Bigbank AS Annual report 2019

Bigbank AS
Annual report 2019

Business name	Bigbank AS
Registry	Commercial Register of the Republic of Estonia
Registration number	10183757
Date of entry	30 January 1997
LEI code	5493007SWCCN9S3J2748
Address	Riia 2, 51004 Tartu, Estonia
Telephone	+372 737 7570
E-mail	bigbank@bigbank.ee
Corporate website	www.bigbank.ee
Reporting period	1 January 2019 – 31 December 2019
Chairman of the management board	Martin Länts
Core business line	Provision of consumer loans and acceptance of deposits
Auditor	Ernst & Young Baltic AS

This annual report of Bigbank AS consists of a chairman's statement, review of operations, social responsibility and sustainability report, corporate governance report and consolidated financial statements together with an independent auditors' report and a profit allocation proposal. The document contains 137 pages.

The reporting currency is the euro and numerical financial data is presented in thousands of euros.

The annual report will be available on the website of Bigbank AS at www.bigbank.ee. The English version of the annual report can be found at www.bigbank.eu.

Development

We develop ourselves to deliver better value tomorrow than today.

Ksenija Niitmäe
Chief Legal Officer

Contents

Our mission

Our mission is to enable people to improve their lives through seamless financial services.

Our vision is to be the most recommended digital financial service provider in the countries we operate.

Executive team of Bigbank

Bigbank Group at a glance

BIGBANK VALUES

Caring

We listen, understand as well as support our customers and each other.

Simplicity

We aim at simplicity in our solutions and in customer experience.

Development

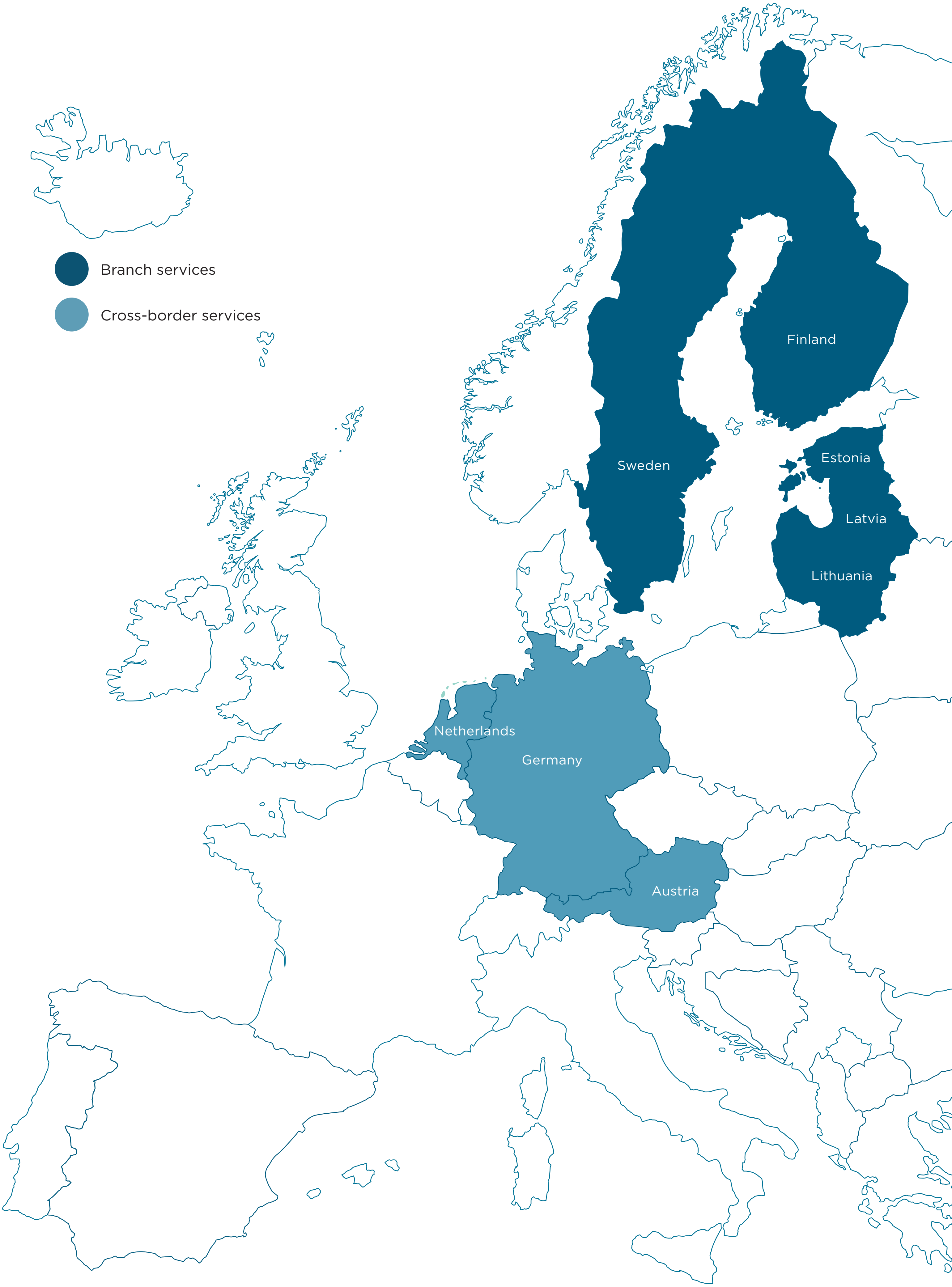
We develop ourselves to deliver better value tomorrow than today.

Result-oriented

We are professional and committed to sustainable knowledge-based performance.

Courage

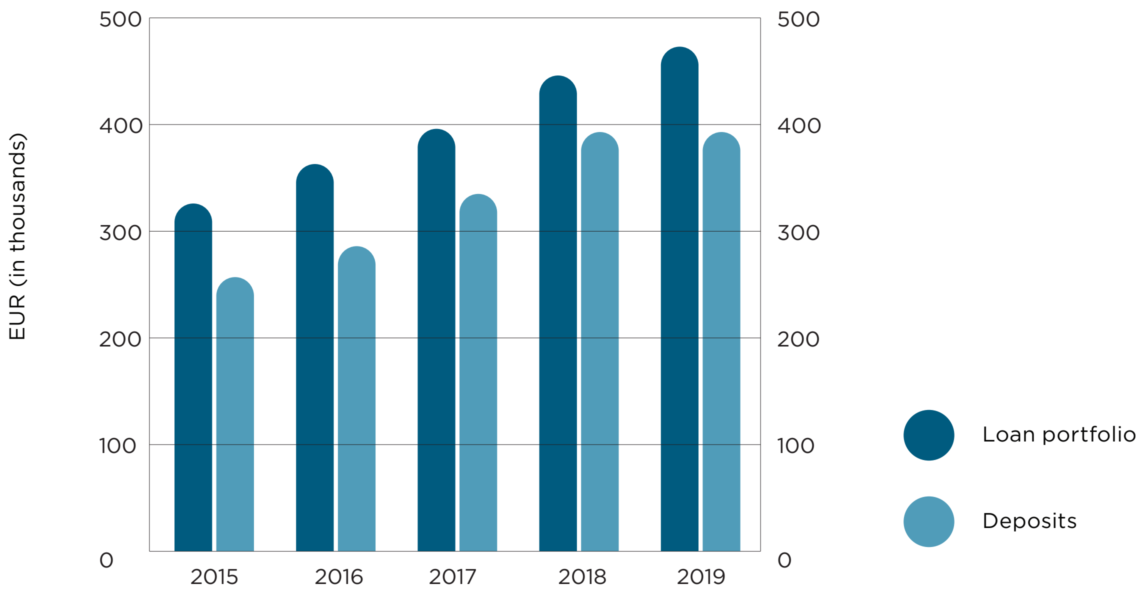
We embrace challenges by taking initiative, making smart decisions and being responsible.


Branch services
Cross-border services
Finland
Sweden
Estonia
Latvia
Lithuania
Netherlands
Germany
Austria

OPERATING COUNTRIES

	Estonia	Latvia	Lithuania	Finland	Sweden	Total
Start of operations	1992	1996	2007	2009	2012	
Loan portfolio, EUR thousand*	102,257	115,495	135,956	76,076	43,671	**473,455**
Number of loans, thousand*	31	33	30	11	8	**113**
Deposit portfolio, EUR thousand*	276,447	23,102	-	40,308	52,981	**392,838**
Number of deposits, thousand*	13	1	-	1	1	**16**
Number of employees*	225	72	67	15	6	**385**

* as at 31 December 2019



Letter of the Chairman of the Management Board

Martin Länts
Chairman of the Management Board

Last year was highly successful for Bigbank. We implemented our new banking system Nest in all countries, and created a new self-service portal and a hire purchase solution. The performing loan portfolio increased to 458.1 million euros and net profit grew by 39% to 24.5 million euros. I am pleased to report that once again we were able to increase customer satisfaction, raising the Net Promoter Score to 39 in the fourth quarter.

Our strong performance and vigorous growth are attributable to our wonderful staff and their commitment to our mission, which is to improve the lives of customers through seamless financial services. I am sincerely grateful that Bigbank has such enthusiastic, caring and smart people who create value for our customers, partners and other stakeholders. I would like to thank you all.

Strategic decisions have had a positive impact

Bigbank's vision is to be the most recommended digital financial service provider in all the countries where we operate. Good customer experience is a priority for us. In 2019, we focused on achieving our strategic goals by continuously improving credit quality and streamlining the bank's operations, which are now supported by the new banking system Nest. This allowed us to earn a profit in all our current markets, including Finland and Sweden. During the period, we discontinued active business operations in Spain. We will continue to service the existing Spanish loan portfolio on a cross-border basis from Estonia. The year 2019 was the midpoint of the current business strategy period 2017-2021 and our strong and sustainable performance reflects that the strategy we have chosen has brought us success.

Next-generation banking software offers unique business opportunities

The period's greatest achievement was definitely technological innovation. Besides previous countries, in 2019 we implemented our new banking platform Nest in Lithuania, Latvia, and Estonia. Together with Nest, we launched a new self-service portal. Since modern solutions provide opportunities for closer cooperation with partners, we enhanced Nest with a partner system which allows offering hire purchase.

The new banking system enables us to better serve our customers, automate labour-intensive processes, streamline reporting, and make high-quality and quick credit decisions. It also improves risk management, simplifies the work of our employees, and facilitates collaboration with partners via various application program interfaces and partner systems. For the third year in a row, we were ranked among the top 10 in the World Banking Technology Awards 2019, this time in the Tech Team of the Year 2019 category.

Satisfied customers are key to doing business

Only satisfied customers empower us to achieve our business goals as well as our vision of being the most recommended digital financial service provider in all the markets where we operate. Therefore, I am pleased to state that in the last quarter of 2019 Bigbank Group's Net Promoter Score increased from 36, measured a year earlier, to 39. This proves that customers value our products and the strategy to offer good terms and excellent customer service.

Bigbank's net profit for 2019 surged to a record-high 24.5 million euros. All branches generated a profit thanks to growth of business volumes, good quality of the loan portfolio, strong employee contribution, and cost-effective operation. Today, Bigbank's loan portfolio amounts to a record-large 473.5 million euros and its quality is higher than ever.

In 2019, Bigbank's long-term employee and CFO Argo Kiltsmann joined the Management Board, where he is responsible for finance. Consistent improvement of management quality is of the utmost importance because we wish to offer our customers increasingly better services.

During the period, we established the corporate banking business line to improve the quality of corporate customer service and develop new products. In addition to Estonia and Lithuania, we started offering business loans in Latvia and supplemented our product portfolio with new business loan products, such as small corporate loans. This was an important step forward: we are now able to serve corporate customers across the Baltics.

Future outlook and growth prospects

Bigbank's vision to be the most recommended digital financial service provider involves a constant drive to grow and develop. To support the Group's growth, we set up a business development unit in 2019. It has started preparations for new product launches and the Group's geographic expansion. The business development unit is also responsible for supporting the existing branches in increasing their profitability.

The microservice-based banking system Nest is a great platform for reaching ambitious goals – we have already started developing a number of new products and services on it. In 2020, our main objective in this area is to broaden the bank's product portfolio. Should an opportunity arise, the new banking system, a working business model, and a strong capital position will also enable Bigbank to expand into new countries.

Martin Länts
Chairman of the Management Board

Review of operations

ECONOMIC ENVIRONMENT

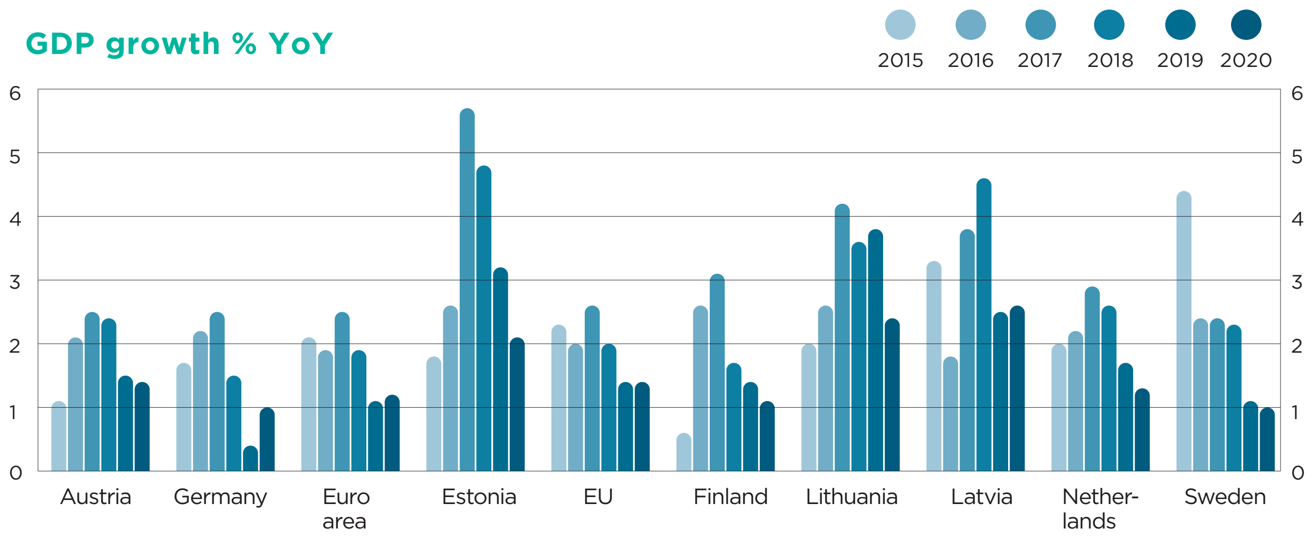
The economy of the European Union (EU) has entered a period of subdued growth and low inflation in the context of high uncertainty and a much less supportive external environment. According to the autumn 2019 forecast of the European Commission (EC), the euro area GDP growth is expected to slow from 1.9% in 2018 to 1.1% in 2019 and to stabilise at 1.2% in the next two years.

Global growth has fallen to a pace usually associated with the brink of recession. International trade in goods has been stagnant and the risks of an increase in trade tensions and geopolitical conflicts have materialised together with uncertainties related to Brexit. It is highly likely that the EU economy will not rebound in the near term.

Labour markets in Europe, however, have remained strong and the unemployment rate has fallen below its pre-crisis level, fuelling robust wage growth, which in the context of historically low borrowing costs has allowed domestic demand to expand at a relatively steady pace. According to the EC, the euro area unemployment rate fell from 8.2% in 2018 to 7.6% in 2019 and will ease to 7.4% in 2020. According to the EC's estimates, in 2019 inflation in the EU continued to be muted, falling to 1.2% from 1.8% in 2018 and is expected to stay there in 2020 as well. The fall in energy prices and the lack of pass-through from robust wage growth to core inflation have kept the inflationary pressures down. In a context of weak demand businesses have been absorbing wage increases by accepting lower profit margins rather than by raising prices

In response to concerns about slowing growth and the escalation in trade tensions, central banks across the world have recently shifted to more accommodative policies. Government bonds rallied remarkably in 2019, leading to lower yields around the world. Given the outlook for subdued economic growth and inflation as well as recent ECB decisions, including renewed monthly net asset purchases, upward pressure on nominal interest rates should be very limited over the next years and real short- and long-term rates are predicted to remain negative by the EC.

GDP growth % YoY



Source: European Commission

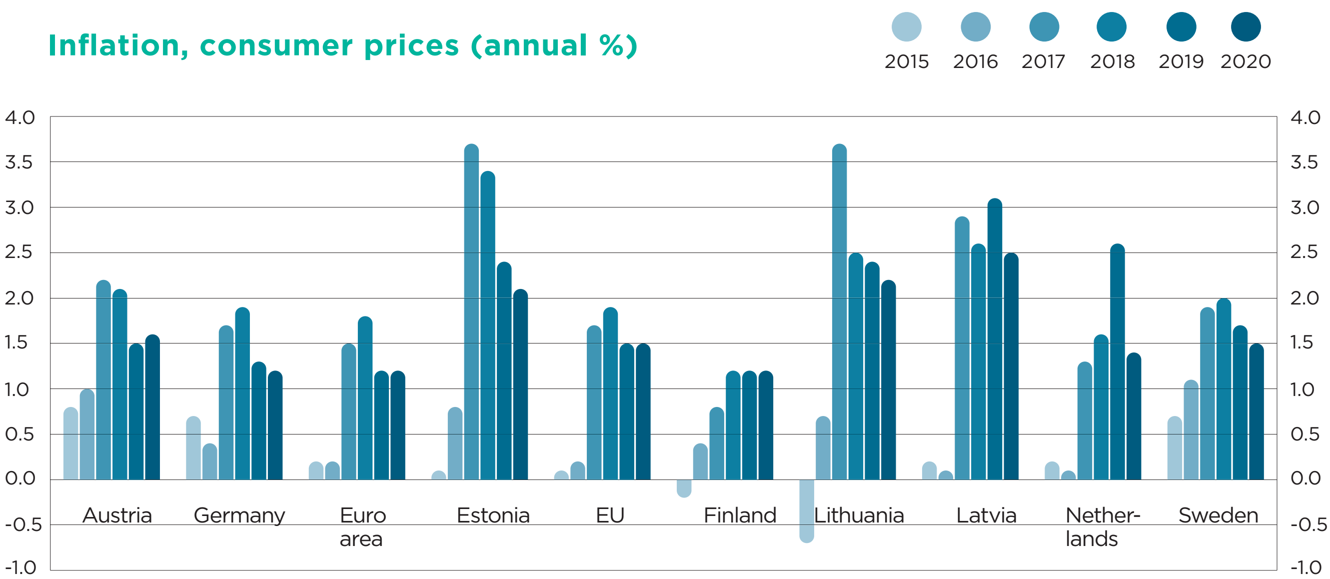
According to the EC, the EU economy is facing a period of very high uncertainty regarding trade and other economic policies, which is expected to last for at least the next few years. Outside Europe, any deviation from the assumption that the current trade and geopolitical tensions will not escalate further, or lower than assumed effectiveness of policy measures to boost global growth in general, and China's growth in particular, could deepen the slowdown in the global economy. Within Europe, any deviation from the relatively benign assumption of a status quo in terms of trading relations between the UK and the EU after Brexit could affect growth prospects negatively. Another downside risk is that the recession in the manufacturing sector could have a bigger spillover effect on the services sector, affecting confidence, net job creation, domestic demand, growth expectations and ultimately resulting in worse growth outcomes.

BALTIC COUNTRIES – ESTONIA, LATVIA AND LITHUANIA

With the exception of Lithuania, growth in the Baltic countries slowed in 2019. According to forecasts, in 2019 economy expanded by 3.2% in Estonia, 3.8% in Lithuania and 2.5% in Latvia. Comparable figures for 2018 were 4.8% in Estonia, 3.6% in Lithuania and 4.6% in Latvia. Growth has been mainly supported by still strong domestic demand, which has offset the effects of a slower international trade as the economies of the main export partners have been weakening. Private consumption has so far been supported by strong employment growth as well as increasing real incomes. Investment growth, however, is set to fade in 2020 as EU fund inflows have peaked. According to the expectations of the EC economic forecast, in 2020 growth will slow to 2.1% in Estonia and 2.4% in Lithuania but will increase to 2.6% in Latvia.

In all three countries, the cyclical peak in economic activity has led to labour shortages and rapidly rising nominal wages. Inflation, however, is forecasted to moderate marginally in the coming years, except for services, whose prices are expected to continue growing rapidly, reflecting the pass-through of high wage growth.

Inflation, consumer prices (annual %)



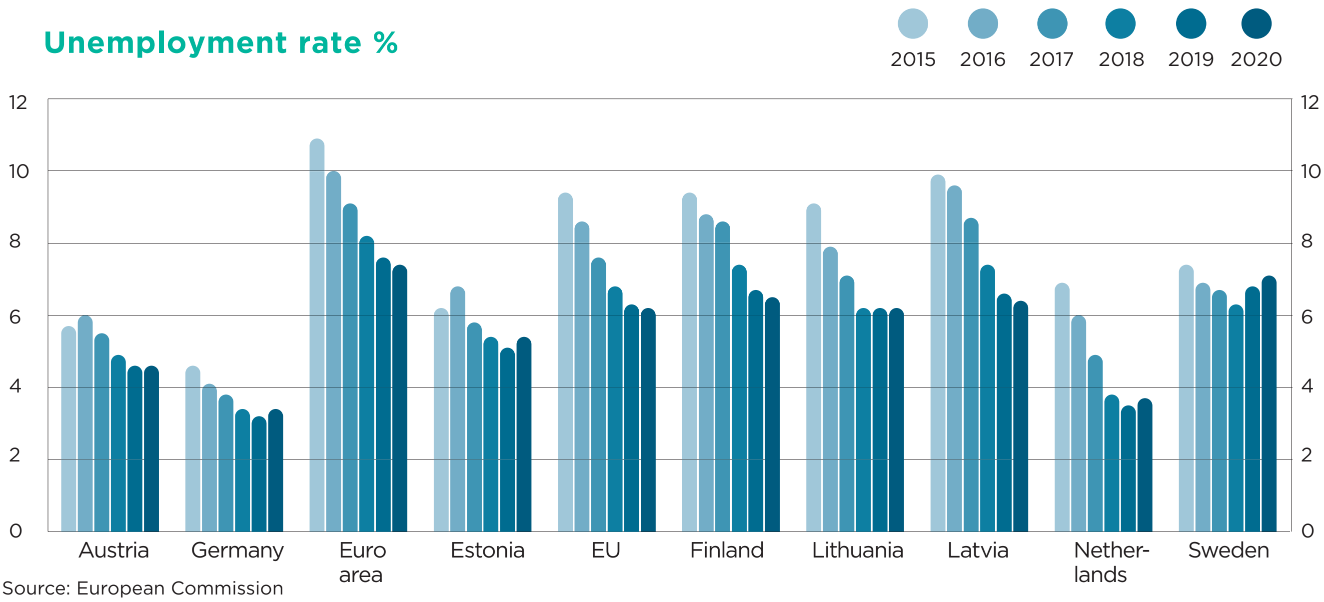
Source: European Commission

NORDIC COUNTRIES – FINLAND AND SWEDEN

Economic activity in Sweden slowed down markedly in the first half of 2019, after several years of relatively brisk growth. GDP growth is forecasted to fall from the 2% peak in 2018 to 1.7% in 2019 and further to 1.5% in 2020. Domestic demand and investment in particular are weak, but exports are still holding up quite well, so net exports are set to become the economy's engine of growth.

Finland saw a slowdown to 1.2% growth already in 2018 and its economy is predicted to maintain the same growth rate for the next few years. Unemployment is set to fall gradually to its structural level while inflation is expected to remain low. The pass-through from higher wages into services, however, has been smaller than in the past.

As the Nordic business cycle is closely aligned with that of its main trading partners, a deterioration in the external environment would weigh on the export sector. Downside risks also remain on the domestic side, as a sharper-than-expected worsening in the labour market could have a negative impact on private consumption.



Source: European Commission

CENTRAL EUROPE AND BENELUX COUNTRIES – AUSTRIA, GERMANY, AND THE NETHERLANDS

The German economy is on the brink of a technical recession as a multi-quarter economic contraction has become a reality. On an annual basis, GDP growth is projected to fall from 1.4% in 2018 to 0.4% in 2019 and to recover back to just 1% in 2020. The slowdown of the German economy, which is among the largest in the EU, is affecting all EU countries, especially those which are dependent on international trade. The labour market has so far remained robust with record-high employment and increasing wages.

Economic growth in Austria is expected to moderate but remain robust in 2019 and to stabilise in 2020. Domestic demand is set to remain the main growth driver, with strong private consumption supported by fiscal measures. GDP growth is expected to slow from 2.4% in 2018 to 1.5% in 2019 and to 1.4% in 2020.

In the Netherlands, after solid growth of 2.6% in 2018, the economy has started to cool. Growth is expected to drop to 1.7% in 2019 and 1.3% in 2020. The contribution from net exports is expected to turn negative against the backdrop of a weak external environment, whereas domestic demand should remain resilient, supported by rising wages and private consumption, resulting from rising employment and wages, is set to drive solid consumption growth.

OVERVIEW OF THE YEAR 2019

For Bigbank AS (Bigbank, the Group), 2019 was the most successful year ever. Both the volume of the loan portfolio and net profit closed at record levels. At 31 December 2019, the Group's assets totalled 574,193 thousand euros, having increased by 45,676 thousand euros (8.6%) during the year. The growth in total assets resulted primarily from loans to customers, which grew by 7.4% to 459,656 thousand euros.

Loans to customers increased the most at the Estonian business unit, where growth amounted to 19,978 thousand euros. In terms of branches, loans to customers remained the largest at the Lithuanian branch, where the year-end figure was 137,900 thousand euros, accounting for 30% of the Group's total loans to customers.

The Group ended the year with a record net profit of 24,453 thousand euros, an improvement of 6,927 thousand euros (39.5%) year on year. The rise in net profit is mainly attributable to the low level of credit losses. Net impairment losses on loans and financial investments decreased by 4,680 thousand euros (41.2%) in 2019, dropping to 6,675 thousand euros. Credit losses decreased through a successful implementation of the Group's strategy. By focusing on serving clients with a lower credit risk, we have been able to consistently increase our performing loan portfolio and reduce our credit losses. At the year-end, non-performing loans accounted for 2.9% of total loans to customers. By the end of 2019, the credit quality of all branches' loan portfolios was satisfactory or high.

Thanks to a strong net profit, the Group's equity grew by 16.4% to 141,053 thousand euros. The Group's capitalisation is solid. ROE increased to 18.7%, which is well above the 15% target set in our strategy.

One of Bigbank's key targets for 2019 was to implement its new self-created banking software, Nest, at its Baltic entities. Nest is a modern microservices-based information system, which covers all the main bank functions from customer service, product offering and self-service to debt handling and real-time accounting. Nest has been developed to support business growth, new products and markets through automation, and to improve customer experience and the speed of service. In 2019, the Group's cross-border activities (deposits from Germany, the Netherlands and Austria) were transferred to Nest, data migration was carried out and Nest was implemented in all three Baltic states one by one. The Finnish and Swedish branches were already operating on Nest, having adopted it in 2017 and 2018 respectively. Nest is one of the key reasons behind the Group's strong growth and profitability. It has increased automation and operating efficiency: in the year of strong growth, Bigbank was able to reduce other operating expenses by 1,301 thousand euros (- 10.0%). The information system's active development will continue in the current year with the main focus on new products and markets.

On 5 June 2019, the supervisory board of Bigbank AS decided to close the Spanish branch Bigbank AS Consumer Finance, Sucursal en España and carry out all activities required for that purpose. The decision will have no significant impact on the Group's future performance because the new business activities of the Spanish branch were discontinued already from 6 April 2018 due to insufficient profitability. The branch concentrated on serving the existing customers and improving the credit quality of its loan portfolio. The volumes decreased and from November 2019 it became reasonable to continue serving the remaining customers on a cross-border basis via the parent bank and to liquidate the Spanish branch. The member of the management board of Bigbank AS Sven Raba has been appointed responsible for terminating the activities of the branch.

In 2019, Bigbank strengthened its team with the leaders of two important areas. In March, the business development area was created, which has been led by Targo Raus ever since. In June, the corporate banking area was created, which is led by Ingo Põder. These steps show the Group's ambition to increase its focus on new products and business customers. In the second quarter of 2019, Bigbank started serving business customers at the Latvian branch. Previously, business customers were served only at the Estonian business unit and the Lithuanian branch.

OUTLOOK FOR 2020

Most experts are predicting an economic slowdown for 2020. Still, there is no immediate threat of a crisis and Bigbank's own economic forecast for its home markets is somewhat stronger. Despite being prepared for a cooler economic environment, we have growth plans for all our home markets in 2020. The plans are supported by Nest, which enables us to work more efficiently and launch new products and product adjustments more quickly, and our newly strengthened management team.

Interest rates are not expected to rise in any of our home markets. Accordingly, we are planning to increase the product range and the volume of the loan portfolio. We will continue to invest in technologies that support a digital lender's business model and to improve the Group's operating efficiency.

Bigbank is also exploring possibilities to expand to a new home market in 2020.

KEY PERFORMANCE INDICATORS

Financial position indicators (in thousands of euros)	31 Dec 2019	31 Dec 2018
Total assets	574,193	528,517
Loans to customers	459,656	427,964
of which loan portfolio	473,455	445,679
of which interest receivable	10,494	6,122
of which impairment allowances	-24,293	-23,837
Deposits from customers	392,838	393,020
Equity	141,053	121,174

Financial performance indicators	2019	2018
Interest income	66,950	66,386
Interest expense	-6,390	-6,099
Salaries and associated charges	-14,917	-15,089
Other operating expenses	-11,722	-13,023
Net loss allowances on loans and financial investments	-6,675	-11,355
Profit for the year	24,453	17,526

For the year	2019	2018
Average equity	131,114	117,210
Average assets	551,355	493,927
Average interest-earning assets	511,866	461,555
Average interest-bearing liabilities	403,008	362,740
Total income (gross)	72,427	72,034

Ratios	2019	2018
Common equity Tier 1 capital ratio	22.2%	21.6%
Tier 1 capital ratio	22.2%	21.6%
Total capital ratio	23.2%	22.7%
Leverage ratio	19.2%	19.3%
Liquidity coverage ratio (LCR)	644.0%	907.0%
Net stable funding ratio (NSFR)	132.8%	126.0%
Minimum requirement for eligible liabilities (MREL)	21.0%	20.9%
Return on assets (ROA)	4.4%	3.5%
Return on equity (ROE)	18.7%	15.0%
Profit margin (PM)	33.8%	24.3%
Return on loans	14.5%	15.7%
Asset utilization ratio (AU)	13.1%	14.6%
Price difference (SPREAD)	11.5%	12.7%
Cost to income ratio (CIR)	49.6%	50.6%
Equity multiplier (EM)	4.2	4.2
Earnings per share (EPS), euros	305.66	219.08
Yield on interest-earning assets	13.1%	14.4%
Cost of interest-bearing liabilities	1.6%	1.7%

EXPLANATIONS

Average financial position indicators (equity, assets) are calculated as the arithmetic means of respective indicators, i.e. carrying value at end of previous reporting period + carrying value at end of current reporting period / 2

Average interest-earning assets are calculated as the arithmetic means of interest-earning assets in the statement of financial position i.e. carrying value of interest-earning assets at end of previous reporting period + carrying value of interest-earning assets at end of current reporting period / 2

Average interest-bearing liabilities are calculated as the arithmetic means of interest-bearing liabilities in the statement of financial position i.e. carrying value of interest-bearing liabilities at end of previous reporting period + carrying value of interest-bearing liabilities at end of current reporting period / 2

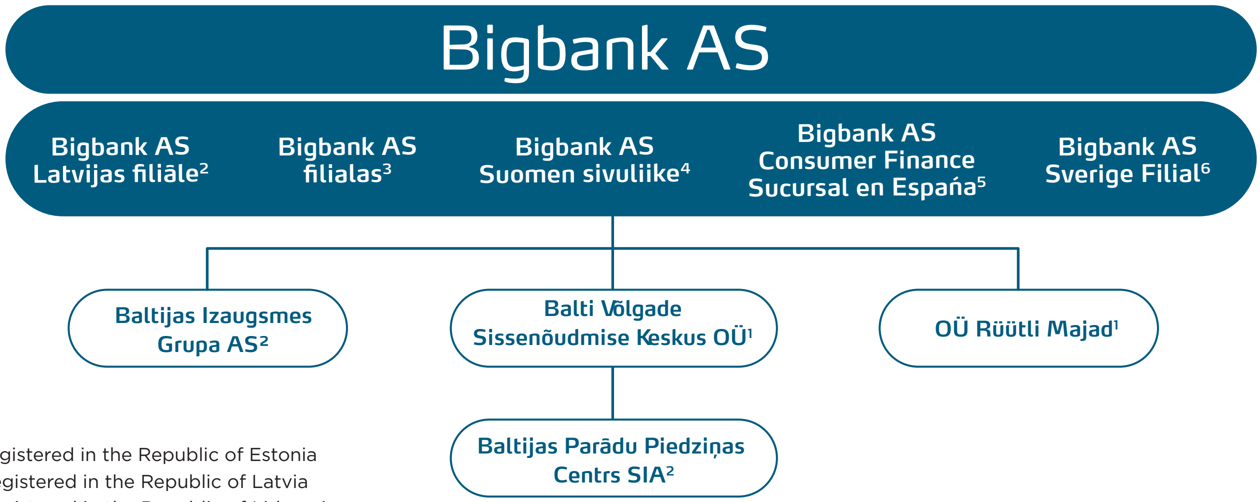
Common equity Tier 1 capital ratio (%) = common equity Tier 1 capital / total risk exposure amount * 100
Tier 1 capital ratio (%) = Tier 1 capital / total risk exposure amount * 100
Total capital ratio (%) = total own funds / total risk exposure amount * 100
Leverage ratio (%) = Tier 1 capital / total leverage ratio exposure * 100
Liquidity coverage ratio (LCR, %) = high-quality liquid assets / net cash outflows over the next 30 days * 100
Net stable funding ratio (NSFR, %) = stable funding / required stable funding * 100
Minimum requirement for eligible liabilities (MREL, %) = (total own funds + eligible liabilities) / total liabilities * 100
Return on assets (ROA, %) = profit for the year / average assets * 100
Return on equity (ROE, %) = profit for the year / average equity * 100
Profit margin (PM, %) = profit for the year / total income * 100
Return on loans = (interest income on loan portfolio + income from debt collection) / average loan portfolio
Asset utilisation ratio (AU) = total income / average assets
Price difference (SPREAD) = interest income / interest-earning assets – interest expense / interest-bearing liabilities
Cost to income ratio (CIR) = total operating costs to net income
Equity multiplier (EM) = average assets / average equity
Earnings per share (EPS) = profit for the year / period's average number of shares outstanding
Total income = interest income + fee and commission income + other income
Yield on interest-earning assets = interest income / average interest-earning assets
Cost of interest-bearing liabilities = interest expense / average interest-bearing liabilities

ABOUT BIGBANK GROUP

Bigbank AS was founded on 22 September 1992. A licence for operating as a credit institution was obtained on 27 September 2005.

Bigbank's core services are consumer loans and term deposits.

The Group's structure at the reporting date:



[1] registered in the Republic of Estonia
[2] registered in the Republic of Latvia
[3] registered in the Republic of Lithuania
[4] registered in the Republic of Finland
[5] registered in the Kingdom of Spain, under liquidation
[6] registered in the Kingdom of Sweden

The branches in Latvia, Lithuania, Finland and Sweden offer lending services similar to those of the parent. The parent and its Latvian, Finnish and Swedish branches also offer deposit services. In addition, Bigbank AS provides cross-border deposit services in Germany, the Netherlands and Austria. The core business of OÜ Rüütli Majad is managing the real estate. Baltijas Izaugsmes Grupa AS has no active operations. Balti Võlgade Sissenõudmise Keskus OÜ and its subsidiary support the parent and its branches in debt collection.

In 2019, Spanish branch of the bank "Bigbank AS Consumer Finance Sucursal en España" was closed and remaining customers were served cross-border by parent bank in Estonia. At 31 December 2019 the Spanish branch was under liquidation.

SHAREHOLDERS

The shares in Bigbank AS are held by two individuals, each holding the same number of shares. At 31 December 2019, the shareholders were:

Shareholder	Number of shares	Interest
Parvel Pruunsild (chairman of the supervisory board)	40,000	50.0%
Vahur Voll (member of the supervisory board)	40,000	50.0%

The shares in Bigbank AS are registered with the Estonian Central Depository for Securities. Use of voting power carried by the shares has not been restricted. The company is not aware of any shareholder agreements under which the shareholders pursue a joint policy by means of pooling their votes or otherwise restrict use of voting power. Except for shares, Bigbank AS has not issued any securities that grant control of the company.

LITIGATION

At 31 December 2019, the Group was not involved in any significant litigation.

EMPLOYEES

The Group's business growth and remarkable development in recent years have been achieved through the efforts of a committed and professional team of almost 400 employees.

EMPLOYEE PROFILE BY COUNTRIES AS AT 31 DECEMBER 2019

Country	Number of employees	Number of male employees	Number of female employees	Share of male employees	Share of female employees	Average length of service	Average age
Estonia	225	99	126	44%	56%	50 months	34 years
Finland	15	8	7	53%	47%	57 months	38 years
Latvia	72	13	59	18%	82%	66 months	31 years
Lithuania	67	29	38	43%	57%	52 months	32 years
Sweden	6	1	5	17%	83%	36 months	33 years
Total	**385**	**150**	**235**	**39%**	**61%**	**54 months**	**33 years**

Table: Employee profile by countries as at 31 December 2019

As of 31 December 2019 the number of employees was 385 compared with 436 at the end of 2018. When planning the most important activities in human resource management in 2020, we take into account that a large part of our employees (40%) are under 30 years of age and 36% have less than 23 months of service.

THE EMPLOYEE EXPERIENCE STRATEGY FOCUS AREAS FOR 2018-2021 ARE AS FOLLOWS:

- Bigbank is an attractive employer and we follow value-based recruitment principles.
- We deliver excellent induction for new and internally rotating employees.
- We provide excellent management and leadership service to employees, including employees on a long-term leave (e.g. parental leave).
- Our remuneration system performs well.
- We ensure short and long-term replacement staff for business-critical positions and functions.
- Work environment and tools help our employees do their job well and efficiently and stay healthy.

The main results of 2019 by focus areas were as follows:

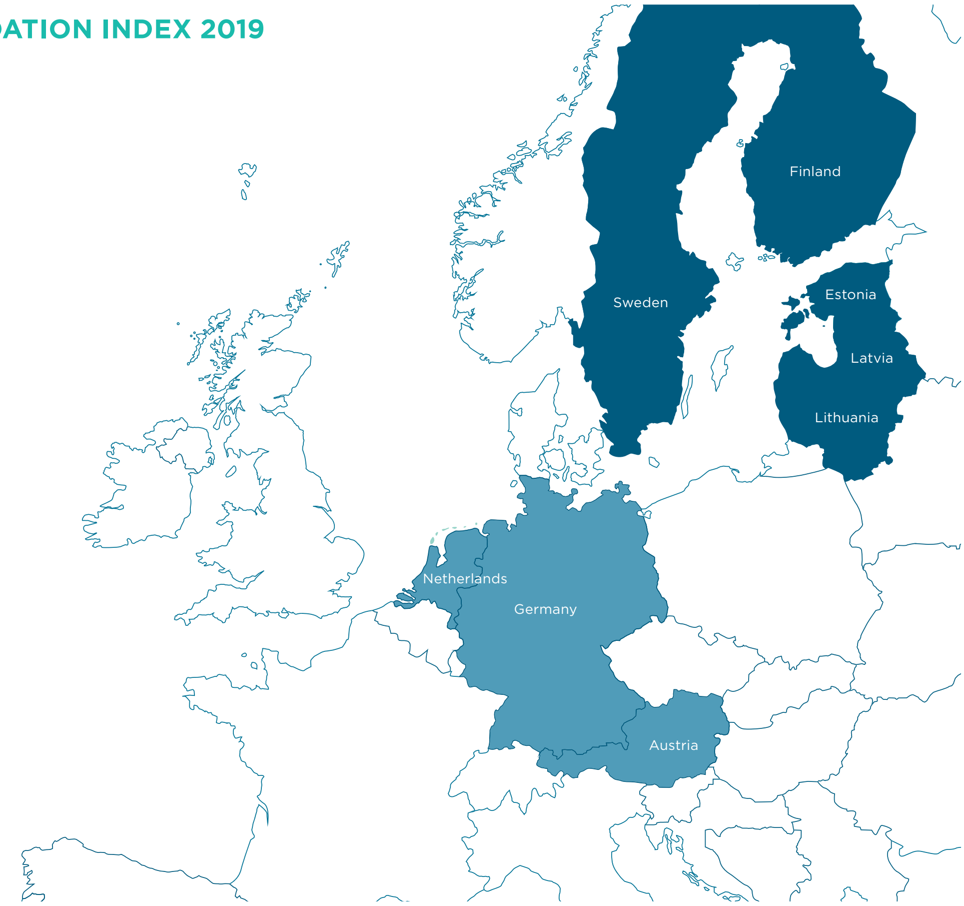
Focus 1: Bigbank is an attractive employer and we follow value-based recruitment principles

The most important factor in recruiting new employees is still the willingness of our own employees to recommend Bigbank as an employer.

To understand and regularly monitor employee experience, we started collecting employee feedback in 2018 on a quarterly basis in all cities where Bigbank has an office and staff. In the third quarter, the recommendation index was positive in all cities.

EMPLOYEE RECOMMENDATION INDEX 2019

- Tallinn 3.7
- Tartu 3.8
- Riga 3.7
- Vilnius 4.1
- Helsinki 4.0
- Stockholm 4.0



We recruit vacancies from within the Group at first. In 2019, a significant number of key positions in branches and group level units were recruited internally, thus creating an opportunity for capable employees to move between different levels of management, areas, countries, and cities. We are proud to have a really strong increasing trend among Bigbank alumni coming back after some time. In 2019, the returning rate increased by 25% compared to 2018.

Already in 2018 we complemented our recruitment process with value-based assessment methods. In the end of summer of 2019, we organised group-wide value awareness workshops to improve management quality and raise awareness of Bigbank values internally. This program aims to make value communication a part of everyday conscious management and will continue in 2020.

We consciously introduced Bigbank's culture and experience to our target prospects in social media channels. Our official pages (such as lifeatbigbank in Instagram) offered visuals and stories that make us who we are today and our staff shared their #bigbankwow experiences through photos and stories in different social media channels.

Our employees posts on Bigbank's Instagram account

Focus 2: We provide excellent support for new and internally rotating employees

Due to the development of the organisation and the situation in the Baltic labour market, supporting the induction of both new and rotating employees continued to be one of the most important priorities of 2019.

Bigbank has a very in-depth induction program, the content of which we apply to each employee, depending on his or her duties and background. As or vision is to become the most recommended digital service provider in the countries we operate, a case study of customer experience is an obligatory part of induction program for all employees, so every new employee would be able to get to know Bigbank's customers and to better understand their own role in delivering excellent customer experience.

Decision engine analyst	I will ensure that the search engine is working and is fast.
Head of data warehouse unit	I shall analyse the customer feedback and shall give input based on this to quality managers, who can then do conclusions from the pros and cons.
Reporting specialist	I shall notice mistakes in the reports and shall notify about them.
IT support specialist	I shall ensure that all employees have a working computer and I shall fast react to problems with computers to find solutions.
Lawyer	I shall support customers to get help from debt collection and predict if the customer case needs to go to court.
Software developer	I will just do my job so that no bugs will appear.
Business analyst	I shall optimise the whole process and make it simpler

Example of the results of a case study

The feedback from new employees to the recruitment process was very positive in 2019. Compared to previous employers, the employee-centered, thoughtful and well-organised process of the induction program was positively highlighted.

Focus 3: We provide excellent management and leadership service to employees, including employees on a long-term leave (e.g. parental leave).

For years, the main goal of improving management quality has been to improve Bigbank's performance through better focus, discipline and ensuring regular and transparent information exchange across the organisation. To achieve this, the training focus for both managers and experienced specialists has been primarily on developing the competencies of execution (4 Disciplines of Execution) and efficiency (Lean management, agile development process). In 2019, we had several external coaches supporting our top managers in their most challenging employee related topics.

The management board of Bigbank AS at the bank's annual seminar in Tallinn in January, 2020

To improve management quality, we continued with a number of initiatives at all levels of management, i.e.:

- Once a quarter, we hold top management seminars, where, additionally to financial results, we also address customer and employee experience issues. The focus of the development of management competencies is mainly on developing change management competencies.
- We organised in-house training programs for branch managers to improve leadership skills and enhance the branch management team's teamwork.
- Many managers participated in external trainings according to their development goals.

Improving leadership skills will continue occupying an important place in our 2020 activities.

Focus 4: Our remuneration system performs well.

In 2019, we upgraded our remuneration policy and remuneration principles based on agreed principles within the company, trends of the labour market and legal requirements, we focused on two major improvements in 2019:

- We set internal control mechanism on KPI quality by making them public in our intranet.
- We increased the independence of managers and teams in deciding the variable remuneration of employees and improved the first line of defence.
-

Due to the changes, the employee feedback to clearness of remuneration principles dropped from 4.3 points in 2018 to 4.1 points in 2019, but overall rating is still above average.

Focus 5: We ensure short and long-term replacement staff for business-critical positions and functions.

Since 2018, we began and in 2019 we continued dealing more systematically with short and long-term substitution, as it is one of the most important factors for ensuring Bigbank's consistent operation and improving the employee experience. Employee feedback on substitution compared to 2018 has improved, from 4.27 points to 4.28 points.

Focus 6: Work environment and tools help our employees do their job well and efficiently and stay healthy.
We monitor employee satisfaction with the work environment and regularly ask quarterly feedback based on country, city, and specific office. By doing so, we identified the key factors for improvement and, within the limits of Bigbank's capabilities, we solved some of these during the year.

The most important long-term project was a thorough analysis of the needs of the office spaces, describing all the organisational, technical and microclimate requirements to be considered in the future when we decide to move to new premises or renovate existing ones.

Compared to previous years, we paid much more attention to raising the health awareness of the employees. We regularly shared information on how they can protect themselves against viral diseases, how to improve their workplace ergonomics, and knowingly use rest breaks to improve their health and exercise without leaving the workplace.

In Estonia, the Bigbank is a member of program of a family-friendly employer, curated by the Ministry of Social Affairs. Getting the initial label is a recognition of our efforts to create a family-friendly organisational culture.

Employee satisfaction with working conditions and the work environment compared to the previous period has not varied its level too much, in 2018 the result was 3.87 points and in 2019 the result was 3.82 points.

Social responsibility and sustainability report

Bigbank's social responsibility and sustainability report is based on the G4 Sustainability Reporting Guidelines (G4 Guidelines) of the Global Reporting Initiative (GRI). The G4 Guidelines offer two options for preparing a sustainability report: the comprehensive option and the core option. Bigbank has prepared its social responsibility and sustainability report using the core option.

CUSTOMERS

Bigbank has customers in eight countries. Our customers prefer to communicate via digital channels and are happy to give us positive feedback about their experience with Bigbank.

Each customer's experience and journey are very important to us: Bigbank's mission is to help people improve their lives through seamless financial services. We want to know what our customers say about us, how they feel about us and whether they are willing to recommend us to others. Customer feedback is read regularly by senior and line managers as well as the staff of business units.

Everyone at Bigbank knows how to contribute to improving customer experience. All our employees set at least one annual goal related to ensuring increasingly better service. This enables us to provide exceptional customer experience that inspires our customers to tell positive stories.

Customer experience management

At Bigbank, our common goal is to deliver premium customer experience end to end. Only by working together can we retain loyal customers that are willing to recommend our products and services. It matters to us what our customers experience from the moment they take an interest in our products and services to the moment they cease using of our products and services.

Bigbank's business strategy for the period 2017-2021 is focused on sustainable growth, which assumes, among other things, consistent improvement of customer experience. At the beginning of 2017, we used the input of our customers to design Bigbank's customer experience strategy. In implementing it in 2019, we took the following steps in all markets:

- We improved customer experience at the following touchpoints: communicating the rejection of a loan application, signing an agreement, one year after signing an agreement, the expiry of an agreement and the debt recovery process. As a result, in 2019 the Net Promoter Score for these touchpoints rose by 12%, 11%, 26%, 11% and 42%, respectively.

- We analysed the share of customers that currently come to us via referrals from friends or acquaintances. In the Baltic states, where Bigbank is well-known the figure is 18% on average.
- We increased the transparency of customer feedback by introducing an automatic feedback monitoring tool, which provides

better insights into the links between the customer profile, contract terms and loyalty.

- We continued to share customer feedback and relevant statistics with all Bigbank employees. This included explaining how we have increased the value provided to customers and highlighting what we could do even better.
- We continued to assess the quality of our customer communication and concluded that we are professional, friendly and supportive both over the phone and by e-mail.
- Since it is important to us that customers should receive all relevant information during their first interaction with us so that they would not have to contact us again with the same matter, we systematised the collection of statistics and information about customer interactions. The new solution provides us with detailed information on how many customers get their issues resolved during the first contact.
- Having completed the implementation of a new customer relationship management system in all countries where we operate, we reintroduced automated collection of customer feedback.
- We began to offer the option of receiving quicker credit decisions in all countries – our customers were pleasantly surprised and praised the speed of our processes.
- We began to provide digital customer experience via a self-service channel. This was an important move because enabling customers to get answers promptly and through the first channel they choose is strategically important to us.
- We sought to deliver more personalised customer experience: at our Estonian entity we made thank-you calls to randomly selected customers whose savings or loan agreement had matured; we began to provide more detailed explanations to customers whose loan applications had been rejected so that they would better understand the reasons; in the Baltic states we began to make personalised small loan offers.
- We continued to invest in regular employee training and staff development with a particular focus on quality enhancement and the implementation of lean work methods.
- We created a new tool designed to facilitate and streamline the assessment of service quality (the tool will be implemented in our work flows in 2020).
- We maintained the efficiency of our customer service processes: our efficiency in responding to customer calls and e-mails remained as high as in 2018 (in 2018 our efficiency indicators for responding to e-mails and calls improved by 10% and 4% year on year, respectively).

Monitoring and measuring customer experience

We collect and monitor customer feedback systematically, to obtain a fair assessment of the service we provide and identify its strengths and weaknesses. Analysing feedback helps us understand what increases our customers' loyalty and what does not. Increasing customer satisfaction and loyalty is also important for our business partners.

To evaluate customer experience, we:

- regularly request feedback on different customer experience touchpoints through the Net Promoter Score, First Contact Resolution and Customer Satisfaction Index (around 2,100 respondents per month);
- measure the effectiveness of customer communication by analysing call centre statistics and assess our employees' communication quality;

- study Bigbank's general brand positioning and image in all markets where we operate through annual brand perception surveys and compare the results with those of our competitors (based on a representative sample of the adult population, with around 1,000 respondents in each country); and
- analyse the feedback provided by customers after they have contacted us by phone or e-mail.

With the above techniques we cover the main touchpoints of different customer groups' customer journeys and gain valuable insights into our customer service, products and pricing.

Customer complaints at Bigbank

Each customer is important to us. During the period under review, we responded to every complaint and analysed what we could do better to prevent the recurrence of issues of a similar nature. Customer complaints were filed at all branches and handled mainly by the front line staff. Where prevention assumes major technological development, the complaint is passed on to the manager responsible for the area who determines the action plan.

Responsible customer service

Quality customer relationships are underpinned not only by product quality but also by responsible customer service. The responsible nature of our customer service is primarily reflected in the following four aspects:

1. Communicating proactively with the customer – Before signing a product agreement, we inform our customers of their obligations and potential risks. We seek solutions together with the customer and prevent potential issues. We conduct communication quality reviews in line with our established quality model and service standard. To make sure that our people have the knowledge they need, we provide training, invest in staff development and regularly test our employees' knowledge.
2. Systematically reviewing and analysing customer experience – Based on customer feedback we proactively prevent potential problems.
3. Ongoing monitoring of complaints and problems – We follow our complaint handling procedure and make changes to our products, services and processes where necessary.
4. Keeping our promises and providing information effectively – We respond quickly to our customers' needs and inquiries.

Customers' assessment of their customer experience

In 2019, our main priorities were work processes and the implementation of our new customer relationship management system. Another focus area was excellent and fast customer service. It is important to us that our customers' loyalty should increase over time. We understand that building loyalty requires time and conscious investment in customer experience enhancement. We are proud and grateful when we receive positive feedback. The most frequent keywords in customer feedback of the period were: fast, friendly, professional, convenient and good contract terms and conditions.

The Net Promoter Scores for most touchpoints of the customer journey improved throughout 2019. The score for the debt proceedings increased the most. In terms of countries, the Net Promoter Scores differed slightly, being

again the highest in Estonia, Lithuania, Germany, Austria and the Netherlands. Customer loyalty is the strongest right after the signature of an agreement.
In implementing the new strategy developed in 2017, we have worked hard to offer better customer experience and increase customer loyalty. In 2019, we maintained a customer-centric approach and our customers' loyalty and trust remained high in all countries where we operate.

BIGBANK AS A RESPONSIBLE EMPLOYER

In recent years, one of Bigbank's most important strategic objectives has been to become a company and an employer with a good reputation. Our aim has been to develop a strong employer brand both internally and externally. In 2019, we widened the diversity of our staff by increasing the share of foreign employees in the headquarter and adjusting our Tartu office to create suitable working conditions for workers with special needs. For balancing the professional and private life of our employees, we offer flexibility to work from home office and/ or attend meetings via video conference upon the need.

In 2019, we followed the Group-level processes that were out in place already in 2018 to ensure the delivery of quality services to employees and better employee experience. At the same time, we strengthened the operations of the first line of defence, related to employment relationship management, recruitment, remuneration and professional development of employees.

In Bigbank, the head of WOW support services function is responsible for establishing, monitoring and reporting Group-level regulations related to services provided to our employees.

At the end of 2019, Bigbank employed 385 people: 225 in Estonia, 72 in Latvia, 67 in Lithuania, 15 in Finland and 6 in Sweden. The annual average number of full-time employees was 399.

RESPONSIBLE ACTIVITIES

In recent years, we have consciously managed our activities as a responsible business, analysing our key stakeholder groups, increasing the benefits we provide to society, developing our employees and work environment and managing the company based on its value to the main stakeholder groups. We believe that a commitment to sustainability, both in the mindset and in plans and activities, is the bedrock of the success of the whole society.

Bigbank appreciates high social contribution and ethical values and acts on the principle of responsibility to ensure that legislative order and good practice is followed. To apply this to the everyday work of Bigbank, we have developed policies and internal rules of procedure that govern the daily work of the organisation.

We observe all rules, legal and regulatory requirements, and best practice conventions which apply to the provision of credit including the principles of responsible lending. This way we can make sure that the credit we provide meets the customer's needs and has been designed so that the customer can repay it on the agreed terms.

Our goal is to increase the consumers' awareness of the nature of credit products and the risks involved in borrowing. This will help consumers make informed and responsible decisions which are based on a review of different offers and take into account their personal preferences and needs. In practice we always emphasise that borrowing decisions should not be made lightly and the need for a loan should be carefully considered. We also always recommend that our customers take loan offers from different service providers in order to find a solution that is the best for them. We approach all our customer individually and try to find solutions that fit them best – even when the customer has run into settlement difficulties.

Responsible lending, raising awareness of it, and improving general financial education are our daily priorities. In partnership with other leading banks operating in Estonia, we contribute to these causes through the activities of the financial education and communication committee of the Estonian Banking Association. As a member of FinanceEstonia, we are also actively involved in designing the Estonian financial services environment and developing financial technology. We participate in this organisation because we want our financial services market to have a diverse range of services and reasonable regulation.

With outmost high priority of Bigbank upon servicing customers, is the prevention of money laundering and terrorism financing, and the implementation of all relevant requirements, with the aim of reducing the probability of the Estonian financial sector being used for criminal purposes, decreasing systemic risks and increasing the stability, reliability and transparency of the financial sector. highest immediately after the signature of the contract and interaction with our customer service staff. Strong customer relationships are largely underpinned by a positive shift in Bigbank's image in the media.

ECONOMIC ACTIVITIES

Bigbank is a successful privately held credit institution with a strategy, which emphasises sustainable and profitable growth with a long-term target that return on equity (ROE) should be above 15%. This level of profitability allows the Group to grow without additional capital injections. In 2017-2019 we were investing heavily in the development of our core system Nest to be a modern highly automated digital bank providing seamless financial services with a focus on lending and accepting term deposits. In 2020 substantial investments into Nest will continue.

Bigbank is not listed on any stock exchange and holds no ratings by public rating agencies. Nevertheless, we value transparency and proper reporting. Thus, we prepare our public reports in a manner that is useful for the reader.

We have established the required internal regulations covering sourcing and outsourcing activities and carefully select our business partners and vendors.

According to Bigbank dividend policy the precondition for dividend payment is that all the regulatory requirements are met. The Group may pay a minimum of 3,000 thousand euros of the Group audited annual net profit in dividends, income tax included, but not exceeding total of 6,000 thousand euros per calendar year. The dividend has been 5,000 thousand euros distributed for 2018 and for 2017 (6,000 thousand euros is expected for 2019).

Bigbank operates through permanent establishments (branches) in five European countries, where it is also registered as a local taxpayer. Bigbank pays all applicable taxes in all the countries where it operates.

ENVIRONMENTAL ACTIVITIES

We make continuous efforts to reduce the environmental impacts of our activities. We seek for ways to reduce business travel and encourage our staff to hold video conferences for both meeting and training purposes. We continue to optimise our processes, primarily through three methods:

- Agile Development, which means short development cycles and constant improvement;
- Lean Operations Management, which is aimed at minimising waste, standardising processes and offering highest value to the customer;
- 4 Disciplines of Execution, which helps maintain focus throughout the organisation.

Our products are digital but we use hardware to offer and provide them. To increase the environmental sustainability of our operations, we recycle our hardware to the maximum and keep its energy costs under control. For example, we have installed a program in our desktop computers which significantly reduces their electricity consumption at night time and weekends when no one is using them. In addition, we sort our waste according to the options offered by the building managers. For example, at our Tartu office, which has a class C energy efficiency certificate, we have set up waste sorting sections where our staff sort biodegradable and municipal waste as well as plastic, metal and glass packaging.

COMMUNITY AND SOCIETY

At Bigbank, we believe that each of us can help make the world around us a better place. We are dedicated and observe the principles of responsible lending in our daily work, contribute actively to the advancement of financial education in all the markets where we operate, and support initiatives important for society through sponsoring and charity work.
As a bank, we understand and recognise our role in the communities where we operate and contribute to the development of those communities. We value healthy lifestyles, cultivation of the mind, and the sustainability of the community. Accordingly, for years we have supported culture, sports, young people and large families through various charity and sponsoring projects.

SPONSORSHIP AND CHARITABLE ACTIVITIES

In 2019, our largest and most outstanding support activities were as follows:

Supporting volleyball. In August 2018, Bigbank AS prolonged its cooperation with the volleyball club SK Duo and signed a new 3-year sponsorship contract of 450,000 euros. Since 2012, Bigbank has been the name sponsor of the Estonian men's volleyball team, **Bigbank Tartu** and since 2018 also the name sponsor of club's women's team, **Tartu Ülikool Bigbank.**

Throughout the years of sponsorship, our aim has been to contribute to the development of this field and Estonian sports in general. We are proud to say that during the years of our collaboration, we have witnessed an enormous leap in the development of Estonian volleyball. Estonian national men's team has qualified for the European Volleyball Championships several times during that time.

In 2019, we rejoiced at Bigbank Tartu volleyball team winning Estonian Cup and Baltic Champions League and becoming second at Estonian Championships. Tartu Ülikool Bigbank's women's volleyball team became Estonian Champions and came second in both Baltic League and Estonian Cup 2019.

Bigbank's Large Family Day. Since 2005, Bigbank has been working with the Estonian Association of Large Families to offer large families with four or more children an opportunity to enjoy a special active day full of fun. Additionally, every year we recognise an active large family that has made a positive impact on the community with the Large Family of the Year title and award. In 2019, the winner of the Large Family of the Year title and award of 7,000 euros put up by Bigbank was the Soon family from Võrumaa that has four children.

Charity fundraising lunches. For several years our employees have been organising charity fundraising lunches to support those in need. Similar to previous years, also in 2019 the staff of our Tartu office cooked delicious dishes for their colleagues. The money raised was donated to purchasing equipment necessary for physically disabled students of Tartu Herbert Masing School.

Animal shelter campaign. For the sixth consecutive year we organised a charitable social media campaign #laiBigbankziedo (#letBigbankDonate). The purpose of the project is to raise the public's awareness of animal welfare issues and support the Labas majas animal shelter. We invited the users of Facebook and Instagram to post pictures of themselves with their pets using the hashtag #laiBigbankziedo. For each posted picture we supported the shelter with 1 euro. In 2019, we raised 4,000 euros which was spent on heating the shelter's 1,000 square metre premises during the winter season.

Marathons in Latvia. For the fifth year in a row we promoted healthy lifestyles by sponsoring Latvia's biggest series of running events which consists of eight full and eight half marathons. The marathons are organised in the summer in the eight Latvian cities: Jelgava, Ventspils, Valmiera, Kuldiga, Rezekne, Sigulda, Liepaja and Daugavpils. In 2019, the series attracted over 25,000 active lifestyle supporters from all age groups.

Volunteering in a Salvation Army's fundraiser. This is an annual charity fundraiser called the Christmas Cauldron to help low-income families at Christmas. There are several collection points all over Finland where people can drop money in collection boxes in the shape of big cauldrons. Also, presents such as clothes and toys are welcome. The employees of our Finnish branch contributed to the fundraiser by guarding the cauldrons in several shifts on two days.

Bigbank's Large Family Day in Estonia, 2019

MEMBERSHIP IN ORGANISATIONS

Bigbank's strategy is to build a strong international reputation and gain recognition as a valuable financial partner. This includes participating in professional organisations and contributing to their work.

Bigbank is a long-term member of the Estonian Chamber of Commerce and Industry and FinanceEstonia. Bigbank is also a member of the Estonian Banking Association and is actively involved in its working groups.

Bigbank is a member of the payment system SWIFT (The Society for Worldwide Interbank Financial Telecommunication) and the cross border settlement system in Euro TARGET2 (Trans-European Automated Real-time Gross Settlement Express Transfer system) managed by Eesti Pank. Bigbank has joined the SEPA (Single Euro Payments Area) Credit Transfer and Instant Credit Transfer scheme as an indirect member.

Caring

We listen, understand as well as support our customers and each other.

Corporate governance report

The Corporate Governance Recommendations (CGR) promulgated by the Estonian Financial Supervision Authority is a set of guidelines designed for listed companies.

Although Bigbank AS's shares are not traded on a regulated market and Bigbank AS has not issued listed bonds either, Bigbank AS has elected to comply, where possible, with the practice suggested by the CGR and the "comply or explain" principle. However, many provisions of the CGR are intended for companies with a wide shareholder base and cannot be adjusted to entities with a limited number of shareholders.

As a credit institution, Bigbank AS is subject to supervision by the Estonian Financial Supervision Authority and its activities are regulated, among other legislation, by the Credit Institutions Act that imposes specific management, governance and reporting requirements. The company is governed through general meeting, the supervisory board and the management board. Election, resignation, removal and authorisation of members of the management board are regulated by the Commercial Code, the Credit Institutions Act and the company's articles of association.

The sections below provide an overview of the governance of Bigbank AS and the requirements of the CGR that are currently not complied with together with relevant explanations. The majority of requirements that are not complied with concern Bigbank AS's shareholder structure and related issues.

GENERAL MEETING

The general meeting that convened on 28th of February 2019 approved the company's annual report, allocation of profit for 2018. 100% of the votes determined by shares were represented at the meetings.

Bigbank AS does not comply with the provisions of the CGR under which the company should publish on its website notice of a general meeting (article 1.2.1), essential information on the agenda of a general meeting (article 1.2.3), and the proposals of the supervisory board and the shareholders regarding the agenda items (article 1.2.4). In 2019, the general meeting was not attended by the members of the management board, the auditor and the members of the supervisory board that are not shareholders (article 1.3.2). Bigbank AS does not make observing the general meeting possible by means of communication equipment (article 1.3.3).

The above requirements are not applicable to a company that has only two shareholders who are also members of the supervisory board and are therefore informed about the company's activity on a current basis. Bigbank AS uses the simplified method of giving notice of the general meeting that is allowed by section $29^4(1^1)$ of the Commercial Code or the company exercises the right of adopting decisions without calling a general meeting that is provided in section 305(2) of the Commercial Code because Bigbank has only two shareholders and consensus in the adoption of decisions is customary.
In other respects, Bigbank AS complies with the provisions of part I of the CGR.

SUPERVISORY BOARD

The supervisory board of Bigbank AS has five members (according to the articles of association the number may range from five to seven):

- **Parvel Pruunsild** – chairman of the supervisory board
- **Vahur Voll** – member of the supervisory board
- **Andres Koern** – member of the supervisory board
- **Juhani Jaeger** – member of the supervisory board
- **Raul Eamets** – member of the supervisory board

The activities of the supervisory board are governed, among other legislation, by the Credit Institutions Act that sets forth requirements for members of the supervisory board, the cooperation between the supervisory board and the management board, and the control mechanisms established by the supervisory board.

The company does not deem it necessary to provide more detailed information about the remuneration of the members of the supervisory board because the effect of the remuneration on the company's financial performance is not significant (article 3.2.5). All members of the supervisory board attended at least half of the meetings held in 2019. As far as the company is aware, in 2019 the members of the supervisory board did not have any material conflicts of interest as defined in article 3.3.2 of the CGR. Transactions with related parties are disclosed in note 28.

The CGR sets forth the independence requirement for members of the supervisory board (article 3.2.2). Two out of the five supervisory board members are shareholders who each hold 50% of the shares and both have served on the supervisory board for over ten years. The company is of the opinion that these connections do not involve a significant risk of a conflict of interest that could lead to the adoption of a decision detrimental to Bigbank AS and that the independence of the supervisory board is ensured. Other supervisory board members have no known connection with the company except for their board member remuneration.

Bigbank AS publishes neither the information about the existence, responsibilities, composition and structural position of the committees created by the supervisory board on its website (article 3.1.3) nor the details of division of labour of the management board and the supervisory board (article 4.1). Considering that the audit committee has been elected by the supervisory board whose members include shareholders and that the members of the audit committee have been elected from among the members of the supervisory board, disclosure of this information on the company's website is not relevant for observing the interests of the shareholders and the investors. Information on the credit committee is not published on the website either as it has no significant value for investors. Shareholders are also members of the supervisory board and they are thus informed.

In other respects, the company complies with parts III and IV of the CGR.

MANAGEMENT BOARD

In 2019, Pavels Gilodo left the management board and Argo Kiltsmann, a head of finance area, became a member of the management board. Martin Länts was elected as a chairman of the management board.

As of 31 December 2019 the management board of Bigbank AS had four members (under the articles of association the number may range from three to five):

- **Martin Länts** – chairman of the management board
- **Sven Raba** – member of the management board
- **Mart Veskimägi** – member of the management board
- **Argo Kiltsmann** – member of the management board

The activities of the management board are governed, among other legislation, by the Credit Institutions Act that sets forth specific requirements for members of the management board and the principles of their remuneration as well as guidance on how to prevent conflicts of interest and avoid breaching the prohibition on competition. According to the Commercial Code and the articles of association, the company may be represented by any member of the management board acting alone.

The management board acts in the best interests of the company, the shareholders and the creditors and is guided by those interests in managing the company's risks, establishing the organisational structure and organising work within the company. The members of the parent company's management board are represented in management bodies of the subsidiaries: Martin Länts; Mart Veskimägi and Sven Raba are members of the council of Baltijas Izaugsmes Grupa AS.

In 2019, Bigbank AS did not comply with article 2.2.7 of the CGR, which provides that the benefits and bonus schemes of each member of the management board should be published on the corporate website and in the corporate governance report and that the principles of remunerating management board members should be explained at the general meeting.

Bigbank AS publishes the aggregate remuneration of the members of the Group's management board in its annual report, transactions with related parties are disclosed in note 29. In addition, the company observes the requirements of the legislation regulating the disclosure of a credit institution's remuneration policy. The requirement of disclosing the remuneration of each member of the management board is primarily aimed at informing the shareholders. In view of the shareholder structure of Bigbank AS, detailed disclosure of this information in the company's corporate governance report is not necessary. The principles of remunerating the members of the management board were not explained at the general meeting because the shareholders are on the supervisory board and thus aware of the principles.

In other respects, the company complies with the provisions of part II of the CGR.

DIVERSITY AND INCLUSION POLICY

At Bigbank AS we believe that a diverse and inclusive workforce is critical to running a sustainable and successful business. Bigbank AS is committed to supporting a diverse work environment in which everyone is treated fairly and with respect.

For Bigbank AS diversity means that every employee with his/her different abilities, qualifications and life experience, is part of the team. Differences, gender equality and diversity provide Bigbank AS with the ability to draw on a variety of experience and competencies that helps increase profitability and ensure that the Bigbank remains an attractive employer. Consequently, gender equality and diversity are of strategic importance.

All employees regardless of gender, ethnic background, religion or belief, age, sexual orientation or physical disability should have equal access to career and other opportunities.

Working conditions, salaries, benefits and other employment terms are designed with the aim of providing equal opportunities and making it easier for all employees to combine work, private life and parenthood.

Bigbank builds talented and diverse teams to drive business results. Talent comes from all cultures, countries, races, genders, sexual orientations, abilities, beliefs, backgrounds and experiences. Bigbank AS creates respectful and inclusive environments where people can thrive. All of Bigbank AS's employees are responsible for treating colleagues with dignity and respect and creating an inclusive culture free from discrimination, bullying, harassment and victimisation irrespective of age, colour, disability, ethnic or national origin, gender, gender expression, gender identity, marital status, pregnancy, race, religion or belief, or sexual orientation.

DISCLOSURE OF INFORMATION

Articles 5.2 and 5.3 of the CGR are not observed in the following: the financial calendar, information about general meetings and the schedule of meetings specified in article 5.6 of the CGR are not disclosed on the corporate website.

In 2019, Bigbank AS did not publish its financial calendar because the regularity of reporting is provided, among other things, in the Credit Institutions Act. The company issues quarterly reports within two months after the end of each quarter. Disclosure of a term for publishing a notice of calling a general meeting is not relevant in view of the small number of shareholders.

Currently Bigbank AS does not deem it necessary to publish information about meetings with investors and analysts or media and the presentations arranged for them on its website because no price sensitive information is disseminated at those meetings (articles 5.5. and 5.6). The information about general meetings is not published because of the small number of shareholders.

All the information is not currently available in English at the websites (article 5.2), as the Group does not consider it necessary regarding the shareholders' circle. In other respects, the company complies with the provisions of part V of the CGR.

REPORTING

Bigbank AS is audited by Ernst & Young Baltic AS since 2013. Olesia Abramova is the lead auditor. Bigbank AS complies with the auditor rotation requirement.

Bigbank AS does not observe this part of article 6.1.1 of the CGR, which provides that the auditor should attend the meeting of the supervisory board that reviews the annual report. The supervisory board is informed about the company's performance on a quarterly basis. Upon necessity the information provided to the supervisory board includes information about the results of audit procedures that have been conducted. The members of the supervisory board have not deemed it necessary to have the auditor attend the meeting of the supervisory board that reviews the annual report. The members of the supervisory board do not sign the annual report. The position of the supervisory board is presented in the supervisory board's written report on the company's annual report.

In addition to the statutory audit, the following non-audit services were provided by the auditor in the reporting period: a) general tax advice in Sweden, and b) reporting on the accuracy of data and the eligibility of loans included in the reports related to the ECBs targeted long-term refinancing operations (TLTRO-III) the Group is taking part in.

The supervisory board does not fully comply with articles 6.1.1 and 6.2.1 of the CGR that regulate notifying and informing shareholders because both shareholders are on the supervisory board and thus informed about the work of the supervisory board and the auditor.

RISK MANAGEMENT AND CONTROL FUNCTIONS

The Group's supervisory board carries out ultimate supervision of the Group's activities by enacting the general risk management principles and strategy required for the proper functioning of the Group's risk organisation and by providing a basis for an adequate internal control system.

The internal control system is a management tool that covers the activities of the entire Group and is an integral part of the Group's internal processes. The management board is responsible for the establishment and functioning of an effective internal control system. The need for and the scope of controls is determined by the extent and nature of the risks. The management board has to ensure that the Group's organisation and administration are appropriate and that the Group's operations are in compliance with external and internal rules. The management board reports regularly to the supervisory board on developments in the Group's risk exposure.

The primary objectives of the risk control functions are to protect the Group's financial strength and limit the impact of potential adverse events on the Group's capital, liquidity, and financial results.

The Group uses the three lines of defence model, where the first line of defence is the business units and branches. Managers of all levels are responsible for the effectiveness of risk controls in their units, branches and areas. The second line of defence is the functions and units responsible for overseeing the Group's risk management: the risk management and credit risk area and the compliance unit. The Group's internal audit department provides independent assurance and is the third line of defence.

The compliance unit is responsible for ensuring that the Group complies with all applicable laws, rules and regulations, because failure to comply may result in regulatory sanctions (including restrictions on business activities, fines or additional reporting requirements) and financial and/or reputational damage. The compliance function acts proactively to assure the Group's compliance through information, advice, control and follow-up. The compliance unit reports directly to the management board. The credit risk area is responsible for managing the credit approval process, ensuring sound day-to-day credit risk management and acting as a second line of defence in credit risk taking (the Group's head of credit and local credit risk officers). Local credit risk officers report regularly to country credit committees which have the power to veto credit decisions and to approve loans which are beyond the authority of lower levels. The highest level decisions are made by the Group's credit committee, which has the ultimate right to veto credit decisions. The Group's credit committee is formed by the supervisory board. The head of the credit risk area reports regularly to the risk committee and the management board.

The risk management area's responsibility is to develop and implement the Group's risk management framework; assist risk owners and management in developing processes and controls to manage and assess risks; facilitate and monitor implementation of risk management practices by risk owners; conduct independent risk identification, assessment, monitoring and reporting; provide guidance and training on risk management processes for raising risk awareness; and identify risk-related issues.

The risk management area consists of the operational risk control unit, the quality control unit, the financial crime prevention unit and the risk reporting and financial risk control unit. The heads of the units of the risk management area report regularly to the risk committee and the management board on the Group's risk profile and overall development in the risk level.

Within the risk management area, the financial risk prevention unit's (FCPU) role is to ensure that the Group fulfils its obligations in relation to anti-money laundering, terrorist financing prevention and monitoring politically exposed persons as required by the law and internal regulations and to facilitate the development of controls that support the detection and prevention of fraud. The FCPU reports directly to the management board.

The objectives and principles of risk management are described in more detail under note 3. Risk and capital management.

The internal audit unit is a structural unit of the Group, which is directly accountable to the Group's supervisory board and is therefore independent of the Group's management board. The unit consists of two internal auditors and the head of the unit. Internal audit is an independent, objective assurance and consulting activity designed to add value and improve the Group's operations by using a systematic and disciplined approach to evaluate the efficiency and effectiveness of the risk management, governance and control processes. Internal audit adds value if it is in concordance with the Group's strategic objectives, focuses on important business risks, operates proactively and proficiently, and meets the expectations of the stakeholders. The internal audit unit acts on the basis of the statute approved by the Group's supervisory board. The statute of the internal audit unit describes the requirements to the internal audit with regard to independence, proficiency, authority, tasks, and scope of activities as well as the principles of quality assurance. The internal audit unit's work plan is approved by the Group's supervisory board.

WHISTLEBLOWING HOTLINE

The whistleblowing hotline is part of the Group's corporate governance culture and its aim is to support the enforcement of the Group's values and agreed code of conduct, promote openness and consideration of other employees.

Bigbank's employees have a possibility to send notifications of possible internal misconduct, that may include breaching the general rules of conduct established by the Group and procedures regulating internal work organisation as well as violation of legislation and neglect for the principles of good banking practice.

The whistleblowing hotline is coordinated by the head of the internal audit unit, who reports directly to the supervisory board of Bigbank AS.

REMUNERATION PRINCIPLES

The Group's remuneration policy is established by the supervisory board in order to ensure a fair and transparent remuneration system that would be in compliance with prudent and efficient risk management principles and that would support achievement of the Group's long-term objective – to become recognised as the best financial services provider by customers and to ensure effective risk management and the Group's strong reputation as an employer in all countries where Bigbank's branches and subsidiaries operate. The purpose is to ensure that remuneration decisions deliver sustainable value growth for all key stakeholders, including customers, shareholders and employees; to promote desired performance, conduct and values'-based behaviour and to ensure that the manner of remuneration does not impede the employees from acting honestly, fairly, transparently and professionally, taking into account the rights and interests of customers and to prevent the risk that the remuneration drives excessive risk taking and conflict of interest The remuneration system ensures equal treatment of employees as rewards are based on the employee's performance and professional development during the year.

The supervisory board approves the Group's remuneration policy and reviews it annually in the fourth quarter or as needed. According to the policy, the management board approves the remuneration principles, including the principles for establishing annual key performance indicators (KPIs), evaluating employee performance and reviewing fixed pay. Remuneration principles also include guidelines for establishing performance pay principles at the branch or function level. The management board monitors the implementation of the remuneration principles, asking feedback from employees at least once a year in December.

The core principle of the remuneration system is to ensure a good balance between individual and team performance and quality risk management which takes into account capital adequacy and liquidity requirements along with trends in the economic environment.
The remuneration structure consists of two parts:

- Fixed remuneration including:
  - a basic monthly salary fixed in the employment contract, which is determined based on the employee's responsibilities and competence and reviewed annually based on the employee's performance and the trends prevailing in the labour market of the country involved;
  - benefits provided by the Group to all employees in all countries at the same rate, for example sports benefits, compensated absences for taking care of health, birth

benefits etc.;
- benefits arising from local legislation or collective agreements.

- Variable remuneration including:
  - performance pay agreed with the employee, which depends on the achievement of the Group's long-term objectives and fulfilment of relevant, measurable and balanced criteria;
  - performance pay paid on objective grounds and generally on a one-off basis, based on extraordinary results and/or engagement of the employee, timely fulfilment of specific projects and other similar situations.

The establishment of a separate remuneration committee is not deemed to be necessary, and the role of the remuneration committee is fulfilled by Bigbank's supervisory board which is responsible for approving and supervising the group-wide remuneration policy and adopting decisions related to the remuneration of the members of the management board, the internal audit function and the material risk takers. The remuneration policy is reviewed by the supervisory board at least once a year. Preparation of the policy and related group-wide internal regulations is the responsibility of the head of support services who makes amendment proposals to the management board, which submits relevant amendment proposals for approval by the supervisory board. General remuneration principles, including the rules for the provision of variable remuneration, are approved by the Group's management board. Branch- and area-specific remuneration decisions are made by heads of branches and areas in line with the Group's policy and rules.

As required by the law, Bigbank has defined material risk takers which include the senior management (members of the supervisory and management boards); employees responsible for control functions; employees who have a significant impact on the Group's risk profile; and staff whose remuneration equals or exceeds the lowest remuneration of the members of the Group's management board. The self-assessment is performed on a consolidated level including all branches and subsidiaries of the Bank. At least once a year, in December, or when the Group structure changes affecting the list of material risk takers and/or new positions are established affecting the list of material risk takers, the list of positions evaluated as material risk takers shall be evaluated according to the qualitative and quantitative criteria set out in Article 3 and on the quantitative criteria as set out in Article 4 of the of the Regulation (EU) No 604/2014 of 4 March 2014 by the head of risk management area, chief compliance officer, head of WOW support services and members of the management board to determine what positions should be considered as material risk takers. The supervisory board approves the list of material risk takers based on the proposal of the management board. As at 31 December 2019, the list included 32 positions. The list is changed based on changes in staff or the Group's work arrangement. The principles underlying the fixed remuneration of material risk takers are the same as for the rest of the Group's employees. The share of performance related pay in the total annual remuneration may not exceed 100% of annual fixed remuneration which should ensure carefully calculated risk-taking. The Group may withhold performance related pay either in full or in part, reduce performance related pay, or demand partial or full repayment of disbursed performance related pay when the Group's results do not meet the target.

Bigbank AS operates in one business line. Therefore, it does not disclose quantitative summary data on remuneration by business line.

In 2019, the remuneration (excluding social costs) provided to material risk takers of the group and its subsidiaries totalled 2,551 thousand euros, the figure consisting of fixed remuneration of 2,095 thousand euros, performance related pay of 453 thousand euros and severance payment of 3 thousand euros. The performance related pay allocated for performance in 2019, is determined at the end of the first quarter of the following financial year, and management estimates that the amount of the reserve at 31 December 2019 is sufficient.

Result oriented

We are professional and committed to sustainable knowledge-based performance.

Olga Jeromenok
Management Accounting Analyst

(In thousands of euros)

Consolidated financial statements

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December	Note	2019	2018
Assets			
Cash balances at central banks	4	32,855	29,691
Due from other banks	4	21,085	36,261
Debt instruments at fair value through other comprehensive income	5	31,390	13,484
Loans to customers	6,7	459,656	427,964
Other receivables	8	1,738	1,484
Prepayments	9	1,265	1,732
Property and equipment	10	5,157	3,625
Investment properties	11	1,781	1,866
Intangible assets	12	19,254	12,381
Assets classified as held for sale		12	29
Total assets		**574,193**	**528,517**
Liabilities			
Loans from central banks	13	23,000	-
Deposits from customers	14	392,838	393,020
Lease liability		2,096	-
Subordinated notes		4,965	4,960
Provisions		2,137	1,884
Other liabilities	15	7,118	5,197
Deferred income and tax liabilities	16	986	2,282
Total liabilities		**433,140**	**407,343**
Equity	17		
Paid-in share capital		8,000	8,000
Capital reserve		800	800
Other reserves		1,232	806
Retained earnings		131,021	111,568
Total equity		**141,053**	**121,174**
Total liabilities and equity		**574,193**	**528,517**

The notes on pages 49 to 129 are an integral part of these consolidated financial statements.

(In thousands of euros)

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Note	2019	2018
Interest income	18	66,950	66,386
Interest expense	19	-6,390	-6,099
Net interest income		**60,560**	**60,287**
Fee and commission income		4,287	3,573
Fee and commission expense		-240	-312
Net fee and commission income		**4,047**	**3,261**
Net loss on exchange differences		-194	-315
Net loss/profit on derecognition of non-financial assets		-13	-274
Other income	20	1,190	2,075
Total income		**65,590**	**65,034**
Salaries and associated charges	21	-14,917	-15,089
Other operating expenses	22	-11,722	-13,023
Depreciation and amortisation expense	10,12	-3,298	-2,063
Provision expenses		-304	-1,261
Net impairment losses on loans and financial investments	7	-6,675	-11,355
Gains/losses resulting from changes in the fair value of investment properties	11	100	-61
Other expenses	23	-2,591	-2,755
Profit/loss from assets classified as held for sale		23	-256
Total expenses		**-39,384**	**-45,863**
Profit before income tax		**26,206**	**19,171**
Income tax	27	-1,753	-1,645
Profit for the year		**24,453**	**17,526**
Other comprehensive income			
Other comprehensive income to be reclassified to profit or loss in subsequent periods:			
Exchange differences on translation of foreign operations		181	322
Changes in the fair value of debt instruments at FVOCI		4	-191
Net other comprehensive income to be reclassified to profit or loss in subsequent periods	17	**185**	**131**
Other comprehensive income to be reclassified to profit or loss in subsequent periods:			
Revaluation of land and buildings		241	-
Net other comprehensive income not to be reclassified to profit or loss in subsequent periods		**241**	**-**
Other comprehensive income for the year		**426**	**131**
Total comprehensive income for the year		**24,879**	**17,657**
Basic earnings per share (EUR)	30	306	219
Diluted earnings per share (EUR)	30	306	219

The notes on pages 49 to 129 are an integral part of these consolidated financial statements.

(In thousands of euros)

CONSOLIDATED STATEMENT OF CASH FLOWS

	Note	2019	2018
Cash flows from operating activities			
Interest received		60,406	60,381
Interest paid		5,586	-4,854
Salary and other operating expenses paid		-29,316	-31,008
Other income and fees received		6,535	8,290
Other expenses and fees paid		-3,808	-5,197
Recoveries of receivables previously written off		25,479	36,422
Loans provided		-266,377	-276,236
Repayment of loans provided		209,155	180,760
Change in mandatory reserves with central banks and related interest receivables	4	371	-269
Proceeds from customer deposits		94,327	135,912
Paid on redemption of deposits		-91,662	-75,146
Income tax paid		-2,006	-2,153
Effect of movements in exchange rates		-112	-186
Net cash used in / from operating activities		**-2,594**	**26,716**
Cash flows from investing activities			
Acquisition of property and equipment and intangible assets	10,12	-8,624	-7,426
Proceeds from sale of property and equipment		92	29
Proceeds from sale of investment properties		138	38
Acquisition of financial instruments	5	-21,824	-3,025
Proceeds from redemption of financial instruments	5	4,177	741
Net cash used in investing activities		**-26,041**	**-9,643**
Cash flows from financing activities			
Interest paid on subordinated bonds	28	-330	-330
Proceeds from loans from central bank	13,28	23,000	-
Payment of principal portion of lease liabilities	28	-723	-
Dividends paid	17	-5,000	-5,000
Net cash from / used in financing activities		**16,947**	**-5,330**
Effect of exchange rate fluctuations		47	-243
Decrease/increase in cash and cash equivalents		**-11,641**	**11,500**
Cash and cash equivalents at beginning of year	4	64,621	53,121
Cash and cash equivalents at end of year	4	**52,980**	**64,621**

The notes on pages 49 to 129 are an integral part of these consolidated financial statements.

(In thousands of euros)

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

	Attributable to equity holders of the parent				
	Paid-in share capital	Capital reserve	Other reserves	Retained earnings	Total
Balance at 1 January 2018	**8,000**	**800**	**675**	**103,771**	**113,246**
Changes on initial adoption of IFRS 9	**-**	**-**	**-**	-4,729	-4,729
Restated balance at 1 January 2018	8,000	800	675	99,042	108,517
Profit for the year	-	-	-	17,526	17,526
Other comprehensive income					
Exchange differences on translating foreign operations	-	-	322	-	322
Net change in fair value of debt instrument at FVOCI	-	-	191	-	191
Total other comprehensive income	**-**	**-**	**131**	**-**	**131**
Total comprehensive income for the year	**-**	**-**	**131**	**17,526**	**17,526**
Dividend distribution	-	-	-	-5,000	-5,000
Total transactions with shareholders	**-**	**-**	**-**	**-5,000**	**-5,000**
Balance at 31 December 2018	**8,000**	**800**	**806**	**111,568**	**121,174**
Balance at 1 January 2019	8,000	800	806	111,568	121,174
Profit for the year	**-**	**-**	**-**	**24,453**	**24,453**
Other comprehensive income					
Exchange differences on translating foreign operations	-	-	181	-	181
Net change in fair value of debt instrument at FVOCI	-	-	4	-	4
Revaluation of land and buildings	**-**	-	241	**-**	241
Total other comprehensive income	**-**	**-**	**426**	**-**	**426**
Total comprehensive income for the year	**-**	**-**	**426**	**24,453**	**24,879**
Dividend distribution	-	-	-	-5,000	-5,000
Total transactions with shareholders	**-**	**-**	**-**	**-5,000**	**-5,000**
Balance at 31 December 2019	**8,000**	**800**	**1,232**	**131,021**	**141,053**

Please refer note 17.
The notes on pages 49 to 129 are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements

NOTE 1. GENERAL INFORMATION AND SIGNIFICANT ACCOUNTING POLICIES

1.1 GENERAL INFORMATION

Bigbank AS is a company incorporated and domiciled in Estonia that holds an activity licence of a credit institution. The consolidated financial statements as at and for the year ended 31 December 2019 comprise Bigbank AS (also referred to as the "parent company"), its Latvian, Lithuanian, Finnish, Spanish and Swedish branches and its subsidiaries AS Baltijas Izaugsmes Grupa, OÜ Rüütli Majad and Balti Võlgade Sissenõudmise Keskus OÜ and the subsidiary of Balti Võlgade Sissenõudmise Keskus OÜ - SIA Baltijas Paradu Piedzinas Centrs (together referred to as the "Group"). The business name Bigbank AS was registered on 23 January 2009. The Bank's former business name was Balti Investeeringute Grupi AS.

STATEMENT OF COMPLIANCE

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board (IASB) as adopted by the European Union (IFRS EU). The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements except where indicated otherwise.

Under the Estonian Commercial Code, final approval of the annual report including the consolidated financial statements that has been prepared by the management board and approved by the supervisory board rests with the general meeting. Shareholders may decide not to approve the annual report that has been prepared and submitted by the management board and may demand preparation of a new annual report.

These consolidated financial statements include the primary statements of the parent company (see note 32) in addition to required part prepared under International Financial Reporting Standards as adopted by the European Union because it is required by the Estonian Accounting Act and capital ratios (see note 32) for regulatory purposes that have been prepared in accordance with Regulation (EU) no 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms. These parent company primary statements are not separate financial statements as defined by IAS 27.

The management board of Bigbank AS has prepared these consolidated financial statements and authorised them for issue on 27 February 2020.

The group annual report, which has been authorised for issue by the management board, needs to be approved by the supervisory board and the shareholders. The shareholders may decide not to approve the group annual report but they have never done so and there is no reason to expect that they will.

BASIS OF PREPARATION

The figures reported in the financial statements are presented in thousands of euros. The consolidated financial statements are prepared on the historical cost basis except that some assets and liabilities are measured at their fair values (financial instruments categorised at fair value through other comprehensive income (FVOCI) and investment properties) and on the revaluation method basis (land and buildings). Group entities apply uniform accounting policies. The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. Apart from the accounting policy changes resulting from the adoption of IFRS 16 effective from 1 January 2019, these policies have been consistently applied to all the periods presented, unless otherwise stated

In accordance with the Estonian Accounting Act, the parent company's unconsolidated financial statements (statement of financial position, statement of comprehensive income, statement of cash flows and statement of changes in equity) are disclosed in the notes to the consolidated financial statements. The financial statements of Bigbank AS are presented in note 32 *Unconsolidated statements of parent company as a separate entity*. The parent company's financial statements are prepared using the same accounting policies and measurement bases as those applied on the preparation of the consolidated financial statements except that in the unconsolidated financial statements investments in subsidiaries and associates are measured at cost.

1.2. CHANGES IN ACCOUNTING POLICIES
ADOPTION OF NEW OR REVISED STANDARDS AND INTERPRETATIONS

IFRS 16 Leases

The Group has adopted IFRS 16 using the modified retrospective method from 1 January 2019, and has not restated comparatives for the 2018 reporting period, as permitted under the specific transitional provisions in the standard. The reclassifications and the adjustments arising from the new leasing rules are therefore recognised in the opening balance sheet on 1 January 2019.

The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and d requires lessees to recognise most leases on the balance sheet. Lessor accounting under IFRS 16 is substantially unchanged from IAS 17. Lessors will continue to classify leases as either operating or finance leases using similar principles as in IAS 17. Therefore, IFRS 16 does not have an impact for leases where the Group is the lessor.

On the adoption of IFRS 16, the Group recognised lease liabilities in relation to leases which had previously been classified as operating leases under IAS 17, *Leases*. The liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as at 1 January 2019. The weighted average lessee's incremental borrowing rate applied to the lease liabilities as at 1 January 2019 was 1.21%. In applying IFRS 16 for the first time, the Group used the following practical expedients permitted by the standard:

- applying a single discount rate to a portfolio of leases with reasonably similar characteristics;
- relying on previous assessments on whether leases are onerous as an alternative to performing an impairment review – there

(In thousands of euros)

were no onerous contracts as at 1 January 2019;

- accounting for operating leases with a remaining lease term of less than 12 months as at 1 January 2019 as short-term leases;
- excluding initial direct costs from the measurement of the right-of-use asset at the date of initial application; and
- sing hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

The Group also elected not to reassess whether a contract is, or contains a lease at the date of initial application. Instead, for contracts entered into before the transition date the Group relied on its assessment made applying IAS 17, *Leases*, and IFRIC 4, *Determining whether an Arrangement contains a Lease.* For leases previously classified as finance leases the Group recognised the carrying amount of the leased asset and the lease liability as the carrying amounts of the right-of-use asset and the lease liability at the date of initial application, 2,766 thousand euros respectively. The measurement principles of IFRS 16 were only applied after 1 January 2019.

The change in accounting policy affected the following items in the consolidated statement of financial position as at 1 January 2019:

Asset / Liabilities class	Impact of adopting IFRS 16
Increase in property and equipment	2,766
Increase in lease liability	2,766

IFRIC Interpretation 23 *Uncertainty over Income Tax Treatment*

The interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 *Income Taxes*. It does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The interpretation specifically addresses the following:

- whether an entity considers uncertain tax treatments separately;
- the assumptions an entity makes about the examination of tax treatments by taxation authorities;
- how an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates; and
- how an entity considers changes in facts and circumstances.

The Group determines whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments and uses the approach that better predicts the resolution of the uncertainty.
The Group applies significant judgement in identifying uncertainties over income tax treatments. Since the Group operates in a complex multinational environment, it assessed whether the interpretation had an impact on its consolidated financial statements.

Upon the adoption of the interpretation, the Group considered whether it has any uncertain tax positions, particularly those relating to transfer pricing. The Group's - the branches and the subsidiaries' - tax filings in different jurisdictions include deductions related to transfer pricing and the taxation authorities may challenge those tax treatments. The Group determined, based on its tax compliance and transfer pricing study, that it is probable that its tax treatments (including those for the subsidiaries) will be accepted by the taxation authorities. The interpretation did not have an impact on the consolidated financial statements of the Group.

(In thousands of euros)

1.3 SIGNIFICANT ACCOUNTING POLICIES

CONSOLIDATION

Branches

A branch is an economic entity established for offering services on behalf of a company. A branch is not an independent legal person. The company is liable for the obligations arising from the activities of its branch. The company has to maintain separate accounts concerning its foreign branches. The financial statements of a branch with separately maintained accounts are included in the consolidated financial statements from the date the activity of the branch commences until the date the activity of the branch ceases.

Subsidiaries

Subsidiaries are all entities over which the Group has control. Control is achieved when the Group 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. Specifically, the Group controls an investee if, and only if, the Group 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.

Generally, there is a presumption that a majority of voting rights result in control. Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are deconsolidated from the date that control ceases.

		Ownership interest	
Subsidiary	**Country of incorporation**	**2019**	**2018**
AS Baltijas Izaugsmes Grupa	Republic of Latvia	100%	100%
OÜ Rüütli Majad	Republic of Estonia	100%	100%
Balti Võlgade Sissenõudmise Keskus OÜ	Republic of Estonia	100%	100%
SIA Baltijas Parādu Piedziņas Centrs	Republic of Latvia	100%	100%

Transactions eliminated on consolidation

In preparing consolidated financial statements, the financial statements of all entities controlled by the parent (except for subsidiaries acquired for resale) are combined with those of the parent line by line. Intra-group balances and transactions and any unrealised income and expenses and gains and losses arising from intra-group transactions are eliminated in preparing the consolidated financial statements but only to the extent that there is no evidence of impairment. Group entities apply uniform accounting policies. Where necessary, the accounting policies of subsidiaries and branches are adjusted to conform to those adopted for the consolidated financial statements.

FOREIGN CURRENCY

Foreign currency transactions

A transaction in a foreign currency is recorded in the functional currency by applying the exchange rate quoted by the central bank at the date of the transaction. In the statement of financial position, monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the central bank exchange rates ruling at that date. The foreign currency gain or loss on monetary items is the difference between the amortised cost in the functional currency at the beginning of the year and the amortised cost in foreign currency translated at the exchange rate at the end of the year. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign exchange differences arising on retranslation are recognised in the statement of comprehensive income within *Net gain/loss on financial transactions.*

Financial statements of the Group's foreign operations

The financial statements of each Group entity are prepared in the currency of the primary economic environment in which the entity operates ("the functional currency"). The consolidated financial statements are presented in thousands of euros, which is the Group's presentation currency. Accordingly, the assets and liabilities of foreign operations, including fair value adjustments, are translated to euros at the foreign exchange rates of the European Central Bank ruling at the reporting date. The revenues and expenses of foreign operations are translated to euros using the average foreign exchange rate for the period. Exchange differences arising on translating foreign operations are recognised in *Other reserves* in equity and in the statement of comprehensive income, in *Exchange differences on translating foreign operations* in other comprehensive income.

OFFSETTING

Financial assets and financial liabilities are set off and the net amount is presented in the consolidated statement of financial position only when the Group has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

FINANCIAL INSTRUMENTS

Financial instruments – key measurement terms

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 best evidence of fair value is price in an active market. An active market is one in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Fair value of financial instruments traded in an active market is measured as the product of the quoted price for the individual asset or liability and the quantity held by the entity. This is the case even if a market's normal daily trading volume is not sufficient to absorb the quantity held and placing orders to sell the position in a single transaction might affect the quoted price. The quoted market price used to value financial assets is the current bid price.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees, are used to measure fair value of certain financial instruments for which external market pricing information is not available. Fair value measurements are analysed by level in the fair value hierarchy as follows: (i) level one are measurements at quoted prices (unadjusted) in active markets for identical assets or liabilities, (ii) level two measurements are valuations techniques with all material inputs observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices), and (iii) level three measurements are valuations not based on solely observable market data (that is, the measurement requires significant unobservable inputs).

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the transaction had not taken place. Transaction costs include fees and commissions paid to agents (including employees acting as selling agents), advisors, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

Amortised cost (AC) is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any allowance for expected credit losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the gross carrying amount of the financial instrument.

The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount, which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate. For assets that are purchased or originated credit impaired (POCI financial assets) at initial recognition, the effective interest rate is adjusted for credit risk, i.e. it is calculated based on the expected cash flows on initial recognition instead of contractual payments.

Financial instruments – initial recognition

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 AC and investments in debt instruments measured at FVOCI, resulting in an immediate accounting loss.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date on which the Group commits to deliver a financial asset. All other purchases are recognised when the entity becomes a party to the contractual provisions of the instrument.

Financial assets – classification and subsequent measurement – measurement categories

The Group classifies financial assets in the following measurement categories: FVTPL, FVOCI and AC. The classification and subsequent measurement of debt financial assets depends on: (i) the Group's business model for managing the related assets portfolio and (ii) the cash flow characteristics of the asset.

Financial assets – classification and subsequent measurement – business model

The business model reflects how the Group manages the assets in order to generate cash flows – whether the Group's objective is: (i) solely to collect the contractual cash flows from the assets ("hold to collect contractual cash flows",) or (ii) to collect both the contractual cash flows and the cash flows arising from the sale of assets ("hold to collect contractual cash flows and sell") or, if neither of (i) and (ii) is applicable, the financial assets are classified as part of "other" business model and measured at FVTPL.

Business model is determined for a group of assets (on a portfolio level) based on all relevant evidence about the activities that the Group undertakes to achieve the objective set out for the portfolio available at the date of the assessment. Factors considered by the Group in determining the business model include the purpose and composition of a portfolio.

Financial assets – reclassification

Financial instruments are reclassified only when the business model for managing the portfolio as a whole changes. The reclassification has a prospective effect and takes place from the beginning of the first reporting period that follows after the change in the business model.

Financial assets – write-off

Financial assets are written-off, in whole or in part, when the Group exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The write-off represents a derecognition event. The Group may write-off financial assets that are still subject to enforcement activity when the Group seeks to recover amounts that are contractually due, however, there is no reasonable expectation of recovery.

Financial assets – derecognition

The Group derecognises financial assets when (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership, but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose restrictions on the sale.

Financial assets – modification

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, including determining whether a significant increase in credit risk (SICR) has occurred. The Group also assesses whether the new loan or debt instrument meets the solely payments of principal and interest (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 assess 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.

Financial liabilities – measurement categories

Financial liabilities are classified as subsequently measured at AC, except for (i) financial liabilities at FVTPL: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in securities), contingent consideration recognised by an acquirer in a business combination and other financial liabilities designated as such at initial recognition and (ii) financial guarantee contracts and loan commitments.

Financial liabilities – derecognition

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires). An exchange between the Group and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms and conditions of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Cash and cash equivalents

Cash and cash equivalents are items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash and cash equivalents include all interbank placements with original maturities of less than three months. Funds restricted for a period of more than three months on origination are excluded from cash and cash equivalents, both in the statement of financial position and for the purposes of the statement of cash flows. Cash and cash equivalents are carried at AC because: (i) they are held for collection of contractual cash flows and those cash flows represent SPPI, and (ii) they are not designated at FVTPL. The statement of cash flows is prepared using the direct method.

Mandatory reserve deposits with the central banks. Mandatory reserve deposits with the central banks are carried at AC and represent non-interest bearing mandatory reserve deposits, which are not available to finance the Group's day to day operations, and hence are not considered as part of cash and cash equivalents for the purposes of the consolidated statement of cash flows.

Due from other banks. Amounts due from other banks are recorded when the Group advances money to counterparty banks.

Investments in debt securities

Based on the business model and the cash flow characteristics, the Group classifies investments in debt securities as carried at FVOCI. Debt securities are carried at FVOCI if they are held for collection of contractual cash flows and for selling, where those cash flows represent SPPI, and if they are not designated at FVTPL. Interest income from these assets is calculated using the effective interest method and recognised in profit or loss. An impairment allowance estimated using the expected credit loss model is recognised in profit or loss for the year. All other changes in the carrying value are recognised in OCI. When the debt security is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from OCI to profit or loss. Interest income from these financial assets is included in *Interest income.*

The Group's debt instruments at FVOCI comprised solely of quoted bonds that are graded in the top investment category by the Moody's Investors Service and, therefore, are considered to be in stage 1 as low credit risk investments. It is the Group's policy to measure such instruments on a 12-month ECL basis. In all cases, the Group considers that there has been a significant increase in credit risk when contractual payments are more than 30 days past due. As at 31 December 2019, there are no such cases that would be classified under stages 2 or 3.

Loans to customers

Loans and advances to customers are recorded when the Group advances money to purchase or originate a loan due from a customer. Based on the business model and the cash flow characteristics, the Group classifies loans and advances to customers into AC measurement category: loans that are held for collection of contractual cash flows and those cash flows represent SPPI and loans that are not voluntarily designated at FVTPL. Loss allowances are determined based on the forward-looking ECL models.

Financial assets impairment

The Group assesses, on a forward-looking basis, the ECL for debt instruments measured at AC and FVOCI and for the exposures arising from loan commitments and financial guarantee contracts. The Group measures ECL and recognises credit loss allowance at each reporting date. The measurement of ECL reflects: (i) an unbiased and probability weighted amount that is determined by evaluating a range of possible outcomes, (ii) time value of money and (iii) all reasonable and supportable information that is available without undue cost and effort at the end of each reporting period about past events, current conditions and forecasts of future conditions.

For *Loans to customers* and *Debt instruments at FVOCI*, the ECL is based on the 12-month ECL. The 12-month ECL is the portion of lifetime ECLs that results from default events on a financial instrument that are possible within 12 months after the reporting date. However, when there has been a significant increase in credit risk since origination, the allowance will be based on the lifetime ECL.

For *Other receivables*, the Group has applied the standard's simplified approach and has calculated ECLs based on lifetime expected credit losses. The Group has established a provision matrix that is based on the Group's historical credit loss experience.

Recognition of loss allowances for impaired receivables

A receivable is impaired when there is objective evidence, such as an identified event and/or observable data, that an event or events has or have adversely affected the amount and timing of the future cash flows of the customer to the extent that repayment of the entire receivable by the customer, taking into account the collateral, is unlikely and the receivable has been identified as impaired during impairment assessment.

Receivables are assessed for impairment and loss allowances are recognised by reference to credit risk parameters Probability of Default (PD) and Loss Given Default (LGD), which are updated at least once a year or whenever there is a significant change in risk assessments.

Homogenous receivables have similar characteristics such as historical payment behaviour, collateral, or other features. Individual impairment assessment is applied to receivables from companies, receivables exceeding 100,000 euros and other receivables that have not been grouped. Specific impairment allowances are created for an individual receivable or a group of receivables that has or have been found to be impaired, i.e. for impairment losses incurred. The Group assesses receivables for impairment both on an individual and collective basis. Collective impairment assessment is applied to all homogenous groups of receivables whose amount is not individually significant and whose individual assessment would be unreasonable.

Specific impairment assessments are made and specific loss allowances are established using three principal methods:

- the discounted cash flow method, which is used to assess homogenous group of unsecured retail receivables;
- evaluation of the net realisable value of collateral, which is used to assess retail receivables secured with real estate or other assets;
- the combined method, which is used to assess receivables from companies.

Unsecured retail receivables are assessed for impairment by comparing the nominal carrying amount of the item or group of items prior to the recognition of impairment with the present value of the expected future cash flows of the item or group of items, discounted at the effective interest rate. An impairment loss for a receivable or a group of receivables is identified when the total discounted present value of the expected future cash flows of the receivable or group of receivables is less than the carrying amount of the receivable or group of receivables. The difference between carrying value and the present value of expected future cash flows is recognised as the impairment of the receivable or group of receivables. The effective interest rate applied is the original interest rate of the receivable or the weighted average original interest rate of the group of receivables (the rate recorded in the agreement before its termination or expiry).

Impairment methodology for financial assets, including unsecured retail receivables

The Group applies for assessment and accounting of unsecured retail receivables a three-stage approach depending on whether the claim is performing or not and if the claim is performing, whether there any signs for special attention. The methodology is based on Expected Credit Loss (ECL) formula which is calculated by multiplying the Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD). The Group has implemented country-specific PD and LGD estimates by different product types where sufficient statistical data is available. For product types where sufficient statistical data is not yet available the PD and LGD estimates are calculated using estimates of closest similar product type(s). PD and LGD values were re-calculated in the fourth quarter based on the relevant statistical data of the Group. PD estimates are adjusted for forward-looking component which takes into the account expected macroeconomic scenarios in the countries where the Group has credit risk exposures. This approach is summarized as follows:

Stage 1 – 12-month ECL applies to all claims, which have no signs of material increase in credit risk. The ECL will be computed using a 12-month PD that represents the probability of default occurring over the next 12 months. For those assets with a remaining maturity of less than 12 months, a PD is used that corresponds to remaining maturity.

Stage 2 – applies to claims which have sign(s) of a material increase in credit risk recognized as payment delay more than 30 days at the reporting date or in the last six months period prior to the reporting date. Computation of ECL is based on lifetime PD that represents the probability of default occurring over the remaining estimated life of the financial asset.

Stage 3 – applies to defaulted and uncollectible claims or claims which are restructured due to financial difficulties of a counterparty. Similar to Stage 2, the allowance for credit losses will continue to capture the lifetime expected credit losses where the PD is equal to 100%.

Financial assets that are credit-impaired upon initial recognition (POCI) are categorised within Stage 3 with a carrying value already reflecting the lifetime expected credit losses.

ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Group expects to receive. The shortfall is then discounted at an approximation to the asset's original effective interest rate.

Signs of a significant increase in risk may include, but are not limited to a repayment delay of 30 or more days in the last six months of a reporting period. A settlement delay of 30 or more days is assessed based on their actual occurrence. The rest of the signs of increased risk and their impact are analysed case by case and the change in a customer's risk level is made based on management's judgement. This assessment is dynamic in nature, allowing the financial assets to move back to Stage 1 if the increase in credit risk has decreased since origination and there have been no evidences of increase in credit risk in the last six months period.

Definition of default and write-off

Any of the following events regarding the client imply a payment default resulting in insolvency or the possibility of it occurring in the future, in which case the contract is to be classified as non-performing:

i. Improbability of receiving payments. The contract is a performing contract, but on the basis of objective evidence, it may be presumed that the client will be unable to settle all of the financial obligations and the situation cannot be solved satisfactorily.
ii. Payment delay in fulfilling a financial obligation. The contract is deemed to be non-performing if the client is no longer able or willing to fulfil payment obligations, e.g. upon any of the following events:(a) payments are past due for more than 90 days; (b) a letter of contract termination, including a demand for payment, has been sent to the client; (c) the contract has expired, but all debts have not been settled; (d) the client is bankrupt or deceased or bankruptcy, liquidation or debt restructuring proceedings have been initiated against the client; (e) identity theft, i.e. misuse of the credit receiver's identity has been identified.

If a claim is uncollectible or it is not possible or economically practical to implement measures for collecting a claim, the credit may be written off the statement of financial position.

Impairment methodology for receivables secured with collateral

Receivables secured with real estate or other assets are assessed for impairment using evaluation of the net realisable value of collateral. The net realisable value of collateral is calculated based on the market value of the collateral at the date of assessment, the right of claim and the forced sale costs. Where the carrying amount of the receivable exceeds the net realisable value of collateral, the difference (the unsecured portion) is recognised as an impairment loss and loss allowances are recorded.

Combined method

Receivables from companies are assessed for impairment using the combined method. First, the unsecured portion is determined by evaluating the net realisable value of collateral. After that the impairment loss on the unsecured portion is identified using the discounted cash flow method. The discount rate is the effective interest rate of the loan. Any accruals associated with a loan assessed for impairment individually are applied the same impairment rate that is assigned to the underlying loan.

Receivables are written off the statement of financial position when all reasonable restructuring and collection procedures have been performed and further recovery is unlikely. When a loan receivable is written off in the statement of financial position, the carrying amount of the loan portfolio and the loss allowance are reduced accordingly. Recoveries of items written off the statement of financial position are accounted for on a cash basis and are presented in the statement of comprehensive income in *Net impairment losses on loans and financial investments.*

Loss allowances, changes in loss allowances and reversals of loss allowances on loan receivables are recognised in the statement of financial position in Loans to customers and in the statement of comprehensive income in *Net impairment losses on loans and financial investments.*

PROPERTY, EQUIPMENT AND RIGHT-OF-USE ASSETS

Items of property and equipment, excluding land and buildings, are carried at historical cost less any accumulated depreciation and any accumulated impairment in value. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

When the recoverable amount of an item of property and equipment decreases below its carrying amount, the item is written down to its recoverable amount. Impairment losses are recognised as an expense as incurred. Changes in the expected useful life are accounted for by changing the amortisation period or methodology, as appropriate, and treated as changes in accounting estimates.

Depreciation is charged to the statement of comprehensive income on a straight-line basis over the estimated useful life of each part of an item of property and equipment. Depreciation commences as of the acquisition of the item. Right-of-use assets are presented together with property and equipment in the statement of financial position. Right-of-use assets are depreciated on a straight-line basis over the lease term.

The estimated useful lives assigned to asset classes are as follows:

Asset class	Useful life
Land and works of art	are not depreciated
Buildings	25 - 50 years
Cars and office equipment	5 years
Computers	3 - 4 years
Other equipment and fixtures	5 years

The assets' residual values and useful lives are reviewed at each reporting date and whenever circumstances arise, which may have a significant impact on the useful life of an asset or asset class, and adjusted if appropriate. The effect of changes in estimates is recognised in the current and subsequent periods.

Land and buildings are measured at fair value at the date of the latest revaluation less any subsequent deprecation on buildings and impairment losses. Fair value is based on the market value determined by external valuers or the management's estimate. Valuations are performed with sufficient frequency to ensure that the carrying amount of a revalued asset does not differ materially from its fair value.

A revaluation surplus is recorded in other comprehensive income and credited to the *Other reserves* in equity. However, to the extent that it reverses a revaluation deficit of the same asset previously recognised in profit or loss, the increase is recognised in profit and loss. A revaluation deficit is recognised in the statement of profit or loss, except to the extent that it offsets an existing surplus on the same asset recognised in the asset revaluation reserve. When an item of land and buildings is revalued, any accumulated depreciation at the date of the revaluation is eliminated against the gross carrying amount of the asset and the net amount restated to the revalued amount of the asset. Upon disposal, any revaluation reserve relating to the particular asset being sold or reclassified is transferred to retained earnings. Revaluation reserve is used only when the asset is derecognised.

Depreciation expense is recognised as *Depreciation and amortisation expense* in the statement of comprehensive income.

INTANGIBLE ASSETS

Costs associated with maintaining software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Group are recognised as intangible assets when the following criteria are met:

- it is technically feasible to complete the software so that it will be available for use;
- management intends to complete the

software and use or sell it;

- there is an ability to use or sell the software;
- it can be demonstrated how the software will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software are available; and
- the expenditure attributable to the software during its development can be reliably measured.

Directly attributable costs that are capitalised as part of the software include employee costs and an appropriate portion of relevant overheads. Capitalised development costs are recorded as intangible assets and amortised from the point at which the asset is ready for use.

The Group's intangible assets primarily include capitalised information and banking technology solution called Nest and other capitalised computer software. Intangible assets are carried at cost less any accumulated amortisation and any impairment losses. An intangible asset is amortised on a straight line basis over expected useful lives of 5 to 15 years. Amortisation expense is recognised as *Depreciation and amortisation expense* in the statement of comprehensive income.

IMPAIRMENT OF NON-FINANCIAL ASSETS

At each reporting date, management assesses whether there is any indication that an asset may be impaired. If there is such indication, the asset is tested for impairment and its recoverable amount is identified. The recoverable amount is the higher of the asset's fair value (less costs to sell) and value in use that is found using the discounted cash flow method. Where tests indicate that the recoverable amount of an asset is lower than its carrying amount, the asset is written down to the recoverable amount. Where the recoverable amount of an asset cannot be identified, the recoverable amount of the smallest group of assets it belongs to (its cash-generating unit) is determined. Impairment losses are expensed as incurred.

If tests of the recoverable amount indicate that an impairment loss recognised for an asset in prior years no longer exists or has decreased, the former write-down is reversed and the asset's carrying amount is increased. The increased carrying amount cannot exceed the carrying amount that would have been determined (considering normal depreciation or amortisation) had no impairment loss been recognised.

For information on the impairment of financial assets, please refer to subsection *Financial assets.*

INVESTMENT PROPERTIES

Investment properties are land and buildings held to earn rental income or for capital appreciation, or both and which are not occupied by the Group. An investment property is initially recognised at cost, including transaction costs. After initial recognition, an investment property is measured to fair value at each reporting date. Gains and losses arising from changes in the fair value of an investment property are recognised in profit or loss in the period in which they arise and presented under *Gains/losses resulting from changes in the fair value of investment properties.* Fair values are determined on an annual valuation performed by the management and/or professional appraisers.

Rental income earned is recorded in the profit or loss for the year under *Other income.*

Investment properties are derecognised either when they have been disposed of or when they are permanently withdrawn from use and no future economic benefit is expected from their disposal. Gains and losses arising from derecognition of an investment property are recognised in profit or loss in the period of derecognition.

NON-CURRENT ASSETS CLASSIFIED AS HELD FOR SALE (OR DISPOSAL GROUPS)

Non-current assets and disposal groups, which may include both non-current and current assets, are classified in the statement of financial position as Assets held for sale if their carrying amount will be recovered principally through a sale transaction, including loss of control of a subsidiary holding the assets, within twelve months after the end of the reporting period. Assets are reclassified when all of the following conditions are met: (a) the assets are available for immediate sale in their present condition; (b) the Group's management approved and initiated an active programme to locate a buyer; (c) the assets are actively marketed for sale at a reasonable price; (d) the sale is expected within one year and (e) it is unlikely that significant changes to the plan to sell will be made or that the plan will be withdrawn. Non-current assets or disposal groups classified as held for sale in the current period's statement of financial position are not reclassified or re-presented in the comparative statement of financial position to reflect the classification at the end of the current period.

A disposal group is a group of assets (current or non-current) to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction. Non-current assets are assets that include amounts expected to be recovered or collected more than twelve months after the end of the reporting period. If reclassification is required, both the current and non-current portions of an asset are reclassified.

Held for sale disposal groups as a whole are measured at the lower of their carrying amount and fair value less costs to sell. Held for sale premises and equipment are not depreciated or amortised. Reclassified non-current financial instruments are not subject to write down to the lower of their carrying amount and fair value less costs to sell.

FAIR VALUE MEASUREMENT

The Group measures financial instruments at fair value at each reporting date. Also, fair values of financial instruments measured at amortised cost are disclosed in note 29.
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 a principal market, in the most advantageous market for the asset or liability.

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

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- 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.

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 Group's management determines the policies and procedures for both recurring fair value measurement, such as investment properties and unquoted financial assets, and for non-recurring measurement, such as assets PPE (land and buildings). External valuers are involved for valuation of significant assets, such as land and buildings.

At each reporting date, the management analyses the movements in the values of assets and liabilities which are required to be re-measured or re-assessed as per the Group's accounting policies. 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 external valuers, also compares each change 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 as explained above.

LEASES (POLICY APPLICABLE BEFORE 1 JANUARY 2019)

The determination of whether an arrangement is a lease, or 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 or whether the arrangement conveys a right to use the asset.

The Group as a lessee

Leases that do not transfer to the Group substantially all of the risks and benefits incidental to ownership of the leased items are operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term. Contingent rental payable is recognised as an expense in the period in which they it is incurred.

The amount of future minimum lease payments under non-cancellable operating leases is determined based on the non-cancellable periods of the contracts. In the case of contracts that can be cancelled subject to a notice period, the notice period is treated as the non-cancellable period. In the case of contracts that can be cancelled subject to mutual agreement, the non-cancellable period is deemed to last for six months.

The Group as a lessor

Leases where the Group does not transfer substantially all of the risk and benefits of ownership of the asset are classified as operating leases. Rental income is recorded as earned based on the contractual terms of the lease in *Other operating income*. Initial direct costs incurred in negotiating operating leases are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

LEASES (POLICY APPLICABLE AS OF 1 JANUARY 2019)

The Group assesses at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Group as a lessee

The Group applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Group recognises lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

Right-of-use assets

The Bank recognises right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Right-of-use assets are depreciated on a straight-line basis over the lease term. Right-of-use assets are presented together with property and equipment in the statement of financial position.

The right-of-use assets are presented within note 10 *Property and equipment* and are subject to impairment in line with the Group's policy as described in note 1 *Impairment of non-financial assets.*

Lease liabilities

At the commencement date of the lease, the Group recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (less any lease incentives receivable), variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Group and payments of penalties for terminating the lease, if the lease term reflects exercising the option to terminate. Variable lease payments that do not depend on an index or a rate are recognised as expenses in the period in which the event or condition that triggers the payment occurs.

The Group leases commercial premises. Rental contracts are typically made for fixed periods of 3 to 10 years and, as a rule, include extension and termination options. Leases are negotiated on an individual basis and may contain different terms and conditions.

The Group as a lessor

Leases in which the Group does not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in revenue in the statement of profit or loss due to its operating nature. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognized as revenue in the period in which they are earned.

FINANCIAL LIABILITIES

Financial liabilities comprise deposits from customers, liabilities arising from securities, bank loans, accrued expenses and other liabilities. Deposits and subordinated notes are the Group's sources of debt capital.
On initial recognition, a financial liability is measured at fair value minus directly attributable transaction costs. Subsequently a financial liability is measured at its amortised cost using the effective interest rate method. A financial liability is removed from the statement of financial position when it is discharged or cancelled or expires.

Subordinated notes

A note is classified as a subordinated note if on the winding up or bankruptcy of the credit institution the note is to be satisfied after the justified claims of all other creditors have been satisfied.

Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. A restructuring provision is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring has either commenced or has been announced publicly. Provisions are not recognised for future operating losses. A provision for an onerous contract is recognised when the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. A provision for an onerous contract is measured at the lower of the present value of the expected cost of terminating the contract and the expected net cost of continuing with the contract.

Financial guarantees and loan commitments

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Loan commitments are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees are initially recognised at their fair value, which is amortised over the life of the financial guarantee. Provisions for expected credit losses are done in accordance with the Group's policies for calculating ECL, as brought out above. Credit limits are only offered to corporate customers and are fully secured by a mortgage. Unused but committed credit limits can be used if the customer fulfils all the credit conditions including the customer does not have any overdue payments to the Group. Therefore, the credit risk of unused credit limits is assessed as low.

Financial guarantees issued and loan commitments are accounted off the statement of financial position. Provisions for expected credit losses are recognised in the income statement.

STATUTORY CAPITAL RESERVE

In accordance with the Commercial Code of the Republic of Estonia, the capital reserve of a company may not amount to less than one tenth of its share capital. Thus, every year when profits are allocated, the parent company has to transfer at least one twentieth of its net profit for the year to the statutory capital reserve until the required level is achieved. The capital reserve may not be distributed to shareholders but it may be used for covering losses if the latter cannot be covered with unrestricted equity and for increasing share capital through a bonus issue.

INTEREST INCOME AND INTEREST EXPENSE RECOGNITION

Interest income and interest expense are recognised using the effective interest rates of the underlying assets and liabilities.

Interest income and interest expense include interest and similar income and expense respectively. Income and expenses similar to interest include items related to the contractual/redemption term of an asset or liability or the size of the asset or liability. Such items are recognised over the effective term of the asset or liability. Interest income and expense are recognised using the original effective interest rate that is used to discount the estimated future cash flows of the asset or liability. The original effective interest rate calculation takes into account all costs and income that are directly related to the transaction, including contract and arrangement fees, etc.

FEE INCOME AND EXPENSE

Fee income comprises other fees received from customers during the period and fee expense comprises fees paid to other credit institutions. Fees and commissions income is recognised in the fair value of the considerations received or receivable for the services provided in the ordinary course of the Group's activities. Fees and commissions income and expense are recognised on an accrual basis. Loan fees (less direct expenses) are included in the calculation of the effective interest rate.

OTHER INCOME

Other income comprises:

- income from debt collection and recovery proceedings (late payment interest, fines, etc.), which is recognised on an accrual basis as relevant services are rendered;
- gain from early redemption of the Group's liabilities, which is recognised at the date of redemption;
- miscellaneous income includes revenue from the sale of goods, which is recognised when the goods are sold to the customer, and income on the sale services, which is recognised in the accounting period in which the services are rendered; and
- dividend income (in the parent's financial statements), which is recognised when the right to receive payment is established.

OTHER EXPENSES

Other expenses comprise:

- expenses related to enforcement proceedings (including notaries' fees, bailiffs' and debt collection charges, state fees and levies);
- regulatory and supervision charges (contributions to the Guarantee Fund and supervision charges);
- costs of registry inquiries and similar items;
- expenses related to investment properties; and;
- expenses related to securities.

Other expenses are recognised when the service has been rendered and the liability has been incurred.

EMPLOYEE BENEFITS

Short-term employee benefits are measured on an undiscounted basis and they are recognised as an expense when the service has been rendered. The Group recognises liabilities (provisions) and costs related to employee bonus schemes if the bonuses are clearly fixed and are related to the accounting period.

INCOME TAX

Income tax is recognised in the consolidated financial statements in accordance with legislation enacted or substantively enacted by the end of the reporting period. Income tax comprises current tax and is recognised in profit or loss for the year, unless it is recognised directly in equity because it relates to transactions that in the same or different period are also recognised directly in equity. Current tax is the amount expected to be paid, or recovered, in respect of taxable profits or losses for the current and prior periods. Taxable profits or losses are based on estimates if the consolidated financial statements are authorised for issue prior to the filing of relevant tax returns. Taxes other than income tax are recorded within *Salaries and associated charges* and other *Operating expenses*. Advance payments of income tax, charged at the rate of 14% of quarterly profit before tax, which credit institutions have been required to make in Estonia since 2018, are recorded as tax expense.

In accordance with the Estonian Income Tax Act, corporate income tax is not levied on profit earned but on profit distributed as dividends. The standard tax rate is 20% (20/80 of the amount distributed as the net dividend). Regularly distributed dividends are eligible to a reduced, 14% tax rate. This rate may be applied to a dividend extending to up to three previous calendar years average dividend distribution on which income tax has been paid (2018 is the first year included in the calculation). The income tax payable on dividends is reduced by the amount of any advance payments made. Corporate income tax payable on dividends is recognised as an expense in the period in which the dividends are declared, irrespective of when the dividends are distributed. Because of the specific nature of the taxation system, companies registered in Estonia do not acquire deferred tax assets or incur deferred tax liabilities on temporary differences between the carrying amounts and tax bases of their assets and liabilities. Since 2018, the Latvian corporate income tax legislation has been similar to the Estonian one: profit is taxed when it is distributed and deferred tax assets and liabilities do not arise. The tax rate is 20% (applied to the gross taxable amount).

(In thousands of euros)

The profits earned in Lithuania, Finland, Spain and Sweden that have been adjusted for permanent and temporary differences as permitted by local tax laws are subject to income tax.

Corporate income tax rates outside Estonia

	2020	2019	2018
Estonia*	14.0%	14.0%	14.0%
Latvia	-	-	-
Lithuania	15.0%	15.0%	15.0%
Finland	20.0%	20.0%	20.0%
Sweden	21.4%	21.4%	22.0%
Spain	30.0%	30.0%	30.0%

* In Estonia, corporate income tax is not levied on profit earned but on profit distributed as dividends (20/80 of the amount distributed as the net dividend). Credit institutions are required to make advance payments of income tax on profit earned at the rate of 14%.

At foreign entities, deferred tax is recognised whereby the deferred tax assets and liabilities arising from temporary differences between the carrying amounts and tax bases of assets and liabilities are recognised in the statement of financial position. In the consolidated financial statements, deferred tax liabilities are recognised in the statement of financial position in *Deferred tax liabilities*. A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised.

EARNINGS PER SHARE

Basic earnings per share are calculated by dividing net profit for the year by the weighted average number of ordinary shares outstanding during the period.

For the purposes of calculating diluted earnings per share, the net profit attributable to ordinary equity holders and the weighted average number of shares outstanding are adjusted for the effects of all dilutive potential ordinary shares. The Group has not issued any financial instruments that could dilute earnings per share. Therefore, basic and diluted earnings per share are equal.

The Group is not listed on a stock exchange. Therefore, the information presented in note 31 to the financial statements is voluntary.

NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS THAT THE GROUP HAS ADOPTED DURING THE YEAR (ENDORSED BY EU)

New and/or amended IFRSs which have been adopted by the Group as of 1 January 2019, but did not have any material impact on the Group:

IFRS 9 *Prepayment features with negative compensation* (amendment). The amendment allows financial assets with prepayment features that permit or require a party to a contract either to pay or receive reasonable compensation for the early termination of the contract (so that, from the perspective of the holder of the asset there may be 'negative compensation'), to be measured at amortized cost or at fair value through other comprehensive income. These amendments had no impact on the consolidated financial statements of the Group.

IAS 28 *Long-term Interests in Associates and Joint Ventures* (amendments). The amendments relate to whether the measurement, in particular impairment requirements, of long-term interests in associates and joint ventures that, in substance, form part of the 'net investment' in the associate or joint venture should be governed by IFRS 9, IAS 28 or a combination of both. The amendments clarify that an entity applies IFRS 9, before it applies IAS 28, to such long-term interests for which the equity method is not applied. In applying IFRS 9, the entity does not take account of any adjustments to the carrying amount of long-term interests that arise from applying IAS 28. These amendments had no impact on the consolidated financial statements of the Group as the Group does not have such long-term interests in associates and joint ventures.

IAS 19 *Plan Amendment, Curtailment or Settlement* (amendments). The amendments require entities to use updated actuarial assumptions to determine current service cost and net interest for the remainder of the annual reporting period after a plan amendment, curtailment or settlement has occurred. The Amendments also clarify how the accounting for a plan amendment, curtailment or settlement affects applying the asset ceiling requirements. The amendments had no impact on the consolidated financial statements of the Group as it did not have any plan amendments, curtailments, or settlements during the period.

The IASB has issued the *Annual Improvements to IFRSs 2015 – 2017 Cycle*, which is a collection of amendments to IFRSs. The management has assessed the effect of this standards and it had not any significant impact on the Group.

- IFRS 3 *Business Combinations* and IFRS 11 *Joint Arrangements:* The amendments to IFRS 3 clarify that when an entity obtains control of a business that is a joint operation, it remeasures previously held interests in that business. The amendments to IFRS 11 clarify that when an entity obtains joint control of a business that is a joint operation, the entity does not remeasure previously held interests in that business. These amendments had no impact on the consolidated financial statements of the Group as there is no transaction where joint control is obtained.

- IAS 12 *Income Taxes:* The amendments clarify that the income tax consequences of dividends are linked more directly to past transactions or events that generated distributable profits than to distributions to owners. Therefore, an entity recognizes the income tax consequences of dividends in profit or loss, other comprehensive income or equity according to where it originally recognized those past transactions or events. Since the Group's current practice is in line with these amendments, they had no impact on the consolidated financial statements of the Group.

- IAS 23 *Borrowing Costs:* The amendments clarify paragraph 14 of the standard that, when a qualifying asset is ready for its intended use or sale, and some of the specific borrowing related to that qualifying asset remains outstanding at that point, that borrowing is to be included in the funds that an entity borrows generally. Since the Group's current practice is in line with these amendments, they had no impact on the consolidated financial statements of the Group.

NEW AND REVISED INTERNATIONAL FINANCIAL REPORTING STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE AND NOT EARLY ADOPTED

Certain new standards and interpretations have been issued that are mandatory for the annual periods beginning on or after 1 January 2020 or later, and which the Group has not early adopted:

Conceptual Framework in IFRS standards. The IASB issued the revised Conceptual Framework for Financial Reporting on 29 March 2018. The Conceptual Framework sets out a comprehensive set of concepts for financial reporting, standard setting, guidance for preparers in developing consistent accounting policies and assistance to others in their efforts to understand and interpret the standards. IASB also issued a separate accompanying document, amendments to references to the Conceptual Framework in IFRS Standards, which sets out the amendments to affected standards in order to update references to the revised Conceptual Framework. Its objective is to support transition to the revised Conceptual Framework for companies that develop accounting policies using the conceptual framework when no IFRS Standard applies to a particular transaction. For preparers who develop accounting policies based on the Conceptual Framework, it is effective for annual periods beginning on or after 1 January 2020.

IAS 1 *Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors: Definition of 'material'* (amendments). The amendments are effective for annual periods beginning on or after 1 January 2020 with earlier application permitted. The amendments clarify the definition of material and how it should be applied. The new definition states that, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity'. In addition, the explanations accompanying the definition have been improved. The amendments also ensure that the definition of material is consistent across all IFRS Standards. The amendments to the definition of material is not expected to have a significant impact in the Group's consolidated financial statements.

IAS 1 *Presentation of Financial Statements: Classification of Liabilities as Current or Non-current* (amendments). The amendments are effective for annual periods beginning on or after 1 January 2022 with earlier application permitted. These amendments have not yet been endorsed by the EU. The amendments help companies determine whether, in the statement of financial position, debt and other liabilities with an uncertain settlement date should be classified as current (due or potentially due to be settled within one year) or non-current and clarify that such classification should be based on rights that are in existence at the end of the reporting period. The amendments also include clarifying the classification requirements for debt instrument that might be settled by converting it into equity. Management has assessed the impact of application of the amendments to be minimal since the Group presents its assets and liabilities in order of liquidity in its consolidated statement of financial position.

IFRS 9, IAS 39 and IFRS 7 (amendments). The amendments are effective for annual periods beginning on or after 1 January 2020 and must be applied retrospectively. Earlier application is permitted. In September 2019, the IASB issued amendments to IFRS 9, IAS 39 and IFRS 7, which concludes phase one of its work to respond to the effects of Interbank Offered Rates (IBOR) reform on financial reporting. Phase two will focus on issues that could affect financial reporting when an existing interest rate benchmark is replaced with a risk-free interest rate (an RFR). The amendments published, deal with issues affecting financial reporting in the period before the replacement of an existing interest rate benchmark with an alternative interest rate and address the implications for specific hedge accounting requirements in IFRS 9 *Financial Instruments* and IAS 39 *Financial Instruments: Recognition and Measurement*, which require forward-looking analysis. The amendments provided temporary reliefs, applicable to all hedging relationships that are directly affected by the interest rate benchmark reform, which enable hedge accounting to continue during the period of uncertainty before the replacement of an existing interest rate benchmark with an alternative nearly risk-free interest rate. There are also amendments to IFRS 7 Financial Instruments: Disclosures regarding additional disclosures around uncertainty arising from the interest rate benchmark reform. Management is currently assessing the impact of the amendments on the Group's consolidated financial statements.

A number of new standards and interpretations have been issued but not effective for the Group for annual periods beginning on or after 1 January 2020 which accordingly do not have any significant impact on the Group's financial statements

IFRS 3: *Business Combinations* (amendments). The IASB issued amendments in Definition of a Business (Amendments to IFRS 3) aimed at resolving the difficulties that arise when an entity determines whether it has acquired a business or a group of assets. The amendments are effective for business combinations for which the acquisition date is in the first annual reporting period beginning on or after 1 January 2020 and to asset acquisitions that occur on or after the beginning of that period, with earlier application permitted. These amendments have not yet been endorsed by the EU.

Amendment in IFRS 10 *Consolidated Financial Statements* and IAS 28 *Investments in Associates and Joint Ventures:* Sale or Contribution of Assets between an Investor and its Associate or Joint Venture. The amendments address an acknowledged inconsistency between the requirements in IFRS 10 and those in IAS 28, in dealing with the sale or contribution of assets between an investor and its associate or joint venture. The main consequence of the amendments is that a full gain or loss is recognized when a transaction involves a business (whether it is housed in a subsidiary or not). A partial gain or loss is recognized when a transaction involves assets that do not constitute a business, even if these assets are housed in a subsidiary. In December 2015 the IASB postponed the effective date of this amendment indefinitely pending the outcome of its research project on the equity method of accounting. The amendments have not yet been endorsed by the EU.

The Group plans to adopt the above mentioned standards and interpretations on their effectiveness date provided they are endorsed by the EU. Unless otherwise described above, the new standards and interpretations are not expected to affect significantly the Group's consolidated financial statements.

NOTE 2. SIGNIFICANT ACCOUNTING ESTIMATES AND ASSUMPTIONS

The preparation of financial statements in conformity with IFRS EU requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making estimates about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The impact of management's estimates is most critical regarding loss allowances for loans and interest receivables. The measurement of expected credit loss (ECL) allowance for financial assets measured at amortised cost and FVOCI is a significant estimate that involves determination of methodology, models and data inputs. Details of ECL measurement methodology are disclosed in note 1 (see the section *Financial assets impairment*) and the loss allowances in note 7. The following components have a major impact on credit loss allowance: definition of default, determining criteria for significant increase in credit risk, probability of default (PD), exposure at default (EAD), and loss given default (LGD), establishing groups of similar financial assets for the purpose of measuring ECL, as well as models of macro-economic scenarios. The Group regularly reviews and validates the models and inputs to the models to reduce any differences between expected credit loss estimates and actual credit loss experience. The Group used supportable forward looking information for measurement of ECL, primarily an outcome of its own macro-economic forecasting model.

The carrying amounts of property and equipment are identified by applying internally established depreciation rates. Depreciation rates are determined by reference to the items' estimated useful lives (see the section *Property and equipment* in note 1). Land and buildings are initially recognised at the acquisition cost and subsequently measured at revalued amount. The management uses the estimate of an asset's market value provided by an independent expert as a basis for fair value estimation, if needed (see note 30).

Fair value of investment properties is measured on a yearly basis, and book values adjusted to reflect any changes in market values (see the section *Investment properties* in note 1 and note 11 and 30).

The carrying amounts of intangible assets are identified by applying internally established amortisation rates. Amortisation rates are determined by reference to the items estimated useful lives (see the section *Intangible assets* in note 1) which is generally 5 to 15 years.

At the end of each reporting period management assesses whether there is any indication of impairment of intangible assets. If any such indication exists, management estimates the recoverable amount.

The Group capitalises the costs of developing information and banking technology solution Nest. Initial capitalisation of the costs is based on managements judgement that the technological and economic feasibility is certain. This usually occurs when the development phase has reached a defined milestone according to an established project management model. In determining the amounts to be capitalised, management makes assumptions regarding the expected future cash generation of the project, discount rates to be applied and the expected period of benefits, which for Nest is 15 years.

The Group leases mainly office premises. The leases of office premises generally have a term of 3 to 10 years and the contracts include extension and termination options. Lease terms are negotiated on an individual basis and may contain different terms and conditions. The Group applies judgement in assessing whether it is reasonably certain that it will exercise the option to extend or terminate a lease. That is, it considers all relevant factors that create an economic incentive for it to exercise either the extension or termination option. After the commencement date, the Group reassesses the lease term if there has been a significant event or change in circumstances that is within its control and affects its ability to exercise or not to exercise the option to extend or terminate (e.g. significant customisation or improvement of the leased asset). The periods covered by an option to extend the lease of office premises are not included in the lease term because the Group has historically both exercised and not exercised the option. Furthermore, the periods covered by a termination option are included in the lease term only when they are reasonably certain not to be exercised.

Since the Group operates in a complex multinational environment, management considered whether it has any uncertain tax positions, particularly those relating to transfer pricing. The tax filings of Bigbank and its branches and subsidiaries in different jurisdictions include deductions related to transfer pricing and the taxation authorities may challenge the tax treatments. Management has determined, based on the Group's tax compliance and transfer pricing principles, that it is probable that the Group's tax treatments (including those for the branches) would be accepted by the tax authorities if the Group has appropriate transfer pricing documentation to support its approach.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised.

NOTE 3. RISK AND CAPITAL MANAGEMENT

RISK AND CAPITAL MANAGEMENT PRINCIPLES

Risk is defined as a potential unexpected change in loss or income or in the value of assets, which can be described by probability distribution.

Effective risk and capital management is an essential component of the Group's management. It has a crucial impact on the long term results and sustainability of a business model. Aim of the risk and capital management shall be managing volatility of financial performance and maintain confidence among the customers, shareholders and regulators.

Following principles shall be followed in risk and capital management:

- **Well-balanced portfolio.** Group maintains a well-diversified credit portfolio and takes limited risk in financial markets. Since uncertain changes in any individual position may seriously affect Group's overall risk position, over-reliance on single counterparties and concentrations of risk are avoided.
- **Risk profile by significant countries of operation and significant product groups.** The credit portfolio is reasonably balanced between different countries of operation and products. The management board determines at least annually the maximum exposure limits for individual countries of operation and significant product groups. Any target risk profile change must take into account established limits and potential effects. The actual risk profile is regularly measured against such limits.
- **Quality of assets.** Any changes in the target risk profile that may significantly affect the quality of assets are properly analysed and assessed before the changes are made.
- **Strong liquidity position.** The Group maintains a conservative liquidity risk profile and a sufficient portfolio of liquid assets at all times. Concentrations of funding and liquid assets are avoided.
- **Adequate capital.** The Group maintains a strong and rather conservative capitalisation level (capital adequacy). The Group makes sure that it has adequate capital to cover its risks and comply with regulatory (Pillar 1) and internal capital requirements (Pillar 2) as well as the minimum capital requirements. Detailed capital requirements are outlined in the Own Funds and Capital section of this note.
- **Reasonable risk level.** The Group does not accept unreasonably high risk even when there is potential for exceptionally high profit as a result of risk taking. Risks which the Group cannot assess or manage adequately or for which it does not have sufficient experience or knowledge are avoided.
- **Low tolerance to specified types of risks.** The Group has low tolerance to certain risk types as specified in the policies for individual risks. Target risk profiles which increase such risks are avoided.
- **Reliable structure of the statement of financial position.** The Group is not required to maintain a specific structure of the statement of financial position but any target risk profile that may have a significant impact on the structure of the statement of financial position is carefully assessed (the impacts of the changes in the structure of the statement of financial position are analysed) and changed, where necessary, before it is approved.

The primary objectives of risk management are to protect the Group's financial strength and limit the impact of potential adverse events on the Group's capital, liquidity and financial results.

Risk management principles for the entire Group are established in the Risk Policy approved by the supervisory board of Bigbank AS. Risk taking is an integrated part of all Group's business activities where risk management supports business activities and decision making process ensuring that that there is an appropriate balance between risk and reward. Risk management is an integral part of the strategic decision making and daily business decision making process. The primary goals of risk management are to ensure that the outcomes of risk-taking activities are consistent with the Group's strategies and risk appetite, and that there is an appropriate balance between risk and reward.

RISK MANAGEMENT FRAMEWORK

The supervisory board of Bigbank AS has established the Group's risk management framework in the Risk Policy. The Group's risk management framework consists of four key elements: 1) risk culture, 2) risk governance, 3) risk appetite and 4) risk management.

The main risk the Group has identified in its operations is credit risk, which arises in lending to customers. Other material risks are market risk (including IRRBB, i.e. interest rate risk in the banking book), liquidity risk, operational risk, reputational risk, business and strategic risk. In order to cover these risks Group holds a capital buffer and liquidity reserves for unforeseen events. The Group assesses and identifies the risks continuously, as a part of its internal capital adequacy assessment process (ICAAP) and internal liquidity assessment process (ILAAP).

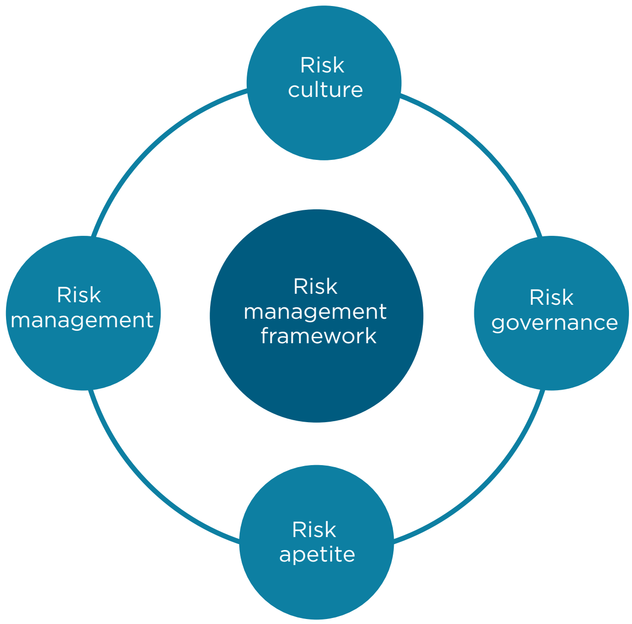


Fig. Risk Management Framework

Risk culture

Risk culture means norms, attitudes and behaviours related to risk awareness, risk-taking and risk management, and the controls that shape decisions on risks in the Group. Risk culture influences the decisions of management and employees during the day-to-day activities and has an impact on the risks they assume. A sound and consistent risk culture should be a key element of Group's effective risk management and should enable to make sound and informed decisions. Risk culture is developed through policies, communication and staff training regarding the Group's activities, strategy and risk profile. Employees should be fully aware of their responsibilities relating to risk management. Risk management should not be confined to risk specialists or internal control functions. Business units are primarily responsible for managing risks on a day-to-day basis in line with the Group's policies, procedures and controls, taking into account the Group's risk appetite and risk capacity. A strong risk culture includes:

- Tone from the top - the management board is responsible for setting and communicating the Group's core values and expectations. Group's management, including key function holders, should contribute to the internal communication of core values and expectations to employees.
- Accountability - relevant employees at all levels should know and understand the core values of the Group and, to the extent necessary for their role, its risk appetite and risk capacity. They should be capable of performing their roles and be aware that they will be held accountable for their actions in relation to the Group's risk- taking behaviour.
- Effective communication and challenge- a sound risk culture should promote an environment of open communication and effective challenge in which decision-making processes encourage a broad range of views, allow for testing of current practices, stimulate a constructive critical attitude among employees, and promote an environment of open and constructive engagement throughout the entire organisation.
- Incentives - appropriate incentives should play a key role in aligning risk-taking behaviour with the Group's risk profile and its long-term interest.

Risk governance

The Group's risk governance structure is described with a focus on the key responsibilities relating to risk-taking decisions and oversight.

The general risk governance structure is based on the three lines of defence model. Under the concept, all employees of the Group are responsible for managing risk, but all have their specific roles and responsibilities. The functions are separated into three lines as follows:

- **First line of defence** - functions that own and manage risks (risk owners)
- **Second line of defence** - functions that oversee risks (risk management and compliance functions)
- **Third line of defence** - functions that provide independent assurance (internal audit and audit committee)

Each line of defence has specific roles and responsibilities for risk management and risk control.

Fig. Three lines of defence model

Group has three main levels where risk management decisions are made:

1) the supervisory board;
2) the management board; and
3) credit committees.

Based on general-level decisions and the authorities granted, operational decisions are made by risk owners and operational units. The Group keeps the functions of risk management, decision-making and monitoring processes as separate and independent as possible. Due to the size of the Group some of the above functions may be mixed, however the Group's organisational structure is designed so that it ensures the segregation of duties between operational and monitoring/control functions in order to prevent conflicts of interest.

The supervisory board defines the risk appetite based on the business strategy, approves the risk and capital management policy and policies for other material risk types.

The management board is responsible for implementing and maintaining risk management procedures, processes and systems for all of the Group's material products, activities, processes and systems, consistent with the Group's risk appetite and tolerance. The management board identifies and assesses regularly all risks involved in the Group's activities, to make sure that the risks are monitored and controlled. The management board is responsible for implementing an internal control system and a risk limit system and ensuring the sound functioning of ICAAP and ILAAP.

The system of credit committees consists of the Group's credit committee, country credit committees and their sub-committees. The Group's credit committee is the highest level decision-making body which is responsible for supervising country credit committees and adopting lending decisions exceeding 1 million euros.

The risk committee is a non-decision making committee and it provides a platform for discussing, coordinating and agreeing strategic issues related to risks, capital, funding and liquidity. The IT risk committee is a sub-committee of the risk committee. The risk committee is established and members are nominated by the Group's management board. The risk committee is responsible for monitoring and assessing all risks identified within the scope of the risk and capital strategy and framework determined by the supervisory board and the management board.

Risk appetite

Risk appetite expresses the level of aggregated risks that the Group is willing to take according to the business model and within the risk tolerance in order to achieve strategical goals. The Group has defined risk appetite for all main risk categories identified and has established processes and measures for how the actual risk profile is assessed and managed. Risk appetite is forward-looking, in line with the strategic planning horizon and regularly reviewed.

Fig. Elements of risk appetite

Following are the elements of risk appetite:

- **Financial objectives.** Risk management must support the achievement of financial objectives as long as these objectives include sustainable growth in earnings, maintenance of capital adequate for the Group's risk profile, and the availability of financial resources for meeting financial obligations on a timely basis and at reasonable prices.
- **Strategic principles.** Risk strategy and the target risk profile are based on the overall strategy, however risk management and risk capacity are inherent in the strategy making process. The Group's strategy takes into account risks and capital as well as the risk strategy and is regularly reviewed and updated to reflect changes in strategic plans.
- **Risk tolerance measures.** Risk tolerance is the maximum risk level the Group can accept within particular risk category taking into account the capital, risk management and risk control capacity and regulatory restrictions. Risk tolerance is established based on quantitative metrics.
- **Risk management principles.** Applicable external regulations, best practice and risk management principles specified in the Group's internal regulations provide the qualitative foundation for the risk tolerance framework. Business needs may not override risk management principles.
- **Risk capacity.** Risk capacity is defined as the maximum level of risk that the Group can assume in both normal and distressed situations before breaching regulatory constraints and obligations to stakeholders.

Risk management

Effective risk management includes techniques that are guided by the risk framework and are integrated into the Group's strategies and business planning process. The risk management process consists of following activities:

- risk identification;
- risk assessment;
- risk monitoring;
- risk control;
- risk measurement;
- risk reporting.

Fig. Risk management process

Risk identification. Risk identification is a regular process the Group uses to identify risks that are or might be material for the Group. The risk identification is expected to be comprehensive and take both normative and economic perspectives into account.

Risk assessment. Risk assessment of new products and systems shall be performed before they are implemented. Principles of proportionality and efficiency apply – extent of assessment shall be in accordance with the potential impact and importance of risk in aggregated risk profile of the Group.

Assessment of the actual risk profile against the Group's risk appetite shall be carried out regularly.

Risk monitoring. Regular monitoring system shall ensure that business activities are within approved limits and in line with regulations, and are aligned with the Group's strategies and target risk profile. Any breaches of limits or regulations shall be immediately reported by the head of respective unit and escalated to senior management, committees, management board and/or the supervisory board depending on the limit or internal instruction. The Group has in place system of risk indicators (incl. escalation levels) addressing all identified material risk categories, engage in regular monitoring of key financial and non-financial risk indicators to monitor changes in the financial conditions and risk profile of the Group.

Risk control. The significant part of risk management is risk control - internal procedures, processes and limits framework. The necessity for internal rules arises from internal needs for proper risk management and from regulatory minimum requirements. All identified material risks and related processes are covered with internal rules, limits and control system. All internal regulations are guided by the Group's general risk management principles and target risk profile, and set the limits and controls within which the Group and its subsidiaries can operate. The development of internal rules is actively coordinated on group level, however head of each area, branch and subsidiary is fully responsible for compliance with local regulations in their areas of responsibility or country of operations. All internal regulations shall follow the group level principles of establishing internal regulations in the Group.

Key risk policies and general risk management strategies, principles, risk governance and general limits are approved by the supervisory board. Management level general risk procedures are approved by the management board. Risk management policies shall be reviewed and updated once a year.

Risk measurement. Risk Management Area is responsible for developing and maintaining an appropriate suite of risk measurement techniques to support the operations of the various business lines (risk owners), and measurement of capital adequacy on the Group-wide basis. All material risks shall be measured using quantitative metrics and monitored regularly. Risk measurement principles shall be annually reviewed and approved by the management board.

Stress testing, sensitivity analysis and scenario analysis are proactive methods used for evaluating the impact of various factors on the risks profile and respective capital need. Stress testing is integrated with the Group's risk management framework and capital adequacy assessment process and it shall enable to evaluate possible impact of relevant business and strategic decisions. Stress testing of material risks shall be performed at least once every year or more frequently and results shall be reported to the management board and supervisory board.

Risk reporting. Risks are monitored and reported by all material risk types, by products and by all branches. Head of risk management area is responsible for implementing appropriate organisation, policies, procedures and systems to ensure that risks are measured, evaluated, aggregated, analysed and regularly reported to the management board. Supervisory board is on a quarterly basis fully informed by the CEO and head of risk management area on the development of Group's overall risk situation as well as other risk related matters.

RISK APPETITE AND TARGET RISK PROFILE

The target risk profile is based on the risk appetite and it includes the level and types of risks the Group is willing to take within its risk capacity and in line with its business model to achieve its strategic objectives. The Group describes in its target risk profile the nature and level of each material risk identified. Determination and updating of the target risk profile is an integral part of annual strategic planning during the budgeting process.
The Group uses a four-step scale to determine levels of risk appetite:

- *Low* (1) – Safe and proven solutions. Low risk and minimal return.
- *Moderate* (2) – Reactive. Moderate risk level and potentially lower return.
- *Above average* (3) - Proactive. Above average risk with high profit potential. Decisions made based on the balance of risk and return.
- *High* (4) – Priority on business needs. High risk of loss which can be tolerated only in the case of very high profit potential.

The actual risk profile is assessed and compared with the target profile at least quarterly. The assessment results are reported to the management board and supervisory board within regular risk reports.

Credit risk

Credit risk is the risk that the counterparty to a transaction is not capable or willing to perform its contractual obligations. Credit risk arises in the Group's direct lending operations and its investment activities where counterparties have repayment or other obligations to the Group. The Group distinguishes between credit risk arising from (i) the loan portfolio (including items accounted for off the statement of financial position); (ii) money market operations; and (iii) bond portfolio.

Credit risk of loan portfolio is the most significant risk of the Group and the most significant driver of risk weighted assets. The Group determines the credit risk levels in loan portfolio based on the ECL estimates as follows:

- Low risk – ECL up to 2%
- Moderate risk – ECL over 2% up to 6%
- Above average risk – ECL over 6% up to 10%
- High risk – ECL over 10%

The Group's appetite for the credit risk is on Moderate level. However, it is carefully distinguished between different sub-profiles within the loan portfolio and risk sub-profile for different products or countries differentiates significantly from Low level (1) to Above average level (3), based on strategic plans and risk analysis.

Credit risk of the loan portfolio is controlled by:

- using highly predictive credit risk assessment and fraud detection models in the selection of customers, which minimises losses and the risk of crediting customers in the above average risk class;
- using automated underwriting and inquiries to external databases to ensure standardised, compliant and efficient decision-making;
- focusing only on creditworthy private customers and companies with a proven track record;
- consistently following responsible lending principles;
- implementing systematic monitoring processes to follow-up credit risk limits and

risk indicators on country, product, partner and customer level.

In providing credit, the Group observes good banking practice and high ethical standards. The Group makes sure that its activities do not compromise any generally accepted ethical, environmental or legal principles. The Group does not enter into transaction with counterparties whose ethical or moral standards are questionable.

The Group has not implemented specific techniques to mitigate credit risk in the calculation of regulatory capital requirements.

The credit risk of money market operations arises from the Group's payment services and money market activities through exposures to credit institutions. The credit risk of payment services results from holding liquid assets and supporting the Group's main activities with payment solutions.

The risk is managed by diverse counterparties, high credit rating standards, counterparty exposure limits and regular monitoring/reviews to minimise the probability of the default of any single counterparty.

The credit risk of money market operations is managed at Group level. All branches and subsidiaries observe Group-level principles, rules and limits. The finance function is the first line of defence in managing the credit risk of money market. The second line of defence is the risk management function.

The credit risk of the bond portfolio arises from debt instruments. The strategy and risk appetite for credit risk in bond portfolio is set, managed and monitored as part of liquidity and market risk management. Credit risk in bond portfolio is handled by the finance area as a first line of defence. Risk management area acts as a second line of defence.

Within credit risk the Group has identified the following risks:

- Concentration risk - the risk resulting from a large risk exposure to a counterparty, or connected counterparties, or connected counterparties that are affected by a common risk factor or when there is a strong positive correlation between risks.
- Country risk - the risk resulting from the economic, political or social situation in the country where the counterparty is located.
- Collateral risk - the risk arising from the type, value, form, and methods of disposing of the asset pledged as collateral for a transaction.

Concentration risk

Concentration risk is the risk of being significantly exposed to a single counterparty or related counterparties or counterparties that are influenced by the same risk factor.

The Group determines concentration risk taking into account exposures to a single counterparty or related counterparties as well as exposures to a single industry, region or risk factor. The Group's loan portfolio concentration risk strategy is to avoid a significant impact of the default of any single counterparty with a well-diversified loan portfolio, where the majority of single customer or connected customer concentrations are below 0.1% of total loan portfolio.

The Group has established following concentration risk limits:

- Maximum loan amount per single contract or project (corporate loans);
- Maximum exposure to counterparty or related counterparties (corporate loans);

- Maximum exposure to counterparty or related counterparties (consumer loans);
- Maximum share of a specific country in Group's credit portfolio;
- Maximum share of corporate and real estate loans in Group's credit portfolio;
- Maximum unsecured exposure to counterparty or related counterparties (corporate loans).

The Group's total receivables from a borrower and parties related to the borrower may not, at any time, exceed 10% of the Group's net own funds (please refer to subsection Own funds and capital). At 31 December 2019 and at 31 December 2018, the Group did not have any customers with a high risk concentration, i.e. customers whose liability would have exceeded 10% of the Group's net own funds.

In addition to credit risk management techniques, concentration risk is managed by applying the following measures:

- In its business operations, the Group focuses on serving individuals and small and medium-sized enterprises.
- Customers are identified with due care and using due procedure.
- The customers' reciprocal relations are determined through relevant enquiries.
- The Group monitors the concentration of its credit risk exposure to any single factor and limits, where necessary, exposure to any customer group that is related to or impacted by that factor.

Country risk

Country risk is the risk resulting from the economic, political or social situation in the country where the counterparty is located or the probability of the occurrence of an environmental, political or social event, which may lead to a default by a large group of debtors (collective debtor risk). The Group's strategy is to have a well-balanced portfolio across the countries of operation. Over-concentration on one particular country is avoided by setting limits to single country exposures, new sales per country and the credit quality of single country portfolios. Exposure to the one particular country shall not exceed 40% of the total loan portfolio.

Collateral risk

Collateral risk is the risk arising from the type, value, form, and methods of disposing of the asset pledged as collateral for a transaction.

The Group consciously limits its collateral risk, assuming that its lending policies and volumes mitigate credit risk more effectively than receipt of collateral and associated cash flows.

The Group monitors the effects of fluctuations in the market value of collateral.

Collateral risk is managed using the following principles:

- Consumer loans do not require asset collaterals but can be additionally guaranteed by suretyship from a private person.
- Requirements for collateral depend on the type of the loan. Real estate and business loans have to be secured with physical collateral (real estate collateral provided under the law of property such as a mortgage on immovable property). Consumer loans and small business loans may be secured with suretyship from a private person. In making financing decisions, the Group does not rely simply on the borrower's business

plan or economic activities and additional collaterals or securities are required.

- In the case of small and medium-sized loans it is expedient to accept collateral provided under the law of obligations. The Group is aware that the legal enforceability of real estate collateral (collateral provided under the law of property) and the regulation governing its realisation process restrict the use of such collateral in the Group's business activity.
- Loans are granted in accordance with the limits established by the Group, taking into account the size of the loan and the ratio of the loan amount to the value of the collateral.
- The sufficiency and value of acceptable real estate or other collateral is determined based on its current value considering the changes that will occur over time. Where necessary, the value of collateral is determined with the assistance of experts (e.g. real estate appraisers).
- The Group accepts as loan collateral only such immovable properties whose market value has been determined in a written valuation report issued by a real estate company with whom the Group has a corresponding agreement. Collateral risk is estimated by reference to the valuation report prepared by the real estate company and subjective valuation performed by the Group's staff.
- The agreements made with real estate companies regarding the valuation of assets set out the real estate company's liability for incorrect appraisal.
- The Group accepts only collateral located in an area with an active and transparent real estate market. Such areas are determined in partnership with real estate companies and experts accepted by the Group. Acceptable real estate collaterals include, above all, mortgages of the first ranking entered in the land register, which should ensure full satisfaction of the Group's claims even when the market value of the collateral decreases.
- The property put up as collateral under the law of property has to be insured throughout the loan term with an insurance company accepted by the Group at least to the extent of the replacement cost of the property.

The Group pledges its own assets as a collateral only if it is required by funding agreements or currency forward and swap contracts.

Credit risk management

The Group's credit risk strategy and risk profile are developed using input and risk assessments from all countries and branches that know local market conditions. The overall risk profile of the loan portfolio is managed at Group level. Group-level credit risk limits are approved by the supervisory board, country-level limits are approved by the management board. All branches and subsidiaries shall follow Group-level principles and approved credit risk limits. In case of the breach of a limit, action plan to achieve target level shall immediately be presented to the management board. Breaches of group-level limits are further escalated to the supervisory board.

Customers are selected using highly predictive credit risk assessment and fraud detection models, which minimises losses and the risk of crediting high-risk or insolvent customers. The Group's goal is to automate as many credit decisions as possible.

Each lending decision made by the Group has to be based on a prior loan analysis. During loan analysis, the Group identifies, on the basis of available information, whether there are any circumstances which undermine the customer's ability and/or willingness to duly service the credit, which may cause the Group to suffer a loss. Each branch and business unit is fully responsible for processing loan analyses and evaluating the credit risk of each transaction even if the final decision is taken at a higher level. Credit committees, underwriters, and sales staff who are involved in making credit decisions and heads of branches are the first line of defence in managing credit risk. The Group's credit risk area is the second line of defence in managing the credit risk of the loan portfolio. Adherence to internal processes and decision-making authorities are regularly monitored by internal credit controller.

The Group manages its credit risk in accordance with the provisions of the Credit Institutions Act, the regulations issued by the Governor of the Bank of Estonia, the Financial Supervisory Authority, the Estonian Banking Association and other regulatory bodies in Estonia and other countries, where Group operates, and its own credit policy.

The Group's credit policy and relevant procedures for analysing and providing loans are regularly reviewed and updated to reflect changes in the economic environment, the Group's credit risk appetite and the counterparties' settlement behaviour.

Risk-taking decisions are made collectively by the credit committees or relevantly authorised employees in keeping with the limits and restrictions set by the Group's supervisory and management boards.

An important component of the Group's credit risk profile is risk mitigation through a well-diversified loan portfolio, avoiding concentrations of risks related to a single counterparty, single product or single country and controlling risk-taking and changes in the risk profile. Large unsecured credit risk exposures are avoided by limiting maximum credit amounts and credit risk is mitigated through a strong collateral position, which is ensured by accepting liquid and typical assets easy to foreclose.

The Group's credit policy relies on the following risk management approach:

- Loans are mostly provided to individuals. At 31 December 2019, loans to individuals accounted for 93.8% of the loan portfolio. The repayment ability of private persons is by nature more stable than that of companies and less influenced by stress scenarios of economic environment than enterprises.
- Loans are granted under carefully drafted legal agreements and recovery proceedings are conducted in full compliance with applicable law. According to the Group's assessment, there are currently no features in the Baltic, Scandinavian and Spanish legislation or legal practice that might exert a significant additional negative impact on the recovery of loan receivables.
- The Group applies proactive and flexible debt management and results-oriented recovery proceedings.
- Risks are controlled by highly diversified loan portfolio. At 31 December 2019, the average loan balance was 4,214 euros and 100 largest loans accounted for 6.6% of the total loan portfolio. Smaller receivables are generally easier to recover even in the circumstances of a severe economic downturn because the borrower's settlement power is not weakened by the scarcity of (re)financing opportunities and the Group's receivables can usually be settled with regular monthly income.

In its lending operations, the Group focuses on consumer loans and hire-purchase services which are income based. In addition, in Estonia, Latvia and Lithuania, the Group provides loans to small and medium-sized enterprises. At 31 December 2019, the loans to companies accounted for 6.2% of the Group's loan portfolio.

The Group determines corporate exposure limits for the single customer group which cannot exceed 1/3 of the country total loan portfolio.

To obtain an overview of the exposures of the total loan portfolio, the credit risk department monitors the development of the loan portfolio, the customers' payment behaviour and credit risk, and conducts regular stress tests that focus on assessing the effects that various possible though not probable events may have on the Group's financial performance and capital. Such events include growth in settlement arrears due to adverse changes in the macroeconomic environment, specific developments and changes in the dynamics of settlement defaults.

Measurement and classification of credit risk

Loan customers' credit risk is measured in a quantifiable manner through the Group's internal scoring models (at the moment of credit origination) and rating models (during the lifetime of the credit). A customer's credit rating is embedded in the Group's risk management system and it is used for assessing the customer's payment ability and the probability of default, creating loss allowances, assigning credit limits, measuring receivables and determining the frequency of credit risk assessments and the principles of monitoring credit risk.

A credit rating is an assessment characterising the counterparty in a transaction or the credit risk of a receivable that is used to grade customers or receivables based on the extent of the credit risk exposure. The system of credit ratings differentiates customers and receivables according to their risk level, based on the probability of default in light of the customer's financial position, creditworthiness, value and marketability of collateral (security) and other circumstances that may influence the customers' ability to meet their obligations to the Group.

Each customer is assigned a credit rating at the time the loan application is reviewed. The rating is revised when monitoring indicates that circumstances underlying the credit rating have changed. Circumstances are reviewed monthly. The frequency of changing the rating depends on the features of the group of loans and the loan class. The ratings of companies are updated at least once a year or whenever there is reason to believe that the borrower's credit risk has changed; in the case of non-performing loans the rating is reviewed once a quarter. The ratings of retail customers are updated whenever there is a significant change in the borrower's credit risk.

The main parameters the Group uses in assessing credit risk are the probability of default (PD), loss given default (LGD) and exposure at default (EAD). The probability of default reflects how high is the probability that the loan customer will experience a settlement default of more than 90 days by the 12th month after the assessment. Loss given default reflects the economic loss that may occur in the event of default of more than 90 days on the basis of country- and product-specific loss rates identified using historical loss statistics, which have been, if needed, adjusted to reflect expert opinions. The exposure is equal to the carrying amount of the receivable. Credit risk is assessed by expected credit loss (ECL) formula $ECL = PD * LGD * EAD$. LGD and PD estimates are updated at least once per year.

(In thousands of euros)

A loan is classified as non-performing on the occurrence of any of the following events associated with the customer, which will or may lead to imminent or future insolvency:

- Low probability of collecting payments. The loan (agreement) is performing but on the basis of objective evidence it is reasonable to assume that the customer is unable to meet the existing financial obligations (loan principal, associated interest and contract fee) in full and the situation cannot be resolved in a satisfactory manner.
- Default on meeting a significant financial obligation. The loan (agreement) is classified as non-performing when the customer is over 90 days in default on the obligation to pay a significant amount of loan principal, interest or fees or the loan is materially restructured so that the remaining balance of loan principal or the accrued interest is reduced and the circumstances causing the customer's financial difficulty have not been eliminated.

To better evaluate credit risk, the Group divides loan receivables into six major classes using an internal rating system for determining their quality:

- *Very good.* The customer's ability to pay and factual payment behaviour are very good. There is no evidence suggesting that weaknesses could emerge.
- *Good.* The customer's estimated ability and willingness to pay and factual payment behaviour are good. The Group is not aware of any circumstances that could cause the receivable not to be settled in accordance with the originally agreed terms and the customer's credit risk is low or moderate.
- *Satisfactory.* The customer's estimated ability and willingness to pay and factual payment behaviour are satisfactory. There may occur up to 60-day defaults and the receivable may have to be restructured in order to eliminate weaknesses. The customer's credit risk is moderate, i.e. ordinary.
- *Weak.* The customer has clearly identifiable economic weaknesses. The customer is making payments but there may occur up to 60-day defaults, which is why the receivable has to be restructured. Repayment of the loan is probable but the customer's credit risk is high.
- *Inadequate.* The customer is more than 90 days in default on significant commitments or there have been done restructuring activities without which the customer would be in default. Settlement of the entire receivable is unlikely if the situation does not change.
- *Irrecoverable.* The customer is insolvent, repayment is unrealistic and the Group does not have economically effective measures for collecting the receivable or the customer has been declared bankrupt.

Loan portfolio by internal rating classes

As at 31 December	2019	2018
Very good	228,759	224,604
Good	160,988	138,620
Satisfactory	53,940	55,549
Weak	8,063	10,823
Inadequate	21,541	15,692
Irrecoverable	164	391
Total	**473,455**	**445,679**

(In thousands of euros)

Loans whose principal or interest payments are in arrears break down as follows:

Loss allowances by ageing of loans as at 31 December 2019

	Loan receivable	Loss allowance	Risk position
Loan portfolio not past due	398,456	-8,206	390,250
Loan portfolio past due	74,999	-14,094	60,905
Total	**473,455**	**-22,300**	**451,155**
Past due portfolio according to days past due:			
Up to 30 days	45,654	-1,729	43,925
31-60 days	9,513	-2,054	7,459
61-90 days	4,457	-1,334	3,123
Over 90 days	15,375	-8,977	6,398
Total past due portfolio	**74,999**	**-14,094**	**60,905**

Loss allowances by ageing of loans as at 31 December 2018

	Loan receivable	Loss allowance	Risk position
Loan portfolio not past due	372,947	-8,995	363,952
Loan portfolio past due	72,732	-12,876	59,856
Total	**445,679**	**-21,871**	**423,808**
Past due portfolio according to days past due:			
Up to 30 days	44,163	-2,032	42,131
31-60 days	9,120	-2,094	7,026
61-90 days	4,846	-1,590	3,256
Over 90 days	14,603	-7,160	7,443
Total past due portfolio	**72,732**	**-12,876**	**59,856**

Policy for creation of loss allowances

The policies for creating loss allowances for loans are described in note 1.

The Group creates loss allowances to mitigate the risk of a decline in the value of its loan receivables, i.e. their impairment. To mitigate the risks associated with the customers' payment behaviour and to cover credit losses, the Group has created loss allowances, which at 31 December 2019 totalled 22,300 thousand euros, accounting for 4.7% of the total loan portfolio (31 December 2018: 21,871 thousand euros; 4.9%). Contractual amount outstanding on financial assets that were written off during the reporting period and are still subject to enforcement activity is 1,665 thousand euros. Further information on impairment allowances is presented in note 7.

(In thousands of euros)

Cash and bank balances by the banks' credit ratings*

According to the management's estimate, the exposure of cash and cash equivalents held at central banks and other banks has low credit risk. All loans to and receivables from central banks and credit institutions have been serviced and paid in time. For depositing liquid funds, the Group's risk management policy prefers credit institutions that have higher equity and better credit rating.

Not rated credit institutions are local credit institution, which does not have external credit rating. Based on the information from the market, the Group assesses that the credit institution has good credit quality.

At 31 December 2019 and 31 December 2018, the Group's receivables from central banks and credit institutions are not over-due, these receivables are either on demand or have maturity less than 3 months. Taking this into account, the expected credit loss on the receivables from central banks and credit institutions is immaterial and therefore no allowances for them have been recorded on the balance sheet.

For the purpose of ECL measurement cash and cash equivalents balances are included in Stage 1. The ECL for these balances represents an insignificant amount, therefore the Group did not recognise any credit loss allowance for cash and cash equivalents.

The Group uses Moody´s Investors Service as the external credit assessment institution (ECAI) in the calculation of its risk-weighted exposure amounts in accordance with the rules laid down in Regulation (EU) 575/2013. The Group uses ECAI for the following exposure classes: (i) exposures to central governments or central banks; (ii) exposures to regional or local governments; (iii) exposures to public sector entities; (iv) exposures to multilateral development banks; (v) exposures to international organisations; (vi) exposures to institutions.

The cash balances at banks, including central banks, based on Moody's Investors Service ratings or their equivalents, are as follows:

As at 31 December	2019	2018
P-1	44,627	44,954
P-2	6,612	13,970
not rated	2,701	7,028
Total	**53,940**	**65,952**

* Ratings are based on the ratings of the banks or their parent companies.

Cash balances with the central banks, including mandatory reserve deposits in amount of 32,855 thousand euros have low credit risk and therefore rating P-1 is assigned.

(In thousands of euros)

Debt instruments at fair value through other comprehensive income by ratings

The debt instruments at fair value through other comprehensive income (see note 5), based on Moody's Investors Service ratings or their equivalents, are as follows:

As at 31 December	2019	2018
Aaa-Aa3	5,754	4,299
A1-A3	11,966	3,141
Baa1-Baa3	13,670	6,044
Total	**31,390**	**13,484**

Exposure to counterparty credit risk

Counterparty risk arises in cases where a counterparty in a FX, interest, equity, credit or commodity derivative transaction defaults and fails to meet its financial obligations and the collateral that has been received is insufficient to cover the claim. The financial loss in this case is the replacement cost, that is, the cost of replacing an existing transaction by a new transaction with similar characteristics but at current market prices. The Group had no exposure to counterparty credit risk as at 31 December 2019 and as at 31 December 2018.

Market risk

Market risk is the risk of loss resulting from changes in market prices and rates which are unfavourable for the Group (including changes in interest rates, credit spreads, equity prices, foreign exchange rates and commodity prices), the correlations between them and volatility. Within market risk the Group has identified foreign currency risk (FX risk) and interest rate risk.

The Group does not accept commodity risk. The Group did not have any risk positions stemming from the equity instruments as at 31 December 2019 and at 31 December 2018.

Market risk may arise from the Group's activity in the financial markets and from the majority of the Group's products (loans, deposits). Market risks predominantly arises from the Group's core business activities, taking market risk is not the main activity. The Group avoids concentrations of market risk. The Group's market risk strategy is conservative and the Group's general market risk appetite is on the Moderate level.

Supervisory board approves the strategy, risk appetite and risk policy for market risk management. Treasury unit is responsible for managing market risk. Management Board approves market risk limits and detailed regulations for the market risk management. Risk reporting and financial risk control unit is responsible for measuring, monitoring and reporting on the market risk, also for independent verification of the valuations of debt instruments held at fair value. All violations of early-warning indicators and limits are escalated to a higher level as required by the Market Risk Policy.

Foreign currency risk is the risk of loss due to changes in spot or forward prices and the volatility of currency exchange rates. The risk appetite of foreign currency risk is on the Low level. Foreign currency risk management is based on the principle that net open currency positions must not exceed 2% of net own funds and taking speculative positions is avoided. Foreign currency risk is measured by the FX single and aggregated position level.

(In thousands of euros)

The Group's foreign currency position in Swedish krona arises from services provided to customers at the Swedish branch.

Net currency positions as at 31 December 2019

	Position in the statement of financial position		Off-balance sheet position		Net position
	Assets	Liabilities	Assets	Liabilities	
EUR (euro)	500,771	379,646	-	21,001	100,124
SEK (Swedish krona)	54,168	53,494	-	-	674

Net currency positions as at 31 December 2018

	Position in the statement of financial position		Off-balancesheet position		Net position
	Assets	Liabilities	Assets	Liabilities	
EUR (euro)	459,361	349,764	-	18,430	91,167
SEK (Swedish krona)	56,769	57,579	-	-	-810
GBP (British pound)	6	-	-	-	6

* For liabilities included in the position off the statement of financial position, see note 26.

Foreign currency risk is measured additionally by using sensitivity analysis. The following tables reflect the potential impact of positions exposed to currency risk on the Group's profit and equity. If the reporting-date exchange rates of the foreign currencies against the euro had strengthened/weakened by 10%, the impact would have been as follows:

Effect of a potential exchange rate change on profit and equity as at 31 December 2019

	Exposure	Monetary impact	% of equity
SEK (Swedish krona)	-674	67	0.0%
Total	**-674**	**67**	**0.0%**

Effect of a potential exchange rate change on profit and equity as at 31 December 2018

	Exposure	Monetary impact	% of equity
SEK (Swedish krona)	-810	81	0.1%
GBP (British pound)	6	1	0.0%
Total	**-804**	**82**	**0.1%**

Interest rate risk is the risk that the value of the Group's assets and liabilities could be negatively affected by changes in interest rates. Interest rate risk stemming from the bond portfolio is a risk to the earnings or market value of the bond portfolio due to uncertain future interest rates.

The Group withdrew in 2019 exemption from the trading book pursuant to Article 94 of EU Regulation 575/2013. By derogation, the own funds requirements for trading book related activities were replaced by the own fund requirements related to credit risk.

Group's interest rate risk appetite for bond portfolio is on the Moderate level. Market risk stemming from the bond portfolio is driven by the Group's goal to maintain a strong liquidity position. The secondary purpose of holding bond portfolio is to support the Group's profitability, but profit expectations shall not override liquidity requirements. The Group does not take speculative trading positions and does not provide customer-focused trading activities.

Interest rate risk stemming from the bond portfolio is measured by using stress tests and scenario analyses which are performed at least on a quarterly basis. The Group tests its bond portfolio by applying historical scenarios (extreme movements in market factors which have been observed in the past) and also hypothetical scenarios (extreme movements that could potentially happen in the future).

Interest rate risk of the banking book (IRRBB) is the current or prospective risk to both the earnings and the economic value of the Group arising from adverse movements in interest rates that affect interest rate sensitive instruments, including gap risk and option risk.

IRRBB is a significant risk for the Group. The main sources of structural IRRBB are adverse changes in loan and/or deposits interest rates.

In the target risk profile, the Group's appetite for this risk is on the Moderate level. Risk versus return considerations are applied. The basis of the Group's IRRBB strategy is to maintain a balanced position in the short-term (next 12-24 months) perspective and a controlled open risk position in the longer perspective by active management of the structure and maturities interest-sensitive assets and liabilities.

During the assessment of IRRBB, as a first step all sources of risk arising from interest-rate-sensitive positions are identified. At least on a quarterly basis Group measures interest rate risk which may be arising from:

- the timing mismatch in the maturity and repricing of assets and liabilities and off-balance sheet short and long-term positions (repricing risk);
- changes in the slope and the shape of the yield curve (yield curve risk);
- options, including embedded options, e.g. consumers redeeming fixed-rate products when market rates change (option risk).

Group measures its IRRBB exposure in terms of both potential changes to economic value of equity (EVE), and changes to expected 12-months net interest income (NII) or earnings. Due to reason that consumer loan contracts are frequently repaid before contractual maturity Group uses behavioural cash flows instead of contractual cash flows when calculating interest rate risk in order to capture the optionality.

Group uses different sensitivity analyses and scenarios to assess the interest rate risk arising from the banking book, i.e. the supervisory shock scenario, according to which yield curve has a parallel shift of 200 basis points, as well as other scenarios taking into account changes in the yield curve and individual risk profile.

As at 31 December 2019, the impact of the supervisory shock scenario (200 bps parallel shift) to 12-months net interest income (NII) was 718 thousand euros and to the economic value (EVE) was 4,852 thousand euros.

Group didn't use hedging instruments for market risk mitigation as at 31 December 2019.

Liquidity risk

Liquidity risk is the risk that the Group is unable to fulfil its obligations in a timely manner or in the full extent without incurring significant costs.

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Within liquidity risk the Group has identified funding risk, which is the risk of being unable to engage resources without negatively affecting the daily activities or financial position.

The liquidity risk framework covers both liquidity management on standard conditions and in the event of a liquidity crisis. The Group's liquidity risk strategy is to maintain a conservative liquidity risk profile and sufficient liquidity reserves. Maintaining strong liquidity position is one of the main priorities of the Bank. The Group shall at all times be able to fulfill its obligations in a timely and full manner both in normal and crisis situations as long as possible. Liquidity risk management is based on conservative assumptions.

The main objective of the Group's funding strategy is to ensure sufficient and stable funding of the core activities using the Group's own capital and external financing. The secondary objective of the funding management is optimisation of the costs, size and composition of external resources involved, but cost-effectiveness and cost-competitiveness may not override sufficient, stable and conservative funding requirements. Group's funding is primarily based on retail term deposits. Starting from 2019, the Group is taking part in the ECBs targeted long term refinancing operations (TLTRO-III). Diversification is a key part of the Groups overall funding and liquidity management strategy.

Funding strategy is closely related to asset quality and structure management. The Bank's assets structure and its maturities shall correspond to the funding structure and shall not rely on very short-term funding resources. The Group avoids the concentration of funding.

In the Group's target risk profile, the appetite for liquidity risk is on the *Low* level and the appetite for taking funding risk is on the *Moderate* level.

Supervisory board approves liquidity risk strategy and liquidity risk appetite by the liquidity risk policy. Management board approves the liquidity risk limits and detailed procedures for liquidity risk management. The responsibility over liquidity risk management lies in the treasury unit. Risk reporting and financial risk control unit is responsible for the risk control, measurement and reporting to the management. Requirements for the liquidity risk reporting (recipients, content of reports, frequency) and measurement are established in the liquidity risk policy. Liquidity risk reporting to the management board and supervisory board is at least on a quarterly basis, risk level is monitored on a daily basis. The conservative liquidity risk profile is kept within the limits set by the supervisory board. The management board has established a set of early warning indicators to identify the emergence of increased risks or vulnerabilities in the banks liquidity position or potential funding needs. Any breaches of limits and key risk indicators thresholds shall be escalated according to requirements set by the policy.

The Group measures liquidity risk using different ratios. The regulatory measure LCR (liquidity coverage ratio) indicates whether the Group has sufficient liquid assets to cover short-term liabilities that correspond to net cash-flow during 30 days under stress. The Group also measures its liquidity risk by calculating tolerance period which is a time period under stress conditions the Group is able to continue business as usual and fulfil its obligations without engaging additional resources or changing its activity plans. Regulatory NSFR (net stable funding ratio) is defined as the amount of available stable funding relative to the amount of required stable funding.

(In thousands of euros)

Liquidity risk management measures

	31 Dec 2019	31 Dec 2018
Liquidity coverage ratio (LCR)	644.0%	907.0%
Tolerance period (in months)	3.6	5.7
Net stable funding ratio (NSFR)	132.8%	126.0%
Loan to deposit ratio	117.0%	109.0%
Liquidity reserve and assets ratio	10.2%	14.7%
Long term (over 1 year) funding to total funding ratio	59.5%	50.1%

The Group conducts regular liquidity risk stress tests (at least semi-annually) as a part of its overall stress testing programme, to understand the impact of adverse events on its risk exposure and on the quantitative and qualitative adequacy of its liquid assets, and to determine whether the Group's liquidity buffer is sufficient to react or cover risks that may crystallise during different types of stress scenarios and/or to address risks posed by control, governance or other deficiencies. Stress test are conducted using at least three different scenarios- idiosyncratic, market-wide and combined scenario.

The outcome of stress testing is integrated into the Group's strategic planning process for liquidity and funding and used to increase the effectiveness of liquidity management in the event of a crisis, including the Group's recovery planning. Stress testing results are used to determine the minimum size and composition of the liquidity buffer. Stress test results are reported to the management board and supervisory board.

Management of the Group's liquidity and funding is centralised, funding of the subsidiaries and branches is provided on a Group level. The Bank regularly assesses that there are no material restrictions and hindrances to intragroup transfer of liquidity.

The Group has a contingency plan in place which defines the actions to be taken should the Group encounter a liquidity shortfall in a stressed emergency situation. The plan describes the strategy, policy and activity plan for coping with liquidity crises of different magnitude, and stipulates a clear chain of command and escalation procedures. The contingency plan is tested regularly.

The Group constantly monitors the situation in financial markets and opportunities of alternative funding instruments. In order to mitigate liquidity risk the Group may consider various measures, such as partial sale of claims, participation in the loan programs of the European Central Bank, money market placements from other credit institutions and credit lines from other credit institutions.

(In thousands of euros)

Remaining maturities of financial assets and liabilities as at 31 December 2019

	Past due	Less than 1 month	1-12 months	1-5 years	Over 5 years	Total
Financial assets						
Cash and bank balances	-	51,240	2,700	-	-	53,940
Loans to customers	13,046	10,468	108,124	268,710	59,308	459,656
Of which loan portfolio	4,545	10,468	108,124	268,710	59,308	451,155
Of which interest receivables	8,501	-	-	-	-	8,501
Debt instruments at fair value through other comprehensive income	-	-	1,300	26,358	3,732	31,390
Other receivables	113	1,373	252	-	-	1,738
Total financial assets	**13,159**	**63,081**	**112,376**	**295,068**	**63,040**	**546,724**
Financial liabilities						
Loans from central banks	-	-	-	23,000	-	23,000
Deposits from customers	-	20,658	150,295	191,522	30,363	392,838
Subordinated notes	-	-	-	-	4,965	4,965
Lease liabilities	-	61	573	1,100	362	2,096
Total financial liabilities	**-**	**20,719**	**150,868**	**215,622**	**35,690**	**422,899**
Net exposure	**13,159**	**42,362**	**-38,492**	**79,446**	**27,350**	**123,825**

Remaining maturities of financial assets and liabilities as at 31 December 2018

	Past due	Less than 1 month	1-12 months	1-5 years	Over 5 years	Total
Financial assets						
Cash and bank balances	-	49,425	16,527	-	-	65,952
Loans to customers	16,924	8,074	97,377	256,079	49,510	427,964
Of which loan portfolio	12,767	8,074	97,377	256,079	49,511	423,808
Of which interest receivables	4,156	-	-	-	-	4,156
Debt instruments at fair value through other comprehensive income	-	516	-	8,777	4,191	13,484
Other receivables	139	882	326	137	-	1,484
Total financial assets	**17,063**	**58,897**	**114,230**	**264,993**	**53,701**	**508,884**
Financial liabilities						
Deposits from customers	-	21,032	180,243	170,176	21,569	393,020
Subordinated notes	-	-	-	-	4,960	4,960
Total financial liabilities	**-**	**21,032**	**180,243**	**170,176**	**26,529**	**397,980**
Net exposure	**17,063**	**37,865**	**-66,013**	**94,817**	**27,172**	**110,904**

(In thousands of euros)

The negative mismatch of assets and liabilities in the 1-12 months' bucket has decreased but the Group's maturing deposits still exceed its new short-term loan portfolio. The negative gap in this period is planned to be refinanced with term deposits from customers.

Expected undiscounted future cash flows of the Group's financial liabilities as at 31 December 2019

	Carrying amount	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Payables to suppliers (note 15)	**2,096**	2,096	-	-	-	-	2,096
Loans from central banks (note 13)	**23,000**	-	-	-	23,000	-	23,000
Deposits from customers (note 14)	**392,838**	21,064	24,882	130,167	202,887	32,972	411,972
Subordinated notes	**4,965**	-	-	330	1,319	5,989	7,638
Lease liabilities	**2,096**	63	125	467	1,138	367	2,160
Unused portions of credit lines and bank guarantees (note 26)	**21,001**	102	130	3,301	17,468	-	21,001
Total liabilities	**445,996**	**23,325**	**25,137**	**134,265**	**245,812**	**39,328**	**467,867**

Expected undiscounted future cash flows of the Group's financial liabilities as at 31 December 2018

	Carrying amount	Less than 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Payables to suppliers (note 15)	**1,131**	1,131	-	-	-	-	1,131
Deposits from customers (note 14)	**393,020**	15,207	25,616	160,304	180,674	23,493	405,294
Subordinated notes	**4,960**	-	-	329	1,319	6,319	7,967
Unused portions of credit lines and bank guarantees (note 26)	**18,430**	67	512	6,528	11,323	-	18,430
Total liabilities	**417,541**	**16,405**	**26,128**	**167,161**	**193,316**	**29,812**	**432,822**

Operational risk

Operational risk is risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. The definition includes compliance risk and legal risk, but excludes strategic and reputational risks.

Operational risk consists of different sub-risks such as legal risk, compliance risk (including money laundering and terrorist financing risk), information security risk and information and communication technology risk.

Operational risk entails the following risks:

- Legal risk is the risk resulting from non-conformity with or misinterpretation of legislation, contracts, good practice and standards of ethics. Legal risk may materialise in any of the above risk types, as the Group may become subject to claims or proceedings due to contractual or other legal responsibilities.
- Compliance risk is the risk that failure to fully meet laws, regulations, internal rules and obligations to customers, employees and other stakeholders may impair the Group's business model, reputation and financial condition. Money laundering and terrorist financing (ML/TF) risk which is part of compliance risk is defined as the risk of the Group being used for ML/TF due to weaknesses and non-compliances in internal processes.
- Information and communication technology (ICT) risk is the risk of losses due to the inappropriateness or failure of hardware and software, which can compromise the availability, integrity, accessibility and security of technical infrastructure and data.

Strategy and processes of management of operational risk are defined in Operational Risk Policy approved by Supervisory Board. The Group's strategy is to keep operational risk at a reasonably minimal level and to minimise potential losses while taking into account the Group's strategic objectives and the principle o

General management of operational risk and compliance risk takes place on Group level: all branches and subsidiaries comply with Group level principles, rules and limits. However, every head of branch is responsible for operational and compliance risk management on the branch/country level.

Incident handling

The Group has established the common methodology and implemented supporting system to ensure Group-wide reporting and management of loss events and incidents. Incidents and loss events which have above average impact (level 3 on scale 1-4) shall be escalated to the branch Executive Board and/or Head(s) of Area(s). Incidents and Loss events which have high impact (level 4 on scale 1-4) will be immediately escalated to the Management Board and as well to the branch Executive Board and/or Head(s) of Area(s), if relevant.

Risk assessments

All structural units are involved in annual risk and control self-assessment (RCSA) process to identify and assess the risks and controls, and to implement adequate measures to reduce the risks when relevant.

There is a specific risk analysis tool created to manage the risks arising from different changes, e.g. launch of new products or services; outsourcing etc.

Business continuity management
The Group has established business continuity management framework to guarantee the continuity or recovery of Group's operations and manage "low probability – high impact" incidents like IT disruptions, natural disasters, pandemics etc.

The capital requirement to cover operational risk is identified using the standardised approach.

Other material risks

Other material risks include reputational risk, business and strategic risks.

Reputational risk is the current or prospective risk to the Group earnings, own funds or liquidity arising from damage to the Group's reputation.

Reputational risk is the current or prospective risk to the Group's rnings, own funds or liquidity arising from damage to the Group's reputation. Business risk is the risk that inadequate business decisions or inadequate implementation of decisions or changes in customer expectations or inadequate implementation of new technologies will result in loss or significantly reduced revenues.

Strategic risk is the risk resulting from an inadequate strategy or inadequate implementation of the strategy.

Reputational risk and strategic risk are an essential part of the business model which are analysed as part of strategic and operational planning.

The Group's risk appetite for reputational risk in the target risk profile is on a *Low* level while the target risk profile for business and strategic risk is on a *Moderate* level.

Strategic risk is managed by implementing suitable strategy, which corresponds to the current economic environment and is based on a comprehensive planning process, and by responding adequately and in a timely manner to changes. The Group's strategy for reputational risk management is to avoid situations that could potentially have a negative impact on its reputation and cause a decrease in revenue or loss of trust. Reputation building begins with customer experience management and controlled creation of public opinion. On an ongoing basis, business and control units identify, manage, and assess internal and external factors that could impede achievement of strategic objectives or may have a negative impact on reputation.

OWN FUNDS AND CAPITAL

Bigbank's ability to take risk depends on its risk-bearing capacity. A key factor which determines risk-bearing capacity is stable earnings. These allow to build a strong capital base which can be used to absorb potential risks and (unexpected) losses. The Group holds at all times capital adequate for covering all of its material risks and regulatory requirements.

The methods used by the Group for calculating own funds are stipulated in regulation (EU) No. 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms (CRR) and Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (CRD 4) as transposed into Estonian law.

The Group classifies items as own funds based on relevant regulatory requirements. The most important components of the Group's own funds are:

- **Common Equity Tier 1 Capital (CET1)** including:
  - o **Paid-in share capital.** The Group's paid-in share capital amounts to 8,000 thousand euros.
  - o **Capital reserve** (as other reserves pursuant to Article 4 (117) of EU Regulation 575/2013). In line with the requirements of the Commercial Code, the Group has created a statutory capital reserve which at 31 December 2019 amounted to 800 thousand euros.
  - o **Prior years retained earnings.** Profits retained in previous years have been audited by an independent external auditor. The figure has been determined by taking into account all relevant taxes and dividend distributions. At 31 December 2019, the Group's prior period retained earnings totalled 106,568 thousand euros.
  - o **Other reserves** include accumulated other comprehensive income.
  - o **Profit eligible** includes net profit for the reporting period that has been verified by an independent external auditor in the review of the financial information (2019: nine months), less foreseeable dividends proportionally and following the permit of the Estonian Financial Supervision Authority.

- **Tier 2 Capital,** including:
  - o **Subordinated bonds.** As of 31 December 2019 Group had issued subordinated bonds of 5,000 thousand euros with a remaining 10 year maturity.

The Group deducts from CET1 intangible assets, provisions which have not been verified by an independent external auditor in the review of financial information and other items specified in the law.

The Group has included 9 months' audited income, less foreseeable dividends proportionally with the permission of the Financial Supervisory Authority, in the total amount of 13,787 thousand euros into CET1 capital.

In 2017, the Group issued 5,000 thousand euros worth of 10-year subordinated bonds which are treated as Tier 2 capital. There are no other Tier 2 capital instruments outstanding.

At 31 December 2019, the Group's total own funds amounted to 113,851 thousand euros.

(In thousands of euros)

As at 31 December	2019	2018
Paid up capital instruments	8,000	8,000
Other reserves	800	800
Prior years retained earnings	106,568	94,042
Other accumulated comprehensive income	1,231	997
Other intangible assets	-19,254	-12,381
Profit eligible	11,537	9,970
Adjustments to CET1 due to prudential filters	-31	-191
Common equity Tier 1 capital	**108,851**	**101,237**
Tier 1 capital	**108,851**	**101,237**
Tier 2 capital	**5,000**	**5,000**
Deductions	-	-
Total own funds	**113,851**	**106,237**

Total risk exposure

The methods used by the Group for calculating the total risk exposure and single risk positions are stipulated in CRR. The Group uses the standardised approach in calculating capital requirements for the credit risk, market risk and the operational risk.

As at 31 December	2019	2018
Risk weighted exposure amounts for credit and counterparty credit risks (standardized approach)		
Central governments or central banks	-	1,246
Institutions	3,260	12,141
Corporates	22,886	40,210
Retail	312,757	286,451
Secured by mortgages on immovable property	4,586	3,215
Exposures in default	14,926	11,418
Claims on institutions and corporates with a short-term credit assessment	2,393	-
Other items	9,910	8,735
Total risk weighted exposure amounts for credit and counterparty credit risks (standardised approach)	**370,718**	**363,416**
Total risk exposure amount for position, foreign exchange and commodities risks	**18,821**	**-**
Total risk exposure amount for operational risk (standardised approach)	**101,632**	**104,953**
Total risk exposure amount for credit valuation adjustment (standardised approach)	**-**	**-**
Total risk exposure amount	**491,171**	**468,369**

(In thousands of euros)

Capital ratios

As at 31 December	2019	2018
CET1 Capital ratio	22.2%	21.6%
T1 Capital ratio	22.2%	21.6%
Total capital ratio	23.2%	22.7%
Leverage ratio	19.2%	19.3%
Minimum requirement for eligible liabilities (MREL)	21.0%	20.9%

Total capital ratio has been calculated for Bigbank AS Group. At 31 December 2019, total capital ratio at the level of the parent company was 22.2% (31 December 2018: 22.6%).

The composition of the Group's own funds, their treatment and the calculation of capital ratios are in accordance with the CRR.

The definition of a consolidation group for the purposes of calculating capital adequacy does not differ from the definition of a consolidation group for the purposes of preparing financial statements.

In June 2019, the Financial Supervision Authority set a new minimum requirement for eligible liabilities (MREL) as 14.31% of Group's total liabilities and own funds. At 31 December 2019 the Group's own funds and eligible liabilities actual ratio was 21.0%.

Capital management

The capital management objectives are to ensure that the Group has an optimal structure of assets and liabilities and adequate capital to cover, at all times, all identified material risks and risk-related activities (*capital adequacy*) and that the Group complies with all capital adequacy requirements.

The main tools for capital management are continuous internal capital adequacy assessment process (ICAAP), regular capital planning and capital allocation.

The main principles of the Group's capital management are as follows:

- Ensuring capital adequacy is an integral part of strategic and daily business decision-making as well as an integral part of the daily risk management process.
- The Group evaluates and estimates the risk level and the capital need for covering all identified material risks on a continuous basis.
- The Group's capital must, at all times, be adequate for covering all of its material risks (must at all times exceed its aggregated risks).
- The Group assesses continuously possible future capital requirements (capital planning) for ensuring a prudent level of capitalisation taking into account additional capital needs (planned growth, strategic plans), dividend policy, potential changes in the regulatory environment as well as possible macroeconomic downturns.
- The Group performs capital adequacy assessment both on a solo and consolidated basis.
- The Group defines the minimum capital requirement and the target capital requirement needed for ensuring the sustainability of its operations;
- The Group does not accept any risk, if its capital is inadequate for covering future losses resulting from the materialisation of this risk.

(In thousands of euros)

Minimum regulative capital requirement as at 31 December 2019

	Common equity Tier 1 capital ratio	Tier 1 capital ratio	Total capital ratio
Base capital requirement	4.5%	6.0%	8.0%
Pillar 2 capital charge	1.4%	1.9%	3.4%
Total SREP capital requirement (TSCR)	5.9%	7.9%	11.4%
Capital conservation buffer	2.5%	2.5%	2.5%
Systemic risk buffer	0.4%	0.4%	0.4%
Countercyclical risk buffer	0.2%	0.2%	0.2%
Total capital requirement (OCR)	**9.2%**	**11.2%**	**14.7%**

Conservative principle is used in capital management and additional capital buffer is maintained in addition to the total capital requirement. In 2019 the Group's target was to maintain the total ratio at least 16.7%. From December 2019 a new total capital requirement came into effect and the Group's target ratio is 15.7%.

As at 31 December 2019 the total capital ratio was 23.2% which exceeds the regulatory requirement. Group's common equity Tier1 (CET1) capital ratio was 22.2% and Tier 1 capital ratio was 22.2%. The Group meets the minimum regulative capital requirement as at 31 December 2019.

NOTE 4. CASH AND BANK BALANCES AND CASH EQUIVALENTS

Cash and balances at banks as at 31 December 2019

	Estonia	Latvia	Lithuania	Finland	Sweden	Total
Cash and balances at central banks	**29,354**	**1,000**	**-**	**2,501**	**-**	**32,855**
Of which mandatory reserves*	810	-	-	149	-	959
Of which surplus on mandatory reserves	28,544	1,000	-	2,352	-	31,896
Due from banks	**6,278**	**2,147**	**1,937**	**732**	**1,435**	**21,085**
Of which cash balances at banks	3,577	2,147	1,937	732	1,435	18,384
Of which term deposits at banks	2,700	-	-	-	-	2,700
Of which interest receivable from banks	1	-	-	-	-	1
Total	**35,632**	**3,147**	**1,937**	**3,233**	**1,435**	**53,940**
of which cash and cash equivalents	**34,821**	**3,147**	**1,937**	**3,084**	**9,991**	**52,980**

(In thousands of euros)

Cash and balances at banks as at 31 December 2018

	Estonia	Latvia	Lithuania	Finland	Spain	Sweden	Total
Cash and balances at central banks	**16,127**	**-**	**-**	**13,564**	**-**	**-**	**29,691**
Of which mandatory reserves*	1,246	-	-	84	-	-	1,330
Of which surplus on mandatory reserves	14,881	-	-	13,480	-	-	28,361
Due from banks	**20,065**	**2,389**	**2,205**	**2,664**	**7,503**	**1,435**	**36,261**
Of which cash balances at banks	4,064	2,389	2,178	2,664	7,003	1,435	19,733
Of which term deposits at banks	16,000	-	27	-	500	-	16,527
Of which interest receivable from banks	1	-	-	-	-	-	1
Total	**36,192**	**2,389**	**2,205**	**16,228**	**7,503**	**1,435**	**65,952**
of which cash and cash equivalents	**34,945**	**2,389**	**2,205**	**16,144**	**7,503**	**1,435**	**64,621**

* The mandatory reserve requirement is fulfilled in accordance with the Regulation (EC) No. 1745/2003 of the ECB of 12 September 2003 on the application of minimum reserves (ECB/2003/9). The mandatory reserve rate is 1% of deposits and borrowings with maturities up to 2 years, after allowed deductions, filled by average of period set by the European Central Bank, by depositing the appropriate amount of euros on TARGET2 account with the Bank of Estonia.

Cash and cash equivalents

As at 31 December	2019	2018
Demand and overnight deposits with credit institutions	18,384	19,733
Term deposits with credit institutions with maturity of less than 3 months	2,700	16,527
Surplus on the mandatory reserves with central banks	31,896	28,361
Total cash and cash equivalents	**52,980**	**64,621**

NOTE 5. DEBT INSTRUMENTS

As at 31 December	2019	2018
Debt instruments by issuer		
General governments' bonds	4,759	4,701
Credit institutions' bonds	6,583	3,145
Other financial corporations' bonds	2,083	511
Non-financial corporations' bonds	17,965	5,127
Total debt instruments	**31,390**	**13,484**
Debt instruments by currency		
EUR (euro)	28,841	11,633
SEK (Swedish krona)	2,549	1,851

Debt securities in amount of 25,767 thousand euros were pledged as collateral at 31 December 2019 (see note 25).

(In thousands of euros)

A reconciliation of changes in the fair value of debt instruments measured at FVOCI is as follows:

	2019	2018
Opening balance at 1 January	13,484	11 210,
Acquisition of new financial instruments	21,824	3,025
Redemption of financial instruments	-4,177	-741
Changes in fair value	3	-191
Accrued interest	277	239
Foreign exchange adjustments	-21	-58
Balance at 31 December	**31,390**	**13,484**

(In thousands of euros)

NOTE 6. LOANS TO CUSTOMERS

Loans to customers as at 31 December 2019

	Estonia	Latvia	Lithuania	Finland	Sweden	Total
Loan receivables from customers	102,257	115,495	135,956	76,076	43,671	473,455
Loss allowance for loans	-5,181	-6,419	-2,802	-5,169	-2,729	-22,300
Interest receivable from customers	2,215	2,417	4,789	824	249	10,494
Loss allowances for interest receivables	-901	-865	-43	-139	-45	-1,993
Total loans to customers, incl. interest and allowances	**98,390**	**110,628**	**137,900**	**71,592**	**41,146**	**459,656**
Share of region	21.4%	24.1%	30.0%	15.6%	8.9%	100.0%

Loans to customers as at 31 December 2018

	Estonia	Latvia	Lithuania	Finland	Spain	Sweden	Total
Loan receivables from customers	80,796	102,390	123,706	73,784	11,661	53,342	445,679
Loss allowance for loans	-3,097	-6,307	-1,857	-5,611	-1,905	-3,094	-21,871
Interest receivable from customers	1,712	2,443	535	913	184	335	6,122
Loss allowances for interest receivables	-999	-805	-18	-93	-24	-27	-1,966
Total loans to customers, incl. interest and allowances	**78,412**	**97,721**	**122,366**	**68,993**	**9,916**	**50,556**	**427,964**
Share of region	18.3%	22.9%	28.6%	16.1%	2.3%	11.8%	100.0%

Loan receivables from customers* by loan type

As at 31 December	2019	2018
Income-based loan	436,288	406,570
Surety loans	2,378	1,642
Loans secured with real estate	34,778	37,441
Loans against other collaterals	11	26
Total loan receivables from customers	**473,455**	**445,679**

* Loan receivables from customers comprise loan principal.

Loan receivables from customers* by contractual currency

As at 31 December	2019	2018
EUR (euro)	429,784	392,337
SEK (Swedish kronor)	43,671	53,342
Total loan receivables from customers	**473,455**	**445,679**

* Loan receivables from customers comprise loan principal.

(In thousands of euros)

Ageing analysis as at 31 December 2019*

	Not past due	30 days or less	31-60 days	61-90 days	Over 90 days	Total
Income-based loans						
Loan portfolio	365,629	42,818	9,038	4,219	14,584	436,288
Loss allowance	-7,928	-1,640	-2,034	-1,334	-8,687	-21,623
Surety loans						
Loan portfolio	1,854	188	109	2	225	2,378
Loss allowance	-8	-3	-10	-1	-160	-182
Loans secured with real estate						
Loan portfolio	30,964	2,648	366	235	565	34,778
Loss allowance	-269	-87	-10	-	-129	-495
Loans against other collaterals						
Loan portfolio	10	1	-	-	-	11
Loss allowance	-	-	-	-	-	-
Total loan portfolio	**398,457**	**45,655**	**9,513**	**4,456**	**15,374**	**473,455**
Total loss allowance	**-8,205**	**-1,730**	**-2,054**	**-1,335**	**-8,976**	**-22,300**

Ageing analysis as at 31 December 2018*

	Not past due	30 days or less	31-60 days	61-90 days	Over 90 days	Total
Loans against income						
Loan portfolio	343,897	35,752	8,726	4,718	13,477	406,570
Loss allowance	-8,934	-2,014	-2,092	-1,589	-6,853	-21,482
Surety loans						
Loan portfolio	1,226	82	20	3	311	1,642
Loss allowance	-56	-12	-2	-1	-216	-287
Loans secured with real estate						
Loan portfolio	27,801	8,327	374	125	814	37,441
Loss allowance	-5	-6	-	-	-90	-101
Loans against other collaterals						
Loan portfolio	23	2	-	-	1	26
Loss allowance	-	-	-	-	-1	-1
Total loan portfolio	**372,947**	**44,163**	**9,120**	**4,846**	**14,603**	**445,679**
Total loss allowance	**-8,995**	**-2,032**	**-2,094**	**-1,590**	**-7,160**	**-21,871**

* Total loan principals only, does not include interest receivable.

(In thousands of euros)

NOTE 7. LOSS ALLOWANCES FOR LOANS RECEIVABLES FROM CUSTOMERS

Loss allowances as at 31 December 2019

	Loan receivables	Interest receivables	Total receivables subject to impairment	Total loss allowances
Stage 1	417,390	6,215	423,605	-7,721
Stage 2	34,363	1,073	35,436	-5,070
Stage 3	21,702	3,206	24,908	-11,502
Total	**473,455**	**10,494**	**483,949**	**-24,293**

Loss allowances as at 31 December 2018

	Loan receivables	Interest receivables	Total receivables subject to impairment	Total loss allowances
Stage 1	394,944	2,338	397,282	-8,514
Stage 2	33,529	782	34,311	-5,639
Stage 3	17,206	3,002	20,208	-9,684
Total	**445,679**	**6,122**	**451,801**	**-23,837**

Development of allowances in 2019

	Opening balance	Increases due to origination	Decrease due to de-recognition repayments and disposals	Changes due to change in credit risk (net)	Decrease in allowance account due to write-offs	Closing balance
Stage 1	-8,514	-3,892	1,826	2,544	315	-7,721
Stage 2	-5,639	-1,274	581	-815	2,077	-5,070
Stage 3	-9,684	-1,514	1,412	-5,694	3,978	-11,502
Total	**-23,837**	**-6,680**	**3,819**	**-3,965**	**6,370**	**-24,293**

Development of allowances in 2018

	Opening balance	Increases due to origination	Decrease due to de-recognition repayments and disposals	Changes due to change in credit risk (net)	Decrease in allowance account due to write-offs	Closing balance
Stage 1	-11,020	-5,377	2,955	4,588	340	-8,514
Stage 2	-2,951	-1,916	550	-2,106	784	-5,639
Stage 3	-19,727	-842	5,582	-1,784	7,087	-9,684
Total	**-33,698**	**-8,135**	**9,087**	**698**	**8,211**	**-23,837**

(In thousands of euros)

Loss allowances by loan assessment category as at 31 December 2019

	Loans receivables	Interest receivables	Total receivables subject to impairment	Total loss allowances
Collectively assessed items	436,822	10,144	446,966	-23,686
Individually assessed items	36,633	350	36,983	-607
Total	**473,455**	**10,494**	**483,949**	**-24,293**

Loss allowances by loan assessment category as at 31 December 2018

	Loans receivables	Interest receivables	Total receivables subject to impairment	Total loss allowances
Collectively assessed items	407,713	5,848	413,561	-23,715
Individually assessed items	37,966	274	38,240	-122
Total	**445,679**	**6,122**	**451,801**	**-23,837**

Collectively assessed items include homogenous groups of receivables whose individual amount is not significant, historical settlement pattern and collateralisation or other features are similar and which are not assessed for impairment individually.

Individually assessed items include receivables from companies, receivables exceeding 100,000 euros and other receivables that have not been collectively assessed.

NOTE 8. OTHER RECEIVABLES

As at 31 December	2019	2018
Customer receivables and other miscellaneous receivables	1,625	1,345
Collection, recovery and other charges receivable	358	261
Impairment allowance for other receivables	-245	-122
Total	**1,738**	**1,484**

NOTE 9. PREPAYMENTS

As at 31 December	2019	2018
Tax prepayments	620	1,179
Prepaid other taxes	5	23
Prepayments to suppliers and prepaid expenses	640	530
Total	**1,265**	**1,732**

(In thousands of euros)

NOTE 10. PROPERTY AND EQUIPMENT

As at 31 December	Land and buildings	Right-of-use assets: commercial premises	Other items	Total
Cost				
Balance at 1 January 2018	1,514	-	3,522	5,036
Purchases	-	-	1,334	1,334
Sales	-	-	-99	-99
Write-off	-	-	-330	-330
Effect of movements in exchange rates	-	-	-1	-1
Balance at 31 December 2018	**1,514**	**-**	**4,426**	**5,940**
Effect of adoption of IFRS 16 as at 1 January 2019 (note 1)	-	2,776	-	2,776
Purchases	-	-	430	430
Sales	-	-	-271	-271
Write-off	-	-	-354	-354
Revaluation recognised in other comprehensive income*	76	-	-	76
Revaluation and price adjustment	-	46	-	46
Effect of movements in exchange rates	-	-2	-1	-3
Balance at 31 December 2019	**1,590**	**2,820**	**4,230**	**8,640**
Depreciation				
Balance at 1 January 2018	-58	-	-1,532	-1,590
Depreciation charge for the year	-59	-	-1,053	-1,112
Sales	-	-	73	73
Write-off	-	-	313	313
Effect of movements in exchange rates	-	-	1	1
Balance at 31 December 2018	**-117**	**-**	**-2,198**	**-2,315**
Depreciation charge for the year	-59	-733	-1,091	-1,883
Sales	-	-	214	214
Write-off	-	-	335	335
Transfer*	166	-	-	166
Balance at 31 December 2019	**-10**	**-733**	**-2,740**	**-3,483**
Carrying amount				
Balance at 1 January 2018	1,456	-	1,990	3,446
Balance at 31 December 2018	1,397	-	2,228	3,625
Balance at 31 December 2019	**1,580**	**2,087**	**1,490**	**5,157**

* Land and buildings are measured using the revaluation model. The accumulated depreciation as at the revaluation date was eliminated against the gross carrying amount of the revalued asset, see note 30.

(In thousands of euros)

Set out below are the carrying amounts of lease liabilities (note 15) and the movements during the period:

	2019
As at 1 January – effect of adoption of IFRS 16 (note 1)	2,776
Accretion of interest (note 19)	30
Additions	46
Payments	-753
Effect of movements in exchange rates	-3
Carrying amount at end of year	**2,096**

The Group had total cash outflows for leases of 753 thousand euros. The initial application of IFRS 16 resulted in non-cash additions to right-of-use assets and lease liabilities of 2,776 thousand euros at 1 January 2019.

If land and buildings were measured using the cost model, the carrying amounts would be as follows:

As at 31 December	2019	2018
Cost	1,869	1,869
Depreciation	-1,163	-1,089
Net carrying amount	**706**	**780**

NOTE 11. INVESTMENT PROPERTIES

As at 31 December	2019	2018
Opening balance at 1 January	**1,866**	**1,878**
Additions	-	104
Sales	-185	-55
Net profit/loss from fair value adjustment (note 30)	100	-61
Closing balance at 31 December	**1,781**	**1,866**

The investment properties comprise a building in Tartu and also plots, houses and apartments originally pledged by customers as loan collateral and later bought by the Group through auctions.

The Group earned rental income derived from investment properties of 96 thousand euros in financial year 2019 (2018: 105 thousand euros).

The operating expenses were 54 thousand euros, (2018: 53 thousand euros), please see note 24.

The Group has no restrictions on the realisation of its investment properties and no contractual obligations to purchase, construct or develop investment properties or for repairs, maintenance and enhancements.

(In thousands of euros)

NOTE 12. INTANGIBLE ASSETS

	2019	2018
Cost at beginning of year	**15,002**	**9,203**
Purchases	8,288	6,148
Of which purchased intangible assets	4,113	3,275
Of which capitalised payroll	4,175	2,873
Write-off	-22	-348
Reclassification*	-	-1
Cost at end of year	**23,268**	**15,002**
Amortisation at beginning of year	-2,621	-1,731
Amortisation charge for the year	-1,415	-951
Write-off	22	61
Amortisation at end of year	**-4,014**	**-2,621**
Carrying amount at beginning of year	12,381	7,472
Carrying amount at end of year	**19,254**	**12,381**

The Group has substantially increased its investments in the information and banking technology solution called Nest, the first stage of which was implemented in 2017 in Finland and second in 2018 in Sweden. In 2019, Nest has been deployed in Lithuania, Latvia and Estonia. The purchases also include the capitalised payroll and payroll-related costs for employees who were directly associated with the Nest development of 4,175 thousand euros (2018: 2,873 thousand euros), see note 21. The carrying amount of Nest as at 31 December 2019 was 18,429 thousand euros (31 December 2018: 11,814 thousand euros).

NOTE 13. LOANS FROM CENTRAL BANKS

In December 2019, the Group got financing from ECB's Targeted Long Term Refinancing Operations (TLTRO-III) in amount of 23,000 thousand euros with initial maturity of 3 years and which is secured by a portion of debt securities.

The targeted longer-term refinancing operations (TLTROs) are Eurosystem operations that provide financing to credit institutions. By offering banks long-term funding at attractive conditions they preserve favourable borrowing conditions for banks and stimulate bank lending to the real economy. The third TLTRO programme consists of a series of seven targeted longer-term refinancing operations, each with a maturity of three years, starting in September 2019 at a quarterly frequency. Borrowing rates in these operations can be as low as the average interest rate on the deposit facility prevailing over the life of the operation.

(In thousands of euros)

NOTE 14. DEPOSITS FROM CUSTOMERS

As at 31 December	2019	2018
Term deposits	**393,020**	**393,020**
Term deposits by customer type		
Individuals	380,321	379,843
Legal persons	12,517	13,177
Term deposits by currency		
EUR (euro)	339,857	337,040
SEK (Swedish kronor)	52,981	55,980
Term deposits by maturity		
Maturing within 1 months	20,658	15,120
Maturing between 1 and 6 months	58,158	71,274
Maturing between 6 and 12 months	92,137	111,408
Maturing between 12 and 18 months	34,535	34,716
Maturing between 18 and 24 months	59,481	50,735
Maturing between 24 and 36 months	57,909	57,803
Maturing between 36 and 48 months	27,319	21,016
Maturing between 48 and 60 months	12,278	9,070
Maturing in over 60 months	30,363	21,878
Average deposit amount	24	24
Weighted average interest rate	1.5%	1.6%
Weighted average duration until maturity (months)	21.2	20.5
Weighted average total contract term (months)	40.7	36.1

Annual interest rates of deposits offered to customers as at 31 December 2019

Interest rates of deposits offered to customers depend on the country as well as the deposit term, currency and amount, and interest payment method. Deposit terms range from 1 month to 10 years. Respective interest rates range from 0.3% to 2.3% per year (2018: same).

Deposits with the shortest term of 1 month are offered in Estonia, Latvia, Finland, Austria and Germany. In Sweden, the shortest term for deposits is 6 months and in the Netherlands 12 months. The minimum deposit amount is 500 euros or 10,000 Swedish krona.

(In thousands of euros)

NOTE 15. OTHER LIABILITIES

As at 31 December	2019	2018
Received surplus payments	4,188	1,946
Payables to employees	1,619	1,510
Supplier payables	778	1,131
Other payables	533	610
Total other liabilities	**7,118**	**5,197**

Received surplus payments include surplus repayments of loans by customers that are paid prematurely and not yet matched to particular loan contracts due to uncertainty of nature of these payments.

NOTE 16. DEFERRED INCOME AND TAX LIABILITIES

As at 31 December	2019	2018
Income tax payable (note 27)	313	1,161
Other taxes payable	671	741
Prepayments from customers	2	380
Total deferred income and tax liabilities	**986**	**2,282**

NOTE 17. EQUITY

Share capital

Bigbank AS is a limited company, whose minimum and maximum authorised share capital amount to 5,113 thousand euros and 12,782 thousand euros respectively. Share capital as at 31 December 2019 and 31 December 2018 consists of 80,000 fully paid in ordinary shares with a par value of one hundred euros each. Each share carries one vote at meetings of the company, granting the holder the right to participate in the management of the company, the distribution of profits and the distribution of residual assets on the dissolution of the company.

Statutory capital reserve

The capital reserve is established in accordance with the Estonian Commercial Code. Under the latter, the capital reserve is established using annual net profit transfers. Each year, the parent company has to transfer at least one twentieth of net profit for the year to the capital reserve until the reserve amounts to one tenth of share capital. The capital reserve may be used for covering losses and increasing share capital. The capital reserve may not be used for making distributions to shareholders.

(In thousands of euros)

Other reserves

Other reserves comprise:

- Exchange differences on translating foreign operations. This item comprises foreign currency differences arising from the translation of the financial statements of the Group's foreign operations that use functional currencies other than the Group's functional currency.
- Asset revaluation reserve comprises the increase in the carrying value of land and buildings classified as *Property and equipment* as a result of revaluation.
- Fair value changes of debt instruments measured at FVOCI comprises the change in fair value of the debt instruments at fair value through other comprehensive income.

As at 31 December	2019	Change	2018	Change	2017
Exchange differences on translating foreign operations	874	181	693	322	371
Asset revaluation reserve	545	241	304	-	304
Fair value changes of debt instruments measured at FVOCI	-187	4	-191	-191	-
Total other reserves	**1,232**	**426**	**806**	**131**	**675**

Unrestricted equity

At 31 December 2019, the Group's unrestricted equity amounted to 131,021 thousand euros (31 December 2018: 111,568 thousand euros).

Dividends

In 2019 and 2018, the company made the following dividend distributions:

- 2019: 62.50 euros per share, i.e. 5,000 thousand euros in aggregate; and
- 2018: 62.50 euros per share, i.e. 5,000 thousand euros in aggregate.

NOTE 18. INTEREST INCOME

	2019	2018
Interest income on loans to customers	66,593	66,112
Interest income on debt instruments	277	239
Interest income on deposits	17	6
Other interest income	63	29
Total interest income	**66,950**	**66,386**

NOTE 19. INTEREST EXPENSE

	2019	2018
Interest expense on deposits	5,956	5,712
Interest expense on bonds	334	334
Interest expense on lease liabilities	30	-
Other interest expense	70	53
Total interest expense	**6,390**	**6,099**

(In thousands of euros)

NOTE 20. OTHER INCOME

	2019	2018
Income from debt recovery proceedings*	771	1,647
Miscellaneous income	419	428
Total other income	**1,190**	**2,075**

* Income received for reimbursement of recovery and enforcement costs and legal fees, etc.

NOTE 21. SALARIES AND ASSOCIATED CHARGES

	2019	2018
Salaries	11,581	11,260
Social security costs	2,994	3,473
Employee health costs and fringe benefits including associated taxes	342	356
Total salaries and associated charges	**14,917**	**15,089**

Total salaries and associated charges were higher by 4,175 thousand euros together with capitalised payroll and payroll-related costs associated with the Nest development in 2019, see note 12. Annual average number of employees working full time was 399 (2018: 418).

NOTE 22. OTHER OPERATING EXPENSES

	2019	2018
Marketing expenses	6,938	6,668
Rental charges payable under operating leases	-	917
Short-term leases	118	-
Office and other similar administrative expenses	472	579
Other personnel-related expenses	1,119	1,177
Software licensing and other information technology costs	1,336	1,426
Other services	386	512
Postal supplies and charges	467	276
Telephone and other communications expenses	499	590
Miscellaneous operating expenses	387	878
Total other operating expenses	**11,722**	**13,023**

(In thousands of euros)

NOTE 23. OTHER EXPENSES

	2019	2018
Expenses related to registry inquires	1,116	1,294
Expenses related to enforcement proceedings	406	440
Legal regulation charges	629	588
Expenses from investment properties	53	52
Miscellaneous expenses	387	381
Total other expenses	**2,591**	**2,755**

NOTE 24. OPERATING LEASES

The Group as a lessee

The Group adopted standard IFRS 16 on 1 January 2019 that eliminates the classification of leases into operating and finance leases that was provided in IAS 17 and, instead, introduces a single accounting model for lessees. As a result adopting IFRS 16, the Group recognised right of use asset of office premises in amount of 2,776 thousand euros against a corresponding lease liability on 1 January 2019 and instead operating lease expense in 2019, the depreciation charge of 733 thousand euros and interest expense on leased ROA liability of 30 thousand euros was recognised, see notes 1, 10 and 19. For changes in lease liabilities see note 28.

The Group has lease contracts for office premises. Lease terms mostly fall between 3 and 10 years. Leases of office premises can be cancelled by giving one month's to 10 years' notice. Fixed-term lease contracts can be extended on market terms. The Group also has certain leases of office premises with terms of 12 months or less and leases of office equipment of low value. The Group applies the short-term lease and lease of low-value assets recognition exemptions to these leases. Expenses on short-term leases included in *Other operating expenses* were 118 thousand euros in 2019.

(In thousands of euros)

The Group as a lessor

Minimum non-cancellable operating lease rentals receivable in subsequent periods

As at 31 December	2019	2018
Up to 1 year	36	42
1 to 5 years	45	96

For the rental income and operating expenses see note 11.

NOTE 25. ASSETS PLEDGED AS COLLATERAL

Asset encumbrance arises from collateral pledged against secured funding and other collateralised obligations. At 31 December 2019, total 25,767 thousand euros (31 December 2018: 0) of debt securities were pledged as a collateral in order to get targeted long term refinancing operations (TLTRO) low cost funding through Eurosystem's open market operations.

NOTE 26. CONTINGENT LIABILITIES

At 31 December 2019, the unused portions of the Group's credit lines totalled 21,001 thousand euros (31 December 2018: 18,430 thousand euros).

Contingent income tax liabilities

At 31 December 2019, the Group's undistributed profits totalled 131,021 thousand euros (31 December 2018: 111,568 thousand euros).

Under the Estonian Income Tax Act, in 2019 profit distributions, including dividend distributions, were subject to income tax calculated as 20/80 of the net distribution. The maximum income tax liability that could arise if all of the undistributed profits were distributed as dividends amounts to 26,404 thousand euros. Thus, the maximum amount that could be distributed as the net dividend is 104,817 thousand euros.
The income tax payable on dividends is calculated by reducing the tax base by the profits attributed to foreign permanent establishments (branches) and reducing the tax payable by advance payments of income tax that credit institutions are required to make in Estonia. The Groups actual expected maximum income tax liability that could arise if all of the undistributed profits were distributed as dividends amounts to 12,836 thousand euros and the maximum amount that could be distributed as the net dividend is 118,185 thousand euros.

The maximum contingent income tax liability has been calculated under the assumption that the net dividend and the dividend tax expense reported in the income statement for 2019 cannot exceed total distributable profits as at 31 December 2019.

NOTE 27. INCOME TAX EXPENSE

Income tax expense

	2019	2018
Current income tax expense	1,753	1,645

(In thousands of euros)

Current tax expense has been calculated on net profit earned in Lithuania, Finland and Sweden and it includes advance payments of income tax that credit institutions are required to make in Estonia.

There are no income tax consequences attached to the payment of dividends in either 2019 or 2018 by the Group to its shareholders.

Reconciliation of accounting profit and income tax expense

	2019	2018
Consolidated profit before tax	26,206	19,171
The parent company's domestic tax	521	-
Effect of tax rates in foreign jurisdictions	1,232	1,580
Effect of income tax of previous years	-	65
Income tax expense reported in statement of comprehensive income	**1,753**	**1,645**

NOTE 28. ADDITIONAL CASH FLOW INFORMATION

Changes in liabilities arising from financing activities in 2019

	Subordinated notes	Loans from central banks	Lease liability
Opening balance	4,960	-	2,776*
Cash flow items:			
Issuances	-	23,000	-
Repayment	-330	-	-723
Non-cash flow items:			
Movement in accrued interest and revaluation	335	-	46
Effect of movements in exchange rates	-	-	-3
Balance at 31 December 2019	**4,965**	**23,000**	**2,096**

* Lease liability was recognised on 1 January 2019, see note 24.

Changes in liabilities arising from financing activities in 2019

	Subordinated notes
Opening balance	4 977
Cash flow items:	
Repayment	-330
Non-cash flow items:	
Movement in accrued interest	313
Balance at 31 December 2018	**4 960**

NOTE 29. RELATED PARTIES

For the purposes of these financial statements, parties are related if one controls the other or exerts significant influence on the other's business decisions. Related parties include:

- shareholders of Bigbank AS;
- members of Group companies' management and supervisory boards;
- close family members of the above;
- companies connected with the above persons, except where the persons cannot exert significant influence on the company's business decisions.

In 2019, the remuneration of the members of the Group's management and supervisory boards including relevant taxes amounted to 1,069 thousand euros (2018: 951 thousand euros) and 70 thousand euros (2018: 70 thousand euros) respectively.

As at 31 December 2019, the Group had a claim to related parties of 44 thousand euros (*Loans to customer*) (31 December 2018: 37 thousand euros), the interest income on that claim amounted to 2 thousand euros in 2019 (2018: 2 thousand euros). Loans granted to related parties are issued at market conditions.

The Group is financing Group subsidiaries and branches with long term loans. Such loans are eliminated in consolidated financial statements.

NOTE 30. FAIR VALUES OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Management believes that the fair values of the assets and liabilities reported in the consolidated statement of financial position as at 31 December 2019 and at 31 December 2018 do not differ significantly from their carrying amounts.

(In thousands of euros)

	Carrying amount		Fair value	
Financial assets as at 31 December	**2019**	**2018**	**2019**	**2018**
Cash and balances at central banks (note 4)	32,855	29,691	32,855	29,691
Cash and balances at banks (note 4)	21,085	36,261	21,085	36,261
Debt instruments at fair value through other comprehensive income (note 5)	31,390	13,484	31,390	13,484
Loans to customers (note 6,7)	459,656	427,964	459,656	427,964
Other financial receivables (note 8)	1,738	1,484	1,738	1,484
Total financial assets	**546,724**	**508,884**	**546,724**	**508,884**

	Carrying amount		Fair value	
Financial liabilities as at 31 December	**2019**	**2018**	**2019**	**2018**
Loans from central banks (note 13)	23,000	-	23,000	-
Deposits from customers (note 14)	392,838	393,020	392,838	393,020
Subordinated notes	4,965	4,960	4,965	4,960
Other financial liabilities (note 15)	9,214	5,197	9,214	5,197
Total	**407,017**	**403,177**	**407,017**	**403,177**

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1);
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2);
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

(In thousands of euros)

Fair value hierarchy as at 31 December 2019

	Level 1	Level 2	Level 3	Total
Assets measured at fair value				
Debt instruments at fair value through other comprehensive income (note 5)	31,390	-	-	31,390
Land and buildings (note 10)	-	-	1,580	1,580
Investment properties (note 11)	-	-	1,781	1,781
Assets for which fair values are disclosed				
Loans to customers (note 6,7)	-	-	459,656	459,656
Other financial receivables (note 8)	-	-	1,738	1,738
Total assets	**31,390**	**-**	**464,755**	**496,145**
Liabilities measured at fair value				
Liabilities for which fair values are disclosed				
Loans from central banks (note 13)	-	-	23,000	23,000
Deposits from customers (note 14)	-	-	392,838	392,838
Subordinated notes	-	-	4,965	4,965
Lease liability	-	-	2,096	2,096
Other financial liabilities (note 15)	-	-	7,118	7,118
Total liabilities	**-**	**-**	**430,017**	**430,017**

Fair value hierarchy as at 31 December 2018

	Level 1	Level 2	Level 3	Total
Assets measured at fair value				
Debt instruments at fair value through other comprehensive income (note 5)	13,484	-	-	13,484
Land and buildings (note 10)	-	-	1,397	1,397
Investment properties (note 11)	-	-	1,866	1,866
Assets for which fair values are disclosed				
Loans to customers (note 6,7)	-	-	427,964	427,964
Other financial receivables (note 8)	-	-	1,484	1,484
Total assets	**13,484**	**-**	**432,711**	**446,195**
Liabilities measured at fair value				
Liabilities for which fair values are disclosed				
Deposits from customers (note 14)	-	-	393,020	393,020
Subordinated notes	-	-	4,960	4,960
Other financial liabilities (note 15)	-	-	5,197	5,197
Total liabilities	**-**	**-**	**403,177**	**403,177**

There have been no transfers between Level 1 and Level 2 during 2019 and 2018.

The *Level 3 loans to customers* that amounts to 459,656 thousand euros are measured at amortised cost using the effective interest rate method less any loss allowances. For fair valuation purpose the estimated cash-flows have been discounted at the prevailing market interest rates, the result being not materially different from that recognised under the amortised cost method using effective interest rate.

The Group's accounting policy on loans to customer is discussed in note 1 (section *Financial assets*) and 3. Management estimates that the selected accounting policy on loans reflects the fair value of loans to customers.

The Level 3 *land and buildings* that amounts to 1,580 thousand euros consists of real estate in Tallinn (see note 10).

The properties in Tallinn are revalued using the income approach and market approach. The market approach means that valuations performed by the valuer are based on active market prices, significantly adjusted for differences in the nature, location or condition of the specific property. For valuation of property in Tallinn, for prior year the valuer has taken as basis the prices per square metre of residential space in Tallinn city that were in the range of 3,020 – 3,102 euros.

Under the discounted cash flow method, fair value is estimated using assumptions regarding the benefits and liabilities of ownership over the asset's life including an exit or terminal value. This method involves the projection of a series of cash flows on a real property interest. To this projected cash flow series, a market-derived discount rate is applied to establish the present value of the income stream associated with the asset. The estimated rental value per square meter per month is 11 euros, the rent growth 2%, long-term vacancy rate 5%, and vacancy rate for the first year 30% and discount rate 9% for commercial property in Tallinn.

Valuations are performed with sufficient frequency to ensure that the fair value of a revalued asset does not differ materially from its carrying amount (see note 1, the section Property and equipment and *Fair value measurement*, and note 2). Management has assessed that the fair value has changed and therefore the revaluation was made in year 2019.

The Level 3 *investment properties* that amount to 1,781 thousand euros consist of real estate in Tartu and also plots, houses and apartments originally pledged by customers as loan collateral and later bought by the Group through auctions (see note 11) are measured at the fair value in the financial statements and valuations are performed by the management using market approach.

The investment property in Tartu is valued using the cost model (residual value method) based on the highest and best use of the property. The residual value method takes into account the profit that can be achieved on a development if the existing property would be developed and sold as private flats. Following inputs were used for prior year valuation of the properties in Tartu: price per square metre of flats in Tartu old town 2,500 euros and development costs per square metre 865 euros.

Valuations of investment property are performed at each reporting date to make sure that the assets are measured at fair value and not at close-to-fair value at the reporting date (see note 1, the section *Investment properties* and *Fair value measurement*, and note 2). The Group engaged an independent valuation expert to assess the fair values of its investment properties, land and buildings at 31 December 2019 and based on the valuation, the assets were remeasured in 2019.

NOTE 31. EARNINGS PER SHARE

	2019	2018
Net profit for the year, in thousands of euros	24,453	17,526
Number of shares at beginning of year	80,000	80,000
Number of shares at end of year	80,000	80,000
Weighted average number of ordinary shares outstanding	80,000	80,000
Earnings per share, in euros	**306**	**219**

At the end of 2019 and 2018 the Group did not have any potential dilutive ordinary shares. Therefore, diluted earnings per share equal basic earnings per share.

NOTE 32. UNCONSOLIDATED STATEMENTS OF PARENT COMPANY AS A SEPARATE ENTITY

The parent company's unconsolidated financial statements have been prepared in accordance with the Accounting Act of the Republic of Estonia, and do not constitute parent company's separate financial statements in the meaning of IAS 27 "Separate financial statements".

(In thousands of euros)

Statement of financial position

As at 31 December	2019	2018
Assets		
Cash and balances at central banks	32,855	29,691
Cash balances at banks	20,328	35,748
Debt instruments at fair value through other comprehensive income	31,390	13,484
Loans to customers	459,656	427,964
Receivables from subsidiaries	864	864
Investments in subsidiaries	579	579
Other receivables	1,731	1,479
Prepayments	1,263	1,732
Property and equipment	3,963	2,609
Investment properties	98	264
Intangible assets	19,254	12,381
Total assets	**571,981**	**526,795**
Liabilities		
Loans from central banks	23,000	-
Deposits from customers	392,838	393,019
Liabilities to subsidiaries	1,792	1,870
Subordinated notes	4,965	4,960
Lease liability	2,070	-
Provisions	2,137	1,884
Other liabilities	7,095	5,172
Deferred income and tax liabilities	959	2,247
Total liabilities	**434,856**	**409,152**
Equity		
Paid-in share capital	8,000	8,000
Capital reserve	800	800
Other reserves	997	770
Retained earnings	127,328	108,073
Total equity	**137,125**	**117,643**
Total liabilities and equity	**571,981**	**526,795**

(In thousands of euros)

Statement of comprehensive income

As at 31 December	2019	2018
Interest income	66,965	66,408
Interest expense	-6,423	-6,135
Net interest income	**60,542**	**60,273**
Net fee and commission income	4,047	3,261
Net loss on exchange differences	-194	-315
Net loss on derecognition of non-financial assets	-14	-299
Other income	1,068	1,915
Total income	**65,449**	**64,835**
Salaries and associated charges	-14,526	-14,711
Other operating expenses	-11,765	-13,054
Depreciation and amortisation expense	-3,238	-2,015
Provision expenses	-304	-1,261
Net impairment losses on loans and financial investments	-6,737	-11,415
Other expenses	-2,874	-3,033
Total expenses	**-39,444**	**-45,489**
Profit before income tax	**26,005**	**19,346**
Income tax	-1,750	-1,643
Profit for the year	**24,255**	**17,703**
Other comprehensive income/expense		
Other comprehensive income to be reclassified to profit or loss in subsequent periods:		
Exchange differences on translating foreign operations	181	322
Changes in the fair value of debt instruments at FVOCI	4	-191
Net other comprehensive income to be reclassified to profit or loss in subsequent periods	**185**	**131**
Other comprehensive income to be reclassified to profit or loss in subsequent periods:		
Revaluation of land and buildings	42	-
Net other comprehensive income not to be reclassified to profit or loss in subsequent periods	**42**	**-**
Other comprehensive income for the year	**227**	**131**
Total comprehensive income for the year	**24,482**	**17,834**

(In thousands of euros)

Statement of cash flows

As at 31 December	2019	2018
Cash flows from operating activities		
Interest received	60,422	60,403
Interest paid	-5,621	-4,883
Salary and other operating expenses paid	-28,912	-30,674
Other income and fees received	6,398	8,083
Other expenses and fees paid	-4,127	-5,441
Recoveries of receivables previously written off	25,408	36,346
Loans granted	-266,377	-276,236
Repayment of loans granted	209,133	180,825
Change in mandatory reserves with central banks and related interest receivables	371	-269
Proceeds from customer deposits	94,327	135,910
Paid on redemption of deposits	-91,662	-75,146
Income tax paid	-2,004	-2,178
Effect of movements in exchange rates	-112	-186
Net cash used in / from operating activities	**-2,756**	**26,554**
Cash flows from investing activities		
Acquisition of property and equipment and intangible assets	-8,624	-7,426
Proceeds from sale of property and equipment	92	29
Proceeds from sale of investment properties	119	23
Acquisition of financial instruments	-21,824	-3,025
Proceeds from redemption of financial instruments	4,177	741
Net cash used in investing activities	**-26,060**	**-9,658**
Cash flows from financing activities		
Interest paid on subordinated bonds	-330	-330
Received loans from central bank	23,000	-
Repayment of loans from companies	-74	-
Payment of principal portion of lease liabilities	-711	-
Dividends paid	-5,000	-5,000
Net cash from / used in financing activities	**16,885**	**-5,330**
Effect of exchange rate fluctuations	47	-243
Decrease/increase in cash and cash equivalents	**-11,885**	**11,323**
Cash and cash equivalents at beginning of period	64,109	52,786
Cash and cash equivalents at end of period	**52,224**	**64,109**

(In thousands of euros)

Cash and cash equivalents

As at 31 December	2019	2018
Demand and overnight deposits with banks	17,627	19,221
Term deposits with banks	2,701	16,527
Surplus on mandatory reserves with central banks	31,896	28,361
Total	**52,224**	**64,109**

Statement of changes in equity

	Share capital	Statutory capital reserve	Other reserves	Retained earnings	Total
Balance at 1 January 2018	**8,000**	**800**	**639**	**100,099**	**109,538**
Changes on initial adoption of IFRS 9	-	-	-	-4,729	-4,729
Restated balance at 1 January 2018	8,000	800	639	95,370	104,809
Profit for the year	-	-	-	17,703	17,703
Other comprehensive income					
Exchange differences on translating foreign operations	-	-	322	-	322
Net change in fair value of debt instrument at FVOCI	-	-	-191	-	-191
Total other comprehensive income	**-**	**-**	**131**	**-**	**131**
Total comprehensive income for the year	**-**	**-**	**131**	**17,703**	**17,834**
Dividend distribution	-	-	-	-5,000	-5,000
Total transactions with shareholders	**-**	**-**	**-**	**-5,000**	**-5,000**
Balance at 31 December 2018	**8,000**	**800**	**770**	**108,073**	**117,643**
Balance at 1 January 2019	**8,000**	**800**	**770**	**108,073**	**117,643**
Profit for the year	-	-	-	24,255	24,255
Other comprehensive income					
Exchange differences on translating foreign operations	-	-	181	-	181
Net change in fair value of debt instrument at FVOCI	-	-	4	-	4
Revaluation of land and buildings	-	-	42	-	42
Total other comprehensive income	**-**	**-**	**227**	**-**	**227**
Total comprehensive income for the year	**-**	**-**	**227**	**24,255**	**24,482**
Dividend distribution	-	-	-	-5,000	-5,000
Total transactions with shareholders	**-**	**-**	**-**	**-5,000**	**-5,000**
Balance at 31 December 2019	**8,000**	**800**	**997**	**127,328**	**137,125**

(In thousands of euros)

As at 31 December	2019	2018
Unconsolidated equity at end of period	**137,125**	**117,643**
Investments in subsidiaries:	-579	
Carrying value	-579	-579
Carrying value under the equity method	4,507	4,110
Adjusted unconsolidated equity at end of period	**141,053**	**121,174**

Signatures

The management board has prepared the review of operations and financial statements of Bigbank AS for 2019.

Martin Länts		
Chairman of the Management Board	28 February 2020	*[signed digitally]*
Sven Raba		
Member of the Management Board	28 February 2020	*[signed digitally]*
Mart Veskimägi		
Member of the Management Board	28 February 2020	*[signed digitally]*
Argo Kiltsmann		
Member of the Management Board	28 February 2020	*[signed digitally]*

Simplicity

We aim at simplicity in our solutions and in customer experience.

Keiu Kalaus
Head of WOW Support Services

Independent Auditor’s Report

Building a better working world

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Translation of the Estonian Original

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Bigbank AS

Opinion

We have audited the consolidated financial statements of Bigbank AS and its subsidiaries (the Group), which comprise the consolidated statement of financial position as at 31 December 2019, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2019, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the European Union.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (Estonia). Our responsibilities under those standards are further described in the “Auditor’s responsibilities for the audit of the financial statements” section of our report. We are independent of the Group in accordance with the Code of Ethics for Professional Accountants (Estonia), and we have fulfilled our other ethical responsibilities in accordance with the requirements of the code of ethics.

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

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor’s responsibilities for the audit of the consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying financial statements.

Key Audit Matter	*How our audit addressed the key audit matter*
Impairment of loans to customers As disclosed in Note 6 *Loans to customers* to the consolidated financial statements, the carrying amount of loan receivables as at 31 December 2019 amounts to EUR 459 656 thousand which corresponds to 80% of the Group's assets. Impairment of loans is a subjective area due to the level of judgement applied by the management in determining the extent of credit losses which is dependent on the credit risk related to such loans and receivables. Such an assessment is inherently uncertain, involving forecasting of future macroeconomic conditions in a number of scenarios as well as an assessment of the credit standing of the exposures by employing models based on a series of historical data and assumptions and an assessment of valuation and timing of recovery of collaterals. The use of different modelling techniques and assumptions around the calculation of the expected credit losses could produce significantly different estimates of loss allowance. These models require the significant judgment of management regarding appropriate segmentation, the identification of significant changes in credit risk, the inclusion of forward-looking elements as well as the application of management overlays to reflect on circumstances beyond the modelling capabilities. The Group is applying the expected credit loss model as required by IFRS 9. The Group's impairment allowance policy is presented in the accounting policies section in Note 1 sub-section *Financial assets impairment* to the consolidated financial statements. Critical accounting estimates and judgments are set out in Note 2 *Significant accounting estimates and assumptions* to the consolidated financial statements. Given the complexity and judgements related particularly to the calculation of expected credit losses, the impairment allowance for loans to customers is considered a key audit matter.	Our audit procedures included, amongst others: • We gained an understanding and tested the key controls over the loan issuance, booking and monitoring and loan impairment provisioning process. We obtained and read the Group's Impairment provisioning policy that is based on the IFRS 9 and involved our internal IFRS 9 specialists to assess its compliance with the requirements of IFRS 9. • We assessed the Group's methodology regarding the identification of impairment indications and determination by the management of the expected credit losses, including governance over the determination of key judgements. This included the determination of probability weighted macroeconomic scenarios, staging criteria and the credit risk parameters models. • For expected credit losses for loans assessed in stage 1 or stage 2 we tested the models used for calculation of probability of default and loss given default, by assessing their key assumptions and then reimplementation with the assistance of our internal IFRS9 specialist. • We tested the mathematical accuracy of the impairment allowance calculations. On sample basis we tested the data flow in the models and verified the correctness of parameters subject to estimation by tracing them to the original source documents for the purposes of testing information prepared by the entity (IPE). • For the loss allowance of impaired loans assessed on an individual basis (stage 3), our evaluation was focused on the loans with the most significant potential impact on the consolidated and separate financial statements. We understood the developments at the borrower and the basis of measuring the expected credit loss considering the key judgments given the borrowers' circumstances. We also re-performed management's impairment calculation on a sample basis. We assessed the key assumptions underlying the impairment identification and quantification such as estimated future cash flows, including the realizable value of collaterals and estimates of recovery on default. • For expected credit loss for loans calculated on a collective basis (stages 1 and 2) we analyzed the Group's methodology, inputs and assumptions used. We also tested the completeness and accuracy of the underlying loan information used in the expected credit loss models by agreeing details to the Group's source systems as well as re-performing the calculation of the expected credit loss. For the key assumptions in the model, we evaluated evidence provided by the management. • We performed analytical procedures, such as a comparison of loan loss impairment allowance balances to industry levels, comparison to prior year, movements between stages etc. • Finally, we assessed the completeness of the related disclosures contained in Note 7 *Loss allowances for loans receivables from customers*, 6 *Loans to customers and* 2 *significant accounting estimates and assumptions* to the consolidated financial statements.

Other information

Management is responsible for the other information. Other information consists of Bigbank group at a glance, Letter of the chairman of the management board, Review of the operations, Social responsibility and sustainability report and Corporate Governance Report, but does not consist of the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

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

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the International Financial Reporting Standards as adopted by the European Union, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (Estonia) 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 financial statements.

As part of an audit in accordance with International Standards on Auditing (Estonia), we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the 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 financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We are also required to provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

Other requirements of the auditor's report in accordance with Regulation (EU) No 537/2014 of the European Parliament and of the Council.

Appointment and approval of the auditor

In accordance with the decision made by the shareholder we have been chosen to carry out the audit of Group's consolidated financial statements the first time in 2013. Our appointment to carry out the audit of Group's consolidated financial statements in accordance with the decision made by shareholder has been renewed annually and the period of total uninterrupted engagement is 7 years.

Consistence with Additional Report to Supervisory Board and Audit Committee

Our audit opinion on the annual financial statements expressed herein is consistent with the additional report to the Supervisory Board and Audit Committee of the Group, which we issued in accordance with Article 11 of the Regulation (EU) No. 537/2014 on the same date as the date of this report.

Non audit services

We confirm that in light of our knowledge and belief, services provided to the Group are consistent with the requirements of the law and regulations and do not comprise non-audit services referred to in Article 5(1) of the Regulation (EU) No 537/2014 of the European Parliament and of the Council.

In addition to statutory audit services and services disclosed in the financial statements, no other services were provided by us to the Company and its controlled undertakings.

The responsible certified auditor on the audit resulting in this independent auditors' report is Olesia Abramova.

Tallinn, 28 February 2020

/signed digitally/

Olesia Abramova
Authorised Auditor's number 561
Ernst & Young Baltic AS
Audit Company's Registration number 58

Profit allocation proposal

The total consolidated distributable profits of Bigbank AS as at 31 December 2019 comprise of:

Earnings retained in prior years as at 31 December 2019	106,568	thousand euros
Net profit for 2019	24,453	thousand euros
Total distributable profits as at 31 December 2019	**131,021**	**thousand euros**

The management board of Bigbank AS proposes to the general meeting to distribute the profit for the reporting period as follows:

1. Dividend distribution (75.00 euros per share)	6,000	thousand euros;
2. Transfer to retained earnings	18,453	thousand euros;
Balance of retained earnings after allocations	**125,021**	**thousand euros.**

Martin Länts

Chairman of the Management Board 28 February 2020 *[signed digitally]*

Sven Raba

Member of the Management Board 28 February 2020 *[signed digitally]*

Mart Veskimägi

Member of the Management Board 28 February 2020 *[signed digitally]*

Argo Kiltsmann

Member of the Management Board 28 February 2020 *[signed digitally]*