# FINANCIAL STATEMENTS 2018

LUMINOR GROUP AB

CONSOLIDATED ADMINISTRATION REPORT,
SEPARATE AND CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018

# TABLE OF CONTENTS

# CEO STATEMENT

**Building a modern, accessible and truly Baltic banking partner to our customers**

I started as CEO of Luminor in October 2017, when the company was created through the merger of DNB's and Nordea's Baltic operations. It was clear then that the transformation of merging and harmonizing these operations into one, modern, pan-Baltic operation would require a lot of effort, but was a necessity to create the nimble, efficient and customer-oriented bank we want to be.

In 2018 we took the first steps on this journey by merging six legal entities into one pan-Baltic organization, by beginning the task of setting up one harmonized and independent IT infrastructure and by launching a number of operating initiatives to improve the viability, profitability and agility of the bank.

Through the hard work of all our employees, we have so far had only minor disruptions to our customer service, which will remain our key priority throughout this transformation.

It is clear that the on-going digitalization of our industry, enabling easy access to products and services and increasing the time available for value-added advice, is dramatically changing customers' perceptions and demands of their banks. So far, financial "disruptors" have primarily operated in the product part of our value chain, but with time they will target banking distribution too, through open architecture aggregator platforms.

I believe in a coherent, trustworthy and complete bank offering, utilizing our core competences of assessing credit risk, helping customers with payments and cash handling, and offering competitive and relevant savings advice, in the best interest of our customers.

Banking should be easy, affordable and accessible, and that requires a deep customer understanding, efficiency and scale in order to be competitive in the long-term.

The transformation we have embarked on is crucial for us to achieve the independence and efficiency required to deliver this vision to our customers, as well as for being an attractive partner for innovative 'FinTech' companies.

Our financial results improved quite substantially in 2018 reaching net profit of EUR 125 m, not least considering we had extraordinary expenses for the ongoing transformation of around EUR 26 million. However, profitability is far from satisfactory with a ROE of 7.1%.

To ensure we have the means to invest in relevant solutions and strong service to our customers, we have to improve the bank's profitability. Our earnings are also our first line of defense against any set-backs in the economic or credit environment.

Our activities to improve profitability will be focused around four priority areas, all of which were initiated during the year:

1) Improve our efficiency. One of the rationales behind the merger in 2017 was to create better economies of scale, and to extract synergies. We will harmonize overhead and group functions, remove duplicative and wasteful activities, consolidate our branch

network and create more automated processes. We will also ensure that *all* activities in the bank are relevant to our customers.

2) Improve Luminor's funding position. As the third largest player in the market, we should not have a materially different loan-to-deposit ratio from our large competitors. As a response, we have increased our focus on deposits, which will soon be aided by an improved technology offering. We are also well underway with our wholesale funding strategy, having raised our EUR 350m inaugural senior secured bond in October 2018 under our new EMTN program, and are already evaluating further issuances. We are also preparing to issue covered bonds, where we expect that the the Estonian covered bond legislation will come into effect during the latter part of 2019. We acknowledge that we are a new issuer in the global capital markets, but are working hard to educate investors about our story and build trust in the funding markets through transparency and by delivering on our promises.

3) Improve capital efficiency. Luminor is the only large Baltic bank still working under the standardized capital approach under the Basel framework. Even if the differences to the Internal Rating Based approach will decline with Basel 4, we need to ensure we steer and price risk in an adequate way to build an efficient balance sheet, as well as working with our understanding, stress testing, and modelling of our credit risks, to close the gap to our competitors, regarding capital consumption. This work will take time, and it will probably involve regulatory approvals for new risk models, but it will be prioritized.

4) Ensure fair and rational pricing of risk. Even when adjusting for our relative operating cost and capital disadvantage versus our competitors, over half of our loan portfolio fails to reach a profitability level above cost of capital. We will strive to price our business fairly and transparently, and to win business on relevance to our customers in our offering and service. We are convinced that we can improve our profitability and remain competitive.

We will also ensure that our capital and risk levels are calibrated in a way which allows Luminor to withstand a severe downturn without having to ask for additional capital from its owners. We believe that the stability and independence of a bank from a capital planning perspective is paramount to gaining trust from all stakeholders - customers, the funding market, employees, owners and the broader society.

We are continuing the hard work and large investments that we have made over the past years into improving our systems and processes for compliance and prevention of money laundering. The latter topic has received significant, but needed, scrutiny during the year, and will remain a key focus of authorities, regulators, media and the wider society, both in the region and abroad.

This will remain a key priority for us as a bank. Our proficiency in monitoring and detecting cases of attempted, or suspicious, money laundering, is continuously improving. However, we can never fully protect ourselves from attempts to abuse our bank for these rogue purposes, but we must tirelessly continue to improve and refine the customer scrutiny before and after on-boarding, improve our transaction monitoring, and report what we find to the authorities. The hard work and investments will continue.

The Baltic economic environment is benign currently, with healthy growth rates in GDP, almost full employment and balanced current accounts. Savings rates are also on healthy levels. The Baltic region is also benefitting from low indebtedness compared to many other European countries, with average government debt/GDP of 31.8% and average household debt/GDP of 26.3%.

While this gives room for a sound improvement of living standards relative to our European neighbors in the years to come, we also need to be mindful that times can change, and that as one of the leading bank in the region we play an important role in these respects being large employers and credit providers.

I would also like to highlight another significant event during the year, namely that a consortium led by private equity funds managed by Blackstone - one of the world's largest private equity firms - in September 2018 agreed with Nordea and DNB to acquire 60% of Luminor, with an option to acquire Nordea's remaining 20% over the coming years.

With Blackstone, we get an owner-partner, fully supportive of investing in making Luminor the preferred banking partner for consumers and companies in the region. We now have both the operational and financial muscle to accelerate our change agenda, for the benefit of all our stakeholders. The transaction is subject to regulatory approval, but is expected to close in the middle of 2019.

In September, Luminor received its first independent credit rating, when Moody's assigned the bank a Baa1/P2. Subsequently we issued our first senior unsecured bond - a EUR 350m three-year benchmark transaction - as an important first step to securing our long-term funding needs as an independent company.

As mentioned, our change program continues and accelerates in 2019. This year, our focus is on improving Luminor's IT-environment and on improving our underlying profitability and funding position. In addition, we are launching a major initiative to upgrade our online services across our three markets, towards both households and corporates. We also have ongoing initiatives to simplify our product and service portfolios, to make the bank even more accessible to all customers. As a result, we expect to incur a high level of exceptional and restructuring costs during the year.

The transformation will not be without its challenges, but we will work tirelessly to ensure our customers are well served. Ultimately, all our investments in building this bank are supporting our goal to create the modern, accessible, truly Baltic banking partner that our customers deserve.

Finally - let me extend a warm thank you to our two most important stakeholders - our customers, and all of my colleagues within the bank - for this last year. As long as we have the trust of our customers, and the integrity, intelligence and energy of all our employees, I know our other stakeholders will also be happy.

# LUMINOR GROUP AB CONSOLIDATED ADMINISTRATION REPORT FOR THE YEAR 2018

## INTRODUCTION

Luminor Group AB (or "Luminor") is a holding company established in the Kingdom of Sweden and it is a 100% shareholder of each of the Baltic Luminor banks: Luminor Bank AS (Estonia), Luminor Bank AS (Latvia) and Luminor Bank AS (Lithuania). Luminor Group AB's commercial register number is 559072-8316 and it is headquartered in Stockholm.

Luminor was established on 1 October 2017 through the merger of DNB Bank ASA (Commercial Register no. 984 851 006) and Nordea Bank AB (currently Nordea Bank Abp, as after 1 October 2018 Nordea is domiciled in Finland, following the execution of the cross-border reversed merger between Nordea Bank AB (publ) and Nordea Bank Abp, registration no. 2858394-9) Baltic operations to create a new-generation financial service provider for local Baltic businesses and financially active people.

During 2018 Luminor continued with cross-border merger activities. The cross-boarder merger agreement (merger terms) was signed on 29 March 2018 in Tallinn, Estonia. In May 2018 Luminor received a confirmation from the European Central Bank that the branches in Latvia and Lithuania could be established and commence their activities. On 28 June 2018 Luminor received a regulatory approval from the European Central Bank to carry out the cross-border merger. In July 2018 the branches in Lithuania and Latvia were established and branch managers appointed  (this structure was left as non-operating till merger takes effect). The merger will take place on 2 January 2019.

Luminor is the third-largest financial services provider in the Baltics, with ca 1 million clients, ca 3,000 employees, 16% market share in deposits and 22% market share in lending. Total shareholder equity of Luminor amounts to 1.8 billion euros and it is capitalised at CET1 18%. Luminor's vision is to become the best financial ecosystem for its customers.

## MACROECONOMIC OVERVIEW

After entering the peak of the business cycle the global economic recovery did become less synchronized in 2018. Escalating trade tensions, tightening of global monetary conditions, geopolitical strains were among the key sources of elevated uncertainty, which resulted in softer business and consumer expectations, as well as increasing market volatility. Markets' risk-off sentiment hit emerging economies the most and fed safer assets of the developed world. In addition, Emerging Asia, the core engine of the global economy, fell in the epicentre of escalating trade disputes between the U.S. and China. Meanwhile, the U.S. economy, supported by pro-cyclical fiscal stimulus, remained in a good shape. It grew by nearly 3% y/y last year underpinned by further strengthening in the labour markets with emerging signs of wage pressures. The Euro area, the key destination of exports for the Baltic economies, faced softening economic pulse. Euro-area GDP decelerated from a rather strong 2.4% y/y pace in Q1 2018 (0.4% q/q) to a modest 1.6% y/y (0.2% q/q) in Q3 2018, reflecting predominantly weaker impetus from external trade, increasing uncertainty, as well as a number of temporary demand (incl. weather-related) and supply-side factors encompassing difficulties in the car industry (in adapting to new emission-test procedures in Q3). All that resulted in Euro-area annual growth moderated from a bold 2.5% leap in 2017 to a still healthy close to 2% y/y recovery last year.

**The Baltic countries** have continued to demonstrate robust economic expansion, outpacing Euro-area average by a solid margin. The economic upturn in recent years was broad-based resting on all main growth pillars, i.e. accelerating domestic demand, increasing business appetite for productive investments and expanding exports revenues. Estonia's growth rate decelerated from a strong 4.9% y/y pace in 2017 to 3.8% y/y (Q1-Q3 2018). In Latvia, the exceptionally strong recovery has continued on the heels of resilient domestic demand, expanding construction and retail activities with an average 4.7% growth rate recorded during the first three quarters of 2018 (4.6% y/y in 2017). Only marginal moderation of strong above-trend growth rate, very much like Estonia, has taken hold in Lithuania with 3.3% y/y GDP development in Q1-Q3 2018 (following 4.1% y/y a year before). Notably softer momentum in Q3 resulted largely from temporary factors (drought affecting agriculture), with overall expansion in investments and manufacturing continuing strong. After the summer months the threat from further escalation of global trade tensions, rising oil prices and EM vulnerabilities have on balance increased the growth risks for the region. Despite a solid underlying demand trend this may weigh on export confidence, orders and could potentially dampen investments appetite. The impact on business and consumer confidence has so far been limited. Overall, despite the accumulating headwinds in the external sector, the economic backdrop in the Baltic countries has remained favourable with ongoing tightening in labour market and unemployment rates falling to new post-crisis lows.

## OPERATIONS - MAIN ACTIVITIES

**The strategic priorities of Luminor have been defined as follows:**

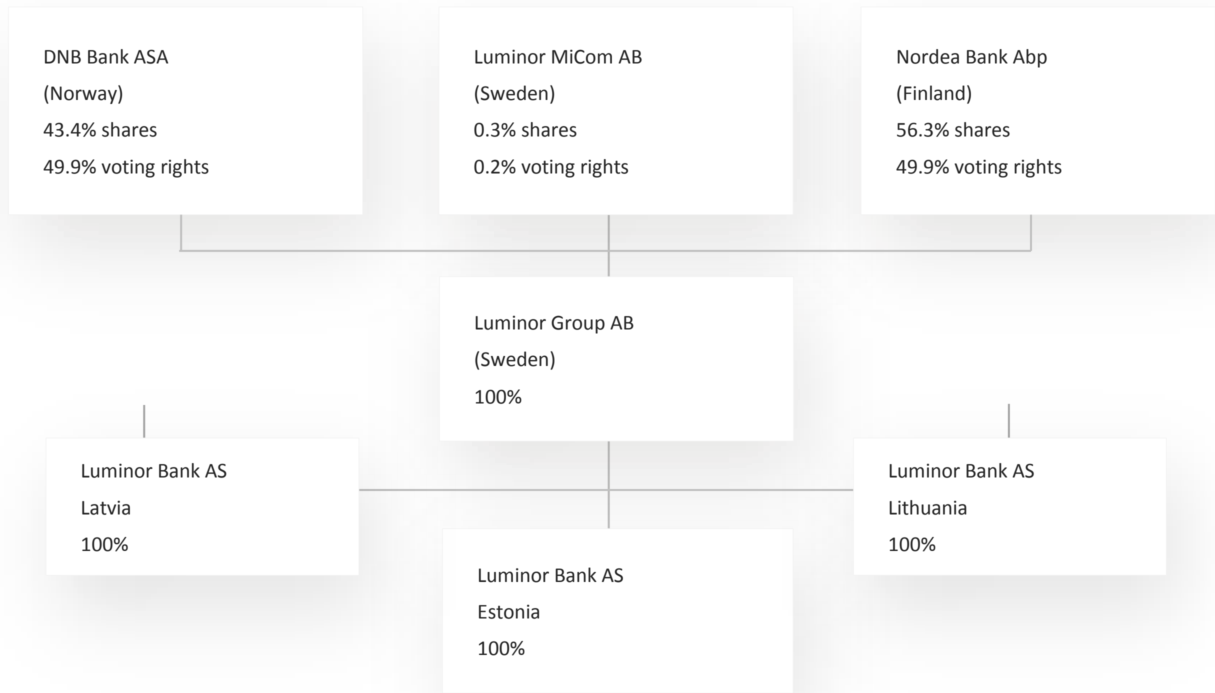
- Creation of a leading customer-centric, primary Baltic bank with Nordic roots: Achieve service excellence and implement operational excellence;
- Operational and funding independence over time: IT separation and consolidation, set-up of required group functions and drive balance sheet efficiencies; and
- Profitability: Achieve a sustainable return on equity in line with the company's cost of equity.

The Luminor Group AB Board of Directors takes strategic decisions, overviews risk management and compliance with the laws and regulations within the Group.

The Luminor Group AB Board of Directors exercises the rights of the shareholders of each of the banks in Lithuania, Latvia and Estonia. According to the Articles of Association of the Luminor Group AB, the Luminor Group AB Board is composed of 1-8 directors and up to 6 deputy directors, elected and discharged by the Shareholders Meeting of Luminor Group AB. As of December 2018 the Luminor Group AB Board has 6 members. The Shareholders Meeting also has the right to appoint and discharge a managing director (CEO).

The decisions of the Board of Directors are implemented via the Supervisory Councils and Management Boards of local Banks. The Board of Directors approves business plan for the Group and each fiscal year approves an update of the short-term financial plan for the Group. Specific matters handled by the Board of Directors as well as reporting to the Board of Directors are outlined in the Governance Policy. The Board of Directors meetings are held at least quarterly.

**Group overview-structure**




Luminor banks in Latvia, Lithuania and Estonia each owns several subsidiaries and other shareholdings, including, among others, regulated subsidiaries like pension fund management companies, an insurance broker company (in Estonia) and leasing companies, as well as special purpose vehicles owning repossessed assets and a real estate broker company (in Lithuania).

Nordea Bank Abp and DNB Bank ASA are ultimate owners of holding company Luminor Group AB. Nordea Bank Abp and DNB Bank ASA have equal voting rights in Luminor Group AB. Nordea Bank Abp owns 56.3% and DNB Bank ASA owns 43.4% of proprietary rights, which reflects the proportional contribution of each bank made at the closure of the Luminor Group transaction on 1 October 2017.

DNB Bank ASA (commercial register number 984 851 006) is Norway's largest financial services group and one of the largest in the Nordic region in terms of market capitalization. The DNB group offers a full range of financial services, including loans, savings, advisory services, insurance and pension products for retail and corporate customers. DNB Bank ASA has a credit rating (S&P AA-, Moody’s Aa2).

Nordea group is the largest financial services group in the Nordic markets (Denmark, Finland, Norway and Sweden) measured by total income, with additional operations in Russia and Luxembourg, and branches in a number of other international locations. Nordea Group offers a comprehensive range of banking and financial products and services to household and corporate customers, including financial institutions. Nordea Bank Abp (Finnish registration number 2858394-9) has a credit rating (Fitch AA-, Moody’s Aa3).

During 2018 Luminor group continued to focus on the following initiatives as its main priority areas: oversee banks' direction, results, risk management, IT development activities, including planning new digital platforms and new offerings to the target customers, migration plans.

## SIGNIFICANT EVENTS DURING THE YEAR

During 2018 Luminor continued with cross-border merger activities. The cross-boarder merger agreement (merger terms) was signed on 29 March 2018 in Tallinn, Estonia. In May 2018 Luminor received a confirmation from the European Central Bank that the branches in Latvia and Lithuania could be established and commence their activities. On 28 June 2018 Luminor received a regulatory approval from the European Central Bank to carry out the cross-border merger. In July 2018 the branches in Lithuania and Latvia were established and branch managers appointed (this structure was left as non-operating till merger takes effect). The merger took place on 2 January 2019.

On 13 September 2018 an agreement was signed between DNB Bank ASA and Nordea Bank AB with Braavos Bidco Limited (the ultimate shareholders of which belong to a consortium led by funds managed by Blackstone ("Blackstone")) to sell the majority stake in Luminor Bank AS (Estonia). As a part of the transaction, Blackstone will acquire a 60% majority stake in the bank. Nordea and DNB will retain an equal 20% equity stake in Luminor and will continue to support Luminor group with long term funding, expertise and ongoing representation in the governing bodies of Luminor. Additionally, Blackstone has entered into an agreement with Nordea to purchase their remaining 20% stake over the coming years. The closing of the transaction is subject to European Central Bank's and local supervisory authorities' approvals and is anticipated to occur in the first half of 2019.

In September 2018 the rating agency Moody's assigned to Luminor Estonia a first-time deposit credit rating of Baa1 and senior MTN rating of Baa2.

As inaugural public bond issue, on 18 October 2018 Luminor issued three-year senior unsecured bonds in amount of 350 million euros.

## COMPLIANCE AND ANTI-MONEY LAUNDERING RELATED MATTERS

Luminor has chosen to serve primarily customers having strong presence and connection to the Baltic countries avoiding to take on unnecessary risk that follows through having non-residential customers. Focusing on serving the Baltic customers we continuously aim for a full transparency in customers background, availability of KYC data and economic rationale in activities. At Luminor, we have zero tolerance towards money laundering and other financial crime. Luminor has developed and implemented a comprehensive set of measures to identify, manage and control its risks. We comply with sanctions laws and follow the guidelines, recommendations and standards issued by local regulatory and supervisory authorities and relevant international organizations, as well as those issued by local banking associations and financial intelligence units in each Baltic state.

Our Compliance and Anti-Money Laundering (AML) functions are operating at the pan-Baltic level, having competence centers and highly experienced professionals in the following areas: data protection, AML/ Certified Fraud Examiners (CFT), FATCA, IT compliance and digital channels, business integrity, bank products & new product development. Luminor's AML, Compliance and Anti-Financial Crime units employs over 100 professionals, maintaining a robust compliance framework and processes through the organization.

## SIGNIFICANT EVENTS AFTER 31 DECEMBER 2018

On 2 January 2019 Luminor completed its cross-border merger and continues its operations in all Baltic countries through the Estonian registered bank and its branches in Latvia and Lithuania. After the completion of the merger all assets, rights and liabilities of Luminor Latvia and Luminor Lithuania were transferred to Luminor Bank AS in Estonia. The bank will continue the same activities in Latvia and Lithuania through its locally established branches.

Starting from 2 January 2019 the deposits and financial instruments of the depositors and investment services clients of Luminor Bank AS Latvian branch and Luminor Bank AS Lithuanian branch will be guaranteed by the deposit guarantee and investor protection scheme established and operated by the Estonian Guarantee Fund.

As of 2 January 2019, after completion of the merger, Luminor has a new organizational set up, a new governance structure and new members of management bodies. Erkki Raasuke will continue as Luminor ’s CEO and Nils Melngailis will be chairing the supervisory board.

### The new governance structure of Luminor:

**Supervisory Council of Luminor Bank AS**

- Nils Melngailis, Chairman of the Council
- Bjørn Erik Naess, Member of the Council
- Jörgen Christian Andersen, Member of the Council
- Michael Jackson, Member of the Council
- Trygve Young, Member of the Council

On 23 January 2019 two additional council members were appointed to Luminor Bank AS - Ari Kaperi and Nadine Faruque.

**Management Board of Luminor Bank AS**

- Erkki Raasuke, Chairman of the Management Board
- Christian Wallentin, Member of the Management Board, CFO, Head of Financial division
- Kristina Siimar, Member of the Management Board, Head of Products and Offerings
- Kerli Gabrilovica, Member of the Management Board, Head of Luminor Latvian branch
- Andrius Načajus, Member of the Management Board, Head of Luminor Lithuanian branch
- Hannu Saksala, Member of the Management Board, Head of Risk division

On 31 January 2019 Christian Wallentin, CFO and Head of Financial division has resigned from his position and management board, to pursue other interests. Following Wallentins resignation, Tina Kukka Head of Transformation Management Office, will assume the role of interim CFO and lead the Financial division along with her current duties. Luminor is in the process to appoint a new permanent Chief Financial Officer.

The permanent committees which were previously established for each Baltic country separately are going forward and operating as single committees on a group level, comprising Audit Committee, Risk Committee, Nomination Committee and Remuneration Committee.

After completing the cross-border merger, Luminor has taken steps to re-organize its operative model. On 7 January 2019 Luminor has decided to proceed with the next phase of transformation, including changing operating model. The bank aims to transform its operating model by simplifying its structure and decision process, unifying and executing IT consolidation, strengthening its controls, and becoming more efficient, more resilient and more resolvable. During 2019 Luminor will be simplifying its operating model and reducing its staff numbers from the current ca 3000 employees, at all levels (including management), with reductions comprising of around 130 employees in Estonia, 250 employees in Latvia and 420 employees in Lithuania.

Through the consolidation of its technological platforms, the right-sizing of the business and the simplification of the product and service portfolio, Luminor aims to significantly reduce operating expenses, accelerate its transformation to build and execute in areas of superior customer experience and ensure higher capacity to invest for the future.

## INFORMATION ON PERFORMANCE RESULTS

Luminor Group started banking operations in the Baltics in October 2017 after combining DNB and Nordea Baltic businesses. Accordingly, since October 2017 comparative figures include Luminor Bank AS (Estonia), Luminor Bank AS (Latvia), Luminor Bank AB (Lithuania) and holding company Luminor Group AB (Sweden). Prior to this date, only the results of the holding company Luminor Group AB (Sweden) are included.

| KEY FIGURES (T EUR) | 31.12.2018 |
|---|---|
| Net profit | 124 949 |
| | |
| Average equity | 1 757 148 |
| Return on equity (ROE), % | 7.1 |
| | |
| Average assets | 15 201 023 |
| Return on assets (ROA), % | 0.8 |
| | |
| Net interest income | 259 733 |
| Average interest earning assets | 14 844 146 |
| Net interest margin (NIM) % | 1.7 |
| | |
| Cost / Income ratio, % | 62.3 |

**Explanations**

Average equity (attributable to owners of the Luminor Bank AS) = (Equity of current year end + Equity of previous year end) / 2

Return on equity (ROE) = Net profit/Average equity * 100

Average assets = (Assets of current year end + Assets of previous year end) / 2

Return on assets (ROA) = Net profit/Average assets * 100

Average interest earning assets = (Average interest earning assets of current year end + Average interest earning assets of previous year end) / 2

Net interest margin (NIM) = Net interest income/Average interest earning assets * 100

Cost/Income Ratio = Total Operating Expenses/Total Operating Income * 100

Luminor Group has managed to maintain its business momentum while integrating the operations to achieve a solid financial result in 2018. Net profit for the year amounted to 124.9 million EUR. As compared, in 2017, a loss of 5.7 million EUR incurred affected by higher impairment costs for the period. Total operating income in 2018 reached 361.4 million EUR, of which net interest income was 259.7 million EUR. Total operating expenses stood at 225.1 million EUR., including extraordinary expenses of around EUR 26 million for the transition transformation work mostly related to IT expenses (56%), staff (30%) and other transformation costs (14%).

Loans to the public stood at 11.5 billion EUR at 31 December 2018 decreasing by 1.8% compared to 31 December 2017. Loans to non-financial corporate customers comprised 46% and loans to households 51% of the credit portfolio of Luminor. The market share of Luminor's loans in Baltics was approximately 22%.

Deposits from customers totalled 9.1 billion EUR at 31 December 2018, increasing 7.6% from 31 December 2017. Deposits from non-financial corporate customers comprised 43% and deposits from households 41% of the customer deposit portfolio of Luminor. The majority of deposits are from Baltic residents and 98% of all deposits are from EU residents. The market share of Luminor's deposits in Baltics was approximately 16%. The loan-to-deposit ratio was 126% at 31 December 2018 compared to 139% at 31 December 2017.

## CREDIT QUALITY

Credit quality remains good with decreasing levels of impaired loans as Luminor puts a strong focus on non-performing asset management. The Luminor Group also pays special attention to determining proper and acceptable risk criteria that are applicable in credit decision making as well as in monitoring process seeking to sustain optimal credit risk level.

In 2018, Group lending portfolio had decreased, continuing to focus on sound credit quality and efforts to right-size and reprice the portfolio, in order to ensure adequate risk adjusted profitability of each individual exposure. Positive portfolio quality trend is supported by lower level of non-performing loans, despite the broader default definition according to IFRS9. Impaired loans were at 5.3% for the end of 2018 (5.5% in 2017), while total on-balance sheet allowances amounted to EUR 190.4 million, adding up to 30.7% provisioning ratio. Majority of the gross impaired loans were related to non-financial corporations' exposures primarily in Latvia and Lithuania.

Luminor continuously reviews and updates credit risk strategy to maintain sound credit culture and sustain high quality of assets.

**Asset quality of Luminor Group AB as of 31 December 2018**

| T EUR | Household | Non-financial corporations | Other financial corporations | General governments | Total* |
|---|---|---|---|---|---|
| Gross Loans | 5 968 156 | 5 419 771 | 58 752 | 215 866 | 11 662 545 |
| Allowances | (96 654) | (92 769) | (966) | (18) | (190 407) |
| Net Loans | 5 871 502 | 5 327 002 | 57 786 | 215 848 | 11 472 138 |
| Gross Impaired Loans | 238 183 | 381 617 | 0 | 0 | 619 800 |

| | | | | | |
|---|---|---|---|---|---|
| Credit Impairment ratio, % | 1.62 | 1.71 | 1.64 | 0.01 | 1.63 |
| Gross Impaired Loans vs Gross Loans (NPL ratio), % | 3.99 | 7.04 | 0.00 | 0.00 | 5.31 |
| Allowances vs Gross impaired Loans, % | 40.58 | 24.31 | N/A | N/A | 30.72 |

*excluding Loans to Credit Institutions

**Explanations:**

Impairment ratio % = Allowances / Gross Loans

Gross impaired loans vs Gross Loans (NPL ratio) % = Gross impaired Loans / Gross Loans

Allowances vs Impaired Loans = Allowances(Provisions) / Gross Impaired Loans

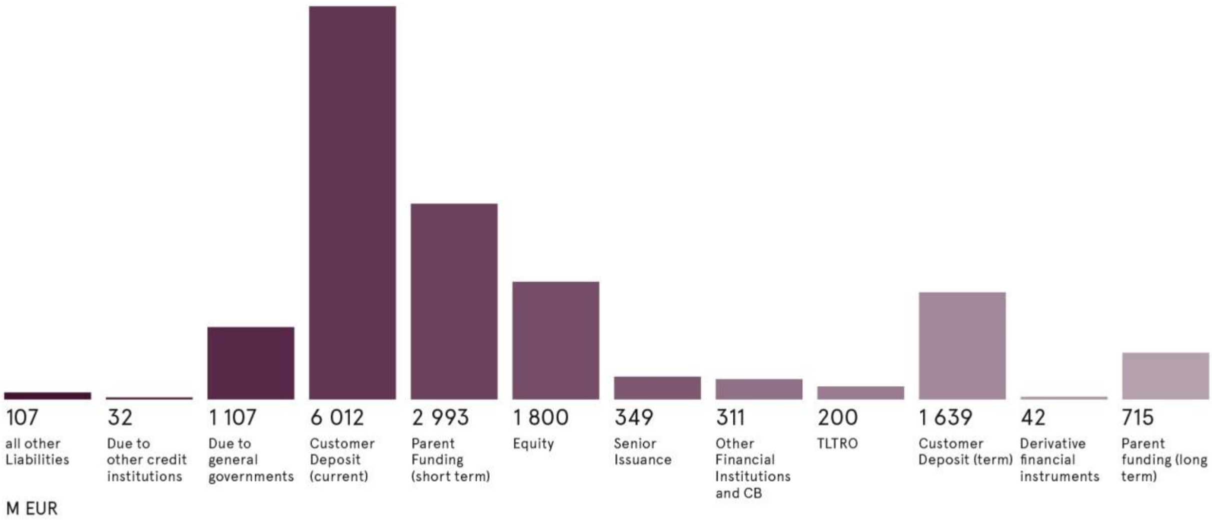
## FUNDING

One of the main objectives for Luminor is to create a self-sustainable banking group. In order to achieve this, one key prerequisites is to gradually replace parent funding with other forms of funding – deposits and wholesale funding from 3rd parties. Luminor has achieved tangible results in getting closer to being a self-funded independent banking group. In September 2018 Moody's assigned Luminor Bank AS (Estonia) a Senior Unsecured Medium-Term Note Program rating of Baa2. The assignment of rating was followed by a 350 million senior unsecured inaugural public bond issue with a maturity of 3 years. Despite the market turbulence at the time of issuance, Luminor was able to attract investors around Europe supported by good local demand.

On a year-over-year comparison Luminor was able to grow deposits from the public by 640 million EUR. As a result Luminor's market share in deposits increased from 15% to 16%. In 2019 it is expected that the deposit portfolio will continue increasing.

Among other sources of funding Luminor is also using TLTRO II (Targeted Long-Term Refinancing Operations II) and parent funding. Parent funding is provided by two parent banks in the form of a syndicated loan, where each parent bank provides 50%. In addition to the current outstanding utilized funding, there is also an unutilized committed credit line of 896 million EUR in place as at 31 December 2018 (31 December 2017: 676 million EUR). As at 31 December 2018 outstanding TLTRO funding was 199.5 million EUR (31 December 2017: 360.5 million EUR).

At the end of 2018, Luminor had utilised 3 708 million euro in funding from the parent banks.




Funding of Luminor is optimized between short and long-term funding to have the Net Stable Funding Ratio (NSFR) above 100%. As at 31 December 2018 NSFR was 123% (31 December 2017: 119%). For the purpose of NSFR calculation,  to mortgages that would qualify for 35% or lower risk weight currently 85% Required Stable Funding factor is applied.

## RATING

On 13 September 2018 Moody's assigned first-time ratings to Luminor Bank AS (Estonia), including long- and short-term foreign- and local currency depositdeposit ratings of Baa1/P-2, outlook is stable. On 11 October 2018 Moody's confirmed a local currency long-term senior unsecured credit rating of Baa2 to Luminor Bank AS (Estonia).

The ratings assigned to Luminor Bank AS (Estonia) reflect the forward-looking assessment of the group's operations as a whole (Luminor), which, by January 2, 2019, is  expected to legally consolidate Luminor Estonia, Luminor Bank AS (Latvia) and Luminor Bank AB (Lithuania). At that time, the Latvian and Lithuania banks will become branches of the Estonian entity. Expected majority ownership change was also taken into account.

## LIQUIDITY

Luminor's structural liquidity risk is conservative and well-balanced and appropriately adopted to the current economic and regulatory environment. The short-term liquidity risk is measured using the Liquidity Coverage Ratio (LCR), calculated according to the EBA Delegated Act. LCR was 189% as at 31 December 2018 (31 December 2017: 157%).

The liquidity buffer, consisting of highly liquid assets in accordance with the Delegated Act, amounted 3,226 million EUR as at 31 December 2018 (31 December 2017: 2,662 million EUR). Due to low interest rate levels, which do not support holding Luminor's liquidity buffer in debt securities, only 167,6 million EUR was invested in bonds and other interest-bearing securities and 3,115 million EUR was held in the central bank as at 31 December 2018.

## CAPITAL

Capitalization of Luminor is sufficient to ensure the financial stability of the Group and satisfy the capital needed to deliver the business strategy. Total Capital Ratio of Luminor is 18.0% as at 31 December 2018 (31 December 2017: 17.8%), which it comfortably above the internal target of 17.0% and the applicable regulatory requirements.

The Total Capital Ratio is fully covered by Common Equity Tier 1 (CET1) capital. Own funds of Luminor are 1,661 million EUR as at 31 December 2018 (31 December 2017: 1,687 EUR). For calculating Credit and Market risk Luminor is using the Standardized method in the Capital Adequacy calculations. Operational risk is calculated using theBasic Indicator Approach method.

As at 31 December 2018 the Leverage Ratio, calculated according to Basel Committee on Banking Supervision requirements, was 10.4% (31 December 2017: 10.5%). Leverage ratio is calculated as bank's total Tier 1 own funds divided by its total risk exposure measure (including risk position on assets and off the balance sheet liabilities).

Additional information is provided on the Luminor Group web site regarding own funds and own funds requirements in accordance with among others regulation (EU) No 575/2013.

## PRIORITIES FOR 2019

Luminor´s core business is to serve entrepreneurial people in the Baltics, with primary focus on local companies as well as financially active people with an entrepreneurial mind-set.

After Luminor establishment the new strategic goals were set by Luminor management board in the beginning of 2018. One of the biggest goals of Luminor has been to complete the activities associated with the merger and build a single well-functioning organisation.

Luminor is focused on a customer experience excellence on the basis of data and knowledge, strong local presence with large-scale advantages, operational excellence and strong, performance driven, culture that is rooted in our core values – curiosity, collaboration and focus. Luminor will measure its performance through return on equity, underlying cost to income ratio, CET1 ratio and annual credit risk cost.

This starting point impacts many of our strategic choices and short to medium-term activities, but we are determined to execute on our key strategic priorities:

- Excel in customer experience, including new product offerings and improved customer service
- Launch of new digital channels. Today Luminor is a traditional bank with digital products, services and channels. Luminor aims to be a fully digital bank with modern technological platforms
- Ensure robust compliance / AML
- Consolidating information technology systems and operational independence (carve out from parent banks and customer migration into one platform per country)
- Improve capital efficiency and balance sheet risk management
- Quality of talent and leadership
- Improve cost-position to strengthen operational resilience

| PROPOSED DISTRIBUTION OF PROFITS | |
|---|---|
| The following funds are at the disposal of the Annual General Meeting (EUR): | |
| Other non-restricted reserves | 1 635 434 664 |
| Profit (loss) for the year | (1 283 931) |
| **Total** | **1 634 150 733** |
| The Board of Directors and Chief Executive Officer propose that the earnings be distributed as follows (EUR): | |
| To be carried forward | 1 634 150 733 |
| **Total** | **1 634 150 733** |

# CONSOLIDATED INCOME STATEMENT

| KEUR | Note | 2018 | 16 08 2016 – 31 12 2017 |
|---|---|---|---|
| Interest income calculated using the effective interest method | | 238 945 | 60 042 |
| Other similar income | | 60 421 | 14 431 |
| Interest and similar expenses | | (39 633) | (10 007) |
| **Net interest income** | G8 | **259 733** | **64 466** |
| Commission income | | 109 578 | 28 141 |
| Commission expenses | | (25 817) | (6 713) |
| **Net commission income** | G9 | **83 761** | **21 428** |
| Gain or losses on financial assets and liabilities designated at fair value through profit/loss, net | | (659) | (21) |
| Gain or losses on financial assets and liabilities held for trading, net | | 15 323 | 1 589 |
| Gain or losses on exchange rate differences | | 14 191 | 16 927 |
| Dividend income | | 89 | 11 |
| Other operating income | | 5 473 | 1 282 |
| Other operating expenses | G10 | (16 509) | (13 363) |
| **Total operating income** | | **361 402** | **92 319** |
| General administration expenses | G11 | (216 372) | (64 419) |
| Depreciation and amortization | G12 | (8 760) | (2 134) |
| Share of profit from an associate | G14 | 860 | 964 |
| Net impairment (losses)/ reversal on loans to customers | G15 | 6 313 | (13 833) |
| Net impairment (losses)/ reversal on other assets, change in fair value of investment property and provisions | G13, G15 | (4 327) | (5 660) |
| **Operating profit** | | **139 116** | **7 237** |
| Tax on profit for the year | G16 | (14 167) | (12 907) |
| **Profit (loss) for the year** | | **124 949** | **(5 670)** |

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | 2018 | 16 08 2016 – 31 12 2017 |
|---|---|---|
| **Profit (loss) for the year** | **124 949** | **(5 670)** |
| | | |
| **Items that will be reclassified to the income statement** | | |
| Changes in the fair value of assets at fair value through other comprehensive income | (4) | 1 680 |
| **Total items that will be reclassified to the income statement** | **(4)** | **1 680** |

| | | |
|---|---|---|
| **Items that will not be reclassified to the income statement** | | |
| Changes in the fair value of assets at fair value through other comprehensive income | 1 515 | - |
| Changes of deferred tax asset through other comprehensive income | 85 | - |
| **Total Items that will not be reclassified to the income statement** | **1 600** | **-** |
| **Changes in comprehensive income after tax** | **1 596** | **1 680** |
| **Comprehensive income after tax** | **126 545** | **(3 990)** |

(all amounts are in EUR thousand, if not otherwise stated)

# CONSOLIDATED BALANCE SHEET

| | Note | 31 12 2018 | 31 12 2017 |
|---|---|---|---|
| **Assets** | | | |
| Cash and balances with central banks | G17 | 3 293 090 | 2 620 838 |
| Loans to credit institutions | G18 | 186 197 | 409 506 |
| Loans to the public | G19 | 11 472 138 | 11 680 897 |
| Bonds and other interest-bearing securities | G21 | 141 673 | 164 202 |
| Equity instruments | G22 | 7 607 | 5 830 |
| Investments in managed pension funds | | 4 356 | 4 526 |
| Investments in associates | G23 | 6 256 | 6 110 |
| Derivative instruments | G24 | 45 697 | 27 753 |
| Intangible assets | G25 | 7 414 | 9 257 |
| Property, plant and equipment | G26 | 16 383 | 40 482 |
| Investment properties | G27 | 23 970 | 51 283 |
| Current tax assets | G16 | 886 | 90 |
| Deferred tax assets | G16 | 908 | 1 350 |
| Other assets | G28 | 76 096 | 67 937 |
| Non-current assets and disposal groups held for sale | G29 | 25 347 | 3 966 |
| **Total assets** | | **15 308 018** | **15 094 027** |
| **Liabilities** | | | |
| Due to credit institutions | G30 | 3 939 396 | 4 761 243 |
| Deposits and borrowing from the public | G31 | 9 069 885 | 8 429 796 |
| Debt securities issued | G32 | 349 333 | 65 007 |
| Derivative instruments | G24 | 42 457 | 33 173 |
| Current income tax liabilities | G16 | 6 873 | 3 288 |
| Provisions | G33 | 5 914 | 2 146 |
| Other liabilities | G34 | 57 964 | 53 035 |
| Accrued expences and deferred income | G35 | 36 142 | 32 097 |
| **Total liabilities** | | **13 507 964** | **13 379 785** |
| **Equity** | | | |
| Share capital | | 10 000 | 10 000 |
| Share premium reserve | | 1 645 099 | 1 645 099 |
| Reserves | G36 | 3 510 | 1 914 |
| Retained earnings | | 141 445 | 57 229 |
| **Total equity** | | **1 800 054** | **1 714 242** |
| **Total liabilities and equity** | | **15 308 018** | **15 094 027** |

(all amounts are in EUR thousand, if not otherwise stated)

# CONSOLIDATED CHANGES IN SHAREHOLDERS' EQUITY

| | Share capital | Share premium reserve | Other reserves | Retained earnings | Total equity |
|---|---|---|---|---|---|
| **Equity carried forward August 16, 2016** | **-** | **-** | **-** | **-** | **-** |
| Profit (loss) for the period | - | - | - | (5 670) | (5 670) |
| Other comprehensive income for the period | - | - | 1 680 | - | 1 680 |
| **Total comprehensive income for the period** | **-** | **-** | **1 680** | **(5 670)** | **(3 990)** |
| | | | | | |
| **Transactions with the owners:** | | | | | |
| Share capital | 6 | - | - | - | 6 |
| Shareholder contribution | 9 994 | 10 000 | - | - | 19 994 |
| New capital share issue | - | 1 635 099 | - | - | 1 635 099 |
| Other increase/decrease in equity | - | - | 234 | 62 899 | 63 133 |
| **Total** | **10 000** | **1 645 099** | **234** | **62 899** | **1 718 232** |
| | | | | | |
| **Equity carried forward December 31, 2017** | **10 000** | **1 645 099** | **1 914** | **57 229** | **1 714 242** |
| Changes on initial application of IFRS 9 | - | - | - | (40 733) | (40 733) |
| **Restated balance at 1 January, 2018** | **10 000** | **1 645 099** | **1 914** | **16 496** | **1 673 509** |
| | | | | | |
| Profit (loss) for the year | - | - | - | 124 949 | 124 949 |
| Other comprehensive income | - | - | 1 596 | - | 1 596 |
| **Total comprehensive income for the year** | **-** | **-** | **1 596** | **124 949** | **126 545** |
| | | | | | |
| **Transactions with the owners:** | | | | | |
| Share capital | - | - | - | - | - |
| Shareholder contribution | - | - | - | - | - |
| New capital share issue | - | - | - | - | - |
| Other increases/decreases in equity | - | - | - | - | - |
| **Total** | **-** | **-** | **-** | **-** | **-** |
| | | | | | |
| **Equity carried forward December 31, 2018** | **10 000** | **1 645 099** | **3 510** | **141 445** | **1 800 054** |

(all amounts are in EUR thousand, if not otherwise stated)

# CONSOLIDATED CASH FLOW STATEMENT

| Indirect method | 2018 | 16 08 2016 – 31 12 2017 |
|---|---|---|
| **Operating activities** | | |
| Operating profit | 139 116 | 7 237 |
| Adjustment for non-cash items in profit/loss: | | |
| *-Net impairment (losses)/ reversal on loans to customers* | (6 313) | 13 833 |
| *-Net impairment (losses)/ reversal on other assets, change in fair value of investment property and provisions* | 4 327 | 5 210 |
| *-Dividend received* | (949) | - |
| *-Unrealised changes in value* | (14 191) | - |
| *-Depreciation, amortisation and impairment* | 8 760 | 2 134 |
| *-Accrued interest income and expenses, net derivative loss (gain)* | 1 133 | - |
| Income tax paid | (14 167) | 771 |
| **Cash flow before from current operations before changes in working capital** | **117 716** | **29 185** |
| | | |
| **Cash flow from changes in working capital** | | |
| Increase (-) / decrease (+) of lending to the public | 168 027 | (11 680 897) |
| Increase (-) / decrease (+) of other assets | 198 165 | (589 096) |
| Increase (-) / decrease (+) of deposits and borrowing from the public | (181 758) | 13 191 039 |
| Increase (-) / decrease (+) of liabilities | 12 742 | 78 232 |
| **Cash flow form current operations** | **197 176** | **999 278** |
| | | |
| **Investing activities** | | |
| Acquisitions of property and equipment | (4 983) | (91 765) |
| Acquisitions of intangible assets | (3 955) | (9 257) |
| Acquisition of investment property | (204) | - |
| Disposal of property and equipment | 1 424 | - |
| Disposals of investment propety | 23 059 | - |
| Dividend received | 949 | - |
| Other cash receipts related to investing activities | 20 776 | - |
| Investments in securities | - | (174 558) |
| **Cash flow from investing activities** | **37 066** | **(275 580)** |
| | | |
| **Financing activities** | | |
| Capital increase | - | 1 709 905 |
| Debt securities issued | 284 326 | 65 007 |
| Investments in associates | - | (6 110) |
| **Cash flow from financing activities** | **284 326** | **1 768 802** |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | |
|---|---|---|---|
| Exchange rate differences in cash and cash equivalents | | 14 191 | (7 094) |
| | | | |
| **Cash flow for the period** | | **650 475** | **2 514 591** |
| Cash and cash equivalents, January 1 | | 2 514 591 | - |
| **Cash and cash equivalents, 31 December** | | **3 165 066** | **2 514 591** |
| | | | |
| **Cash and cash equivalents include:** | **G17** | **3 165 066** | **2 514 591** |
| Cash and balances in Central Banks | | 3 165 066 | 2 514 591 |

# PARENT COMPANY'S INCOME STATEMENT AND STATEMENT OF OTHER COMPREHENSIVE INCOME

| | Note | 2018 | 16 08 2016 – 31 12 2017 |
|---|---|---|---|
| Net revenue | P2 | 3 595 | 1 328 |
| **Total operating income** | | **3 595** | **1 328** |
| | | | |
| Other external expenses | | (2 546) | (10 292) |
| Personnel expenses | P4 | (2 313) | (679) |
| **Total operating expenses** | P3 | **(4 859)** | **(10 971)** |
| **Operating profit** | | **(1 264)** | **(9 643)** |
| | | | |
| **Result from financial assets:** | | | |
| Other operating expenses | | (20) | ( 21) |
| **Profit (loss) from financial assets** | | **(20)** | **(21)** |
| | | | |
| **Profit (loss) after financial assets** | | **(1 284)** | **(9 664)** |
| | | | |
| Tax on profit for the year | P5 | - | - |
| **Profit (loss) for the year / Comprehensive income after tax** | | **(1 284)** | **(9 664)** |

(all amounts are in EUR thousand, if not otherwise stated)

# PARENT COMPANY'S BALANCE SHEET

| | Note | 31 12 2018 | 31 12 2017 |
|---|---|---|---|
| **Assets** | | | |
| **Fixed assets** | | | |
| **Financial fixed assets** | | | |
| Shares in Group companies | P6 | 1 645 093 | 1 645 093 |
| **Current assets** | | | |
| Other receivables | P7 | 6 | 636 |
| Prepaid expenses and accrued income | P8 | 85 | 300 |
| Cash and cash equivalents | | 851 | 854 |
| **Current assets, total** | | **942** | **1 790** |
| **Total assets** | | **1 646 035** | **1 646 883** |
| | | | |
| **Equity** | | | |
| **Restricted equity** | | | |
| Share capital | | 10 000 | 10 000 |
| **Non-restricted equity** | | | |
| Share premium reserve | | 1 645 099 | 1 645 099 |
| Retained earnings | | (9 664) | - |
| Profit (loss) for the year | | (1 284) | (9 664) |
| **Equity, total** | | **1 644 151** | **1 645 435** |
| | | | |
| **Liabilities** | | | |
| **Current liabilities** | | | |
| Liabilities to Group companies | | 16 | 2 |
| Other liabilities | P9 | 996 | 456 |
| Accrued expenses and deferred income | P10 | 872 | 990 |
| **Total liabilities** | | **1 884** | **1 448** |
| | | | |
| **Total equity and liabilities** | | **1 646 035** | **1 646 883** |

(all amounts are in EUR thousand, if not otherwise stated)

# PARENT COMPANY'S CHANGES IN SHAREHOLDERS' EQUITY

| | Share capital | Other non-restricted reserves | Retained earnings | Total equity |
|---|---|---|---|---|
| **Equity carried forward August 16, 2016** | **-** | **-** | **-** | **-** |
| Profit (loss) for the period | - | - | (9 664) | (9 664) |
| **Total comprehensive income for the period** | **-** | **-** | **(9 664)** | **(9 664)** |
| | | | | |
| **Transactions with the owners:** | | | | |
| Share capital | 6 | - | - | 6 |
| Shareholder contribution | 9 994 | 10 000 | - | 19 994 |
| New capital share issue | - | 1 635 099 | - | 1 635 099 |
| **Total** | **10 000** | **1 645 099** | **-** | **1 655 099** |
| | | | | |
| **Equity carried forward December 31, 2017** | **10 000** | **1 645 099** | **(9 664)** | **1 645 435** |
| | | | | |
| **Equity carried forward January 1, 2018** | **10 000** | **1 645 099** | **(9 664)** | **1 645 435** |
| Distribution of profits | - | - | - | - |
| Profit (loss) for the year | - | - | (1 284) | (1 284) |
| Other comprehensive income for the year | - | - | - | - |
| **Total comprehensive income for the year** | **-** | **-** | **(1 284)** | **(1 284)** |
| | | | | |
| **Transactions with the owners:** | | | | |
| Share capital | - | - | - | - |
| Shareholder contribution | - | - | - | - |
| New capital share issue | - | - | - | - |
| **Total** | **-** | **-** | **-** | **-** |
| | | | | |
| **Equity carried forward December 31, 2018** | **10 000** | **1 645 099** | **(10 948)** | **1 644 151** |

As at 31 December 2018 and as at 31 December 2017, the authorized capital of the Parent company is EUR 10 000, which is divided into 200000000 ordinary registered shares, which have been fully paid, with EUR 0,05 par value each.

(all amounts are in EUR thousand, if not otherwise stated)

# PARENT COMPANY'S CASH FLOW STATEMENT

| Indirect method | Note | 2018 | 16 08 2016 – 31 12 2017 |
|---|---|---|---|
| **Operations activities** | | | |
| Operating profit | | (1 264) | (9 643) |
| Unrealized part of financial items, net | | (20) | - |
| Interest received | | - | (21) |
| **Cash flow before from current operations before changes in working capital** | | **(1 284)** | **(9 664)** |
| | | | |
| **Cash flow from changes in working capital** | | | |
| Decrease (+) / increase (-) of other receivables | | 844 | (936) |
| Increase (+) / decrease (-) of liabilities | | 437 | 1 448 |
| **Cash flow form current operations** | | **(3)** | **(9 152)** |
| | | | |
| **Investing activities** | | | |
| Investments of subsidiaries | | - | (808 463) |
| **Cash flow from investing activities** | | **-** | **(808 463)** |
| | | | |
| **Financing activities** | | | |
| Sharecapital | | - | 6 |
| Shareholders Contribution | | - | 10 000 |
| New share issue | | - | 808 463 |
| **Cash flow from financing activities** | | **-** | **818 469** |
| | | | |
| **Cash flow for the year** | | **(3)** | **854** |
| **Cash and cash equivalents at year-end** | | **851** | **854** |
| | | | |
| **Cash and cash equivalents refers to the company's bank accounts** | | **851** | **854** |

# NOTES TO FINANCIAL STATEMENTS

## ACCOUNTING PRINCIPLES

The consolidated accounts for Luminor Group AB (Parent Company) for the financial year ending 31 December 2018 have been approved by the Board of Directors for publication on 21 March 2019 and will be presented for adoption by the Annual General Meeting on 27 March 2019. Neither the Group's shareholders nor others have the power to amend the financial statements after issue.

The registered office of the Parent Company Luminor Group is c/o Nordea Bank AB, smålandsgatan 17, 105 71 Stockholm.

### G1: BASIS FOR COMPILATION OF ACCOUNTS

#### Statement of compliance with applied regulations

The consolidated financial statements are compiled in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU.. The consolidated accounts have been compiled in accordance with the Swedish Annual Accounts Act for Credit Institutions and Securities Companies (ÅRKL 1995:1559) as Luminor Group AB is regarded as a financial holding company, meaning that the Group also has to apply this law's provisions on compilation of consolidated accounts. The consolidated accounts have also been compiled in accordance with the Swedish Financial Supervisory Authority's regulations and general recommendations regarding annual accounts for credit institutions and security companies (FFFS 2008:25), including all applicable amended regulations, the Swedish Financial Reporting Board's recommendation RFR 1 Supplementary accounting rules for the Group and the Recommendation of the Swedish Financial Reporting Board. The Parent Company's annual report is prepared in accordance with the Swedish Annual Accounts Act (1995:1554) and with application of the Swedish Financial Reporting Boards RFR 2 Accounting for legal entities. This means that IFRS valuation and information rules are applied with the exceptions and supplements specified in the section concerning the Parent Company's accounting principles.

The financial statements are prepared on a historical cost basis, as modified by the initial recognition of financial instruments based on fair value, and by the revaluation of investment properties and financial instruments categorized at fair value through profit or loss ("FVTPL") and at fair value through other comprehensive income ("FVOCI").

**Prior year figures were adjusted where needed in order to make them comparable to current year presentation:**

- Cash and balances with Central banks (Note G17 for the year ending 31 December 2017) are reported in the balance sheet and presented in three separate lines Cash, Balances in Central banks, Term deposit (Note G17 Cash and balances with central banks). Mandatory reserve requirement is presented in separate „of which" line in Balances in Central banks.
- Loans to public (Note G19 for the financial statements for the year ending 31 December 2017) is extended to meet disclosure requirements after IFSR9 implementation.
- Other assets (Note G27 for the financial statements for the year ending 31 December 2017) and Prepaid expenses and accrued income (Note G28 for the financial statements for the year ending 31 December 2017) were combined in the balance sheet and presented in Other assets (Note G28) for the financial statements for the year ending 31 December 2018.
- Other assets are reported in the balance sheet (for the year ending 31 December 2017) and split into two separate lines Other assets and Non-current assets and disposal groups held for sale and presented as Other assets (Note G28) and Non-current assets and disposal groups held for sale (Note G29)
- Equity instruments (Note G21 for the financial statements for the year ending 31 December 2017) are reported in two separate

lines in the balance sheet and presented as Equity instruments (Note G21) and Investment in managed pension funds for the financial statements for the year ending 31 December 2018.

- Interest-bearing securities eligible as collateral with Central banks and Bonds and other interest-bearing securities (Note G20 for the year ending 31 December 2017) are combined in one line in the balance sheet and presented as Bonds and other interest-bearing securities (G21). In addition debt securities (34 357 thousand EUR) measured at amortised cost reported in the balance sheet under bonds (for the year ending 31 December 2017) are reclassified to loans to pulic.
- Interest income (Note G8 for the year ending 31 December 2017) are reported in two separate lines in the income statement and presented as Interest income calculated using the effective interest method and Other similar income (Note G8) for the year ending 31 December 2018.
- Impairment of financial assets (Note G15 Credit losses for the year ending 31 December 2017) are reported in two separate lines in the income statement and presented as Impairment of assets (Note G15) and Provisions (Note G13) for the year ending 31 December 2018.
- General administrative expenses (Note G11 for the financial statements for the year ending 31 December 2017) are disclosed in more detailed by adding new financial line items related to adminstrative expenses (Note G11 for the year ending 31 December 2018).
- Mandatory reserves are transfered from Reserves line and presented in Retained earnings line in the balance sheet and in the consolidated changes in shareholders' equity statement for the year ending 31 December 2018 and the year ending 31 December 2017.

The company's functional currency and reporting currency is EUR and, unless otherwise stated, all amounts are reported in thousands of Euro (KEUR).

### Basis for consolidation

The consolidated accounts include the Parent Company and its subsidiaries as of 31 December each year. The financial reports of the Parent Company and subsidiaries included in the consolidated accounts relate to the same period and have been compiled in accordance with the accounting principles applicable to the Group.

All balances within the Group, income, expenses, profits or losses arising in transactions between companies covered by the consolidated accounts are eliminated in their entirety. A subsidiary is included in the consolidated accounts from the time of acquisition, which is the date on which the Parent Company takes on controlling influence and is included in the consolidated accounts until the date on which the controlling interest ceases.

Controlling influence exists when the Parent Company directly, or indirectly through subsidiaries, holds over half of the voting rights in a company.

## G2: ADOPTION OF NEW AND/OR CHANGED IFRS AND INTERNATIONAL FINANCIAL REPORTING INTERPRETATIONS COMMITTEE (IFRIC) INTERPRETATIONS

The accounting policies adopted are consistent with those of the previous financial year except for the following amended IFRSs which have been adopted by the Group as of 1 January 2018:

## IFRS 9: Financial Instruments

**Key features of the new standard are:**

- Financial assets are required to be classified into three measurement categories: those to be measured subsequently at amortised cost, those to be measured subsequently at fair value through other comprehensive income (FVOCI) and those to be measured subsequently at fair value through profit or loss (FVPL).
- Classification for debt instruments is driven by the entity's business model for managing the financial assets and whether the contractual cash flows represent solely payments of principal and interest (SPPI). If a debt instrument is held to collect, it may be carried at amortised cost if it also meets the SPPI requirement. Debt instruments that meet the SPPI requirement that are held in a portfolio where an entity both holds to collect assets' cash flows and sells assets may be classified as FVOCI. Financial assets that do not contain cash flows that are SPPI must be measured at FVPL (for example, derivatives). Embedded derivatives are no longer separated from financial assets but will be included in assessing the SPPI condition.
- Investments in equity instruments are always measured at fair value. However, management can make an irrevocable election to present changes in fair value in other comprehensive income, provided the instrument is not held for trading. If the equity instrument is held for trading, changes in fair value are presented in profit or loss.·
- Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The key change is that an entity will be required to present the effects of changes in own credit risk of financial liabilities designated at fair value through profit or loss in other comprehensive income.
- IFRS 9 introduces a new model for the recognition of impairment losses – the expected credit losses (ECL) model. There is a 'three stage' approach which is based on the change in credit quality of financial assets since initial recognition. In practice, the new rules mean that entities will have to record an immediate loss equal to the 12-month ECL on initial recognition of financial assets that are not credit impaired (or lifetime ECL for trade receivables). Where there has been a significant increase in credit risk, impairment is measured using lifetime ECL rather than 12-month ECL. The model includes operational simplifications for lease and trade receivables.
- Hedge accounting requirements were amended to align accounting more closely with risk management. The standard provides entities with an accounting policy choice between applying the hedge accounting requirements of IFRS 9 and continuing to apply IAS 39 to all hedges because the standard currently does not address accounting for macro hedging.

The Group has adopted IFRS 9 as issued by the IASB in July 2014 with a date of adoption of 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements. The Group did not early-adopt IFRS 9 in previous periods. As permitted by the transitional provisions of IFRS 9, the Group elected not to restate comparative figures. Any adjustment to the carrying amounts of financial assets and liabilities at the date of transition were recognised in the opening retained earnings of the current period. The adoption of IFRS 9 has resulted in the changes in accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets.

## Impact of the adoption of IFRS 9

Set out below are disclosures relating to the impact of the adoption of IFRS 9 on the Group.

**Classification and measurement of financial instruments**

The measurement category and the carrying amount of financial assets and liabilities in accordance with IAS 39 and IFRS 9 at January 2018 are compared as follows:

(all amounts are in EUR thousand, if not otherwise stated)

| Financial assets | Original measurement category under IAS 39 | New measurement category under IFRS 9 | IAS 39 carrying amount 31 Dec 2017 | New carrying amount under IFRS9 1 Jan 2018 |
|---|---|---|---|---|
| Cash and balances with central banks | Loans and receivables | Amortised cost | 2 620 838 | 2 620 838 |
| Loans to credit institutions | Loans and receivables | Amortised cost | 409 506 | 409 462 |
| Bonds and other interest bearing securities | Fair value through profit or loss | Fair value through profit or loss/ Fair value through other comprehensive income | 164 202 | 164 202 |
| Derivative financial instruments | Fair value through profit or loss | Fair value through profit or loss | 27 753 | 27 753 |
| Investments in managed pension funds | Financial assets at FVTPL | Financial assets at FVTPL | 4 526 | 4 526 |
| Equity instruments | Available for sale/ Financial assets at FVTPL | Fair value through other comprehensive income | 5 830 | 5 830 |
| Loans to public | Loans and receivables/Investmets held to maturity | Amortised cost | 34 357 | 34 357 |
| Loans to public | Loans and receivables | Amortised cost | 11 646 540 | 11 609 884 |

Debt securities held for liquidity purposes were designated to FVTPL (under fair value option) because of accounting mismatch. The Group and Bank buy derivatives (interest rate swaps) to economicaly hedge the risk of debt securities fair value. Derivatives are in trading portfolio with the fair value changes through profit or loss, so to avoid or significantly reduce accounting mismatch, debt securities are designated at fair value using the fair value option (FVO).

There were no changes for classification and measurement of financial liabilities.

**Reconciliation of statement of financial position balances from IAS 39 to IFRS 9**

The following table reconcile the carrying amounts of financial assets, from their previous measurement category in accordance with IAS 39 to their new measurement categories upon transition to IFRS 9 on 1 January 2018:

| Financial assets | IAS 39 carrying amount 31 Dec 2017 | Reclassif-cations | Remea-surements | IFRS 9 carrying amount 1 Jan 2018 |
|---|---|---|---|---|
| **Amortised cost** | | | | |
| **Cash and balances with central banks** | | | | |
| Opening balance under IAS 39 and closing balance under IFRS 9 | 2 620 838 | - | - | 2 620 838 |
| | | | | |
| **Loans to credit institutions** | | | | |
| Opening balance under IAS 39 | 409 506 | - | - | - |
| Remeasurement (ECL allowances) | - | - | (44) | - |
| Closing balance under IFRS 9 | - | - | - | 409 462 |
| | | | | |
| **Loans to public** | | | | |
| Opening balance under IAS 39 | 11 646 540 | - | - | - |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | | |
|---|---|---|---|---|
| Remeasurement (ECL allowances) | - | - | (36 656)* | - |
| Closing balance under IFRS 9 | - | - | - | 11 609 884 |
| **Financial assets measured at amortised cost – total** | **14 676 884** | **-** | **(36 700)** | **14 640 184** |
| **Fair value through profit or loss** | | | | |
| **Bonds and other interest bearing securities** | | | | |
| Opening balance under IAS 39 and closing balance under IFRS 9 | 164 202 | (1 415) | - | 162 787 |
| **Investments in managed pension funds** | | | | |
| Closing balance under IAS 39 and opening balance under IFRS 9 | 4 526 | - | - | 4 526 |
| **Equity instruments** | | | | |
| Closing balance under IAS 39 and opening balance under IFRS 9 | 18 | (18) | | - |
| **Derivative financial instruments** | | | | |
| Opening balance under IAS 39 and closing balance under IFRS 9 | 27 753 | - | - | 27 753 |
| **Financial assets at fair value through profit or loss – total** | **196 499** | **(1 433)** | **-** | **195 066** |
| **Fair value through other comprehensive income** | | | | |
| **Equity instruments** | | | | |
| Opening balance under IAS 39 and closing balance under IFRS 9 | 5 812 | 18 | - | 5 830 |
| **Debt securities** | | | | |
| Opening balance under IAS 39 and closing balance under IFRS 9 | - | 1 415 | - | 1 415 |
| **Assets at fair value through other comprehensive income - total** | **5 812** | **1 433** | **-** | **7 245** |

** The change in amount 6 069 thousand euros compared to 2018 6 month interim report is related to clarification in the management estimates.

### Reconciliation of impairment allowance balance from IAS 39 to IFRS 9

The following table reconciles the prior period's closing impairment allowance measured in accordance with the IAS 39 incurred loss model to the new impairment allowance measured in accordance with the IFRS 9 expected loss model at 1 January 2018:

(all amounts are in EUR thousand, if not otherwise stated)

| Financial assets | Loss allowance under IAS 39/Provision under IAS 37 | Reclassifi-cations | Remeasure-ments | Credit loss allowance under IFRS 9 |
|---|---|---|---|---|
| **Amortised cost** | | | | |
| Cash and balances with central banks | - | - | - | - |
| Loans to credit institutions | - | - | (44) | (44) |
| Loans to public | (306 345) | - | 87 | (306 258) |
| **Total** | **(306 345)** | **-** | **43** | **(306 302)** |

**Reconciliation of changes on initial application of IFRS 9**

The following table includes summary information on changes on initial application of IFRS 9 reported in statement of changes in equity:

| **Remeasurements to loans, of which:** | **(36 700)** |
|---|---|
| Credit loss allowances | 43 |
| Reported under loan gross amount for originated credit impaired balances | (36 743) |
| **Provisions (Note 33)** | **(4 033)** |
| **Total impact on equity** | **(40 733)** |

### IFRS 15: Revenue from Contracts with Customers

The new standard introduces the core principle that revenue must be recognised when the goods or services are transferred to the customer, at the transaction price. Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements. When the consideration varies for any reason, minimum amounts must be recognised if they are not at significant risk of reversal. Costs incurred to secure contracts with customers have to be capitalised and amortised over the period when the benefits of the contract are consumed. Management has assessed that this standard does not have any material impact on its financial statements.

### IFRS 15: Revenue from Contracts with Customers (Clarifications)

The amendments do not change the underlying principles of the standard but clarify how those principles should be applied. The amendments clarify how to identify a performance obligation (the promise to transfer a good or a service to a customer) in a contract; how to determine whether a company is a principal (the provider of a good or service) or an agent (responsible for arranging for the good or service to be provided); and how to determine whether the revenue from granting a licence should be recognised at a point in time or over time. In addition to the clarifications, the amendments include two additional reliefs to reduce cost and complexity for a company when it first applies the new standard. Management has assessed that this standard does not have any material impact on its financial statements.

Other new or revised standards or interpretations that became effective for the first time for the financial year beginning on 1st of January 2018 did not have material impact to the Group.

## G3: STANDARDS ISSUED BUT NOT YET EFFECTIVE

Certain new or revised standards and interpretations have been issued that are mandatory for the Group's annual periods beginning on or after 1 January 2019 and which the Group has not early adopted.

**IFRS 16 "Leases" (issued on 13 January 2016 and effective for annual periods beginning on or after 1 January 2019).** The new standard sets out the principles for the recognition, measurement, presentation and disclosure of leases. All leases result in the lessee obtaining the right to use an asset at the start of the lease and, if lease payments are made over time, also obtaining financing. Accordingly, IFRS 16 eliminates the classification of leases as either operating leases or finance leases as is required by IAS 17 and, instead, introduces a single lessee accounting model. Lessees will be required to recognise: (a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value; and (b) depreciation of lease assets separately from interest on lease liabilities in the income statement. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The Group decided that it will apply the standard using the modified retrospective method. The Group decided to recognise the right-of-use assets at the date of initial application, measuring them at their carrying amount as if the standard had been applied since the commencement date, but discounted using the incremental borrowing rate at the date of initial application. The Group recognized the right-of-use asset in the amount of 30,7 million Euro, lease liability in the amount of 33,2 million Euro and the impact to the equity as of 1st January 2019 amounted to 2,5 million Euro, decreasing its balance

**IFRIC 23, Uncertainty over Income Tax Treatments (issued on 7 June 2017 and effective for annual periods beginning on or after 1 January 2019).** IAS 12 specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. The interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. An entity should determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments based on which approach better predicts the resolution of the uncertainty. An entity should assume that a taxation authority will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations. If an entity concludes it is not probable that the taxation authority will accept an uncertain tax treatment, the effect of uncertainty will be reflected in determining the related taxable profit or loss, tax bases, unused tax losses, unused tax credits or tax rates, by using either the most likely amount or the expected value, depending on which method the entity expects to better predict the resolution of the uncertainty. An entity will reflect the effect of a change in facts and circumstances or of new information that affects the judgments or estimates required by the interpretation as a change in accounting estimate. Examples of changes in facts and circumstances or new information that can result in the reassessment of a judgment or estimate include, but are not limited to, examinations or actions by a taxation authority, changes in rules established by a taxation authority or the expiry of a taxation authority's right to examine or re-examine a tax treatment. The absence of agreement or disagreement by a taxation authority with a tax treatment, in isolation, is unlikely to constitute a change in facts and circumstances or new information that affects the judgments and estimates required by the Interpretation. Management has not yet evaluated the impact of this standard.

**Prepayment Features with Negative Compensation - Amendments to IFRS 9 (effective for annual periods beginning on or after 1 January 2019).** The amendments enable measurement at amortised cost of certain loans and debt securities that can be prepaid at an amount below amortised cost, for example at fair value or at an amount that includes a reasonable compensation payable to the borrower equal to present value of an effect of increase in market interest rate over the remaining life of the instrument. In addition, the text added to the standard's basis for conclusion reconfirms existing guidance in IFRS 9 that modifications or exchanges of certain financial liabilities measured at amortised cost that do not result in the derecognition will result in an gain or loss in profit or loss. Reporting entities will thus in most cases not be able to revise effective interest rate for the remaining life of the loan in order to avoid an impact on profit or loss upon a loan modification. Management has not yet evaluated the impact of this standard.

There are no other new or revised standards or interpretations that are not yet effective that would be expected to have a material impact on the Group".

## G4: USE OF JUDGEMENTS AND ESTIMATES IN THE PREPARATION OF FINANCIAL STATEMENTS

The preparation of financial statements in conformity with the International Financial Reporting Standards require the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of current events and actions, actual results ultimately may differ from those estimates.

### Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values. For fair value of financial assets and liabilities refer to Note G 37.

### Fair value of investment properties

Investment properties are stated at fair value, which for the major part of properties has been determined according to valuations performed by accredited independent valuers and/or internal valuation specialists of the Group. The valuation model for the Group's investment properties was formed based on market comparable and income approaches. For fair value of investment properties refer to Note G 26.

### Deferred tax asset

Deferred tax asset is recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax asset that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies. For carrying amounts see Note 9.

### Investment in subsidiaries

The Bank assesses whether an impairment loss for the subsidiaries should be recorded in the income statement at least once a year. In determining whether an impairment loss should be recorded in the income statement, the Group makes judgments as there is any observable data indicating that there is a measurable changes in the estimated future cash flows, business growth and risk cost of subsidiaries.

Future events may occur which will cause the assumptions used in arriving at the estimates to change. The effect of any changes in estimates will be recorded in the financial statements, when determinable.

## G5: SIGNIFICANT ACCOUNTING JUDGMENTS

### Accounting for merger with Nordea

During the Merger with Nordea an assessment was done on the accounting principle to be used for the transaction.

**Control according to IFRS 10**

An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. (IFRS 10.6). Thus, an investor controls an investee if and only if the investor has all the following:

- power over the investee;
- exposure, or rights, to variable returns from its involvement with the investee; and
- the ability to use its power over the investee to affect the amount of the investor's returns. (IFRS 10.7)

**Joint control according to IFRS 11**

The formation of Luminor was a cooperation between DNB and Nordea with the intention for joint decisions and control of the Luminor operations. Shareholders have equal voting rights each and all decisions of relevant activities are taken by the Board of Directors where shareholders appoint two members each and jointly appoint an independent chairman. There are no other factors that indicate that one of the investors has the power to exercise control over the investee as defined in IFRS 10. To account for transaction as a joint venture, management of the Bank had assessed that the agreed decision rules and processes meet the criteria of IFRS 11 as a joint arrangement:

- The parties are bound by a contractual arrangement.
- The contractual arrangement gives two or more of those parties joint control of the arrangement. (IFRS 11.5)

Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. (IFRS 11.7)

It was concluded that both parties (DNB and Nordea) control the arrangement collectively. Also the conclusion was made that joint control exists because the decisions about the relevant activities require the unanimous consent of the parties that collectively control the arrangement.

In the formation of a joint arrangement, when no acquirer can be identified the guidance in IFRS 3 Business Combinations cannot be used as IFRS 3.2(a) specifically scopes out "the accounting for the formation of a joint arrangement in the financial statements of the joint arrangement itself" from this standard. Therefore the Bank selected in its accounting policy for how to account for this transaction by using the general guidance in IAS 8.10-12 - it was decided to use the carrying values. For more information on the accounting policy please refer to section Combination of entities under common control and usage of the pooling of interest method below.

**Alignment of Accounting Policies between DNB and Nordea**

The accounting policies of the two businesses merged were reviewed and no major differences were identified in the accounting principles applied.

### Intangible assets licensing agreements

The management of the Group has concluded that intangible asset licensing agreements where the Group is a licensee and the rights received under the licensing agreement are non-exclusive are out of scope of *IAS 17 Leases*. In addition, the management considers that non-exclusive rights received under such licensing agreements do not give a control of underlying intangible assets. Therefore, no intangible assets should be recognized in the Group's financial statements in accordance with *IAS 38 Intangible Assets*. Finally, the management considers that such licensing agreements should not be recognized as an intangible asset as it represents an executory contract as defined in *IAS 37 Provisions, Contingent Liabilities and Contingent Assets* that are not recognized, unless are onerous. Fees paid according such licensing agreements are recognized as expenses when incurred.

### Onerous contract

The Group has a long term agreement re IT services provided by DNB Invest Denmark AS. According to this agreement the Group compensates to the service provider for the development and usage of IT systems. As a consequence of the merger, the Management has assessed that those systems will be ceased to use in 4 years time and will be replaced by new systems then. Based on that, the assessment of the IT contract becoming onerous (the Group has an obligation to pay for the amounts relating to year 5 and onwards, although no benefit will be realised from this payment) was done and the provision of EUR 43 million was recognised in Group's financial statements. The provision was assessed based on the amounts that are related to year 5th and onwards.

In addition to that the payment schedule of the IT agreement was changed by agreeing to pre-pay the amount payable for year 5 and onwards (according to the original schedule) in 2017. After the payment was done the respective prepayment was netted with the liabilities accounted for the onerous contract as no services are to be received in the future for the prepayment made.

### Impairment of financial assets

IFRS 9 fundamentally changed the credit loss recognition methodology. The standard replaced IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. The Bank is required to recognize an allowance for expected losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination, in which case, the allowance is based on the probability of default over the life of the asset. Loss allowances based on lifetime expected credit losses are calculated also for purchased or originated credit-impaired assets (POCI) regardless of the changes in credit risk during the lifetime of an instrument. The Bank has established a policy to perform an assessment at the end of each reporting period of whether credit risk has increased significantly since initial recognition by considering the change in the risk of default occurring over the remaining life of the financial instrument.

The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Bank's internal credit grading model, which assigns PDs to the individual grades
- The Bank's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis and the qualitative assessment
- The segmentation of financial assets when their ECL is assessed on a collective basis
- Development of ECL models, including the various formulas and the choice of inputs
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs

- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

The assets to test for impairment are divided into three groups depending on the stage of credit deterioration. Stage 1 includes assets where there has been no significant increase in credit risk or which are classified as low risk (rating categorised as "Investment grade" or higher), stage 2 includes assets where there has been a significant increase in credit risk and stage 3 includes defaulted assets. Significant assets in stage 3 are tested for impairment on an individual basis, while for insignificant assets a collective assessment is performed. In stage 1, the allowances equal the 12 month expected credit loss. In stage 2 and 3, the allowances equal the lifetime expected credit losses.

One important driver for size of allowances under IFRS 9 is the trigger for transferring an asset from Stage 1 to Stage 2. Luminor uses a mix of absolute and relative changes (0.6 p.p. and 2.5 times) in 12 month point-in-time Probability of Default (PD) to determine whether there has been a significant increase in credit risk. In addition, customers with forbearance measures, included in watch list and contracts with payments more than thirty days past due are also transferred to Stage 2.

## G6: ACCOUNTING PRINCIPLES APPLIED

### Consolidation

**The subsidiaries are all investees over which the Bank has:**

- Power over the investee (i.e., existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee;
- The ability to use its power over the investee to affect its returns.

The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Bank controls another entity. The subsidiaries are fully consolidated from the date on which control is transferred to the Bank. They are de-consolidated from the date that control ceases. For more details on investments into subsidiaries refer to Note 20.

The accounting policies of the subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Bank. Inter-company transactions, balances and unrealised gains and losses on transactions between group companies are eliminated.

### Combination of entities under common control and usage of the pooling of interest method

A combination of entities under common control is a transaction when the controlling parties before and after a business combination are the same and the control is not transitory. IFRS 3, 'Business combinations' is not applied to business combinations between entities under common control, therefore such business combinations are accounted for using the pooling of interest method of accounting.

According to the pooling of interest method the assets and liabilities of the combining entities are reflected at their carrying amounts. No adjustments are made to reflect fair values, or recognize any new assets or liabilities, at the date of the combination that would otherwise be done under the acquisition method. No 'new' goodwill is recognized as a result of the combination. The only goodwill that is recognized is any existing goodwill relating to either of the combining entities. Any difference between the consideration paid/transferred or investment cost and the equity 'acquired' is reflected within equity.

## Investment in associates

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but does not have a control over those policies.

The Group's investment into associate is accounted for using the equity method and initially recognised at cost. The carrying amount of the investment is adjusted to recognise changes in the Group's share of net assets of the asssociate since the acquisition date. The statement of profit or loss reflects the Group's share of the results of operations of the associate. The financial statements of the associate are prepared for the same reporting period as the Group.

Once a year the Group determines whether there is objective evidence that the investment in the associate is impaired. If there is such evidence the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and then recognises the loss as share of profit of an associate in the statement of profit or loss.

For more details on investments in an associate refer to Note G 22.

## Foreign currency translation

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in EUR, which is the Bank's and subsidiaries' functional and presentation currency.

All monetary assets and liabilities denominated in foreign currencies are translated into EUR at the official rate of the Bank of Lithuania prevailing at the reporting period end. Gains and losses arising from this translation are included in the income statement for the period. Non-monetary items carried at cost are translated using the exchange rate at the date of the transaction, whilst assets carried at fair value are translated at the exchange rate when the fair value was determined.

Transactions denominated in foreign currency are recorded at the rate ruling on the date of the transaction. Exchange differences arising from the settlement of transactions denominated in foreign currency are charged to the income statement at the time of settlement using the exchange rate ruling at that date.

## Recognition of income and expenses

### Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' and 'interest expense' in the income statement using the effective interest rate method. The effective interest rate method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. Loan origination fees for loans and other credit related fees are deferred (together with any incremental costs) and accounted for as an adjustment to the effective interest rate calculation for each issued loan separately.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

**Commission income and expense**

Fees and commissions are recognised over time on a straight line basis as the services are rendered, when the customer simultaneously receives and consumes the benefits provided by the Group's performance. Such income includes fees for account maintenance, account servicing fees, account subscription fees, portfolio and other asset management advisory and service fees, wealth management and financial planning services, or fees for servicing loans on behalf of third parties. Variable fees are recognised only to the extent that management determines that it is highly probable that a significant reversal will not occur.

**Other fee and commission income**

Other fee and commission is recognised at a point in time when the Group satisfies its performance obligation, usually upon execution of the underlying transaction. The amount of fee or commission received or receivable represents the transaction price for the services identified as distinct performance obligations. Such income includes fees for arranging a sale or purchase of foreign currencies on behalf of a customer, fees for processing payment transactions, fees for cash settlements, collection or cash disbursements, as well as, commissions.

## Dividend income

Dividends are recognised in the income statement when the entity's right to receive payments is established.

## Taxation

**Income taxes**

The Group's tax consists of current and deferred tax. Income tax is recognized in the income statement unless it relates to items recognized in other comprehensive income or directly in equity.

Current tax is that paid or received pertaining to the current year, calculated applying tax rates that have been established (or to all intents and purposes established) on the balance sheet date. Any adjustment of current tax attributable to previous periods also belongs here.

Deferred tax is calculated based on temporary differences between the reported tax bases of assets and liabilities. Temporary differences are not taken into account in consolidated goodwill, or for differences arising on the initial recognition of assets and liabilities that are not business combinations that, at the time of the transaction, affect neither accounting nor taxable profit. Nor are temporary differences taken into account that relate to participations in subsidiaries, associates and affiliates and that are not expected to be reversed in the foreseeable future. The valuation of deferred tax provided is based on how carrying amounts of assets or liabilities are expected to be realized or settled. Deferred tax is calculated by applying the tax rates and tax rules that have been set or essentially are set as of the balance sheet date.

Deferred tax assets for deductible temporary differences and loss carryforwards are recognized to the extent that it is probable that the amounts can be utilized against future taxable income.

The carrying amount for deferred tax assets is reviewed on each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available. The reduction is reversed to the extent it is deemed likely that sufficient taxable profits will later be available.

Current tax assets and current tax liabilities are offset when there is a legally enforceable right to offset. This entails items relating to taxes levied by the same taxation authority on either the same taxable entity or a different taxable entity, where there is an intention either to settle these tax items net or to reclaim the tax asset at the same time as the tax liability is settled. Deferred tax assets and deferred tax liabilities are generally offset to the extent that this is permitted for current tax assets and current tax liabilities.

***Income taxes in Sweden***

Taxable income is subject to corporate tax at a flat rate of 22%.

***Income taxes in Estonia***

According to the Income Tax Act, the annual profit earned by enterprises is not taxed in Estonia and thus there are no temporary differences between the tax bases and carrying values of assets and liabilities and no deferred tax assets or liabilities arise. Instead of taxing the net profit, the distribution of retained earnings is subject to taxation on the amount paid out as net dividends. The corporate income tax arising from the payment of dividends is accounted for as an expense in the period when dividends are declared, regardless of the actual payment date or the period for which the dividends are paid.

Starting from 1 April 2018, the quarterly accounting profits of credit institutions are subject to corporate income tax at the rate of 14%. The tax is payable by the 10th day of the third month of the following quarter. Once the profits are distributed, an additional income tax of up to 6% is further payable, which adds up to the total tax rate of up to 20%. The rate of the additional tax depends on the regularity of the dividend payments. If no dividends are paid, the advance tax payments are not refunded.

***Income taxes in Lithuania***

In accordance with the Lithuanian Law on Corporate Income Tax, the current income tax rate is 15 % on taxable income. Expenses related with taxation charges and included in these financial statements are based on calculations made by the management in accordance with the Lithuanian tax legislation.

Deferred income tax is provided using the balance sheet liability method on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for the financial reporting purposes.

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that a taxable profit will be available against which the losses can be utilised. Judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits.

Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the statement of financial position date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Tax losses can be carried forward for indefinite period. The losses from disposal of securities can only be used to offset the profit earned from sale of securities. The losses from disposal of securities can be carried forward for 5 consecutive years. Starting with 1 January 2014 tax losses carried forward can be used to reduce the taxable income.

Deferred tax related to fair value re-measurement of financial assets classified as at fair value through other comprehensive income which are charged or credited to other comprehensive income, is also credited or charged to other comprehensive income and subsequently recognised in the income statement together with the deferred gain or loss.

***Income taxes in Latvia***

Corporate income tax for the reporting period is included in the financial statements based on the management's calculations prepared in accordance with Latvian Republic tax legislation.

On July 28, 2017, a new Corporate Income Tax Law was adopted, which stipulates that from January 1, 2018, the corporate income tax is levied on profit that arose after 2017 if it is distributed or conditionally distributed profit arise. When the law came into force, there were no longer any reason for the existence of a deferred tax asset or liability and in 2017, and the Group eliminated previously recognized deferred tax asset from the balance sheet, including a reduction in that asset in the profit and loss account for the year 2017. Transitional provisions of the law provide that taxpayers will be able to utilise the unused tax losses accumulated by 31 December 2017 during next 5 taxation years for reducing the tax payable on distributed profits by no more than 50% each year, as well as to use provisions created by 31 December 2017 that resulted in the increase of taxable income during the respective tax periods, for reduction of taxable profits, in the amount of their reduction.

From taxation year 2018, corporate income tax will be calculated on the basis of distributed profit (20/80 of the net amount payable to shareholders). Corporate tax on distributed profit will be recognized when the shareholders of the Group make a decision about profit distribution.

The Group calculates and pays corporate income tax also for the conditionally distributed profit (20/80 of calculated taxable base), which includes taxable objects in accordance with the Corporate Income Tax law, such as the expenditure not related to economic activity, the doubtful debts of debtors and the loans to the related parties, if they meet criteria provided in the Corporate Income Tax law, as well other expenses exceeding statutory limits for deduction. Corporate income tax for the conditionally distributed profit is recognized in the profit or loss statement in the year for which it is assessed. Corporate income tax for the distributed profit and corporate income tax for the conditionally distributed profit is included in the profit and loss statement line item "Corporate income tax for the reporting year" and disclosed by the components in the notes to the financial statements.

**Other taxes**

Other taxes are included in other expenses in the income statement.

**Cash and balances with Central Banks**

For purposes of the cash flow statements cash and cash equivalents comprise cash balances, non-restricted balances due from the Central Banks, due from other credit institutions with original maturity less than 3 months and insignificant risk due to change in value. Cash and cash equivalents as specified above are defined in cash flow statement.

## Financial assets and liabilities

**Classification and measurement**

Financial instruments at FVTPL are initially recorded at fair value. All other financial instruments are initially recorded at fair value adjusted for transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets. After the initial recognition, an ECL allowance is recognised for financial assets measured at amortised cost.

Subsequent measurement of financial assets depends on the classification performed by the Group at initial recognition. At initial recognition, financial assets can be classified into one of the following categories:

- Financial assets measured at fair value through profit or loss,
- Financial assets measured at fair value through other comprehensive income (OCI),
- Financial assets measured at amortised cost.

Classification is performed based on both the Group's business model for managing financial assets and the characteristics of contractual cash flows of the financial assets. However, financial assets that meet the amortised cost or fair value through other comprehensive income measurement criteria, may be designated on initial recognition by the Group to fair value through profit or loss measurement option, provided that particular qualifying criteria for accounting mismatch are met. Additionally, the Group may make an irrevocable election at initial recognition for particular investments in equity instruments that would otherwise be measured at fair value through profit or loss to present subsequent changes in fair value in other comprehensive income.

**On initial recognition, financial liabilities are classified into one of the following categories:**

- Financial liabilities measured at amortised cost,
- Financial liabilities measured at fair value through profit or loss.

**Financial liability is classified as measured at fair value through profit or loss if:**

- It meets the definition of held for trading and
- It is designated upon initial recognition to fair value through profit or loss measurement option

All other financial liabilities are classified as measured at amortised cost.

**Financial assets and liabilities measured at fair value through profit or loss**

### Trading securities

Trading securities are securities which were acquired either for generating a profit from short-term fluctuations in price or dealer's margin, or are securities included in a portfolio in which a pattern of short-term profit taking exists. Trading securities are initially recognised at fair value, which is based on quoted bid prices. All related realised and unrealised gains and losses are included in net trading income or expenses. Dividends received are included in dividend income.

All purchases and sales of trading securities that require delivery within the time frame established by regulation or market convention ('regular way' purchases and sales) are recognised at settlement date, which is the date that an asset is delivered to or by the Group**.**

**Derivative financial instruments**

Derivative financial instruments including foreign exchange forwards, swaps, options (both written and purchased) and other derivative financial instruments are initially recognised in the statement of financial position at their fair value. Fair values are determined according to the model, based on market observable inputs. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Changes in the fair value of derivatives held for trading are included in net trading income.

Fair values of the derivative financial instruments are disclosed in Note G 23.

### Securities for liquidity management

Securities which were acquired for liquidity management purposes and are within held to collect and sell business model are initially recognised at fair value, which is based on quoted bid prices. All related realised and unrealised gains and losses are included in net gain (loss) on transactions with securities. Dividends received are included in dividend income

FVTPL option was ellected for those securities because it leads to significant reduction or elimination of accounting mismatch.

### Hedge Accounting

At the inception of a hedge relationship, the Group formally designates and documents the hedge relationship to which it wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge.

The documentation includes identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the Group will assess whether the hedging relationship meets the hedge effectiveness requirements (including the analysis of sources of hedge ineffectiveness and how the hedge ratio is determined). A hedging relationship qualifies for hedge accounting if it meets all of the following effectiveness requirements:

- There is ‘an economic relationship’ between the hedged item and the hedging instrument.
- The effect of credit risk does not ‘dominate the value changes’ that result from that economic relationship.
- The hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the Group actually hedges and the quantity of the hedging instrument that the Group actually uses to hedge that quantity of hedged item.

The Group applies the fair value hedge. Fair value hedges when hedging the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment.

The change in the fair value of a hedging instrument is recognised in the statement of profit or loss. The change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item and is also recognised in the statement of profit or loss.

For fair value hedges relating to items carried at amortised cost, any adjustment to carrying value is amortised through profit or loss over the remaining term of the hedge using the effective interest (EIR) method. The EIR amortisation may begin as soon as an adjustment exists and no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

If the hedged item is derecognised, the unamortised fair value is recognised immediately in profit or loss. When an unrecognised firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognised as an asset or liability with a corresponding gain or loss recognised in profit or loss.

## Financial assets measured at fair value through other comprehensive income

Financial assets at fair value through other comprehensive income include financial assets that are invested in equity shares and debt securities Those assets are intended to be held for an indefinite period of time and are initially recognised at fair value based on quoted bid prices or amounts derived from discounted cash flow models. Unrealised gains and losses arising from changes in the fair value of financial assets classified are recognised in other comprehensive income (OCI). When the financial asset is derecognised the cumulative gain or loss previously recognised in OCI is not reclasified to profit or loss.

Dividends receivable are included separately in dividend income when the right of the payment has been established.

All regular way purchases and sales of securities are recognised at settlement date, which is the date that an asset is delivered to or by the Group. All other purchases and sales are recognised as derivative forward transactions until settlement.

## Repurchase and reverse repurchase agreements

The securities sold under agreements to repurchase at a specified future date are not derecognised from the statement of financial position as the Bank retains substantially all the risks and rewards of ownership. The corresponding cash received is recognised in the consolidated statement of financial position as an asset with a corresponding obligation to return it, including accrued interest as a liability, reflecting the transaction’s economic substance as a loan to the Bank.

The securities purchased under agreements to resell at a specified future date are not recognised in the statement of financial position. Reverse repurchase agreements are classified as loans and receivables to other banks or customers, and are accounted for using the amortised cost method. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

## Financial assets and liabilities measured at amortised cost

**Loans**

Loans and advances are financial assets held for collection of contractual cash flows and those cash flows represent SPPI.

Loans are carried at amortised cost using the effective interest method.

Loans and advances are recognised at their settlement date, when cash is advanced to borrowers. From the date of signing a contractual agreement till the settlement date they are accounted for as off-balance sheet items.

**Loans, deposits and bonds issued**

All financial liabilities (loans, deposits, bonds issued) are recognised initially at fair value and, in the case of loans and borrowings, net of directly attributable transaction costs. After the initial recognition, the interest-bearing loans, deposits and bonds issued by the Group are recognised at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR method. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as net interest income in the statement of profit and loss.

### Impairment losses on loans, finance lease receivables and other financial assets

Losses on loan, finance lease receivables and other financial assets are assesed on a forward looking basis,. The Group measures ECL and recognises credit loss allowance at each reporting date. Impairment allowances are determined based on the forward-looking ECL models.

When a loan is uncollectible, it is written off against the related allowances for loan impairment. Such loans are written off after all necessary procedures have been completed and the amount of the loss has been determined.

### Renegotiated loans

The Group sometimes renegotiates or otherwise modifies the contractual terms of the financial assets. The Group assesses whether the modification of contractual cash flows is substantial considering, among other, the following factors: significant change in interest rate, change in the currency denomination, new collateral or credit enhancement that significantly affects the credit risk associated with the asset or a significant extension of a loan when the borrower is not in financial difficulties.

If the modified terms are substantially different, the rights to cash flows from the original asset expire and the Group derecognises the original financial asset and recognises a new asset at its fair value. The date of renegotiation is considered to be the date of initial recognition for subsequent impairment calculation purposes. The Group also assesses whether the new loan or debt instrument meets the SPPI criterion. Any difference between the carrying amount of the original asset derecognised and fair value of the new substantially modified asset is recognised in profit or loss, unless the substance of the difference is attributed to a capital transaction with owners.

In a situation where the renegotiation was driven by financial difficulties of the counterparty and inability to make the originally agreed payments, the Group compares the original and revised expected cash flows to assets whether the risks and rewards of the asset are substantially different as a result of the contractual modification. If the risks and rewards do not change, the modified asset is not substantially different from the original asset and the modification does not result in derecognition. The Group recalculates the gross carrying amount by discounting the modified contractual cash flows by the original effective interest rate (or credit-adjusted effective interest rate for POCI financial assets), and recognises a modification gain or loss in profit or loss.

### Derecognition of financial assets and liabilities

#### Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised where:

- The rights to receive cash flows from the asset have expired; or
- The Bank and the Group has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; and
- The Bank and the Group either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank and the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Bank and the Group's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank and the Group could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's and the Group's continuing involvement is the amount of the transferred asset that the Bank and the Group may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's and the Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

**Financial liabilities**

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the income statement.

**Intangible assets**

An intangible asset is recognised only when its cost can be measured reliably, it is controlled by the Group as a result of past events and it is probable that the expected future economic benefits that are attributable to it will flow to the Group. The Group controls an asset if the Group has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses (if any).

The useful lives of intangible assets are assessed to be either finite or indefinite.The Group had no intangible assets with indefinite useful life as of 31 December 2018 and 31 December 2017. Intangible assets with finite lives are amortised using the straight–line method over the useful economic life. Amortization normally occurs over 3 - 5 years. The amortisation period and the amortization method for an intangible asset with a finite useful life are reviewed at least at each financial year-end in order to reflect the pattern of consumption of such asset.

**Investment properties**

Investment properties are measured initially at cost, including transaction costs. The carrying amount includes the cost of replacing part of an existing investment property at the time that cost is incurred if the recognition criteria are met; and excludes the costs of day to day servicing of an investment property. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the reporting date. Gains or losses arising from changes in the fair values of investment properties are included in the income statement in the period in which they arise.

Investment properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. The difference between the net disposal proceeds and the carrying amount of the asset is recognised in the income statement in the period of derecognition.

Transfers are made to or from investment property only when there is a change in use. For a transfer from investment property to owner occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

**Property, plant and equipment**

Property, plant and equipment are held at historical cost less accumulated depreciation and any impairment in value. Depreciation is provided on a straight-line basis to write off proportionally the cost of each asset over its estimated useful life. Fixtures and fittings, computers and other hardware are normally written off after 3 -10 years.

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Gains and losses on disposals of property, plant and equipment are determined by reference to their carrying amount and are charged to the income statement. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each statement of financial position date.

Asset maintenance costs are charged to the income statement when they are incurred. Significant renewals of assets are capitalised and depreciated over the remaining useful life period of the improved asset.

**Non-current assets held for sale**

Non-current assets classified as held for sale are measured at the lower of their carrying amount and fair value less costs to sell. Non-current assets are classified as held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset is available for immediate sale in its present condition, management has committed to the sale and the sale is expected to be completed within one year from the date of classification.

Non-current assets classified as held for sale are not depreciated or amortised.

**Leases**

The determination of whether an arrangement is a lease or it contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

**Group is the lessee**

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. The total payments made under operating leases are charged to the income statement on a straight-line basis over the period of lease and included into other administrative expenses.

**Group is the lessor**

**Operating leases**

Assets leased out under operating leases are included in property, plant and equipment in the statement of financial position. They are depreciated over their expected useful lives on a basis consistent with similar owned assets. Rental income is recognised on a straight-line basis over the lease term.

**Finance leases**

A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred. When assets are held subject to a finance lease, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return. Initial direct costs are included in the initial measurement of the lease receivables.

**Employee benefits**

**Social security contributions**

The Group pays social security contributions to the state Social Security Fund (the Fund) on behalf of its employees based on the defined contribution plan in accordance with the local legal requirements. A defined contribution plan is a plan under which the Group pays fixed contributions into the Fund and will have no legal or constructive obligations to pay further contributions if the Fund does not hold sufficient assets to pay all employees benefits relating to employee service in the current and prior period. The social security contributions are recognised as an expense on an accrual basis and are included within staff costs. Social security contributions each year are allocated by the Fund for pension, health, sickness, maternity and unemployment payments.

**Termination benefits**

Termination benefits are payable when an employee’s employment is terminated on initiative of employer or the employment is terminated by mutual employee’s and employer’s agreement. The Group recognises termination benefits when it is demonstrably committed to either terminate the employment of current employees according to a detailed formal plan without possibility of withdrawal or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after statement of financial position date are discounted to present value. Termination benefits are included within staff costs in the income statement and within other liabilities in the statement of financial position.

**Provisions**

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. The expense relating to any provision is recognised in the income statement. If the effect of the time value of money is material, provisions are discounted using current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a borrowing cost.

**Onerous contracts provision**

Onerous contracts provision is recognised when the Group has a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it.

**Financial guarantees and credit-related commitments**

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was given. The fair value of the financial guarantee on the initial recognition does not include the gross receivable for future premiums not yet due. Subsequent to initial recognition, the bank's liabilities under such guarantees are measured at the higher of the initial measurement, less amortisation calculated to recognise in the income statement the fee income earned on a straight line basis over the life of the guarantee or the best estimate of the expenditure required to settle any financial obligation arising at the statement of financial position date. These estimates are determined based on forward looking ECL basis.. Any increase in the liability relating to guarantees is taken to the income statement under other operating expenses.

Documentary and commercial letters of credit represent written undertakings by the Bank and the Group on behalf of a customer authorising a third party to draw drafts on the Bank and the Group up to a stipulated amount under specific terms and conditions.

**Fair value of assets and liabilities**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of the principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible to by the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

When the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgement is used in establishing fair values.

The fair value of interest-bearing financial instruments is estimated based on discounted cash flows using the interest rates for items with similar terms and risk characteristics. In the case of inactive markets the establishment of valuation techniques for measuring the fair value is provided.

**Offsetting financial assets and financial liabilities**

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

**Off-balance sheet items**

Off-balance sheet derivative transactions are marked to market at the reporting date and any arising profit or loss is recognised in the income statement for the period and treated as an asset or liability in the statement of financial position respectively.

All liabilities that might give rise to statement of financial position exposures are accounted for as off-balance sheet liabilities. This allows the Bank and the Group to assess capital requirement and to allocate funds required to cover those obligations.

**Contingencies**

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. A contingent asset is not recognised in the financial statements but disclosed when an inflow of economic benefits is probable.

**Earnings per share**

Basic earnings per share amounts are calculated by dividing net result for the year attributable to ordinary equity holders of the parent by the weighted number of ordinary shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net result attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

**Subsequent events**

Post-year-end events that provide additional information at the statement of financial position date (adjusting events) are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes when material.

## G7: RISK MANAGEMENT

The aim of risk management activity at Luminor Group is to maintain a risk profile that delivers predictable income and loss volatility. While implementing a sound risk management policy the Group focuses not only on minimising the potential risk but also on improving pricing and achieving efficient capital allocation.

The risk management function of the Group is organised in such a way that ensures efficient risk management and fulfilment of the principles stipulated in the Risk Policy and Strategy.

**The risk management principles are the following:**

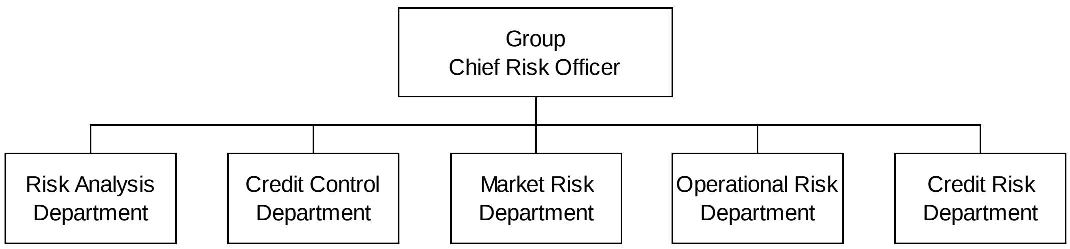
- Risk Accountability: every area in the Group is accountable for the risks arising from their activities.
- Risk Governance: risk needs to be considered as part of the governance around any and every business decision.
- Risk Identification, Assessment, Management and Reporting: all material exposures must be identified, assessed, managed and reported in a timely and accurate manner.
- Internal Control system: a comprehensive internal control system must be in place to ensure that risk management and controls are executed in accordance with the guiding principles, minimum standards, risk appetite, limits and mandates.

The Group maintains the Recovery Plan following the Bank Recovery and Resolution Directive adopted by the European Parliament. The plan serves as one of the risk management prevention tools and should ensure restoration of the Group's solvency following situations of severe stress without any involvement by or support from the authorities or tax payers.

The Group analyses, evaluates, accepts and manages the risks or combinations of risks it is exposed to. The most important types of risk the Group is exposed to are credit risk, market risk, liquidity risk, operational risk and other risk (business risk, reputational risk). Concentration risk is assessed as part of credit risk, other types of concentration were assessed to be less material for the Group. Compliance risk is treated as part of operational risk. Market risk includes foreign exchange risk and interest rate risk.

The risk management in the Group is organized in such a way that any possible conflicts of interest would be avoided. The function of all-type risk control is segregated from risk taking, i.e. from the front-office units.

**Risk division organisational structure:**




The control function for the major material risk – credit risk – is under the responsibility of the Credit Risk Department, Credit Control Department and Risk Analysis Department. The control over operational risk management within the Group and information security lies under the responsibility of Operational Risk Department. The functions of Market Risk Department embrace market risk and liquidity risk control. All organizational units within Risk division represent the second line of defense and report directly to the Group Chief Risk Officer (CRO). The Chief Credit Officer for each bank from the Credit Risk Department acts as local CRO, who is as well the member of the Management Board.

Risk management processes and effectiveness of internal control are assessed by the Internal Audit Department (third line of defense).

The internal control – as a system of organizational measures, actions and internal procedures – ensures the effective and efficient operations and prudent conduct of business, the compliance with laws and regulations, the adequate assessment and control of risk, as well as the reliability of financial and non-financial information and submission thereof in a timely manner. The Management Board is responsible for creation and maintenance of effective internal control system in the Group.

The Management Board approves the procedures having significant impact on risk management and risk mitigation measures associated with the risk management. In certain cases when it is not prohibited by legal or regulatory requirements responsibility for approval is delegated to the Chief Risk Officer.

Non-structural unit of each Luminor Bank in Estonia, Latvia, Lithuania – Risk Committee – advises the Management Board and the Supervisory Council on the overall actual and future risk appetite and strategy, on the optimal capital structure. Also it aims to optimize the Bank's asset and liability structure with regard to acceptable risk and return. The Risk Committee considers and makes proposals on the main risk-related processes. Risk reports covering analysis of all the risks are presented to the Risk Committee on a regular basis.

The Credit Committee is a decision making body regarding individual credit cases and contributes to development of a sound and uniform credit culture in the Group. The Credit Committee provides recommendations regarding important credit regulations and setting goals for the desired portfolio quality.

## 1: CREDIT RISK

Credit risk means the risk for the Group to incur losses due to the customers' failure to fulfil their financial obligations towards the Group. Credit exposures arise principally in lending activities and it is the most significant risk in the Group's business. The credit risk arises also from investment activities (e.g. debt securities) as well as from the off-balance sheet financial instruments, such as loan commitments, guarantees and letters of credit.

The key elements of credit risk management are the Group Credit Policy, Credit Strategy for business customers and Credit Strategy for private individuals. Practical aspects of the application of the principles set out in these documents' and decision-making processes are regulated by the Credit Manual for business customers and Credit Manual for private individuals.

The Group's principal objective for lending is that the loan portfolio should have a quality and a composition which ensure profitability in the short and long term. The target is that the loan portfolio should maintain the credit risk profile varying from low to moderate. The assessment of creditworthiness should be based on customer's ability to perform on its financial obligations. Cash flows from customers' activities dedicated for loan payments should be clearly understandable and sustainable.

Credit decisions are made by Credit Committees and by authorised individuals according to defined powers to act which are risk adjusted. The decision of the Credit Committee to grant a loan shall be unanimous. Powers to act for individuals are personal and based on the competence level. Four-eyes principle is followed. Final approval of credits above a certain level is done together with the independent credit officers. In cases of small credit card limits/consumer credits one pair of eyes may be replaced by rating.

The regular reports are designed to be provided to the Group's management bodies to follow the level and developments of the assumed credit risk.

## 1.1: Credit risk management

### (a) Loans to public, including finance lease receivables

The credit risk is managed by carrying out a thorough analysis of the customer before issuing credits and by monitoring thereof after credit disbursement.

Risk models are essential elements of the credit process and tools for management of the Group's credit risk. The Group measures credit risk by means of rating models yielding probability of default (PD) and risk grade as well as by loss given default (LGD) and exposure at default (EAD) parameters. These risk models are constantly improved based on the results of analysing the historical credit-risk-related data and tested for reliability (validated).

Rating models, which yield probability of default (PD) and risk grade, are used to estimate default risk of counterparty, to determine compliance of customers and exposures with the Credit Strategy, to determine correct decision-making level and to set requirements for the frequency of follow up within the regular monitoring process. The assessment is made by using the customer / product segment specific rating models, which are used for homogeneous groups of customers:

- large corporates,
- corporates,
- small and medium-sized enterprises (SMEs),
- microbusiness (e.g., small single ownership companies),
- real estate projects of legal entities,
- individual customers.

All credits granted to customers are classified by risk using these rating models every time a commitment is renewed or, unless otherwise decided, at least once a year.

Loans to private individuals are assessed based on application scorings when decision is made. After the loans are granted, they are monitored by periodical evaluation of the customer's status using the behavioural scorings.

In addition to credit decision making, the outputs of internal risk models are applied in credit pricing, loan portfolio quality monitoring and risk reporting as well as economic capital (risk-adjusted capital, hereinafter referred to as RAC) calculation. RAC is used for decision making with respect to strategic capital allocation, i.e. for determining the strategic segments in lending activity, as well as capital planning for the Group.

Whenever large business customers are provided with loans, in addition a risk-adjusted profitability for the Group is assessed at both an individual loan and customer level, i.e. a risk-adjusted return on risk-adjusted capital (RAROC) is measured. The same principles of RAC-based pricing as well as RAROC-based profitability assessment are also extended to the other segments of the loan portfolio through the standardized pricing tools or rules. The risk-based credit pricing tools for all customer / product segments are monitored regularly and updated, if needed.

In 2018 the considerable amount of efforts were continued to be aimed towards implementation of a uniform landscape of rating models and risk parameters (which is mainly based on the rating models and risk parameters developed internally by former DNB subsidiaries in the Baltics) in the Group after combination of operations of DNB and Nordea in the Baltics by 1st October 2017. As well, the Group focused on further improvement of its impairment quantification approach under IFRS 9, which heavily relies on outputs from internal risk models adjusted to fit IFRS 9 purposes.

(all amounts are in EUR thousand, if not otherwise stated)

In 2018 the Group reviewed and updated its internal approach towards allocation of RAC for individual loans and customers taking into account its regulatory capital requirements and internally targeted capitalisation levels. As a result, principles and tools for RAC-based pricing decisions were reviewed and amended too.

The Group considers building of competence of its employees as a prerequisite for creating a sound credit culture within the organization. Therefore it puts a special emphasis on internal training of its employees involved in credit activities on credit analysis, usage of rating models, understanding of risk parameters, which make an integral part of decision making, and risk-based pricing principles.

In 2018, high attention was dedicated to training of employees involved in credit activities on rating models and risk parameters, risk-based pricing principles, RAROC-based profitability measurement and relationship between them, risk data quality assurance issues as well as to ensure the common understanding of these issues through the whole Group. This was supported by review of the Group's internal documentation regulating credit risk management area (including as well newly prepared Rating Guidelines) with aim to provide more detailed guidance, what facilitates alignment of understanding of the employees from the different parts of organization in this transitional period following the combination of operations of DNB and Nordea in the Baltics.

The Group's internal rating scale for performing customers and mapping of external ratings are provided below:

<table>
<tr><th>Rating grade</th><th>PD range</th><th>Standard & Poor's / Fitch</th><th>Moody's</th><th>Investment / speculative grade</th><th>Risk level</th></tr>
<tr><td>1.a</td><td>0.01 – 0.02 %</td><td>AAA – A+</td><td>Aaa – Aa1</td><td rowspan="8">Investment grade</td><td rowspan="9">Low risk</td></tr>
<tr><td>1.b</td><td>0.02 – 0.04 %</td><td>AA – AA-</td><td>Aa2 – Aa3</td></tr>
<tr><td>1.c</td><td>0.04 – 0.06 %</td><td>A+</td><td>A1</td></tr>
<tr><td>1.d</td><td>0.06 – 0.08 %</td><td>A</td><td>A2</td></tr>
<tr><td>1.e</td><td>0.08 – 0.10 %</td><td>A-</td><td>A3</td></tr>
<tr><td>2.a</td><td>0.10 – 0.18 %</td><td>BBB+</td><td>Baa1</td></tr>
<tr><td>2.b</td><td>0.18 – 0.25 %</td><td>BBB</td><td>Baa2</td></tr>
<tr><td>3</td><td>0.25 – 0.50 %</td><td>BBB-</td><td>Baa3</td></tr>
<tr><td>4</td><td>0.50 – 0.75 %</td><td>BB+</td><td>Ba1</td><td rowspan="9">Speculative grade</td></tr>
<tr><td>5</td><td>0.75 – 1.25 %</td><td>BB</td><td>Ba2</td><td rowspan="3">Moderate risk</td></tr>
<tr><td>6</td><td>1.25 – 2.00 %</td><td></td><td></td></tr>
<tr><td>7</td><td>2.00 – 3.00 %</td><td>BB-</td><td>Ba3</td></tr>
<tr><td>8</td><td>3.00 – 5.00 %</td><td>B+</td><td>B1</td><td rowspan="6">High risk</td></tr>
<tr><td>9</td><td>5.00 – 8.00 %</td><td>B</td><td>B2</td></tr>
<tr><td>10.a</td><td rowspan="4">8.00 – 40.00 %</td><td>B-</td><td>B3</td></tr>
<tr><td>10.b</td><td>CCC+</td><td>Caa1</td></tr>
<tr><td>10.c</td><td>CCC and lower</td><td>Caa2 and lower</td></tr>
<tr><td>10.d</td><td></td><td></td></tr>
</table>

**(b) Due from banks and other credit institutions**

The counterparty risk of banks and financial institutions is managed by selecting high quality counterparties before establishing the limits and by monitoring thereof after. The Group's portfolio shall be dominated by investment risk grade counterparties or counterparties with high importance in countries with a speculative risk grade. Counterparties not rated by any of the major rating agencies are handled as exceptions.

In Luminor a separate dedicated Financial Institutions unit acts as a single core competence center and ensures holistic overview of the Group's exposure on counterparties and countries. The unit among other things is centrally responsible for:

- analysing the counterparties and countries, preparing the limit proposals and rating recommendations;
- maintaining high quality counterparty portfolio including review of bank and country limits on an annual basis;
- following-up and monitoring of the portfolio including any early warning indicators.

The risk grade and probability of default (PD) of banks and countries is based on the available risk classifications from rating agencies Moody's, Standard & Poor's and Fitch (see 1.1.a) paragraph).

All counterparties and countries with valid limits are risk classified. In case the external rating for a counterparty is not available a conservative expert judgment is a basis for the Group internal rating, which reflects the counterparty's credit strength, derived from the macroeconomic factors and counterparty's own solvency and liquidity factors, together with its qualitative non-financial adjustments.

All limits of counterparties and countries are reviewed at least once a year with the purpose to assess the counterparty's creditworthiness, review the risk grade as well as the available limits. Externally non-rated counterparties always have an individual assessment.

All externally rated counterparties and countries are monitored on a quarterly basis with the focus on the rating actions taken by external credit rating agencies. Externally non-rated banks are monitored with the emphasis on an evaluation of the ownership changes, financial standings and any other relevant information and signals that may affect the bank's credit standing. Early warning signal monitoring that could potentially indicate a material change in the credit risk of counterparties is an important part of a regular monitoring of the counterparties.

**(c) Debt securities**

Debt securities exposure of the Group at the end of year 2018 is 141,7 million euro compared to 164,2 million euro at the end of 2017.. The credit risk arising from them is considered as being immaterial. Most of these debt securities are issued by the governments of Lithuania and Latvia. The remaining part consists of international bonds guaranteed by France, Belgium and Luxembourg governments which are treated as level 1 assets in (Liquidity Coverage Ratio) LCR calculation, and a minor part of Lithuanian and Estonian corporate bonds. Total weighted duration of the portfolio at the end of year 2018 is about 1.4 years compared to 1.8 year at the end of 2017. Debt securities investments are performed in accordance with the limits set by the Luminor Management Board and Supervisory Council of Luminor banks. Limit utilization is monitored on daily basis.

### 1.2: Risk limit control and mitigation policies

**(a) Concentration risk**

The Group manages, limits and controls concentration of credit risk – in particular, to individual counterparties and groups of the associated counterparties as well as to economic sectors.

The Group's portfolio of the products bearing credit risk derived from lending to the groups of the connected borrowers and a single borrower is well diversified. Besides the legal lending limit according to Capital Requirements Regulation (<25% of eligible capital) Luminor has imposed the internal large exposures limit (<10% of eligible capital).

| Group | Eligible capital | Legal lending limit | Large exposure limit |
|---|---|---|---|
| mEUR | 1 661 | 415.2 | 166.1 |

Concentration risk of lending to the economic sectors is regarded as being material and is closely monitored and controlled. Complimentary to the regulatory requirements to limit the large exposures to a single borrower or the group of related borrowers, the Group implements limits to economic sectors, i.e. a possible concentration in certain economic sectors at the Group level is restricted by the internal percentage lending limits. The legal entities economic sectors concentration limits are disclosed in the table below. At the end of the year 2018, the loan portfolio of the Group was well diversified by economic sectors and none of the set limits was breached.

| Economic sector | Limit 31 December 2018 |
|---|---|
| Real estate | 30% |
| including for projects under development | 10% |
| Construction | 10% |
| Retail trade | 20% |
| Wholesale trade | 20% |
| Food processing | 20% |
| Timer & metal processing | 20% |
| Other manufacturing | 20% |
| Any other industry | 20% |

The geographical concentration risk is not considered as being material in the Group's business since the principle of focusing on domestic customers is followed.

The Group's activity regarding risk concentrations is defined in the Credit Strategy.

Some other specific risk control and mitigation measures are outlined further on.

**(b) Collateral**

Sustainable debt servicing capacity is the essential element in the lending process, giving less importance to the pledged collateral measure.

The Group mitigates credit risk through taking of collaterals for funds advanced. Types of collateral considered by the Group as the most acceptable for securing loans and advances are the following:

- Property rights over financial instruments (debt securities, equities, cash);
- Guarantees;
- Residential real estate mortgage;
- Commercial and other real estate mortgage;
- Business assets (equipment, inventory, transport vehicles).

When deciding on the type of collateral the maturity of the loans is taken into account. Long-term loans preferably should be covered by long-term property, mainly residential properties. More information on collaterals, value assessments of collaterals, periodical review of collateral values is provided in 1.5.b).

Long-term financing and lending to business customers are generally secured. Revolving facilities and consumer loans to private individuals are usually unsecured. Debt securities, treasury and other eligible bills are generally unsecured. In order to minimise the credit loss the Group may seek for additional collateral from the counterparty as the impairment indicators for certain individual loans and advances are noticed.

For finance lease receivables the lessor remains the owner of the leased object. Therefore, in case of customer default the lessor is able to gain control on the risk mitigation measures and realise them in a rather short period.

**(c) Derivative financial instruments**

Derivative financial instruments including foreign exchange contracts, interest rate swaps and options, commodity swaps are initially recognized and subsequently carried at their fair value are revalued at least monthly. Fair values are obtained from quoted market prices and discounted cash flows as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

Margining agreements are established with the clients. Credit lines are usually granted to manage credit risk of these financial instruments. Cash or securities are less frequent option to be used as a collateral. Derivatives are used to hedge market risk positions arising from ordinary banking operations and from derivative transactions with clients.

The Group's counterparty credit risk represents the potential cost to replace derivative contracts if counterparties fail to perform their obligation. The Group assess counterparties in order to control the level of credit risk taken. The counterparty credit risk is managed primarily through limitation of exposures to each counterparty, regular valuation of exposures and collateralization of exposures.

**(d) Credit-related commitments**

Other credit-related commitments assumed by the Group include guarantees, letters of documentary credit, commitments to grant a credit which expose the Group to the same credit risk as the loans do. The key aim of these instruments is to ensure that funds are available to a customer as required. The aforementioned commitments are collateralised either by the funds in the Bank's account, by material assets (real estate being the preference) or other collaterals such as third party guarantees. With respect to credit risk arising from commitments to extend credit, the Group is exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customer's ability to repay the loans already granted.

### 1.3: Impairment policies

Starting from 1st January 2018 the Group implemented and followed the requirements of IFRS 9 for loss allowance assessment for expected credit losses.

**(a) General ECL assessment principles**

With the adoption of IFRS 9 three stages model was introduced:

- Stage 1 – part of the portfolio for which no significant deterioration in credit quality has occurred since initial recognition (or the exposure is of low credit risk) and the financial instrument is not considered credit-impaired;

- Stage 2 – part of the portfolio for which significant deterioration in credit quality has occurred since initial recognition, evidenced by the SICR – significant increase in credit risk - indicator, and the financial instrument is not considered credit-impaired;
- Stage 3 – credit-impaired part of the portfolio. Luminor equates default and credit-impairment definitions so that all defaulted exposures are treated as credit-impaired and all credit-impaired exposures are treated as defaulted. This approach is based on the fact that the default definition used by Luminor covers all events indicated by IFRS 9 as possible evidence that financial instrument is credit-impaired and all of these events are considered by Luminor as having a detrimental impact on the estimated future cash flows from the instrument.

Additional category is POCI financial assets - financial assets that were purchased or originated as credit-impaired. POCI assets are subject to unchanging classification, i.e. financial asset once classified as POCI remains in this group until derecognized. The POCI classification is determined at financial instrument level.

**Luminor applies low credit risk exemption to the following classes of exposures:**

- central governments,
- central bank,
- regional governments,
- local authorities and
- institutions.

The counterparty must fulfil the condition of having credit rating indicating investment grade.

With the shift from IAS 39 to IFRS 9 approach incurred loss model was replaced by expected credit loss (ECL) model. For Stage 1 financial assets loss allowances equal to 12-month ECL while for Stage 2 and Stage 3 financial instruments lifetime ECL is calculated.

For Purchased or Originated Credit Impaired (POCI) financial assets ECL is estimated in the lifetime horizon till the maturity. The loss expected at initial recognition is referred to as Initial impairment. At subsequent periods only the cumulative changes in the lifetime expected credit losses, since initial recognition, are recognised in profit or loss.

**(b) Default definition**

Luminor identifies default when either or both of the following default indicators have taken place:

- 1. The customer is past due more than 90 days on any material obligation to the Luminor;
- 2. The customer is considered unlikely to pay its credit obligations to the Luminor.

For exposure to banks the default is recognized when payments are due more than 7 days.

For the purpose of unlikeliness to pay identification, elements taken as indications of unlikeliness to pay include the following:

- Distressed restructuring of credit obligation (forbearance triggering non-performing status in accordance with FINREP instruction requirements);
- Major financial problems of the customer (present or expected), i.e. significant financial difficulties;
- Recognition of specific credit risk adjustment resulting from a significant decline in credit quality of the exposure;
- Bankruptcy of the customer or similar protection;
- Disappearance of an active market for a financial asset because of financial difficulties of the customer;

- Sell of credit obligation at material credit-related economic loss;
- Purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses;
- Credit fraud;
- External rating indicating default.

The default is recognised on customer level.

Return to a non-defaulted status is possible not earlier than after 3 months when all default triggers cease to be met. During those 3 months of the probation period the timely payments by a customer should be ensured. The exemption from the general rule of probation is the distressed restructuring where at least 1 year needs to pass since the moment of extending restructuring measures and the moment when a customer is deemed to have an ability to comply with the post-restructuring conditions. This approach is consistent with FINREP instruction requirements for cure of forborne non-performing exposures.

**(c) Significant increase in credit risk**

Generally the financial asset is treated as facing significant increase in credit risk if at least one of the following SICR indicators is identified after initial recognition of the financial instrument and was not present as of its origination:

- Significant increase of 12-month PD – significant increase of point-in-time (PIT) forward-looking 12-month PD since initial recognition until reporting date (2.5 times and 0.6 p.p. jointly),
- Risk grade 9 or 10 – risk grade 9 or 10 as of reporting date,
- 30 days past due – more than 30 days past due as of reporting date,
- Forborne performing – forborne performing status as of reporting date (forbearance not triggering non-performing status) in accordance with FINREP instruction reporting requirements,
- Watch list – watch list status as of reporting date.

All of the SICR indicators are recognized at financial instrument level in order to track changes in credit risk since initial recognition date for particular financial instrument, even though some of them refer to the customer's characteristics.

Luminor does not apply probation period for backward stage transfer of Stage 2 assets.

**(d) 12-month and lifetime expected credit losses**

Collective assessment of impairment is performed for all financial instruments that are not defaulted as of the reporting date, i.e. are classified to either Stage 1 or Stage 2 or are non-defaulted POCI asset.

The expected loss is calculated as probability weighted average of losses expected in different macroeconomic scenarios. Expected loss in concrete macroeconomic scenario is calculated as the multiple of point-in-time probability of default (PIT PD), point-in-time loss given default (PIT LGD), exposure at default (EAD) and cumulative prepayment rate and is discounted using a discount rate:

- Macroeconomic scenario based PIT PD is probability that the performing exposure defaults during particular time period provided that it has survived until the beginning of this period. PIT PD approach is applicable for all financial instruments for which the internal rating models are available.
- Macroeconomic scenario based PIT LGD is the expected percentage share of an exposure that would be irretrievably lost if the default event occurs. For the evaluation of PIT LGD curves PD-dependent model is used, in which the LGD estimates are dependent on projected point-in-time PDs.
- EAD is the exposure at default parameter which represents total exposure under a specific facility upon default. For instalment

(all amounts are in EUR thousand, if not otherwise stated)

products (i.e. products with contractual repayment schedules), the EAD term structure is shaped by contractual amortization. For revolving products (e.g. credit lines, credit cards or overdrafts), limit utilization approach is used for the purpose of EAD term structure estimation. For standard off-balance exposures (guarantees and letters of credit) the credit conversion factors are determined to account for expected off-balance exposure withdrawals applicable for the default date.

- Cumulative prepayment rate describes the cumulative likelihood that the exposure would be fully prepaid (i.e. closed before its contractual maturity) in the periods up to the end of analyzed period. The application of cumulative prepayment rate is limited in scope to these portfolios for which the prepayments are not captured by the PD model.
- The rules for discount rate assignment depends on the type of financial instrument and availability of the contractual repayment schedule. For facilities for which contractual repayment schedules are available, the effective interest rate (EIR) or its approximation (i.e. nominal rate) is applied as a discount rate. In case of exposures without the contractual repayment schedules, which contain both the financial asset and off-balance sheet item (e.g. credit lines, credit cards), best possible proxy of the EIR is applied. In case of exposures without the contractual repayment schedules, representing the off-balance products (guarantees, letters of credit), contractual rate associated with the exposure is applied or, if it is not available, the relevant market rate.

PIT PD curves, PIT LGD curves and EAD curves are estimated for all months until the maturity date of the facility. If the facility is classified to Stage 1, expected losses are estimated over the period of up to 12 months. If the facility is classified to Stage 2 then the expected loss is estimated over the period up to maturity date of the facility.

Estimation of PD and LGD curves take into account forward looking macroeconomic information. Methodology of estimation of these risk parameters includes modelling of the relationship between risk parameters and macroeconomic variables. Forecasts of macroeconomic variables under different scenarios for 3 upcoming years together with scenario probabilities are prepared by Luminor macroeconomists. Three macroeconomic scenarios are considered: baseline/realistic, positive, and pessimistic scenario (with the highest probability weight for the baseline/realistic scenario). Macroeconomic scenarios that are prepared for the estimation of expected losses are consistent with scenarios which are used in credit risk stress testing process. Three macroeconomic variables - annual change in real GDP, unemployment rate and annual change of residential real estate price – are included in the modelling for the Private individuals segment and two of them – annual change in real GDP together with unemployment rate – are used for modelling in the case of the Legal entities segment. The following tables show the parameters that were used for macroeconomic modelling on the 31 December 2018 in each country. Starting from the fourth year it is assumed that risk parameters (PD and LGD) converge to their long term average levels.

**Estonia**

| Macroeconomic variables | Optimistic scenario | | | Baseline scenario (realistic) | | | Pessimistic scenario | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2019 | 2020 | 2021 | 2019 | 2020 | 2021 | 2019 | 2020 | 2021 |
| **Probability for scenario, %** | | **30%** | | | **60%** | | | **10%** | |
| Annual change in real GDP, % | 4.7 | 4.1 | 3.5 | 3.2 | 2.7 | 2.5 | -1.5 | -0.7 | 2.3 |
| Unemployment rate, % | 5.5 | 5.5 | 5.4 | 6.3 | 6.5 | 6.7 | 9.4 | 10.1 | 11.0 |
| Annual change of residential real estate price, %** | 8.7 | 7.0 | 6.0 | 5.5 | 4.3 | 3.0 | -11.0 | -5.0 | 0.0 |

(all amounts are in EUR thousand, if not otherwise stated)

**Latvia**

| Macroeconomic variables | Optimistic scenario | | | Baseline scenario (realistic) | | | Pessimistic scenario | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2019 | 2020 | 2021 | 2019 | 2020 | 2021 | 2019 | 2020 | 2021 |
| **Probability for scenario, %** | | **30%** | | | **60%** | | | **10%** | |
| Annual change in real GDP, % | 4.8 | 4.2 | 4.2 | 3.6 | 3.2 | 3.0 | -0.8 | -0.9 | 2.1 |
| Unemployment rate, % | 6.3 | 5.8 | 5.5 | 6.7 | 6.3 | 6.1 | 8.4 | 9.8 | 10.0 |
| Annual change of residential real estate price, % | 8.0 | 8.0 | 7.0 | 6.0 | 5.0 | 5.0 | -7.0 | -4.0 | 1.0 |

**Lithuania**

| Macroeconomic variables | Optimistic scenario | | | Baseline scenario (realistic) | | | Pessimistic scenario | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2019 | 2020 | 2021 | 2019 | 2020 | 2021 | 2019 | 2020 | 2021 |
| **Probability for scenario, %** | | **20%** | | | **70%** | | | **10%** | |
| Annual change in real GDP, % | 4.5 | 4.0 | 4.0 | 3.0 | 2.5 | 2.5 | -1.0 | -0.5 | 1.5 |
| Unemployment rate, % | 5.8 | 5.4 | 5.0 | 6.2 | 5.9 | 5.9 | 8.5 | 9.5 | 9.0 |
| Annual change of residential real estate price, % | 7.0 | 6.0 | 5.0 | 4.0 | 3.0 | 2.0 | -8.0 | 0.0 | 2.0 |

Regular follow up is ensured for all material exposures. Regularity and deepness of the assessment is based on the risk level and size of the exposure. The aim of the follow up is 1) to identify worsening of the situation and start early actions to improve Bank's position and 2) identify occurrence of *Unlikely to Pay* criteria. Credit-impaired large exposures that are above materiality thresholds and with loss event are reviewed every quarter or more frequently when individual circumstances require. Valuation is updated when there are significant changes in cash flows otherwise it is performed at least once a year.

For Stage 3 exposures (or defaulted POCI assets), which are classified as material, Luminor evaluates the impairment amount on individual basis (individual assessment) under discounted cash flows (DCF) method, where both future cash flows from borrower's operations and cash flows from collateral are taken into account. Two scenarios – base case and risk case – with certain probability weights are used. For exceptional cases usage of one scenario can be sufficient. The circumstances when only one scenario might be acceptable could be the deep workout case or the case when total exposure of defaulted borrower falls below the materiality threshold.

For Stage 3 exposures (or defaulted POCI assets), which are classified as immaterial, Luminor evaluates the impairment amount on collective basis (collective assessment). Impairment is calculated applying the pool rate for unsecured part. Different pool rates are applied for three homogeneous pools distinguished by Luminor:

- mortgage loans and private credits to private individuals,
- consumer loans and other loans to private individuals (including leasing),
- SMEs (all financial instruments to legal entities).

**(e) Sensitivity analysis**

**Estonia:**

The following table shows the impact on the 31 December 2018 ECL allowance of changing the PD thresholds for SICR. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognized.

**ECL impact of (TEUR)**

| Actual absolute threshold applied | Actual relative threshold applied | Change in absolute threshold | Change in relative threshold | Lower thresholds | Higher thresholds |
|---|---|---|---|---|---|
| 2.5 | 0.006 | -/+ 20% | -/+ 12bps | 149 | (144) |

The following table shows the impact on the 31 December 2018 ECL allowance of changing the pessimistic and optimistic scenario probabilities. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognized.

**ECL impact of (TEUR)**

| Pessimistic scenario probability applied | Optimistic scenario probability applied | Change in pessimistic scenario probability | Change in relative threshold | Lower pessimistic scenario probability | Higher pessimistic scenario probability |
|---|---|---|---|---|---|
| 0.1 | 0.2 | -/+ 200bps | +/- 200bps | (20) | 15 |

**Latvia:**

The following table shows the impact on the 31 December 2018 ECL allowance of changing the PD thresholds for SICR. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognized.

**ECL impact of (TEUR)**

| Actual absolute threshold applied | Actual relative threshold applied | Change in absolute threshold | Change in relative threshold | Lower thresholds | Higher thresholds |
|---|---|---|---|---|---|
| 2.5 | 0.006 | -/+ 20% | -/+ 12bps | 329 | (154) |

The following table shows the impact on the 31 December 2018 ECL allowance of changing the pessimistic and optimistic scenario probabilities. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognized.

**ECL impact of (TEUR)**

| Pessimistic scenario probability applied | Optimistic scenario probability applied | Change in pessimistic scenario probability | Change in relative threshold | Lower pessimistic scenario probability | Higher pessimistic scenario probability |
|---|---|---|---|---|---|
| 0.1 | 0.2 | -/+ 200bps | +/- 200bps | (37) | 35 |

**Lithuania:**

The following table shows the impact on the 31 December 2018 ECL allowance of changing the PD thresholds for SICR. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognized.

**ECL impact of (TEUR)**

| Actual absolute threshold applied | Actual relative threshold applied | Change in absolute threshold | Change in relative threshold | Lower thresholds | Higher thresholds |
|---|---|---|---|---|---|
| 2.5 | 0.006 | -/+ 20% | -/+ 12bps | 797 | (349) |

The following table shows the impact on the 31 December 2018 ECL allowance of changing the pessimistic and optimistic scenario probabilities. Increases in ECL (positive amounts) represent higher impairment allowances that would be recognized.

**ECL impact of (TEUR)**

| Pessimistic scenario probability applied | Optimistic scenario probability applied | Change in pessimistic scenario probability | Change in relative threshold | Lower pessimistic scenario probability | Higher pessimistic scenario probability |
|---|---|---|---|---|---|
| 0.1 | 0.2 | -/+ 200bps | +/- 200bps | (10) | 7 |

**(f) Risk assessment on modified financial assets**

As a rule, each time the modification of a financial instrument takes place due to financial problems of the debtor the new rating/scoring should be obtained and new PD assigned, the loan should be marked as forborne if the FINREP instruction reporting definition is met. Therefore, as a result of modification the loan would be classified as Stage 2 if forborne performing status is assigned (or Stage 3 if forborne non-performing status is assigned) and/or the loan would be classified as Stage 2 if the change in PD is considered significant. In case of substantial modification resulting in derecognition of the asset and the origination of the new one, the newly recognized asset is classified as either POCI asset (if credit-impaired) or Stage 1 (if not credit-impaired).

**(g) Write-off policy**

The Group writes off financial assets, in whole or in part, which are considered as being non collectible. Generally the indication that financial assets are non collectible is the situation when all collaterals (except guarantees of private individuals) are sold. However the write-off fact does not limit the Group's recovery measures towards particular customer. The outstanding contractual amount on financial assets that were written off during the year ended 31 December 2018 and are still subject to enforcement activity was EUR 43,766 thousand.

### 1.4: Maximum exposure to credit risk before collateral held or other credit enhancements

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Credit risk exposures relating to on-balance sheet assets subject to impairment are as follows: | | |
| **Balances with central banks** | **3 293 090** | **2 620 838** |
| **Due from banks and other credit institutions** | **186 197** | **409 506** |
| **Loans and advances to customers, including finance lease receivables:** | **11 472 138** | **11 680 897** |
| **Loans and advances to financial institutions** | **57 786** | **32 590** |
| **Loans to individuals (retail):** | **5 871 502** | **5 906 183** |
| - Mortgage loans | 4 988 077 | 5 072 649 |
| - Consumer and card loans | 143 807 | 141 545 |
| - Other (reverse repurchase agreements, other loans backed by securities, other) | 190 468 | 190 296 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | |
|---|---|---|
| - Leasing | 549 150 | 501 693 |
| **Loans to business customers:** | **5 542 850** | **5 742 214** |
| - Loans | 3 712 645 | 3 747 215 |
| - Factoring | 336 488 | 400 782 |
| - Leasing | 1 493 717 | 1 594 217 |
| **Credit risk exposures relating to off –balance sheet items subject to impairment are as follows:** | **1 984 264** | **2 243 794** |
| - Financial guarantees | 406 147 | 469 578 |
| - Loan commitments and other credit related liabilities | 1 578 117 | 1 774 216 |
| | **16 935 690** | **16 955 034** |
| Credit risk exposures relating to on-balance sheet assets not subject to impairment are as follows | | |
| **Financial assets held for trading:** | **1 006** | **2 325** |
| - Debt securities | 1 006 | 2 325 |
| **Securities designated at fair value through profit or loss** | **139 402** | **161 876** |
| - Debt securities | 139 402 | 161 876 |
| | **-** | **-** |
| **Derivative financial instruments** | **45 697** | **27 753** |
| **Securities at fair value OCI/ Securities available for sale** | **1 265** | **-** |
| - Debt securities | 1 265 | - |
| | **17 123 060** | **17 146 988** |

The table above represents credit risk exposure at 31 December 2018 and 2017, without taking into account any credit risk mitigation techniques. On-balance sheet assets are reported above based on the net carrying amount as they appear in the statement of financial position.

Loans and advances to banks and customers account for 68 % of the total maximum exposure of the Group (2017: 71 %).

The Group pays special attention on determining proper and acceptable risk criteria that are applicable in decision making on granting of loans as well as on monitoring process seeking to sustain optimal credit risk level.

Due to the improved risk profile of the existing customers, inflow of new performing customers into the portfolio as well as due to write-offs, positive trends in the quality of the portfolio of loans and advances to customers are noticeable.

### 1.5: Loans to public, including finance lease receivables

Loans and advances (including finance lease receivables) at 31 December 2017 are summarized as follows:

| | Group |
|---|---|
| Neither past due nor impaired | 10 826 758 |
| Past due but not impaired | 506 180 |
| Impaired | 654 304 |
| Gross | 11 987 242 |
| Less: allowance for impairment | (306 345) |
| Net | 11 680 897 |

(all amounts are in EUR thousand, if not otherwise stated)

Past due but not impaired loans and finance lease receivables mean loans and advances and finance lease receivables that are past due but have no allowances for impairment and default status at the same time.

Impaired loans and finance lease receivables mean defaulted loans and advances and finance lease receivables that have non-zero impairment.

In 2017, the Group's total impairment allowance for loans and leases was EUR 306,345 thousand and it accounted for 2.6 % of the Group's respective portfolio. The Group's impaired loans and finance lease receivables to customers made 5.5 % of the respective portfolio.

**Loans and finance lease receivables neither past due nor impaired**

| 31 December 2017 | Business customers | Individual customers | Total |
|---|---|---|---|
| Low risk | 1 473 047 | 4 007 021 | 5 480 068 |
| Moderate risk | 3 329 491 | 1 338 272 | 4 667 763 |
| High risk | 508 736 | 170 191 | 678 927 |
| **Total** | **5 311 274** | **5 515 484** | **10 826 758** |

**Loans and finance lease receivables past due but not impaired**

| 31 December 2017 | Business customers | Individual customers | Total |
|---|---|---|---|
| Past due up to 30 days | 153 645 | 206 446 | 360 091 |
| Past due 31-60 days | 36 852 | 52 272 | 89 124 |
| Past due 61-90 days | 5 886 | 21 999 | 27 885 |
| Past due more than 90 days | 8 674 | 20 406 | 29 080 |
| **Total** | **205 057** | **301 123** | **506 180** |

**Impaired loans and finance lease receivables**

| 31 December 2017 | Business customers | Individual customers | Total |
|---|---|---|---|
| Individually assessed impaired loans | 494 529 | 159 775 | 654 304 |
| Fair value of collateral | 244 208 | 92 927 | 337 135 |

Gross amount and credit loss allowance amount for loans and advances at 31 December 2018 are disclosed in the table below:

| 31 December 2018 | Gross | Of which initial impairment of POCI | Allowance for impairment | Net |
|---|---|---|---|---|
| Due from banks and other credit institutions | **186 201** | **0** | **(4)** | **186 197** |
| Financial institutions | **58 752** | **(2 252)** | **(966)** | **57 786** |
| Business customers | **5 635 637** | **(28 575)** | **(92 787)** | **5 542 850** |
| -Loans | 3 786 630 | (27481) | (73 985) | 3 712 645 |
| -Factoring | 341 175 | (608) | (4 687) | 336 488 |
| -Leasing | 1 507 832 | (486) | (14 115) | 1 493 717 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | | |
|---|---|---|---|---|
| Individual customers | **5 968 156** | **(3 355)** | **(96 654)** | **5 871 502** |
| -Mortgage loans | 5 070 840 | (3 013) | (82 763) | 4 988 077 |
| -Consumer and card loans | 146 995 | (39) | (3 188) | 143 807 |
| -Other loans | 198 645 | (254) | (8 177) | 190 468 |
| -Leasing | 551 676 | (49) | (2 526) | 549 150 |
| **Total** | **11 848 766** | **(34 182)** | **(190 411)** | **11 658 335** |

The credit quality of loans and advances at 31 December 2018 is disclosed in the tables below according to the risk scale as set in the Credit Manual (see 1.1.a) paragraph): probability of default for low risk rating grades (1 to 4) is in the range from 0.00 % to 0.75 %, for moderate risk rating grades (5 to 7) it is from 0.75 % to 3.00 %, for high risk rating grades (from 8 to 10) it is from 3.00 % to 40.00 %.

**Due from banks and other credit institutions**

| | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| Low risk | 143 709 | - | - | - | 143 709 |
| Moderate risk | 42 482 | - | - | - | 42 482 |
| High risk | - | - | - | - | - |
| Default | - | - | 10 | - | 10 |
| **Gross** | **186 191** | **-** | **10** | **-** | **186 201** |
| Of which initial impairment | - | - | - | - | - |
| Less: allowance for impairment | (4) | - | - | - | (4) |
| **Net** | **186 187** | **-** | **10** | **-** | **186 197** |

**Loans and advances to financial institutions**

| | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| Low risk | 6 534 | 414 | - | - | 6 948 |
| Moderate risk | 45 652 | 1 475 | - | - | 47 128 |
| High risk | 760 | 2 837 | - | - | 3 597 |
| Default | - | - | 2 | 1 078 | 1 080 |
| **Gross** | **52 946** | **4 726** | **2** | **1 078** | **58 752** |
| Of which initial impairment | - | - | - | (2 252) | (2 252) |
| Less: allowance for impairment | (916) | (50) | - | | (966) |
| **Net** | **52 030** | **4 676** | **2** | **1 078** | **57 786** |

(all amounts are in EUR thousand, if not otherwise stated)

**Loans to business customers**

| | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Loans** | | | | | |
| Low risk | 1 319 643 | 231 951 | - | 1 | 1 551 595 |
| Moderate risk | 1 298 215 | 409 524 | | 1 315 | 1 709 054 |
| High risk | 39 493 | 151 822 | - | 2 237 | 193 552 |
| Default | - | - | 296 767 | 35 662 | 332 429 |
| **Gross** | **2 657 351** | **793 297** | **296 767** | **39 215** | **3 786 630** |
| Of which initial impairment | - | - | - | (27 481) | (27 481) |
| Less: allowance for impairment | (3 598) | (6 115) | (74 596) | 10 324 | (73 985) |
| **Net** | **2 653 754** | **787 182** | **222 171** | **49 539** | **3 712 645** |
| | | | | | |
| **Factoring** | | | | | |
| Low risk | 111 249 | 3 674 | - | - | 114 923 |
| Moderate risk | 193 477 | 5 499 | - | - | 198 976 |
| High risk | 13 353 | 8 291 | - | - | 21 644 |
| Default | - | - | 5 307 | 326 | 5 633 |
| **Gross** | 318 078 | 17 464 | 5 307 | 326 | 341 175 |
| Of which initial impairment | - | - | - | (608) | (608) |
| Less: allowance for impairment | (907) | (90) | (3 702) | 12 | (4 687) |
| **Net** | 317 171 | 17 374 | 1 605 | 338 | 336 488 |
| | | | | | |
| **Leasing** | | | | | |
| Low risk | 201 131 | 41 433 | - | 66 | 242 631 |
| Moderate risk | 837 653 | 170 777 | | 84 | 1 008 514 |
| High risk | 79 764 | 133 971 | - | 475 | 214 210 |
| Default | - | - | 41 201 | 1 277 | 42 478 |
| **Gross** | **1 118548** | **346 181** | **41 201** | **1 902** | **1 507 832** |
| Of which initial impairment | - | - | - | (486) | (486) |
| Less: allowance for impairment | (2 381) | (4 800) | (7 018) | 84 | (14 115) |
| **Net** | **1 116 167** | **341 381** | **34 183** | **1 986** | **1 493 717** |

(all amounts are in EUR thousand, if not otherwise stated)

**Loans to individual customers**

| | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Mortgage loans** | | | | | |
| Low risk | 3 918 228 | 32 329 | - | 2 543 | 3 953 100 |
| Moderate risk | 592 556 | 103 485 | - | 1 417 | 697 458 |
| High risk | 24 903 | 184 780 | - | 1 110 | 210 793 |
| Default | - | - | 200 157 | 9 332 | 209 489 |
| **Gross** | **4 535 687** | **320 594** | **200 157** | **14 402** | **5 070 840** |
| Of which initial impairment | - | - | - | (3 013) | (3 013) |
| Less: allowance for impairment | (4 153) | (21 131) | (56 633) | (846) | (82 763) |
| **Net** | **4 531 553** | **299 463** | **143 524** | **13 556** | **4 988 077** |
| **Consumer and card loans** | | | | | |
| Low risk | 34 027 | 1 259 | - | 9 | 35 295 |
| Moderate risk | 74 629 | 10 337 | - | 4 | 84 970 |
| High risk | 21 074 | 2 441 | - | 1 | 23 516 |
| Default | - | - | 3 198 | 17 | 3 215 |
| **Gross** | **129 730** | **14 037** | **3 198** | **31** | **146 996** |
| Of which initial impairment | - | - | - | (39) | (39) |
| Less: allowance for impairment | (682) | (245) | (2 274) | 15 | (3 188) |
| **Net** | **129 046** | **13 792** | **924** | **45** | **143 807** |
| **Other loans** | | | | | |
| Low risk | 41 400 | 2 507 | - | - | 43 907 |
| Moderate risk | 93 730 | 28 497 | - | 5 | 122 232 |
| High risk | 7 731 | 6 598 | - | 33 | 14 362 |
| Default | - | - | 16 988 | 1 156 | 18 144 |
| **Gross** | **142 861** | **37 602** | **16 988** | **1 194** | **198 645** |
| Of which initial impairment | - | - | - | (254) | (254) |
| Less: allowance for impairment | (352) | (400) | (7 056) | (369) | (8 177) |
| **Net** | **142 509** | **37 202** | **9 932** | **825** | **190 468** |
| **Leasing** | | | | | |
| Low risk | 71 215 | 1 121 | - | - | 72 398 |
| Moderate risk | 458 905 | 8 419 | - | 39 | 467 363 |
| High risk | 2 829 | 1 748 | - | 3 | 4 580 |
| Default | - | - | 7 128 | 207 | 7 334 |
| **Gross** | **532 949** | **11 350** | **7 128** | **162** | **551 676** |
| Of which initial impairment | - | - | | (49) | (49) |
| Less: allowance for impairment | (1 701) | (111) | (647) | (67) | (2 526) |
| **Net** | **531 248** | **11 239** | **6 481** | **182** | **549 150** |

(all amounts are in EUR thousand, if not otherwise stated)

**a) Information about credit loss allowances**

The following tables disclose the changes in the credit loss allowance for loans and advances between the beginning and the end of the reporting period.

**Due from banks and other credit institutions**

| | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(44)** | **-** | **-** | **-** | **(44)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | - | - | - | - | - |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | - | - | - | - | - |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | - | - | - | - | - |
| -remaining credit risk changes | 40 | - | (6) | - | 34 |
| New originated or purchased | (2) | - | - | - | (2) |
| Derecognised | 2 | - | - | - | 2 |
| Write-offs | - | - | 6 | - | 6 |
| Other movements | - | - | - | - | - |
| **Closing balance at 31 December 2018** | **(4)** | **-** | **-** | **-** | **(4)** |

**Loans and advances to financial institutions**

| | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(71)** | **(79)** | **-** | **388** | **238** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 2 | (3) | - | - | (1) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | - | 2 | - | - | 2 |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (15) | 12 | - | - | (3) |
| -remaining credit risk changes | (133) | 16 | - | (388) | (505) |
| New originated or purchased | (729) | - | - | - | (729) |
| Derecognised | 31 | 2 | - | - | 33 |
| Write-offs | - | - | - | - | - |
| Other movements | (1) | - | - | - | (1) |
| **Closing balance at 31 December 2018** | **(916)** | **(50)** | **-** | **-** | **(966)** |

(all amounts are in EUR thousand, if not otherwise stated)

**Loans to business customers**

| Loans | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(5 390)** | **(3 959)** | **(147 037)** | **363** | **(156 023)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 8 | (1 191) | - | - | (1 183) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | - | 22 | (4 688) | (7) | (4 673) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (4 075) | 2 243 | 333 | - | (1 499) |
| -remaining credit risk changes | 7 276 | (3 128) | 11 831 | (2 336) | 13 643 |
| New originated or purchased | (3 518) | (476) | (1 190) | 3 | (5 181) |
| Derecognised | 330 | 362 | 3 547 | (252) | 3 987 |
| Write-offs | 1 773 | 9 | 62 634 | 12 802 | 77 218 |
| Other movements | (2) | 3 | (26) | (249) | (274) |
| **Closing balance at 31 December 2018** | **(3 598)** | **(6 115)** | **(74 596)** | **10324** | **(73 985)** |

| Factoring | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(129)** | **(12)** | **(11 985)** | **-** | **(12 126)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 24 | (316) | - | - | (292) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | 4 | - | (893) | - | (889) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (13) | 2 | - | - | (11) |
| -remaining credit risk changes | (733) | 233 | 1 479 | 12 | 991 |
| New originated or purchased | (288) | (7) | (90) | - | (385) |
| Derecognised | 228 | 10 | 313 | - | 551 |
| Write-offs | - | - | 7 476 | - | 7 476 |
| Other movements | - | - | (2) | - | (2) |
| **Closing balance at 31 December 2018** | **(907)** | **(90)** | **(3 702)** | **12** | **(4 687)** |

(all amounts are in EUR thousand, if not otherwise stated)

| Leasing | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(2 226)** | **(6 511)** | **(8 630)** | **57** | **(17 310)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 358 | (769) | - | - | (411) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | 92 | 417 | (4 914) | (98) | (4 503) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (1 395) | 251 | 1 054 | - | (90) |
| -remaining credit risk changes | 2 056 | 1 871 | (1 007) | (7) | 2 913 |
| New originated or purchased | (1 442) | (481) | (930) | (75) | (2 928) |
| Derecognised | 143 | 420 | 2 472 | 9 | 3 044 |
| Write-offs | 33 | 2 | 4 944 | 198 | 5 177 |
| Other movements | - | - | (7) | - | (7) |
| **Closing balance at 31 December 2018** | **(2 381)** | **(4 800)** | **(7 018)** | **84** | **(14 115)** |

**Loans to individual customers**

| Mortgage loans | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(5 982)** | **(25 079)** | **(57 863)** | **(1 086)** | **(90 010)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 329 | (2 045) | - | 4 | (1 712) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | 7 | 143 | (8 911) | (17) | (8 778) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (181) | 117 | 87 | 4 | 27 |
| -remaining credit risk changes | 2 881 | 5 180 | 2 442 | (362) | 10 141 |
| New originated or purchased | (1 346) | (125) | (531) | - | (2 002) |
| Derecognised | 141 | 705 | 1 139 | (103) | 1 882 |
| Write-offs | - | - | 7 256 | 714 | 7 970 |
| Other movements | (2) | (27) | (252) | - | (281) |
| **Closing balance at 31 December 2018** | **(4 153)** | **(21 131)** | **(56 633)** | **(846)** | **(82 763)** |

(all amounts are in EUR thousand, if not otherwise stated)

| Consumer and card loans | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(622)** | **(194)** | **(2 466)** | **33** | **(3 249)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | - | (158) | - | (1) | (159) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | - | 4 | (815) | (8) | (819) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (41) | 4 | 23 | - | (14) |
| -remaining credit risk changes | 188 | 74 | (170) | (16) | 76 |
| New originated or purchased | (266) | (12) | (89) | (1) | (368) |
| Derecognised | 35 | 14 | 226 | (4) | 271 |
| Write-offs | 23 | 23 | 1 017 | 11 | 1 074 |
| Other movements | - | - | - | - | - |
| **Closing balance at 31 December 2018** | **(683)** | **(245)** | **(2 274)** | **14** | **(3 188)** |

| Other loans | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(287)** | **(1 336)** | **(21 827)** | **(525)** | **(23 975)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 4 | 67 | - | - | 71 |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | - | 25 | (1 872) | - | (1 847) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (99) | 26 | 3 | - | (70) |
| -remaining credit risk changes | 135 | 200 | 1 500 | 44 | 1 879 |
| New originated or purchased | (240) | (7) | (248) | (21) | (516) |
| Derecognised | 121 | 617 | 838 | (20) | 1 556 |
| Write-offs | 13 | 9 | 14 572 | 153 | 14 747 |
| Other movements | 1 | (1) | (22) | - | (22) |
| **Closing balance at 31 December 2018** | **(352)** | **(400)** | **(7 056)** | **(369)** | **(8 177)** |

| Leasing | Stage 1 (12-months ECL) | Stage 2 (lifetime ECL for SICR) | Stage 3 (lifetime ECL for credit-impaired) | POCI | Total |
|---|---|---|---|---|---|
| **Opening balance at 1 January 2018** | **(1 130)** | **(121)** | **(2 477)** | **(75)** | **(3 803)** |
| Changes due to change in credit risk: | | | | | |
| -transfer to lifetime (from Stage 1 to Stage 2) | 19 | (42) | - | (2) | (25) |
| -transfer to credit-impaired (from Stage 1 and Stage 2 to Stage 3) | 19 | 1 | (347) | 8 | (319) |
| -transfer to 12-months ECL (from Stage 2 and Stage 3 to Stage 1) | (393) | 6 | 428 | - | 41 |
| -remaining credit risk changes | 355 | 78 | 742 | (10) | 1 165 |
| New originated or purchased | (674) | (42) | (55) | (41) - | (812) |
| Derecognised | 81 | 9 | 205 | 5 | 300 |
| Write-offs | 22 | - | 857 | 48 | 927 |
| Other movements | - | - | - | - | - |
| **Closing balance at 31 December 2018** | **(1 701)** | **(111)** | **(647)** | **(67)** | **(2 526)** |

The most significant changes in the loss allowances and the changes in the gross carrying amount by the same amount were due to the write-offs, the most impacted financial instruments were business customers loans (decrease by 77 218 tEUR) and individual customers other loans (decrease by 14 747 tEUR) and mortgage loans (decrease by 7 970 tEUR).

**b) Information about collaterals of loans**

Upon initial recognition of loans and advances, the fair value of collateral is based on the valuation techniques commonly used for the corresponding types of collateral. Market values (or purchase price, whichever is lower) are used for real estate and movable assets serving as collateral. The value of collateral should be reconsidered periodically. The frequency and conditions mostly depend on performing/non-performing status and exposure size. The value of residential real estate is recalculated periodically by applying the indices.

The Group takes into account guarantees issued by the State, other parties issuing guarantees which are equivalent to the State guarantees, municipalities, banks in disclosing information on guarantees serving as collateral. Guarantees and warranties issued by other parties (private individuals, legal entities), although they mitigate the risk, are considered to be immaterial and are not disclosed here.

If exposure is secured by several different types of collateral, priority in recognition of a collateral is based on its liquidity. Securities, cash and guarantees are treated as the types of collateral with highest liquidity followed by residential real estate and then other real estate. Movable assets like transport vehicles, equipment and other assets are treated as having lowest liquidity.

(all amounts are in EUR thousand, if not otherwise stated)

**Group loans and advances to customers**

| | Business customers | % | Individual customers | % | Total | % |
|---|---|---|---|---|---|---|
| **Unsecured loans** | **1 562 193** | **27%** | **325 446** | **5%** | **1 887 639** | **16%** |
| **Loans collateralized by:** | **4 132 196** | **73%** | **5 642 710** | **95%** | **9 774 906** | **84%** |
| - residential real estate | 153 314 | 3% | 4 719 046 | 79% | 4 872 360 | 42% |
| - other real estate | 1 810 771 | 32% | 163 788 | 3% | 1 974 559 | 17% |
| - securities | 1 219 | 0% | 115 | 0% | 1 334 | 0% |
| - guarantees | 216 670 | 4% | 215 578 | 4% | 432 248 | 4% |
| - other assets | 1 950 222 | 34% | 544 183 | 9% | 2 494 405 | 21% |
| **Total** | **5 694 389** | **100%** | **5 968 156** | **100%** | **11 662 545** | **100%** |

The amount of credit-impaired loans is reported together with the value of related collateral held as security in the tables below. Credit-impaired loans are most often secured by real estate and movable assets. Value for such collateral is equal to its market value (not liquidation value), which is updated shortly after identification of default.

| 31 Dec 2018<br>Credit-impaired loans | Gross | Of which initial impairment | Allowance for impairment | Net | Fair value of collateral |
|---|---|---|---|---|---|
| Business customers | 381 617 | (30 643) | (75 033) | 306 584 | 326 907 |
| Individual customers | 238 183 | (2 572) | ( 68 468) | 169 714 | 197 797 |
| **Total** | **619 800** | **(33 215)** | **(143 351)** | **476 298** | **524 704** |

### 1.6: Exposures rated by External Credit Assessment Institutions

Table below presents analysis of debt securities of the Group by rating agency designation at 31 December 2018 based on Fitch's ratings or their equivalent.

| 31 Dec 2018<br>Rating | Trading securities | Securities designated at fair value through profit or loss | Securities designated at FVTOCI | Total |
|---|---|---|---|---|
| Aaa | - | - | - | **-** |
| From Aa3 to Aa1 | - | 23 076 | - | **23 076** |
| From A3 to A1 | 103 | 116 326 | 1 265 | **117 694** |
| From Baa1 to Ba3 | 903 | - | - | **903** |
| From B1 to B3 | - | - | - | **-** |
| No rating | - | - | - | **-** |
| **Total** | **1 006** | **139 402** | **1 265** | **141 673** |

| 31 Dec 2017<br>Rating | Trading securities | Securities designated at fair value through profit or loss | Total |
|---|---|---|---|
| Aaa | - | - | **-** |
| From Aa3 to Aa1 | - | 30 197 | **30 197** |
| From A3 to A1 | 2 189 | 131 680 | **133 869** |
| From Baa1 to Ba3 | 136 | - | **136** |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | |
|---|---|---|---|
| From B1 to B3 | - | - | - |
| No rating | - | - | - |
| **Total** | **2 325** | **161 877** | **164 202** |

### 1.7: Concentration of risks of financial assets with credit risk exposure

**Economic sectors**

The following tables break down the loans and advances to customers at their carrying amounts, as categorized by the economic sectors of our counterparties.

| | Amount 2018 | % 2018 |
|---|---|---|
| Financial intermediation | 88 690 | 0.8% |
| Agriculture, hunting, forestry, fishing | 698 081 | 6.1% |
| Manufacturing | 799 485 | 7.0% |
| Electricity, gas, water supply | 218 404 | 1.9% |
| Construction | 131 260 | 1.1% |
| Wholesale and retail trade | 1 142 761 | 10.0% |
| Transport, storage, communication | 537 997 | 4.7% |
| Real estate activities | 1 209 607 | 10.5% |
| Public sector | 245 362 | 2.1% |
| Other industries | 705 379 | 6.1% |
| Private individuals | 5 695 130 | 49.6% |
| **Total** | **11 472 138** | **100.0%** |

## 2: MARKET RISK

The Group takes on low exposure to market risk, which can be treated as the risk of losses in on- and off-balance sheet positions arising from adverse movements in market parameters such as currency exchange rates (currency risk), interest rates (interest rate risk), equity prices (equity risk) or commodity prices (commodity risk). The most significant part of market risk for the Group is interest rate risk while significance of other risks is lower.

Interest rate risk is assessed using the basis point value (BPV) method, which measures the impact on the value of net cash flows given a one basis point (0.01%) parallel shift in market interest rates. An exchange rate risk is evaluated by calculation of open foreign exchange positions. The BPV calculations are performed on a regular basis and submitted to the Group's Management, as well as Group's Markets and Treasury & ALM departments. Interest rate and foreign exchange risks are restricted by the limits determined by the Management Boards and Supervisory Councils of Luminor banks (Luminor bank AS (Estonia), Luminor Bank AS (Latvia) and Luminor Bank AB (Lithuania). and monitored on regular basis by the Market Risk department.

### 2.1: Market risk measurement approaches

The Group is mainly focused on foreign exchange and interest rate risk management.

Interest rate risk is assessed as an impact of yield curve's parallel shift on a present value of the gap between total liabilities and total assets. In general assets have longer maturities than liabilities, which creates risk due to open interest rate position. Therefore, interbank funding is attracted to decrease the discrepancy between long and short terms. In addition to this, interest rate swaps are used to achieve and maintain an acceptable level of interest rate risk.

Foreign exchange (hereinafter referred to as FX) risk is assessed as an open position between assets and liabilities in a respective currency. Open positions for all currencies in the Group are restricted by the limits set by the Management Boards and Supervisory Councils of Luminor banks and monitored on a daily basis.

## 2.2: FX risk

The Group's main exposure is towards euro currency (EUR), while positions of other currencies are not significant. Conservative approach to FX risk is followed within the Group. It is measured as the nominal value of the open FX positions converted to EUR using European Central Bank (ECB) rates. The Group is responsible for staying within the given limits – both intraday and overnight. Some technical deviations from limits are allowed only for short term when servicing customers. The Group has approved limits for USD, sum of other currencies, maximum of other currencies and total currencies.

**The Group's exposure to FX risk (in thousand EUR)**

| Currency | 31 December 2018 | 31 December 2017 |
|---|---|---|
| USD | 232 | 355 |
| Max of other currencies | 375 | 94 |
| Sum of other currencies | 1 090 | 333 |
| **Total** | **1 149** | **1 044** |

**Sensitivity of FX risk**

FX risk is limited by amounts of open FX positions. For sensitivity calculation of FX risk, all exposures shall be converted into possible loss amounts, i.e. open FX position is multiplied by possible FX rate change. This parameter for the Group is 5.4% for all currencies and is developed using VaR approach based on 99 per cent confidence level and 10 days holding period. Horizon of data analysed includes the latest financial crisis in 2008-2009 and is at least 5 years of historical developments of FX rates.

Calculation of sensitivity of FX risk shows immaterial impact for the Group in 2018.

## 2.3: Interest rate risk

The main source of interest rate risk in the Group is repricing risk – risk related to the timing mismatch in the maturity and repricing of assets and liabilities of on- and off-balance sheet positions. Pursuant to Luminor Market Risk policy interest rate risk is limited in terms of BPV, i.e. the change in net cash flows (gaps) given a one basis point (0.01%) parallel shift in market interest rates. Separate limits for Banking and Trading activities are approved by the Management Boards and Supervisory Councils of Luminor banks as well as limits for different currencies: EUR, USD, NOK and all other currencies. When calculating the total exposure the sums of BPV in each currency are aggregated irrespective if the total exposure in each individual currency is a short or long position, i.e. netting of positions between currencies is not allowed. The main part of the interest rate risk arises from the positions that are denominated in euro currency. Using derivatives is major attribute of interest risk management, please also refer to accounting principles for hedge accounting.

Changes in interest rates do not have to be the same for all time bands. To limit risk exposure resulting from different time bands, so-called gapping limits are determined for each of them. Limit established for each time bands is defined as a percentage of the total BPV limit allocated to the relevant currency. All time bands till one year period are limited to 100% of total BPV, 1-2 years gap is limited to 120% of total BPV, and all time bands above 2 years has the limit of 150% of total BPV.

**The Group's BPV exposure by currencies for both trading and banking activities in EUR:**

| Currency | 31 December 2018 | 31 December 2017 |
|---|---|---|
| EUR | (10 530) | (30 400) |
| USD | 2 831 | 1 400 |
| NOK | 522 | 300 |
| Other currencies | (98) | (100) |

**Sensitivity of interest rate risk**

Interest rate risk exposure cannot exceed BPV limits approved by the Management Boards and Supervisory Councils of Luminor banks. Assuming a 200 basis points parallel shift of the yield curve, sensitivity of interest rate risk shall be calculated multiplying total BPV exposure by interest rate change. The above mentioned shift of the yield curve creates the following impact on the Group's equity and profit / loss in thousands EUR:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Equity | 1 455 | 2 190 |
| Profit / Loss | 20 205 | 3 507 |

### 2.4: Equity and commodity risk

The Group does not have any open positions in commodity and equity instruments as all commodity transactions are hedged back-to-back and the Group does not engage in proprietary stock trading. The shares of SWIFT and VISA are recognized as participation in the settlement systems rather than any kind of investment in shares. However, as these shares are repriced based on their market value, the Group measures equity sensitivity using 1 year value-at-risk (VaR) method with 99% confidence including latest finance crysis data which indicates possible loss of 16.6% of total equity value. The impact on the Group's shares in thousands EUR is the following:

| | 31 December 2018 | 31 December 2017 |
|---|---|---|
| Shares | 1 262 | 967 |

## 3: LIQUIDITY RISK

Liquidity risk means the risk that the Group is unable to meet its financial obligations in time, the risk to incur losses due to the sudden decrease in financial resources (e.g. a financial crisis situation may result in a delay of incoming payments) or an increase in price of the new resources designed for refinancing. The consequence of liquidity risk occurrence may be the failure to meet obligations to repay depositors and fulfil loan commitments. The Group uses a range of liquidity metrics for measuring, monitoring and controlling liquidity risk including Liquidity Coverage Ratio (LCR), Net Stable Funding Ratio (NSFR), internal liquidity limits.

Liquidity risk is managed in a manner to ensure a constant ability to settle contractual obligations. The Group has developed a set of early warning indicators for a timely identification of liquidity crises, and business and funding contingency funding plans to manage the Group's liquidity during the market disruption. Liquidity risk management strategy is reviewed at least annually or after any significant change in the internal or external environment the Group operates in.

### 3.1: Liquidity risk management process

**Liquidity risk is managed across three Lines of Defence:**

- The First Line of Defence comprises the Group's Treasury & ALM (TALM) and the Business Areas. TALM is responsible for the daily liquidity management and Funds Transfer Pricing (FTP). To ensure funding in situations where Luminor is in urgent need of cash and the normal funding sources do not suffice, Luminor holds a liquidity buffer that consists of central bank cash and high quality securities that can be readily sold or used as collateral in funding operations.
- Market Risk department acts as the Second Line of Defence and is responsible for providing independent oversight of liquidity risk.
- The Third Line of Defence includes the Group's Internal Audit, which is responsible for providing independent oversight of the First and Second Lines of Defence.

Liquidity risk management is divided into long-term (1 year), short-term (1 week to 3 months) risk management and intraday liquidity management. The aim of short-term liquidity management is to meet the daily need for funds to ensure the compliance with the reserve and liquidity requirements set by the ECB, as well as the compliance with internal liquidity limits. Short-term liquidity is maintained through daily monitoring of the liquidity status, day-to-day funding and trading the appropriate financial instruments for liquidity purposes. Long-term liquidity risk management is supported by analysing the estimated future cash flows taking into account the deposit and loan portfolio growth as well as possible refinancing sources.

For the purpose of liquidity risk assessment the liquidity gap is analysed taking into account the maturity of cash flows. The liquidity risk is restricted by imposing the internal limits on liquidity gap. Utilization of this limit is subject to regular monitoring and reporting to various management bodies in the Group.

Liquidity gap is calculated by analysing the Group's net refinancing situation within one week, one month and three months applying a "business as usual" approach. Liquid assets and short term liabilities are included in liquidity gap calculation for respective terms (1 week to 3 months).

Liquidity Coverage Ratio is calculated as the ratio of a credit institution's liquidity buffer to its net liquidity outflows over a 30 calendar day stress period and shall be expressed as a percentage. Since Lithuania, Latvia and Estonia are all members of the EU, LCR is applicable to the Group as a Europe wide requirement. Minimum limit of LCR is set at 100%, however the Group has substantial buffer and maintains a higher ratio. LCR is intended to promote short-term resilience of the Group's liquidity risk profile and requires to hold risk-free assets that may be easily liquidated on markets in order to meet required payments for outflows net of inflows during a thirty-day crisis period without the support from the central bank.

(all amounts are in EUR thousand, if not otherwise stated)

The analysis of the Group's main balance sheet items by remaining maturity is summarized in Note 41.

The Net Stable Funding Ratio (NSFR) is defined as the amount of available stable funding relative to the amount of required stable funding over the one year time horizon. Minimum requirement for NSFR is 100%, however the Group has a substantial buffer and maintains a higher ratio.

**Liquidity metrics of the Group:**

| Liquidity metric | 31 December 2018 | 31 December 2017 |
|---|---|---|
| 1W liquidity gapping | EUR 3 113 million | EUR 2 899 million |
| 1M liquidity gapping | EUR 2 923 million | EUR 2 718 million |
| 3M liquidity gapping | EUR 2 187 million | EUR 2 286 million |
| LCR | 189% | 157% |
| NSFR | 123% | 119% |
| Loan to deposit ratio | 129% | 140% |

### 3.2: Off - balance sheet items

The analysis of nominal off-balance sheet items by remaining maturity is as follows:

| 31 December 2018 | On Demand | Up to 3 months | From 3 to 12 months | From 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Financial guarantees | 406 037 | - | - | - | - | 406 037 |
| Letters of credit | 1 396 | 28 417 | 53 087 | 323 | - | 83 223 |
| Commitments to grant loans and finance leases | 62 640 | 195 402 | 643 553 | 300 910 | 101 684 | 1 304 189 |
| Capital commitments and other commitments to acquire assets | 434 | - | - | - | - | 434 |
| Other commitments | 5 869 | 29 671 | 35 017 | 51 638 | 68 186 | 190 381 |
| **Total** | **476 376** | **253 490** | **731 657** | **352 871** | **169 870** | **1 984 264** |

| 31 December 2017 | On Demand | Up to 3 months | From 3 to 12 months | From 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Financial guarantees | 469 578 | - | - | - | - | 469 578 |
| Letters of credit | 1 206 | 45 233 | 32 218 | 3 577 | - | 82 234 |
| Commitments to grant loans and finance leases | 253 555 | 165 272 | 328 425 | 439 969 | 81 583 | 1 268 804 |
| Capital commitments and other commitments to acquire assets | 977 | - | - | - | - | 977 |
| Other commitments | 46 499 | 56 113 | 103 183 | 125 348 | 91 058 | 422 201 |
| **Total** | **771 815** | **266 618** | **463 826** | **568 894** | **172 641** | **2 243 794** |

(all amounts are in EUR thousand, if not otherwise stated)

### 3.3: Liquidity buffer and collateral management

The Group has a contractual agreement for funding in place with shareholders DNB Bank ASA and Nordea Bank AB. This strongly mitigates the likelihood of funding liquidity risk which may be caused by deposit run off, wholesale funding risk (roll over and new issuance), unexpected outflows from off-balance sheet obligations and legal risks (e.g. not being able to do issuance due to legal restrictions). As the Group is going towards more reliance on self-funding rather than on support from shareholders, other funding sources are being established or are already in place for diversifying the funding base.

The Group is taking part in the ECB's Eurosystem open market operations. In particular, the Group is a user of the ECB Targeted Long Term Refinancing Operations (TLTRO). In addition, a significant part of funding is attracted through retail and corporate deposits. Moreover, the Group has already issued EUR 350 million of its own senior debt securities and is considering to increase this amount in the future even more, which would further diversify the possibilities for receiving funding.

The main liquidity buffer is the Group's Target subaccount with the central bank, where the Group held EUR 3.06 billion at the end of year 2018. This buffer can be utilized at any time when the need arises. The Group has established a liquidity portfolio with intention to accumulate high quality liquid debt securities. The portfolio is accounted at fair value. Currently the size of the portfolio is set at the level of EUR 180 million with relatively short portfolio average duration and maximum duration of the debt securities is set at 5 years. The portfolio is targeting to ensure the continuity of the Group's operations and provides the stabilisation effect for all liquidity risk metrics including LCR. The securities held in the portfolio are by definition unencumbered and available for instant raise of funds in unexpected or stressed situations. At the end of year 2018 most of this portfolio has been pledged as a collateral in order to get Targeted Long Term Refinancing Operations (TLTRO) low cost funding through Eurosystem's open market operations. Pledged debt securities are accounted separately from the liquidity portfolio and are not included into liquid assets, for instance in LCR calculations. Part of loans issued to entities with the government rating (municipalities and government institutions) are pledged as a collateral as well.

### 3.4: Non-derivative cash flows

Undiscounted cash flows below describe liability side outflows which are represented by nominal contract amounts together with accrued interest till the end of the contract. Possible early repayments foreseen in the loan agreements are included into cash flows calculations.

| 31 December 2018 | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Due to banks and other credit institutions | 25 046 | 6 095 | 2 670 950 | 1 245 115 | - | 3 947 206 |
| Due to customers | 7 446 681 | 711 886 | 826 061 | 85 365 | 5 497 | 9 075 490 |
| Debt securities issued | - | - | 5 250 | 360 500 | - | 365 750 |
| Other financial liabilities | 15 896 | 1 108 | 3 181 | 8 858 | 13 | 29 056 |
| **Total liabilities (contractual maturity dates)** | 7 487 623 | 719 089 | 3 505 442 | 1 699 838 | 5 510 | 13 417 502 |

| 31 December 2017 | Up to 1 month | 1-3 months | 3-12 months | 1-5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Due to banks and other credit institutions | 134 342 | 82 294 | 2 620 423 | 1 939 825 | - | 4 776 884 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | | | | |
|---|---|---|---|---|---|---|
| Due to customers | 7 261 720 | 467 205 | 659 253 | 38 918 | 3 533 | 8 430 629 |
| Debt securities issued | - | - | - | 65 007 | - | 65 007 |
| Other financial liabilities | 36 090 | 2 375 | 2 743 | 1 869 | 67 | 43 144 |
| **Total liabilities (contractual maturity dates)** | 7 432 152 | 551 874 | 3 282 419 | 2 045 619 | 3 600 | 13 315 664 |

### 3.5: Derivative cash flows

Tables below analyse cash flows from derivative instruments.

| 31 December 2018 | Up to 1 month | 1 to 3 months | 3 to 12 months | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Derivatives settled on a net basis | 81 | 498 | 1 898 | 8 443 | (970) | 9 950 |

| 31 December 2017 | Up to 1 month | 1 to 3 months | 3 to 12 months | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|---|---|
| Derivatives settled on a net basis | 20 | 359 | 262 | 3 989 | (402) | 4 228 |

## 4: CAPITAL MANAGEMENT

The capital is calculated and allocated for the risk coverage following the regulations in the CRD IV and CRR of the European Union and the local Regulators legal acts. The Group's objectives in capital management are as follows:

- consistency with Luminor Group's long-term strategy (including meeting the risk appetite of the Group) and the Dividend policy;
- the ability to pursue the business objectives;
- fulfillment of both internal and external capitalization targets (capital adequacy);
- sufficient and proper composition of capital that would withstand stressful events.

Capital adequacy assessment is performed on a quarterly basis in accordance with the Information guidelines in respect of risk management and capital adequacy disclosure (Pillar3) report.

**The Group's regulatory capital is divided into two tiers:**

1) Tier 1/Common Equity Tier 1 (CET 1) capital consists of the ordinary shares, share premium, retained earnings of the previous financial year, accumulated other comprehensive income, other reserves, value adjustments due to the requirements for prudent valuation and less the intangible assets, deferred tax assets and other deductions.
2) Tier 2 capital consists of transitional adjustments related to the accumulated other comprehensive income.

The risk-weighted assets are measured by means of risk weights classified according to the nature of each assets and counterparty, taking into account collaterals and guarantees eligible for risk mitigation. A similar treatment with some adjustments is adopted for the off-balance sheet exposures.

(all amounts are in EUR thousand, if not otherwise stated)

The table below summarizes the composition of regulatory capital and the ratios of the Group at the end of 2018:

| | Group 31 12 2018 | Group 31 12 2017 |
|---|---|---|
| Tier 1/Common Equity Tier 1 (CET 1) capital | 1 660 621 | 1 685 857 |
| Tier 2 capital | - | 229 |
| **Total own funds** | **1 660 621** | **1 686 086** |
| | | |
| **Total risk exposure amount** | **9 206 164** | **9 435 770** |
| | | |
| Tier1/Common Equity Tier 1 (CET 1) capital ratio, % | 18.04% | 17.87% |
| **Capital ratio, %** | **18.04%** | **17.87%** |

Luminor assesses the material risks it is exposed to and calculates the internal capital for the risks not covered or not fully covered by the Pillar 1 capital as part of the Internal Capital Adequacy Assessment Process (ICAAP). The overall ICAAP approach in Luminor is to comprehensively assess whether the current, projected and stressed levels of capital are adequate considering both the regulatory requirements and targets set by Supervisory Council.

Luminor uses a combination of quantitative and qualitative assessment regarding decision if each particular risk or group of risks are subject to Pillar 2 capital add-on calculation.

Credit risk is fully covered by Pillar 1 capital which is calculated using Standardised approach.

The concentration risk is assessed for the asset classes exposed to credit risk. Besides the imposed limits on lending, the Group calculates the internal capital requirement for name concentration risk and economic sectors concentration risk.

As the regulatory capital requirement is calculated for the interest rate risk arising from the trading book, the Group additionally assesses and calculates the internal capital requirement for the interest rate risk arising from the banking book.

In order to assess internal capital requirement for operational risk the Group has applied qualitative and quantitative approaches. Money laundering and terrorism financing and sanction risk, cyber risk, compliance risk and model risk are included under operational risk and are assessed as a one group.

The Group set aside additional capital for business risk.

The Luminor Group calculates the total internal capital requirement as Pillar 1 capital according to regulatory requirements adjusted by the amounts evaluated for the risks identified during self-assessment and ICAAP. A detailed overview of the ICAAP process is included in Pillar 3 annual disclosure.

## 5: OPERATIONAL RISK

Within one year following the merge Luminor continued to pursue strategic initiatives and goals by changing ownership, governance structure and corporate mindset. Responding to increased focus in the area of money-laundering prevention and compliance within Baltic banking industry in 2018, the top priority for Luminor was building strong internal controls and sound risk culture.

Luminor Group Operational Risk is an independent internal control function within second line of defense and covers operational risk management, information security, physical security and personal data protection.

Operational risk management in Luminor is governed by Operational Risk Policy and underlying tools, the main principle of which is that operational risk should be low and risk management should ensure that risk of unexpected losses is reduced. Each manager and process owner is responsible for management of risks inherent to the activities and processes of their area and to foster sound risk management culture in their respective reporting lines.

Operational risk incidents in Luminor are reported, registered in operational risk incident database and continuously followed. Operational risk incident database represents valuable information source for Management Reporting, Business Impact Assessment, annual Risk Control Self-Assessment and internal Stress Testing, which are important elements in operational risk management framework in Luminor.

Information Security is an integral part of risk management as Luminor is striving to provide the best digital offering in the market and be the first to launch innovative solutions. This requires wide usage of Information and Communication Technology (ICT) systems to empower and automate business processes. Information Security processes in Luminor are designed to protect information against accidental or malicious disclosure, modification, or destruction and to meet regulatory, legislative and contractual requirements concerning information security. To comply with General Data Protection Regulation (GDPR) Luminor has established Data Protection Officers function and renewed required internal regulations, technical and organizational measures. All employees at all levels are constantly trained in information security and data protection areas to maintain awareness of the associated risks and necessary measures.

Luminor management is kept updated on the status of operational risk through the periodic and on-demand risk reports, results of annual Risk Control Self-Assessment and Stress Testing exercises. Management reports include presentation of key group-wide operational risks, relevant improvement measures and detailed qualitative assessment. Annual operational risk stress test analysis helps management to understand the nature and extent of vulnerabilities to which Luminor is exposed in order to consider them in the strategic planning.

Luminor insurance coverage is an additional element in operational risk management. Insurance contracts limit the financial consequences of undesirable incidents, which occur in spite of established security routines and risk-mitigating measures. The insurance program additionally covers legal liabilities related to Luminor operations.

## 6: STRESS TESTS

Besides the regular assessment of the risks and the capital requirement calculation, the Group also performs stress tests for the credit, liquidity, market (interest rate and foreign exchange), operational risks and the stress testing of the financial plan (business risk). The purpose of the stress-testing is to evaluate whether the Group’s capital is sufficient to cover those extraordinary losses that might occur in the case where the testing scenario is realised as well as to prepare the contingency plan for the Group. In order to evaluate the losses caused by the aforesaid risks the realisations of the baseline, adverse, severe adverse and fail or likely to fail (FOLTF) scenarios are assumed. Liquidity risk is tested under the following scenarios: an Idiosyncratic scenario, a market wide scenario and a combination of the two ( i.e. combined).

(all amounts are in EUR thousand, if not otherwise stated)

# OTHER NOTES TO THE FINANCIAL STATEMENTS

## G8: NET INTEREST INCOME

| | 2018 | 16.08.2016 -31.12.2017 |
|---|---|---|
| **Interest income** | | |
| Interest income calculated using the effective interest method: | | |
| Loans and advances to customers at amortised cost | 237 030 | 59 622 |
| Deposits at amortised costs | 1 698 | 360 |
| Debt securities at amortised cost | 217 | 60 |
| **Total interest income calculated using effective interest method** | **238 945** | **60 042** |
| Other similar income: | | |
| Finance leases | 57 972 | 14 238 |
| Financial assets held for trading | 1 165 | 28 |
| Debt securities at fair value through profit or loss | 460 | 164 |
| Deposits with other banks | 824 | 1 |
| **Total other similar income** | **60 421** | **14 431** |
| **Total interest income** | **299 366** | **74 473** |
| | | |
| **Interest expenses** | | |
| Interest expenses for liabilities to credit institutions | (15 136) | (3 650) |
| Interest expenses for deposits and loans to the public | (8 939) | (1 726) |
| Issued securities | (4 217) | (875) |
| Other interest expenses | (11 341) | (3 756) |
| **Total interest expenses** | **(39 633)** | **(10 007)** |
| **Net interest income** | **268 616** | **67 898** |
| Of which attributable to financial assets and liabilities valued at fair value through profit/loss | 460 | 164 |

## G9: NET COMMISSION

| | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| **Commission income** | | |
| Payments | 60 687 | 16 086 |
| Securities commission | 10 407 | 2 238 |
| Guarantees | 9 506 | 1 115 |
| Loans and deposits | 5 805 | 1 128 |
| Factoring | 4 183 | 687 |
| Account maintenance | 4 080 | 1 671 |
| Insurance commission | 2 923 | 248 |
| Other | 11 987 | 4 968 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | |
|---|---|---|
| **Total commission income** | **109 578** | **28 141** |
| **Commission expenses** | | |
| Payments | (14 247) | (3 389) |
| Cards maintenance | (7 281) | (2 034) |
| Securities commission | (350) | (230) |
| Guarantees | (80) | (454) |
| Other | (3 859) | (606) |
| **Total commission expenses** | **(25 817)** | **(6 713)** |
| **Net commission** | **83 761** | **21 428** |

## G10: OTHER OPERATING EXPENSES

| | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| Taxes other than income tax and deductible VAT | (5 925) | (873) |
| Revaluation expenses of real estate and investment property | (3 137) | (9 511) |
| Deductible VAT | (1 824) | (425) |
| Investment property maintenance | (1 180) | - |
| Other insurance expenses (bank risk, etc.) | (721) | (4) |
| Other legal expenses (notarial services, issued documents of state institutions, etc.) | (615) | (989) |
| Other expenses* | (3 107) | (1 561) |
| **Total** | **(16 509)** | **(13 363)** |

*Major part of other expenses comprises of representative expenses and maintenance cost of assets taken over for debt.

## G11: GENERAL ADMINISTRATIVE EXPENSES

| | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| Personnel expenses | (113 605) | (30 381) |
| Office equipment and maintenance expenses | (26 472) | (6 244) |
| IT Development, Operations and other service expenses | (27 104) | - |
| Rent of premises* | (8 155) | (1 963) |
| Maintenance expenses | (4 791) | (1 373) |
| Cash collection, consultancy and other services expenses | (12 357) | (9 840) |
| Regulatory and association fees | (2 936) | (59) |
| Transportation, post and communications expenses | (3 313) | (786) |
| Advertising and marketing expenses | (3 217) | (1 494) |
| Training and business trip expenses | (2 790) | (272) |
| Other expenses | (11 632) | (12 007) |
| **Total** | **(216 372)** | **(64 419)** |

*Expenses of the lessee’s significant lease arrangement of central office is amounted to EUR 879 thousand in year 2017 and EUR 3 509 thousand in year 2018.

(all amounts are in EUR thousand, if not otherwise stated)

## PERSONNEL EXPENSES

| | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| **Distribution of personnel expenses** | | |
| Salaries and other remuneration | (81 779) | (21 651) |
| Social insurance contribution | (24 360) | (6 470) |
| Other personnel expenses | (7 466) | (2 260) |
| **Total personnel expenses** | **(113 605)** | **(30 381)** |

Social security tax payments include a contribution to state pension funds. The Group has no legal or constructive obligation to make pension or similar payments beyond social security tax. The Group had no pension or other long term employee benefits.

| | 2018 | 16.08.2016 -31.12.2017 |
|---|---|---|
| **Salaries and other remuneration to** Board members, Chief Executive Officer and corresponding officials | (1 753) | (580) |
| **Social security expenses to** Board members, Chief Executive Officer and corresponding officials | (487) | (99) |
| **Other personnel expenses to** Board members, Chief Executive Officer and corresponding officials | (73) | - |

| Average number of employees covers the following geographical markets | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| **Estonia** | | |
| - of whom women | 556 | 474 |
| - of whom men | 191 | 150 |
| **Total** | **747** | **624** |
| | | |
| **Latvia** | | |
| - of whom women | 678 | 715 |
| - of whom men | 350 | 298 |
| **Total** | **1 028** | **1 013** |
| | | |
| **Lithuania** | | |
| - of whom women | 905 | 758 |
| - of whom men | 398 | 350 |
| **Total** | **1 303** | **1 108** |
| | | |
| **Sweden** | | |
| - of whom women | - | - |
| - of whom men | 1 | 1 |
| **Total** | **1** | **1** |

(all amounts are in EUR thousand, if not otherwise stated)

| Total | | |
|---|---|---|
| - of whom women | 2 139 | 1 947 |
| - of whom men | 940 | 799 |

| Remuneration to auditors and audit companies | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| Audit services | 839 | 393 |
| Other services | 281 | 6 |
| **Total** | **1 120** | **399** |

## G12: AMORTIZATION AND DEPRECIATION OF TANGIBLE AND INTAGIBLE ASSETS

| | 2018 | 16.08.2016 - 31.12.2017 |
|---|---|---|
| Property, Plant and Equipment | (6 322) | (1 380) |
| Other intangible assets | (2 438) | (754) |
| **Total** | **(8 760)** | **(2 134)** |

## G13: PROVISIONS EXPENSES

| | 2018 | 16.08.2016 -31.12.2017 |
|---|---|---|
| Commitments and guarantees given | (1 553) | (272) |
| Other provisions | 20 | (178) |
| **Total** | **(1 533)** | **(450)** |

## G14: SHARE OF PROFIT OF AN ASSOCIATE, PROFIT NON CURRENT ASSETS HELD FOR SALE

| | 2018 | 16.08.2016 -31.12.2017 |
|---|---|---|
| Share of profit of an associate | 860 | 906 |
| Profit non current assets held for sale | - | 58 |
| **Total** | **860** | **964** |

## G15: IMPAIRMENT OF ASSETS

| | 2018 | 16.08.2016 -31.12.2017 |
|---|---|---|
| **Net impairment (losses)/ reversal on loans to customers** | **6 313** | **(13 833)*** |
| | | |
| Impairment on other assets and change in fair value of investment property | (4 141) | (5 210) |
| Provisions (Note G13) | (1 533) | (450) |
| Gains or (-) losses on derecognition of commitments | 1 347 | - |
| **Net impairment (losses)/ reversal on other assets, change in fair value of investment property and provisions** | **(4 327)** | **(5 660)** |

*Major part of impairment in 2017 comprise of impairment for one off case.

(all amounts are in EUR thousand, if not otherwise stated)

## G16: TAXES

| | 2018 | 16.08.2016 -31.12.2017 |
|---|---|---|
| Current tax for the year | 12 161 | 1 341 |
| Adjustment of current tax for previous years | 1 479 | (1 714) |
| Deferred tax related to temporary differences | 527 | 3 392 |
| Revesal of deferred tax | - | 9 888 |
| **Tax on net income for the year** | **14 167** | **12 907** |
| | | |
| Profit before tax | 139 116 | 7 237 |
| Tax as per current tax rate for the Parent Company (22%) | 30 606 | 1 592 |
| Difference in overseas tax rates | (17 627) | 13 723 |
| Adjustment of current tax | 1 479 | (1 714) |
| Reversal of deferred tax | - | (9 888) |
| Effect of non-deductible expenses/non-taxable income | (291) | 9 194 |
| Income tax for the year | 14 167 | 12 907 |
| **Effective tax** | **10%** | **178%** |
| | | |
| **Deferred tax recognised in the balance sheet** | | |
| Opening balance, deferred tax assets | 1 350 | 13 577 |
| Change due to reorganisation (transfer of business from Nordea) | - | 1 053 |
| Charged/ (credited) to other comprehensive income | 85 | - |
| Recognised in the income statement | (527) | (3 392) |
| Reversal of deferred tax | - | (9 888)* |
| **Closing balance, deferred tax assets** | **908** | **1 350** |

Taxation accounting principles are disclosed in Note G6.

* When the law came into force in Latvia in 2018, there were no longer any reason for the existence of a deferred tax asset or liability and in 2017 the Group eliminated previously recognized deferred tax asset of Latvian Luminor Bank AS from the balance sheet, including a reduction in that asset in the profit and loss account for the year 2017.

## G17: CASH AND BALANCES WITH CENTRAL BANKS

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Cash | 178 440 | 178 147 |
| | | |
| Balances in Central Banks in EUR | 3 095 653 | 2 442 691 |
| Balances in Central Banks in other currencies | - | - |
| **Total** | **3 095 653** | **2 442 691** |
| of which mandatory reserve requirement | 109 027 | 106 247 |
| | | |
| Term deposit | 18 997 | - |
| | | |
| **Total cash and balances with central banks** | **3 293 090** | **2 620 838** |

(all amounts are in EUR thousand, if not otherwise stated)

Required reserves held with Central banks are calculated according to reserve maintenance calendar announced by ECB. All required reserves are held only in EUR. Central banks in Lithuania, Latvia and Estonia do not pay interest for the required reserves.

As at 31 December 2018 term deposit of 18 997 thousand EUR was pledged for TLTRO (targeted longer-term refinancing operations) programme loan with Central Bank.

## G18: LOANS TO CREDIT INSTITUTIONS

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Demand deposits | 146 302 | 194 852 |
| Loans | 39 899 | 214 654 |
| **Total** | **186 201** | **409 506** |
| Allowances | (4) | - |
| **Total** | **186 197** | **409 506** |

## G19: LOANS TO THE PUBLIC

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Individual customers | 5 968 156 | 6 010 024 |
| Business customers | 5 635 637 | 5 890 449 |
| Financial institutions | 58 752 | 86 769 |
| **Total** | **11 662 545** | **11 987 242** |
| | | |
| Provision for probable loan losses | (190 407) | (306 345) |
| **Total loans to the public** | **11 472 138** | **11 680 897** |

Allowances for loans to the public are as follows:

| | Opening balance at 1 January 2018 | Changes in allowance for loan impairment | Derecognition | Write-off | Closing Balance at 31 december 2018 |
|---|---|---|---|---|---|
| | | | | | |
| **Loans and advances to financial institutions** | **238** | **(1 237)** | **33** | **-** | **(966)** |
| **Loans to business customers** | **(185 459)** | **(4 781)** | **7 582** | **89 871** | **(92 787)** |
| Loans | (156 023) | 833 | 3 987 | 77 218 | (73 985) |
| Factoring | (12 126) | -588 | 551 | 7 476 | (4 687) |
| Leasing | (17 310) | (5 026) | 3 044 | 5 177 | (14 115) |
| **Loans to individual customers** | **(121 037)** | **(4 344)** | **4 009** | **24 718** | **(96 654)** |
| Mortgage loans | (90 010) | (2 605) | 1 882 | 7 970 | (82 763) |
| Consumer and card loans | (3 249) | (1 284) | 271 | 1 074 | (3 188) |
| Other loans | (23 975) | -505 | 1 556 | 14 747 | (8 177) |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | | | |
|---|---|---|---|---|---|
| Leasing | (3 803) | 50 | 300 | 927 | (2 526) |
| **Loans to Customers Allowances** | **(306 258)** | **(10 368)** | **11 624** | **114 595** | **(190 407)** |

## G20: LEASES

| | Within one year | Between one and five years | Later than five years | Total |
|---|---|---|---|---|
| Gross investment | 650 582 | 1 476 046 | 50 201 | 2 176 829 |
| Present value of future minimum lease payments at balance sheet date | 33 150 | 57 541 | 1 493 | 92 184 |
| **Gross investment** | | | | |
| Balance as at 31 December 2017 | 460 932 | 1 686 543 | 44 988 | 2 192 463 |
| Change during 2018 | 189 650 | (210 497) | 5 213 | (15 634) |
| Balance as at 31 December 2018 | 650 582 | 1 476 046 | 50 201 | 2 176 829 |
| **Unearned finance income on finance leases** | | | | |
| Balance as at 31 December 2017 | 30 985 | 62 593 | 444 | 94 022 |
| Change during 2018 | 2 165 | (5 052) | 1 049 | (1 838) |
| Balance as at 31 December 2018 | 33 150 | 57 541 | 1 493 | 92 184 |
| **Net investments in finance leases before impairment** | | | | |
| Balance as at 31 December 2017 | 429 947 | 1 623 950 | 44 544 | 2 098 441 |
| Balance as at 31 December 2018 | 617 432 | 1 418 505 | 48 708 | 2 084 645 |

## G21: INTEREST-BEARING SECURITIES

| | Nominal amount 2018 | Carrying amount 2018 | Nominal amount 2017 | Carrying amount 2017 |
|---|---|---|---|---|
| Interest-bearing securities eligible as collateral with central banks | 57 119 | 57 577 | 161 734 | 164 202 |
| Bonds and other interest-bearing securities | 83 458 | 84 096 | - | - |
| **Total** | **140 577** | **141 673** | **161 734** | **164 202** |

## G22: EQUITY INSTRUMENTS

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Listed | 3 581 | 2 526 |
| Unlisted | 4 026 | 3 304 |
| **Total** | **7 607** | **5 830** |

## G23: INVESTMENT IN ASSOCIATES

| | 2018 | 2017 |
|---|---|---|
| Carrying amount at beginning of year | 6110 | - |
| Share of profit for the year | 860 | 384 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | |
|---|---|---|
| Dividends | (408) | - |
| Acquisitions | - | 5 566 |
| Divestments | (236) | - |
| Impairment | (70) | - |
| Reclasification | - | 160 |
| **Carrying amount at end of year** | **6 256** | **6 110** |

| 2018 | Domicile | No. of shares | % of share capital | % of voting power | Equity | Profit (loss) for the year | Book value |
|---|---|---|---|---|---|---|---|
| UAB ALD Automotive | LTL | 51 | 25 | 25 | 34 678 | 336 | 1 734 |
| ALD Automotive Eesti AS | EE | 25 606 | 25 | 25 | 5 523 | 209 | 1 509 |
| SIA ALD Automotive | LV | 950 | 25 | 25 | 112 754 | 332 | 2 923 |
| SIA Kredītinformācijas Birojs | LV | 2 653 | 22,6 | 22,6 | 836 | (90) | 90 |
| | | | | | | | **6 256** |

As a result of the acquisition of the shares of Luminor Lizingas, UAB in October 2017, the Group also acquired:

- 25% of the shares of ALD Automotive in each Baltic country which provides full service leasing and fleet management solutions.
- 22.6 % of the shares of AS “Kredītinformācijas Birojs" (KIB). AS “Kredītinformācijas Birojs" provides credit information for companies and individuals and risk management solutions. AS “Kredītinformācijas Birojs" is located in Latvia.

| 2017 | Domicile | No. of shares | % of share capital | % of voting power | Equity | Profit (loss) for the year | Book value |
|---|---|---|---|---|---|---|---|
| UAB ALD Automotive | LTL | 51 | 25 | 25 | 29 394 | 84 | 1 658 |
| ALD Automotive Eesti AS | EE | 25 606 | 25 | 25 | 4 524 | 723 | 1 465 |
| SIA ALD Automotive | LV | 950 | 25 | 25 | 11 369 | 1 946 | 2 827 |
| SIA Kredītinformācijas Birojs | LV | 2 653 | 22,6 | 22,6 | 853 | (532) | 160 |
| | | | | | | | **6 110** |

## G24: DERIVATIVE INSTRUMENTS

| | Nominal amount | Positive market values | Negative market values |
|---|---|---|---|
| **As at 31 December 2018** | | | |
| Derivatives held for trading | | | |
| Interest rate-related contracts | 3 020 308 | 10 237 | 9 425 |
| Currency-related contracts | 1 027 717 | 31 493 | 29 374 |
| Commodity-related contracts | 50 849 | 3 967 | 3 658 |
| **Total** | 4 098 874 | 45 697 | 42 457 |
| **As at 31 December 2017** | | | |
| Derivatives held for trading | | | |
| Interest rate-related contracts | 2 244 044 | 8 967 | 8 271 |
| Currency-related contracts | 1 391 815 | 16 809 | 22 990 |
| Commodity-related contracts | 28 070 | 1 977 | 1 912 |
| **Total** | 3 663 929 | 27 753 | 33 173 |

(all amounts are in EUR thousand, if not otherwise stated)

## HEDGING ACTIVITIES

### Fair value hedge

At 31 December 2018 the Group had 2 interest rate swap agreements in place with a notional amounts of EUR 200 000 000 and EUR 150 000 000 (2017: €Nil) whereby the Group receives a fixed rate of interest of 1.50% and pays floating interest at 6 months EURIBOR + 1.478% and 3 months EURIBOR + 1.526% on the notional amount respectively. The swaps are being used to hedge the exposure to changes in the fair value of its fixed rate 1.50% senior unsecured bond. Trade date is 10 October 2018, effective date is 18 October 2018 and maturity date is 18 October 2021 for both interest swap agreements.

There is an economic relationship between the hedged item and the hedging instruments as the terms of the interest rate swaps match the terms of the fixed rate loan (i.e. notional amount maturity payment and reset dates). The Group has established a hedge ratio of 1:1 for the hedging relationships, as the underlying risk of the interest rate swaps is identical to the hedged risk component. To test hedge effectiveness, the Group uses the hypothetical derivative method and compares the changes in the fair value of the hedging instrument against the changes in the fair value of the hedged item attributable to the hedged risk.

Hedge ineffectiveness can theoretically arise from:

- A different interest rate curve applied to discount the hedged item and hedging instrument
- Differences in the timing of cash flows of the hedged item and hedging instrument, also a different day count
- The counterparties' credit risk differently impacting the fair value movements of the hedging instrument and hedged item

## G25: INTAGIBLE ASSETS

| | Goodwill | Other intangible assets | Total |
|---|---|---|---|
| **Accumulated costs** | | | |
| **As at 16 August 2016** | **-** | **-** | **-** |
| Additions | 351 | 30 995 | 31 346 |
| Disposals | - | (1 032) | (1 032) |
| **As at 31 December 2017** | **351** | **29 963** | **30 314** |
| Additions | - | 3 956 | 3 956 |
| Disposals | - | (4 589) | (4 589) |
| **As at 31 December 2018** | **351** | **29 330** | **29 681** |
| **Accumulated amortization and impairments**<br>**As at 16 August 2016** | | | |
| Accumulated amortization | - | (20 615) | (20 615) |
| Disposals | - | (442) | (442) |
| **As at 1 December 2017** | **-** | **(21 057)** | **(21 057)** |
| Accumulated amortization | - | (2 438) | (2 438) |
| Disposals | - | 3 565 | 3 565 |
| Impairment for the year* | - | (2 337) | (2 337) |
| **As at 31 December 2018** | **-** | **(22 267)** | **(22 267)** |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | |
|---|---|---|---|
| Carrying amount at 31 December 2017 | 351 | 8 906 | 9 257 |
| Carrying amount at 31 December 2018 | 351 | 7 063 | 7 414 |

| | | | |
|---|---|---|---|
| **Acquisition cost fully depreciated assets still in use** | | | |
| at 31 December 2017 | - | 4 387 | 4 387 |
| at 31 December 2018 | - | 5 625 | 5 625 |

In 2018, based on the estimated expected future cash flows, the Group recorded impairment losses amounted to EUR 2,3 million to intangible assets.

## G26: PROPERTY, PLANT, AND EQUIPMENT

| | Property | Equipment | Total |
|---|---|---|---|
| **Accumulated costs as at 16 August 2016** | - | - | - |
| Additions | 47 593 | 43 315 | 90 908 |
| Disposals | (4 232) | (3 884) | (8 116) |
| **As at 31 December 2017** | **43 361** | **39 431** | **82 792** |
| Additions | 548 | 3 439 | 3 987 |
| Disposals | (1 480) | (6 788) | (8 268) |
| Reclassification to held for sale | (28 448) | - | (28 448) |
| **As at 31 December 2018** | **13 981** | **36 082** | **50 063** |
| | | | |
| **Accumulated amortization and impairments** | | | |
| **As at 16 August 2016** | - | - | - |
| Accumulated amortization | (15 030) | (31 085) | (46 115) |
| Impairment for the year | 362 | 2 306 | 2 668 |
| Disposals | 1 419 | (282) | 1 137 |
| **As at 31 December 2017** | **(13 249)** | **(29 061)** | **(42 310)** |
| Accumulated amortization | (1 350) | (4 972) | (6 322) |
| Impairment for the year | (8) | (20) | (28) |
| Disposals | 1 308 | 7 791 | 9 099 |
| Reclassification to held for sale | 5 881 | 0 | 5 881 |
| **As at 31 December 2018** | **(7 418)** | **(26 262)** | **(33 680)** |
| | | | |
| Carrying amount at at at 31 December 2017 | 30 112 | 10 370 | 40 482 |
| Carrying amount at at at 31 December 2018 | 6 563 | 9 820 | 16 383 |
| **Acquisition cost fully depreciated assets still in use** | | | |
| at 31 December 2017 | 1 588 | 29 727 | 31 315 |
| at 31 December 2018 | 1 762 | 8 357 | 10 119 |

(all amounts are in EUR thousand, if not otherwise stated)

## G27: INVESTMENT PROPERTIES

The investment properties are stated at fair value. The Group's management determines the policies and procedures for fair value measurement. External valuators are involved for significant valuations. Involvement of external valuers is decided upon annually. The management analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed in line with the Group's accounting policies at least once a year. For this analysis, the management verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to contracts and other relevant documents. The management, in conjunction with the Group's internal and external valuators, also compares each of the changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable. For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

The valuation model for the Group's investment properties was formed based on the market comparable approach method. Under the market comparable approach, the fair value of property is estimated based on comparable transactions. The market comparable approach is based upon the principle of substitution under which a potential buyer will not pay more for the property than it will cost to buy a comparable substitute property. The unit of comparison applied by the Group is the price per square metre (sqm). Valuations of investment property were performed as at 31 December 2018. There were reclassifications of investment property made between levels during 2018 and no reclassifications during 2017. All investment property that was revalued based on the comparable approach method with no significant adjustments to observable prices is clasified as Level 2, the rest of the investment property that was revalued using the comparable approach method with significant adjustments to observable prices and income approach is clasified as Level 3.

| | 2018 | 16.08.2016 – 31.12 2017 |
|---|---|---|
| **As at 1 January** | **51 283** | **-** |
| Acquisitions | 216 | 110 041 |
| Assets classified as held for sale | (3 960) | (3 697) |
| Net result from adjustments of fair value | (3 722) | (16 933) |
| Reclassifications to and from real estate used in business operations | - | 1 283 |
| Disposals (sale) | (19 847) | (39 411) |
| | | |
| **Carrying amount at the end of the year** | **23 970** | **51 283** |
| | | |
| **Amounts recognized in profit or loss** | | |
| Rental income | 349 | 1 532 |
| Direct operating expenses for investment properties that generated rental income during the period | (246) | (1 046) |
| Direct operating expensens for investment properties that did not generated rental income during the period | (1 659) | (1 118) |
| Changes in fair value | (2 923) | (9 841) |
| **Total** | **(4 479)** | **(10 473)** |

(all amounts are in EUR thousand, if not otherwise stated)

## RECONCILIATION OF BALANCES OF CLASSES OF INVESTMENT PROPERTY:

| | Land plots | Buildings residential | Buildings commercial and other | Total 2017 |
|---|---|---|---|---|
| **Book value as at 16 August 2016** | - | - | - | - |
| Additions, purchases of new properties | 34 746 | 46 674 | 28 621 | **110 041** |
| Reclassifications from property plant and equipment | 1 008 | - | 275 | **1 283** |
| Classified as held for sale | (1 773) | (1 314) | (610) | **(3 697)** |
| Net result from adjustment to fair value projects | (8 784) | (5 710) | (2 439) | **(16 933)** |
| Disposal | (7 511) | (13 793) | (18 107) | **(39 411)** |
| **Book value as at 31 December 2017** | **17 686** | **25 857** | **7 740** | **51 283** |

| | Land plots | Buildings residential | Buildings commercial and other | Total 2018 |
|---|---|---|---|---|
| **Book value as at 31 December 2017** | **17 686** | **25 857** | **7 740** | **51 283** |
| Additions, purchases of new properties | 132 | 72 | - | **204** |
| Additions, capitalised investments | 7 | 5 | - | **12** |
| Movement between classes of investment property | 496 | 1 810 | (2 306) | - |
| Classified as held for sale | (3 191) | (651) | (118) | **(3 960)** |
| Net result from adjustment to fair value projects | (2 470) | (1 413) | 161 | **(3 722)** |
| Disposal | (4 166) | (14 520) | (1 161) | **(19 847)** |
| **Book value as at 31 December 2018** | **8 494** | **11 160** | **4 316** | **23 970** |

## RECONCILIATION OF BALANCES OF CLASSES OF INVESTMENT PROPERTY BY LEVELS:

| | Land plots | | Buildings | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Other Level 2 | Other Level 3 | Commer-cial Level 2 | Residen-tial Level 2 | Commer-cial Level 3 | Residen-tial Level 3 | Other Level 2 | Other Level 3 | Total 2017 |
| **Book value as at 16 August 2016** | - | - | - | - | - | - | - | - | - |
| Acquisitions | 466 | 34 280 | - | 1 650 | 28 481 | 45 024 | - | 140 | 110 041 |
| Reclassifications from property plant and equipment | - | 1 008 | - | - | 275 | - | - | - | 1 283 |
| Reclassifications from/to other Level | 173 | (173) | - | 915 | - | (915) | - | - | - |
| Disposals (sale) | - | (7 511) | - | (68) | (18 107) | (13 725) | - | - | (39 411) |
| Classified as held for sale | - | (1 773) | - | - | (560) | (1 314) | - | (50) | (3 697) |
| Net gains (loss) resulting from adjustment to fair value | (43) | (8 741) | - | (82) | (2 388) | (5 628) | - | (51) | (16 933) |
| **Book value as at 31 December** | **596** | **17 090** | **-** | **2 415** | **7 701** | **23 442** | **-** | **39** | **51 283** |

(all amounts are in EUR thousand, if not otherwise stated)

| | Land plots | | Buildings | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Other Level 2 | Other Level 3 | Commer-cial Level 2 | Residen-tial Level 2 | Commer-cial Level 3 | Residen-tial Level 3 | Other Level 2 | Other Level 3 | Total 2018 |
| **Book value as at 1 January** | **596** | **17 090** | **-** | **2 415** | **7 701** | **23 442** | **-** | **39** | **51 283** |
| Acquisitions | - | 132 | - | - | - | 72 | - | - | 204 |
| Additions, capitalised investments | - | 7 | - | - | - | 5 | - | - | 12 |
| Reclassifications from/to other Level | 1 037 | (1 037) | 176 | 678 | (176) | (678) | 79 | (79) | - |
| Movement between classes of investment property | - | 496 | - | - | (2 306) | 1 810 | - | - | - |
| Disposals (sale) | (206) | (3 960) | - | (1 574) | (1 161) | (12 946) | - | - | (19 847) |
| Classified as held for sale | (23) | (3 168) | - | (222) | (168) | (429) | - | 50 | (3 960) |
| Net gains (loss) resulting from adjustment to fair value | (86) | (2 384) | - | (80) | 171 | (1 333) | - | (10) | (3 722) |
| **Book value as at 31 December** | **1 318** | **7 176** | **176** | **1 217** | **4 061** | **9 943** | **79** | **-** | **23 970** |

## G28: OTHER ASSETS

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Prepayments and receivables | 29 889 | 24 617 |
| Deferred expenses - IT | 2 856 | 1 429 |
| Accrued income (for banking services) | 1 638 | 2 407 |
| Transit accounts | 11 894 | 14 110 |
| VAT recoverable | 635 | 409 |
| Repossessed assets and prepaid expenses of leasing contracts | 5 741 | 6 605 |
| Taxes | - | 2 138 |
| Other prepaid expences and accrued income | 2 716 | 1 307 |
| Guarantee deposits for auctions and prepayments for investment property | 4 779 | - |
| Credit card claims and other payment services | 12 551 | 10 650 |
| Other | 3 397 | 4 265 |
| **Total** | **76 096** | **67 937** |

(all amounts are in EUR thousand, if not otherwise stated)

## G29: NON-CURRENT ASSETS AND DISPOSAL GROUPS HELD FOR SALE

| | Land plots | | Buildings | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Other Level 2 | Other Level 3 | Commer-cial Level 2 | Residen-tial Level 2 | Commer-cial Level 3 | Residen-tial Level 3 | Other Level 2 | Other Level 3 | Total 2017 |
| **Book value as at 16 August 2016** | **-** | **-** | **-** | **-** | **-** | **-** | **-** | **-** | **-** |
| Acquisitions | - | 940 | 3 500 | 269 | 5 861 | 320 | - | - | 10 890 |
| Reclassifications from/to investment property | - | 388 | - | - | 556 | 40 | - | 50 | 1 034 |
| Disposals (sale) | - | (937) | (3 500) | - | (3 201) | (320)- | - | - | (7 958) |
| **Book value as at 31 December** | **-** | **391** | **-** | **269** | **3 216** | **40** | **-** | **50** | **3 966** |

| | Land plots | | Buildings | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Other Level 2 | Other Level 3 | Commer-cial Level 2 | Residen-tial Level 2 | Commer-cial Level 3 | Residen-tial Level 3 | Other Level 2 | Other Level 3 | Total 2018 |
| **Book value as at 1 January** | **-** | **391** | **-** | **269** | **3 216** | **40** | **-** | **50** | **3 966** |
| Reclassifications from investment property | 23 | 3 168 | - | 127 | 168 | 524 | - | - | 4 010 |
| Reclassifications from property plant and equipment | - | - | - | - | 22 567 | - | - | - | 22 567 |
| Reclassifications from/to other Level | 2 176 | (2 176) | 72 | 177 | (72) | (177) | - | - | - |
| Disposals (sale) | (23) | (1 382) | - | (367) | (3 110) | (271) | - | (50)- | (5 203) |
| Net gains (loss) resulting from adjustment to fair value | - | (1) | 72 | 206 | 8 | - | - | - | 7 |
| **Book value as at 31 December** | **2 176** | **-** | **72** | **206** | **22 777** | **116** | **-** | **-** | **25 347** |

## G30: DUE TO CREDIT INSTITUTIONS

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Term deposits | 3 917 244 | 4 690 165 |
| Demand deposits | 22 152 | 71 077 |
| **Total** | **3 939 396** | **4 761 242** |

## G31: DEPOSITS AND BORROWING FROM THE PUBLIC

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Term deposits | 1 932 891 | 1 390 014 |
| Demand deposits | 7 136 994 | 7 039 782 |
| **Total** | **9 069 885** | **8 429 796** |

(all amounts are in EUR thousand, if not otherwise stated)

## G32: DEBT SECURITIES ISSUED

In October 2018 Luminor Bank AS issued its inaugural bond under the Luminor Euro Medium Term Notes (EMTN) program. The company issued EUR 350 000 000 of fixed-rate bonds maturing October 2021 with annual coupons and bearing interest at an annual rate of 1.50%. There were no specific covenants related to the bond issuance. The amortised cost of debt securities issued amounts to 349 333 thousand EUR as at 31 December 2018.

Luminor Bank AS has completed the first bond issue during Q4 2017. The company issued senior bond on 20 December 2017 in amount of 65 000 thousand EUR at a rate of 0.33% per annum, with term of 2 years. There were no specific covenants related to the bond issuance. These bonds were redeemed in whole on 03 October 2018 on terms and subject to the conditions contained in the “Terms and Conditions of the Notes” (Clause 15) dated 15 December 2017.

| | 2018 | 2017 |
|---|---|---|
| **Bond 2** | **349 333** | **-** |
| **Bond 1** | **-** | **65 007** |

## G33: PROVISIONS

| | Loan commitments and guarantee commitments | Legal disputes | Restructuring | Other | Total |
|---|---|---|---|---|---|
| **31 December 2017** | 757 | 123 | 1 000 | 266 | 2 146 |
| Changes on initial application of IFRS9 | 4 033 | - | - | - | 4 033 |
| Provisions during the year | 2 087 | - | 1 138 | 10 | 3 235 |
| Amortised | (2 316) | (30) | (1 022) | (132) | (3 500) |
| **31 December 2018** | | | | | |
| **Total** | **4 561** | **93** | **1 116** | **144** | **5 914** |
| Current (less than one year) | 2 458 | 93 | 1 116 | 144 | 3 811 |
| Non-current (more than one year) | 2 103 | - | - | - | 2 103 |
| **Total** | **4 561** | **93** | **1 116** | **144** | **5 914** |

Provisions on off-balance sheet loan commitments and guarantees under IFRS 9 by stages as at the end of the period are as follows:

| | Stage 1 | Stage 2 | Stage 3 | Total |
|---|---|---|---|---|
| **As at 1 January 2018** | **657** | **100** | **-** | **757** |
| Changes on initial application of IFRS 9 | 2 874 | 343 | 816 | 4 033 |
| Increase in provisions | 1 818 | 187 | 82 | 2 087 |
| Amortised | (3 890) | 2 170 | (596) | (2 316) |
| **As at 31 December 2018** | **1 459** | **2 800** | **302** | **4 561** |

(all amounts are in EUR thousand, if not otherwise stated)

The movement of provisions as at 2017 was as follows:

| | Loan commitments and guarantee commitments | Legal disputes | Restructuring | Other | Total |
|---|---|---|---|---|---|
| **As at 16 August 2016** | - | - | - | - | - |
| Provisions during the year | 757 | 321 | 1 000 | 44 051* | 46 129 |
| Amortised | - | (198) | - | (43 412)** | (43 610) |
| Written back | - | - | - | (373) | (373) |
| **Total as at 31 December 2017** | **757** | **123** | **1 000** | **266** | **2 146** |
| Current (less than one year) | 238 | - | 1 000 | 266 | 1 504 |
| Non-current (more than one year) | 519 | 123 | - | - | 642 |
| **Total** | **757** | **123** | **1 000** | **266** | **2 146** |

*The major part comprise of provisions for onerous contracts related to IT systems.

** Netted with advance payment made according the updated IT licence agreement.

## G34: OTHER LIABILITIES

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Transit accounts (for payments of loans) | 14 208 | 21 971 |
| Transit accounts | 6 724 | 1 221 |
| Payables | 17 238 | 9 063 |
| Advance payment | 7 718 | 5 566 |
| Prepayments from leasing customers | 5 309 | 8 418 |
| Taxes | 1 624 | 144 |
| Invoices to be paid | 635 | 1 759 |
| Credit card transactions | 2 021 | 467 |
| Other liabilities | 2 487 | 4 426 |
| **Total** | **57 964** | **53 035** |

## G35: ACCRUED EXPENSES AND DEFERRED INCOME

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Accrued expenses for unused annual leave and bonuses | 17 158 | 14 386 |
| Accrued unearned finance income on finance leases | 2 525 | 1 040 |
| Operating costs | 3 107 | 2 699 |
| Accrued expenses - IT | 4 448 | 2 231 |
| Accrued expenses - other not received invoices | 2 392 | 1 568 |
| Accrued expenses for Stability fee payments | 576 | 1 469 |
| Accrued expenses -projects | 501 | 877 |
| Accrued expenses for payments to deposit guarantee fund and Finance and Capital Market Comission | 983 | 884 |
| Deferred income | 145 | 49 |
| Other accrued expenses | 4 307 | 6 894 |
| **Total** | **36 142** | **32 097** |

(all amounts are in EUR thousand, if not otherwise stated)

## G36: RESERVES

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Fair value changes on financial assets at fair value through other comprehensive income | 3 276 | 1 680 |
| Other reserves | 234 | 234 |
| **Total** | **3 510** | **1 914** |

## G37: PLEDGED ASSETS AND CONTINGENT LIABILITIES

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| **Pledged assets** | | |
| Loans granted to governmental institutions | 132 138 | 187 737 |
| Debt securities | 110 982 | 237 017 |
| **Total** | **243 120** | **424 754** |
| | | |
| **Contingent liabilities** | | |
| Loan commitments given | 1 304 189 | 1 268 804 |
| Financial guarantees given | 406 037 | 469 578 |
| Other commitments given | 274 038 | 505 412 |
| **Total** | **1 984 264** | **2 243 794** |

As at 31 December 2018, Funds of Central Bank (EUR 173 000 thousand) contain proceeds from the ECB under targeted longer-term refinancing operations (TLTROs)( 31 December 2017 EUR 300 000). The carrying amount of pledged assets under this agreement amounted to EUR 243 120 thousand (EUR 132 138 thousand loans granted to governmental institutions, EUR 110 982 thousand acquired central government bonds). *)(* 31 December 2017 EUR 187 737 thousand loans granted to governmental institution, EUR 237 017 thousand acquired central government bonds ).

**Legal claims**. As at 31 December 2018, contingent liabilities that may arise as a result of pending court proceedings in which the Bank would appear as a respondent amounted to EUR 10 207 thousand (2017: EUR 5 545 thousand), of which EUR 1 100 thousand (2017: EUR 1 100 thousand) for legal claims related to group of (ex-Nordea Bank) customers claim (regarding modification of mortgage loan agreements under which loans were issued in Swiss Francs and commitment to calculate negative interest), the Bank does not see the need for provisions for this case as the risk is remote and EUR 1 184 thousand (2017: EUR 1 679 thousand) for legal claims related to index linked bonds and 7 923 thousand (2017: EUR 2 766 thousand) for other legal claims. The Bank established a provision of EUR 93 thousand (2017: EUR 123 thousand) against potential losses in relation to the outcome of legal claims.

(all amounts are in EUR thousand, if not otherwise stated)

## G38: CLASSIFICATION OF FINANCIAL INSTRUMENTS

Classification of financial instruments as at 31 December 2018 was as follows:

| | At fair value through profit/loss | | Financial assets at amortised cost | At fair value through other comprehensive income | Financial liabilities measured at amortised cost | Total carrying amount |
|---|---|---|---|---|---|---|
| | Trading | Other | | | | |
| **Assets** | | | | | | |
| Cash and balances with Central Banks | - | - | 3 293 090 | - | - | 3 293 090 |
| Loans to credit institutions | - | - | 186 197 | - | - | 186 197 |
| Loans to public | - | - | 11 472 138 | - | - | 11 472 138 |
| Bonds and other interest-bearing securities | 1 006 | 139 402 | - | 1 265 | - | 141 673 |
| Equity instruments | - | - | - | 7 607 | - | 7 607 |
| Investments in managed pension funds | - | 4 356 | - | - | - | 4 356 |
| Derivative instruments | 45 536 | 161 | - | - | - | 45 697 |
| **Total financial assets** | **46 542** | **143 919** | **14 951 425** | **8 872** | **-** | **15 150 758** |
| **Liabilities** | | | | | | |
| Due to credit institutions | - | - | - | - | 3 939 396 | 3 939 396 |
| Deposits and borrowing from the public | - | - | - | - | 9 069 885 | 9 069 885 |
| Debt securities issued | - | - | - | - | 349 333 | 349 333 |
| Derivative instruments | 42 457 | - | - | - | - | 42 697 |
| **Total financial liabilities** | **42 457** | **-** | **-** | **-** | **13 358 614** | **13 401 071** |

Classification of financial instruments as at 31 December 2017 was as follows:

| | At fair value through profit/loss | | Investments held to maturity | Loans and receivables | Financial assets available for sale | Financial liabilities measured at amortised cost | Total carrying amount |
|---|---|---|---|---|---|---|---|
| | Trading | Other | | | | | |
| **Assets** | | | | | | | |
| Cash and balances with Central Banks | - | - | - | 2 620 838 | - | - | 2 620 838 |
| Loans to credit institutions | - | - | - | 409 506 | - | - | 409 506 |
| Loans to public | - | - | 1 513 | 11 679 384 | - | - | 11 680 897 |
| Bonds and other interest-bearing securities | 2 325 | 161 877 | - | - | - | - | 164 202 |
| Equity instruments | - | 18 | - | - | 5 812 | - | 5 830 |
| Investments in managed pension funds | - | 4 526 | - | - | - | - | 4 526 |
| Derivative instruments | 27 753 | - | - | - | - | - | 27 753 |
| **Total financial assets** | **30 078** | **166 421** | **1 513** | **14 709 728** | **5 812** | **-** | **14 913 552** |
| **Liabilities** | | | | | | | |
| Due to credit institutions | - | - | - | - | - | 4 761 243 | 4 761 243 |
| Deposits and borrowing from the public | - | - | - | - | - | 8 429 796 | 8 429 796 |
| Debt securities issued | - | - | - | - | - | 65 007 | 65 007 |
| Derivative instruments | 33 173 | - | - | - | - | - | 33 173 |
| **Total financial liabilities** | **33 173** | **-** | **-** | **-** | **-** | **13 256 046** | **13 289 219** |

(all amounts are in EUR thousand, if not otherwise stated)

## G39: FAIR VALUE MEASUREMENT OF FINANCIAL INSTRUMENTS

Fair value measurement of financial instruments measured at fair value as at 31 December 2018 was as follows:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **Financial assets held for trading** | | | | |
| Derivative instruments | - | 45 536 | - | 45 536 |
| Debt securities | 1 006 | - | - | 1 006 |
| **Total** | **1 006** | **45 536** | **-** | **46 542** |
| | | | | |
| **Financial assets designated at fair value through profit or loss** | | | | |
| Debt securities | 83 192 | 56 210 | - | 139 402 |
| **Total** | **83 192** | **56 210** | **-** | **139 402** |
| | | | | |
| **Non-trading financial assets mandatorily at fair value through profit or loss** | | | | |
| Investments in managed pension funds | - | 4 356 | - | 4 356 |
| **Total** | **-** | **4 356** | **-** | **4 356** |
| | | | | |
| **Financial assets at fair value through other comprehensive income** | | | | |
| Debt securities | 1 265 | - | - | 1 265 |
| Shares | - | - | 7 607 | 7 607 |
| **Total** | **1 265** | **-** | **7 607** | **8 872** |
| **Financial liabilities held for trading** | | | | |
| Derivative instruments | - | 42 457 | - | 42 457 |
| **Total** | **-** | **42 457** | **-** | **42 457** |

Fair value measurement of financial instruments as at 31 December 2017 was as follows:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **Financial assets held for trading** | | | | |
| Derivative instruments | - | 27 753 | - | 27 753 |
| Debt securities | 2 325 | - | - | 2 325 |
| **Total** | **2 325** | **27 753** | **-** | **30 078** |
| | | | | |
| **Financial assets designated at fair value through profit or loss** | | | | |
| Equity instruments | - | 4 526 | 18 | 4 544 |
| Debt securities | 85 568 | 76 309 | - | 161 877 |
| Loans and advances | - | - | - | - |
| **Total** | **85 568** | **80 835** | **18** | **166 421** |
| **Financial assets at fair value through other comprehensive income** | | | | |
| Equity instruments | - | - | 5 812 | 5 812 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | | |
|---|---|---|---|---|
| **Total** | **-** | **-** | **5 812** | **5 812** |
| **Financial liabilities held for trading** | | | | |
| Derivative instruments | - | 33 173 | - | 33 173 |
| **Total** | **-** | **33 173** | **-** | **33 173** |

Financial instruments are distributed by 3 levels of the fair value:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities.
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable.
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

The fair value of all Bank contracted derivatives is defined as level 2. These are interest rate swaps and in all cases pricing is based on market observable inputs. For assets and liabilities that are recognized at fair value on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period. There were no movement of securities between the levels during 2018.

There were no movements of financial instruments between the levels during 2018 and 2017.

The carrying amount of shares on level 3 consists of Visa Inc. and Swift shares with fair value changes recognised in other comprehensive income. The significant unobservable inputs used in the fair value measurement of shares on level 3 are as follows: conversion rate, trading price, liquidity discount. The table below shows the changes in the fair value of securities from a 10% increase or decrease respectively in the liquidity discount, all other inputs being constant.

| | **Impact of change of liquidity discount** | |
|---|---|---|
| | **increase +10%** | **decrease -10%** |
| Increase / (decrease) in fair value as at December 31, 2018 | 952 | (952) |

**Change in financial instruments in level 3:**

| | **Shares 2018** | **Shares 2017** |
|---|---|---|
| Beginning balance | 5 830 | - |
| Additions | 1 130 | 5 830 |
| Disposals | - | - |
| Unrealised gains/losses for assets held at the end of the reporting period | 647 | - |
| **Closing balance** | **7 607** | **5 830** |

Non-trading financial assets mandatorily at fair value through profit or loss (Pension Funds) - The value date method is used in the acquisition of pension fund units managed by Luminor Pensions Estonia AS and they are initially recognised at acquisition cost, which is the fair value paid for them. Pension fund units are revalued according to the effective net asset value on the balance sheet date.

(all amounts are in EUR thousand, if not otherwise stated)

**Principles for information about the fair values of financial instruments which are carried at amortised cost**

For assets and liabilities not carried at fair value book value is estimated to be a reasonable approximation of fair value. Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgment is required to establish fair values.

The fair value of loans to customers, customer deposits, amounts due from credit institutions and amounts due to credit institutions and other financial assets and liabilities, obligations under finance leases is estimated by discounting future cash flows using rates currently available for debt on similar terms, credit risk and remaining maturities.

In assessing the fair value for financial assets, the management has performed discounted cash flow analysis; up-to-date market information at assessment moment is being used for assessing cash flows. For loans, where base interest rates are pegged to floating market interest rates, the Group has considered difference between average interest margin of issued loans and average interest margin for newly issued loans. Given that for part of the loan portfolio this margin has not been changed (increased) since issuance, the Group has estimated that for such loans the carrying value is considered equal to fair value.

Fair value of financial liabilities at amortized cost such as Loans and deposits from credit institutions and Deposits from customers which are not on demand have been estimated based on discounted cash flow model using interest rates for similar products as at period end. Fair value of those financial liabilities that are on demand or have floating interest rate have been estimated to be approximately equal to its carrying amount.

The table below summarizes the fair values of financial assets and liabilities recognized at amortized cost in the statement of financial position instruments:

| | Level 1 | Level 2 | Level 3 | Total | Carrying value |
|---|---|---|---|---|---|
| **As at 31 December 2018** | | | | | |
| **Assets** | | | | | |
| Loans to credit institutions | - | 67 264 | 118 933 | **186 197** | **186 197** |
| Loans to the public | - | - | 11 484 286 | **11 484 286** | **11 472 138** |
| **Liabilities** | | | | | |
| Due to credit institutions | - | - | 3 906 454 | **3 906 454** | **3 939 396** |
| Financial liabilities at amortised cost | - | - | 9 098 414 | **9 098 414** | **9 069 885** |
| Debt securities issued | | 349 333 | | 349 333 | 349 333 |
| **As at 31 December 2017** | | | | | |
| **Assets** | | | | | |
| Loans to credit institutions | **-** | 204 910 | 204 596 | **409 506** | **409 506** |
| Loans to the public | **-** | - | 11 538 838 | **11 538 838** | **11 680 897** |
| **Liabilities** | | | | | |
| Due to credit institutions | - | - | 4 772 381 | **4 772 381** | **4 761 243** |
| Financial liabilities at amortised cost | - | - | 8 429 462 | **8 429 462** | **8 429 796** |
| Debt securities issued | | | 65 007 | **65 007** | **65 007** |

(all amounts are in EUR thousand, if not otherwise stated)

## G40: RELATED PARTY DISCLOSURES

The following Group's balances were outstanding with ultimate owners (DnB and Nordea) related companies:

| | Ultimate companies 2018 | Ultimate companies 2017 |
|---|---|---|
| **Assets** | | |
| Loans to credit institutions | 172 634 | 386 057 |
| Loans to the public | 0 | 12 |
| Derivative instruments | 32 946 | 16 094 |
| Other assets | 567 | 224 |
| **Total** | **206 147** | **402 387** |
| **Liabilities** | | |
| Due to credit institutions | 3 714 129 | 4 281 983 |
| Deposits and borrowing from the public | - | 2 658 |
| Derivative instruments | 16 851 | 15 144 |
| Other liabilities | 2 447 | 1 855 |
| **Total** | **3 733 427** | **4 301 640** |
| | | |
| **Income and expenses** | | |
| Interest income | 14 230 | 8 544 |
| Interest expenses | (10 251) | (5 380) |
| Net commission and fee income | (10) | (241) |
| Other income | 3 826 | 956 |
| Other expenses | (8 383) | (8 900) |
| **Total** | **(588)** | **(5 021)** |

There are no intragroup provision for doubtful debts and no intragroup doubtful debts expenses.

Payments to management are disclosed in Note P4.

As at 31 December 2018 loans and advances with asociate ALD Automotive amounted to 13 401 thousand EUR, Deposits - 154 thousand EUR, interest income - 21 thousand EUR and interest expenses - 71 thousands EUR.

## G41: LIQUIDITY RISK

The strucutre of Group's assets and liabilities by remaining maturity as at 31 December 2018 were as follows:

| | within three months | 3 to 6 months | 6 to 9 months | 9 to 12 months | More than 12 months | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and balances with central banks | 3 274 291 | - | - | - | 18 799 | 3 293 090 |
| Loans (to credit institutions and to the public) | 605 820 | 678 599 | 567 414 | 497 542 | 9 308 960 | 11 658 335 |
| Debt securities | 29 041 | 13 156 | 2 295 | 6 721 | 90 460 | 141 673 |

(all amounts are in EUR thousand, if not otherwise stated)

| | | | | | | |
|---|---|---|---|---|---|---|
| Equity instruments | - | - | - | - | 7 607 | 7 607 |
| Investments in managed pension funds | - | - | - | - | 4 356 | 4 356 |
| Derivative instruments | 6 096 | 4 096 | 3 493 | 5 347 | 26 665 | 45 697 |
| **Total assets** | **3 915 248** | **695 851** | **573 202** | **509 610** | **9 456 847** | **15 150 758** |
| **Liabilities** | | | | | | |
| Deposits and borrowing (from credit institutions and from the public) | 8 622 423 | 97 904 | 678 998 | 2 828 855 | 781 101 | 13 009 281 |
| Debt securities issued | - | - | - | - | 349 333 | 349 333 |
| Derivative instruments | 3 159 | 2 609 | 2 104 | 4 201 | 30 384 | 42 457 |
| **Total liabilities** | **8 625 582** | **100 513** | **681 102** | **2 833 056** | **1 160 818** | **13 401 071** |

The strucutre of Group's assets and liabilities by remaining maturity as at 31 December 2017 were as follows:

| | within three months | 3 to 6 months | 6 to 9 months | 9 to 12 months | More than 12 months | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and balances with central banks | 2 620 838 | - | - | - | - | 2 620 838 |
| Loans (to credit institutions and to the public) | 1 440 096 | 614 836 | 681 098 | 393 817 | 8 960 556 | 12 090 403 |
| Debt securities | 32 137 | 137 | 98 | 15 020 | 116 810 | 164 202 |
| Equity instruments | - | - | - | - | 5 830 | 5 830 |
| Investments in managed pension funds | - | - | - | - | 4 526 | 4 526 |
| Derivative instruments | 3 473 | 923 | 1 207 | 1 715 | 20 435 | 27 753 |
| **Total assets** | **4 096 544** | **615 896** | **682 403** | **410 552** | **9 108 157** | **14 913 552** |
| **Liabilities** | | | | | | |
| Deposits and borrowing (from credit institutions and from the public) | 8 146 278 | 736 288 | 1 719 941 | 599 687 | 1 988 845 | 13 191 039 |
| Debt securities issued | - | - | - | - | 65 007 | 65 007 |
| Derivative instruments | 7 227 | 1 834 | 854 | 1 483 | 21 775 | 33 173 |
| **Total liabilities** | **8 153 505** | **738 122** | **1 720 795** | **601 170** | **2 075 627** | **13 289 219** |

## G42: SUBSEQUENT EVENTS

On 2 January 2019 Luminor completed its cross-border merger and continues its operations in all Baltic countries through the Estonian registered bank and its branches in Latvia and Lithuania. After the completion of the merger all assets, rights and liabilities of Luminor Latvia and Luminor Lithuania were transferred to Luminor Bank AS in Estonia. The bank will continue the same activities in Latvia and Lithuania through its locally established branches.

Starting from 2 January 2019 the deposits and financial instruments of the depositors and investment services clients of Luminor Bank AS Latvian branch and Luminor Bank AS Lithuanian branch will be guaranteed by the deposit guarantee and investor protection scheme established and operated by the Estonian Guarantee Fund.

As of 2 January 2019, after completion of the merger, Luminor has a new organizational set up, a new governance structure and new members of management bodies. Erkki Raasuke will continue as Luminor 's CEO and Nils Melngailis will be chairing the supervisory board.

# PARENT COMPANY NOTES

## P1: APPLIED ACCOUNTING POLICIES

The Parent Company's annual report is prepared in accordance with the Swedish Annual Accounts Act (1995:1554) and with application of the Swedish Financial Reporting Boards RFR 2 Accounting for legal entities. This means that the IFRS valuation and disclosure rules are applied, with certain exceptions and additions, depending on legal provisions, mainly in the Swedish Annual Accounts Act, and also on the link between accounting and taxation. The differences between the Group's and the Parent Company's accounting policies are show below.

### Classification

Fixed assets, long-term liabilities and provisions principally consist of amounts that are expected to be realized (recovered) or paid more than 12 months after the balance sheet date. Current assets and current liabilities principally consist of amounts that are expected to be realized (recovered) or paid within 12 months of the balance sheet date.

### Shares in subsidiaries

Shares in subsidiaries are recognized in the Parent Company according to the cost method, which means that transaction costs are included in the carrying amount.

### Shareholders' contribution

Shareholder contributions are recognized directly against equity by the recipient and capitalized in shares and units.

### Current financial assets

Current financial assets are valued according to the lower of cost or market principle.

### Untaxed reserves

The tax legislation in Sweden permits provisions in individual companies for special reserves and funds. This means that within certain limits, companies may allocate and retain recognized profits in the operations without immediate taxation. These untaxed reserves are only subject to taxation when they are liquidated. However, in the consolidated financial statement untaxed reserves are divided into deferred tax liabilities and equity.

### Group contributions received and paid

Group contributions received from subsidiaries are recognized as financial income. Group contributions paid by the Parent Company to a subsidiary are recognized as an increase in participations in Group companies.

Group contributions received by subsidiaries from the Parent Company are recognized in the subsidiary in equity. Group contributions paid by subsidiaries to the Parent Company are recognized in equity.

Group contributions received from associated companies are recognized in equity. Group contributions paid to associated companies are also recognized in equity in the subsidiary.

(all amounts are in EUR thousand, if not otherwise stated)

## P2: NET SALES

Net sales are made up entirely of internal Group invoicing, referring to administrative services.

## P3: OTHER EXTERNAL EXPENSES

| | 2018 | 2017 |
|---|---|---|
| Consultancy costs | (2 010) | (6 365) |
| Auditors fee | (51) | (111) |
| Management fee | (9) | (120) |
| Other | (475) | (3 696) |
| **Total** | **(2 545)** | **(10 292)** |
| **Remuneration to auditors and audit companies** | | |
| Audit services | (34) | (36) |
| Audit services outside the assignment | (17) | (33) |
| Other services | - | (42) |
| **Total audit services** | **(51)** | **(111)** |

## P4: PERSONNEL EXPENSES

| | 2018 | 2017 |
|---|---|---|
| **Salaries and other remuneration** | | |
| Board members, Chief Executive Officer and corresponding officials | (1 753) | (580) |
| Other employees | - | - |
| **Total salaries and other remuneration** | **(1 753)** | **(580)** |
| | | |
| **Social security expenses** | | |
| Board members, Chief Executive Officer and corresponding officials | (487) | (99) |
| Other employees | - | - |
| **Total social security expenses** | **(487)** | **(99)** |
| | | |
| **Other personnel expenses** | | |
| Board members, Chief Executive Officer and corresponding officials | - | - |
| Other employees | (73) | - |
| **Total other personnel expenses** | **(73)** | **-** |
| | | |
| **Total personnel expenses** | **(2 313)** | **(679)** |
| | | |
| **Average number of employees** | **1** | **1** |
| **Total** | | |
| of whom women | 1 | 1 |
| of whom men | - | - |

(all amounts are in EUR thousand, if not otherwise stated)

## P5: TAXES

| | 2018 | 2017 |
|---|---|---|
| Current tax expense (-) / tax income (+) | - | - |
| Adjusted tax from previous year | - | - |
| Deferred tax related temporary differences | - | - |
| **Tax on profit for the year** | **-** | **-** |
| Profit (loss) before tax | (1 284) | (9 664) |
| Tax as per current tax rate for the Parent company, 22% | 282 | 2 126 |
| **Effective tax** | **(1 002)** | **(7 538)** |

## P6: PARTICIPATIONS IN GROUP COMPANIES

| | 2018 | 2017 |
|---|---|---|
| On 1 January | 1 645 093 | - |
| Acquisition | - | 1 645 093 |
| **Carrying amount** | **1 645 093** | **1 645 093** |

| | Domicile | No. of shares | % of share capital | % of voting power | Equity | Profit (loss) for the year | Book value |
|---|---|---|---|---|---|---|---|
| **2018** | | | | | | | |
| Luminor Bank AB | LT | 5 710 134 | 100 | 100 | 770 063 | 55 237 | 702 007 |
| Luminor Bank AS | LV | 191 178 337 | 100 | 100 | 554 367 | 45 022 | 526 625 |
| Luminor Pank AS | EE | 937 643 | 100 | 100 | 476 566 | 25 974 | 416 461 |
| | | | | | | | **1 645 093** |
| **2017** | | | | | | | |
| Luminor Bank AB | LT | 5 710 134 | 100 | 100 | 726 576 | (10 861) | 702 007 |
| Luminor Bank AS | LV | 191 178 337 | 100 | 100 | 534 308 | 11 742 | 526 625 |
| Luminor Pank AS | EE | 937 643 | 100 | 100 | 459 419 | 12 951 | 416 461 |
| | | | | | | | **1 645 093** |

## P7: OTHER RECEIVABLES

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| VAT reclaim | 6 | 630 |
| Other receivables | - | 6 |
| **Total** | **6** | **636** |

## P8: PREPAID EXPENSES AND ACCURED INCOME

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Accrued income | - | 300 |
| Prepaid expenses | 85 | - |
| **Total** | **85** | **300** |

(all amounts are in EUR thousand, if not otherwise stated)

## P9: OTHER LIABILITIES

| | 31 12 2018 | 31 12 2017 |
|---|---|---|
| Social security and employee tax | 13 | 13 |
| Other liabilities | 983 | 443 |
| **Total** | **996** | **456** |

## P10: DETAILS OF PURCHASES AND SALES BETWEEN GROUP COMPANIES

Luminor Group AB has invoiced EUR 3 595 thousand (2017: 1 024 thousand) to group companies and have made purchase from group companies amounting to EUR 55 thousand (2017: 201). The sales to group companies relates to management services and reinvoicing of expenses according to the cost split agreement. The purchase from group companies are reinvoicing of travel expenses and other expenses related to the board and management of Luminor Group AB.

As of 31 December 2018, Luminor Group AB has intercompany payables to the subsidiaries of total EUR 16 and 31 December 2017 as of EUR 2 thousand.

## P11: PROPOSED DISTRIBUTION OF PROFITS

| | |
|---|---|
| **The following funds are at the disposal of the Annual General Meeting (EUR):** | |
| Other non-restricted reserves | 1 635 434 664 |
| Profit (loss) for the year | (1 283 931) |
| **Total** | **1 634 150 733** |
| **The Board of Directors and Chief Executive Officer propose that the earnings be distributed as follows (EUR):** | |
| To be carried forward | 1 634 150 733 |
| **Total** | **1 634 150 733** |

**Nils Melngailis**
Chairman of the Board

**Bjorn Erik Naes**
Board member

**Trygve Young**
Board member

**Jorgen Christian Andersen**
Board member

**Ari Kaperi**
Board member

# Auditor's report

*Unofficial translation*

To the general meeting of the shareholders of Luminor Group AB,
corporate identity number 559072-8316

## Report on the annual accounts and consolidated accounts

### *Opinions*

We have audited the annual accounts and consolidated accounts of Luminor Group AB for the year 2018.

In our opinion, the annual accounts have been prepared in accordance with the Annual Accounts Act and present fairly, in all material respects, the financial position of parent company and the group as of 31 December 2018 and its financial performance and cash flow for the year then ended in accordance with the Annual Accounts Act. The consolidated accounts have been prepared in accordance with the Annual Accounts Act for Credit Institutions and Securities Companies and present fairly, in all material respects, the financial position of the group as of 31 December 2018 and their financial performance and cash flow for the year then ended in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU, and the Annual Accounts Act for Credit Institutions and Securities Companies The statutory administration report is consistent with the other parts of the annual accounts and consolidated accounts.

We therefore recommend that the general meeting of shareholders adopts the income statement and balance sheet for the parent company and the group.

### *Basis for Opinions*

We conducted our audit in accordance with International Standards on Auditing (ISA) and generally accepted auditing standards in Sweden. Our responsibilities under those standards are further described in the Auditor's Responsibilities section. We are independent of the parent company and the group in accordance with professional ethics for accountants in Sweden and have otherwise fulfilled our ethical responsibilities in accordance with these requirements.

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

### *Other matter*

The audit of the annual accounts for the period of 16 August 2016 – 31 December 2017 and consolidated accounts for the period of 1 October 2017 – 31 December 2017 was performed by Ernst & Young AB who submitted an auditor´s report dated 28 June 2018, with unmodified opinions in the Report on the annual accounts and consolidated accounts.

### *Responsibilities of the Board of Director's and the Managing Director*

The Board of Directors and the Managing Director are responsible for the preparation of the annual accounts and consolidated accounts and that they give a fair presentation in accordance with the Annual Accounts Act and, concerning the consolidated accounts, in accordance with IFRS, as adopted by the EU, and the Annual Accounts Act for Credit Institutions and Securities Companies. The Board of Directors and the Managing Director are also responsible for such internal control as they determine is necessary to enable the preparation of annual accounts and consolidated accounts that are free from material misstatement, whether due to fraud or error.

In preparing the annual accounts and consolidated accounts, The Board of Directors and the Managing Director are responsible for the assessment of the company's and the group's ability to continue as a going concern. They disclose, as applicable, matters related to going concern and using the going concern basis of accounting. The going concern basis of accounting is however not applied if the Board of Directors and the Managing Director intend to liquidate the company, to cease operations, or has no realistic alternative but to do so.

### *Auditor's responsibility*

Our objectives are to obtain reasonable assurance about whether the annual accounts and consolidated accounts as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs and generally accepted auditing standards in Sweden will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these annual accounts and consolidated accounts.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the annual accounts and consolidated accounts, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinions. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of the company's internal control relevant to our audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Director's and the Managing Director.
- Conclude on the appropriateness of the Board of Director's and the Managing Director's use of the going concern basis of accounting in preparing the annual accounts and consolidated accounts. We also draw a conclusion, based on the audit evidence obtained, as to whether any material uncertainty exists related to events or conditions that may cast significant doubt on the company's and the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the annual accounts and consolidated accounts or, if such disclosures are inadequate, to modify our opinion about the annual accounts and consolidated accounts. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause a company and a group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the annual accounts and consolidated accounts, including the disclosures, and whether the annual accounts and consolidated accounts represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient and appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated accounts. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our opinions.

We must inform the Board of Directors of, among other matters, the planned scope and timing of the audit. We must also inform of significant audit findings during our audit, including any significant deficiencies in internal control that we identified.

## Report on other legal and regulatory requirements

### *Opinions*

In addition to our audit of the annual accounts and consolidated accounts, we have also audited the administration of the Board of Director's and the Managing Director of Luminor Group AB for the year 2018 and the proposed appropriations of the company's profit or loss.

We recommend to the general meeting of shareholders that the profit be appropriated in accordance with the proposal in the statutory administration report and that the members of the Board of Director's and the Managing Director be discharged from liability for the financial year.

### *Basis for Opinions*

We conducted the audit in accordance with generally accepted auditing standards in Sweden. Our responsibilities under those standards are further described in the Auditor's Responsibilities section. We are independent of the parent company and the group in accordance with professional ethics for accountants in Sweden and have otherwise fulfilled our ethical responsibilities in accordance with these requirements.

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

## *Responsibilities of the Board of Director's and the Managing Director*

The Board of Directors is responsible for the proposal for appropriations of the company's profit or loss. At the proposal of a dividend, this includes an assessment of whether the dividend is justifiable considering the requirements which the company's and the group's type of operations, size and risks place on the size of the parent company's and the group' equity, consolidation requirements, liquidity and position in general.

The Board of Directors is responsible for the company's organization and the administration of the company's affairs. This includes among other things continuous assessment of the company's and the group's financial situation and ensuring that the company´s organization is designed so that the accounting, management of assets and the company's financial affairs otherwise are controlled in a reassuring manner. The Managing Director shall manage the ongoing administration according to the Board of Directors' guidelines and instructions and among other matters take measures that are necessary to fulfill the company's accounting in accordance with law and handle the management of assets in a reassuring manner.

## *Auditor's responsibility*

Our objective concerning the audit of the administration, and thereby our opinion about discharge from liability, is to obtain audit evidence to assess with a reasonable degree of assurance whether any member of the Board of Directors or the Managing Director in any material respect:

- has undertaken any action or been guilty of any omission which can give rise to liability to the company, or
- in any other way has acted in contravention of the Companies Act, the Annual Accounts Act or the Articles of Association.

Our objective concerning the audit of the proposed appropriations of the company's profit or loss, and thereby our opinion about this, is to assess with reasonable degree of assurance whether the proposal is in accordance with the Companies Act.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with generally accepted auditing standards in Sweden will always detect actions or omissions that can give rise to liability to the company, or that the proposed appropriations of the company's profit or loss are not in accordance with the Companies Act.

As part of an audit in accordance with generally accepted auditing standards in Sweden, we exercise professional judgment and maintain professional skepticism throughout the audit. The examination of the administration and the proposed appropriations of the company's profit or loss is based primarily on the audit of the accounts. Additional audit procedures performed are based on our professional judgment with starting point in risk and materiality. This means that we focus the examination on such actions, areas and relationships that are material for the operations and where deviations and violations would have particular importance for the company's situation. We examine and test decisions undertaken, support for decisions, actions taken and other circumstances that are relevant to our opinion concerning discharge from liability. As a basis for our opinion on the Board of Directors' proposed appropriations of the company's profit or loss we examined the Board of Directors' reasoned statement and a selection of supporting evidence in order to be able to assess whether the proposal is in accordance with the Companies Act.

Stockholm 21 March 2019

PricewaterhouseCoopers AB

Marcus Robertsson
Authorized Public Accountant