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REPORT

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BANCA
SISTEMA
CONTEMPORARY BANK

SEPTEMBER 2018

Banca SISTEMA Group

**INTERIM CONSOLIDATED
FINANCIAL REPORT AT
30 SEPTEMBER 2018**

BANCA
S I S T E M A

CONTENTS

DIRECTORS' REPORT	5
COMPOSITION OF THE PARENT'S MANAGEMENT BODIES	6
COMPOSITION OF THE INTERNAL COMMITTEES	7
FINANCIAL HIGHLIGHTS AT 30 SEPTEMBER 2018	8
SIGNIFICANT EVENTS DURING THE REPORTING PERIOD	9
FACTORING	11
SALARY-BACKED LOANS	13
FUNDING ACTIVITIES	14
INCOME STATEMENT RESULTS	16
THE MAIN STATEMENT OF FINANCIAL POSITION AGGREGATES	21
CAPITAL ADEQUACY	27
OTHER INFORMATION	28
RELATED PARTY TRANSACTIONS	28
ATYPICAL OR UNUSUAL TRANSACTIONS	28
SIGNIFICANT EVENTS AFTER THE REPORTING DATE	28
BUSINESS OUTLOOK AND MAIN RISKS AND UNCERTAINTIES	29
CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS	31
STATEMENT OF FINANCIAL POSITION	32
INCOME STATEMENT	34
STATEMENT OF COMPREHENSIVE INCOME	35
STATEMENTS OF CHANGES IN EQUITY	36
STATEMENT OF CASH FLOWS (direct method)	38
ACCOUNTING POLICIES	39
GENERAL BASIS OF PREPARATION	40
STATEMENT OF THE MANAGER IN CHARGE OF FINANCIAL REPORTING	57
ANNEX	59

DIRECTORS' REPORT

COMPOSITION OF THE PARENT'S MANAGEMENT BODIES

Board of Directors

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

Board of Statutory Auditors

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

Independent Auditors

KPMG S.p.A.

Manager in charge of financial reporting

Mr. Alexander Muz

¹ Meets the independence requirement pursuant to art. 147-ter, paragraph 4, and art. 148, paragraph 3 of Legislative Decree no. 58 of 24 February 1998, but it also does not meet the provisions of art. 3, criteria for application 3.c.1.b and 3.c.2 of the Self-regulation Corporate Governance Code issued by Borsa Italiana.

² Meets the independence requirement pursuant to art. 147-ter, paragraph 4, and art. 148, paragraph 3 of Legislative Decree no. 58 of 24 February 1998, but it also does not meet the provisions of art. 3, criteria for application 3.c.1.b and 3.c.2 of the Self-regulation Corporate Governance Code issued by Borsa Italiana.

³ Director co-opted by the Board of Directors on 13 July 2018 replacing Mr. Pugelli who tendered his resignation from the position with effect from 30 June 2018.

⁴ Appointed as a Standing Auditor at the Shareholders' Meeting on 14 December 2017 and shall remain in office until the end of the Board of Statutory Auditors' term.

⁵ On 14 December 2017, following the appointment of the new Standing Auditor, he was once again appointed Alternate Auditor at the Shareholders' Meeting and shall remain in office until the end of the Board of Statutory Auditors' term.

COMPOSITION OF THE INTERNAL COMMITTEES

Internal Control and Risk Management Committee

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

Appointments Committee

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

Remuneration Committee

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

Ethics Committee

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

Supervisory Body

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

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

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

FINANCIAL HIGHLIGHTS AT 30 SEPTEMBER 2018

Statement of financial position data (€,'000)

Total Assets		3,152,730	36.5%	■ 30 Sep 2018
		2,309,233		
Securities Portfolio		777,028	109.4%	■ 31 Dec 2017
		370,989		
Loans - Factoring		1,575,647	22.5%	■ 30 Sep 2017
		1,285,726		
Loans - Salary-backed loans and SME		642,574	15.6%	
		556,061		
Funding - Banks and REPOs		1,060,362	44.6%	
		733,156		
Funding - Term Deposits		863,393	93.1%	
		447,093		
Funding - Current Accounts		557,810	9.3%	
		510,349		

Income Statement data (€,'000)

Net interest income		53,038	-2.0%
		54,131	
Net fee and commission income		10,624	44.5%
		7,352	
Total income		64,530	3.0%
		62,638	
Personnel Expenses		(14,448)	13.1%
		(12,772)	
Other administrative expenses		(16,247)	8.6%
		(14,958)	
Pre-tax profit		29,015	-6.9%
		31,157	

Performance Indicators

Cost/income		47.8%	5.5%
		45.3%	
ROAE		17.9%	-16.7%
		21.5%	

SIGNIFICANT EVENTS DURING THE PERIOD FROM 1 JANUARY TO 30 SEPTEMBER 2018

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

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

On 09 April 2018, following the authorisations granted by the Bank of Italy, two new branches dedicated exclusively to the collateralised lending business were opened in Naples and Palermo.

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

On 23 April 2018, the shareholders’ meeting was held during which the Board of Directors’ mandate was

renewed with the appointment of nine members.

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

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

On 19 June, the Bank completed the acquisition of a 19.90% stake in the share capital of ADV Finance S.p.A. (“ADV Finance”), a registered financial intermediary (under art. 106 of the Consolidated Banking Act) that since 2010 has offered in Italy, through agents and brokers, a complete range of services related to salary- and pension-backed personal loans (CQS/CQP). The transaction, valued at € 0.6 million, is consistent with Banca Sistema’s growth objective for the CQS/CQP business outlined in the 2018-2020 Strategic Plan and is aimed at reinforcing the existing commercial partnership with ADV Finance. The agreements between the shareholders of ADV Finance and Banca Sistema provide for the possibility for the latter to increase its investment by an additional 20% within the next 24 months. On 22 June, the Board of Directors approved the start of market making activities and thus allocated € 40,000 to it for the purchase and disposal of treasury shares within the scope of the authorisation granted at the Shareholders’ Meeting of 27 April 2017 and in accordance with the terms authorised by the Bank of Italy on 13 September 2017.

The programme was suspended on 5 October 2018 to start the treasury share repurchase programme for the purpose of supporting the remuneration and incentive policies for key personnel for an overall amount not exceeding € 200,000, which was concluded on 12 October, the day on which the market making activity

programme resumed and which was terminated on 27 October 2018.

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

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

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

On 28 September 2018, the Bank signed a binding

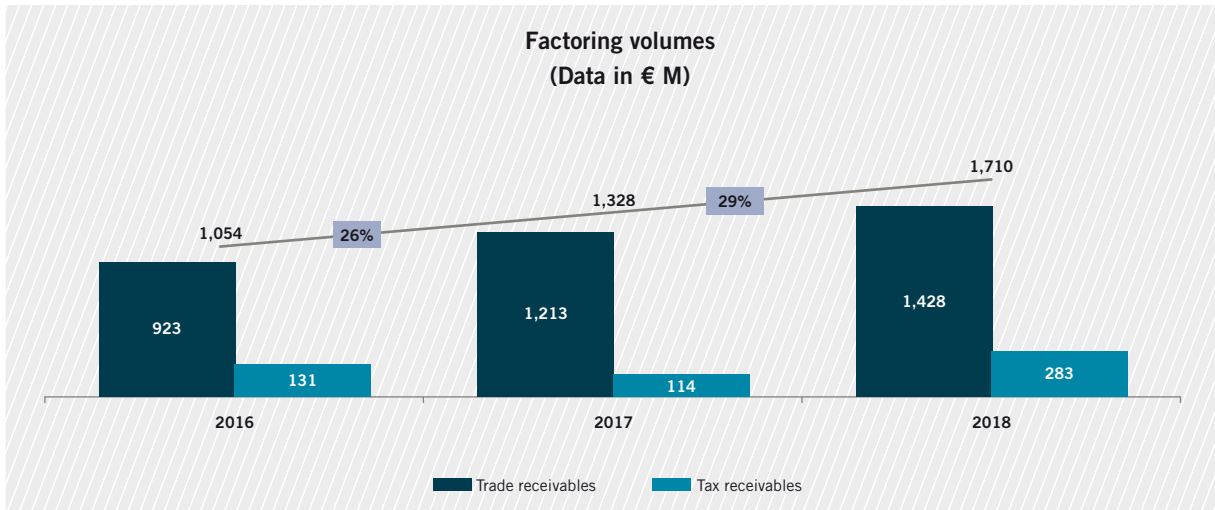
agreement for the acquisition of 100% of Atlantide S.p.A., a registered financial intermediary (under art. 106 of the Consolidated Banking Act) and active in the granting of salary- and pension-backed personal loans (CQS/CQP) since 2010. Atlantide, headquartered in Bologna, has 23 employees and provides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

The value of the transaction is € 2.4 million (equal to the shareholders' equity of Atlantide at 30 June 2018), which will be paid upon completion of the acquisition agreement; the agreement also includes a variable component to be paid upon achievement of certain objectives. All the proceeds resulting from the completion of the transaction will be used by Atlantide's current shareholders to buy Banca Sistema's shares on the open market, subject to a maintenance obligation of three years. The agreement is expected to be completed by the end of the first quarter of 2019 following the authorisation of the Supervisory Authority. The transaction had an impact of 15bps on Banca Sistema's CET1 ratio at 30 June 2018. Atlantide is slated to be merged into Banca Sistema in 2019.

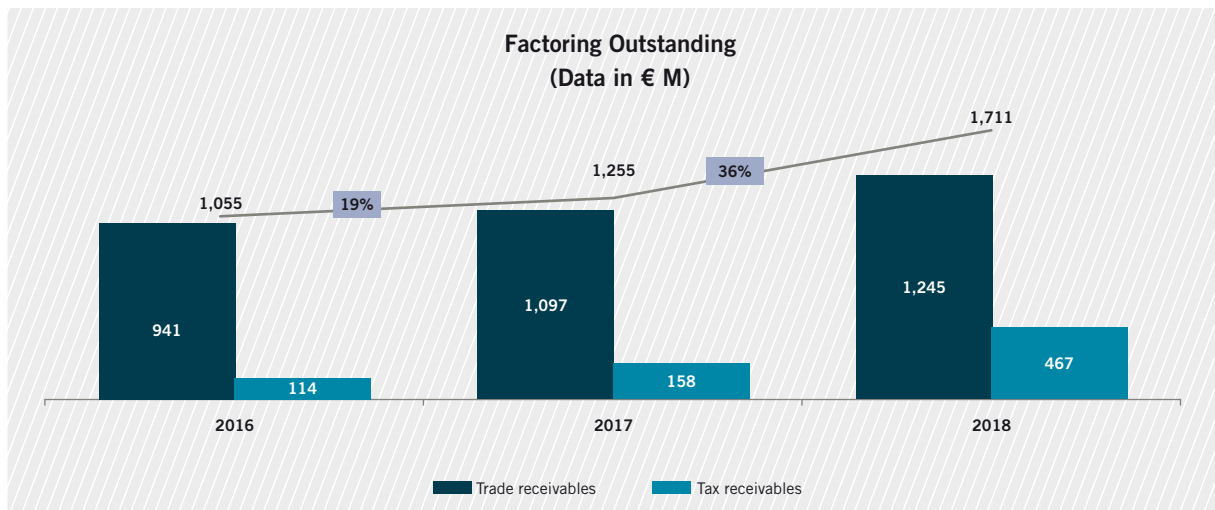
FACTORING

Banca Sistema and factoring activities

The Banca Sistema Group's total turnover as at 30 September 2017, confirming its ability to continue September 2018 was € 1,710 million, up 29% on growing year-on-year.

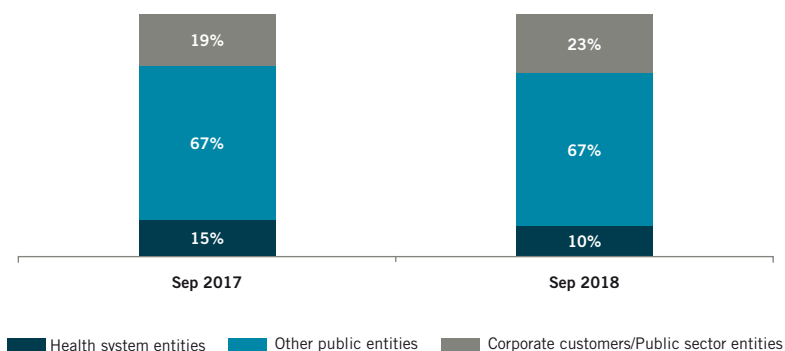


Outstanding loans as at 30 September 2018 amounted to € 1,711 million, up 36% on the € 1,255 million at 30 September 2017 mainly due to increased volumes acquired in 2018 compared to collections during the same period.



The chart below shows the ratio of debtors to the total exposure in the outstanding receivables portfolio at 30

September 2018 and 2017. The Group's core factoring business remains the Public Administration entities segment.



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

In September 2018, the external networks accounted for 29% of total turnover. The following table shows the factoring turnover by product type:

PRODUCT (amounts in millions of Euro)	30.09.2018	30.09.2017	€ CHANGE	% CHANGE
Trade receivables	1,428	1,213	215	18%
<i>of which, without recourse</i>	<i>1,195</i>	<i>871</i>	<i>324</i>	<i>37%</i>
<i>of which, with recourse</i>	<i>233</i>	<i>342</i>	<i>(109)</i>	<i>-32%</i>
Tax receivables	282	115	167	146%
<i>of which, without recourse</i>	<i>270</i>	<i>107</i>	<i>163</i>	<i>152%</i>
<i>of which, with recourse</i>	<i>12</i>	<i>8</i>	<i>5</i>	<i>63%</i>
TOTAL	1,710	1,328	382	29%

In absolute terms, the growth in turnover derives mainly from the purchase of receivables from public or similar

type debtors, while in relative terms the best performance was recorded in the tax receivables sector.

SALARY-BACKED LOANS

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

As at 30 September 2018, the Bank has ten ongoing agreements with specialist distributors in the sector.

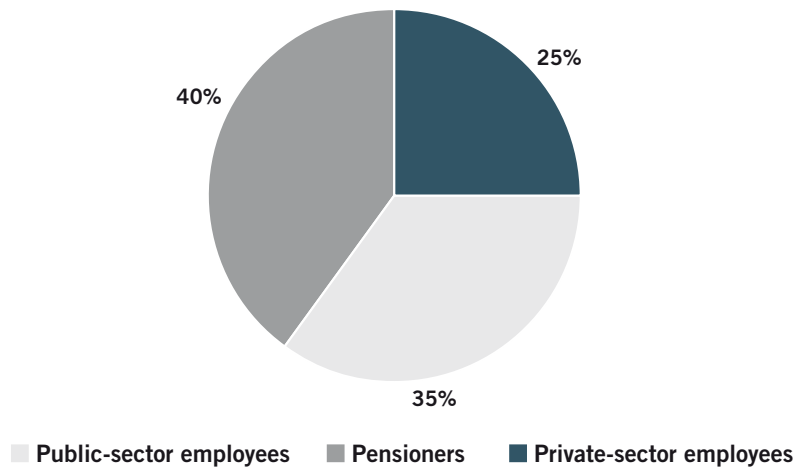
A salary- or pension-backed loan (CQS/CQP) is a consumer loan product that allows customers to allocate up to a fifth of their salaries or pensions to the payment of loan instalments.

The volumes acquired from the beginning of the year until September 2018 amounted to € 152 million, including private-sector employees (25%), pensioners (40%) and public-sector employees (35%). Therefore, over 75% of the volumes refer to pensioners and employees of Public Administration, which remains the Bank's main debtor.

	30.09.2018	30.09.2017	€ CHANGE	% CHANGE
No. of applications	7,667	8,743	(1,076)	-12%
Volumes disbursed (millions of Euro)	152	176	(23)	-13%

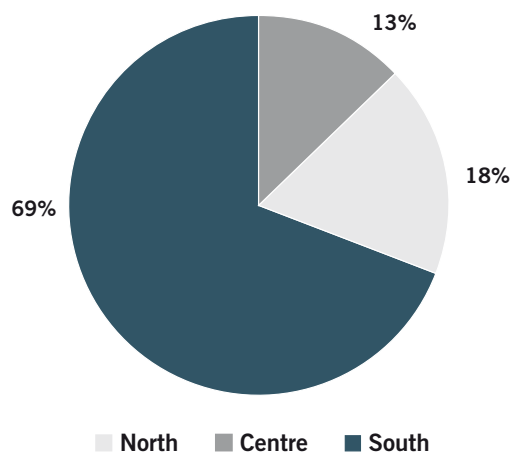
As inferred from the table, the amounts disbursed in September 2018 are down from what was disbursed in September 2017.

CQ disbursed volumes - Breakdown



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

CQ disbursed volumes - Breakdown by geographical area



FUNDING ACTIVITIES

Treasury portfolio

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

The balance at 30 September 2018 increased compared to 31 December 2017 and was equal to a nominal € 775 million (compared to € 362.5 million at 31 December 2017). The increase in the treasury portfolio allowed for optimal management of the Treasury commitments which are increasingly characterised by a concentration of transactions in very specific periods.

Beginning in May 2018, the fair value trend of the treasury portfolio was marked by significant volatility as a consequence of the political uncertainties. In the third quarter, the level of government bond yields and the spread between Italian and German bonds remained high. The market was particularly affected by price pressure on Italian securities caused by the decisions on the deficit target for the next three years which were in contrast with

the commitments undertaken at EU level.

At 30 September, the nominal amount of securities in the HTCS (formerly AFS) portfolio amounts to € 240 million (compared to € 279 million as at 31 December 2017) with a duration of 1 year and 7.5 months (7.3 months in the previous year).

During 2018 the securities at amortised cost portfolio ("HTC" or "Held to Collect") was established, made up entirely of Italian government securities. At 30 September, the HTC portfolio amounted to € 435 million with an average residual duration of 2 years and 5 months.

The HTC ("Held to Sell") securities portfolio was also established, made up entirely of short-term Italian government securities. At 30 September, the HTS portfolio amounted to a nominal € 100 million with an average remaining duration of 6.3 months.

The three portfolios have an overall duration of 1 year and 11 months.

Wholesale funding

As at 30 September 2018, wholesale funding was about 48% of the total, mainly comprising bonds, inter-bank deposits and refinancing transactions with the ECB (51% as at 31 December 2017).

The 2017 issues of € 175 million of senior bonds maturing on 13 October 2020 and € 16.5 million of the subordinated loan maturing on 30 March 2027, placed with institutional investors, have enabled a diversification of the sources of funding and a significant increase in their duration.

The securitisation transactions of Quinto Sistema Sec. 2016 and Quinto Sistema Sec. 2017, completed with a partly-paid securities structure and "progressive growth of the securitised portfolio" (a "warehouse" structure), permitted an efficient and effective source of funding dedicated to the CQS portfolio to be maintained throughout the year. On 25 June, the Quinto Sistema Sec. 2017 Senior securities (Class A) and Mezzanine

securities (Class B1) of the salary- and pension-backed loan (CQ) securitisation transaction were given a rating by Moody's (Aa2 and Baa3, respectively) and by DBRS (A-high and A-low, respectively) and were admitted to trading on the Luxembourg Stock Exchange. The Senior class securities may be used as collateral in Eurosystem refinancing transactions. Quinto Sistema Sec. 2017 is the second ABS transaction of salary- and pension-backed loans by Banca Sistema to be given a rating. The 2017 transaction later incorporated the loans portfolio from the first securitisation, thus bringing it to around € 400 million. A ramp up period will also follow that will end in February 2019 for a maximum total amount of € 660 million. The transaction will allow Banca Sistema to continue to grow its salary-/pension-backed loan business, thus optimising its funding structure dedicated to this same segment.

At the end of May a senior bond was successfully issued

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

The Group also used the interbank deposit market

both through the e-MID platform and through bilateral agreements with other banks. Existing bank deposits at 30 September 2018 totalled € 296 million. Such funding allows short-term treasury needs to be met by exploiting the moderate level of interest rates and enables the diversification of funding.

Retail funding

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

Retail funding accounts for 52% of the total and is composed of the account Si Conto! Corrente and the product Si Conto! Deposito.

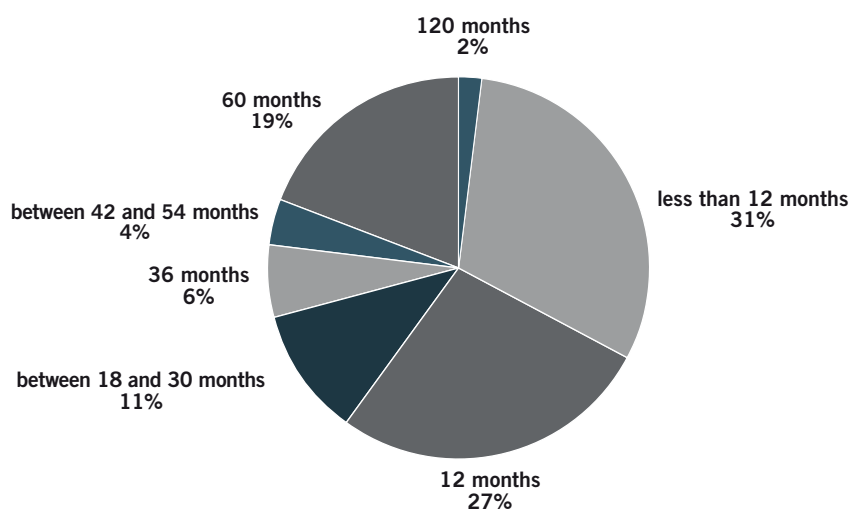
Total term deposits as at 30 September 2018 amounted to € 863 million, an increase of 93% compared to 31

December 2017.

The above-mentioned amount also includes total term deposits of € 224 million (obtained with the help of a partner platform) held with entities resident in Germany, Austria and Spain (accounting for 27% of total deposit funding), an increase of € 106 million over the same period of the previous year.

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

Breakdown of deposit accounts as at 30 September



Current accounts increased from 4,492 (as at 30 September 2017) to 5,440 as at 30 September 2018, while the

current account balance at 30 September 2018 increased 19% over the same period in 2017 to € 558 million.

INCOME STATEMENT RESULTS

INCOME STATEMENT (€,'000)	30.09.2018	30.09.2017	€ Change	% Change
Net interest income	53,038	54,131	(1,093)	-2.0%
Net fee and commission income	10,624	7,352	3,272	44.5%
Dividends and similar income	227	227	-	0.0%
Net trading expense	(461)	70	(531)	<100%
Gain from sales or repurchases of financial assets/liabilities	1,102	858	244	28.4%
Total income	64,530	62,638	1,892	3.0%
Net impairment losses on loans and receivables	(4,334)	(3,057)	(1,277)	41.8%
Net financial income	60,196	59,581	615	1.0%
Personnel expense	(14,448)	(12,772)	(1,676)	13.1%
Other administrative expenses	(16,247)	(14,958)	(1,289)	8.6%
Net accruals to provisions for risks and charges	(51)	(82)	31	-37.8%
Net impairment losses on property and equipment/intangible assets	(213)	(229)	16	-7.0%
Other operating income (expense)	133	(321)	454	<100%
Operating costs	(30,826)	(28,362)	(2,464)	8.7%
Losses on equity investments	(355)	(62)	(293)	>100%
Pre-tax profit	29,015	31,157	(2,142)	-6.9%
Income taxes for the period	(9,879)	(9,309)	(570)	6.1%
Profit for the period attributable to the owners of the parent	19,136	21,848	(2,712)	-12.4%

The comparative figures represent a mere restatement of the statutory figures for the three months ended 30 September 2017 in accordance with IFRS 9. Therefore, they do not represent the net amounts resulting from retrospective application of the aforementioned accounting standard and consequently are not perfectly comparable with each other.

The result for the third quarter of 2018 was a profit for the period of € 19.1 million, slightly down compared to the previous period of the previous year, mainly due to an increase in operating costs not offset by total income. In the third quarter of 2018, the expected rates of recovery of default interest on factoring and the related collection times used for the estimate as at 30 September 2018

were updated in the light of the progressive consolidation of the historical data series; the adjustment of these estimates led to the recognition of total interest income of € 6.6 million, of which € 4.9 million attributable to previous years.

The results for the same period in the previous year also benefited from the change in the estimate for the probability of collection of default interest which led to the recording of higher interest income of € 9 million, of which € 3.7 related to prior years. Results in the prior year also benefited from a € 3.9 million release related to bad exposures with troubled municipalities and greater tax benefits which had a positive impact on lowering the tax rate.

NET INTEREST INCOME (€,000)	30.09.2018	30.09.2017	€ Change	% Change
Interest and similar income				
Loans and receivables portfolios	69,407	66,360	3,047	4.6%
Securities portfolio	166	144	22	15.3%
Other	856	265	591	>100%
Financial liabilities	1,155	1,549	(394)	-25.4%
Total interest income	71,584	68,318	3,266	4.8%
Interest and similar expense				
Due to banks	(2,138)	(1,214)	(924)	76.1%
Due to customers	(10,279)	(9,885)	(394)	4.0%
Securities issued	(5,114)	(2,257)	(2,857)	>100%
Financial assets	(1,015)	(831)	(184)	22.1%
Total interest expense	(18,546)	(14,187)	(4,359)	30.7%
Net interest income	53,038	54,131	(1,093)	-2.0%

Net interest income was slightly lower than in the same period of the previous year, due to a larger increase in interest expense with respect to interest income. Net interest income remained essentially stable when excluding the non-recurring interest expense component of € 0.8 million linked to TLTRO II.

The total contribution of the factoring portfolio was € 53.6 million, a decrease of 1% over the same period in the previous year; when considering the commission component associated with the factoring business over nine months, contribution increased by 4.7%. The component linked to default interest from legal action at 30 September 2018 was € 20.1 million compared to (€ 19.1 million in the first nine months of 2017, excluding € 2.8 million relating to the early closing of the guarantee agreement provided by the former shareholder of Beta Stepstone, company acquired in 2016 and merged into Banca Sistema the following year):

- of which € 6.6 million resulting from the updated recovery estimates, and € 4.9 million from previous years (€ 9.0 million at 30 September 2017, of which € 3.7 million from previous years);
- of which € 9.3 million by keeping recovery estimates constant (€ 4.7 million at 30 September 2017);
- of which € 4.2 million (€ 5.4 million in the first nine months of 2017) coming from net collections during the period (difference between the amount collected during

the period, equal to € 8.8 million, of which € 8.1 million in the first nine months of 2017 compared to what was recognised on an accruals basis in previous periods).

The amount of the stock of default interest from legal actions accrued at 30 September 2018, relevant for the allocation model, was € 100 million (€ 84 million at the end of the third quarter of 2017) while the loans and receivables recorded in the financial statements amounted to € 44.5 million.

The positive impact on income was also driven by growth in interest on the salary- and pension-backed portfolios, which rose from € 9.1 million to € 14.1 million, whereas interest declined on the SME portfolios, which contributed € 1.6 million to the total, following the strategic decision to discontinue this area of the business.

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

The “other” interest income mainly includes income generated from hot money transactions and interest generated by collateral-backed loan activities which

contributed € 0.2 million.

The cost of funding increased compared to the same period of the previous year following the increase in interest on securities issued that was strictly related to the new bond issues, and therefore to higher stock compared to the same period of the previous year, which allowed for greater diversification in the forms of funding and a duration greater than the previous funding mix.

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

Financial assets at 30 September 2018 were largely composed of the negative yield on Italian government bonds and the above par acquisition of a loan portfolio consisting of collateral-backed loans.

NET FEE AND COMMISSION INCOME (€ ,000)	30.09.2018	30.09.2017	€ Change	% Change
Fee and commission income				
Collection activities	826	746	80	10.7%
Factoring activities	11,502	7,972	3,530	44.3%
Other	537	452	85	18.8%
Total fee and commission income	12,865	9,170	3,695	40.3%
Fee and commission expense				
Placement	(1,866)	(1,468)	(398)	27.1%
Other	(375)	(350)	(25)	7.1%
Total fee and commission expense	(2,241)	(1,818)	(423)	23.3%
Net fee and commission income	10,624	7,352	3,272	44.5%

Net fee and commission income of € 10.6 million increased by 44.5% due to the greater commissions from factoring. These should be considered together with interest income, since it makes no difference from a management point of view whether profit is recognised in the commissions and fees item or in interest in the without recourse factoring business.

Commissions on collection activities, related to the service of reconciliation of third-party invoices collected from Public Administration are in line with the same period of the previous year, while other fee and commission income, which primarily includes commissions and fees from collection and payment services, the keeping and management of current accounts, and fees related to the

collateral-backed loan business, amounting to € 108 thousand, have increased.

The placement fees and commissions paid to third parties increased due to their close correlation with the increase in the factoring volumes disbursed. Fee and commission expense includes the origination costs of factoring receivables of € 985 thousand (€ 1,114 thousand in the same period of last year) while the remainder includes returns to third party intermediaries for the placement of the SI Conto! Deposito product on volumes placed in Germany, Austria and Spain.

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

RESULTS OF THE SECURITIES PORTFOLIO (€,000)	30.09.2018	30.09.2017	€ Change	% Change
Net trading income (expense)				
Realised gains	14	1	13	>100%
Valuation loss/gain	(475)	69	(544)	<100%
Total	(461)	70	(531)	<100%
Gain (loss) from sales or repurchases				
Gains from HTCS portfolio debt instruments	1,102	858	244	28.4%
Total	1,102	858	244	28.4%
Total profit from the securities portfolio	641	928	(287)	-30.9%

Net trading income (expense) is mainly generated by the market value of the Italian government bonds included in the trading portfolio that have suffered a decrease in fair value as a result of the tensions in the financial markets. The remaining duration of the securities in the trading portfolio at 30 September 2018 was 6.3 months. Therefore, in the short term the temporary loss from market valuation will be fully recovered, even if only as a result of the reduction in the remaining duration. The gains generated by the proprietary HTCS portfolio made a greater contribution than in same period of the previous year.

Impairment losses on loans and receivables at 30 September 2018 amounted to € 4.3 million and were up on the same period of the previous year, inasmuch as 2017 had been influenced by releases of € 3.9 million tied to bad exposures with troubled local authorities; net of these releases, these impairment losses are decreasing. On the other hand, while not significant, the new method resulting from the application of IFRS 9, which is based on an “expected loss” model compared to the previous “incurred loss” model, led to an increase in impairment losses on performing loans classified as stage 2. The loss rate at 30 September 2018 amounts to 28 bps.

PERSONNEL EXPENSE (€,000)	30.09.2018	30.09.2017	€ Change	% Change
Wages and salaries	(13,463)	(11,926)	(1,537)	12.9%
Social security contributions and other costs	(231)	(241)	10	-4.1%
Directors' and statutory auditors' remuneration	(754)	(605)	(149)	24.6%
Total	(14,448)	(12,772)	(1,676)	13.1%

The increase in personnel expense is mainly due to the increase in the average number of employees from 147 to 181, an increase in gross annual salaries, and an

additional cost component related to some non-compete agreements. The number of employees is provided in the following table:

FTEs	30.09.2018	31.12.2017	30.09.2017
Senior managers	20	19	20
Middle managers (QD3 and QD4)	41	39	40
Other personnel	118	98	93
Total	179	156	153

OTHER ADMINISTRATIVE EXPENSES (€,000)	30.09.2018	30.09.2017	€ Change	% Change
IT expenses	(3,482)	(3,274)	(208)	6.4%
Consultancy	(3,362)	(2,724)	(638)	23.4%
Servicing and collection activities	(2,047)	(2,105)	58	-2.8%
Rent and related fees	(1,579)	(1,501)	(78)	5.2%
Indirect taxes and duties	(1,459)	(1,054)	(405)	38.4%
Resolution Fund	(942)	(807)	(135)	16.7%
Car hire and related fees	(637)	(649)	12	-1.8%
Expense reimbursement and entertainment	(530)	(568)	38	-6.7%
Other	(505)	(741)	236	-31.8%
Expenses related to management of the SPVs	(417)	(291)	(126)	43.3%
Insurance	(297)	(270)	(27)	10.0%
Advertising	(280)	(231)	(49)	21.2%
Audit fees	(237)	(219)	(18)	8.2%
Infoprovder expenses	(197)	(218)	21	-9.6%
Stationery and printing	(37)	(92)	55	-59.8%
Telephone and postage expenses	(130)	(129)	(1)	0.8%
Maintenance of movables and real properties	(109)	(85)	(24)	28.2%
Total	(16,247)	(14,958)	(1,289)	8.6%

The rise in IT expenses is linked to the increase in services provided by the outsourcer due to the increase in Group operations as well as to IT updates on new products.

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

the merger of the previous Quinto Sistema Sec. 2016 securitisation into it.

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

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

THE MAIN STATEMENT OF FINANCIAL POSITION AGGREGATES

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

ASSETS (€,'000)	30.09.2018	31.12.2017	€ Change	% Change
Cash and cash equivalents	327	161	166	>100%
Financial assets measured at fair value through profit or loss	99,732	1,201	98,531	>100%
Financial assets measured at fair value through other comprehensive income	241,705	285,610	(43,905)	-15.4%
Financial assets measured at amortised cost	2,756,992	1,970,495	786,497	39.9%
a) loans and receivables with banks	43,100	36,027	7,073	19.6%
b1) loans and receivables with customers - loans	2,278,301	1,850,290	428,011	23.1%
b2) loans and receivables with customers - debt instruments	435,591	84,178	351,413	>100%
Equity investments	2,179	1,190	989	83.1%
Property and equipment	27,164	24,272	2,892	11.9%
Intangible assets	1,787	1,790	(3)	-0.2%
<i>of which: goodwill</i>	<i>1,786</i>	<i>1,786</i>	-	<i>0.0%</i>
Tax assets	8,103	10,198	(2,095)	-20.5%
Other assets	14,741	14,316	425	3.0%
Total assets	3,152,730	2,309,233	843,497	36.5%

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

The first nine months ending 30 September 2018 closed with total assets up 36.5% (at € 3.2 billion) on the end of 2017, mainly due to the effect of the increase in the portfolios of receivables with customers and the securities portfolio.

The item Financial assets measured at fair value through profit or loss ("HTS") includes the short-term portion (equal to 6.3 months) of the Bank's government securities portfolio and is managed for trading purposes. At 30 September, the portfolio, which was established in 2018, was impacted by the decrease in the value of Italian government securities which were the subject of market tension resulting from

the uncertainty following the general elections in Italy. At 30 September 2018, the portfolio reported a valuation loss of € 0.4 million.

The securities portfolio relating to Financial assets measured at fair value through other comprehensive income ("HTCS" or "Held to collect and Sale") of the Group is mainly comprised of Italian government bonds with an average remaining duration of about 1 year and 7.5 months (the remaining average duration at the end of 2017 was 7.3 months). This is consistent with the Group investment policy. The government securities portfolio amounted to € 240 million at 30 September 2018 (€ 279 at 31 December 2017). The associated valuation reserve was negative at the end of the period, amounting to € 4.5 million before the tax effect. In addition to government securities, the HTCS portfolio also includes 200 shares of the Bank of Italy, amounting to € 5 million and purchased in July 2015, and the Axactor Norway shares, which at 30 September 2018 had a positive net fair value reserve of € 0.4 million, resulting in a period-end amount of € 1.6 million.

LOANS AND RECEIVABLES WITH CUSTOMERS (€,000)	30.09.2018	31.12.2017	€ Change	% Change
Factoring	1,575,647	1,285,726	289,921	22.5%
Salary-/pension-backed loans (CQS/CQP)	608,825	500,480	108,345	21.6%
Loans to SME	33,749	55,581	(21,832)	-39.3%
Current accounts	23,698	5,975	17,723	>100%
Pledge on receivables	4,884	1,366	3,518	>100%
Compensation and Guarantee Fund	30,456	865	29,591	>100%
Other loans and receivables	1,042	297	745	>100%
Total loans	2,278,301	1,850,290	428,011	23.1%
Securities	435,591	84,178	351,413	>100%
Total loans and receivables with customers	2,713,892	1,934,468	779,424	40.3%

The item loans and receivables with customers under Financial assets measured at amortised cost (hereinafter HTC, or “Held to Collect”), is composed of loan receivables with customers and, beginning in 2018, the securities portfolios that were classified separately until 31 December 2017 in the line “held-to-maturity securities”. Outstanding loans for factoring receivables compared to the total in the item, excluding the amounts of the securities portfolio, were unchanged from the end of 2017 at 69%. Their absolute value grew as a result of accumulated turnover in the last three quarters. Compared to the same period last year, turnover grew by 29%, to € 1,710 million (€ 1,329 million at 30 September 2017). Salary- and pension-backed loans grew in terms of their outstanding amount thanks to new loans, which fell by 13% compared with the same period of the previous year (the new volumes acquired in the first nine months amounted to € 152 million),

while government-backed loans to SMEs fell, which is in line with the strategic decision to discontinue this line of business.

At the end of 2016, the Parent began developing the collateralised loan business. Accordingly, in addition to the Milan, Rome and Pisa branches, branches in Naples and Palermo were opened. Outstanding volumes at 30 September 2018, totalling € 4.9 million, are the result of loans granted during the year of € 5.4 million, which includes the acquisition of one portfolio of third-party receivables amounting to € 1.3 million.

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

Securities are composed entirely of Italian government securities with an average duration of 2.3 years for an amount of € 435 million.

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

STATUS	30.09.2017	31.12.2017	31.03.2018	30.06.2018	30.09.2018
Bad exposures	39,799	44,577	44,867	53,412	60,566
Unlikely to pay	24,083	24,061	37,621	30,765	31,305
Past due	89,145	74,690	76,626	89,335	97,263
Non-performing	153,027	143,328	159,114	173,532	189,134
Performing - Stage 1			1,715,702	1,949,299	2,020,872
Performing - Stage 2			73,131	67,260	101,813
Total Performing	1,480,346	1,734,845	1,788,833	2,016,559	2,122,685
Total loans and receivables with customers	1,633,373	1,878,173	1,947,947	2,190,091	2,311,819
Individual impairment losses	19,864	22,293	23,413	26,629	27,662
Collective impairment losses	5,703	5,590	5,324	5,496	5,856
of which Stage 1			4,870	5,059	5,287
of which Stage 2			454	437	569
Total impairment losses	25,567	27,883	28,737	32,125	33,518
Net exposure	1,607,806	1,850,290	1,919,210	2,157,966	2,278,301

The ratio of gross non-performing loans to the total portfolio went from 7.6% at 31 December 2017 to 8.3% at the end of the third quarter of 2018. The increase in the absolute value of non-performing loans compared to 31 December 2017 is mainly tied to new factoring positions that moved to the bad exposures category and also to receivables that were acquired relating to debtors already considered bad exposures. The amount of past due loans is attributed to factoring receivables without recourse from Public Administration and is considered normal for the sector and does not represent an issue in terms of credit quality and probability of collection. Net bad exposures remained at moderate levels and amounted to 1.8% of total loans and receivables with customers, while the coverage ratio of non-performing loans was equal to 14.6%.

Equity investments include the Bank's current equity investment of 10% in Axactor Italy S.p.A., a company operating on the bad financial and commercial exposures management market, as well as in the management and recovery of receivables between individuals. The increase during the period is mainly attributed

to the pro-quota capital increase of € 724 thousand subscribed by Banca Sistema, partially offset by its loss for the period. Equity investments also include the acquisition for € 0.6 million of a 19.90% stake in the share capital of ADV Finance S.p.A. ("ADV Finance"), a registered financial intermediary (under art. 106 of the Consolidated Banking Act) that since 2010 has offered in Italy, through agents and brokers, a complete range of services related to salary- and pension-backed personal loans (CQS/CQP).

Property and equipment includes the property located in Milan, which will also be used as Banca Sistema's new offices following the completion of the renovation work. Its current carrying amount is € 26.4 million. The other capitalised costs include furniture, fittings and IT devices and equipment.

Intangible assets refer essentially to the goodwill generated by the acquisition of the former subsidiary Solvi S.r.l. that was subsequently merged into the Parent. Other assets include amounts being processed after the end of the year and advance tax payments of approximately € 6.6 million.

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

LIABILITIES AND EQUITY (€,'000)	30.09.2018	31.12.2017	€ Change	% Change
Financial liabilities measured at amortised cost	2,902,827	2,083,435	819,392	39.3%
a) due to banks	609,188	517,533	91,655	17.7%
b) due to customers	1,985,566	1,284,132	701,434	54.6%
c) securities issued	308,073	281,770	26,303	9.3%
Tax liabilities	15,905	10,118	5,787	57.2%
Other liabilities	79,551	71,996	7,555	10.5%
Post-employment benefits	2,412	2,172	240	11.0%
Provisions for risks and charges	8,396	6,745	1,651	24.5%
Valuation reserves	(2,843)	367	(3,210)	<100%
Reserves	117,840	98,105	19,735	20.1%
Share capital	9,651	9,651	-	0.0%
Treasury shares (-)	(145)	(149)	4	-2.7%
Profit for the period/year	19,136	26,793	(7,657)	-28.6%
Total liabilities and equity	3,152,730	2,309,233	843,497	36.5%

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

Wholesale funding, which represents about 48% (51% at 31 December 2017) of the total, rose in absolute terms from the end of 2017 following an increase in funding through REPOs, and in part an increase in ECB deposits. The contribution of bond funding to total wholesale funding was 28.3% (36.5% at 31 December 2017).

DUE TO BANKS (€,'000)	30.09.2018	31.12.2017	€ Change	% Change
Due to Central banks	312,851	192,064	120,787	62.9%
Due to banks	296,337	325,469	(29,132)	-9.0%
<i>Current accounts and demand deposits</i>	5,030	13,969	(8,939)	-64.0%
<i>Term deposits</i>	291,307	311,500	(20,193)	-6.5%
Total	609,188	517,533	91,655	17.7%

The total of the sub-item "Due to banks" increased by 17.7% compared to 31 December 2017 due to the increase in funding through refinancing with the

ECB, whose underlying assets are primarily ABS from the salary- and pension-backed loans (CQS/CQP) securitisation.

DUE TO CUSTOMERS (€,'000)	30.09.2018	31.12.2017	€ Change	% Change
Term deposits	863,393	447,093	416,300	93.1%
Financing (repurchase agreements)	451,174	215,623	235,551	>100%
Current accounts	557,810	510,349	47,461	9.3%
Deposits with Cassa Depositi e Prestiti	26,956	38,959	(12,003)	-30.8%
Due to assignors	86,233	72,108	14,125	19.6%
Total	1,985,566	1,284,132	701,434	54.6%

Customer deposits increased compared to the end of the year, mainly due to an increase in financing from repurchase agreements, as a result of an increase in the securities portfolio. The collateral for the repurchase agreements is represented by government securities. The period-end amount of term deposits increased by 93% compared to the end of 2017, reflecting net positive deposits (net of interest accrued) of € 416

million; gross deposits from the beginning of the year were € 774 million, against withdrawals caused mainly by non-renewals totalling € 358 million.

Due to customers also includes financing of € 27 million from Cassa Depositi e Prestiti obtained against collateral consisting solely of loans to SMEs by the Bank.

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

SECURITIES ISSUED (€ ,000)	30.09.2018	31.12.2017	€ Change	% Change
Bond - Tier I	8,155	8,017	138	1.7%
Bond - Tier II	31,931	28,703	3,228	11.2%
Bonds - other	267,987	245,050	22,937	9.4%
Total	308,073	281,770	26,303	9.3%

The nominal amount of securities issued at 30 September 2018 is broken down as follows:

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

At the end of May a senior bond was successfully issued in a club deal reserved for institutional investors that are not related parties, for a total subscribed amount of € 90 million, a term of three years, with a fixed rate and

an all-inclusive cost of 200 bps. This issue replaced the senior loan of 75 million which expired in May.

The provision for risks and charges of € 8.4 million includes the amount of € 3 million, representing the estimated future liabilities attributable to Beta. The remaining balance refers to the estimated portion of the bonus for the year, the deferred portion of the bonus accrued in previous years, and the update to the estimate related to the non-compete agreement. The provision also includes an estimate of the charges relating to legal actions within the framework of a lending transaction in which the end borrower is bankrupt, and the estimated charges for lawsuits and legal disputes, in addition to the estimated charges related to lawsuits with personnel who are no longer active within the company.

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

The reconciliation between the profit for the period and equity of the parent and the figures from the consolidated financial statements is shown below.

(€ ,000)	PROFIT (LOSS)	EQUITY
Profit/equity of the parent	19,908	145,732
Assumption of value of investments	-	(15,386)
Consolidated loss/equity	(772)	13,293
Equity attributable to the owners of the parent	19,136	143,639
Equity attributable to non-controlling interests	-	(30)
Group equity	19,136	143,609

CAPITAL ADEQUACY

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

OWN FUNDS (€,000) AND CAPITAL RATIOS	30.09.2018	31.12.2017
Common Equity Tier 1 (CET1)	136,749	125,767
ADDITIONAL TIER 1	8,000	8,000
Additional Tier 1 capital (T1)	144,749	133,767
TIER2	29,403	28,239
Total Own Funds (TC)	174,152	162,006
Total risk weighted assets	1,227,788	1,058,017
of which, credit risk	1,075,574	909,012
of which, operational risk	143,487	143,487
of which, market risk	8,727	2,402
of which, CVA	0	3,116
Ratio - CET1	11.1%	11.9%
Ratio - AT1	11.8%	12.6%
Ratio - TCR	14.2%	15.3%

Total own funds were € 174.2 million at 30 September 2018 and included the profit for the period, net of dividends estimated on the profit for the period, which were equal to a pay-out of 25% of the Parent's profit.

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

Banca Sistema received notice of the Bank of Italy's decision regarding the consolidated capitalisation requirements that came into effect on 1 January

2018 following the outcome of the Supervisory Review and Evaluation Process (SREP). The capitalisation requirements, according to the transitory criteria, are as follows:

- CET1 ratio of 7.125% + additional +0.75% above the minimum regulatory requirement;
- TIER1 ratio of 8.875% + additional +1.0% above the minimum regulatory requirement;
- Total capital ratio of 11.225% + additional +1.35% above the minimum regulatory requirement.

OTHER INFORMATION

Research and Development Activities

No research and development activities were carried out in 2018.

RELATED PARTY TRANSACTIONS

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

ATYPICAL OR UNUSUAL TRANSACTIONS

During 2018, the Group did not carry out any atypical or unusual transactions, as defined in Consob Communication no. 6064293 of 28 July 2006.

SIGNIFICANT EVENTS AFTER THE REPORTING DATE

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

BUSINESS OUTLOOK AND MAIN RISKS AND UNCERTAINTIES

The growth trend in lending continued in the third quarter of 2018. Further consolidation in the factoring and salary- and pension-backed loans (CQS/CQP)

business continues to be one of the main objectives in 2018 and the following years.

Milan, 31 October 2018

On behalf of the Board of Directors

The Chairperson

Luitgard Spögler



The CEO

Gianluca Garbi



CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

STATEMENT OF FINANCIAL POSITION

Assets		(Amounts in thousands of Euro)	
		30.09.2018	31.12.2017 (*)
10.	Cash and cash equivalents	327	161
20.	Financial assets measured at fair value through profit or loss	99,732	1,201
	<i>a) financial assets held for trading</i>	99,732	1,201
30.	Financial assets measured at fair value through other comprehensive income	241,705	285,610
40.	Financial assets measured at amortised cost	2,756,992	1,970,495
	<i>a) loans and receivables with banks</i>	43,100	36,027
	<i>b) loans and receivables with customers</i>	2,713,892	1,934,468
70.	Equity investments	2,179	1,190
90.	Property and equipment	27,164	24,272
100.	Intangible assets	1,787	1,790
	<i>of which:</i>		
	<i>goodwill</i>	1,786	1,786
110.	Tax assets	8,103	10,198
	<i>a) current</i>	-	3,471
	<i>b) deferred</i>	8,103	6,727
130.	Other assets	14,741	14,316
	Total assets	3,152,730	2,309,233

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

Liabilities and equity		30.09.2018	31.12.2017 (*)
10.	Financial liabilities measured at amortised cost	2,902,827	2,083,435
	<i>a) due to banks</i>	609,188	517,533
	<i>b) due to customers</i>	1,985,566	1,284,132
	<i>c) securities issued</i>	308,073	281,770
20.	Financial liabilities held for trading	-	-
60.	Tax liabilities	15,905	10,118
	<i>a) current</i>	2,955	-
	<i>b) deferred</i>	12,950	10,118
80.	Other liabilities	79,551	71,996
90.	Post-employment benefits	2,412	2,172
100.	Provisions for risks and charges:	8,396	6,745
	<i>a) commitments and guarantees issued</i>	5	-
	<i>b) pension and similar obligations</i>	-	-
	<i>c) other provisions for risks and charges</i>	8,391	6,745
120.	Valuation reserves	(2,843)	367
150.	Reserves	78,605	58,807
160.	Share premium	39,205	39,268
170.	Share capital	9,651	9,651
180.	Treasury shares (-)	(145)	(149)
190.	Equity attributable to non-controlling interests (+/-)	30	30
200.	Profit for the period/year	19,136	26,793
	Total liabilities and equity	3,152,730	2,309,233

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

INCOME STATEMENT

(Amounts in thousands of Euro)

Items	30.09.2018	30.09.2017 (*)
10. Interest and similar income	71,584	68,318
of which: interest income calculated with the effective interest method	70,430	68,318
20. Interest and similar expense	(18,546)	(14,187)
30. Net interest income	53,038	54,131
40. Fee and commission income	12,865	9,170
50. Fee and commission expense	(2,241)	(1,818)
60. Net fee and commission income	10,624	7,352
70. Dividends and similar income	227	227
80. Net trading expense	(461)	70
100. Gain from sales or repurchases of:	1,102	858
b) financial assets measured at fair value through other comprehensive income	1,102	858
120. Total income	64,530	62,638
130. Net impairment losses on:	(4,334)	(3,057)
a) financial assets measured at amortised cost	(4,334)	(3,057)
150. Net financial income	60,196	59,581
190. Administrative expenses	(30,695)	(27,730)
a) personnel expense	(14,448)	(12,772)
b) other administrative expenses	(16,247)	(14,958)
200. Net accruals to provisions for risks and charges	(51)	(82)
b) other net accruals	(51)	(82)
210. Net impairment losses on property and equipment	(210)	(201)
220. Net impairment losses on intangible assets	(3)	(28)
230. Other operating income (expense)	133	(321)
240. Operating costs	(30,826)	(28,362)
250. Losses on equity investments	(355)	(62)
290. Pre-tax profit from continuing operations	29,015	31,157
300. Income taxes	(9,879)	(9,309)
310. Post-tax profit from continuing operations	19,136	21,848
330. Profit for the period/year	19,136	21,848
350. Profit for the period attributable to the owners of the parent	19,136	21,848

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

STATEMENT OF COMPREHENSIVE INCOME

(Amounts in thousands of Euro)

		30.09.2018	31.12.2017
10.	Profit for the period	19,136	26,793
	Items, net of tax, that will not be reclassified subsequently to profit or loss		
20.	Equity instruments designated at fair value through other comprehensive income	-	-
30.	Financial liabilities designated at fair value through profit or loss (changes in own credit rating)	-	-
40.	Hedging of equity instruments designated at fair value through other comprehensive income		
50.	Property and equipment		
60.	Intangible assets		
70.	Defined benefit plans	47	37
80.	Non-current assets classified as held for sale	-	-
90.	Share of valuation reserves of equity-accounted investments:	-	-
	Items, net of tax, that will be reclassified subsequently to profit or loss	-	-
100.	Hedges of foreign investments	-	-
110.	Exchange rate gains (losses)	-	-
120.	Cash flow hedges	-	-
130.	Hedging instruments (non-designated elements)		
140.	Financial assets (other than equity instruments) measured at fair value through other comprehensive income	(3,784)	(95)
150.	Non-current assets classified as held for sale	-	-
160.	Share of valuation reserves of equity-accounted investments:	-	-
170.	Total other comprehensive expense, net of income tax	(3,737)	(58)
180.	Comprehensive income (Items 10+170)	15,399	26,735
190.	Comprehensive income attributable to non-controlling interests	-	-
200.	Comprehensive income attributable to the owners of the parent	15,399	26,735

STATEMENTS OF CHANGES IN EQUITY AS AT 30.09.2018

Amounts in thousands of Euro

	Balance at 31.12.2017	Change in opening balances	Balance at 1.1.2018	Allocation of prior year profit		Changes during the period										Equity attributable to the owners of the parent at 30.09.2018	Equity attributable to non-controlling interests at 30.09.2018				
				Reserves	Dividends and other allocations	Transactions on equity															
Share capital:																					
a) ordinary shares	9,651	-	9,651	-	-	-	-	-	-	-	-	-	-	-	-	-	-	9,651	-		
b) other shares	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Share premium	39,268	-	39,268	-	-	(63)	-	-	-	-	-	-	-	-	-	-	-	39,205	-	-	
Reserves	58,807	(224)	58,583	19,877	-	145	-	-	-	-	-	-	-	-	-	-	-	78,605	-	-	
a) Income-related	59,133	(224)	58,909	19,877	-	6	-	-	-	-	-	-	-	-	-	-	-	78,792	-	-	
b) other	(326)	-	(326)	-	-	139	-	-	-	-	-	-	-	-	-	-	-	(187)	-	-	
Valuation reserves	367	527	894	-	-	-	-	-	-	-	-	-	-	-	-	-	-	(2,843)	-	-	
Equity instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	
Treasury shares	(149)	-	(149)	-	-	4	-	-	-	-	-	-	-	-	-	-	-	(145)	-	-	
Profit for the period/year	26,793	-	26,793	(19,877)	(6,916)	-	-	-	-	-	-	-	-	-	-	-	-	19,136	19,136	-	
Equity attributable to the owners of the parent	134,737	303	135,040	-	(6,916)	86	-	-	-	-	-	-	-	-	-	-	-	15,399	143,609	-	-
Equity attributable to non-controlling interests	30	-	30	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	30

Group equity still includes the dividend of € 6,916 thousand, which was distributed in May 2018.

STATEMENT OF CHANGES IN EQUITY AS AT 30.09.2017

Amounts in thousands of Euro

	Balance at 31.12.2016	Change in opening balances	Balance at 1.1.2017	Allocation of prior year profit		Changes in reserves	Changes during the period							Equity attributable to the owners of the parent at 30.09.2017	Equity attributable to non-controlling interests at 30.09.2017	
				Reserves	Dividends and other allocations		Transactions on equity									Comprehensive income at 30.09.2017
							Issue of new shares	Repurchase of treasury shares	Extraordinary dividend distribution	Change in equity instruments	Derivatives on treasury shares	Stock Options	Changes in equity investments			
Share capital:																
a) ordinary shares	9,651	-	9,651	-	-	-	-	-	-	-	-	-	-	-	-	9,651
b) other shares	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Share premium	39,352	-	39,352	-	-	(63)	-	-	-	-	-	-	-	-	-	39,289
Reserves	39,608	-	39,608	19,201	-	3	-	-	-	-	-	-	-	-	-	58,812
a) income-related	39,918	-	39,918	19,201	-	14	-	-	-	-	-	-	-	-	-	59,133
b) other	(310)	-	(310)	-	-	(11)	-	-	-	-	-	-	-	-	-	(321)
Valuation reserves	425	-	425	-	-	-	-	-	-	-	-	-	-	-	-	365
Equity instruments	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Treasury shares	(52)	-	(52)	-	-	52	(149)	-	-	-	-	-	-	-	-	(149)
Profit for the period/year	25,313	-	25,313	(19,201)	(6,112)	-	-	-	-	-	-	-	21,848	-	-	21,848
Equity attributable to the owners of the parent	114,296	-	114,296	-	(6,112)	(8)	-	-	-	-	-	-	21,788	-	-	129,816
Equity attributable to non-controlling interests	20	-	20	-	-	10	-	-	-	-	-	-	-	-	-	30

STATEMENT OF CASH FLOWS (direct method)

Amounts in thousands of Euro

	30.09.2018	30.09.2017
A. OPERATING ACTIVITIES		
1. Operations	33,091	30,629
▪ interest income collected	71,584	65,938
▪ interest expense paid	(18,546)	(11,807)
▪ dividends and similar income	227	227
▪ net fees and commissions	10,624	7,352
▪ personnel expense	(8,833)	(9,372)
▪ other expenses	(16,114)	(15,279)
▪ other income	-	-
▪ taxes and duties	(5,851)	(6,430)
2. Cash flows used for financial assets	(850,522)	(194,493)
▪ financial assets held for trading	(98,992)	591
▪ financial assets designated at fair value through profit or loss	-	-
▪ financial assets measured at fair value through profit or loss	-	-
▪ financial assets measured at fair value through other comprehensive income	41,797	91,747
▪ financial assets measured at amortised cost	(790,831)	(287,421)
▪ other assets	(2,496)	590
3. Cash flows generated by financial liabilities	828,959	171,197
▪ financial liabilities measured at amortised cost	819,392	162,071
▪ financial liabilities held for trading	-	-
▪ financial liabilities designated at fair value through profit or loss	-	-
▪ other liabilities	9,567	9,126
Net cash flows generated by operating activities	11,528	7,333
B. INVESTING ACTIVITIES		
1. Cash flows generated by	-	-
▪ sales of equity investments	-	-
▪ dividends from equity investments	-	-
▪ sales of property and equipment	-	-
▪ sales of intangible assets	-	-
▪ sales of subsidiaries and business units	-	-
2. Cash flows used in	(4,446)	(1,151)
▪ purchases of equity investments	(1,344)	(300)
▪ purchases of property and equipment	(3,102)	(863)
▪ purchases of intangible assets	-	12
▪ sales of subsidiaries and business units	-	-
Net cash flows used in investing activities	(4,446)	(1,151)
C. FINANCING ACTIVITIES		
▪ issues/repurchases of treasury shares	-	-
▪ issues/repurchases of equity instruments	-	-
▪ dividend and other distributions	(6,916)	(6,112)
▪ acquisitions and disposals of subsidiaries and other business units	-	-
Net cash flows used in financing activities	(6,916)	(6,112)
NET CASH FLOWS FOR THE PERIOD	166	70

RECONCILIATION - ITEMS

Cash and cash equivalents at the beginning of the period	161	98
Total net cash flows for the period	166	70
Cash and cash equivalents: effect of change in exchange rates	-	-
Cash and cash equivalents at the end of the period	327	168

GENERAL BASIS OF PREPARATION

This interim consolidated financial report at 30 September 2018 was drawn up in accordance with art. 154-ter of Legislative Decree no. 58 of 24 February 1998 and Legislative Decree no. 38 of 28 February 2005, pursuant to the IFRS issued by the International Accounting Standards Board (IASB) and endorsed by the European Commission, as established by Regulation (EC) no. 1606 of 19 July 2002, from which there were no derogations.

The specific accounting standards adopted have been amended compared to the financial statements at 31 December 2017 following the introduction as of 1 January 2018 of the new accounting standards IFRS 9 and IFRS 15.

The interim consolidated financial report at 30 September 2018 comprises the statement of financial position, income statement, statement of comprehensive income, statement of changes in equity, statement of cash flows and the notes to the interim consolidated financial report and are accompanied by a Directors' Report on the performance, the financial results achieved and the financial position of the Banca Sistema Group.

Subsequent events

After the reporting date of this condensed interim consolidated financial report, there were no events worthy of mention in the Accounting Policies thereto

Information on the main items of the consolidated financial statements

The interim consolidated financial report was prepared by applying IFRS and valuation criteria on a going concern basis, and in accordance with the principles of accruals and materiality of information, as well as the general principle of the precedence of economic substance over legal form.

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

The use of estimates is essential to preparing the financial

Pursuant to the provisions of art. 5 of Legislative Decree no. 38/2005, the financial statements use the Euro as the currency for accounting purposes. The amounts in the financial statements and the notes thereto are expressed (unless expressly specified) in thousands of Euro.

The financial statements were drawn up in accordance with the specific financial reporting standards endorsed by the European Commission, as well as pursuant to the general assumptions laid down by the Framework for the preparation and presentation of financial statements issued by the IASB.

This interim consolidated financial report includes Banca Sistema S.p.A. and the companies directly or indirectly controlled or connected with it. Compared with the situation as at 31 December 2017, no changes to the scope of consolidation have been reported.

This interim consolidated financial report at 30 September 2018 is accompanied by a statement by the manager in charge of financial reporting, pursuant to art. 154-bis of the Consolidated Finance Act. The consolidated financial statements have been subject to review.

which would have had an impact on the financial position, results of operations and cash flows of the Bank and Group.

statements. The most significant use of estimates and assumptions in the consolidated financial statements can be attributed to:

- the valuation of loans and receivables with customers: the acquisition of performing receivables from companies that supply goods and services represents the Bank's main activity. Estimating the value of these receivables is a complex activity with a high degree of uncertainty and subjectivity. Their value is estimated by using models that include numerous quantitative and qualitative

- elements. These include the historical data for collections, expected cash flows and the related expected recovery times, the existence of indicators of possible impairment, the valuation of any guarantees, and the impact of risks associated with the sectors in which the Bank's customers operate;
- the valuation of default interest pursuant to Legislative Decree no. 231 of 9 October 2002 on performing receivables acquired without recourse: estimating the expected recovery percentages of default interest is complex, with a high degree of uncertainty and subjectivity. Internally developed valuation models are used to determine these percentages, which take numerous qualitative and

quantitative elements into consideration;

- the estimate related to the possible impairment losses on goodwill and equity investments recognised in the financial statements;
- the quantification and estimate made for recognising liabilities in the provision for risks and charges, the amount or timing of which are uncertain;
- the recoverability of deferred tax assets.

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

The transition to financial reporting standard IFRS 9

Regulatory provisions

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

IFRS 9 has introduced significant changes, particularly in regard to the following aspects:

- Classification and measurement of financial instruments;
- Impairment;
- Hedge Accounting.

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

The Standard imposes new rules for classifying financial assets in the following categories:

- Amortised Cost - "AC": this category implies use of the amortised cost measurement method;
- Fair Value through Other Comprehensive Income - "FVOCI": this classification entails measurement at fair value, with recognition of the changes in fair value in a special equity reserve. This reserve is transferred to profit or loss when the financial instrument is sold/redeemed;

- Fair Value through Profit or Loss - "FVTPL": this class governs the measurement of instruments at fair value, with recognition of changes in profit or loss. The FVTPL category is defined by the Standard as a residual category, in which the financial instruments that cannot be classified in the preceding categories are classified based on the Business Model or the results of the test on the characteristics of contractual cash flows (SPPI test).

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

The classification and measurement of financial assets represented by loans and receivables and instruments are based on a two-step approach:

- association of the Business Model with the identified uniform portfolios, where the aggregation by uniform portfolios is determined at a level that reflects how groups of financial assets are managed together to achieve a particular business objective;
- analysis of the characteristics of the contractual cash flows of the instrument carried out on the individual assets at the origination date.

Thus, the Business Model represents the way in which the Bank manages its financial assets, i.e. with which it

intends to realise the cash flows of the debt instruments. It reflects the way in which groups of financial assets are managed together to achieve a particular business objective. It does not depend on management intentions concerning an individual instrument but is decided at a higher level of aggregation.

The possible Business Models delineated by the Standard are as follows:

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

As regards impairment, the new financial reporting

standard requires:

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

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

Adoption of IFRS 9

In regard to the methods used to present the effects of first-time adoption of the Standard, the Bank has exercised the option envisaged in paragraph 7.2.15 of IFRS 9 and paragraphs E1 and E2 of IFRS 1 “First-Time Adoption of International Financial Reporting Standards”. According to those rules - without prejudice to retrospective application of the new measurement and presentation rules prescribed by the Standard - there is no obligation to restate the comparative data in the financial statements on a uniform basis in the financial statements prepared upon first-time adoption of the new standard. According to the instructions given in the report accompanying issuance of Circular no. 262 “Bank financial statements: forms

and drafting rules” - version 5 of 22 December 2017, the banks that claim exemption from the obligation to restate their comparative values will nonetheless have to include, in the first financial statements prepared pursuant to the update to Circular no. 262, a reconciliation statement showing the method used and provide a reconciliation between the data of the last approved financial statements and the first financial statements prepared in accordance with the new rules. Moreover, the form and contents of that disclosure will depend on the autonomous choices of the delegated corporate bodies.

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

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

Classification and measurement of financial instruments

Application of the new classification and measurement methods introduced by IFRS 9 has resulted in reclassification of the securities held in the HTM portfolio pursuant to IAS

39 among financial assets measured at amortised cost. No other effects deriving from definition of the business models and the SPPI test have been recognised.

Impairment

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

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

lifetime of the financial assets;

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

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

Details are provided in the table below:

STATUS	31.12.2017	FTA	01.01.2018
Bad exposures	44,577	-	44,577
Unlikely to pay	24,061	-	24,061
Past due/overdrawn	74,690	-	74,690
Gross non-performing loans - Stage 3	143,328	-	143,328
Individual impairment losses	(22,293)	-	(22,293)
Total net non-performing loans	121,035	-	121,035
Gross performing loans	1,734,845	-	1,734,845
Performing - Stage 1	-	1,619,590	1,619,590
Performing - Stage 2	-	115,255	115,255
Collective impairment losses	(5,590)	(241)	(5,831)
of which Stage 1	(5,152)	(49)	(5,201)
of which Stage 2	(438)	(192)	(630)
Total net performing loans	1,729,255	-	3,463,859
Gross exposure on securities	363,025	-	363,025
Impairment losses on securities	-	(61)	(61)
Net exposure	363,025	-	362,964
Gross off-balance sheet exposure	645	-	645
Impairment losses on endorsement credit	-	(23)	(23)
Net exposure	645	-	622
Gross exposure on loans and receivables with banks	-	-	-
Impairment losses on endorsement credit	-	(9)	(9)
Net exposure	-	-	(9)

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

adoption of IFRS 9.

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

STATEMENT OF FINANCIAL POSITION - ASSETS (in thousands of Euro)	31.03.2018	31.12.2017 (A)	Classification and measurement impact of IFRS 9 (B)	Impairment impact of IFRS 9 (C)	01.01.2018 (A+B+C)
Cash and cash equivalents	199	161	-	-	161
Financial assets measured at fair value through profit or loss	844	1,201	-	-	1,201
Financial assets measured at fair value through other comprehensive income	453,501	285,610	84,965	(61)	370,514
Financial assets measured at amortised cost	2,064,404	1,970,495	(84,178)	(273)	1,886,044
<i>a) loans and receivables with banks</i>	<i>24,652</i>	<i>36,027</i>	<i>-</i>	<i>-</i>	<i>36,027</i>
<i>b) loans and receivables with customers</i>	<i>2,039,752</i>	<i>1,934,468</i>	<i>(84,178)</i>	<i>(273)</i>	<i>1,850,017</i>
Equity investments	1,297	1,190	-	-	1,190
Property and equipment	24,772	24,272	-	-	24,272
Intangible assets	1,788	1,790	-	-	1,790
Tax assets	8,271	10,198	-	110	10,308
Other assets	16,604	14,316	-	-	14,316
Total Assets	2,571,680	2,309,233	787	(224)	2,309,796

STATEMENT OF FINANCIAL POSITION - LIABILITIES (in thousands of Euro)	31.03.2018	31.12.2017 (A)	Classification and measurement impact of IFRS 9 (B)	Impairment impact of IFRS 9 (C)	01.01.2018 (A+B+C)
Financial liabilities measured at amortised cost	2,326,279	2,083,435	-	-	2,083,435
<i>a) due to banks</i>	566,194	517,533	-	-	517,533
<i>b) due to customers</i>	1,477,072	1,284,132	-	-	1,284,132
<i>c) securities issued</i>	283,013	281,770	-	-	281,770
Financial liabilities held for trading	10,219	-	-	-	-
Tax liabilities	10,331	10,118	260	-	10,378
Other liabilities	76,660	71,996	-	-	71,996
Post-employment benefits	2,237	2,172	-	-	2,172
Provisions for risks and charges	6,863	6,745	-	-	6,745
Valuation reserves	214	367	527	-	894
Reserves	85,378	58,807	-	(224)	58,583
Share premium	39,247	39,268	-	-	39,268
Share capital	9,651	9,651	-	-	9,651
Treasury shares (-)	(146)	(149)	-	-	(149)
Equity attributable to non-controlling interests (+/-)	30	30	-	-	30
Profit for the period/year (+/-)	4,717	26,793	-	-	26,793
Total liabilities and equity	2,571,680	2,309,233	787	(224)	2,309,796

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

Below is the statement of reconciliation between equity calculated under IAS 39 and equity under IFRS 9, with a description of the principal effects deriving from the adoption of the new financial reporting standard:

Book equity at 31 December 2017 (IAS 39)	134,767
FTA reserve	(224)
Application of the new impairment model	(224)
Performing loans (stages 1 and 2)	(273)
Non-performing loans (stage 3)	-
Debt instruments	(61)
Tax effect	110
Classification and measurement effects	527
Adjustment of carrying amount of financial assets deriving from application of the Business Model as a balancing entry for the valuation reserve	787
Tax effect	(260)
Total effects of transition to IFRS 9	303
Book equity at 1 January 2018 (IFRS 9)	135,070

The impact deriving from first-time adoption of IFRS 9 on the CET 1 ratio of the Group is 2.1 bps. Therefore, the Bank has decided to allocate this impact in full to Equity.

Other aspects

The interim consolidated financial report was approved on 31 October 2018 by the Board of Directors, which authorised its disclosure to the public in accordance with IAS 10.

ACCOUNTING POLICIES FOR THE MAIN ITEMS OF THE CONSOLIDATED FINANCIAL STATEMENTS

Financial assets measured at fair value through profit or loss

Classification criteria

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

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

it is decided to settle the offset positions on a net basis. Derivatives also include those embedded in complex financial contracts – where the host contract is a financial liability which has been recognised separately.

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

Recognition criteria

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

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

Measurement and recognition criteria for income components

After initial recognition, the financial assets measured at fair value through profit or loss are recognised at fair value. The effects of the application of this measurement criterion are recognised in the income statement. For the

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

In particular, this item includes:

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

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

Derecognition criteria

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

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

Classification criteria

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

- financial assets that are held under a business model whose aim is achieved both through the collection of contractual cash flows and through sale ("Hold to Collect and Sell" business model);
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely

payments of principal and interest on the principal amount outstanding ("SPPI Test" passed).

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

In particular, this item includes:

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

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

Recognition criteria

Initial recognition of the financial assets is at the date of disbursement, based on their fair value including the transaction costs/income directly attributable to the acquisition of the financial instrument. Costs/income having the previously mentioned characteristics that will be repaid by the debtor or that can be considered as

standard internal administrative costs are excluded.

The initial fair value of a financial instrument is usually the cost incurred for its acquisition.

Measurement and recognition criteria for income components

Following initial recognition, financial assets are measured at their fair value with any gains or losses resulting from a change in the fair value compared to the amortised cost recognised in a specific equity reserve recognised in the statement of comprehensive income up until said financial asset is derecognised or an impairment loss is recognised.

For more details on the methods of calculating the fair value please refer to paragraph 17.3 below "Criteria for determining the fair value of financial instruments".

Equity instruments, for which the choice has been made to classify them in this category, are measured at fair value and the amounts recognised in other comprehensive income cannot be subsequently transferred to profit or loss, not even if they are sold (the so-called OCI exemption). The only component related to these equity instruments that is recognised through profit or loss is their dividends. Fair value is determined on the basis of the criteria already described for Financial assets measured at fair value through profit or loss.

For the equity instruments included in this category, which are not quoted on an active market, the cost approach is used as the estimate of fair value only on a residual basis and in a small number of circumstances, i.e., when all the measurement methods referred to above cannot be applied, or when there are a wide range of possible measurements of fair value, in which cost represents the most significant estimate.

Financial assets measured at fair value through other comprehensive income are subject to the verification of the significant increase in credit risk (impairment) required by IFRS 9, with the consequent recognition through profit or loss of an impairment loss to cover the expected losses.

Derecognition criteria

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

Financial assets measured at amortised cost

Classification criteria

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

- the financial asset is held under a business model whose objective is achieved through the collection of expected contractual cash flows (Hold to Collect business model);
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding ("SPPI Test" passed).

In particular, this item includes:

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

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

measured at fair value through profit or loss and under equity, in the specific valuation reserve, in the event of reclassification to Financial assets measured at fair value through other comprehensive income.

Recognition criteria

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

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

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

Measurement and recognition criteria for income components

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

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

The measurement criteria are strictly connected with the stage to which the receivable is assigned, where stage 1 contains performing loans, stage 2 consists of underperforming loans, i.e. loans that have undergone a significant increase in credit risk ("significant deterioration") since the

initial recognition of the instrument, and stage 3 consists of non-performing loans, i.e. the loans that show objective evidence of impairment.

The impairment losses recognised in profit or loss for the performing loans classified in stage 1 are calculated by considering an expected loss at one year, while for the performing loans in stage 2 they are calculated by considering the expected losses over the entire residual contractual lifetime of the asset (Lifetime Expected Loss). The performing financial assets are measured according to probability of default (PD), loss given default (LGD) and exposure at default (EAD) parameters, derived from internal historic series. For impaired assets, the amount of the loss, to be recognised through profit or loss, is established based on individual measurement or determined according to uniform categories and, then, individually allocated to each position, and takes account of forward-looking information and possible alternative recovery scenarios. Impaired assets include financial instruments classified as bad, unlikely-to-pay or past due/overdrawn by over ninety days according to the rules issued by the Bank of Italy, in line with the IFRS and EU Supervisory Regulations. The expected cash flows take into account the expected recovery times and the estimated realisable value of any guarantees. The original effective rate of each asset remains unchanged over time even if the relationship has been restructured with a variation of the contractual interest rate and even if the relationship, in practice, no longer bears contractual interest. If the reasons for impairment are no longer applicable following an event subsequent to the recognition of impairment, impairment gains are recognised in the income statement. The impairment gains may not in any case exceed the amortised cost that the financial instrument would have had in the absence of previous impairment losses. Impairment gains with time value effects are recognised in net interest income.

Derecognition criteria

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

Hedging transactions

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

Equity investments

Classification criteria

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

Recognition criteria

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

Measurement criteria

In the consolidated financial statements, equity investments in subsidiaries are consolidated using the full line-by-line method. Equity investments in associates and joint ventures are both measured at equity. At the end of each financial year or interim report date, an assessment is performed to determine if any objective evidence exists that an investment has been impaired. The recoverable value is then calculated taking into account the present value of the future cash flows that the investment will be able to generate, including the final disposal value of the investment. Any lower value, compared to the carrying amount, resulting from this calculation is charged to the income statement under “240 Gains (losses) on equity investments”. The item also includes any future impairment gains where the reasons for the previous impairment losses no longer apply.

Derecognition criteria

Equity investments are derecognised from the financial statements when the contractual rights to cash flows deriving from the investment are lost or when the investment is transferred, with the substantial transfer of all related risks and rewards. Gains and losses on the sale of equity investments are charged to the income

statement under the item “240 Gains (losses) on equity investments”; gains and losses on the sale of investments other than those measured at equity are charged to the income statement under the item “270 Gains (losses) on sales of investments”.

Property and equipment

Classification criteria

This item includes assets for permanent use, held to generate income, to be leased, or for administrative purposes, such as land, operating property, investment property, technical installations, furniture and fittings and equipment of any nature and works of art.

They also include leasehold improvements to third party assets if they can be separated from the assets in question. If the above costs do not display functional or usefulness-related autonomy, but future economic benefits are expected from them, they are recognised under “other assets” and are depreciated over the shorter period between that of expected usefulness of the improvements in question and the residual duration of the lease. Depreciation is recognised under “Other operating income (expense)”.

Property and equipment also include payments on account for the purchase and restructuring of assets not yet part of the production process and therefore not yet subject to depreciation.

“Operating” property and equipment are represented by assets held for the provision of services or for administrative purposes, while property and equipment held for “investment purposes” are those held to collect lease instalments and/or held for capital appreciation.

Recognition criteria

Property and equipment are initially recognised at cost, including all costs directly attributable to installation of the asset.

Extraordinary maintenance costs and costs for improvements leading to actual improvement of the asset, or an increase in the future benefits generated by the asset, are attributed to the reference assets, and are depreciated based on their residual useful life.

Measurement and recognition criteria for income components

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

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

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

At the end of each year, if there is any evidence that property or equipment that is not held for investment purposes may have suffered an impairment loss, a comparison is made between its carrying amount and its recoverable value, equal to the higher between the fair value, net of any costs to sell, and the related value in use of the asset, intended as the present value of future cash flows expected from the asset. Any impairment losses are recognised in the income statement under “net impairment losses on property and equipment”.

If the reasons that led to recognition of the impairment loss cease to apply, an impairment gain is recognised that may not exceed the value that the asset would have had, net of depreciation calculated in the absence of previous impairment losses.

For investment property, which comes within the scope of application of IAS 40, the measurement is made at the market value determined using independent surveys and the changes in fair value are recognised in the income statement under the item “fair value gains (losses) on property, equipment and intangible assets”.

Derecognition criteria

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

Intangible assets

Classification criteria

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

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

In the absence of one of the above characteristics, the expense of acquiring or generating the asset internally is recognised as a cost in the year in which it was incurred.

Intangible assets include software to be used over several years and other identifiable assets generated by legal or contractual rights.

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

Measurement criteria

Intangible assets are systematically amortised from the time of their input into the production process.

With reference to the goodwill, on an annual basis (or when impairment is detected), an assessment test is carried out on the adequacy of its carrying amount. For this purpose, the cash-generating unit to which the goodwill is attributed, is identified. The amount of any impairment is determined by the difference between the goodwill carrying amount and its recoverable value, if lower. This recoverable value is equal to the higher

amount between the fair value of the cash-generating unit, net of any costs to sell, and its value in use. As stated above, any consequent impairment losses are recognised in the income statement.

Derecognition criteria

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

Non-current assets classified as held for sale

At the date of the financial statements, the Group did not hold any “Non-current assets classified as held for sale”.

Financial liabilities measured at amortised cost

Classification criteria

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

Recognition criteria

These financial liabilities are initially recognised when the deposits are received or when the debt instruments are issued. Initial recognition is based on the fair value of the liabilities, increased by the costs/income of the transaction directly attributable to the acquisition of the financial instrument.

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

The initial fair value of a financial liability is usually equivalent to the amount collected.

Measurement and recognition criteria for income components

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

Derecognition criteria

The above financial liabilities are derecognised from the

statement of financial position when they expire or when they are extinguished. They are derecognised also in the event of repurchase, even temporary, of the previously-issued securities.

Any difference between the carrying amount of the extinguished liability and the amount paid is recognised in the income statement, under “Gain (loss) from sales or repurchases of: financial liabilities”.

If the Group, subsequent to the repurchase, re-places its own securities on the market, said transaction is considered a new issue and the liability is recognised at the new placement price.

Financial liabilities held for trading

Classification and recognition criteria

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

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

Measurement and recognition criteria for income components

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

Derecognition criteria

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

Financial liabilities designated at fair value through profit or loss

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

Current and deferred taxes

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

Income taxes are provided for on the basis of a prudential estimate of the current and deferred taxes. More specifically, deferred taxes are determined on the basis of the temporary differences between the carrying amount of assets and liabilities and their tax bases. Deferred tax assets are recognised in the financial statements to the extent that it is probable that they will be recovered based on the Group's ability to continue to generate positive taxable income.

Deferred tax assets and liabilities are accounted for at equity level with open balances and without offsetting entries, recognising the former under "Tax assets" and the latter under "Tax liabilities".

With respect to current taxes, at the level of individual taxes, advances paid are offset against the relevant tax charge, indicating the net balance under "current tax assets" or "current tax liabilities" depending on whether it is positive or negative.

Provisions for risks and charges

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

The provisions are reviewed at the reporting date of the annual financial statements and the interim financial statements and adjusted to reflect the current best

estimate. These are recognised under their own items in the income statement in accordance with a cost classification approach based on the "nature" of the cost. Provisions related to future charges for employed personnel relating to the bonus system appear under "personnel expense". The provisions that refer to risks and charges of a tax nature are reported as "income taxes", whereas the provisions connected to the risk of potential losses not directly chargeable to specific items in the income statement are recognised as "net accruals to provisions for risks and charges".

Post-employment benefits

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

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

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

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

Repurchase agreements

"Repurchase agreements" that oblige the party selling the relevant assets (for example securities) to repurchase them in the future and the "securities lending" transactions where the guarantee is represented by cash, are considered equivalent to swap transactions and, therefore, the amounts received and disbursed appear

in the financial statements as payables and receivables. In particular, the previously mentioned “repurchase agreements” and “securities lending” transactions are recognised in the financial statements as payables for the spot price received, while those for investments are recognised as receivables for the spot price paid. Such transactions do not result in changes in the securities portfolio. Consistently, the cost of funds and the income from the investments, consisting of accrued dividends on the securities and of the difference between the spot price and the forward price thereof, are recognised for the accrual period under interest in the income statement.

Criteria for determining the fair value of financial instruments

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

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

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

they are presented, the use:

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

cost, adjusted if necessary to take into account significant reductions in value, where the fair value cannot be reliably determined.

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

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

the issuing counterparty, taken from independent surveys, prices corresponding to the fraction of the equity held in the company or obtained using measurement models that do not use market data to estimate significant factors that condition the fair value of the financial instrument). This level includes measurements of financial instruments at cost price.

Business combinations

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

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

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

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

If the business combination is carried out through several transfers;

- the cost of the combination is the overall cost of the individual transactions;

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

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

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

- if an asset is not an intangible asset, it is probable that any future connected economic benefits will flow to the acquiring company and it is possible to assess its fair value reliably;

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

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

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

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

STATEMENT OF THE MANAGER IN CHARGE OF FINANCIAL REPORTING

The undersigned, Alexander Muz, in his capacity as Manager in charge of financial reporting of Banca Sistema S.p.A., hereby states, having taken into account the provisions of art. 154-bis, paragraph 2, of Legislative

decree no. 58 of 24 February 1998, that the accounting information in this interim consolidated financial report at 30 September 2018 is consistent with the company documents, books and accounting records.

Milan, 31 October 2018

Alexander Muz

Manager in charge of financial reporting

A handwritten signature in black ink, appearing to read 'A. Muz', written in a cursive style.

ANNEX

Following below are the tables reconciling the items of the financial statements at 31 December 2017 and the new items introduced by the Bank of Italy since the adoption of IFRS 9. This is a mere restatement of the data, carried out using the continuing values method with respect to the previously applicable IAS 39.

Statement of financial position - Assets (in thousands of Euro)		31.12.2017	Cash and cash equivalents	Financial assets held for trading	Available-for-sale financial assets	Held-to-maturity investments	Loans and receivables with banks	Loans and receivables with customers	Equity investments	Property and equipment	Intangible assets	Tax assets	Other assets	Total
Cash and cash equivalents	161	161	-	-	-	-	-	-	-	-	-	-	-	161
Financial assets measured at fair value through profit or loss	1,201	-	1,201	-	-	-	-	-	-	-	-	-	-	1,201
Financial assets measured at fair value through other comprehensive income	285,610	-	-	285,610	-	-	-	-	-	-	-	-	-	285,610
Financial assets measured at amortised cost	1,970,495	-	-	-	-	-	-	-	-	-	-	-	-	1,970,495
a) loans and receivables with banks	36,027	-	-	-	-	36,027	-	-	-	-	-	-	-	36,027
b) loans and receivables with customers	1,934,468	-	-	-	84,178	1,850,290	-	-	-	-	-	-	-	1,934,468
Equity investments	1,190	-	-	-	-	-	1,190	-	-	-	-	-	-	1,190
Property and equipment	24,272	-	-	-	-	-	-	-	24,272	-	-	-	-	24,272
Intangible assets	1,790	-	-	-	-	-	-	-	-	1,790	-	-	-	1,790
Tax assets	10,198	-	-	-	-	-	-	-	-	-	10,198	-	-	10,198
Other assets	14,316	-	-	-	-	-	-	-	-	-	-	-	14,316	14,316
Total Assets	2,309,233	161	1,201	285,610	84,178	36,027	1,850,290	1,190	24,272	1,790	10,198	14,316	2,309,233	

Statement of financial position - Liabilities
(in thousands of Euro)

	31.12.2017	Due to banks	Due to customers	Securities issued	Tax liabilities	Other liabilities	Post-employment benefits	Provisions for risks and charges	Equity	Total
Financial liabilities measured at amortised cost	2,083,435	-	-	-	-	-	-	-	-	2,083,435
a) due to banks	517,533	517,533	-	-	-	-	-	-	-	517,533
b) due to customers	1,284,132	-	1,284,132	-	-	-	-	-	-	1,284,132
c) securities issued	281,770	-	-	281,770	-	-	-	-	-	281,770
Tax liabilities	10,118	-	-	-	10,118	-	-	-	-	10,118
Other liabilities	71,996	-	-	-	-	71,996	-	-	-	71,996
Post-employment benefits	2,172	-	-	-	-	-	2,172	-	-	2,172
Provisions for risks and charges:	6,745	-	-	-	-	-	-	6,745	-	6,745
Equity	134,767	-	-	-	-	-	-	-	134,767	134,767
Total liabilities and equity	2,309,233	517,533	1,284,132	281,770	10,118	71,996	2,172	6,745	134,767	2,309,233

INTERIM
CONSOLIDATED
DATED FINANCIAL
REPORT
AS AT 30
SEPTEMBER 2018

BANCA
SISTEMA
CONTEMPORARY BANK