.l.	1,778	0	0	1,778		0	1,778	1,778	0
Argo Mortgage 2 S.r.l.	6,822	0	0	6,822		0	6,822	6,822	0
Arrow CMBS 2018 - 1	19,000	0	0	19,000		0	19,000	19,000	0
Berica ABS 3 S.r.l.	11,220	0	0	11,220		0	11,220	11,220	0
BP Mortgages S.r.l.	5,686	0	0	5,686		0	5,686	5,686	0
Citizen Irish Auto Receivables Trust 2017 Dac	1,300	0	0	1,300		0	1,300	1,300	0
Cordusio RMBS Securitisation S.r.l. - Series 2006	975	0	0	975		0	975	975	0
Deco 2014-Tulip Dac	2,297	0	0	2,297		0	2,297	2,297	0
Deco 2015-Harp Limited Dac	6,007	0	0	6,007		0	6,007	6,007	0
Dilosk RMBS 1 Dac	2,008	0	0	2,008		0	2,008	2,008	0
European Residential Loan Securitisation 2017-PL1 Dac	16,755	0	0	16,755		0	16,755	16,755	0
European Residential Loan Securitisation 2018 - 1 Dac	1,855	0	0	1,855		0	1,855	1,855	0
Fastnet Securities 12 Dac	3,627	0	0	3,627		0	3,627	3,627	0
F-E Mortgages S.r.l.	2,128	0	0	2,128		0	2,128	2,128	0
Fino 1 Securitisation S.r.l.	18,861	0	0	18,861		0	18,861	18,861	0
First Swiss Mobility 2017 1 Ag	1,599	0	0	1,599		0	1,599	1,599	0
Grand Canal Securities 2 Dac	4,698	0	0	4,698		0	4,698	4,698	0
Intesa Sec.3 S.r.l.	24,200	0	0	24,200		0	24,200	24,200	0
Madeleine SPV S.r.l.	5,322	0	0	5,322		0	5,322	5,322	0
Marche M6 S.r.l.	30,308	0	0	30,308		0	30,308	30,308	0
Norma Spv S.r.l.		37,197		37,197		2,618	34,579	34,579	0
Pietra Nera Uno S.r.l.	18,980	0	0	18,980		0	18,980	18,980	0
Quarzo S.r.l.	5,000	0	0	5,000		0	5,000	5,000	0
Rural Hipotecario IX Fondo de Titulización de Activos	4,226	0	0	4,226		0	4,226	4,226	0
Sestante Finance S.r.l.	3,816	0	0	3,816		0	3,816	3,816	0
Siena Npl 2018 S.r.l.	0	15,393	581,177	596,570		0	596,570	596,570	0
Storm 2016-I B.V.	10,052	0	0	10,052		0	10,052	10,052	0
Tagus Sociedade de Titularizacao de Creditos S.A.	30,345	0	0	30,345		0	30,345	30,345	0
Taurus 2018-1 IT S.r.l.	2,944	0	0	2,944		0	2,944	2,944	0
Towers CQ S.r.l.	49,304	0	0	49,304		0	49,304	49,304	0
Voba n.5 S.r.l.	12,611	0	0	12,611		0	12,611	12,611	0
Voba n.7 S.r.l.	5,984	0	0	5,984		0	5,984	5,984	0
TOTAL	**348,651**	**52,589**	**581,178**	**982,418**	**0**	**2,618**	**979,800**	**979,800**	**0**

Notes:

2017 Popolare Bari RMBS S.r.l. (POPBA 2017-TV 17/58): vehicle set up pursuant to Italian Law 130/1999. Securitisation having as collateral residential mortgage loans backed by first mortgages, concentrated mainly in the Apulia region. Originator: Banca Popolare di Bari S.p.A..

A-Best Fifteen S.r.l. (ABEST15 TV 17/18 SUB): vehicle set up pursuant to Italian Law 130/1999. Securitisation having as collateral loans for the purchase of motor vehicles originated in Italy by FCA Bank S.p.A..

Argo Mortgage 2 S.r.l. (ARGOM 2 B-TV 04/43 and ARGOM C-TV 04/43 SUB): vehicle set up pursuant to Italian Law 130/1999. Securitisation of residential mortgage loans not classified as bad distributed all over Italy. Originator: Banca Carige S.p.A..

Arrow CMBS 2018-1 (ARWC18 A 18/30 TV, ARWC18 A2 18/30 TV and ARWC 1B-TV 18/30 SUB): securitisation having as collateral leasing on commercial properties for office use originated in France, Belgium and the Netherlands.

Berica ABS 3 S.r.l. (BERICA - TV 14/61 SUB): vehicle set up pursuant to Italian Law 130/1999. Multi-originator securitisation (Banca Popolare di Vicenza and Banca Nuova S.p.A.) which involves the sale without recourse of performing loans made up of residential mortgage loans granted to residents of Italy.

BP Mortgages S.r.l. (BPMO 1C-TV 07/43 SUB) vehicle set up pursuant to Italian Law 130/1999. Securitisation of performing residential property mortgage loans backed by voluntary mortgages distributed all over Italy. Originator: Banco BPM S.p.A..

Citizen Irish Auto Receivables Trust 2017 DAC (CIART C-TV 17/24 SUB): vehicle set up under Irish law. Securitisation having as collateral a portfolio of loans disbursed in Ireland for the purchase of motor vehicles.

Cordusio RMBS Securitisation S.r.l. - Series 2006 (CORD 2C-TV 06/35 SUB) vehicle set up pursuant to Italian Law 130/1999. Securitisation of performing mortgage loans on residential properties distributed all over Italy. Originator: UniCredit S.p.A..

Deco 2014-Tulip Dac (DECO14C 14/24 TV SUB and DECO-TV 14/24 SUB): vehicle set up under Irish law. Securitisation having as collateral loans mainly retail and for offices originated in the Netherlands.

Deco 2015-Harp Limited Dac (DECO15B TV 15/27 SUB): vehicle set up under Irish law. Securitisation having as collateral mainly residential mortgage loans (71.8%) originated in Ireland.

Dilosk RMBS No1 Designated Activity Company (DILSK1B-TV 15/51 SUB): Securitisation of mortgage loans guaranteed by residential properties situated in Ireland. Originator: Bank of Ireland.

European Residential Loan Securitisation 2017-PL1 Dac (ERLS A-TV 17/57, ERLS B 17/57 TV SUB and ERLS17 17/57 TV SUB): vehicle set up under Irish law. Securitisation having as collateral residential mortgage loans originated in Ireland.

European Residential Loan Securitisation 2018 - 1 Dac (ERLS18 A 18/61 TV): vehicle set up under Irish law. Securitisation having as collateral a mix of performing and non-performing loans originated in Ireland.

Fastnet Securities 12 DAC (FSTNT B 16/56 TV SUB): vehicle set up under Irish law. Portfolio comprising mortgage loans originated by Permanent TSB plc and guaranteed by residential properties situated in Ireland.

F-E Mortgages S.r.l. (FEMO 1C-TV 03/43 SUB): vehicle set up pursuant to Italian Law 130/1999. Securitisation of performing mortgage loans on residential properties situated in Italy. Originator: UniCredit S.p.A. (formerly FinecoBank S.p.A.).

Fino 1 Securitisation S.r.l. (FINO CL A 17/45 TV): vehicle set up pursuant to Italian Law 130/1999. Securitisation of loan contracts, credit facilities and loans disbursed in other technical types granted to natural persons and legal persons and classified as impaired financial assets. Originator: UniCredit S.p.A. and Arena NPL ONE S.r.l..

First Swiss Mobility 2017-2-AG (SWMOB 1B 17/27 1 SUB and SWMOB 2C 17/27 2 SUB): vehicle that manages a portfolio of loans disbursed in Switzerland in the form of loans and leasing for the purchase of motor vehicles.

Grand Canal Securities 2 DAC (GCS 2 A TV 17/58 and GCS 2B-TV 17/58 SUB): the vehicle manages a portfolio comprising mortgage loans guaranteed by properties situated in Ireland. Originator: Irish Nationwide Building Society and Springboard Mortgages Ltd.

Intesa Sec.3 S.r.l. (INTS 3C TV 07/33 SUB): vehicle set up pursuant to Italian Law 130/1999. Securitisation of performing mortgage loans on residential properties distributed all over Italy. Originator: Intesa Sanpaolo S.p.A..
Madeleine SPV S.r.l. (MADL B 14/38 3.5 SUB): vehicle set up pursuant to Italian Law 130/1999. The loans involved in the securitisation are salary-backed loans disbursed to Italian public and private employees. Originator: Pitagora S.p.A..
Marche M6 S.r.l. (MARCH 6A2-TV 13/64): vehicle set up pursuant to Italian Law 130/1999. This is a portfolio of performing loans deriving from residential property mortgage loans backed by first mortgages. Originator: Banca delle Marche S.p.A.
Norma SPV: in the context of a transaction to securitise non-performing loans originating in part from banks external to the MPS Group, on 1 July 2017 Banca MPS and MPS Capital Services arranged for the sale of a portfolio of non-performing loans disbursed in the real estate and shipping sectors. The portfolio sold to the vehicle Norma SPV S.r.l. consisted, as of the disposal date, of 19 loans totalling € 284.9 million, of which:

- 12 loans disbursed by Banca MPS totalling € 24.0 million in the real estate sector and € 145.3 million in the shipping sector;
- 7 loans disbursed by MPS Capital Services totalling € 28.8 million in the real estate sector and € 86.8 million in the shipping sector.

At 31 December 2018, the residual debt of the portfolio originated by the MPS Group amounted to € 101 million (of which € 63.8 million and € 37.2 million respectively transferred by Banca MPS and MPS Capital Services). To finance the purchase of this portfolio, on 21 July 2017 the vehicle issued ABS securities (the "securities") in classes A1, B, C and D for the real estate sector and ABS securities in classes A1, B, C1, C2 and D for the shipping sector. The senior classes of both the real estate and shipping operations were placed with institutional investors, while the mezzanine and junior classes were subscribed by each of the transferring banks in proportion to the loans transferred. Specifically, the MPS Group subscribed the following classes:

- Real Estate: Class B for a nominal amount of € 31.2 million; Class C for a nominal amount of € 4.2 million; Class D for a nominal amount of € 15.8 million.
- Shipping: Class B for a nominal amount of € 86.7 million; Class C1 for a nominal amount of € 37.6 million; Class C2 for a nominal amount of 12.0 million; Class D for a nominal amount of € 121.3 million.

The sale of part of the notes did not lead to derecognition of the underlying loans from the financial statements of the transferring Banks, which substantially maintained all the risks and benefits associated with ownership of the receivables transferred.
Pietra Nera Uno S.r.l. (PNER1D TV 18/30 SUB, PNERA 1 A 18/30 TV, PNERA 1 B-TV 18/30 and PNERA1E TV 18/30 SUB): vehicle set up pursuant to Italian Law 130/1999. The loans involved in the securitisation are commercial mortgage loans connected with a number of Italian Outlets. Originator: BRE/Europe 7 NQ S.a r. l..
Quarzo S.r.l. (QUARZ A18/35 TV): vehicle set up pursuant to Italian Law 130/1999. Securitisation having as collateral performing consumer credit contracts originated in Italy. Originator: Compass Banca S.p.A..
Rural Hipotecario IX Fondo de Titulización de Activos (RHIPO A3-TV 07/50): vehicle set up under Spanish law. Multi-originator securitisation having as collateral residential mortgage loans disbursed in Spain.
Sestante Finance S.r.l. (SESTA 03/40 TV SUB): vehicle set up pursuant to Italian Law 130/1999. The loans involved in the securitisation are residential mortgage loans originated in Italy. Originator: Banca Popolare dell'Emilia Romagna S.p.A. (formerly Meliorbanca S.p.A.).
Storm 2016-I B.V. (STORM A2-TV 16/54): vehicle set up under Dutch law. Securitisation having as collateral residential mortgage loans originated in the Netherlands.
Tagus Sociedade de Titularizacao de Creditos S.A.: Portuguese vehicles which issued notes securitised with loans for the purchase/leasing of cars and trucks (AQUA 4B-TV 17/35 SUB) and with electricity receivables (VERSE 5 17/22 0.85, VERSE 6 18/23 1.1 and TAGST A1-TV 09/25).
Taurus 2018-1 IT S.r.l. (TAURUS A 18 TV 18/30): vehicle set up pursuant to Italian Law 130/1999. Securitisation

having as collateral non-residential mortgage loans situated in Italy. Originator: Bank of America Merrill Lynch International Ltd.
Towers CQ S.r.l. (TOWCQ-TV 16/33 SUB e TOW M 2.25 18/33 SUB): vehicle set up pursuant to Italian Law 130/1999. This is a securitisation of salary- or pension-backed loans granted by Accedo S.p.A. (Originator).
Voba n. 5 - Voba n. 7 S.r.l. (VOBAF 5 A 14/51 TV and VOBA 7 A2-TV 18/60): vehicles set up pursuant to Italian Law 130/1999. Securitisation having as collateral performing mortgage loans and unsecured loans disbursed to small and medium-sized enterprises. Originator: Volksbank S.p.A. (formerly Banca Popolare dell'Alto Adige S.p.A.).

The maximum exposure to risk of loss was determined as an amount equal to the book value. During the year of reference, the bank did not provide and has no intention to provide financial or any other type of support.

C.5 Servicer activity - own securitisations: collections of securitised receivables and reimbursement of securities issued by the special purpose vehicle for the securitisation

Nothing to report.

QUANTITATIVE INFORMATION

D. DISCLOSURE ON STRUCTURED ENTITIES NOT CONSOLIDATED IN THE ACCOUNTS (OTHER THAN SPECIAL PURPOSE VEHICLES FOR SECURITISATION)

QUALITATIVE INFORMATION / QUANTITATIVE INFORMATION

Accounting items / Type of structured entity	*Asset accounting portfolios*			*Liability accounting portfolios*				
	Financial assets held for trading	*Financial assets obligatorily measured at fair value*	*Total assets (A)*	*Financial liabilities held for trading*	*Total liabilities (B)*	*Net book value (C=A-B)*	*Maximum exposure to risk of loss (D)*	*Difference between exposure to risk of loss and carrying amount (E=D-C)*
1. Special purpose vehicles								
2. Collective investment undertakings	1,059,995	13,131	1,073,125	166,977	166,977	906,148	1,265,535	359,387
3. Other								
TOTAL	**1,059,995**	**13,131**	**1,073,125**	**166,977**	**166,977**	**906,148**	**1,265,535**	**359,387**

The aggregate includes, in correspondence to the column "Financial assets held for trading":
- € 46.2 million (€ 61.7 million at 31.12.2017) related to interests held by the Bank in units of Open-ended Investment Funds and Exchange Traded Funds that invest in equities, bonds and derivatives. These units are purchased for the purpose of hedging the risks generated by structured bonds issued and funds placed through the Parent Company's network or for the purpose of repurchase on the secondary market of structured funds of which the original structuring has been handled;
- € 1,013.7 million (€ 923.6 million at 31.12.2017) related to exposures in credit and financial derivatives with positive fair value with the following counterparties: Rainbow for € 360.5 million (€ 485.2 million at 31.12.2017) Anima for € 374.1 million (€ 115.3 million at 31.12.2017) Quaestio for € 15.4 million (not present in 2017) and with the Axa Im Deis investment funds for € 263.8 million (€ 325.0 million at 31.12.2017). Rainbow, Anima and Axa Im Deis are Irish-law funds managed respectively by Anima Asset Management and AXA Investment Managers. These funds are divided into segments that are purchased by MPS AXA Financial Limited and represent the funds to which are linked the performance of the Unit-Linked policies placed with its customers with the name "AXA MPS Valore Performance". These are Luxembourg-law funds managed by Quaestio Capital and sold on the MPS network. The Bank operates with Rainbow, Anima, Axa Im Deis and Quaestio as the counterparty with which the derivatives included in the Funds' assets are traded.

The column Financial assets available for sale includes:
- € 1.4 million related to the units of a closed-end real estate fund reserved for qualified investors (Fondo Cosimo I), held by the Bank. The fund's objective is to maximise the returns for its investors through both a growing dividend yield and enhancing the value of the assets in the portfolio.
- € 6.7 million related to units of a closed-end multi-segment Italian alternative mutual investment fund (Idea CCR I and II). First Italian DIP (Debtor-in-possession) Financing funds, they pursue the purpose of contributing to relaunching medium-sized Italian businesses in financial difficulty, but with solid fundamentals.
- € 2.4 million related to units of a private contribution closed-end real estate investment fund (Athens RE Fund B)

reserved for qualified investors. The fund, managed by Unipol Sai Investimenti SGR, holds prestigious tourist complexes located in Tuscany and Sicily.
- € 2.6 million related to the units of a closed-end alternative real estate investment fund reserved for professional investors (Fondo Rainbow), held by the Bank. The fund's objective is to maximise the returns for its investors by enhancing the value of investments made. The fund, managed by Serenissima SGR, holds some hotel complexes located in Apulia.

The column Financial liabilities held for trading includes:
- € 167.0 million (€ 172.7 million at 31.12.2017) related to the negative fair value of credit and financial derivatives with the following counterparties: Rainbow for € 49.4 million (€ 107.6 million at 31.12.2017), Anima for € 96.8 million (€ 34.1 million at 31.12.2017), Quaestio for € 6.8 million and with the Axa Im Deis investment funds managed by AXA Investment Managers for € 13.9 million (€ 31.0 million at 31.12.2017).

The entities in question finance themselves by issuing units.
The maximum exposure to risk of loss was indicated as an amount equal to the book value for exposures in units in collective investment undertakings other than financial and credit derivatives, for which the reference is to the positive fair value plus the add-on (calculated taking into account also the positions with negative fair value).
During the year of reference, the Bank did not provide and has no intention of providing financial or any other type of support to the unconsolidated structured entities indicated above.
There are no sponsored unconsolidated structured entities for which the Bank, at the reporting date, holds interests.

E. SALE TRANSACTIONS

Financial assets sold but not fully derecognised

QUALITATIVE INFORMATION

The assets indicated in the following tables are debt and credit securities and have been sold in the context of repurchase agreements with repurchase obligations at maturity. Also present are loans sold in the context of the "Norma Spv" securitisation, with related liabilities against them, not yet derecognised.
Repurchase agreements, as for similar securities lending operations described in paragraph 8 of the Notes to the Financial Statements - part B - Other transactions, are carried out, largely, to cover similar operations in the other direction in the context of the dynamic and complex management of Global Markets business.
Considering SFTs (Securities Financing Transactions) as a whole, there emerges a net total funding position, related to the financing of long positions in securities.
The underlying assets of repurchase agreements are mainly Italian government securities, mostly BTPs. The bank-owned securities used for repurchase agreements are posted among assets in the balance sheet, under item 20. "Financial assets measured at fair value through profit or loss", and the related benefits and risks remain, in any case, those of the Bank. Securities transferred are shown as "committed" but this status does not exclude the possibility of selling them, by covering the momentary lack of the availability of the security through securities lending or reverse repurchase agreements.

QUANTITATIVE INFORMATION

E.1 Financial assets sold fully recognised and associated financial liabilities: carrying amounts

The financial assets sold but not derecognised are shown below at full and at carrying amount.

	Financial assets sold fully recognised				*Associated financial liabilities*		
	Carrying amount	*of which involved in securitisation transactions*	*of which involved in sale contracts with agreement to repurchase*	*of which impaired*	*Carrying amount*	*of which involved in securitisation transactions*	*of which involved in sale contracts with agreement to repurchase*
A. Financial assets held for trading	**4,851,228**		**4,851,228**		**4,786,078**		**4,786,078**
1. Debt securities	4,851,222		4,851,222		4,786,072		4,786,072
2. Equity securities	6		6		6		6
3. Loans							
4. Derivatives							
B. Other financial assets obligatorily measured at fair value	**37,197**	**37,197**		**37,196**	**2,618**	**2,618**	
1. Debt securities							
2. Equity securities							
3. Loans	37,197	37,197		37,196	2,618	2,618	
C. Financial assets designated at fair value	**0**						
1. Debt securities							
2. Loans							
D. Financial assets measured at fair value through other comprehensive income	**60,691**		**60,691**		**55,864**		**55,864**
1. Debt securities	60,691		60,691		55,864		55,864
2. Equity securities							
3. Loans							
E. Financial assets measured at amortised cost	**0**						
1. Debt securities							
2. Loans							
Total 31/12/2018	**4,949,116**	**37,197**	**4,911,919**	**37,196**	**4,844,560**	**2,618**	**4,841,942**
Total 31/12/2017	**4,888,258**	**46,531**	**4,841,727**		**4,806,550**		

E.2 Financial assets sold partially recognised and associated financial liabilities: carrying amounts

Repurchase agreements carried out using own securities "transferred and not derecognised" were entered into for approximately 40% with the Parent Company MPS and for approximately 56% with Cassa Compensazione e Garanzia.

E.3 Sale transactions with liabilities with recourse only on assets sold but not fully derecognised: fair value

	Fully recognised	*Partially recognised*	*Total 31/12/2018*	*Total 31/12/2017*
A. Financial assets held for trading				
1. Debt securities				
2. Equity securities				
3. Loans				
4. Derivatives				
B. Other financial assets obligatorily measured at fair value	**37,197**	**0**	**37,197**	
1. Debt securities				
2. Equity securities				
3. Loans	**37,197**		**37,197**	
C. Financial assets designated at fair value				
1. Debt securities				
2. Loans				
D. Financial assets measured at fair value through other comprehensive income				
1. Debt securities				
2. Equity securities				
3. Loans				
E. Financial assets measured at amortised cost				**46,531**
1. Debt securities				
2. Loans				**46,531**
Total financial assets	**37,197**	**0**	**37,197**	**46,531**
Total associated financial liabilities	**(2,618)**		**(2,618)**	**2,508**
Net value 31/12/2018	**34,579**		**34,579**	
Net value 31/12/2017				**44,023**

B. Financial assets sold and fully derecognised with recognition of continuing involvement

Qualitative information

There is nothing to report.

Quantitative information

There is nothing to report.

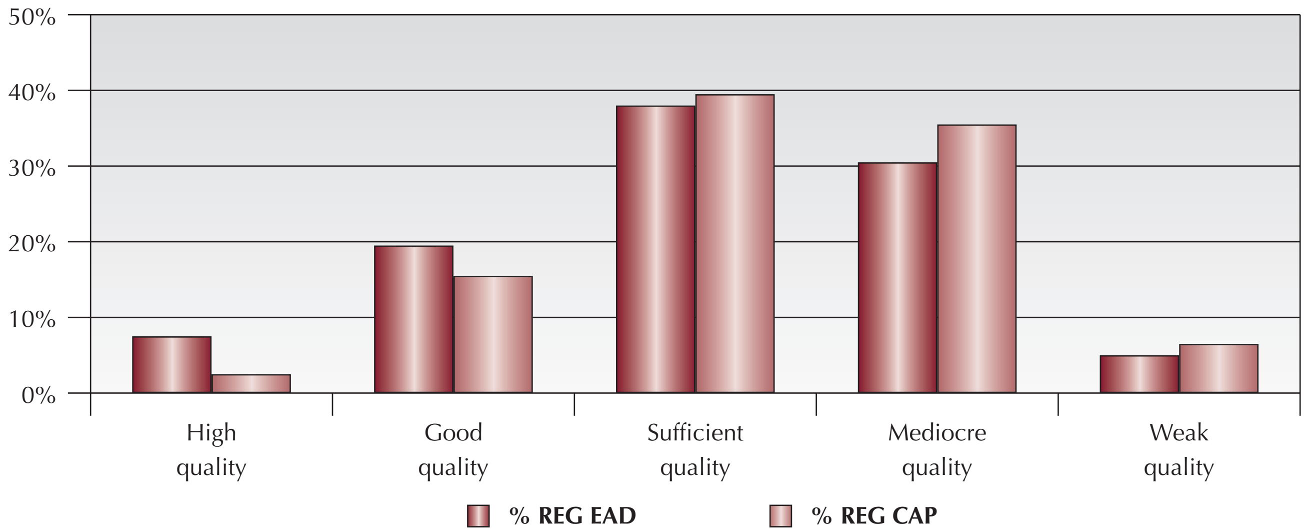
E.4 Covered bond transactions

The Bank issued no covered bank bonds.

F. CREDIT RISK MEASUREMENT MODELS

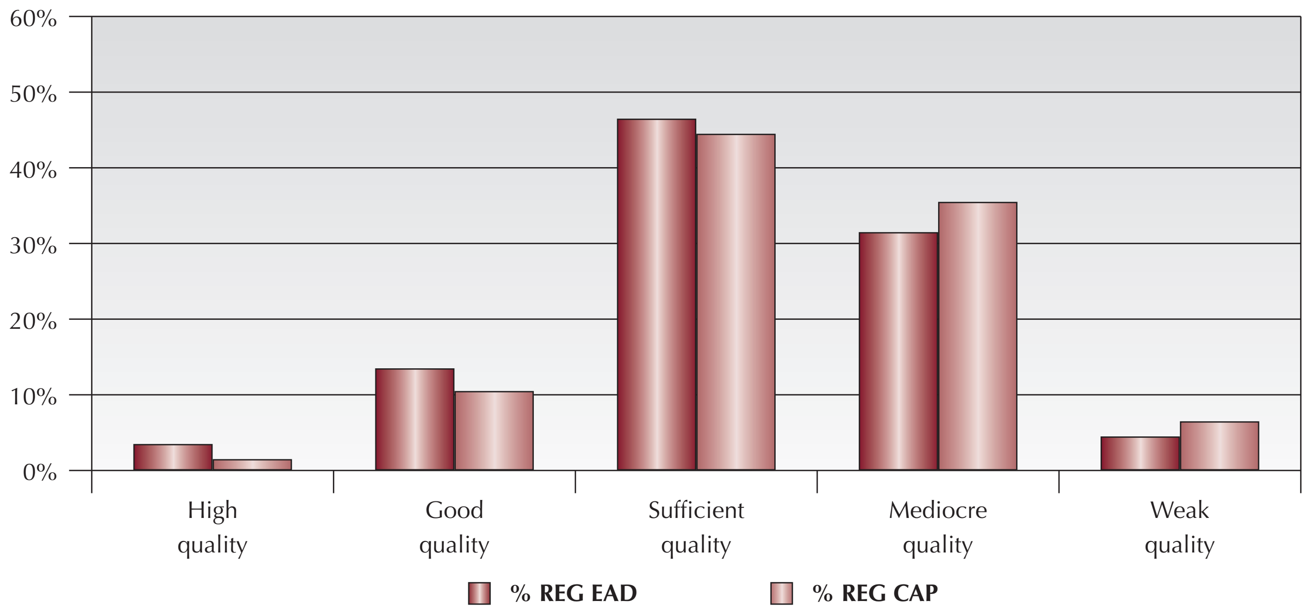
For the purposes of the quantitative disclosure on credit risk, the distribution of the credit quality of the Bank's portfolio at 31/12/2018 for risk exposure (EAD REG) and Regulatory Capital (CAP REG) is presented below. The chart below shows that approximately 27.1% of the exposures at risk are granted to high- and good-quality customers (positions in financial assets are excluded), while 68.4% are granted to customers of sufficient or mediocre quality. The grading indicated below also includes the exposures to unsupervised banks, government bodies and financial and banking entities, not included in the AIRB models. For these counterparties, a credit standing assessment is any case attributed, using official ratings when available, or appropriate internally computed values.

QUALITY DISTRIBUTION OF PERFORMING LOAN PORTFOLIO
BANCA MPS CAPITAL SERVICES - 31.12.2018



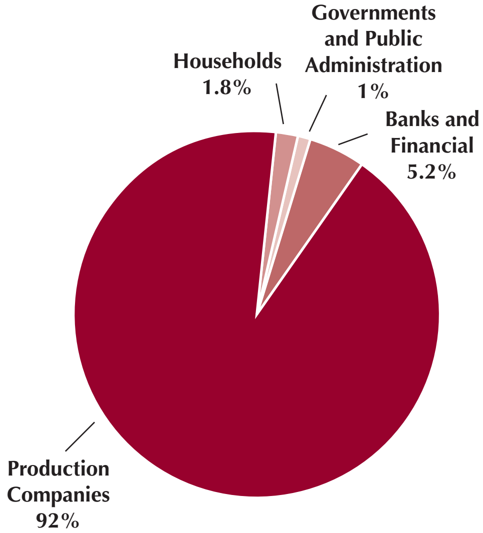
The chart below, instead, shows the distribution of credit quality only in relation to the Corporate and Retail portfolios for which the MPS Group has received from the Supervisory Authority the authorisation for use of the advanced internal models relating to the PD and LGD parameters. We can note that the proportion of exposures with high and good quality at 31/12/2018 is 17.2% of total exposures, compared to 77.6% of exposures to borrowers with sufficient or mediocre quality.

QUALITY DISTRIBUTION OF PERFORMING LOAN PORTFOLIO CORPORATE AND RETAIL SEGMENTS BANCA MPS CAPITAL SERVICES - 31.12.2018

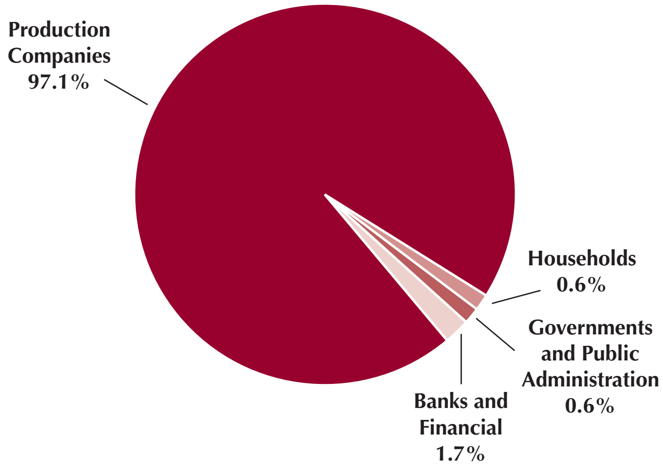


The findings obtained at the end of 2018, indicate that the exposures at risk are mainly related to the sectors "Production Companies" (92% of total disbursements) and "Banks and Financial Firms" (5.2%). The remaining portion is divided between the "Households" and "Governments and Public Administration" sectors, with 1.8% and 1%, respectively.
In terms of Regulatory Capital, this is absorbed for 97.1% by the segment of "Production Company" customers. These are followed by "Banks and Financial Firms" with 1.7%, and "Governments and Public Administration" and "Households" both with 0.6%.

RISK EXPOSURE
BANCA MPS CAPITAL SERVICES - 31.12.2018

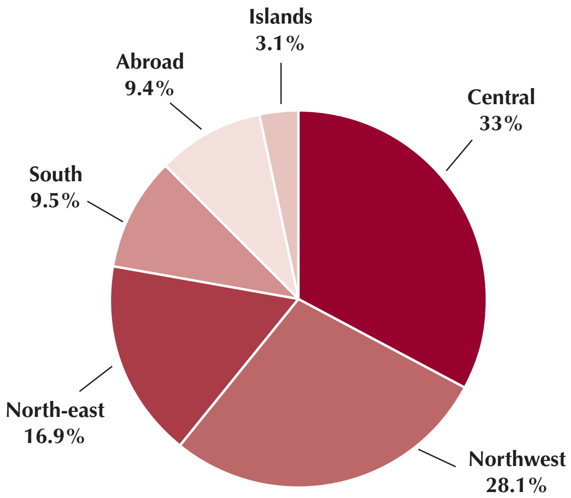


REGULATORY CAPITAL
MPS CAPITAL SERVICES - 31/12/2018

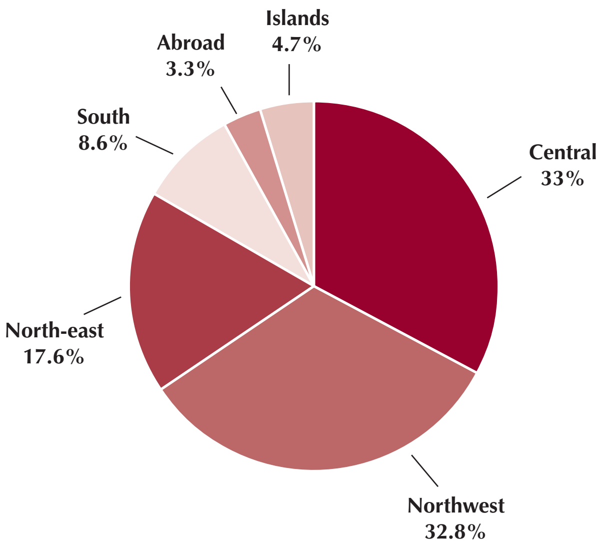


Analysis of the geographical distribution of the Bank's customers shows that risk exposures are mainly concentrated in the Central regions (33%), followed by the North West and North East (with 28.1% and 16.9%, respectively), the South (9.5%), Foreign Countries (9.4%), and the Islands (3.1%).
The absorption of Regulatory Capital also finds more explanation in the composition of lending more concentrated in the Centre (33%), the North-west (32.8%), the North-east (17.6%), the South (8.6%), the Islands (4.7%) and Foreign Countries (3.3%).

RISK EXPOSURE
BANCA MPS CAPITAL SERVICES - 31.12.2018

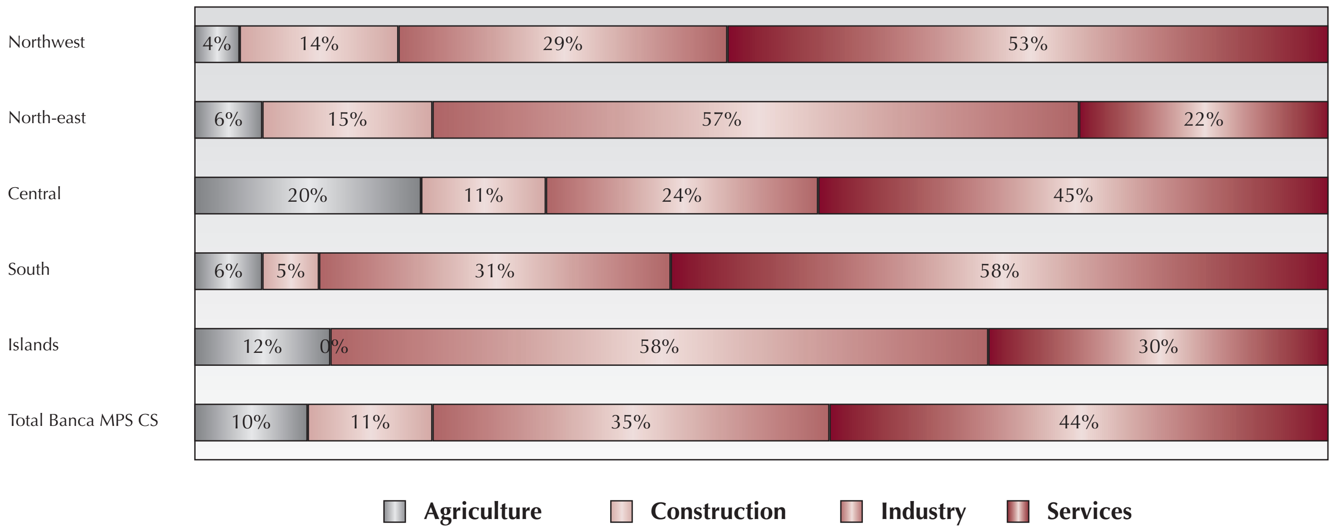


REGULATORY CAPITAL
MPS CAPITAL SERVICES - 31/12/2018



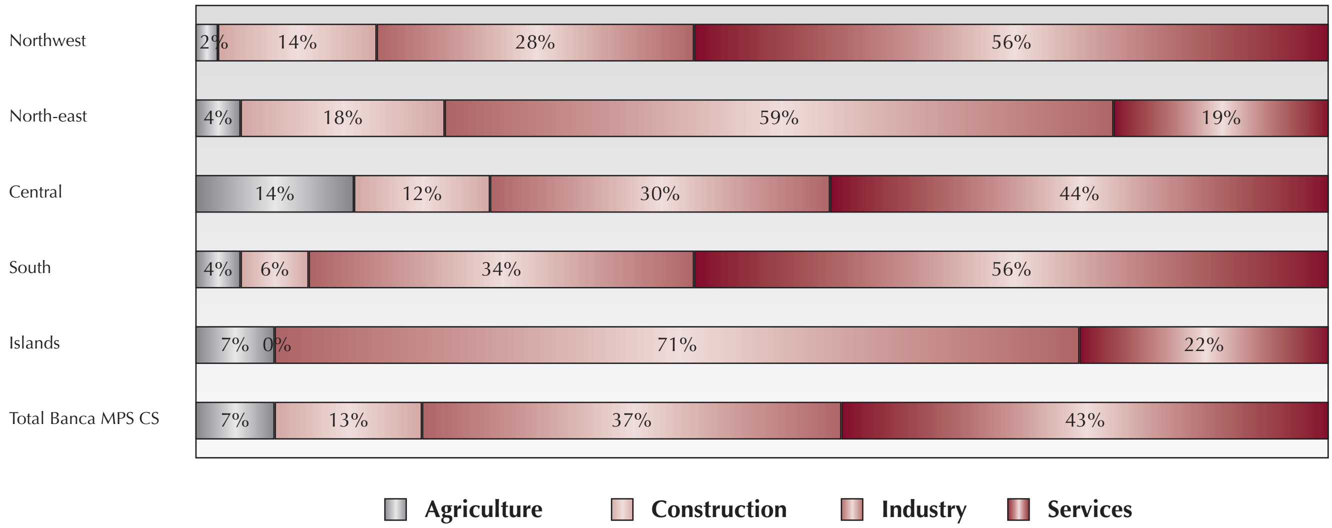
The charts below, finally, show only for Corporate customers in Italy, the percentage distribution by individual Geographical Area of the exposure to Default and of the absorption of Regulatory Capital by business segment.
The highest portion of Exposure to Default of Companies is concentrated in the Services segment in all Geographical Areas, except in the North-east and the Islands, where Industry prevails with 57% and 58% respectively. Out of the total, the concentration on Services is 44% and is followed by that on Industry (35%), on Building with 11% and finally on Agriculture (10%).

BANCA MPS CAPITAL SERVICES
CLIENTELA CORPORATE ITALIA IN BONIS AL 31/12/2018
Distribuzione dell'Esposizione al Default (EAD REG) per Area Geografica e per ramo di attività



Also as regards Regulatory Capital (CAP), the largest concentration in total is related to the Services sector. Only in the Northeast and the Islands did the Industry sector dominate (59% and 71%, respectively).

BANCA MPS CAPITAL SERVICES
PERFORMING ITALIAN CORPORATE CUSTOMERS 31/12/2018
Distribution of Regulatory Capital by geographical area and business



SECTION 2 - MARKET RISKS

2.1 Interest rate risk and price risk - regulatory trading book

The risk management model for market risks related to the Trading Book

The MPS Group's Regulatory Trading Book (RTB) is made up of the set of Regulatory Trading Books managed by the Banking Parent Company (BMPS) and by MPSCS. The RTBs of the other subsidiaries are closed to market risks. Transactions in derivatives, also brokered on behalf of the same customers, are centralised and the risk is monitored by MPSCS.
The market risks of the trading book are monitored for operating purposes in terms of Value-at-Risk (VaR). The Group Finance and Liquidity Committee is tasked with directing and coordinating the overall process for management of the Group's proprietary finance, ensuring consistency between the management actions of the different business units.
The Group's Trading Book is subject to daily monitoring and reporting by the Parent Company's Financial Risk Officer Area, on the basis of proprietary systems. The operational VaR is calculated independently with respect to the operating departments, using the internal risk measurement model implemented by the Risk Management Unit itself, in line with the leading international best practices. Solely for reporting purposes, on the subject of Market Risks the Group, and within it the Bank, employs in any case the standardised approach.
The operating limits on trading activities are expressed for each level of authority in terms of VaR diversified between risk factors and portfolios and monthly and annual Stop Loss and Stress. In addition, the credit risk of the trading book, besides being included in the VaR calculations and in the respective limits for the credit spread risk part, is also subject to specific operating limits with regard to bond issuer and concentration risk, which envisage notional ceilings for types of guarantor and rating classes.
The VaR is calculated with a confidence interval of 99% and a holding period of the positions of one business day. The method used is that of historic simulation with daily full revaluation of all the elementary positions, on a window of 500 historic readings of the risk factors (lookback period) with daily flow. The VaR calculated in this manner makes it possible to take into account all the effects of diversification between risk factors, portfolios and type of instruments traded. It is not necessary to hypothesise up front any functional form in the distributions of the returns of the activities and also the correlations between different financial instruments are implicitly captured in the VaR on the basis of the historic joint performance of the risk factors. The historical scenarios used in the model are constructed as the daily change, in terms of ratio, of the single risk factors; the shock created is applied to the current market level making the VaR measurement reactive to the changing market conditions.
Periodically, the management reporting flow on market risks is forwarded to the Risk Management Committee, to the Managing Director, to the Chairperson and to the Board of Directors of the Parent Company in the Risk Management Report, the instrument through which the Top Management and the Governing Bodies are informed about the Group's overall risk profile.
The macro-types of risk factors considered within the Internal Markets Risks Model are IR, EQ, CO, FX, CS, as illustrated below:
- IR: interest rates on all the relevant curves, inflation curves and related volatility;
- EQ: equity prices, indexes and related volatility;
- CO: commodity prices;
- FX: exchange rates and related volatility;
- CS: credit spread levels.

The VaR (or diversified VaR, or Net VaR) is calculated and separated daily for internal management purposes, also with

respect to other analysis dimensions:
• organisation/operations of the Portfolios,
• for Financial Instruments,
• for Risk Families.

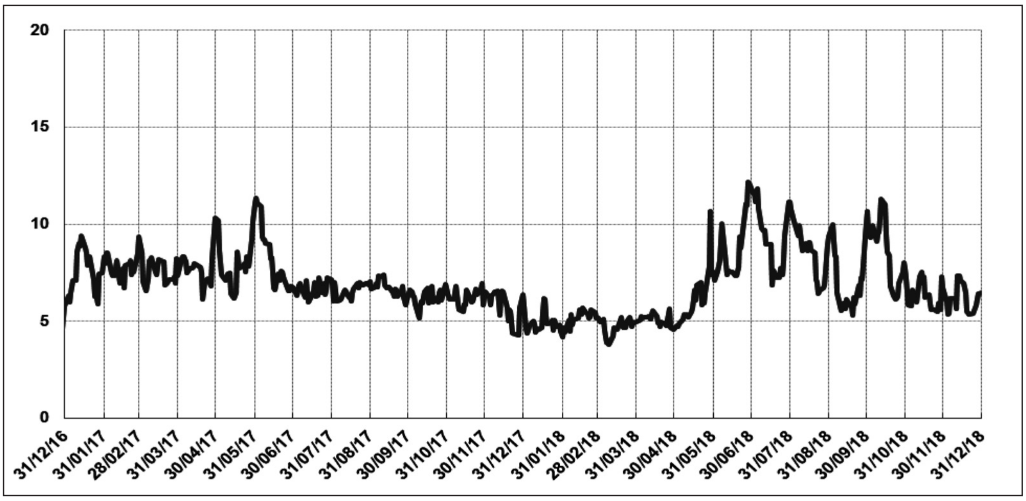
It is then possible to assess the VaR in relation to each combination of these dimensions so as to be able to facilitate very detailed analyses of the phenomena which affect the portfolios.
With reference in particular to the risk factors, the following are identified: the Interest Rate VaR (IR VaR), the Equity VaR (EQ VaR), the Commodity VaR (CO VaR), the Forex VaR (FX VaR) and the Credit Spread VaR (CS VaR). The algebraic sum of these components produces the "Gross VaR" (or non-diversified VaR) which compared with the diversified VaR makes it possible to quantify the benefit of diversification between risk factors deriving from holding portfolios allocated on asset classes and risk factors that are not perfectly correlated. This information too can be analysed along all the aforesaid dimensions.
The model makes it possible to produce diversified VaR metrics for the entire Group, in order to be able to appreciate in an integrated manner all the diversification effects that can be generated among the banks of the Group, by virtue of the joint specific positioning implemented by the different business units.
Additionally, scenario analyses and stress tests are regularly conducted on the various risk factors with differentiated granularity levels for the entire structure of the Group portfolio tree and for all analysed categories of instruments.
Stress tests make it possible to assess the ability of the Bank to absorb sizeable potential losses upon the occurrence of extreme market events, in order to identify the measures to take to reduce the risk profile and preserve the capital. Stress tests are developed on the basis of historical and discretionary scenarios. Historical scenarios are defined on the basis of actual disruptions historically recorded on the markets. These scenarios are identified on the basis of a time interval in which the risk factors were subjected to stress. No particular hypotheses are necessary with respect to the correlation between risk factors, observing what happened historically in the identified stress period.
Stress tests based on discretionary scenarios consist of hypothesising the occurrence of extreme variations in some market parameters (interest and exchange rates, stock market indexes, credit spreads and volatility) and of measuring the corresponding impact on the value of the portfolios, irrespective of their actual historical occurrence. The discretionary stress scenarios currently examined are simple (only one risk factor changes) and joint (several risk factors change simultaneously). Simple discretionary scenarios are calibrated to hit independently one category of risk factors at a time, hypothesising that the shocks will not propagate to the other factors. Joint discretionary scenarios instead are aimed at evaluating the impact of global shocks that simultaneously hit all types of risk factors.

***

During 2018 the market risks of the Regulatory Trading Book of the subsidiary showed, in terms of VaR, a trend influenced mainly by the proprietary trading activity in the CS and IR segments (operations in Italian Government Securities and Long Futures) and, to a lesser extent, for Client Driven activities in the EQ segment (options and equity futures on the main market indices).
The volatility of the VaR recorded starting from the end of the second quarter of the year was due both to changes in the market parameters and to trading activity, the latter connected to the cycles of operations in auctions on short-term Italian Government Securities. The upward trend of the Italian credit spread recorded starting from the end of May caused a considerable increase in the VaR measure, through a succession of peaks when the market parameters increased and corresponding to new queue scenarios on the historical simulation model. Exposure to risk, represented by the VaR metric was in part offset by hedging activities using short positions on BTP futures on the medium/long term.

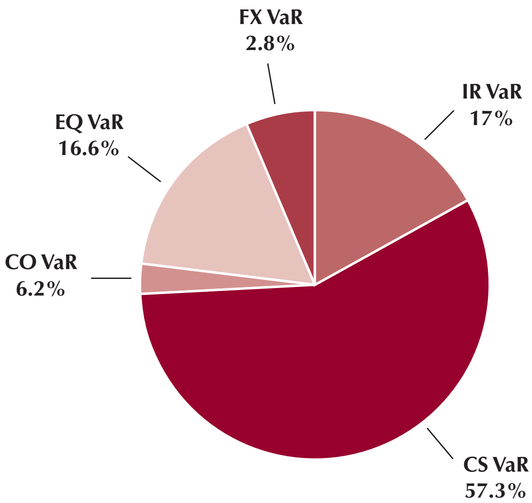
The trend described was attenuated in the last quarter of the year, at the same time as a reduction of the exposure in Italian government securities.

MPS CAPITAL SERVICES: SUPERVISORY TRADING BOOK
VAR 99% 1 DAY IN EUR/MLN



In terms of VaR breakdown by risk factors, as of 31/12/2018 the MPSCS portfolio is mainly absorbed by the Credit Spread risk factor (CS VaR, 57.3%). This is followed by the interest-rate risk factor (IR VaR, 17%), the equity risk factor (EQ VaR, 16.6%), the commodity risk factor (CO VaR 6.2%) and the Forex risk factor (FX VaR 2.8%).

VAR MPS CAPITAL SERVICES
Supervisory trading book
VaR Breakdown per Risk Factor: 31/12/2018



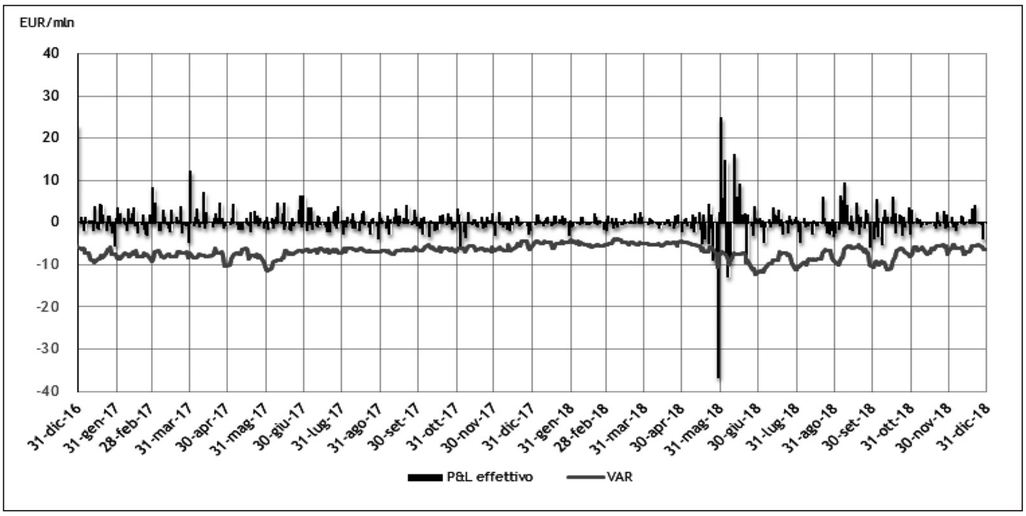
MPS CAPITAL SERVICES VaR PNV 99% 1 day in EUR/mln		
	VaR	Date
Period End	6.46	31/12/2018
Minimum	3.80	09/03/2018
Maximum	12.18	28/06/2018
Average	6.78	

During 2018 MPSCS's RTB VaR oscillated between a minimum of € 3.8 million at 9/03/2018 and a maximum of € 12.18 million at 28/06/2018 recording an average value of € 6.78 million. The RTB VaR at 31/12/2018 was € 6.46 million.

VaR model backtesting

The MPS Group has implemented a structure of retrospective tests in compliance with the current regulations for Market Risks within its risk management system.
Backtesting involves checks carried out on the results of the VaR model with respect to the daily change in the portfolio value, in order to evaluate the predictive ability of the model in terms of the accuracy of the risk measurements produced. If the model is robust, then the periodic comparison of the daily estimate of the VaR with the daily losses from trading activities related to the following day should show that the effective losses are higher than the VaR with a frequency in line with that defined by the confidence level.
In the light of the current regulatory provisions, the Risk Management Area has found it appropriate to carry out the test using theoretical and effective backtesting, and to integrate it within the Group's management reporting systems. The first type of test (Theoretical Backtesting) has greater statistical significance in reference to the evaluation of the accuracy of the VaR model ("non-contaminated test").
The second type of test (Effective Backtesting), answers the need to verify the predictive reliability of the VaR model in reference to the actual operations of the Bank (daily trading losses and gains), net of the effects of interest maturing between day t-1 and t for securities and the effect of fees.
These "net" P&L results are compared with the VaR of the previous day. If the losses are greater than those predicted by the model, a so-called "exception" is recorded.
The graph below shows the results of the Effective Backtesting of the internal Market Risk Model, in relation to the Bank's Supervisory Trading Book for 2018:

MPS CAPITAL SERVICES EFFECTIVE BACK TESTING OF SUPERVISORY TRADING BOOK



There were 5 exceptions resulting from the backtesting in the first half of 2018. These exceptions were concentrated between the end of May and June 2018, as consequence of the increase in volatility of the Italian credit spread due to the climate of political uncertainty that arose in the period following the elections with regard to formation of the new Government.

QUALITATIVE INFORMATION

A. GENERAL ASPECTS

A.1 Interest Rate Risk

The Bank's trading activity is carried out by the Global Markets Department. The bank manages a portfolio of its own which contains trading positions on rates and on credit. In general, interest rate positions are taken on through the purchase or sale of bonds, as well as through the construction of positions in listed derivatives (for example futures) and OTC instruments (for example IRSs, swaptions). The activity is carried out exclusively on the Bank's own behalf, with absolute return targets, in compliance with the delegated limits in terms of VaR and monthly and annual Stop Loss.

As regards the credit risk present in the trading book, in general the positions on securities are managed both by purchase or sale of bonds issued by companies, and through the construction of synthetic positions in derivative instruments. The activity aims to obtain long or short positions on single issuers, or a long or short exposure on particular types of securities. The activity is carried out exclusively on the Bank's own behalf, with absolute return targets, and in compliance with the further specific issuer and concentration risk limits.

A.2 Price Risk

With reference to the price risk factor the Bank manages an owned portfolio and assumes trading positions on equities, indexes and commodities. In general, equity security positions are taken on through the purchase or sale of shares, as well as through the construction of positions in listed derivatives (for example futures) and OTC instruments (for example options). The activity is carried out exclusively on the Bank's own behalf, with absolute return targets, in compliance with the delegated limits of VaR and monthly and annual Stop Loss. The trading is carried out by the Global Markets Department.

B. Interest rate risk and price risk: management processes and measurement methods

With regard to the market risk management process pertaining to management and the methods for gauging the interest rate risk and the price risk, reference should be made to the matters already described in the section “The risk management model for market risks inherent to the trading portfolio”.

QUANTITATIVE INFORMATION

1. Supervisory trading book: breakdown by residual life (repricing date) of the on-balance-sheet financial assets and liabilities and the financial derivatives.

This table is not provided in that a sensitivity analysis is provided for interest rate and price risk for the supervisory trading book on the basis of internal models.

2. Supervisory trading book: breakdown of exposures for equity securities and stock indexes for the main stock market countries.

This table is not provided in that a sensitivity analysis is provided for interest rate and price risk for the supervisory trading book on the basis of internal models.

3. Supervisory trading book - internal models and other methods for sensitivity analysis

The interest rate and price risk of the Trading Book is monitored in terms of VaR and scenario analysis.

3.1 Interest Rate Risk

The positions are managed by special desks, each with its own specific operating limits. Each desk adopts an integrated risk management approach (also for risks other than interest rate risk, when permitted) in order to benefit from the natural hedges deriving from simultaneously holding positions whose risk factors are not perfectly correlated.
The positions pertaining to the Trading Book are all classified for accounting purposes as Held For Trading, and Market Value changes are recorded directly in the Income Statement.
The simulated interest rate scenarios are:
• parallel shift +100 bps on all the interest rate curves and inflation curves;
• parallel shift -100 bps on all the interest rate curves and inflation curves;
• parallel shift of +1% of all the volatility surfaces of all the interest rate curves.

The overall effect of the scenario analyses is presented below:

MPS CAPITAL SERVICES Trading Portfolio
Figures in € millions

Risk Family	Scenario	Total Effect
Interest Rate	+ 100 bps on all curves	15.38
Interest Rate	- 100 bps on all curves	(14.56)
Interest Rate	+1 point interest rate volatility	0.00

To complete the interest rate risk analysis, the sensitivity analysis of the Bank's Trading Book credit spread risk linked to the volatility of issuers' credit spreads is reported below. The simulated scenario for the sensitivity analysis is:
• parallel shift of +1 bp on all credit spreads.

MPS CAPITAL SERVICES Trading Portfolio
Figures in € millions

Risk Family	Scenario	Total Effect
Credit Spread	+ 1bp on all curves	(1017)

3.2 Price Risk

The positions are managed by special desks, each with its own specific operating limits. Each desk adopts an integrated risk management approach (also for risks other than the rate risk, when allowed) in order to benefit from the natural hedges deriving from simultaneously holding positions whose risk factors are not perfectly correlated.
The simulated price scenarios are:
• +1% of each equity, commodity, index price,
• -1% of each equity, commodity, index price,
• +1% of all the volatility surfaces of all the equity and commodity risk factors.
The positions pertaining to the Trading Book are all classified for accounting purposes as Held For Trading, and Market Value changes are recorded directly in the Income Statement. The overall effect of the scenario analyses for the Equity and Commodity segments is presented below:

MPS CAPITAL SERVICES Trading Portfolio
Figures in € millions

Risk Family	Scenario	Total Effect
Equity	+1% Equity Prices (prices, indexes)	(2.58)
Equity	-1% Equity Prices (prices, indexes)	2.46
Equity	+1 point Equity Volatility	0.07

MPS CAPITAL SERVICES Trading Portfolio
Figures in € millions

Risk Family	Scenario	Total Effect
Commodity	+1% commodity prices	0.04
Commodity	-1% commodity prices	(0.04)
Commodity	+1 point commodity volatility	(0.02)

2.2 Interest rate risk and price risk - banking book

QUALITATIVE INFORMATION

A. Interest rate risk and price risk: general aspects, management processes and measurement methods

A.1 Interest Rate Risk

The Banking Book consists of all exposures not contained in the Trading Portfolio and, in accordance with international best practices, identifies all the Bank's commercial transactions associated with transforming maturity dates of assets and liabilities and financial assets for the ALM (treasury and risk hedging derivatives).
The definition of the perimeter of the banking book (aligned with that of the regulatory banking book) and the process of centralising management of the ALM is governed by the Parent Company's Board of Directors in line with the instructions provided in the supervisory regulations (Circular n° 285 issued by the Bank of Italy). The framework involves the centralisation of Asset & Liability Management in the Parent Company's Finance, Treasury and Capital Management Area (FTCMA) and the definition and monitoring of the operating limits in view of the interest rate risk of the Montepaschi Group's Banking Book.
The operating and strategic choices of the Banking Book, adopted by the Finance and Liquidity Committee and monitored by the Parent Company's Risk Management Committee, are based first of all on exposure to the interest rate risk for a change in the economic value of the assets and liabilities of the Banking Book, applying a parallel shift of 25 bps, 100 bps and 200 bps, the latter in accordance with the provisions of the "second pillar" of the Basel Regulations. Sensitivity analyses of the Interest Margin are also regularly carried out for different interest rate change assumptions. The ALM model of the Montepaschi Group, incorporates in the measurements of the exchange rate risk a behavioural model which takes into account the phenomenon of early repayments of mortgage loans (prepayment risk). The economic value sensitivity measurements are carried out excluding the development of the cash flows from the components not directly related to interest rate risk.
The Group is engaged in the continual updating of the risk measurement methods, through a gradual refinement of the estimation models, in order to include the main phenomena that over time modify the interest-rate risk profile of the banking book.
The Group has adopted a system for governing and managing interest rate risk which, in accordance with the provisions of the Supervisory Authority, employs:
- a quantitative model, on the basis of which the exposure of the Group and of its individual companies/structures to interest rate risk is calculated, in terms of risk indicators;
- risk monitoring processes, aimed at verifying compliance with the operating limits assigned to the Group as a whole and to individual business units;
- risk control and management processes, aimed at carrying out adequate initiatives to optimise the risk profile and to activate any necessary corrective actions.

Within the aforesaid system, the Parent Company centralises the following responsibilities:
- definition of the policies for managing the Group's Banking Book and controlling the related interest rate risk;
- coordination of the implementation of the aforesaid policies within the companies included in the reference perimeter;
- governing the Group's short, medium and long term interest rate risk, both overall and in terms of each individual company, through the centralised operating management.

In its governing function, therefore, the Parent Company defines criteria, policies, responsibilities, processes, limits and instruments for managing the interest rate risk.
The Group Companies, among which the Bank, included in the application perimeter are responsible for complying with the interest rate policies and risk limits defined by the Parent Company and with the capital requirements set by the competent Supervisory Authorities.
Within the defined model, the Parent Company's Finance, Cash and Capital Management Department is responsible for the operating management of the exchange and liquidity risk of the Group as a whole.
Specifically, within the FTCMA, the Strategic Risk Governance Service handles the short-term interest rate risk and the structural interest rate risk. The Area also monitors and manages hedges in accordance with the accounting policies, single monitoring for the formation of the internal interest rates of the "network" (BMPS and other Group companies) for the Euro and currency transactions with maturities beyond the short-term.

A.2 Price Risk

MPSCS's Banking Book subject to price risk is represented by equity instruments classified under the items 20.c "Financial assets obligatorily measured at fair value through profit or loss", 30. "Financial assets measured at fair value through other comprehensive income" and 70. Equity investments.
Measurement of price risk on the Bank's Banking Book is carried out on equity positions held for mainly strategic or institutional/instrumental purposes other than equity investments. The asset relevant for these purposes consists almost exclusively of shares of the Parent Company acquired in 2017 following the so-called "burden sharing" (cf. comment in the paragraph "Equity investments" in the Report on Operations), booked to the aforementioned item 30. Given the limited significance at the consolidated level and owing to the fact that it does not derive from an investment strategy resolved, but from a conversion with a view to burden sharing of a position in subordinated liabilities of the Parent Company, the assets in question are not subjected to a specific process for the management and control of price risk.
In general, assets other than shares of the Parent Company are subject in the same way as other financial assets to monitoring of the trend in value and of the related accounting impact on the equity (through the OCI reserves): given the low significance, no specific information is provided on the internal risk management and control processes concerning the price risk of the banking book.
We must stress that, with reference to the component consisting of equity investments, the internal measurement system uses a measure derived from the regulatory approach, using the standardised approach, to determine Internal Capital. This method entails the exposures in equity instruments being assigned a risk-weighting factor of 100% or 150% if at high risk, unless they have to be deducted from Own Funds. The mechanisms of deduction from Own Funds were innovated by the new supervisory rules (CRD4/CRR), which further widened the perimeter including also investments in non-significant financial sector subjects (<10%), and which introduced excesses on the deduction.

B. Fair value hedging activities

C. Cash flow hedging activities

D. Foreign investment hedging activities
The Bank does not have IAS hedging transactions in place.

QUANTITATIVE INFORMATION

1. Banking book: breakdown by residual life (repricing date) of the financial assets and liabilities

This table is not provided in that a sensitivity analysis is provided for interest rate and price risk for the banking book on the basis of internal models.

2. Banking book: internal models and other methods for sensitivity analysis

2.1 Interest Rate Risk

The Bank's sensitivity, at 31 December 2018, presented a risk exposure profile due to a rise in interest rates. The economic value at risk for a +100 bps parallel shift of the rates curves at year end amounted to € -20.27 million and € +10.94 million for a shift of -100 bps.
The sensitivity of the Bank's net interest income (Margin Sensitivity) in the event of a rise in interest rates of 25bp amounted at the end of 2018 to € +0.16 million (€ -0.22 million for -25 bps).

2.2 Price Risk

At the end of 2018 there were no positions in equities held for mainly strategic or institutional/instrumental purposes.

2.3 EXCHANGE RATE RISK

QUALITATIVE INFORMATION

A. Exchange rate risk: general aspects, management processes and measurement methods.

B. Exchange rate risk hedging activities.

A.1 Regulatory trading book
Exposure to exchange rate risk is of a limited amount and derives mainly from the role played by the Bank in the activity of:
- trading of structured products and of the related hedges put in place, which, owing to their characteristics, entail exposure in non-euro currencies;
- market maker for derivatives carried out for the purpose of hedging the MPS Group's corporate customers.

Operations are in fact concentrated mainly on the crosses of the main G7 currencies. The activity is essentially based on trading and on the aggregate management of risks with a short-term view and with a substantial hedging of the risks originated from commercial transactions. As a risk mitigation strategy, the Bank obtains funding in the same currency as the assets, through deposits with the Parent Company (when necessary) or through the synthetic transformation of funding into Euro. The main financial instruments used in this segment are spot forwards, options and futures. The risks are measured and monitored, as in the other segments, via sensitivity tests and VaR; consequently reference should be made to the description provided above. Management of this risk takes place by aggregating all the risk factors indicated above using the Risk Management system of the Murex application. The activity is carried out mainly by the Global Markets Department, through its own desks that manage their own exposure individually within the delegated limits and in keeping with the trading strategy.

A.2 Banking book
With regard to this type of portfolio, the exchange rate risk is represented by losses which the Bank could incur due to sudden fluctuations in the exchange rates should foreign currency loans and deposits not be balanced. Typically, foreign currency investments are financed by deposits expressed in the same currency without incurring any significant exchange rate risk. At the reporting date of these financial statements the Bank had an essentially balanced foreign exchange position for the banking book.

QUANTITATIVE INFORMATION

1. Distribution by currency of assets, liabilities and derivatives

Items / Currency	*US Dollar*	*Canadian Dollar*	*English Pound*	*Yen*	*Swiss Franc*	*Other currencies*
A. Financial assets	**346,085**	**1,915**	**2,373**	**18,679**	**35,756**	**41,802**
A.1 Debt securities	132,565	-	437	-	1,599	2
A.2 Equity securities	18,496	-	-	887	1,646	1,210
A.3 Loans to banks	8,354	1,915	1,936	4	29,963	36,196
A.4 Loans to customers	186,670	-	-	17,788	2,548	4,394
A.5 Other financial assets						
B. Other Assets	**5**	**-**	**-**		**78**	**5**
C. Financial liabilities	**(429,691)**	**0**	**0**	**(13,179)**	**(10,242)**	**(18,225)**
C.1 Due to banks	(424,698)	-		(11,983)	(10,242)	(18,225)
C.2 Due to customers	(4,993)	-	-	(1,196)	-	-
C.3 Debt securities						
C.4 Other financial liabilities						
D. Other liabilities	**-**	**-**	**-**	**(1,274)**	**-**	**(66)**
E. Financial derivatives	**(131,438)**	**562**	**(33,720)**	**(4,099)**	**5,609**	**(27,197)**
- Options	75,087		(42,665)	(226)	2,238	(138,004)
+ long positions	265,884		6,508	1,860	2,238	346
+ short positions	190,797		49,173	2,086		138,350
- Other derivatives	(206,525)	562	8,945	(3,873)	3,371	110,807
+ long positions	1,161,513	799	38,707	6,039	6,959	153,970
+ short positions	1,368,038	237	29,762	9,912	3,588	43,163
Total on-balance-sheet assets	**346,090**	**1,915**	**2,373**	**18,679**	**35,834**	**41,807**
Total on-balance-sheet liabilities	**(429,691)**	**0**	**0**	**(14,453)**	**(10,242)**	**(18,291)**
Differences (+/-)	**(83,601)**	**1,915**	**2,373**	**4,226**	**25,592**	**23,516**

2. Internal models and other sensitivity analysis methods

The exchange risk is monitored in terms of VaR and analysis scenarios (for the methodology, please refer to the paragraph “The risk management model for market risks related to the trading book”).

The simulated scenarios on exchange rates are:
• +1% of all exchange rates against EUR,
• -1% of all exchange rates against EUR,
• +1% of all volatility surfaces of all exchange rates.

The effect on operating income and on profit for the year was estimated considering only positions classified in the accounts as FVTPL, for which changes in Market Value are recognised directly in the Income Statement. The effect on shareholders’ equity is estimated instead with reference to positions classified in the accounts as FVOCI and to the related hedging under a Fair Value Hedging (FVH) scheme, if present. The total effect is reflected by the algebraic sum of the two components. A summary of the scenario analysis follows.

MPS CAPITAL SERVICES
Figures in € millions

Risk Family	Scenario	Effect on operating income and economic result	Effect on Shareholders’ Equity	Total Effect
Forex	+1% exchange rates against EUR 0.14 (0.01)	0.13		
Forex	-1% exchange rates against EUR	(0.13)	0.01	(0.12)
Forex	+1 point Forex volatility	0.12	0.00	0.12

Section 3 - Derivative instruments and hedging policies

3.1 DERIVATIVE INSTRUMENTS HELD FOR TRADING

A. FINANCIAL DERIVATIVES

A.1 Financial derivatives held for trading: period-end notional values

	Total 31/12/2018				*Total 31/12/2017*			
	Over the counter				*Over the counter*			
		Without central counterparties				*Without central counterparties*		
Underlying assets/ Type of derivatives	*Central counterparties*	*With netting agreements*	*Without netting agreements*	*Organised markets*	*Central counterparties*	*With netting agreements*	*Without netting agreements*	*Organised markets*
1. Debt securities and interest rates	**0**	**362,303,289**	**4,288,181**	**0**	**0**	**250,532,863**	**3,571,521**	**0**
a) options		33,588,331	1,435,378			38,775,669	1,704,858	
b) swaps		325,621,716	1,978,325			210,437,034	1,811,109	
c) forwards			874,478				55,554	
d) futures		3,093,242				1,320,160		
e) other								
2. Equity securities and stock market indices	**0**	**10,447,200**	**6,845**	**43,080**	**0**	**12,986,643**	**41,906**	**350,155**
a) options		8,604,912	6,845	20,363		12,309,209	41,906	285,250
b) swaps		1,445,575				244,368		
c) forwards								
d) futures		396,713		22,717		433,066		64,905
e) other								
3. Currencies and gold	**0**	**3,770,900**	**21,834**		**0**	**4,456,423**	**20,896**	
a) options		1,193,138	21,834			1,215,575	20,896	
b) swaps		1,392,082				1,584,514		
c) forwards		1,174,955				1,656,334		
d) futures		10,725						
e) other								
4. Commodities		**520,463**				**681,777**	**461**	
5. Other underlying assets								
Total	**0**	**377,041,852**	**4,316,860**	**43,080**	**0**	**268,657,706**	**3,634,784**	**350,155**

Note:
for completeness, we can inform you that complex contracts such as collar, strangle, straddle, etc. are presented breaking the instruments down into the elementary options.

A.2 Financial derivatives held for trading: positive and negative gross fair value - breakdown by products

Underlying assets/ Type of derivatives	Total 31/12/2018				Total 31/12/2017			
	Over the counter				Over the counter			
		Without central counterparties				Without central counterparties		
	Central counterparties	With netting agreements	Without netting agreements	Organised markets	Central counterparties	With netting agreements	Without netting agreements	Organised markets
1. Positive fair value	**0**	**4,571,623**	**88,456**	**4,489**	**0**	**4,537,265**	**138,467**	**6,806**
a) Options		259,688	13,236	4,489		377,444	46,845	6,806
b) Interest rate swaps		4,246,211	75,220			4,083,409	91,224	
c) Cross currency swaps		10,224				18,200		
d) Equity swaps		17,418				11,819		
e) Forwards		9,822				29,800	397	
f) Futures		2,395				1,671		
g) Others		25,865				14,922	1	
1. Negative fair value	**0**	**2,823,056**	**39,930**	**4**	**0**	**2,971,282**	**4,218**	**2,251**
a) Options		276,437	1,228	4		538,963	1,503	2,251
b) Interest rate swaps		2,439,089	1,059			2,347,211	2,715	
c) Cross currency swaps		33,327				38,962		
d) Equity swaps		30,642				4,523		
e) Forwards		22,376	37,643			21,386		
f) Futures		3,721				3,533		
g) Others		17,464				16,704		
Total	**0**	**7,394,679**	**128,386**	**4,493**	**0**	**7,508,547**	**142,685**	**9,057**

A.3 OTC financial derivatives held for trading: notional values, positive and negative gross fair value by counterparties

Contracts not included in netting agreements	*Central counterparties*	*Banks*	*Other financial companies*	*Others*
1. Debt securities and interest rates		**1,067,794**	**673,926**	**2,588,080**
- notional value		1,067,785	679,843	2,540,554
- positive fair value		9	2,299	79,044
- negative fair value			8,216	31,518
2. Equity securities and stock market indices		**538**	**13,171**	**1**
- notional value		321	6,523	
- positive fair value		217	6,648	1
- negative fair value				
3. Currencies and gold				**21,875**
- notional value				21,834
- positive fair value				238
- negative fair value				197
4. Commodities				
- notional value				
- positive fair value				
- negative fair value				
5. Other				
- notional value				
- positive fair value				
- negative fair value				
- future exposure				
Contracts included in netting agreements				
1. Debt securities and interest rates		**192,836,848**	**170,596,190**	**669,466**
- notional value		192,336,904	169,316,713	649,672
- positive fair value		1,774,707	2,543,773	19,940
- negative fair value		1,274,763	1,264,296	146
2. Equity securities and stock market indices		**2,314,758**	**8,115,590**	**0**
- notional value		2,316,505	8,130,696	
- positive fair value		50,354	124,250	
- negative fair value		52,101	139,356	
3. Currencies and gold		**3,435,874**	**292,901**	**0**
- notional value		3,479,205	291,695	
- positive fair value		26,884	1,479	
- negative fair value		70,215	273	
4. Commodities		**163,508**	**365,285**	**0**
- notional value		148,506	371,956	
- positive fair value		23,093	7,144	
- negative fair value		8,091	13,815	
5. Other				
- notional value				
- positive fair value				
- negative fair value				

A.4 Residual life of OTC financial derivatives held for trading: notional values

	Underlying elements / Residual life	*Up to 1 year*	*Over 1 year and up to 5 years*	*Over 5 years*	*Total*
A.	**Supervisory trading book**	**114,268,798**	**216,901,904**	**50,188,010**	**381,358,712**
A1	Financial derivatives on debt securities and interest rates	106,064,743	210,548,651	49,978,077	**366,591,471**
A2	Financial derivatives on equity securities and stock indexes	5,284,809	4,959,303	209,933	**10,454,045**
A3	Financial derivatives on foreign currencies and gold	2,428,463	1,364,271		**3,792,734**
A4	Financial derivatives on other valuables	490,783	29,679		**520,462**
A5	Other financial derivatives				**0**
	Total 31/12/2018	**114,268,798**	**216,901,904**	**50,188,010**	**381,358,712**
	Total 31/12/2017	**55,461,817**	**168,079,465**	**48,751,209**	**272,292,491**

In this table the remaining life is determined with reference to the contractual maturity of the derivatives in question, except for the interest rate swaps (IRSs) with variable notional capital, for which the remaining life has been calculated with reference to the single IRS into which they can be broken down.

B. CREDIT DERIVATIVES

B.1 Credit derivatives held for trading: period-end notional values

Transaction categories	Banking book	
	on one item	on several items (basket)
1. Protection purchases		
a) credit default products	523,552	279,400
b) credit spread products		
c) total rate of return swaps		
d) other		
Total 31/12/2018	**523,552**	**279,400**
Total 31/12/2017	**563,793**	**58,814**
2. Protection sales		
a) credit default products	2,715,109	288,570
b) credit spread products		
c) total rate of return swaps		
d) other		
Total 31/12/2018	**2,715,109**	**288,570**
Total 31/12/2017	**2,321,487**	**3,814**

B.2 Credit derivatives held for trading: positive and negative gross fair value - breakdown by products

Portfolio / Type of derivative	31/12/2018	31/12/2017
A. Positive fair value		
a) Credit default products	14,596	11,415
b) Credit spread products		
c) Total rate of return swaps		
d) Others		
Total	**14,596**	**11,415**
B. Negative fair value		**34,211**
a) Credit default products	56,429	34,211
b) Credit spread products		
c) Total rate of return swaps		
d) Others		
Total	**56,429**	**34,211**

B.3 OTC credit derivatives held for trading: notional values, positive and negative gross fair value by counterparties

Contracts not included in netting agreements	*Central counterparties*	*Banks*	*Other financial companies*	*Others*
1. Protection purchase				
- notional value				
- positive fair value				
- negative fair value				
2. Protection sale				
- notional value				
- positive fair value				
- negative fair value				
Contracts included in netting agreements				
1. Protection purchase				
- notional value		461,980	340,972	
- positive fair value		7,756	203	
- negative fair value		2,278	4,310	
2. Protection sale				
- notional value		334,893	2,668,786	
- positive fair value		1,983	4,655	
- negative fair value		90	49,752	

B.4 Residual life of OTC credit derivatives held for trading: notional values

Underlying elements / Residual life	*Up to 1 year*	*Over 1 year and up to 5 years*	*Over 5 years*	*Total*
1. Protection sales	114,500	2,079,894	809,285	3,003,679
2. Protection purchases	114,500	558,452	130,000	802,952
Total 31/03/2018	**229,000**	**2,638,346**	**939,285**	**3,806,631**
Total 31/12/2017	**135,801**	**1,274,069**	**1,538,040**	**2,947,910**

In this table, residual life is determined referring to the contractual maturity of the derivatives.

B.5 Credit derivatives connected with the fair value option: annual changes

Not present in the financial statements.

3.2 ACCOUNTING HEDGES

Not present in the financial statements.

3.3 OTHER INFORMATION ON DERIVATIVE INSTRUMENTS HELD FOR TRADING AND FOR HEDGING

A. FINANCIAL AND CREDIT DERIVATIVES

A.1 OTC financial and credit derivatives: net fair value by counterparty

Contracts included in netting agreements	*Central counterparties*	*Banks*	*Other financial companies*	*Others*
A. Financial derivatives				
1. Debt securities and interest rates				
- notional value		193,404,689	169,996,556	3,190,226
- positive net fair value		9	2,299	79,044
- negative net fair value			8,216	31,518
2. Equity securities and stock market indices				
- notional value		2,316,826	8,137,219	
- positive net fair value		217	6,648	
- negative net fair value				
3. Currencies and gold				
- notional value		3,479,205	291,695	
- positive net fair value				21,834
- negative net fair value				238
4. Commodities				197
- notional value		148,506	371,956	
- positive net fair value				
- negative net fair value				
5. Other				
- notional value				
- positive net fair value		611,877	1,250,260	19,940
- negative net fair value		134,639	36,159	146
A. Credit derivatives				
1. Protection purchase				
- notional value		461,980	340,972	
- positive net fair value			3,042	
- negative net fair value				
2. Protection sale				
- notional value		334,893	2,668,786	
- positive net fair value				
- negative net fair value			2,957	

SECTION 4 - LIQUIDITY RISK

QUALITATIVE INFORMATION

A. Liquidity risk: general aspects, management processes and measurement methods

During 2018 the Group continued to strengthen and make more efficient the strategic and operating processes for managing liquidity risk, paying particular attention to the integration of forward-looking projections for the main liquidity indicators in the context of the corporate decision-making processes.

Group Liquidity Risk Framework
Several years ago the MPS Group adopted a Liquidity Risk Framework, understood as the set of tools, methods, organisational and governance systems which ensures both compliance with national and international regulations and adequate management of the liquidity risk in the short (Operating Liquidity) and medium/long term (Structural Liquidity), under normal business conditions and in the event of turbulence. The Montepaschi Group's liquidity risk reference model is a “centralised” type, which involves management of short-term liquidity reserves and medium/long-term financial balance at the parent company level, guaranteeing solvency on an individual and consolidated basis for the subsidiaries.
Management of the Group’s Operating Liquidity pursues the purpose of ensuring the Group’s ability to satisfy the short-term cash payment commitments. The essential condition for normal operational continuity of the banking activity is to maintain a sustainable difference between the incoming and outgoing cash flows in the short term. The measure of reference in this sphere is the difference between the accumulated net cash flow and the Counterbalancing Capacity, i.e. the liquidity reserve which allows for dealing with stress conditions in the short term, as well as the regulatory liquidity coverage ratio (LCR) - delegated regulation. From the point of view of the very short term, the MPS Group has adopted the system of analysis and monitoring of the intraday liquidity with the objective of guaranteeing the normal development of the treasury day and its ability to meet its intra-day payment commitments.
Management of the Group’s Structural Liquidity aims to ensure the financial balance of the structure according to due dates over a period of time of more than one year, at both Group level and at that of the single companies. Maintaining an adequate dynamic ratio between medium/long term liabilities and assets is aimed at avoiding pressure in respect of both present and future short term collections. Gap ratios serve as the reference metric, measuring the ratio between total loans and funding maturing after 12 months and 3 years, as well as the ratio between loans and commercial funding independent of maturity, in addition to the regulatory net stable funding ratio (NSFR), based on the BCBS definition (Basel Committee for Bank Supervision). The Group has also defined and formalised the Asset Encumbrance management and monitoring framework with the objective of analysing:
- the overall degree of commitment for total assets;
- the existence of a sufficient quantity of assets that can be committed but are free;
- the Group’s ability to transform bank assets into eligible assets (or equivalently to commit non-eligible assets in bilateral operations).

The liquidity position is monitored both under normal conditions in the course of business and in Stress Scenarios of a specific and/or systemic nature according to the Liquidity Stress Test Framework. The exercises have the dual objective of bringing to light immediately the Bank’s main vulnerability to liquidity risk and allowing for prudential determination of the supervisory limits to be applied to the liquidity risk measurement metrics in the context of the annual Risk Appetite Statement.
In the context of the Risk Appetite Framework, the Liquidity Risk Framework contemplates the identification of the

liquidity risk tolerance thresholds, understood as maximum exposure to risk deemed sustainable under normal business conditions and incorporating situations of stress. The short term and medium/long term limits for liquidity risk are based on the definition of these Risk Appetite thresholds. The operating limits system, known as Liquidity Risk Limits, is defined so as to promptly identify any nearing of the risk tolerance threshold defined in the annual process to develop the Risk Appetite Statement.

For immediate warning of possible vulnerability of the liquidity position, the Group has set up Early Warnings, distinguishing them as generic or specific according to whether the purpose of the single indicator is to warn of possible critical aspects regarding the entire economic contest, or specifically to the Group.

Management of operating and structural liquidity is governed by the parent company's Liquidity Management Department, which is responsible for defining and implementing short and medium/long-term funding strategies.

With reference to management of operating liquidity, the Liquidity Management Department manages the Group's liquidity reserves, in order to guarantee the Bank's ability to face planned and unplanned outflows, making use of the various instruments available on the interbank market (unsecured deposits, collateralised deposits, repos), as well as operations with the Central Bank.

With reference to management of structural liquidity, the Liquidity Management Department pursues the objectives detailed in the annual Funding Plan which outlines the medium/long-term strategies in operational terms defined in the Liquidity and Funding Strategy. This defines guidelines for funding activities in terms of risk appetite at the Group level, with a three year time horizon, in compliance with the multi-year risk tolerance thresholds relative to operating and structural liquidity, both internal and regulatory, as defined in the Group's Risk Appetite Statement (RAS).

Additionally, the Liquidity Management Department, in support of the Funding Plan, prepares the **Contingency Funding Plan**, the operating tool to manage liquidity risk that defines action strategies in the case of extreme liquidity tensions, establishing procedures and actions that can be readily put into place to obtain financing sources in the case of emergency. The strategies to be applied are defined on a case by case basis by the Executive Committee during the Liquidity Stress/Crisis session, in consideration of the type, duration and intensity of the crisis and the reference scenario at the time the crisis occurs.

Finally overall internal assessment of liquidity is carried out periodically as part of the strategic ILAAP process consisting mainly of:

- ILAAP Outcomes, that is assessments of a quantitative type (inherent risk) and qualitative type (risk management and controls) on the risk positioning prepared by the Risk Control Unit for the Board of Directors;
- Liquidity Adequacy Statement (LAS), that is the summary statement of the Board of Directors that expresses its vision of liquidity adequacy management.

QUANTITATIVE INFORMATION

Quantitative information regarding liquidity risk is shown below and is broken down based on exposures in Euro and other currencies.

1.1.A Breakdown by contractual residual maturity of financial assets and liabilities - EURO

Items / Maturities	*On demand*	*From over 1 day to 7 days*	*From over 7 days to 15 days*	*From over 15 days to 1 month*	*From over 1 month to 3 months*	*From over 3 months to 6 months*	*From over 6 months to 1 year*	*From over 1 year to 5 years*	*Over 5 years*	*Unspecified duration*
Cash assets	**2,494,911**	**1,109,242**	**637,109**	**2,059,983**	**1,811,640**	**1,780,518**	**3,027,566**	**3,811,703**	**4,640,828**	**148,698**
A.1 Government securities	46	1	2		60,755	863,831	1,701,277	1,115,037	669,880	
A.2 Other debt securities	19,361	119	3,380	8,541	149,559	243,943	75,282	411,637	1,213,958	1,420
A.3 Units in collective investment undertakings	48,213									
A.4 Loans	2,427,291	1,109,122	633,727	2,051,442	1,601,326	672,744	1,251,007	2,285,029	2,756,990	147,278
- banks	1,872,948	385,266	145,270	1,613,918	418,314	449,391	376,290	12,364	325,000	5,325
- customers	554,343	723,856	488,457	437,524	1,183,012	223,353	874,717	2,272,665	2,431,990	141,953
On-balance-sheet liabilities	**4,129,918**	**5,164,031**	**2,116,817**	**1,311,345**	**1,200,948**	**783,568**	**1,031,343**	**4,130,638**	**2,516,354**	
B.1 Current accounts and deposits	1,564,506	330,000	150,000	718,300	50,000	39,633	34,174	3,792,319	1,829,674	
- banks	1,561,343	330,000	150,000	718,300	50,000	39,633	34,174	3,792,319	1,829,674	
- customers	3,163									
B.2 Debt securities				3,436	6,413		9,849	50,000	400,000	
B.3 Other liabilities	2,565,412	4,834,031	1,966,817	589,609	1,144,535	743,935	987,320	288,319	286,680	
Off-balance sheet transactions	**25,121,762**	**18,547,230**	**990,945**	**376,071**	**2,860,524**	**1,591,104**	**1,201,944**	**4,696,569**	**3,409,636**	
C.1 Financial derivatives with exchange of capital										
- long positions	170,075	568,154	75,768	204,611	1,383,766	1,242,211	351,847	816,946	684,186	
- short positions	432,129	1,665,535	680,950	171,460	1,005,923	330,372	315,712	528,423	616,009	
C.2 Financial derivatives without exchange of principal										
- long positions	4,202,618									
- short positions	2,421,111									
C.3 Deposits and loans to be received										
- long positions	11,270,677				100,000					
- short positions		11,200,311			100,000		70,366			
C.4 Irrevocable commitments to grant finance										
- long positions	34,727	5,113,210	234,227		270,835	453	424,019	277,268	230,871	
- short positions	6,583,664	20								
C.5 Financial guarantees given	25					68		78		
C.6 Financial guarantees received										
C.7 Credit derivatives with exchange of capital										
- long positions						9,000	20,000	1,536,927	939,285	
- short positions						9,000	20,000	1,536,927	939,285	
C.8 Credit derivatives without exchange of principal										
- long positions	3,163									
- short positions	3,573									

1.1.B Breakdown by contractual residual maturity of financial assets and liabilities - OTHER CURRENCIES

Items / Maturities	*On demand*	*From over 1 day to 7 days*	*From over 7 days to 15 days*	*From over 15 days to 1 month*	*From over 1 month to 3 months*	*From over 3 months to 6 months*	*From over 6 months to 1 year*	*From over 1 year to 5 years*	*Over 5 years*	*Unspecified duration*
Cash assets	**154,778**		**9**	**27**	**1,668**	**5,498**	**5,852**	**152,088**	**100,105**	**86,637**
A.1 Government securities	5				6	41	47	175	1,664	
A.2 Other debt securities	12		9	27	379	2,937	1,358	60,659	80,763	
A.3 Units in collective investment undertakings	11,163									
A.4 Loans	143,598				1,283	2,520	4,447	91,254	17,678	86,637
- banks	71,858						498	4,234	1,778	
- customers	71,740				1,283	2,520	3,949	87,020	15,900	86,637
On-balance-sheet liabilities	**341,339**			**17,467**	**73,239**	**16,756**	**67**	**21,034**	**1,544**	
B.1 Current accounts and deposits	322,685			17,467	72,420	16,689				
- banks	322,685			17,467	72,420	16,689				
- customers										
B.2 Debt securities										
B.3 Other liabilities	18,654				819	67	67	21,034	1,544	
Off-balance sheet transactions	**572,487**	**53,987**	**351,362**	**57,534**	**1,450,959**	**763,244**	**269,231**	**1,648,021**	**819**	
C.1 Financial derivatives with exchange of capital										
- long positions	11,441	37,800	340,809	29,301	762,155	319,469	34,826	78,777		
- short positions	95,863	16,187	10,553	28,233	688,804	443,775	234,405	102,344		
C.2 Financial derivatives without exchange of principal										
- long positions	277,835									
- short positions	183,992									
C.3 Deposits and loans to be received										
- long positions										
- short positions										
C.4 Irrevocable commitments to grant finance										
- long positions									819	
- short positions	2,744									
C.5 Financial guarantees given										
C.6 Financial guarantees received										
C.7 Credit derivatives with exchange of capital										
- long positions								733,450		
- short positions								733,450		-
C.8 Credit derivatives without exchange of principal										
- long positions	612									
- short positions										

1.2. Self-securitisation transactions

Nothing to report at 31 December 2018.

SECTION 5 - OPERATIONAL RISKS

QUALITATIVE INFORMATION

A. Operational risks: general aspects, management processes and measurement methods

General aspects and Framework Structure
With an administrative provision issued on 12 June 2008, the Montepaschi Group was authorised by the Bank of Italy to use internal models for determining the capital requirements to cover credit and operational risks.
The adoption of the advanced model (AMA) requires banks to:

- develop an internal organisation which defines the roles of the bodies and the corporate departments involved in the operational risk management process;
- develop a control department for gathering and storage of data, calculation of the requirement, assessment of the risk profile and reporting;
- check on the quality of the management system and compliance with the legislative prescriptions on an ongoing basis;
- delegate the internal auditing body to make periodic checks on the Operational Risk management system;
- guarantee over time that the system is effectively used in the corporate operations (use tests).

For this purpose, the Montepaschi Group has developed an integrated system for the management of operational risk, an internal framework built on a governance model which sees all the companies in the scope of application of the AMA model involved. The approach defines the standards, methods and instruments which make it possible to assess the exposure to risk and the effects of the mitigation for each business area.
The advanced approach is conceived in such a way as to combine all the main disclosure sources in a standardised manner (information or data), both qualitative and quantitative (mixed Loss Distribution Approach - Scenario Model).
The quantitative component, of the Loss Distribution Approach (LDA) type, is based on the gathering, analysis and statistical modelling of the historical figures on internal and external loss (provided by the DIPO Consortium - Italian Database of Operating Losses).
The qualitative component is focused on the valuation of the risk profile of each unit and is based on the identification of relevant scenarios. In this context, the involvement of the companies in the AMA scope takes place through the identification of the processes and risks to be assessed, the assessment of the risks by the individuals responsible for the process, the identification of possible mitigation plans, discussions with the relevant units of the priorities and technical-economic feasibility of the mitigation measures.
This is followed by the monitoring of the implementation of the planned measures and of compliance with targets and deadlines.
The Framework identifies the operational risk control unit as the Group Operational Risk Management (ORM) Department (within the parent company's Chief Risk Officer Department).
The Group ORM calculates the capital requirement for covering the operational risks by means of the use of various components of the model (internal data, external data, context and control factors, qualitative analysis) supports the Top Management’s decision making process with a view to creating value by retaining, mitigating and transferring the detected risks and it collects, also for the other companies in the perimeter, the internal loss data and identifies the risks to be assessed in qualitative analyses.
All the main domestic banking and financial components come within the perimeter of the advanced approach (AMA), while for the remaining components and for the foreign companies the basic approaches are instead adopted.
At 31 December 2018 the coverage of the internal model, in terms of the relevant indicator, was more than 95%.

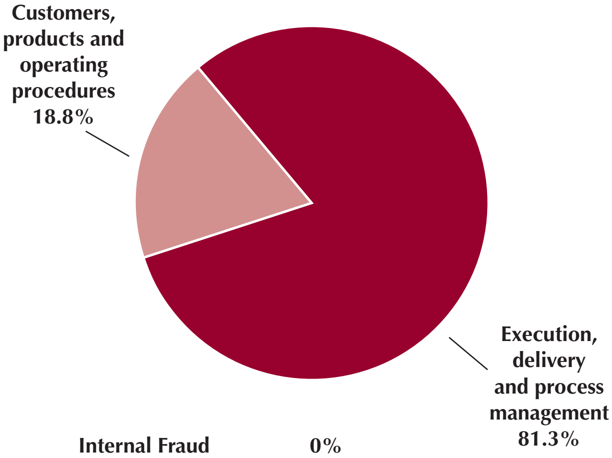
The ORM has also set up a reporting system that provides timely information about operational risks to the Top Management, which translates the strategic principles of the management system into specific management policies. The reports are regularly submitted to the Risk Management Committee and the decision-making bodies.
The adoption of the AMA model has assured, over time, a more knowledgeable management of operational risk, guaranteeing in practice a progressive reduction in the operational risk of the Bank and the Group.
As of 30 June 2017, the Advanced Measurement Model underwent a change involving an increase in the historical depth of internal loss data, going from 5 to 10 years, as well as the introduction of a scaling mechanism for external data, in order to prevent unexpected oscillations in the requirement.

QUANTITATIVE INFORMATION

The percentage distribution of the number of events and of the operating losses recorded in 2018 is given below, divided into the various risk classes mainly linked to the Bank's business, represented in practice by the offer of solutions to a wide range of financial and credit problems (medium and long-term credit products and those of a specialist type, corporate finance assets, capital market products and structured loans):

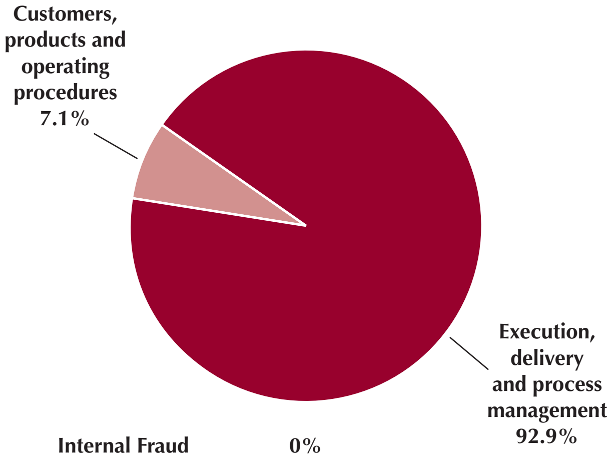
- **customers, products and operating procedures**: losses deriving from breaches relating to professional obligations vis-à-vis customers or from the nature or features of the product or service provided;
- **process execution, delivery and handling**: losses due to shortfalls in the finalization of the transactions or the handling of the processes, as well as losses due to relations with commercial counterparties, sellers and suppliers.

% DISTRIBUTION OF NUMBER OF EVENTS
MPS CAPITAL SERVICES - 31.12.2018



Internal Fraud	0%
External fraud	0%
Lending Ratios	0%
Damages to property, plant and equipment	0%
System malfunctions	0%

% DISTRIBUTION OF LOSSES
MPS CAPITAL SERVICES - 31.12.2018



Internal Fraud	0%
External fraud	0%
Lending Ratios	0%
Damages to property, plant and equipment	0%
System malfunctions	0%

At 31 December 2018 both the numbers of operational risk events and the operating losses were down compared to 2017.

The types of events with the most impact on the income statement were due to shortcomings in the completion of operations or in the management of processes ("Process execution, delivery and handling" class: 93% of the total).

Contingent liabilities related to legal actions

The risks inherent in or related to legal disputes - understood as such those involving judicial bodies and arbitrators - are subject to specific and careful examination by the Bank. In the case of disputes for which the outflow of economic resources to fulfil the implicit legal obligation is estimated as "*probable*", and it also seems possible to make a reliable estimate of the related amount, Provisions for Risk and Charges are set aside with statistical or analytical criteria. If an outflow of economic resources is possible, or when, although it is probable, it is not possible to make a reliable estimate of the financial expense, the contingent liability must be described in the Notes to the Financial Statements. As provided for in paragraph 92 of IAS 37, in extremely rare cases the indication of some or all the information required by the said standard on the subject of disclosure could have a serious adverse effect on the company's position in a dispute with third parties. In these cases the company does not have the obligation to provide the detailed information, but can limit itself to indicating the general nature of the dispute, explaining in any case the reasons that underlie the simplified disclosure.
For legal action with the greatest significance, for macro-category or individually, the main characteristics are illustrated below:

A) *Significant legal actions by macro-category*

A1) Dispute regarding breach of Italian Law 108/1996 on the subject of usury

The notion that the interest conventionally established constitutes usury is the subject of numerous legal actions following, mainly, a judgement of the Court of Cassation (no. 350 of 2013) which, placing itself apparently in contrast with the indications of the Bank of Italy (whose latest clarifications were issued in July 2013), ruled that "*for the purposes of application of art. 644 of the Italian Criminal Code, and of art. 1815 of the Italian Civil Code, paragraph 2, usury is understood as interest that exceeds the limit established by law at the moment in which it is promised or at least agreed, for any reason, therefore also as default interest"*. From the enunciation of this legal principle, we have seen the affirmation of a theory that leads to free loans if the current threshold interest rate is exceeded at the moment of signing, with a simplistic operation of adding together the standard and default interest rates (adding together the interest charged on the loan and interest on arrears). This position has been rejected by the majority of jurisprudence which has considered the addition of standard and default interest rates a logical not to mention a legal error.
In view of the prevailing orientation of the jurisprudence there has been a subsequent diversification of disputes on the subject of usury. In particular we have seen a growing number of actions in which, for the purposes of counting the threshold rate, any expenses (such as fees for early settlement or fees for contractual termination) are also added to the standard interest, expenses and charges received by the Bank under the terms of the contract.

MPS Capital Services Banca per le Imprese S.p.A./Etika Esco S.p.A. dispute

The joint-stock company Etika Esco (hereinafter the "Plaintiff" or "Company") launched a legal action against MPS Capital Services Banca per le Imprese S.p.A. (hereinafter "MPSCS" or the "Bank") at the Court of Florence, alleging the illegitimacy of the Bank's conduct as, after approving a loan of € 20,000,000.00 in favour of a company being set up (hereinafter "Newco Sviluppo Marina Velca") which was to have been wholly controlled by the Plaintiff, did not proceed with the signing of the contract and the consequent disbursements.
It must first be noted that the operation, the subject of an enquiry completed with the resolution of 7 September

2016, was structured to enable the Newco Sviluppo Marina Velca to complete a project for construction of a property complex of approximately 300 houses, and the renovation and expansion of a golf course, in an area owned by Sviluppo Marina Velca S.r.l., situated in the Municipality of Tarquinia (hereinafter “Property Project”).

The Property Project involved an Italian closed-end investment fund which, through a Luxembourg-law special purpose vehicle, held 100% of the capital of Sviluppo Marina Velca S.r.l.
The Bank had already intervened in support of the said project granting, in 2012, to Sviluppo Marina Velca S.r.l. a loan of € 9,400,000.00 (hereinafter the “2012 Loan”), which fell due on 31 July 2014 and of which there remained at September 2016, the period of approval of the loan involved in the legal action, approximately € 11,000,000.00 for principal, past-due interest, default and ancillary charges.
The Company taking over in the Property Project required the acquisition by Etika Esco of a special purpose vehicle (identified as Rell’s Risorse s.r.l.) which was to have purchased the shares of Sviluppo Marina Velca S.r.l. before proceeding to a merger by incorporation. The purchase of the shares of Sviluppo Marina Velca S.r.l. would have required the intervention of the Bank, as guaranteed creditor, in order to authorise the transfer of the shares subject to pledge guaranteeing the 2012 Loan.
Having explained the context of the operation planned by the Company, we can now illustrate briefly the allegations formulated in relation to the Bank’s conduct.
The Plaintiff complains in fact that, after an appointment had been fixed with a notary for transfer of the shares of Sviluppo Marina Velca S.r.l., the Bank communicated only the day before that it could not attend owing to what it claimed were internal delays.
Having missed this appointment for no reason, MPSCS was then said to have assumed an attitude of closure in relation to the Plaintiff, no longer answering the many requests to carry out the loan operation up to 15 March 2017, when the Bank communicated, with arguments and justifications said by the Company to be wholly insufficient, the expiry and/or revocation of the resolution of 7 September 2016.
The Plaintiff asserts that the conditions set by the Bank for the effectiveness of the resolution of 7 September 2016 were all met and, for those not fulfilled, should be considered as fulfilled under the terms of art. 1359 of the Italian Civil Code due to the actions and negligence of the Bank.
The non-completion of the operation to acquire the shares of Sviluppo Marina Velca s.r.l., first, and then of the loan contract with consequent non-disbursement of the amounts, was said to have caused enormous damage to the Company which was quantified at approximately € 96,000,000.00 of which: i) approximately Euro 46,000,000.00 as lost profit as it had not been able to achieve, in the role of General Contractor, the revenue deriving from construction of the Property Project and emerging damage consequent to the requests for payment of the penalties provided for in the construction contracts signed with a view to the aforesaid activity and ii) € 50,000,000.00 as further damage that will accrue while awaiting the amount that will be considered just.
The Bank joined the case regularly replying that none of the conditions detailed in the letter communicating that the loan had been resolved was fulfilled. It was also stressed that a few days after the operation was approved (17 October 2016) the Company had asked MPSCS for an advance on the first disbursement of € 2,600,000.00 to be guaranteed with a mortgage to be granted by the said incorporating company Sviluppo Marina Velca S.r.l., a request from which there emerged a worrying lack of liquidity in the Company which, instead, was supposed to invest, during the construction of the Property Project much more of its own funds.
The changes in creditworthiness that emerged following the aforementioned request for pre-financing, had not only led the Bank to deny the said new disbursement, but also to re-examine, in view of the Company’s manifest lack of liquidity, the operation already resolved arriving at a final decision not to confirm and, therefore, to revoke the said resolution granting the loan also in the light, besides, of the non-observance of the conditions to arrive at the signing of the loan contract.
During the further investigation carried out by the Bank it emerged that the hidden promoter of the operation was also

a person with a seriously unfavourable previous record to whom the Bank had previously refused a loan for the same project.

Concluding its arguments MPSCS made a counterclaim asking for the Plaintiff to be found guilty of vexatious litigation under the terms of art. 96 of the Italian Code of Civil Procedure.

On 22 January 2019 the hearing of first appearance and discussion was held under the terms of art. 183 of the Italian Code of Civil Procedure. The investigating judge, at the request of the parties, granted the terms for the rejoinders pursuant to art. 183, paragraph 6, of the Italian Code of Civil Procedure and adjourned the case for discussion of the evidence to the hearing of 24 September 2019.

With the rejoinder pursuant to art. 183, paragraph 6, no. 1 of the Italian Code of Civil Procedure filed by Etika Esco on 21 February 2019 it was specified that the total petitum is not € 96,000,000.00 because the damage suffered as a consequence of the facts described in the pleading amounts to € 46,188,000.00 “or in any case to a sum of not less than € 50,000,000.00 or more, due for the further damage that in the meantime will accrue for these reasons to the plaintiff, or, subordinately, to the payment of the different amount, also lower, which will be arrived at during the case and/or at which the Judge arrives for the purpose as an equitable amount”.

Part F
Information on Equity

SECTION 1 - THE BANK'S CAPITAL

A. QUALITATIVE INFORMATION

The MPS Group pursues strategic objectives focused on the quantitative and qualitative strengthening of the capital, on structural rebalancing of the liquidity and on achieving sustainable levels of profitability.
With this in view the capital management, planning and allocation activities are of fundamental importance for guaranteeing observance over time both of the minimum capital requirements established by the regulations and by the supervisory authorities and of the degree of risk appetite approved by the Parent Company's strategic supervisory body.

To this end the Risk Appetite Framework (RAF) is used; through this every year the target levels of capitalisation are estimated and the capital is allocated to the business units according to the development expectations and the estimated risk levels, verifying that the capital endowment is sufficient to guarantee observance of the minimum requirements: in the context of the RAF prospective capital adequacy assessments are carried out on a multi-annual time horizon, in both normal and stressful conditions. The analyses are carried out both at the Group level and at the level of all the single legal entities subject to regulatory capital requirements.
Achievement of the targets and compliance with the minimum regulatory requirements are monitored continuously during the year.
The formal corporate processes in which the RAF is applied on at least an annual basis are the budget, the risk appetite review and the ICAAP.
The Group defines the budget targets on the basis of a method for measuring correct corporate performance for the risk, the Risk Adjusted Performance Measurement (RAPM), through which the earnings results are determined net of the cost of the capital to be held for regulatory purposes against the level of risk assumed.
The concepts of capital used are the regulatory supervisory ones: Common Equity Tier 1, Tier 1 and Own Funds; in addition in the context of the RAPM metrics the Invested Capital is also used; this consists of the amount of own capital pertaining to the shareholders (equity) needed to achieve the Common Equity Tier 1 figures, both established in advance as target levels and achieved afterwards as final results.
The concepts of capital at risk used are the regulatory requirements, corresponding to risk weighted assets (RWA), determined on the basis of the rules defined in the regulatory provisions, and economic capital which corresponds to the estimated maximum losses on the measurable risks at a pre-set confidence interval and on the basis of internal models and rules internal to the Group. In the context of the RAPM metrics both measurements are used.

B. QUANTITATIVE INFORMATION

B.1 The Bank's capital: breakdown

Items / Balances	*31/12/2018*	*31/12/2017*
1. Capital	1,669,516	1,669,516
2. Share premiums		161,446
3. Reserves	(407,280)	110,427
- of profits	(407,280)	76,642
a) legal		*41,323*
b) statutory		
c) treasury shares		
d) other	*(407,280)*	*35,319*
- other		33,785
4. Equity instruments		
5. (Treasury shares)		
6. Valuation reserves	(141,441)	(2,242)
- Equity securities designated at fair value through other comprehensive income	*(137,125)*	
- Hedging of equity securities designated at fair value through other comprehensive income		
- Financial assets (other than equity securities) measured at fair value through other comprehensive income	*(1,871)*	*236*
- Property, plant and equipment		
- Intangible assets		
- Foreign investment hedging		
- Cash flow hedging		
- Exchange differences		
- Non-current assets and disposal groups held for sale		
- Financial liabilities designated at fair value through profit or loss (changes in own creditworthiness)		
- Actuarial gains (losses) relating to defined-benefit pension plans	*(2,445)*	*(2,478)*
- Portions of equity investment valuation reserves measured at equity		
- Special revaluation laws		
7. Profit (Loss) for the period	80,699	(632,937)
Total	**1,201,494**	**1,306,210**

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

Assets / Balances	*31/12/2018*		*31/12/2017*	
	Positive Reserve	*Negative Reserve*	*Positive Reserve*	*Negative Reserve*
1. Debt securities		(1,871)	414	(115)
2. Equity securities		(137,125)	39	
3. Loans				
Total	**0**	**(138,996)**	**453**	**(115)**

Note:
the values indicated are gross of tax effects.

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

	Debt securities	*Equity securities*	*Loans*
1. **Opening balances (*)**		**(101,174)**	
2. **Positive changes**	**2,450**	**38**	
2.1 Fair value increases		38	
2.2 Value adjustments for credit risk			
2.3 Transfer to income statement of negative reserves from impairment	2,450		
2.4 Transfers to other shareholder's equity components (equity securities)			
2.5 Other changes			
3. **Negative changes**	**5,032**	**35,989**	
3.1 Reductions of *fair value*	5,032	35,989	
3.2 Write-backs for credit risk			
3.3 Transfer to income statement of positive reserves from realisation			
3.4 Transfers to other shareholder's equity components (equity securities)			
3.5 Other changes			
4. Closing balances	**(2,582)**	**(137,125)**	

(*) The opening balance includes the effects deriving from first application of the new accounting standards IFRS 9 and IFRS 15 at 1 January 2018 described in the paragraph "Transition to the accounting standards IFRS 9 and IFRS 15".

B.4 Valuation reserves for defined benefit plans: yearly changes

	Severance indemnities	*Defined benefit pension funds*	*Tax effect*	*Total*
Opening balances	**(1,257)**	**(1,910)**	**689**	**(2,478)**
Revaluation of net liabilities/assets for defined benefits:				
Yield of plan assets net of interest				
Actuarial gains/losses deriving from changes in demographic assumptions	(6)	92	(23)	**62**
Actuarial gains/losses deriving from changes in financial assumptions	44	50	(26)	**68**
Actuarial gains/losses deriving from past experience	13	(143)	36	**(94)**
Changes in the effect of limitations on the availability of a net asset for defined benefit plans				
Gains/losses from termination of the fund envisaged in the terms of the plan				**0**
Other changes			(3)	**(3)**
Closing balances	**(1,206)**	**(1,911)**	**672**	**(2,445)**

SECTION 2 - OWN FUNDS AND CAPITAL RATIOS

For information on own funds and capital ratios, please see the Report on Operations and the disclosure on own funds and capital adequacy contained in the disclosure to the public ("Third Pillar") provided at the consolidated level, as provided for in Bank of Italy Circular 262 of 22 December 2005 - 5th update - available at the following address: https://www.gruppomps.it/investor-relations

Part G
Business Combinations regarding companies or business units

SECTION 1 - TRANSACTIONS CARRIED OUT DURING THE YEAR

During the year, no business combination transactions were carried out regarding companies or business segments.

SECTION 2 - TRANSACTIONS CARRIED OUT AFTER THE END OF THE YEAR

Nothing to report.

SECTION 3 - RETROSPECTIVE CORRECTIONS

No correction to report.

Part H
Transactions with related parties

In accordance with IAS 24 "key management personnel" includes the following: Directors, Statutory Auditors, General Manager, Assistant General Managers, Heads of Departments who are assigned autonomous decision-making powers.

1. Information about the remuneration of key management personnel

	31/12/2018	*31/12/2017*
Short-term benefits	1,462	1302
Benefits after the termination of the employment relationship		
Other long-term benefits		
Indemnity for the termination of the employment relationship		
Share-based payments		
Other remuneration		
Total	**1,462**	**1302**

2. Information on transactions with related parties

The tables presented below show the accounting effects of the transactions carried out with related parties (2.a with the Parent Company and other group companies; 2.b with key management personnel and other related parties).
In accordance with the accounting standard IAS 24 the Bank has identified its related parties and has complied with the consequent disclosure obligations.
On 4 December 2018 Banca Monte dei Paschi di Siena S.p.A. issued the new "Group Directive on management of prescriptive formalities on the subject of related parties, associated subjects and obligations of bank representatives", which replaced the "Group internal policy on transactions with related parties, associated subjects and obligations of bank representatives of 17.02.2015" and the "Global Policy on transactions with related parties, associated subjects and obligations of bank representatives" of 12.11.2014.
The Directive contains, in a single document, the Group governing conflicts of interest on the subject of transactions with related parties under the terms of CONSOB Regulation no. 17221/2010, with associated subjects under the terms of Bank of Italy Circular no. 263/2006 in Title V, chapter 5, and those on obligations of bank representatives under the terms of art. 136 of the CLB.
In particular, the Directive sets forth the principles and rules to be followed to oversee the risk deriving from situations of possible conflict of interest with certain subjects close to the Parent Comany's decision-making centres. The Directive is addressed to the Parent Bank and to all the subsidiaries, including MPS Capital Services S.p.A., which adopted it with a resolution of its Board of Directors on 21 December 2018.
The Directive was published on the Bank's website and the full version can be consulted at the following web address: http://www.mpscapitalservices.it/NR/rdonlyres/782FF399-FA35-4059-A7E1-E4D7FB7C9C8D/84586/operazioni_con_parti_collegate_e_soggetti_collegat.pdf

2.a Transactions with the Parent Company and with companies of the MPS Banking Group

Items/Balances	*Parent Company*	*MPS Group Companies*	*Total*	*Proportion*
Total financial assets	**5,776,005**	**85,614**	**5,861,619**	**23.253%**
- Financial assets held for trading	1,211,144	44,273	**1,255,417**	13.426%
- Financial assets designated at fair value				
- Financial assets obligatorily measured at fair value				
- Financial assets at fair value through other comprehensive income	22,087	126	**22,213**	23.308%
- Receivables from banks	4,542,753	36,907	**4,579,660**	80.779%
- Receivables from customers				
- Other Assets	21	4,308	**4,329**	1.700%
Total financial liabilities	**15,464,499**	**2,405**	**15,466,904**	**63.142%**
- Financial liabilities measured at amortised cost	15,120,337		**15,120,337**	72.148%
- Financial liabilities held for trading	335,408	13	**335,421**	9.673%
- Financial liabilities designated at fair value				
- Other liabilities	8,754	2,392	**11,146**	15.809%
Guarantees issued and commitments	**1,057,653**		**1,057,653**	**11.309%**
Income statement				
- Interest and similar income	56,274	14,411	**70,685**	23.321%
- Interest and similar expense	(112,514)		**(112,514)**	73.155%
- Fee income	250		**250**	0.548%
- Fee expense	(20,882)		**(20,882)**	58.688%
- Net value adjustments for credit risk	(552)	(5)	**(557)**	(3.257%)
- Operating costs and other expenses and income	(11,850)	(12,981)	**(24,831)**	28.801%

2.b Transactions with key management personnel and other related parties

Upon completion of the precautionary recapitalisation manoeuvre for the parent company, the Ministry of Economy and Finance (MEF) became the controlling shareholder for Banca Monte dei Paschi di Siena; the "MEF Perimeter" column in the table below indicates the balances of the equity and economic items at 31 December 2018 relative to transactions arranged with the MEF and the companies within the MEF perimeter, that is companies directly and indirectly controlled by the MEF and its related companies.

Items/Balances	*Associates*	*Key management personnel*	*Other related parties*	*MEF Perimeter*	*Total*	*Proportion*
Total financial assets	**12,097**	**1,174**	**2,666**	**5,197,831**	**5,213,768**	**20.683%**
- Financial assets held for trading	171		2,665	4,547,272	**4,550,108**	48.662%
- Financial assets designated at fair value						
- Financial assets obligatorily measured at fair value						
- Financial assets at fair value through other comprehensive income				2,229	**2,229**	2.338%
- Receivables from banks						
- Receivables from customers	11,926	1,174		648,326	**661,426**	6.795%
- Other Assets			1	4	**5**	0.002%
Total financial liabilities			**141**	**36,784**	**36,925**	**0.151%**
- Financial liabilities measured at amortised cost				36,162	**36,162**	0.173%
- Financial liabilities held for trading			141	448	**589**	0.017%
- Financial liabilities designated at fair value					**0**	0.247%
- Other liabilities				174		
Guarantees issued and commitments				**80,211**	**80,211**	**0.858%**
Income statement						
- Interest and similar income	121	2	27	19,596	**19,746**	6.515%
- Interest and similar expense				(405)	**(405)**	0.242%
- Fee income			524	9,178	**9,702**	21.254%
- Fee expense						
- Net value adjustments for credit risk	168			(567)	**(399)**	(2.331%)
- Dividends and similar income				232	**232**	(20.489%)
- Operating costs and other expenses and income						

2.d Fees paid to the independent auditing firm and the bodies belonging to its network
(pursuant to art. 149 duodecies of CONSOB Resolution No. 15915 of 3 May 2007)

Type of services	*Party providing service*	*Fees*
Independent auditing	Ernst & Young S.p.A.	210
Certification services	Ernst & Young S.p.A.	18
Consultancy	Ernst & Young Financial-Business Advisors S.p.A.	-
Total		**228**

Note:
the amounts indicated above are net of VAT and ancillary expenses.

GROUP PARENT COMPANY OR EU PARENT BANK

The Bank belongs to the MPS Group and is controlled by Banca Monte dei Paschi di Siena S.p.A., which exercises management and coordination activities.
The basic data of the most recent financial statements (2017) approved by the parent company are provided below.

2.1 Corporate Name: **BANCA MONTE DEI PASCHI DI SIENA S.p.A.**

2.2 Headquarters: Piazza Salimbeni, 3 - Siena, Italy

Other details: Share capital € 15,692,799,350.97
Siena Companies Registry Registration Number, VAT Number and
Tax Code: 00884060526
Banking Register No. 325 Code No. 1030.6
Register of Banking Groups Code No. 1030.6
Enrolled in the Banking Register of the Bank of Italy no. 5274
Member of the Interbank Deposit Protection Fund and the National Guarantee Fund

FINANCIAL STATEMENTS OF THE PARENT COMPANY BANCA MONTE DEI PASCHI DI SIENA AS OF 31.12.2017

Balance sheet *(amounts in € millions)*

Assets		Liabilities and Shareholders' Equity	
Cash and cash equivalents	4,084	Due to banks	26,675
Financial assets held for trading	901	Due to customers	66,718
Financial assets available for sale	15,021	Outstanding securities	19,954
Loans to banks	24,927	Financial liabilities held for trading	802
Loans to customers	71,474	Financial liabilities measured at fair value	415
Hedging derivatives	333	Hedging derivatives	834
Value adjustment to financial assets subject to macro hedging	57		
Value adjustments to financial liabilities subject to macro-hedging	(1)		
Equity investments	3,079	Tax liabilities	1
Property, plant and equipment	1,035	Liabilities associated with non-current assets	0
Intangible assets	39	Other liabilities	3,242
Tax assets	3,072	Employee severance indemnities	192
Non-current assets	3,600	Provisions for risks and charges	1,018
Other assets	1,877	**Total liabilities**	**119,850**
		Shareholders' equity	9,649
Total Assets	**129,499**	**Total Liabilities and Shareholders' Equity**	**129,499**

Income statement	*(amounts in € millions)*
Interest and similar income	2,585
Interest expense and similar charges	(856)
Net interest income	**1,729**
Fee income	1,796
Fee expense	(262)
Net fee and commission income	**1,534**
Dividends and similar income	34
Net trading gains (losses)	14
Net hedging gains (losses)	(18)
Gains (losses) on disposal or repurchase of:	635
Net gains/(losses) on financial assets and liabilities measured at fair value	1
Operating income	**3,929**
Net value adjustments/write-backs due to impairment	(4,531)
Net income from financial management 14	**(602)**
Administrative expenses	(3,102)
Net provisions for risks and charges	(214)
Net value adjustments on property, plant and equipment	(69)
Net value adjustments on intangible assets	(26)
Other operating income/charges	303
Operating costs 20	**(3,108)**
Profit (loss) from equity investments	(103)
Goodwill value adjustments	-
Gains/(losses) on disposal of investments	522
Profit (Loss) from continuing operations before tax	**(3,291)**
Income taxes for the year on current operations	433
Profit (Loss) from current operations net of taxes	**(2,858)**
Gain (Loss) on discontinued operations, net of taxation	-
Profit (Loss) for the period	**(2,858)**

Part I
Share-based Payments

QUALITATIVE INFORMATION

The Bank's Shareholders' Meeting, on 21 December 2018, approved the *2018 Remuneration Report*, compliant in its contents with the analogous Report approved by the Shareholders' Meeting of Banca Monte dei Paschi di Siena on 12 April 2018 under the terms of Art. 123-ter of the Consolidated Finance Act.
The aforementioned report which fulfils the information requirements for listed companies as well as those established under sector regulations, is divided into three sections:
- the "first section", which summarises qualitative information regarding the remuneration policies the Group has adopted;
- the "second section", which describes the criteria used to determine fees to be agreed upon in the case of early termination of the employment relationship or departure from office;
- the "third section", which provides quantitative information about the payment structure for directors, statutory auditors and all key management personnel for CONSOB purposes, as well as "the most significant personnel" pursuant to the Supervisory Instructions.

In particular, the first section of the Report provides average data relative to the fixed payment component, by role and macro-department, at the Group level and for Banca MPS.

Structure of remuneration and incentive systems

In compliance with the requirements which the rules on remuneration and incentives establish for variable remuneration of the "most significant personnel", or:
- anchorage to performance measurement parameters with a view to the medium and long term;
- payment partly up-front and partly in financial instruments;
- disbursement in a minimum time period of three years;
- subjection of the deferred component to malus mechanisms;
- ratio between variable and fixed remuneration not exceeding 100% (1:1 ratio);
- for variable components of a particularly large amount, a deferral percentage of no less than 60% over no less than 5 years;
- presence of effective adjustment mechanisms for ex-post risks, which include qualitative indicators, linked to the conduct of the personnel during the employment relationship with the Bank;

disbursement of variable components in the cited perimeter occurs within the context of the maximum parameters approved by the Shareholders' Meeting - differentiated by clusters as a function of how they meet EB identification criteria (senior management, risk takers, quantitative criteria, etc.); they also include the malus mechanisms established by the Bank.
Malus and claw-back mechanisms indicated are formalised every time a variable component is activated (an incentive system is established or an employment relationship is terminated) and when new employees are hired.
The "most significant personnel" includes individuals from various organisational levels, some of which may accrue an incentive premium of a limited value, which when divided into shares or deferred would lead to insignificant units. In the light of this, for all clusters of the "most significant personnel", with the exception of I (the Managing Director, top management and other I employees reporting to the Managing Director), a bonus significance threshold has been established equal to € 40,000, below which all payments are made entirely in cash/up-front. This threshold - in line with the best market practices - which in any case are not applied if this amount is greater than 50% of the RAL received by the individual classified as "most significant personnel", is deemed appropriate to avoid the excessive assumption of risks by individuals, taking into account that the Bank has decided to adopt an overall prudential position relative to the applications allowed under the supervisory regulations, both with reference to identifying the

perimeter of the most significant personnel and in identifying the maximum theoretical variable thresholds.
For all other executives not included within the perimeter of the "most important personnel" and for all remaining personnel, the maximum percentage of the variable component relative to the fixed component is 50%. Nonetheless, the Bank reserves the right to derogate from this limit in the presence of business roles which, on the market, demonstrate an atypical variable remuneration structure (i.e. remuneration associated with commission revenue). In particular, with regards to the network of financial advisors, given the peculiarity of the remuneration system, which essentially consists of recurring commissions based on amounts managed/administered and non-recurring components deriving from development projects and multi-year loyalty programs similar to variable remuneration, the maximum ratio between variable/non-recurring remuneration and fixed/recurring remuneration is 100%, without prejudice to the deferral over three years of 50% of the amount and the payment of at least 50% in financial instruments and after the fact adjustment mechanisms.
On 12 April 2018, the Shareholders' Meeting of Banca Monte dei Paschi di Siena also approved the Performance Shares Plan, in favour of personnel of Banca Monte dei Paschi di Siena SpA and the subsidiaries which it controls, to be used when necessary to disburse any amounts agreed upon at the time of early termination of employment relationships.

Part L
Segment Reporting

The segment reporting is prepared by the Parent Company Banca Monte dei Paschi di Siena S.p.A. in part L of the Notes to the Financial Statements to its consolidated financial statements as of 31 December 2018.

ATTACHMENTS TO THE NOTES TO THE FINANCIAL STATEMENTS

PENSION FUND OF
MPS Capital Services
Banca per le Imprese S.p.A.

STATEMENT OF ACCOUNT
as of 31 DECEMBER 2018

Pension Fund of MPS Capital Services Banca per le Imprese S.p.A.

EXPLANATORY NOTE TO STATEMENT OF ACCOUNT AS OF 31 December 2018
(amounts in Euro)

The "MPS Capital Services Banca per le Imprese S.p.A. Pension Fund", enrolled in the Special Section of the Covip Register, under No. 9134 is the result of the historic and legal continuation of the supplementary pension scheme set up on 1 January 1974.
The "Fund" is made up of two separate segments with specific endowments aimed at guaranteeing the two benefit systems, in detail:

- the "defined benefit" segment of the "Fund" contains provisions, payable by the company, aimed at adapting the assets of the segment to the actuarial reserve estimated annually by an independent actuary;
- the section of the "defined contribution" Fund has its own separate and autonomous capital. The following are paid into the said section, which does not have a separate legal identity:
  - contributions payable by the Bank and the fund Members;
  - the portion of the employee severance indemnity allocated by the members enrolled to increase the endowment; the assets and liabilities referring to the operations of the segment are recorded in the related items of the Bank's balance sheet, despite maintaining separate asset autonomy with respect to the Bank;
  - the economic results deriving from the financial management of the assets, carried out by parties qualified to perform collective management of savings;

The assets, liabilities, costs, revenues and commitments referring to the segment's operations are not recorded in the Bank's financial statements.
The "Fund" is managed by the Bank's Board of Directors, which avails itself of advisory opinions and the support of a Supervisory Committee; the management of the positions of the members and any other activities, necessary or useful for the "Fund", are carried out by a Manager appointed by the Bank's Board of Directors.

A) "DEFINED BENEFIT" SEGMENT

The value of the Actuarial reserve as of 31.12.2018 was € 4,107,980= and it is recorded under liability item 120a in the Bank's balance sheet.
It is the value estimated so as to guarantee the periodic disbursement of the supplementary benefits of the legal pension to 37 members, all retired, of which 15 men and 11 women receiving a direct pension, along with 11 women receiving an indirect and survivor's pension.
The periodic benefits disbursed in 2018 amounted to € 514,783=.
During the year, it was necessary to increase the fund by € 20,437= to adjust it to the value of the mathematical reserve as calculated by the actuary.
No other members may join the Segment, by effect of the changes made to the Fund Regulations as a result of the collective agreements, but also on the basis of current law provisions.

B) "DEFINED CONTRIBUTION" SEGMENT

Total net assets as of 31 December 2018 amounted to € 45,637,067=.
During 2018, the Bank paid over the contributions payable by the Company to the "Fund", along with those payable by the members to their chosen extent; the portions of employee severance indemnity were also paid over to the extents indicated by said employees in accordance with the Regulations and in compliance with the law.
From the segment there were capital outflows for "transfers and redemptions" of € 3,515,181 in disbursements in the

form of capital of € 280,320.
The disbursements by way of advances on the total position accrued, concerned requests for a total of € 1,194,270= in 2018.
A total of 548 persons are enrolled in the segment of the "Fund" as of 31 December 2018, of which **510** are active, **20** enrolled only in the so-called "Guaranteed" line and **38** are no longer active.

B.1) FINANCIAL MANAGEMENT INFORMATION

The resources of the "Fund" have been spread over seven different investment lines, of which one aimed at receiving the severance indemnity conferred tacitly, in accordance with Article 8, section 9 of Italian Legislative Decree No. 252/2005 (hereinafter, for the sake of brevity, "Guaranteed Line").
The afore-mentioned investment lines correspond to as many asset management schemes open with the Parent Company and managed by the Asset Management Service, with the exception of the so-called Guaranteed Line managed through an AXA-MPS insurance product. The contributions to said investment lines were made on the basis of the individual choice expressed by each member.
The features of the investment lines are as follows:

Description	*Line C001* GPM 386133	*Line C002* GPM 386134	*Line C003* GPM 386135	*Line C004* GPM 386164	*Line C005* GPM 386072	*Line C006* GPM 386163	*Guaranteed line*
Time Horizon(years)	*7-10*	*10-20*	*20-30*	*5*	*5*		*Collective policy*
- Risk free (monetary)				60%	42%	100%	
- Bond component	73%	52%	35%	33%	44%		
- Equity component	27%	48%	65%	7%	14%		

2018 annual return and average returns during the period from asset management

	GPM 386133 *Line C001*	GPM 386134 *Line C002*	GPM 386135 *Line C003*	GPM 386164 *Line C004*	GPM 386072 *Line C005*	GPM 386163 *Line C006*	*Guaranteed line*
2018 Return	**-2.09%**	**-3.62%**	**-4.79%**	**-0.88%**	**-1.39%**	**-1.03%**	**3.70%**
Annual average return for five-year period **2014/2018**	**3.67%**	**4.18%**	**4.59%**	**1.58%**	**1.94%**	**0.03%**	**2.80%**
Annual average return for three-year period **2016/2018**	**0.99%**	**1.17%**	**1.44%**	**0.40%**	**0.55%**	**-0.25%**	**2.87%**

N.B. The figures express only the performance of the asset management portfolios underlying the single segments

The values of the individual portions of the different lines during the five years 2014-2018 are as follows:

date	*Line C001*	*Line C002*	*Line C003*	*Line C004*	*Line C005*	*Line C006*	*Guaranteed line*
31/12/2014	**1.537**	**1.688**	**1.829**	**1.213**	**1.307**	**1.067**	*(1)*
31/12/2015	**1.592**	**1.776**	**1.944**	**1.231**	**1.323**	**1.070**	*(1)*
31/12/2016	**1.636**	**1.827**	**2.010**	**1.247**	**1.346**	**1.070**	*(1)*
31/12/2017	**1.675**	**1.908**	**2.131**	**1.257**	**1.364**	**1.073**	*(1)*
31/12/2018	**1.640**	**1.839**	**2.029**	**1.246**	**1.345**	**1.062**	*(1)*

(1) the insurance policy provides for the management of individual positions

With regard to the management policies of the GPM of the Pension Fund of MPS Capital Services Banca per le Imprese S.p.A., the details for financial year 2018 are as follows.
The monetary component of the portfolios was characterised by a positioning of substantial neutrality in terms of financial duration with respect to the benchmark index and by the investment in very short-term Italian corporate issues with high creditworthiness, mainly at floating rates. The investment in securities issued by the Republic of Italy at a fixed and floating rate with average maturities of about six months accounts for most of the monetary portfolio. The risk-off phase that affected domestic debt, which began in May, strongly penalised the performance of the monetary component.
The bond component of the portfolios was characterised by a positioning of under-weighting with respect to the benchmark index of reference in terms of average financial duration in the first half of the year before coming closer to the value of the benchmark index of reference in the second half of the year. The portfolio continued to maintain diversification in terms of exposures to core and peripheral countries, limiting the core component to solely German government securities, concentrated on the medium-long part of the curve, and differentiating between Italian and Spanish bonds for the periphery. This positioning made it possible to achieve a positive result for the bond component.
The stock component was characterised by investment in ETFs, selected by geographic area, which allowed for a greater degree of diversification. The allocation was kept substantially neutral during the year. The contribution of the equity component was decidedly negative in absolute terms following the traumatic risk-off phase of the markets, with particular magnitude in the last quarter, caused mainly by fears of a sharp slowdown in global growth.

B.2) INFORMATION ON THE FINANCIAL STATEMENTS

The segment's financial statements are represented by a statement of account comprising a balance sheet and income statement, supplemented by the information contained in these explanatory notes. The income statement not only registers the profit or loss, but also the changes which derive from the gathering of the contributions and from the conversion of the individual positions into benefits under the form of capital or a life annuity.
The financial statements are drawn up by showing preference for the representation of substance over form; they are expressed in Euro.

B.2.1 Measurement of the investments and description of the portfolio

The securities have been valued at market value in observance of the accounting approach for financial instruments established by CONSOB.
As of 31 December 2018, there were no derivative contract transactions present in the portfolio.

B.2.2 Criteria for estimating the expenses and income

The charges and income have been recorded on an accrual basis, irrespective of the date of collection or payment.
Interest on benefits and redemptions is calculated at the performance index known as of the date of leaving the Fund, net of taxation.
The tax regime of the defined contribution segment of the pension fund is disciplined by Article 17 of Italian Legislative Decree No. 252/2005 and subsequent amendments and additions.

The Fund Manager

PENSION FUND OF MPS CAPITAL SERVICES BANCA PER LE IMPRESE S.P.A.

BENEFITS OF THE "DEFINED CONTRIBUTION" SEGMENT
STATEMENT OF ACCOUNT AS OF 31 December 2017

BALANCE SHEET

(amounts in Euro)

ACCUMULATION PHASE ASSETS	*31/12/2018*	*31/12/2017*
10 Direct investments	**-**	**-**
20 Assets under management	**45,445,575**	**48,333,823**
20-a) Bank deposits	387,347	(167,705)
20-b) Receivables for repurchase agreements	-	-
20-c) Securities issued by Governments or by international bodies	25,264,828	25,067,467
20-d) Listed debt securities	775,149	715,339
20-e) Listed equity securities	-	-
20-f) Unlisted debt securities	-	-
20-g) Unlisted equity securities	-	-
20-h) UCITS Units in collective investment undertakings	18,337,872	21,573,119
20-i) Options purchased	-	-
20-l) Accrued income and prepaid expenses	380,032	316,730
20-m) Result guarantees released to pension fund	-	-
20-n) Other assets of financial operations	-	561,421
20-o) Investments in insurance operations	300,347	267,452
20-p) Margins and receivables on forward/future transactions	-	-
30 Result guarantees acquired on individual positions	**-**	**-**
40 Assets of administrative operations	**286,625**	**328,607**
40-a) Cash and bank deposits	286,311	328,325
40-b) Intangible fixed assets	-	-
40-c) Property, plant and equipment	-	-
40-d) Other assets of administrative operations	314	282
50 Tax credits	**405,492**	**280**
TOTAL ACCUMULATION PHASE ASSETS	**46,137,692**	**48,662,710**

(amounts in Euro)

ACCUMULATION PHASE LIABILITIES	*31/12/2018*	*31/12/2017*
10 Liabilities of welfare operations	**490,563**	**596,312**
10-a) Payables of welfare operations	490,563	596,312
20 Liabilities of financial operations	**8,215**	**15,828**
20-a) Payables for repurchase agreements	**-**	**-**
20-b) Options issued	-	-
20-c) Accrued expenses and deferred income	-	-
20-d) Other liabilities of financial operations	8,215	15,828
20-e) Payables on forward/future transactions	-	-
30 Result guarantees recognised on individual positions	-	-
40 Liabilities of administrative operations	**(1,140)**	**3,485**
40-a) Employee severance indemnity	-	-
40-b) Other liabilities of administrative operations	(1,283)	3,334
40-c) Deferral of contributions for coverage of administrative charges	143	151
50 Tax payables	**2,987**	**439,887**
TOTAL ACCUMULATION PHASE LIABILITIES	**500,625**	**1,055,512**
100 Net assets destined for benefits	**45,637,067**	**47,607,198**

The item “Tax liabilities” represents the substitute tax applied to the results of financial operations.

INCOME STATEMENT

(amounts in Euro)

		31/12/2018	31/12/2017
10	**Balance of welfare operations**	**(436,462)**	**466,055**
	10-a) Contributions for benefits	4,634,098	4,333,758
	10-b) Advances	(1,194,270)	(1,108,870)
	10-c) Transfers and redemptions	(3,515,181)	(2,540,585)
	10-d) Transformations into annuities	-	-
	10-e) Disbursements under the form of principal	(280,320)	(149,269)
	10-f) Premiums for ancillary benefits	(80,789)	(68,979)
	10-g) Periodic benefits	-	-
	10-h) Other welfare outgoings	-	-
	10-i) Other welfare incomings	-	-
20	**Result of financial operations**	-	-
30	**Result of indirect financial operations**	**(1,903,724)**	**2,298,093**
	30-a) Dividends and interest	722,257	732,668
	30-b) Profits and losses from financial transactions	(2,625,981)	1,565,425
	30-c) Fees and commission on securities lending	-	-
	30-d) Income and charges for repurchase agreements	-	-
	30-e) Spread on result guarantees issued to the pension fund	-	-
40	**Operating charges**	**(34,119)**	**(33,885)**
	40-a) Management company	(34,119)	(33,885)
	40-b) Custodian bank	-	-
50	**Margin of financial operations (20)+(30)+(40)**	**(1,937,843)**	**2,264,208**
60	**Balance of administrative operations**	-	-
	60-a) Contributions to cover administrative expenses	151	151
	60-g) Sundry expenses and income	(8)	-
	60-i) Deferral of contributions to cover administrative expenses	(143)	(151)
		-	-
70	**Change in net assets destined for benefits pre-substitute tax (10)+(50)+(60)**	**(2,374,305)**	**2,730,263**
		-	-
80	**Substitute tax**	**404,174**	**(438,882)**
		-	-
	Change in net assets destined for benefits (70)+(80)	**(1,970,131)**	**2,291,381**

STATEMENT OF ACCOUNT AT 31 December 2018
BREAKDOWN BY INVESTMENT LINE

(amounts in Euro)

BALANCE SHEET

ACCUMULATION PHASE ASSETS	C001	C002	C003	C004	C005	C006	C007
10 Direct investments	**-**	**-**	**-**	**-**	**-**	**-**	**-**
20 Assets under management	**8,961,294**	**14,392,858**	**14,166,257**	**2,614,642**	**3,626,401**	**1,383,776**	**300,347**
20-a) Bank deposits	37,280	88,554	115,266	49,583	8,924	87,740	-
20-b) Receivables for repurchase agreements	-	-	-	-	-	-	-
20-c) Securities issued by Governments or by international bodies	6,535,853	7,594,026	5,155,314	2,105,780	2,832,202	1,041,653	-
20-d) Listed debt securities	-	-	-	266,020	261,026	248,103	-
20-e) Listed equity securities	-	-	-	-	-	-	-
20-f) Unlisted debt securities	-	-	-	-	-	-	-
20-g) Unlisted equity securities	-	-	-	-	-	-	-
20-h) UCITS Units in collective investment undertakings	2,282,473	6,587,079	8,811,733	168,827	487,760	-	-
20-i) Options purchased	-	-	-	-	-	-	-
20-l) Accrued income and prepaid expenses	105,688	123,199	83,944	24,432	36,489	6,280	-
20-m) Result guarantees released to pension fund	-	-	-	-	-	-	-
20-n) Other assets of financial operations	-	-	-	-	-	-	-
20-o) Investments in insurance operations	-	-	-	-	-	-	300,347
20-p) Margins and receivables on forward/future transactions	-	-	-	-	-	-	-
30 Result guarantees acquired on individual positions	**-**	**-**	**-**	**-**	**-**	**-**	**-**
40 Assets of administrative operations	**52,490**	**74,821**	**105,394**	**17,879**	**26,808**	**10,516**	**(1,283)**
40-a) Cash and bank deposits	52,435	74,733	105,394	17,865	26,676	10,509	(1,301)
40-b) Intangible fixed assets	-	-	-	-	-	-	-
40-c) Property, plant and equipment	-	-	-	-	-	-	-
40-d) Other assets of administrative operations	55	88	-	14	132	7	18
50 Tax credits	**51,522**	**143,879**	**186,526**	**6,865**	**13,179**	**3,521**	**-**
TOTAL ACCUMULATION PHASE ASSETS	**9,065,306**	**14,611,558**	**14,458,177**	**2,639,386**	**3,666,388**	**1,397,813**	**299,064**

ACCUMULATION PHASE LIABILITIES								
		C001	**C002**	**C003**	**C004**	**C005**	**C006**	**C007**
10	**Liabilities of welfare operations**	**2,803**	**108,639**	**237,803**	**3,169**	**138,149**	**-**	**-**
	10-a) Payables of welfare operations	2,803	108,639	237,803	3,169	138,149	-	-
20	**Liabilities of financial operations**	**1,438**	**2,721**	**3,009**	**350**	**524**	**173**	**-**
	20-a) Payables for repurchase agreements	-	-	-	-	-	-	-
	20-b) Options issued	-	-	-	-	-	-	-
	20-c) Accrued expenses and deferred income	-	-	-	-	-	-	-
	20-d) Other liabilities of financial operations	1,438	2,721	3,009	350	524	173	-
	20-e) Payables on forward/future transactions	-	-	-	-	-	-	-
30	**Result guarantees recognised on individual positions**	-	-	-	-	-	-	-
40	**Liabilities of administrative operations**	**-**	**-**	**143**	**-**	**-**	**-**	**(1,283)**
	40-a) Employee severance indemnity	-	-	-	-	-	-	-
	40-b) Other liabilities of administrative operations	-	-	-	-	-	-	(1,283)
	40-c) Deferral of contributions for coverage of administrative charges	-	-	143	-	-	-	-
50	**Tax payables**	-	-	-	-	-	-	**2,987**
	TOTAL ACCUMULATION PHASE LIABILITIES	**4,241**	**111,360**	**240,955**	**3,519**	**138,673**	**173**	**1,704**
100	**Net assets destined for benefits**	**9,061,065**	**14,500,198**	**14,217,222**	**2,635,867**	**3,527,715**	**1,397,640**	**297,360**

INCOME STATEMENT	C001	C002	C003	C004	C005	C006	C007
10 Balance of welfare operations	**(27,283)**	**(525,141)**	**(725,068)**	**250,173**	**454,042**	**109,155**	**27,660**
10-a) Contributions for benefits	750,492	1,114,673	989,918	594,447	833,183	310,828	40,557
10-b) Advances	(210,789)	(400,943)	(336,450)	(96,364)	(117,250)	(32,474)	-
10-c) Transfers and redemptions	(552,500)	(1,130,033)	(1,275,652)	(137,105)	(241,365)	(165,629)	(12,897)
10-d) Transformations into annuities	-	-	-	-	-	-	-
10-e) Disbursements under the form of principal	-	(83,681)	(76,348)	(104,882)	(15,409)	-	-
10-f) Premiums for ancillary benefits	(14,486)	(25,157)	(26,536)	(5,923)	(5,117)	(3,570)	-
10-g) Periodic benefits	-	-	-	-	-	-	-
10-h) Other welfare outgoings	-	-	-	-	-	-	-
10-i) Other welfare incomings	-	-	-	-	-	-	-
20 Result of financial operations							
30 Result of indirect financial operations	**(235,462)**	**(677,335)**	**(887,677)**	**(30,717)**	**(62,987)**	**(18,115)**	**8,569**
30-a) Dividends and interest	189,269	236,313	179,601	43,682	63,716	9,676	-
30-b) Profits and losses from financial transactions	(424,731)	(913,648)	(1,067,278)	(74,399)	(126,703)	(27,791)	8,569
30-c) Fees and commission on securities lending	-	-	-	-	-	-	-
30-d) Income and charges for repurchase agreements	-	-	-	-	-	-	-
30-e) Spread on result guarantees issued to the pension fund	-	-	-	-	-	-	-
40 Operating charges	**(5,841)**	**(11,163)**	**(12,402)**	**(1,407)**	**(2,051)**	**(1,255)**	**-**
40-a) Management company	(5,841)	(11,163)	(12,402)	(1,407)	(2,051)	(1,255)	-
40-b) Custodian bank	-	-	-	-	-	-	-
50 Margin of financial operations (20)+(30)+(40)	**(241,303)**	**(688,498)**	**(900,079)**	**(32,124)**	**(65,038)**	**(19,370)**	**8,569**
60 Balance of administrative operations	**-**	**-**	**-**	**-**	**-**	**-**	**-**
60-a) Contributions to cover administrative expenses			151				
60-g) Sundry expenses and income			(8)				-
60-i) Deferral of contributions to cover administrative expenses	-	-	(143)	-	-	-	-
70 Change in net assets destined for benefits pre-substitute tax (10)+(50)+(60)	**(268,586)**	**(1,213,639)**	**(1,625,147)**	**218,049**	**389,004**	**89,785**	**36,229**
80 Substitute tax	**51,522**	**143,879**	**186,526**	**6,865**	**13,179**	**3,521**	**(1,318)**
Change in net assets destined for benefits (70)+(80)	**(217,064)**	**(1,069,760)**	**(1,438,621)**	**224,914**	**402,183**	**93,306**	**34,911**

CERTIFICATION REPORT

Certification Report

The Certification Report issued on 14th March 2019 by Reconta Ernst & Young Spa may be read in the original version of the 2018 Annual Report, written in Italian.

The Certification Report relates only to that version of the Annual Report.

REPORT OF THE BOARD OF STATUTORY AUDITORS

Board of Auditors' Report to the Shareholders' meeting called for the approval of the Financial Statements for the year ending 31/12/2018

(under the terms of Art. 153 of Italian Legislative Decree 58/1998 and Art. 2429 of the Italian Civil Code)

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To the Shareholders' Meeting of the company MPS Capital Services Banca per le Imprese S.p.A.

Dear Shareholders,
During the financial year ending at 31 December 2018, the undersigned Board of Auditors, appointed at the shareholders' meeting of 8 April 2016 (for two of the members in office) and of 20 June 2016 (for the third member in office), carried out supervisory activities in accordance with the provisions of the Italian Civil Code, Italian Legislative Decrees 385/1993 (Consolidated Law on Banking - CLB), 58/1998 (Consolidated Law on Finance - CLF) and 39/2010 (Consolidated Law on Auditing - CLA), the articles of association, those issued by the Independent Administrative Authorities that carry out supervisory and auditing activities, as well as the principles of conduct for Boards of Auditors recommended by the Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili (Italian National Council of Accountants and Accounting Experts).
The Board of Auditors has received the draft financial statements approved by the Board of Directors under the terms of the law. Also on the basis of the indications provided by CONSOB with Communication no. DEM/1025564 of 6 April 2001, as supplemented by the subsequent Communications DEM/3021582 of 4 April 2003 and DEM/6031329 of 7 April 2006, of the "Rules of conduct for boards of statutory auditors of listed companies" published on 15 April 2015 by the Italian National Council of Accountants and Accounting Experts, and of the principles contained in the Code of Conduct, the Board of Statutory Auditors reports as follows.

1 - FOREWORD

1.1 Reference Banking Group

As you know, the Bank is subject to management and coordination activities by the Parent Company, Banca Monte dei Paschi di Siena SpA. Relations with the Parent Company, aimed at optimising synergies and the productivity of the Company within the Group context, include operations carried out for the Parent Company on the financial markets, the agreement related to the option to adhere to National Tax Consolidation for financial years 2016, 2017 and 2018, and the outsourcing of a series of activities and services which are noted later in this report.

1.2 Summary of the operating result at 31 December 2018

The 2018 financial statements show a net profit of € 80.7 million, compared to the loss of € 632.9 recognised the previous year. The positive result was determined by a gross profit before tax of € 37.1 million, to which must be added the positive contribution of item 270 "Income taxes for the year on continuing operations" of € 43.6 million. The figure related to taxes reflects mainly the following trends:

- the recognition, under the terms of paragraphs 1067 and 1068 of the Stability Law for 2019, of IRES and IRAP DTAs on 9/10 of the higher write-downs on loans recognised on FTA of IFRS9, the deductibility of which was deferred to the next 9 years. This component, net of the reversal of the IRAP credit of € 5.8 million recognised on FTA of IFRS9 against the aforesaid higher write-downs on loans, contributed positively to item 270 for € 39.2 million;
- effects consequent to the probability test on non-transformable DTAs due to temporary differences, written down by € 145 thousand; on DTAs recognised against the IRES surcharge at 3.5% on earlier tax losses, written down by € 9.1 million, and on the IRES credit from the consolidator recognised against the conferment to the Parent Company of the said earlier losses, revalued by € 14.4 million.

The complete picture of the items affecting the determination of accounting item 270 is shown in the table on the next page.

(amounts in euro mln)

Detail of item 270 "Income taxes for the year on continuing operations"	
Effects of the Stability Law for 2019	**39.2**
of which: DTA 9/10 adjustments FTA IFRS9	*45.0*
reversal of IRAP credit recognised on FTA IFRS9	*-5.8*
Effects of probability test	**5.2**
of which: *write-down of non transf. DTAs on temp. differences*	*-0.1*
write-down of DTAs tax loss 3.5% IRES surcharge	*-9.1*
revaluation of credit from consolidator IRES 24%	*14.4*
Other components	**-0.8**
Total	**43.6**

2 - ACTIVITY OF THE BOARD OF STATUTORY AUDITORS

The Board of Statutory Auditors met 17 times during financial year 2018; it participated in the Shareholders' Meetings held on 11 April and 21 December 2018 and in 19 meetings of the Board of Directors. It must be acknowledged that during the board meetings the legal information was provided by the Administrative Bodies, including exhaustive information on the activity carried out and the transactions of greatest economic and financial significance performed by the Bank.

During 2018, the Board of Statutory Auditors in office held a meeting with Mr Alessandro Papaniaros, at that time Manager of the Compliance Area of BMPS and Manager of the Compliance Unit of MPSCS, for a discussion on the trends in the activity of the MPSCS Compliance Unit after its outsourcing to BMPS starting from 4/12/2017, two meetings with the AML Office Manager and Risk Officer Mr Gianluca Tortora, and two meetings with the representatives of the Auditing Firm EY SpA, appointed for the independent auditing of the financial statements of MPS Capital Services SpA.

On 6 June 2018, the Board of Statutory Auditors, in the person of the Chairperson, took part, on invitation, in a meeting of the Oversight Committee, from which it also received information periodically during the year.

In the context of the legal provisions, the Board of Statutory Auditors of the Parent Company met the Board of Statutory Auditors in office on 23/07/2018.

In addition, again with the support of the Internal Audit structure, the Board of Statutory Auditors in office carried out a visit to the Naples Area Office, which is under the Corporate Finance Department, during which we examined the procedures for origination and management of loan disbursement and structured finance operations.

On the basis of the activities and checks performed by the Board, we can state that the operations resolved and carried out by the Company were compliant with the law and with the Articles of Association. The Board of Auditors supervised observance of the laws and the Articles of Association.

3 - SUPERVISION OF THE ORGANISATIONAL STRUCTURE, ADEQUACY OF THE INTERNAL CONTROL AND RISK MANAGEMENT SYSTEM

3.1 Monitoring of the control units

The Board of Auditors supervised the operation of the Bank's organisational structure and the adequacy of the overall system of internal controls, ascertaining the efficacy of the structures and units involved, as well as the adequacy of the risk control and management system.

This supervisory activity was carried out through collectively performed audits, obtaining information from the

managers of the corporate units, examining the documents, analysing the results of the work done by the Auditing Firm on the various accounting items which occurred through the meetings that were held during the year. In addition, monitoring was carried out on the activities of the second and third level control units, which are reported on in more detail in the paragraph devoted to this subject.
The Board of Auditors interacted constantly with the Internal Audit Unit, both to receive the necessary assistance to carry out the aforementioned checks and as the recipient of all the inspection reports containing the results of the assessments which the said Unit made during the year.
The Board discussed with the managers of the operating units in order to examine the significant problems, in terms of control and risk of the main operating processes.

3.2 Internal Audit

The Board monitored the activity of the Internal Audit unit, examining the Activity Plan prepared for the year 2018, the reports on the work done during the year and verifying over time the qualitative and quantitative adequacy of the unit and the position of Independence it is considered to have within the context of the Company’s organisational structure.
Particular attention was paid to the Annual Report for the year 2018 on the internal control system, submitted for examination by the Company’s Board of Directors on 27 February 2019.
This report adequately illustrates the programme of activities carried out, the areas examined, the related results and the follow-up activities envisaged for the aspects of improvement. The summary opinion expressed by the Internal Audit unit on the Bank’s control system is “Rating 1 - Green”. As regards this Report, the Board of Statutory Auditors expressed its appreciation for the activity performed, after stressing that the main themes presented in the Report were the subject, during the year, of periodic meetings with the manager of the unit who illustrated the activities performed and the actions taken to resolve the shortcomings highlighted by the auditing activity.

3.3 Compliance

The Board examined, as usual, the activity plan for 2018 prepared by the unit and the reporting pursuant to the annual Compliance Report.
In 2017, the Bank's Organisational Model for the Compliance Unit was modified. In fact, in line with the recommendations received from the European Central Bank, the MPS Group implemented a specific plan to strengthen the Compliance Unit, which involved, among other things:
- centralising the Compliance Units of the Italian subsidiaries within the parent company, which also involved MPS Capital Services S.p.A.. To this end, in December 2017, the Bank's Board of Directors approved the *“Agreement to outsource the Compliance Unit to the Parent Company”*;
- the elimination of the “Common Compliance Model” through centralising operating activities within the Compliance Unit which had previously been entrusted to Specialist Compliance Offices, with the exclusion of those related to “Workplace Health and Safety and Environmental Protection” and “Tax Compliance”.

The work done by the Compliance Unit in 2018 had the main goal of completing the actions described in the 2018 Compliance Plan and implementing the main legislative changes within company regulations and processes.

Special attention was paid to monitoring activities and safeguards established in relation to:
- *ICT Compliance* (Bank of Italy Circular no. 285) and international combating of tax evasion (FATCA/CRS);
- Banking transparency, with the updating of the new release of internal regulatory documents on “Provisions for the Transparency of Banking Transactions and Services” which implemented the developments associated with Italian Legislative Decree 72/2016;

- Fighting usury, by adjusting control procedures to the progressive updates made to the Bank of Italy Supervisory Instructions;
- Protection of personal information (Privacy) with participation in periodic SAL meetings on the "*Project to adjust to "Regulation EU 2016/679 (GDPR)*" and the actions associated with the same;
- Investment services, including defining and carrying out actions necessary to comply with the PRIIPS Regulation, MiFID II Directive and MiFIR Regulation by January 2018.

During the period in question, the Bank received 13 complaints regarding banking services, of which 7 involved complaints of presumed usury related to the rates applied by the Bank. Of these latter, at this time none has been accepted (1 still being processed) and the complaints have been identified as unfounded, as they were the consequence of erroneous calculation of interest on arrears by the customers or their consultants. Four complaints, also not accepted, concern the validity of the sureties (non-adjustment of the maximum amount guaranteed to the ISTAT indices).
The 2018 figures showed a 62.85% decrease in complaints received compared to the previous year (35).
Together with the annual Compliance report, which was illustrated by the manager of the unit to the Board of Directors at the meeting on 27 February 2019, the Compliance unit presented the activity plan for the year 2019, which was examined and assessed positively by this Board of Statutory Auditors.

3.4 Risk Management
The Montepaschi Group has adopted a centralised Risk Management model for the Italian Subsidiary MPS Capital Services, the Risk Control Unit of which is assigned to the corresponding Parent Company Corporate Unit under the Chief Risk Officer Department ("CRO" Department).
In keeping with the rules of the Supervisory Authorities and the powers attributed to the Board of Directors and with the consent of the Board of Statutory Auditors, the pro tempore Manager of the Parent Company's CRO Department is also the Risk Manager of MPS Capital Services.
The risk management services are provided with methods and in ways in line with the prescriptions of the Supervisory Authorities and on the basis of the principles and guidelines established in the Group Policy on the Internal Control System and in the Outsourcing Policy.
The Board of Statutory Auditors received, during the year, the periodic reports containing a cohesive presentation of the risks and of the stage of progress of the projects planned for 2018 (Reporting on the activities).
MPS Capital Services ended 2018 with capital indicators slightly down compared to 31-12-2017 but with a significant strengthening trend in the last quarter following derisking actions carried out.
The MPS Capital Services 2018 Risk Plan included mainly activities to maintain/develop the risk measurement systems, projects to mitigate internal and external inspection gaps, and updates to control activities and methodologies to ensure compliance with national and international supervisory regulations.
The activities not completed relate to making the "Counterparty Risk Limits Framework" more efficient, 70% completed, and the Pelican Project, placed in stand-by by the Parent Company.

3.5 AML and Risk Officer
In 2018, following the centralisation of the Compliance Unit within the Parent Company and outsourcing contract at the same time, the Anti-Money Laundering (AML) Unit was transferred to the newly established AML Office and Risk Officer.
The activity performed by the Anti-Money Laundering Unit in 2018 had as its main driver the performance of actions identified after the risk self-assessment carried out in 2018 as well as those described in the 2017 Plan and

incorporated into the 2018 Plan if they had not been completed. In particular, as provided for in the 2018 Plan, the work planned regarded the following areas:

- Adequate verification
- Organisation and Controls
- Reporting of suspicious transactions
- Personnel training

As regards the first point, during 2018, initiatives continued to recover information for adequate verification of customers still without a KYC questionnaire, in continuity with what was already provided for in 2017. The activities carried out in this area of interest made it possible to achieve a coverage rate of 94.49% at the end of the 4th quarter of 2018. Refinements to the extractions of active customers are, however, still in progress and will determine the perimeter within which to calculate the coverage rate for 2019. In addition, the files with stronger verification showed an increase, owing to the revaluations of numerous customers with high risk profiles, attributable to the wider perimeter of customers classified as PEPs.
On the subject of organisation and controls, it is worth noting the introduction and commissioning of 4 new control records in the last quarter of 2018.
The training plan on the subject of Anti Money Laundering (AML) and Combating the Financing of Terrorism (CFT), which involves 199 resources, advanced considerably during 2018. Training provided up to 31 December 2018 involved 81% of the total planned.
The Anti Money Laundering Unit performed a specific Risk Self-Assessment (AML and Terrorism Financing Risk Self-Assessment) with updated methodology, incorporating the indications received from the Parent Company AML-CFT Unit.

On the basis of this activity:

- The related risk was found to be “medium-low”;
- Vulnerability of the oversight was found to be “Insignificant”, on average. This suggests that the Bank has adopted deterrence and control measures that are reasonably effective at discouraging money laundering and financing of terrorism;
- The combination of risk judgements and the vulnerability of the safeguards led to a “Low” residual risk on the basis of the matrix suggested by the Supervisory Authorities.

As previously noted, the controls structured during 2018 made it possible to intercept phenomena on which mitigation actions were planned.
Lastly, during 2018 the Anti Money Laundering Unit periodically reported on its activities to the Board of Directors, providing exhaustive information. It also remained in constant contact with this Board of Statutory Auditors.

3.6 Outsourcing of functions and activities
The Board of Statutory Auditors notes that the Company has outsourced a series of services and activities to the Parent Company or to third parties through it. During 2018, for the subject in question, there were no regulatory changes at the level of Supervision, while there was a complete revision of the Group’s internal regulations.
The Parent Bank revised the Policy, Directives and Documents for defining principles and responsibilities on the subject of regulating the outsourcing process and, consequently - also with specific measures from the Board of Directors, when expressly provided for - all the related updates were incorporated into the company’s regulations.
The Organisation unit, which has been given the task of overseeing the adequate performance of the outsourced activities, illustrated to the Board of Directors, at its meeting on 6 February 2019, the management of the service

agreements, both intra-group and extra-group, and the activity of monitoring the structured oversight procedures carried out during financial year 2018.
We can note that, during the past year, under the guidance of the Parent Company, all the intra-group contracts were renewed (with the exception of that related to the Compliance Unit, because it was signed at the end of 2017) for the updating of the outsourced services and to add a series of clauses specifically required by the Supervisory Authorities.
At the end of 2018, the situation of the outsourced functions and activities, within the Banking Group or to third parties, is the following:

INTRA-GROUP
- *Compliance Unit;* provider: Banca MPS
- *Property Management:* outsourcing of the provision of services related to the real estate segment; provider: Banca MPS
- *Credit recovery*: management of problem loans related to bad positions; provider: Banca MPS
- *Risk Management and Internal Validation*: provider: Banca MPS
- *Workplace health and safety and Environmental management:* provider: Banca MPS
- *Various services:* Market support, Back Office-Data and Surveys, Regulatory Reporting, Financial Statements: governance and consolidated supervision, Communication, Treasury Purchases and Logistics, Equity investments management, Personnel, Legal and Corporate Management, Specialist Credit Services: ratings decisions; provider: Banca MPS
- *ICT-Information System:* provider: Montepaschi Group Operational Consortium

The oversight of outsourced activities is based on monitoring the performance, every quarter, to check the quality of the services received.
In this context, during 2018, the Parent Company defined new reports to facilitate the summary of the controls performed. On this subject, as usual, the corporate units benefiting from the services provided by the Parent Company were periodically consulted to ascertain the level of satisfaction and highlight any anomalies or critical issues. On this point, during the year, substantial observance of the established levels of service was confirmed.
In relation to the ICT services provided by the Consortium, at the same time as the quarterly meeting to present the data related to the annual progression of the amount of the fee, the performance indicators are examined. Contact is therefore maintained with the consortium units responsible for developing the methodologies for the monitoring/measurement of the quality of the services, with particular attention to assessing the availability of the infrastructures in supporting applications considered “critical” for MPSCS.

OUT-OF-GROUP
- *Back Office - auxiliary services;* provider: Fruendo Srl (*)
- *Back Office - Administration and loan accounting;* provider Accenture SpA (*)
- *Deal Done Trading*; provider: List SpA
- *Bad loan recovery;* provider: Juliet (*)

(*) contracts defined in the context of Group agreements

As is known, the Parent Company has also signed framework agreements on behalf of the subsidiaries in relation to Back Office activities for auxiliary, administration and loan accounting services (with Fruendo S.r.l. and Accenture S.p.A., see above), taking over itself, in addition, management of the formalisation of the contractual relationships and monitoring of the performance.
The recent organisational restructuring carried out by the Parent Company regarded, among other things, a complete

revision of the Credit Recovery Area which, in the past, had been responsible for direct management of recovery of all the Montepaschi Group's bad positions -— and the activation of the credit recovery platform at the company JULIET SPA. This work involved the transfer of the Banca Monte dei Paschi di Siena's bad credit recovery platform and the signing of a servicing contract for management in outsourcing of at least 80% of the bad flows of the Italian banks of the Montepaschi Group.
The monitoring of the out-of-group Outsourced Activities also regarded the service of Application Service Providing for the Deal Done Trading (DDT) Systematic Insourcing System, with regard to the correct operation of the market and prices, the verification of the KPIs defined, the production of reports, among other things.

3.7 Organisation and Control Model pursuant to Italian Legislative Decree 231/01

Some time ago, the Company adopted the Organisation, Management and Control model, pursuant to Italian Legislative Decree 231/2001, prepared according to the ABI guidelines and in accordance with the instructions provided by the Parent Company.
During 2018, the Oversight Committee, pursuant to Italian Legislative Decree 231/2001, saw the entry of a new member, Ms Anna Girello, replacing Mr Salvatore Messina, who resigned.
The 231 Oversight Committee regularly reported, every six months, to the Board of Directors on the activity carried out by the same.
During 2018, the 231 Oversight Committee continued to oversee the operation and observance of MPSCS's 231 Model through various activities.
The provisions of Art. 8.10 of the 231 Oversight Committee Regulations, regarding the transmission to the Board of Auditors of approved Committee meeting minutes, were observed.
From the information acquired from the Oversight Committee, no elements arose which the Board must communicate to the Shareholders' Meeting.

4. SUPERVISION OF THE ADMINISTRATIVE ACCOUNTING SYSTEM AND THE PROCESS OF PREPARING THE FINANCIAL STATEMENTS

4.1 General considerations

The Bank, in preparing the financial statements at 31 December 2018, applied the IAS/IFRS international accounting standards issued by the IASB (International Accounting Standards Board) and the related interpretations provided by the IFRIC (International Financial Reporting Interpretations Committee), endorsed by the European Commission as established by Community Regulation no. 1606 of 19 July 2002 and in force at 31 December 2018, and in accordance with the general assumptions provided for in the Framework for the preparation and presentation of financial statements prepared by the IASB. No exceptions were made to application of the IAS/IFRS accounting standards.
The financial statements at 31 December 2018, and the related annexes, were prepared on the basis of Bank of Italy Circular no. 262 of 22 December 2005 "Banking Financial Statements: Formats and Rules for Compilation" as amended by the fifth update of 22 December 2017. As an annex to the Notes to the Financial Statements, the Annual Report at 31 December 2018 related to the MPS Capital Services Banca per le Imprese SPA Pension Fund is provided.
The financial statements were submitted for legal auditing by Ernst & Young S.p.A., which on 14 March 2019 issued its report; this and the work done by the auditing firm, as far as the Board of Statutory Auditors is responsible, is described below in the present report.
This Board of Statutory Auditors assessed the adequacy of your Bank's administrative accounting system, based on interventions of the Internal Audit department, discussions and inspections carried out directly and through exchanges

of information with the auditing firm.
The Board of Statutory Auditors also met several times with the Financial Reporting Manager. On these occasions, the said Manager did not report any shortcomings in the operating and control processes which, owing to their significance, could affect the judgement of effectiveness and efficiency of the administrative structures and of adequacy and effective application of the administrative and accounting procedures.
The organisational processes are therefore capable of ensuring the correct presentation of the Bank's economic and financial situation and capital and conformity with the IAS/IFRS international accounting standards and the reliability of the content of the Report on Operations.
Regarding joint document 4 of 3 March 2010 (and subsequent updates), issued by the Bank of Italy, CONSOB and IVASS regarding application of the IAS/IFRS, this Board notes that the Financial Statements, Report on Operations and the Notes to the Financial Statements were prepared with the "ongoing concern" assumption, given the assessment carried out regarding its capacity to continue to operate as a functioning entity.

4.2 Financial statements auditing and certification firm
The auditing firm Ernst & Young received the appointment to audit the accounts for the financial years from 2014 to 2022 by the Shareholders' Meeting of 28 April 2014, following the proposal formulated by the pro tempore Board of Statutory Auditors under the terms of Italian Legislative Decree 39/2010.
The same firm sent its report certifying the Bank's financial statements at 31 December 2018, dated 14 March 2019, without any objections, and judged it to be clearly prepared and able to truly and correctly represent the equity, the financial situation, the economic result and the cash flows of MPS Capital Services S.p.A. at 31 December 2018.
The Board of Auditors also notes that the auditing firm included in its certification its judgement of consistency between the report on operations and the financial statements and carried out the procedures as indicated in auditing standard no. 001 as issued by the Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili (National Council of Accountants and Accounting Experts), recommended by CONSOB.
Among the elements of greatest significance contained in the certification report transmitted by the auditing firm, it is worth mentioning specifically that related to first application of the accounting standard IFRS 9, which came into force on 1 January 2018, replacing IAS 39.
During the year the Board of Statutory Auditors met several times with the auditing firm for the necessary exchange of information and in particular on the performance of the activity of legal auditing of the accounts.
In this context, the auditing firm reported on the performance of certain activities particularly aimed at verifying the correct application of the accounting standard IFRS 9, including:

- SPPI: independent re-performance on a sampling basis of the SPPI test carried out by the Bank
- Stage Allocation: verification, on a sampling basis, of the correct classification among the various staging categories
- Models and parameters (impairment): analysis and understanding of the models and parameters used for impairment according to IFRS 9. Analysis of the methods of including forward-looking information in the models (including sales scenarios) and of the methods of determining the Expected Credit Loss.

The auditing firm also transmitted the additional report pursuant to art. 11 of Regulation (EU) 537/2014 drawn up on 14 March 2019 in the context of which it reports that it has not identified significant shortcomings in the internal control system for financial disclosure and/or in the accounting system. No reports were received from the auditing firm on facts considered reprehensible found in the performance of the independent auditing activity and, in the context of the additional report, the absence of significant difficulties in performance of the auditing mandate assigned was acknowledged.
The Board of Statutory Auditors makes known that it has not encountered the presence of critical aspects in relation to possession of the independence requirements on the part of the auditing firm and that it has received confirmation in this sense from the same auditors under the terms of art. 17, paragraph 9, letter a) of Italian Legislative Decree 39/10.

fees paid to the auditing firm for performing the legal auditing of the accounts amounted to a total of € 210 thousand. The firm then carried out further activities (certification services) which entailed fees for € 18 thousand.
We must specify that the above amounts are net of VAT and ancillary expenses.

4.3 Monitoring and adequacy of the regulatory capital

The Board of Statutory Auditors notes that to measure the economic capital absorbed, the models developed internally by the Parent Company based on the Value at Risk approach are applied.
The Parent Company, to which the Bank has outsourced the validation activity, carries out periodic checks on the adequacy of the models used and prepares the supervisory reports on a quarterly basis, including the statements of capital absorption and verification of the adequacy levels.
The Board of Statutory Auditors monitored the preparation of the Company's reporting on the capital, and verified that the Board of Directors monitored on the subject of keeping the regulatory capital at levels such as to ensure compliance with the capital ratios required.
On this point, the Bank has capital ratios higher than the minimums prescribed. The Common Equity Tier 1 ratio (Common Equity Tier 1 capital/Risk-weighted assets) and the Tier 1 ratio (Total Tier 1 Capital/Risk-weighted assets) come out at 13.03% (13.74% at 31/12/2017), while the Total capital ratio (Total Own Funds/Risk-weighted assets) was 18% (18.87% at 31/12/2017). Own Funds came out at € 1,659 million, compared to € 1,711 million at the end of the previous financial year.

5. OTHER AUDITING ACTIVITY AND CERTIFICATIONS

5.1 Members of the Board of Directors

The current Board of Directors, appointed by the Shareholders' Meeting of 07/04/2017, will remain in office until approval of the financial statements for the year at 31 December 2019. At its meeting on 2 May 2017, the Board of Directors appointed Giampiero Bergami as the Managing Director. On 31 May 2017, Antonio Nucci resigned as Chairperson of the Bank and on 18 August 2017 the Shareholders' Meeting filled his position, appointing Mario Comana as Chairperson of the Bank, as well as appointing Riccardo Tiscini to fill the missing Director position. On 01/01/2019, Mr Giampiero Bergami resigned from the position of Managing Director and Director of the bank, as did Ms Ilaria Maria Dalla Riva on 14/02/2019. In this regard, the Board of Directors, at its meeting on 27 February 2019, re-established the minimum number of members of the Board of Directors, co-opting Mr Fabiano Fossali and Ms Mariangela Bonfadini.

5.2 Transactions with related parties, associated subjects, obligations of bank representatives; Self-assessment of the Board of Directors

The Independent Directors, to whom the MPS Capital Services Board of Directors has jointly assigned the tasks and functions previously attributed to the Related Parties Committee, carried out the activities placed under their responsibility under the current legislative and regulatory provisions.
In particular, during financial year 2018, the Independent Directors were involved in the process of self-assessment of the Bank's Board of Directors.
More specifically, on the proposal of the Independent Directors, the Legal Office was identified as the Bank's internal Office tasked assisting and supporting the process of self-assessment of the Board of Directors.
In particular, the Legal Office prepared the self-assessment questionnaire, submitting it to the prior assessment of the

Independent Directors and of the Parent Company's Legal Area. It then analysed the results of the questionnaires and prepared the draft of the final Report, which was submitted to the Independent Directors.
The Report, which summarised the results of the self-assessment process and identified the strong and weak points found, was taken by the Independent Directors to the attention of the Board of Directors for approval of the related resolution on 19 October 2018.
Additionally, the Independent Directors received quarterly reports from the Legal Office on transactions with related and associated parties carried out by the Bank, as defined in the Bank of Italy and CONSOB provisions, performing sample checks on them. They also provided the opinions requested from them in relation to transactions with related parties which, as initially cited, could not be classified as cases for exemption and performed the further activities and tasks under their responsibility, including the issue of the necessary opinions on the subject of approval of the framework resolutions.
From the work done by the Independent Directors no situations and/or transactions have emerged that would be incompatible with the rules set on the matter by the Bank.

5.3 Remuneration policy

The Board verified that the Board of Directors provided a report to the shareholders, at the Shareholders' Meeting held on 21 December 2018, regarding the remuneration policies adopted and their application for financial year 2017.

5.4 Self-assessment of the Board of Statutory Auditors

Bank of Italy Circular No. 285 of 17 December 2013 on Corporate Governance, updated on 6 May 2014, indicates the "self-assessment process" of the strategic supervision, management and control bodies as an essential element of an effective governance system for the Bank. The Board of Statutory Auditors, on the basis of the conclusion of the appointment to prepare the Self-Assessment Report attributed at its meeting on 19 October 2018 to the Legal Office - Corporate and Related Parties Sector of MPSCS, at its meeting on 17 January 2019, approved the Self-Assessment Report, which contains a "substantially adequate" assessment (average score of 3) for all three areas — 1) "Self-Assessment of the Statutory Auditor", 2) "Self-Assessment of the Composition of the Board of Statutory Auditors", 3) "Self-Assessment of the functioning of the Board of Statutory Auditors" — into which the self-assessment questionnaire is divided.

5.5 Opinions

During the year the Board of Auditors gave its opinions on the following subjects:
(i) the 2017 Audit Plan Annual Report and the 2018 Audit Plan;
(ii) the emoluments payable to the Independent Director who is a member of the Oversight Committee pursuant to Italian Legislative Decree 231/2001;
(iii) the indemnities payable to the auditing units;
(iv) the 2018 Validation Plan;
(v) the appointment of the Manager of the Risk Control and Internal Validation Unit;
(vi) the proposal formulated by the Auditing Firm EY SpA for the additional appointment for limited auditing of the quarterly report on operations at 31 March 2018;
(vii) the appointment of the Data Protection Officer (DPO);
(viii) the appointment of the Manager of the Internal Validation Unit;
(ix) the appointment of the New Manager of the Compliance Unit.

5.6 Other certifications
No complaints pursuant to Article 2408 of the Italian Civil Code, nor claims of any other kind, were made to the Board.
During all the activities performed and from the examination of the information obtained from the auditing firm, no omissions and/or irregularities or in any case significant facts, such as to require notification to the Oversight Committees or mention in this report, were found.

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Conclusions
In conclusion, in view of what is described above and having no observations or proposals on the subject of the financial statements, the Board of Statutory Auditors has no objections to:

- the approval of the financial statements for the year ended 31/12/2018, consisting of the balance sheet, the income statement, the statement of comprehensive income, the statement of changes in shareholders' equity with the related changes in the reserves, the cash flow statement and the Notes to the Financial Statements, as well as the associated annexes and the Report on Operations;
- the proposal for allocation of the accounting profit to reduce the retained loss of financial year 2017, as formulated by the Board of Directors.

Florence, 25 March 2019
THE BOARD OF AUDITORS

Mr Graziano Gallo	Chairperson
Mr Werther Montanari	Regular Auditor
Ms Lara Zampiero	Regular Auditor

SHAREHOLDERS' MEETING RESOLUTIONS

Shareholders' Meeting Resolutions

The ordinary Shareholders' Meeting, called and held on first convocation on 10 April 2019, has passed the following resolutions:

POINT 1 OF THE AGENDA

Approval of the 2018 Financial Statements, comprising the balance sheet, the income statement, the statement of changes in shareholders' equity with the related movements in reserves, the statement of cash flows and the Notes, as well as the related attachments and Report on Operations, as a whole and in their individual items, as presented by the Board of Directors.

POINT 2 OF THE AGENDA

Allocation of the profit for the year as follows:

PROPOSED ALLOCATION OF PROFIT FOR 2018		
- to reduce the retained loss of financial year 2017	euro	80,699,464.61
resulting equal to euro 361,730,253.70		
PROFIT FOR 2018	euro	80,699,464.61

POINT 3 OF THE AGENDA

The appointment of two members of the Board of Directors, to re-establish the minimum number following the resignations of Mr Giampiero Bergami and Ms Ilaria Maria dalla Riva, specifically Messrs:

- FABIANO FOSSALI
- MARIANGELA BONFADINI

POINT 4 OF THE AGENDA(point deferred and dealt with in the adjourned session of 21 May 2019)

Appointment of the Board of Auditors, due to termination of the mandate of the former members, composed of:

- FRANCO GHIRINGHELLI, Chairperson
- ANTONELLA GIACHETTI, Regular Auditor
- LOREDANA ANNA CONIDI, Regular Auditor
- AIAN ABBAS HAGI HASSAN, Alternate Auditor
- MICHELE APRILE, Alternate Auditor

POINT 5 OF THE AGENDA(point deferred and dealt with in the adjourned session of 21 May 2019)

Determining the emoluments and treatments for the members of the Board of Statutory Auditors.