BANCO BPM
GROUP

Consolidated interim report

as at 30 June 2018

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This document is a courtesy translation into English of the document in Italian approved by the Board of Directors. In case of any discrepancies or doubts between the English and the Italian versions of the Report, the Italian version prevails.

Banco BPM S.p.A.

Registered office: Piazza F. Meda, 4 - 20121 Milan, Italy
Administrative headquarters: Piazza Nogara, 2 - 37121 Verona, Italy
Fully paid up share capital as at 30 June 2018: EUR 7,100,000,000.00
Tax Code, VAT No. and Milan Companies' Register Enrolment No. 09722490969
Member of the Interbank Deposit Guarantee Fund and the National Guarantee Fund
Parent Company of the Banco BPM Banking Group
Enrolled in the Bank of Italy Register of Banks and the Register of Banking Groups

OFFICERS, DIRECTORS AND INDEPENDENT AUDITORS AS AT 30 JUNE 2018

	Board of Directors
Chairman	Carlo Fratta Pasini
Acting Deputy Chairman	Mauro Paoloni (*)
Deputy Chairman	Guido Castellotti (*)
Deputy Chairman	Maurizio Comoli (*)
Managing Director	Giuseppe Castagna (*)
Directors	Mario Anolli
	Michele Cerqua
	Rita Laura D'Ecclesia
	Carlo Frascarolo
	Paola Elisabetta Maria Galbiati
	Cristina Galeotti
	Marisa Golo
	Piero Sergio Lonardi (*)
	Giulio Pedrollo
	Fabio Ravanelli
	Pier Francesco Saviotti (*)
	Manuela Soffientini
	Costanza Torricelli
	Cristina Zucchetti

(*) members of the Executive Committee

	Board of Statutory Auditors
Chairman	Marcello Priori
Standing Auditors	Maria Luisa Mosconi
	Gabriele Camillo Erba
	Claudia Rossi
	Alfonso Sonato
Alternate Auditors	Chiara Benciolini
	Marco Bronzato
	Paola Simonelli

	General Management
General Manager	Maurizio Faroni
Joint General Manager	Domenico De Angelis
Joint General Manager	Salvatore Poloni

Manager responsible for preparing the Company's financial reports
Gianpietro Val

Independent Auditors
PricewaterhouseCoopers S.p.A.

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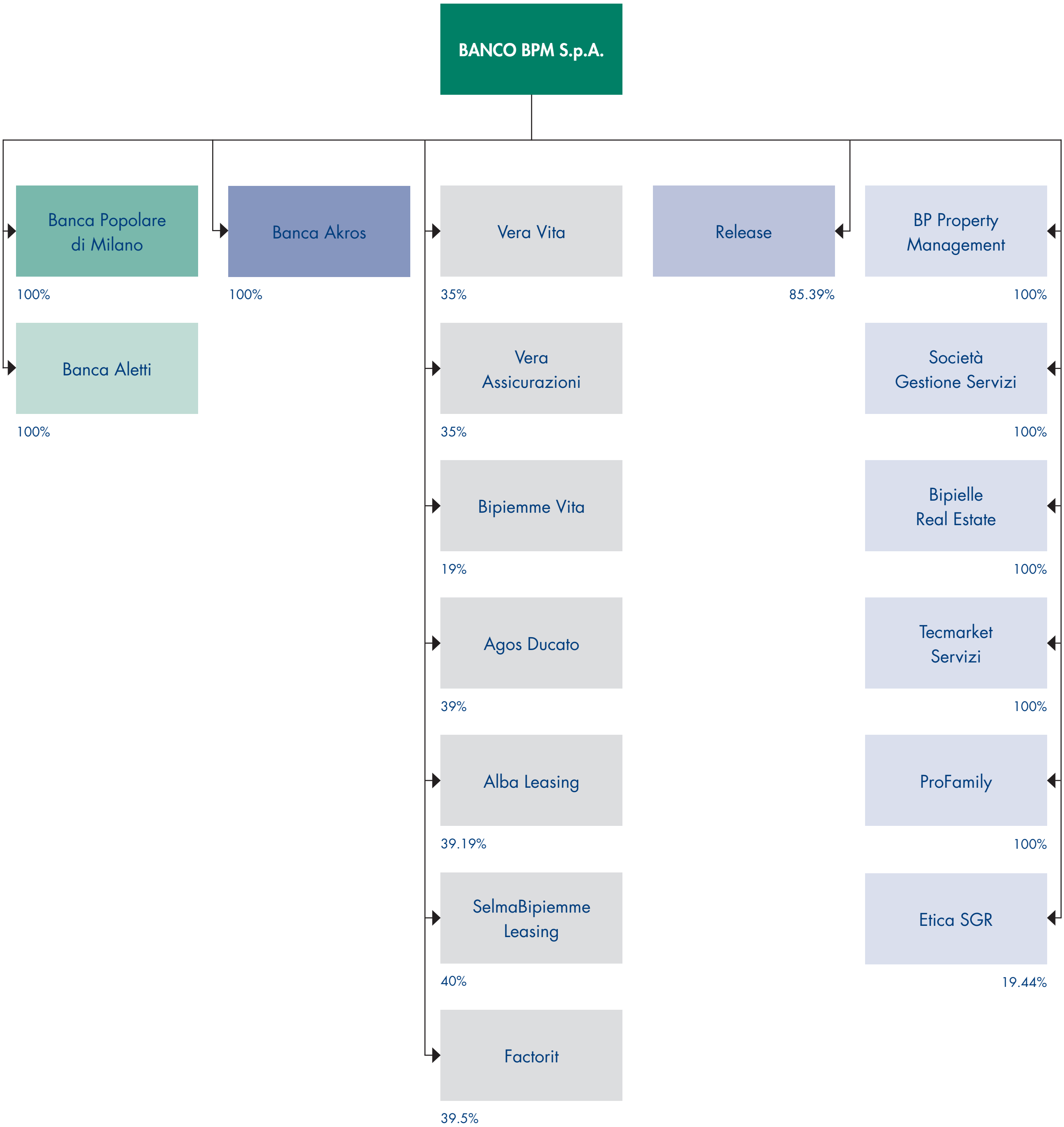
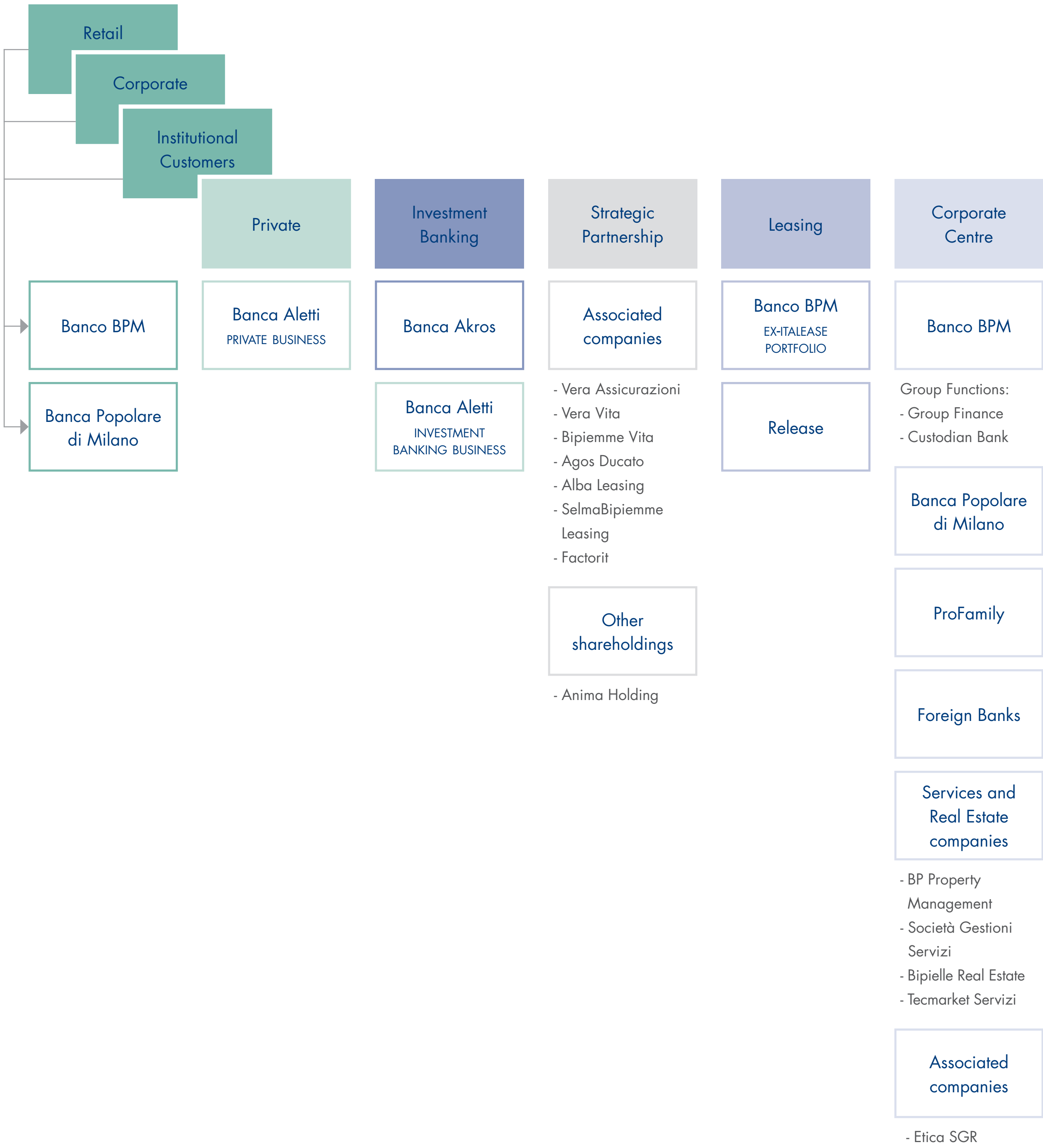


GROUP STRUCTURE: BUSINESS LINES



GROUP TERRITORIAL NETWORK

N° BRANCHES

●	NORTH	1,783
●	CENTRE	347
●	SOUTH AND ISLANDS	189
	TOTAL	2,319

Banco BPM Group Branches in Italy	Number
Banco BPM	1,661
Banca Popolare di Milano	604
Banca Aletti	51
Banca Akros	3
Total (*)	**2,319**

(*) Effective 1 July 2018, the Group has closed 310 branches which were identified as the least performing and/or subject to territorial overlap, as part of the Commercial Network streamlining process.

Presence abroad

The Group's foreign operations include a subsidiary company, Banca Aletti Suisse, and Representative Offices in China (Hong King and Shanghai) and India (Mumbai).

Group financial highlights and economic ratios

Highlights

The highlights and main ratios of the Group, calculated based on the reclassified financial statements, are presented below. The underlying calculations for these are illustrated in the “Results” section of this Report.

(in millions of euro)	1st half 2018 IFRS 9	1st half 2017 IAS 39 (*)	Change
Income statement figures			
Financial margin	1,256.1	1,141.7	10.0%
Net fee and commission income	927.5	1,019.4	(9.0%)
Operating income	2,447.3	2,305.9	6.1%
Operating expenses	(1,390.7)	(1,454.1)	(4.4%)
Profit (loss) from operations	1,056.6	851.9	24.0%
Profit (loss) before tax from continuing operations	503.7	129.8	287.9%
Income (loss) for the period without Badwill	352.6	94.2	274.2%
Parent Company’s net income (loss) for the period	352.6	3,170.4	(88.9%)

(*) The figures for the previous period, originally calculated in compliance with IAS 39, have been reclassified to provide a like-for-like comparison. Provided in the attachments is a reconciliation schedule between the reclassified income statement published in the interim financial Report, as at 30 June 2017 and the reclassified income statement given here.

(in millions of euro)	30/06/2018 IFRS 9	01/01/2018 IFRS 9	31/12/2017 IAS 39	Changes on 31/12/2017
Balance sheet figures				
Total assets	167,029.1	160,206.1	161,206.8	3.6%
Loans to customers (gross)	117,073.5	120,000.7	120,453.0	(2.8%)
Financial assets and hedging derivatives	41,048.6	34,884.8	34,533.2	18.9%
Shareholders' equity	10,834.0	10,834.6	11,900.2	(9.0%)
Customers’ financial assets				
Direct funding	105,505.6	107,525.1	107,509.8	(1.9%)
Indirect funding	93,597.5	101,328.5	101,328.5	(7.6%)
- Asset management	59,168.6	60,545.2	60,545.2	(2.3%)
- Mutual funds and SICAVs	38,324.3	37,605.3	37,605.3	1.9%
- Securities and fund management	5,739.2	6,941.1	6,941.1	(17.3%)
- Insurance policies	15,105.1	15,998.8	15,998.8	(5.6%)
- Administered assets	34,428.9	40,783.3	40,783.3	(15.6%)
Information on the organisation				
Average number of employees and other staff (*)	22,116	23,227	23,227	
Number of bank branches	2,319	2,320	2,320	

(*) Weighted average of full-time equivalent personnel resources, calculated on a monthly basis. This does not include the Directors and Statutory Auditors of Group Companies.

Financial and economic ratios and other Group figures

	30/06/2018 IFRS 9	31/12/2017 IAS 39 (*)
Alternative performance measures		
Profitability ratios (%)		
Annualised ROE (**)	6.73%	4.92%
Annualised Return On Assets (ROA) (**)	0.42%	0.35%
Financial margin / Operating income	51.33%	50.84%
Net fee and commission income / Operating income	37.90%	43.50%
Operating expenses / Operating income	56.83%	65.22%
Operational productivity figures (1000s of euro)		
Loans to customers (gross) per employee (**)	5,293.6	5,185.9
Annualised operating income per employee (***)	221.3	193.0
Annualised operating expenses per employee (***)	125.8	125.9
Credit risk ratios (%)		
Net bad loans / Loans to customers (net)	3.39%	6.02%
Unlikely to pay / Loans to customers (net)	5.44%	5.99%
Net bad loans / Shareholders' equity	33.35%	54.52%
Other ratios		
Financial assets and hedging derivatives / Total assets	24.58%	21.42%
Derivative assets / Total assets	1.34%	1.33%
- trading derivatives / total assets	1.24%	1.18%
- hedging derivatives / total assets	0.11%	0.15%
Net trading derivatives (****) / Total assets	0.72%	0.78%
Gross loans / Direct funding	110.96%	112.04%
Regulatory capitalisation and liquidity ratios		
Common equity tier 1 ratio (CET1 capital ratio)	12.93%	12.36%
Tier 1 capital ratio	13.13%	12.66%
Total capital ratio	15.77%	15.21%
Tier 1 capital ratio / Tangible assets	5.33%	6.01%
Liquidity Coverage Ratio (LCR)	137.93%	125.61%
Leverage ratio	4.95%	5.59%
Banco BPM stock		
Number of outstanding shares	1,515,182,126	1,515,182,126
Official closing prices of the stock		
- Final	2.512	2.620
- Maximum	3.146	3.508
- Minimum	2.100	2.162
- Average	2.834	2.863
Annualised basic EPS (**)	0.467	0.368
Annualised diluted EPS (**)	0.467	0.368

(*) The ratios are determined by excluding the merger difference (badwill in the income statement) and with reference to the data calculated in compliance with IAS 39.

(**) The annualised result does not represent a forecast of profits for the year.

(***) Arithmetic average calculated on a monthly basis in terms of full-time equivalent resources, as shown in the previous table. This does not include the Directors and Statutory Auditors of Group Companies.

(****) The aggregate of net trading derivatives corresponds to the mismatch, in absolute terms, between the derivatives included under Balance Sheet item 20 a) of assets, "Financial assets designated at fair value through profit and loss - held for trading", and item 20 of liabilities, "Financial liabilities held for trading".

The alternative performance indicators (APIs) shown in the table above have been identified by the directors to facilitate the understanding of the economic and financial performance of the Banco BPM Group's operations. The APIs are not envisaged in IAS/IFRS and, although they are calculated based on financial statement data, they are not subject to a full or limited audit.

The above-mentioned indicators are based on the guidelines of the European Securities and Markets Authority (ESMA) of 5 October 2015 (ESMA/2015/1415), applicable as of 3 July 2016, and incorporated in CONSOB communication no. 0092543 of 3 December 2015.

In this regard, it should be specified that for each API, the calculation formula has been provided, and the figures used in the calculations can be identified using the information contained in the table above or in the reclassified financial statements provided in the "Results" section of this report.

Interim report on operations

ECONOMIC SCENARIO

The international economy

In the first half of 2018, the global economy, supported by monetary policies that were generally still accommodating, continued the robust growth of the previous year: in May, the OECD estimated growth in global GDP for 2018 at +3.8% (+3.7% in 2017). Compared to the forecasts at the beginning of the year, however, the speed of expansion in different areas has slowed in recent months, albeit to a limited extent. Various factors are contributing to this reduced dynamism. First, there was a modest slowdown in international trade, the main driver of global expansion in 2017. The World Bank estimates an increase of +4.3% in the whole of 2018, compared to 4.8% in 2017, the highest rate of expansion in the last six years. As yet, the Trump administration's introduction of protectionist measures in trade, starting from the second quarter, has had a limited impact on the international trade flows of the countries involved, but it is affecting the expectations of companies at a global level, possibly leading them to display greater prudence in their investment plans. In addition, outlooks from this perspective are not good. The dispute has worsened with the escalation of retaliatory measures put in place by the countries, primarily China, hit by restrictions. Furthermore, in Europe, several idiosyncratic factors came to the fore, including the growing risks of a disorganised Brexit, adverse weather conditions in Germany and peaks in labour conflicts and strikes in France. The increase in US interest rates and the related strengthening of the dollar against many currencies have resulted in tighter financial conditions for emerging economies during the period in question, which has contributed to making their economic recovery less synchronised with that of industrialised countries. The significant rise in oil prices has also affected several important advanced economies, which are now close to the levels of maximum potential growth, slowing down the trend due to higher production costs.
Specifically, in the first quarter, GDP growth in the United States was lower than the previous quarter, +2.0% annualised compared to +2.9% in the fourth quarter of 2017. In particular, the slowdown in consumer spending played a significant part (+0.9% compared to the previous +4.0%), also due to delays in tax refunds and the statistical effect of seasonality, which has already been noted several times in recent years, in the estimates of the first quarter. Gross fixed investments showed brilliant performance (+7.5%), accompanied by an increase in public spending of +1.3% and a rise in exports of +3.6%, partially compensated by an increase in imports of +3.2%. For the second quarter, the latest estimates available indicate annualised growth of +4.1%, mainly owing to the support of consumption and non-residential investments, confirming the still dynamic pace of US economic growth, which should reach an overall expansion rate of 2.9% for 2018. On the consumer price front, in May, the increase stalled at 2.8%, compared to the previous twelve months, continuing the upward trend which began at the beginning of the year. In June, unemployment rose from 3.8% in May to 4.0%, despite the 213,000 new jobs in non-agricultural sectors. This increase should be interpreted positively, as it reflects an increase in the number of people who were previously discouraged now looking for employment due to the more lively and favourable environment.
The Chinese economy, on the other hand, saw sustained growth, especially in the first quarter, with GDP (+6.8% over twelve months) driven by robust consumption and sustained by public spending measures and the strong performance of exports, compensating for more sluggish activity in real estate, in light of greater restrictions on non-bank credit and tighter financial conditions. This is in line with the estimates of annual GDP growth of 6.5% and inflation of 2.5% (from 2.9% in 2017).
In contrast, Japanese growth marked a downturn. GDP fell in the first quarter compared to the previous one (-0.6% annualised quarterly) for the first time in two years, affected by a slowdown in consumption (-0.4%) and residential construction spending (-7.2%), most likely also dampened by adverse weather conditions during the period. Initial data indicates moderate recovery in the second quarter, bolstered by the accommodating monetary policy. In May, inflation, also boosted by a sudden increase in wages for the month (+2.1% yoy), reached +0.7% per annum, a level so far from that target that the Bank of Japan would not define a time horizon for achieving it.
Lastly, countries exporting commodities experienced strengthening economic activity. Russia benefited from the positive trend in the prices of energy commodities, particularly oil. Brazil, also due to the continued support of monetary policy, despite political uncertainty and the reversal of the previously favourable external financial conditions, saw labour market conditions and household consumption improve, without any significant inflationary trends.
Despite the increase in energy prices and because of relatively moderate wage pressures in advanced economies, consumer inflation on a global scale has confirmed substantial sustainability. In OECD countries, it rose by 2.3% in April, and it actually slowed marginally, net of energy and food items, to 1.9%.

The economy in Europe and Italy

In the euro zone, economic growth slowed, while still remaining relatively high. In the first quarter, GDP rose by 0.4% qoq and +2.5% yoy (+0.7% qoq and +2.8% yoy in the third quarter of 2017). The slowdown, which also reflects the difficulties experienced by several major emerging economies, was primarily due to foreign demand, -0.4% qoq to exports, with a negative contribution to the variation of GDP (-0.2% compared to +1.0% previously), and the sluggishness of investments (+0.5% qoq compared to +1.3% previously, and +0.1% to GDP growth), especially in the capital goods and plant design sectors: two components, exports and investments, which have also made up the backbone of the accelerated growth seen in 2017. Nonetheless, economic expansion remained lively, yet mainly dependent on household consumption, which strengthened (+0.5% qoq, +1.5% yoy and +0.3% the contribution to growth), and of inventories, which accumulated in the period (the contribution of GDP growth went from -0.1% in the 4th quarter of 2017 to +0.2% in the first quarter of 2018). In the second quarter, the economic trend stabilised, and production in the construction sector increased by 1.8% in April compared to March, while industrial production in May increased by 1.3% compared to April, owing to durable and non-durable goods (both components up +2.1% compared to +1.6% for intermediate goods and +0.7% for capital and investment goods). The preliminary estimate of Eurostat for the period shows GDP growth of +0.3% qoq (+2.1% yoy), which was affected by the spread of the reduced dynamism of exports along the supply chains and the tensions connected to restrictions in international trade implemented by the Trump administration from March onwards. The expectation of a dynamic recovery of GDP for the second half of the year, especially in the investment component, should allow for GDP growth for 2018 overall to consolidate at an estimated +2.1%.
Despite the reduced dynamism of the economic environment, consumer prices strengthened. In June, inflation reached 2.0%, based on available estimates, compared to 1.3% at the beginning of the year and at June 2017, also reflecting a more robust trend in labour costs (+2.0% in the first quarter of 2018 compared to +1.4% in the fourth quarter of 2017). Employment also grew, + 0.4% qoq in the first quarter (+1.4% yoy), reflecting the continuing good trend in production.
In Italy, after the sustained trend in the purchase of industrial equipment during 2017, it was expected that the positive trend in the investment cycle would consolidate with the spread of the expansive wave to the other manufacturing sectors, particularly capital goods, and to the entire mechanical sector. Conversely, the weak trend in machinery, equipment and vehicle investments in the first quarter (-2.9% qoq, yet still up +11.4% compared to the same period during the previous year) slowed down the trend in gross fixed investments (-1.4% qoq and +4.5% yoy), despite the continued performance of vehicles. However, this slowdown has only partially dampened the force of domestic demand, which was still fuelled during the period by household consumption (+0.4% qoq and +0.8% yoy), also supported by the moderate expansion of fiscal policy, as well as good performance in the labour market. Exports also slowed (-2.1% compared to the previous quarter) more than in the euro zone, mainly due to a decrease in non-EU demand. Therefore, GDP grew by +0.3% compared to the previous quarter and by 1.4% yoy, disappointing expectations of an acceleration compared to the fourth quarter of 2017 (+0.3% qoq and +1.6% yoy in the quarter in question).
Inflation also accelerated on a national level, reaching 1.3% per annum in June (+0.8% core inflation compared to 0.6% at the beginning of the year) from +0.6% at the beginning of the year (January) and +0.8% in March. Employment growth continued in May, increasing by 315,000 since the beginning of the year (+1.4%) and by 2.0% on a yearly basis, while unemployment stood at 10.7% (10.8% in December 2017).
In the second quarter, economic indicators for the manufacturing sector alternated between signs of slowdown and indications of greater dynamism. In May, according to ISTAT (the Italian Statistics Agency) estimates, industry turnover grew by 1.7% qoq, increasing for the third consecutive month, while industrial production improved by 0.7%, after a drop of 1.3% in April. The first flash estimate available for GDP for the second quarter shows stabilisation (+0.2% qoq and +1.1% yoy). However, the slowdown in the economic situation recorded in the first months of the year led the most accredited economic observers to conservatively revise their GDP expansion estimates for 2018 overall: the Prometeia Institute reduced them to +1.2%, from the previous +1.4%, assuming an increase in exports of 2.3% compared to 2017, and an increase in total domestic demand of +1.4%. The latter should be stimulated by an acceleration in gross fixed investments in the second half of the year, also due to moderate recovery in construction investments, expected to increase by +1.3% on an annual basis.

Regarding public finances, the process of fiscal consolidation continued over the period. At the end of the first quarter, PA net borrowing as a ratio of GDP stood at 3.5%, 0.5% lower than the same quarter in 2017. Indeed, total revenues for the first quarter of 2018 increased year-over-year by 1.3%, while expenditures saw an increase of 0.2%. However, the April Economic and Financial Document (DEF) issued by the outgoing government does not include the program framework, but only provides for an update on macroeconomic estimates—under current legislation the debt to GDP for the whole of 2018 would be 1.6%.

Monetary policy and the financial markets

As noted, the trend of the monetary policies implemented by the major global central banks remains accommodating, despite the slightly more restrictive stance already adopted by the Federal Reserve and also predicted, regarding the extraordinary monetary policy measures, for the European Central Bank. In June, the former raised the reference interest rate (Fed Funds) to 1.75%, completing the seventh increase in official interest rates since the end of 2015 (in March, the minimum Fed Funds rate had been raised to 1.5%), and the currently prevailing expectations are for two more quarterly increases in September and December to implement Quantitative Tightening (QT). The ECB, while reiterating its commitment to purchase securities under the APP (Asset Purchase Plan) for a net amount of 30 billion euro per month until September 2018, has stated that from that date the amount of securities purchased will decrease to 15 billion euro until December 2018 if the inflation trend remains unchanged over the medium term. Purchases will stop from the beginning of 2019, but the policy of reinvesting capital repaid at maturity from securities purchased under the APP will continue. Concerning interest rates, the ECB has confirmed its intention to leave them at their current levels for as long as necessary to attain an inflation rate that is in line with the 2% target and, in any case, at least until the summer of 2019. On the other hand, official interest rates increased in Argentina and Turkey, coinciding with the deterioration of their financial environments, and remained very weak in Japan.
Despite the favourable monetary policy guidelines, international financial conditions have become tighter, and while the main markets of industrialised countries closed the period with a positive outlook, share and bond prices became more volatile. After an initial sharp rise in the first few weeks, the stock markets embarked on a phase of correction, triggered by fears of a more marked rise in expectations of US official interest rates and by a significant increase in long-term interest rates on US T-bonds. The sudden and disorderly overburden of short positions on the volatility of the US stock market temporarily destabilised it in February. However, the initial acute phase of turbulence was absorbed and followed by a prompt recovery of previous course levels as early as March. In the euro zone, heightened uncertainty, followed by the results of the Italian political conference, has led to a return to volatility in Treasury markets. From mid-May, fears of a less rigorous national economic policy have driven the spread between 10-year Italian BTPs (*Buoni del Tesoro Poliennali* - Multi-year Treasury Bonds) and German Bunds to exceed 290 bps in the intraday at the end of May and the yield on ten-year BTPs to over 3% in a few sessions. Tensions from Italian Government securities partially affected other domestic markets. Within the Italian stock market, price volatility rose and premiums on national banking credit default swaps (CDS) rose in the second quarter of 2018 by 56 bps on average, despite the improved economic and financial conditions of the principle intermediaries. Due to the active presence of the ECB in the sovereign debt market and positive economic growth rates, the difficulties of the Italian Treasuries did not affect other partners within the euro zone. Thus, the impact was reduced, and the spread narrowed below 250 bps. at the end of the period. The strengthening of the dollar, especially against the euro, which occurred in the meantime, combined with other effects of the rise in medium/long-term US interest rates, exacerbated the financial conditions of many emerging economies; capital flows towards the latter slowed, while the spreads on their bonds increased. Turkey and Argentina were particularly negatively affected and considerably weakened by elevated external financing needs and by the lively trend in domestic consumer prices. In the US, at the end of the period, returns on ten-year T-bonds rose by over 50 basis points from the beginning of the year, reaching just over 2.8% at the end of the period, after having reached performance levels in excess of 3% for some sessions, the psychological threshold that has not been broken since 2011. Despite the rise in long-term interest rates, at the end of June, the S&P 500 index closed at 2,718 points, with a positive performance of +1.7% since the beginning of the year, while the Eurostoxx index fell by 2.2%: The FTSE MIB index of the Italian Stock Exchange also decreased slightly, closing the period at 21,626, with a negative performance of 1.0% since the beginning of the year.

Domestic banking activity

In the first few months of 2018, the increase in loans to households and businesses continued, with a moderate acceleration already seen in January, due to an increase in demand connected with the consolidation of the economic environment and with the strengthening of productive investments. The trend in loans to households remained solid, both for the purchase of homes and for consumer credit. Systemic risks continued to decrease. The transfer/sale of non-performing loans by various intermediaries led to an improvement in asset quality. Consequently, the percentage of non-performing loans out of total loans continued to fall. Furthermore, the flow of new non-performing loans in relation to total loans, calculated on an annual basis, returned to pre-crisis levels.

In this context, in June 2018, according to data released by the ABI - Italian Banking Association, bank lending to the private sector (measured including loans not recorded in bank balance sheets, since they are securitised, and net of changes in stocks not connected with transactions) grew by 2.5% yoy, while lending to households and businesses alone increased by +2.6% per annum. These figures reflect not only the constant growth rate of loans to households, whose stock in May (latest available data) increased by 2.8%, the same level as the last five months, but also the renewed dynamism of those to businesses, which rose by 1.2% yoy after reaching +2.2% in April, the highest figure since 2011.
For businesses, the growth in demand for credit was driven in the first quarter of the year by requests relating to inventories and working capital and, secondly, for mergers, incorporations and restructuring of corporate structures, while requests for loans to refinance debt were stable. As shown by the Bank Lending Survey concerning bank credit in the euro zone for the first quarter of 2018, the supply of credit was characterised by a slight easing of supply policies for loans to households and to businesses, partly due to competitive pressures among intermediaries. Consequently, margins applied to average loans continued to decline, and average amounts of finance provided to businesses further increased.

During the first half of the year, the trend in total loans requested by households was further strengthened; both mortgage loans for the purchase of homes, supported by an increase in property sales, and the consumer credit component made a positive contribution, without particular geographical differences. In particular, mortgage loans benefited from the still favourable conditions; the interest rate on loans in euro to households for the purchase of homes reached an all-time low, falling to 1.80% (1.83% in May). Similarly, the interest rates applied to new loans to non-financial companies also reached an all-time low in June 2018, falling to 1.37% (1.43% in May).

In terms of domestic credit quality, in the first quarter, the flow of new non-performing loans as a percentage of total loans, net of seasonal factors and calculated on an annual basis, fell compared to the previous quarter and stood at 1.7%, due in particular to the improvement in loans to businesses (at 2.6% from 3.4% at the end of 2017), primarily in the construction sector.
For all groups classified as being significant for supervisory purposes, in the first quarter of 2018, the ratio of non-performing loans to total loans steadily decreased, both gross and net of adjustments, to 10.8% and 5.1% respectively. These ratios were calculated in accordance with the definition used by the ECB. For the banking system as a whole, in May 2018 (the latest available data) the stock of bad loans fell to 49.3 billion euro, -23% compared to the end of 2017. This favourable trend was also fostered by the adoption - from 1 January 2018 - of the new accounting standard IFRS 9, which replaced standard IAS 39, and led to a substantial increase in the coverage rate for total non-performing loans, which increased over the quarter to 55.4% (50.6% at the end of 2017).
Italian banks' exposure to the public sector of the country also fell considerably during the period, with a year-over-year decrease of 44 billion euro in February. The relative stock thus fell to 295 billion euro, and the ratio out of total assets fell from 9.6% to 8.5%.

The stock of total direct funding from customers (deposits and bonds) as at June 2018 increased both compared to the figure at the end of 2017 (+0.6%) and on an annual basis (+1.8%). In keeping with the past, the overall result for the period comes from the constant growth in the various types of short-term deposits and offset the still decreasing trend in the bond component of bank deposits. Deposits from resident customers increased by 6.3% per annum at the end of the period, while the change in bonds was -18.3%.

The bank interest spread, calculated as the difference between the average interest rate on loans and the average interest rate on total funding from households and non-financial corporate customers, stood at 1.87% in June 2018 (17 bps lower compared to 2.04% in June 2017). In the same month, the mark-up (calculated as the difference between the average interest rate on the stock of loans to households and non-financial companies and the 3-month Euribor rate) fell to 292 bps (-21 bps compared to the same month of the previous year), while the mark-down (calculated as the difference between the 3-month Euribor rate and the interest rate on total funding), improved by 4 bps, compared to June 2017, moving from the negative amount of 109 bps to 105 bps.

In the first three months of the year, the capital strength conditions of the major banks were stable. Indeed, according to the most recent estimates provided by the Bank of Italy, the Common Equity Tier 1 (CET1) of this sample stood at 13.2% in March 2018, a level almost identical to that reported at the end of the previous quarter (13.3% in December 2017).

Lastly, in May 2018, asset management recorded a -2.4 billion euro flow of net open-end funds, compared to +2.7 billion euro in April. The assets invested in open-ended Italian and foreign mutual funds at the end of May decreased to 1,009.3 billion euro from 1,013.3 billion euro at the end of 2017, a phenomenon attributable to the correction that occurred on the markets during the period.

SIGNIFICANT EVENTS DURING THE PERIOD

The main events which occurred during the first half of the year are described below.

Process to define the corporate and organisational structure of the Banco BPM Group

Reorganisation of the bancassurance sector

During first half of the year, the reorganisation process of the Bancassurance segment–which began the previous year and was formalised with agreements involving the sale of a 65% share in Popolare Vita and Avipop Assicurazioni and the start of a strategic partnership between Banco BPM and Cattolica lasting 15 years–continued.
On 29 March, following the issue of the required authorisations by the competent authorities, Banco BPM completed the purchase of 50% + 1 share of Avipop Assicurazioni and Popolare Vita for a total value of 803.4 million euro, taking its stake in the share capital of the two companies to 100%. On the same date, 65% of the total share capital held by the Group in Avipop Assicurazioni and Popolare Vita was sold to Cattolica Assicurazioni for 819.6 million euro.
In order to complete the reorganisation of the segment, the extraordinary shareholders' meetings of Avipop Assicurazioni and Popolare Vita approved the adoption of new by-laws and the change of the company names to Vera Assicurazioni S.p.A. and Vera Vita S.p.A..
As a result of the above-mentioned transaction, the Banco BPM Group benefited from a gain of 174.7 million euro, which is recognised in the income statement of the first quarter of 2018.

Reorganisation of the commercial network

On 1 January 2018, the new commercial network model became fully operational, an important project that involved the entire commercial network and the definition of new professional roles.

The model is based on the principles of customer centrality and high service levels through a specialised offer and a greater focus on commercial structures; territorial proximity through the configuration of 8 Territorial Offices for specific reference regions, to which 45 Areas report, which in turn guarantee support and coordination for the Branches (subdivided into Hubs, Coordinated Independent Units, Spokes and Independent Units); rapid decision-making and proactive satisfaction of customer needs.

The project also included the reorganisation of the Corporate Network into 5 Markets and 18 Corporate Centres to enhance the specialisation necessary for the management of Corporate customers. The organisational structure is divided into two business units (Corporate and Large Corporate) and provides for the presence of product/specialist principals for Origination, Structured Finance, Foreign Operations and Trade Finance.

This reorganisation process also underlies the streamlining of the commercial network which, with effective from 1 July, saw the closure of 310 branches that were identified among the predominately underperforming spoke branches and/or by territorial intra-legal entity overlaps, identifying–in accordance with the new Network model–the best reallocation for customers with the aim of minimising inconvenience and retraining around 750 personnel, also to manage the turnover of excess resources.

Reorganisation of the Asset Management segment

On 7 February 2018, as part of the restructuring and streamlining of the Banco BPM Group and its capital management operations related to the strategic restructuring of the asset management sector, consequent to the sale of Aletti Gestielle SGR completed at the end of 2017, Banco BPM defined, *inter alia*, two agreements aimed at transferring the delegated insurance asset management mandates and selling the custodian bank and fund administration activities.

Regarding the first transaction, the Parent Company signed an agreement with Anima Holding that provides for the sale from Banca Aletti to Anima SGR of the delegated insurance asset management mandates carried out on behalf

of the insurance joint ventures linked to the former Banco Popolare bancassurance network, and the definition of a twenty-year partnership related to the conferment to Anima SGR of the delegated management of the assets underlying the insurance products placed by the Banco BPM Group network.
Based on this agreement, Banca Aletti maintains the activity of Banca Custodian internally for deposits relating to the transferred mandates.
The transaction, which was completed on 29 June, led to a positive impact on the income statement in the second quarter equal to 113.6 million euro, before tax.

The second agreement, on the other hand, provides for the sale to BNP Paribas Securities Services of Banco BPM's Custodian Bank division, which consists of the services of the custodian bank, the fund administration and the payment agent for mutual investment funds, closed-end funds, pension funds and real estate.
The sale, which is expected to be completed at the end of September, will amount to 200 million euro, to be paid in cash at the closing, and will have a positive impact on capital ratios and lead to a substantial reduction in operating costs.

Demerger of the Banca Akros Private Banking business unit to Banca Aletti

In March, the deed was signed for the demerger of the Banca Akros Private Banking business unit to Banca Aletti, with particular reference to the contractual relationships related to administered and managed assets business, employment relationships of personnel of the unit, the Rome branch and any other contract relating to the branch.
The demerger was completed on April 1.

Simplification of the Group's corporate structure

During the period, the procedure for winding up the SPE Pami Finance S.r.l. was completed, with it being struck off the Milan Companies Register.
Furthermore, in May the deed was signed for the sale of the associated company Renting Italease S.r.l., 50% owned by Bipielle Real Estate and consolidated using the equity approach.
These operations did not have an impact on the balance sheet or income statement of the Group.

On 26 March 2018, the operation to group the ordinary shares of BPM was completed, in a ratio of 1 new ordinary share for every 25,000 shares held. The operation entailed the elimination of the express nominal value of the shares, by grouping the 126,648,570 existing ordinary shares into 5,065 new ordinary shares with no nominal value.
Due to the aforementioned transaction, Banco BPM holds 100% of the share capital of BPM as of 26 March 2018.

As part of the initiatives to streamline the Group's corporate and operational structure, there are also plans to merge the subsidiaries BPM S.p.A., SGS and BP Property Management into Banco BPM, approved by their respective Boards of Directors on 27 March (for BPM S.p.A.) and 9 May (for the two consortia).
These operations respond to the need to simplify and streamline the structure, optimise and make the most of resources and reduce costs and will be carried out in accordance with the simplified procedures established for wholly-owned companies, without the determination of an exchange rate and without the preparation of the explanatory report by the Board of Directors.
It is expected that the mergers of the two consortia will take effect in 2019, after obtaining the required authorisations from the competent authorities, effective 1 January 2019 for accounting and tax purposes. The merger of BPM S.p.A., on the other hand, is planned for the last quarter of 2018 and will take effect for accounting and tax purposes from 1 January 2018.

The business plan and derisking activities

Assignment without recourse of bad loans

As part of the wider de-risking process, last 31 May, the Parent Group approved the sale of a portfolio of bad loans originating from Group banks with a gross nominal value of approximately 5.1 billion euro to the SPE Red Sea SPV S.r.l..

This sale, known as "Project Exodus", was carried out via a securitisation transaction, for which the Parent Company requested the issue of a State guarantee on the senior securities issued by the SPE pursuant to the Decree Law 18/2016 (GACS).
The operation was completed in June, with the SPE issuing securities totalling approximately 1.9 billion euro, broken down as follows:

- senior securities amounting to 1,656.5 million euro, for which the process for the issue of the guarantee by the Italian government was activated as mentioned above;
- mezzanine securities for 152.9 million euro;
- junior securities for 51 million euro.

The securities were subscribed by Banco BPM, which subsequently sold 95% of the mezzanine and junior securities to a third investor (Christofferson Robb & Company).
With the placement of mezzanine and junior securities, at the end of a competitive process involving the participation of numerous Italian and international investors, the conditions were met to proceed with the derecognition of bad loans sold to the SPE, at a total sale price of 34.3%, a figure that is at the highest levels achieved on the Italian market for this type of transaction.

The transaction is part of the Group's plan to dispose of a nominal amount of 13 billion euro and is in addition to the 4.5 billion euro carried out as from 2016, bringing the remaining portion of planned disposals to 3.4 billion euro.

Other events in the period

Group ratings

Summary table of Banco BPM Group ratings as at 30 June 2018

Rating agency	Type of Rating	Banco BPM
Moody's Investors Service	Long Term on Deposits	Ba1 - Stable outlook
	Long Term on Senior Debt	Ba2 - Negative outlook
	Issuer Rating	Ba2 - Negative outlook
	Short term	NP
	Baseline Credit Assessment	b1
	Counterparty Risk Assessment	Ba1(cr) / NP(cr)
DBRS	Long-Term Issuer Rating	BBB (low) - Negative Trend
	Long Term on Senior Debt	BBB (low) - Negative Trend
	Long Term on Deposits	BBB (low) - Negative Trend
	Short-Term Issuer Rating	R-2 (middle) - Negative Trend
	Short Term on Senior Debt	R-2 (middle) - Negative Trend
	Short Term on Deposits	R-2 (middle) - Negative Trend
	Intrinsic Assessment	BBB (low)
	Support Assessment	SA-3

Summary table of Banca Akros ratings as at 30 June 2018

Rating agency	Type of Rating	Banca Akros
DBRS	Long-Term Issuer Rating	BBB (low) - Negative Trend
	Long Term on Senior Debt	BBB (low) - Negative Trend
	Long Term on Deposits	BBB (low) - Negative Trend
	Short-Term Issuer Rating	R-2 (middle) - Negative Trend
	Short Term on Senior Debt	R-2 (middle) - Negative Trend
	Short Term on Deposits	R-2 (middle) - Negative Trend
	Support Assessment	SA-1

At 30 June 2018, the ratings assigned by Moody's and DBRS to Banco BPM and its subsidiary Banca Akros remained unchanged compared to the end of 2017.

SIGNIFICANT EVENTS AFTER THE END OF THE INTERIM PERIOD

Reorganisation of the Group's corporate structure

On 10 July 2018, the deed was signed for the sale of the entire share held by the subsidiary Bipielle Real Estate in the company Mariner, representing 100% of the share capital. The sale was to BNP Paribas Real Estate Investment Management Italy SGR, as the management company of the alternative closed-end property investment fund reserved for professional investors known as Hita 1, for a consideration in line with the company's book value of approximately 1 million euro.

Changes in officers and directors: renewal of the composition of the Related Parties Committee

Please note that in its meeting on 3 August 2018, the Board of Directors resolved to appoint from among its members Cristina Galeotti as member and Chairman of the Related Parties Committee, until the approval of the 2019 financial statements, replacing Cristina Zucchetti, who maintains the position of Director and member of the Remuneration Committee. The updated composition of the Related Parties Committee is therefore as follows: Cristina Galeotti (Chairperson), Mario Anolli (Deputy Chairperson), Marisa Golo and Costanza Torricelli.

RESULTS

Introduction

The balance sheet and income statement schedules shown below have been reclassified, according to operating criteria, in order to provide clear indications on the Group's general performance based on the economic-financial data that can be determined rapidly and easily.

This report adopts the new IFRS 9 and IFRS 15 accounting standards, as described in the specific section "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers" contained in the Consolidated condensed interim financial statements. Considering the changes introduced with the application of IFRS 9, in order to ensure adequate information on the evolution of the Group's equity and financial situation, the reclassified balance sheet has been prepared providing for comparative purposes and also includes the information as at 1 January 2018 with the adoption of the new accounting standards, in addition to the information relating to 31 December 2017.

More specifically, the reclassified balance sheet as at 30 June 2018 has been adapted to reflect the new accounting categories for financial instruments, as introduced by the fifth update of Bank of Italy Circular no. 262.
In detail, the previous aggregates entitled "Financial assets and hedging derivatives", "Due from banks" and "Loans to customers" have been replaced by the following new aggregates:

- "Loans designated at amortised cost (AC)", which includes the following items:
  - "Loans to banks": these are loans to banks and are recorded under the asset item of the Bank of Italy schedule "40. Financial assets designated at amortised cost: a) due from banks". Therefore, loans represented by securities included in the aggregate of "other financial assets" are excluded;
  - "Loans to customers": this is credit to customers represented by loans, shown under the asset item of the Bank of Italy schedule "40. Financial assets designated at amortised cost: b) Loans to customers". Therefore, loans represented by securities included in the aggregate "Other financial assets" are excluded, with the exception of the exposure represented by senior securities subscribed as part of the securitisation of bad loans originated by the Group (Exodus disposal) amounting to 1,654 million euro.
- "Other financial assets", consisting of the following items:
  - "Financial assets designated at fair value through profit and loss" which includes the financial instruments shown in the portfolios of "Financial assets designated at fair value through profit and loss" and "Hedging derivatives", respectively shown in items 20 and 50 of the assets in the Bank of Italy schedule;
  - "Financial assets designated at fair value through other comprehensive income (OCI)", which corresponds to item 30 of the assets of the Bank of Italy schedule;
  - "Financial assets designated at amortised cost (AC)", which includes credit exposures to banks and customers represented by debt securities (included in item 40 of the assets of the Bank of Italy schedule) with the exclusion of senior securities resulting from the Exodus disposal, as described previously.

Regarding the reclassified liability items, the previous aggregate "Due to customers, debt securities issued and financial liabilities designated at fair value" has been renamed "Direct funding", an aggregate for which separate disclosure is provided between the item "Due to customers" (item 10 b) on the liability statement of the Bank of Italy schedule) and "Debt securities issued and financial liabilities designated at fair value" (items 10 c) and 30 on the liability statement of the Bank of Italy schedule).
For the remaining reclassified balance sheet items, the aggregation criteria illustrated in the 2017 consolidated financial statements have not been changed.

With reference to the reclassified income statement, the adoption of IFRS 9 has led to a redefinition of the aggregates relating to net financial result and to value adjustments for impairment, according to the new categories of financial instruments and the relative measurement criteria. The reconciliation of the new items with the income statement prepared on the basis of Bank of Italy Circular 262 is illustrated below:

- the item "Net financial result" includes results arising from valuation or realisation of all financial instruments, with the exception of credit risk adjustments which are shown separately. Specifically, this item includes dividends on shares classified to the portfolios of financial assets designated at fair value through profit or loss and through other comprehensive income (item 70), profits (losses) on trading and fair value

adjustments in hedge accounting (items 80 and 90), profits (losses) on disposal or repurchase (item 100), with the exception of the result related to the disposal of financial assets designated at amortised cost represented by loans, the profits (losses) on other financial assets and liabilities designated at fair value through profit and loss (item 110);
- the item “Net adjustments on loans to customers” includes item 130 a) “Net adjustments to/recoveries on credit risk related to: a) financial assets designated at amortised cost” relating solely to the component represented by loans to customers and the related economic results from the disposal of the same (included in item 100 a) “Profits (losses) on disposal or repurchase of financial assets designated at fair value through profit and loss”);
- the item “Net adjustments on securities and other financial assets” is represented by the expected losses recognised on securities and on loans to banks classified in the portfolios of “Financial assets designated at amortised cost” (corresponding to item 130 b) “Net adjustments to/recoveries from credit risk related to financial assets designated at fair value through other comprehensive income” and the residual balance of the aforementioned item 130 a) after deducting the component relating to loans to customers);
- the reclassified item “Net provisions for risks and charges” corresponds to item 200 of the income statement schedule required by Bank of Italy Circular no. 262 and also includes provisions for commitments and guarantees given.

For the remaining items in the reclassified income statement, the aggregation and reclassification criteria illustrated in the 2017 consolidated financial statements have not been changed, with the exception of the ordinary and extraordinary charges introduced for banks under the single and national resolution funds (SRF and NRF) and the deposit guarantee scheme (DGS) which, starting from this consolidated interim report, are shown, net of tax, in a separate item in the reclassified income statement called “Charges related to the banking system, net of taxes”.
It should also be noted that, in order to ensure a like-for-like comparison, the expenses and income of the previous periods for the subsidiary Aletti Gestielle SGR, sold in December 2017, have been reclassified under the separate item “Profit (loss) from discontinued operations”, in line with the retrospective representation required by the IFRS 5 accounting standard for discontinued operations, already made in the financial statements at 31 December 2017.
Attached to this report is a reconciliation schedule between the reclassified income statement published in the consolidated interim financial report as at 30 June 2017 and the reclassified income statement restated for comparative purposes included in this document.

Also note that, as specifically permitted by the IFRS 9 accounting standard (par. 7.2.15), Banco BPM has exercised the right not to recalculate the balances for the previous year by applying the new valuation criteria introduced by IFRS 9 from 1 January 2018. It should be noted that, in order to facilitate a more like-for-like comparison:
- in addition to the balance sheet balances at 31 December 2017, the reclassified balance sheet also shows the balances at 1 January 2018, recalculated in compliance with the IFRS 9 and IFRS 15 accounting standards. A reconciliation schedule between the reclassified balance sheet as at 31 December 2017 and the restated balances as at 1 January 2018 is attached;
- in the preparation of the reclassified income statement, the economic results of previous periods have been restated insofar as possible based on the available information. More specifically:
  - the “Net financial result” of the previous periods under comparison was restated to include adjustments for impairment of shares classified in the former portfolio of “Financial assets available for sale”, previously included in the aggregate of “Net adjustments on receivables due from banks and other assets”;
  - the item "Net adjustments on loans to customers" corresponds to the previous aggregate "Net adjustments on loans to customers", net of value adjustments on securities valued at amortised cost, reclassified to the item "Adjustments for credit risk: securities and other assets" and value adjustments on guarantees and commitments now reclassified to the item "Net provisions for other risks and charges";
  - the item “Net adjustments on securities and other financial assets” corresponds to the previous aggregate “Net adjustments on receivables due from banks and other assets”, net of value adjustments on shares but increased by value adjustments on debt securities designated at amortised cost, as shown in the previous points;
  - the item "Net provisions for other risks and charges" corresponds to the same item in the previous aggregate and includes value adjustments on guarantees and commitments.

Additionally, with reference to the representation of the interest margin, it should be noted that the IFRS 9 accounting principle states that interest accrued on impaired financial assets (Stage 3) must be recorded in the financial

statements on the basis of the amortised cost method, i.e. on the basis of the effective interest rate calculated taking into account the expected cash flows. The standard also states that the value recoveries on receivables deriving from the passing of time (time value) must also be included in interest margin. As a result of the adoption of these new rules on exposure, the interest margin for the first half of 2018 increased by 128.9 million euro overall due to the combined effect of the inclusion in this aggregate of recoveries from the time until 31 December 2017 that were shown within the aggregate "net value adjustments on loans and the net recognition of interest accrued on exposures classified as unlikely to pay" (until 31 December 2017 the portion of interest considered non-recoverable was recognised within the item "Net adjustments on receivables").
As described in detail in the "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers" of the Consolidated condensed interim financial statements, the adoption of IFRS 9 has had a significant impact on both the classification and measurement of financial instruments. In addition, the new impairment model introduced by the standard has led to profound changes both in the scope and in the calculation of value adjustments for both performing and impaired loans. Consequently, the reclassified figures (balance sheet and income statement) for the administrative periods compared with the conventional methods described above are not determined on a consistent basis.

Consolidated income statement figures

Reclassified consolidated income statement

Reclassified income statement items (in thousands of euro)	1st half 2018	1st half 2017 (*)	Changes
Interest margin	1,180,109	1,059,756	11.4%
Profits (losses) on investments in associates and companies subject to joint control carried at equity	75,998	81,939	(7.3%)
Financial margin	**1,256,107**	**1,141,695**	**10.0%**
Net fee and commission income	927,513	1,019,379	(9.0%)
Other net operating income	154,179	44,678	245.1%
Net financial result	109,490	100,177	9.3%
Other operating income	**1,191,182**	**1,164,234**	**2.3%**
Operating income	**2,447,289**	**2,305,929**	**6.1%**
Personnel expenses	(879,149)	(913,430)	(3.8%)
Other administrative expenses	(414,589)	(431,348)	(3.9%)
Net value adjustments on property and equipment and intangible assets	(96,946)	(109,289)	(11.3%)
Operating expenses	**(1,390,684)**	**(1,454,067)**	**(4.4%)**
Profit (loss) from operations	**1,056,605**	**851,862**	**24.0%**
Net adjustments on loans to customers	(686,451)	(647,020)	6.1%
Net adjustments on securities and other financial assets	635	(79,177)	
Net provisions for risks and charges	(45,671)	(9,137)	399.8%
Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments	178,550	13,301	insignificant
Profit (loss) before tax from continuing operations	**503,668**	**129,829**	**287.9%**
Taxes on income from continuing operations	(87,257)	(43,776)	99.3%
Charges related to the banking system, net of taxes	(67,428)	(45,008)	49.8%
Profit (loss) from discontinued operations	4	45,793	(100.0%)
Income (loss) attributable to minority interests	3,590	7,394	(51.4%)
Income (loss) for the period without Badwill	**352,577**	**94,232**	**274.2%**
Merger difference (Badwill)		3,076,137	
Parent Company's net income (loss)	**352,577**	**3,170,369**	**(88.9%)**

(*) The figures for the previous period have been reclassified to provide a like-for-like comparison.

Reclassified consolidated income statement – Quarterly changes

Reclassified income statement items *(in thousands of euro)*	**FY 2018**		**FY 2017**			
	Q2	**Q1**	**Q4 (*)**	**Q3 (*)**	**Q2 (*)**	**Q1 (*)**
Interest margin	584,998	595,111	528,768	524,923	511,149	548,607
Profits (losses) on investments in associates and companies subject to joint control carried at equity	33,413	42,585	45,166	38,931	40,354	41,585
Financial margin	**618,411**	**637,696**	**573,934**	**563,854**	**551,503**	**590,192**
Net fee and commission income	450,993	476,520	472,096	458,935	503,605	515,774
Other net operating income	130,029	24,150	24,738	29,401	14,362	30,316
Net financial result	80,182	29,308	41,915	12,957	63,320	36,857
Other operating income	**661,204**	**529,978**	**538,749**	**501,293**	**581,287**	**582,947**
Operating income	**1,279,615**	**1,167,674**	**1,112,683**	**1,065,147**	**1,132,790**	**1,173,139**
Personnel expenses	(437,060)	(442,089)	(420,796)	(450,628)	(456,711)	(456,719)
Other administrative expenses	(203,102)	(211,487)	(204,704)	(236,303)	(233,055)	(198,293)
Net value adjustments on property, plant and equipment and intangible assets	(49,020)	(47,926)	(95,466)	(62,160)	(56,406)	(52,883)
Operating expenses	**(689,182)**	**(701,502)**	**(720,966)**	**(749,091)**	**(746,172)**	**(707,895)**
Profit (loss) from operations	**590,433**	**466,172**	**391,717**	**316,056**	**386,618**	**465,244**
Net adjustments on loans to customers	(360,212)	(326,239)	(673,127)	(340,816)	(354,530)	(292,490)
Net adjustments on securities and other financial assets	(1,593)	2,228	(12,718)	(48,322)	(70,820)	(8,357)
Net provisions for risks and charges	(20,707)	(24,964)	(9,235)	4,615	(9,641)	504
Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments	(1,104)	179,654	12,064	333	(3,765)	17,066
Profit (loss) before tax from continuing operations	**206,817**	**296,851**	**(291,299)**	**(68,134)**	**(52,138)**	**181,967**
Taxes on income from continuing operations	(61,320)	(25,937)	101,759	34,806	1,122	(44,898)
Charges related to the banking system, net of taxes	(18,391)	(49,037)	(6,187)	(26,069)	-	(45,008)
Profit (loss) from discontinued operations	18	(14)	699,971	16,498	25,790	20,003
Income (loss) attributable to minority interests	2,160	1,430	867	1,397	4,256	3,138
Income (loss) for the period without Badwill	**129,284**	**223,293**	**505,111**	**(41,502)**	**(20,970)**	**115,202**
Impairment of goodwill and client relationships net of taxes	-	-	(1,017,616)	-	-	-
Merger difference (Badwill)	-	-	-	-	-	3,076,137
Parent Company's net income (loss)	**129,284**	**223,293**	**(512,505)**	**(41,502)**	**(20,970)**	**3,191,339**

(*) The figures for the previous periods have been reclassified to provide a like-for-like comparison.

In compliance with the instructions contained in Consob Communication no. DEM/6064293 of 28 July 2006, the following paragraphs provide information on the effects that non-recurrent events or transactions had on the consolidated economic result of the periods compared.

For the purposes of identifying the non-recurrent components, the following approaches are used on the whole:

- the results of disposal transactions relating to all fixed assets (investments in associates and companies subject to joint control, property and equipment) are considered to be non-recurrent;
- gains and losses on non-current assets and asset disposal groups held for sale are considered to be non-recurrent;
- the income statement components associated with improvements, reorganisations, etc. (e.g. expenses for use of the redundancy fund, leaving incentives) are considered to be non-recurrent;
- income statement components for a significant amount which are not destined to reoccur frequently (e.g. fines, impairments of fixed assets, effects associated with legislative changes, exceptional results, etc.) are considered to be non-recurrent;
- impacts on the income statement, as long as significant, resulting from valuation aspects and/or changes in parameters in the application of the valuation methods adopted on an on-going basis are instead considered to be recurrent.

In the light of the above criteria, in addition to the amounts already included in items that are per se non-recurrent (e.g. profit (loss) on assets held for sale), the income statement result for the first half of 2018 was affected by the following non-recurring impacts:

- the item "other net operating income" includes the result deriving from the disposal to Anima SGR of the delegated insurance asset management mandates carried out on behalf of the insurance joint ventures linked to the bancassurance network of the former Banco Popolare for 113.6 million euro;
- the item "other administrative expenses" includes integration expenses of 5.1 million euro;
- the item "net adjustments to property and equipment and intangible assets" includes write-downs due to impairment on fixed assets for 1.7 million euro;
- the item "Disposal of investments in associates and companies subject to joint control and other investments" is equal to 178.6 million euro. The main component (amounting to 174.7 million euro) was the result of the reorganisation of the Bancassurance sector which saw the disposal to Cattolica of the two interests in the insurance companies Popolare Vita (now Vera Vita) and Avipop Assicurazioni (now Vera Assicurazioni);
- the item "Charges related to the banking system, net of taxes" includes 18.4 million euro connected to the additional contributions relating to the National Resolution Fund (amounting to 25.5 million euro) net of the related tax of 7.1 million euro.

In the same period of the previous financial year, the income statement included the following non-recurring items:

- the item "interest margin" included interest income on the 2016 TLTRO II loan for a total amount of 31.7 million euro and interest expense of 4.1 million euro, concerning the settlement of a tax dispute in the past;
- the item "Profits (losses) on investments in associates and companies subject to joint control carried at equity" included the negative result of SelmaBipiemme Leasing in the second quarter of 2017, amounting to -10.5 million euro, which was of an extraordinary nature;
- the item "personnel expenses" includes -1.3 million euro in charges relating to the Redundancy Fund;
- the item "other administrative expenses" includes the out-of-period income of 27.2 million euro correlated with the reversal of the fee attributed for the year 2015 to guarantee the convertibility of certain DTAs into tax credits. This amount had been charged to the income statement for 2016 and was no longer due in accordance with the regulatory provisions introduced by Law no. 15 of 17 February 2017. The item also included integration expenses and extraordinary transactions of 25 million euro, which, shown separately as a non-recurring item as from 30 September 2017, was also recalculated for the figures for 30 June 2017;
- "Net value adjustments on property and equipment and intangible assets" included write-downs of 3.5 million euro on software sold following the migration of BPM S.p.A. to the Group's Target IT system;
- the item "Net adjustments on securities and other financial assets" mainly included write-downs on the investments in the Atlante Fund and in the subordinated security issued by Banca Popolare di Vicenza for 61.0 million euro and 15.3 million euro respectively;
- the item "Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments" includes non-recurring net income of 13.3 million euro.

The main income statement items as at 30 June 2018 are illustrated below.

The **interest margin** amounted to 1,180.1 million euro. This figure is not fully comparable with that of the previous year, since, following the adoption of IFRS 9, the interest margin is positively affected by the reclassification of value recoveries on bad loans due to the progressive reduction in the collection times of cash flows considered recoverable which, prior to 1 January 2018, were recorded under net adjustments on loans. However, this aggregate was negatively affected by the non-inclusion of the portion of interest income accrued on non-performing loans deemed non-recoverable which, prior to 1 January 2018, were instead included and offset by the recognition of higher value adjustments on loans for the same amount. Net of these reclassifications, which were positive for a total of 128.9 million euro, the margin amounted to 1,051.2 million euro compared to the adjusted [1] figure of 1,032.2 million euro in the first half of 2017 (+1.8%). The contribution for the second quarter was 585 million euro, which, net of the effects of the introduction of IFRS 9, was up by 1.9% compared to the first quarter of 2018.

The **result of investments in associates and companies subject to joint control measured at net equity** was positive at 76 million euro, down compared to the 81.9 million euro recorded in the same period of the

[1] In the first half of 2017, interest on the TLTRO-II loans for 2016 was recorded for 31.7 million euro.

previous year. The contribution for the second quarter amounted to 33.4 million euro, down compared to the 42.6 million euro recorded in the first quarter, as a result of the lower contribution from insurance companies, also due to the reduction in the equity investment held. Within this aggregate, the main contribution was provided by consumer credit of 62.7 million euro conveyed by the shareholding in Agos Ducato.

Net fee and commission income amounted to 927.5 million euro, down by 9.0% compared to the first half of 2017 which recorded net fee and commission income of 1,019.4 million euro. This decrease is mainly attributable to the management, brokerage and advisory services segment, which made a minor contribution equal to 68 million euro than in the first half of 2017. This trend is mainly due to the well-known turbulence that affected, especially in May and June, Italian government securities and international stock markets and to the reorganisation of the commercial network. The move from a “product” consultancy model to a “portfolio” model required important training activities, reducing the time dedicated to commercial activities. The comparison was also influenced by the particularly intense activity in the placement of asset management products and portfolio management recorded in the first half of 2017 after the slowdown at the end of 2016 following the merger from which the bank originated.

Other net operating income amounted to 154.2 million euro and included the gain of 113.6 million euro realised on the sale to Anima SGR of the delegated insurance asset management mandates carried out on behalf of the insurance joint ventures linked to the bancassurance network of the former Banco Popolare. Net of this component, the aggregate amounted to 40.6 million euro compared to 44.7 million euro in the first half of 2017.

The **net financial result** was 109.5 million euro, compared to 100.2 million euro in the same period of last year. This result was influenced by the higher gains on disposals achieved by pursuing the strategy of reducing exposure to Italian government securities in favour of greater diversification of investments in this category of financial assets. Also for this segment, the comparison with the figures for the previous financial year is not fully consistent following the introduction of IFRS 9. Specifically, income from fair value measurement was recorded in the income statement for a total of 28.1 million euro against financial assets whose fair value changes were recognised directly in equity before 1 January 2018.

Due to these dynamics, total **operating income** amounts to 2,447.3 million euro. Taking into account the effects of the aforementioned reclassifications due to the introduction of IFRS 9, and excluding non-recurring items, this figure stands at the adjusted level of 2,333.7 million euro. Compared to the first quarter of 2018, operating income at the adjusted level was substantially aligned (-0.1%).

Personnel expenses, of 879.1 million euro showed a decrease of 3.8% compared to the 913.4 million euro in the same period of last year. The contribution of 437.1 million euro in the second quarter fell by 1.1% compared to the 442.1 million euro in the first quarter. Personnel expenses decreased mainly due to the reduction in the workforce (-544 resources compared to 31 December 2017). The total number of employees was 22,719 at 30 June 2018, compared to 23,263 at the end of 2017 (25,001 at 31 December 2015).

Other administrative expenses amounted to 414.6 million euro, down 3.9% compared to the figure recorded for the same period of the previous year. The aggregate does not include “system expenses” represented by contributions to the Single Resolution Fund (SRF) and the deposit guarantee scheme (DGS), which are presented, net of tax, as a separate item in the reclassified income statement. Other administrative expenses include the fee of 12.6 million euro for maintaining the deductibility of DTAs (13.4 million euro at 30 June 2017) and integration and merger expenses of 5.1 million euro (25 million euro in the same period of last year). The aggregate for the first half of 2017 benefited from 27.2 million euro linked to the recovery of the expense recognised in 2016 for the convertibility of the DTAs for 2015. Excluding the non-recurring items mentioned above, the item decreased by 5.6% compared to the same period of the previous year due to the efficiency measures implemented. In the second quarter of 2018, administrative expenses amounted to 203.1 million euro, a decrease of 4.0% compared to the figure for the first quarter.

Net value adjustments on property and equipment and investment property and intangible assets for the period amounted to 96.9 million euro, a decrease of 11.3% compared to 109.3 million euro at 30 June 2017, as a result of streamlining the Group's IT system.
Total **operating expenses** were down 4.4% compared to the first half of 2017 and by 1.8% compared to the first quarter of 2018.

Net adjustments on loans to customers amount to 686.5 million euro. This aggregate was also impacted by the introduction of IFRS 9 both for the new methods of determining the valuation of receivables introduced by the new standard and for the reclassifications that affected the interest margin described above. Excluding the impact of reclassifications alone, the figure for the first half of 2018 amounted to 557.5 million euro compared to 647.0 million euro in the first half of 2017. The cost of credit, measured by the ratio of net value adjustments on loans net of IFRS 9 reclassifications to net loans, was 104 b.p., down from 154 b.p. last year[1]. The level of adjustments on loans reflects a rigorous valuation approach intended to maintain high levels of coverage and at seizing any further opportunities to speed up the derisking process.
In the second quarter of 2018, the figure amounted to 360.2 million euro, an increase of 10.4% compared to 326.2 million euro recorded in the first quarter, mainly due to the impact of the Exodus disposal, which was slightly higher than expected due to the situation on financial markets.

The income statement for the first six months also recorded **net recoveries on securities and other financial assets** for 0.6 million euro (compared to net adjustments of 79.2 million euro as at 30 June 2017, which related mainly to write-downs on shares held in the Atlante Fund and other exposures to Venetian banks).

The **provisions for risks and charges** amounted to 45.7 million euro, compared to the 9.1 million euro in the same period last year.

In the first half of 2018, **profits on disposal of investments in associates and companies subject to joint control and other investments** were 178.6 million euro, relating almost entirely to the impact of the reorganisation of the bancassurance sector.

As a result of trends described above, the **income (loss) before tax from continuing operations** and system expenses amounted to 503.7 million euro, compared to the 129.8 million euro in the first half of last year.

The **taxes on income from continuing operations** at 30 June 2018 amounted to 87.3 million euro (43.8 million euro at 30 June 2017).

Charges related to the banking system, net of taxes were charged to the income statement in the first half for 67.4 million euro (45.0 million euro in the same period of last year), which include, net of the correlated tax effect, ordinary contributions to the Single Resolution Fund (SRF) of 68.0 million euro gross (62.4 million euro gross in the first half of 2017), as well as the additional contributions requested by the National Resolution Fund of 25.5 million euro (not present in the previous year).

Considering the share of the profits pertaining to minority interests (+3.6 million euro), the first half of 2018 closed with **net profit for the period** amounting to 352.6 million euro, compared to the net result without badwill of 94.2 million euro achieved in the same period last year (the 3,076.1 million euro in badwill that emerged following the completion of the PPA process brought the net economic result of the first half of 2017 to 3,170.4 million euro).

[1] This figure is not fully comparable as IFRS 9 has introduced a new model of impairment on receivables.

Consolidated balance sheet figures

Reclassified consolidated balance sheet

The following table compares the balance sheet at 30 June 2108 with the balances resulting from the financial statements at 31 December 2017 classified based on the new balance sheet aggregates introduced following the first time adoption of the IFRS 9 accounting standard.
A comparison is also provided with the balances at 1 January 2018, restated to take account of the first time adoption of the new IFRS 9 and IFRS 15 standards.
A reconciliation schedule between the balances at 31 December 2017 and those at 1 January 2018 is attached to this report.

(in thousands of euro)	30/06/2018	01/01/2018	31/12/2017	Changes on 31/12/2017	
Cash and cash equivalents	796,466	976,686	976,686	(180,220)	(18.5)%
Loans measured at Amortised Cost	112,040,845	111,044,748	112,681,902	(641,057)	(0.6)%
- Loans to banks	5,309,943	4,936,507	4,939,223	370,720	7.5%
- Loans to customers (*)	106,730,902	106,108,241	107,742,679	(1,011,777)	(0.9)%
Other financial assets and hedging derivatives	41,048,645	34,884,798	34,533,172	6,515,473	18.9%
- Measured at FV through Profit or Loss	7,977,461	6,417,083	5,184,586	2,792,875	53.9%
- Measured at FV through OCI	19,017,645	16,750,072	17,128,622	1,889,023	11.0%
- Measured at AC	14,053,539	11,717,643	12,219,964	1,833,575	15.0%
Equity investments	1,355,065	1,256,843	1,349,191	5,874	0.4%
Property, plant and equipment	2,733,275	2,735,182	2,735,182	(1,907)	(0.1)%
Intangible assets	1,295,196	1,297,160	1,297,160	(1,964)	(0.2)%
Tax assets	4,903,767	4,897,397	4,520,189	383,578	8.5%
Non-current assets and asset disposal groups held for sale	44,861	106,121	106,121	(61,260)	(57.7)%
Other assets	2,810,958	3,007,162	3,007,162	(196,204)	(6.5)%
Total assets	**167,029,078**	**160,206,097**	**161,206,765**	**5,822,313**	**3.6%**
Due to banks	31,550,552	27,199,304	27,199,304	4,351,248	16.0%
Direct funding	105,505,599	107,525,103	107,509,849	(2,004,250)	(1.9)%
- Due to customers	87,659,619	87,848,146	87,848,146	(188,527)	(0.2)%
- Securities and financial liabilities designated at FV	17,845,980	19,676,957	19,661,703	(1,815,723)	(9.2)%
Other financial liabilities designated at FV	8,964,218	8,704,348	8,707,966	256,252	2.9%
Liability provisions	1,532,028	1,617,312	1,580,461	(48,433)	(3.1)%
Tax liabilities	606,246	691,723	669,494	(63,248)	(9.4)%
Liabilities associated with assets held for sale	4,212,805	35	35	4,212,770	insignificant
Other liabilities	3,771,085	3,576,116	3,576,116	194,969	5.5%
Total liabilities	**156,142,533**	**149,313,941**	**149,243,225**	**6,899,308**	**4.6%**
Minority interests	52,510	57,567	63,310	(10,800)	(17.1)%
Group shareholders' equity	10,834,035	10,834,589	11,900,230	(1,066,195)	(9.0)%
Consolidated shareholders' equity	**10,886,545**	**10,892,156**	**11,963,540**	**(1,076,995)**	**(9.0)%**
Total liabilities and shareholders' equity	**167,029,078**	**160,206,097**	**161,206,765**	**5,822,313**	**3.6%**

(*) Includes senior securities for which the procedure for the issue by the Italian government of the guarantee on the securitisation of bad loans pursuant to Decree Law 18/2016 ("GACS") has been activated.

The changes in the main balance sheet items at 30 June 2018 are described below.

As at 30 June 2018, **direct funding** totalled 105.5 billion euro, showing a decrease of 1.9% compared to the 107.5 billion euro as at 31 December 2017. The decrease recorded during the period concerned both current accounts and sight deposits of the commercial network, down by 1.1 billion euro, and bonds and certificates of deposit (-1.8 billion euro). This trend is in line with the policy aimed at a gradual reduction in the cost of funding thanks to a reduction in the most expensive forms of funding. Repurchase agreements with customers increased (+1.5 billion euro).
Note that the aggregate does not include the stable funding guaranteed by the stock of certificates issued by the Group, which, as at 30 June 2018, was 3.8 billion euro, down compared to the figures at 31 December 2017, equal to 4.0 billion euro.

As at 30 June 2018, **indirect funding**, including certificates, totalled 93.6 billion euro, down compared to the 101.3 billion euro as at 31 December 2017.
More specifically, administered assets amounted to 34.4 billion euro, showing a decrease of 6.4 billion euro. The aggregate included the exit of an institutional customer in the first quarter, with administered assets amounting to 4.8 billion euro, with extremely low margins, and a decrease in the second quarter attributable mainly to the negative performance of markets, which affected the value of securities held in custody. Net of these effects, administered assets were substantially aligned with the figure at the end of December 2017.
On the other hand, managed assets amounted to 59.2 billion euro, with a decrease of 2.3% compared to the 60.5 billion euro as at 31 December 2017, recorded mainly in portfolio management and insurance, partly due to the temporary effect of the reorganisation that is under way in the sector. Conversely, the performance of funds and SICAVs was positive, amounting to 38.3 billion euro, an increase of 1.9% for the first half.

Loans to customers

Net loans to customers amounted to 106.7 billion euro as at 30 June 2018, a decrease of one billion euro compared to the figure as at 31 December 2017, as a result of the disposals of bad loans carried out with the Exodus project and the greater adjustments recorded upon the first time adoption of the IFRS 9 standard, made mainly against bad loans. The aggregate of performing loans rose by 2.7% compared to 31 December 2017. Without considering the effect of senior securities subscribed as part of the Exodus securitisation, performing loans increased by 0.9 billion euro compared to 31 December 2017 (+0.9%).

Credit quality

Introduction

The Bank of Italy Circular no. 262 and the IFRS 3 accounting standard require that, in the case of business combinations, the assets and liabilities acquired are stated at their fair value on the acquisition date; as a result, for the impaired assets acquired, the gross value does not include the positive difference between the nominal value of the receivables and their purchase price.
Theoretically, this forecast is also applicable to the actual merger that gave rise to the Banco BPM Group effective 1 January 2017. Therefore, the impaired assets of the former BPM Group, which from a mere accounting perspective is the entity acquired, are recognised at net purchase value (which in this transaction corresponds to the net value of impaired loans determined on 1 January 2017 following the Purchase Price Allocation process). Due to this representation, these receivables formally appear to lack the adjustment provisions recognised prior to the business combination.

In this case, this method of representation provides, in some respects, partial and potentially distorted disclosures with regard to a representation that shows the receivables acquired as part of the business combination at their nominal value, with separate indication of the related adjustment provisions. Specifically, the method of representation required by the regulations indicated leads to a representation in which the level of coverage of impaired loans is clearly lower than the actual one.
It should also be noted that in the Strategic Plan, as well as in communications with the Supervisory Authority prior to the authorisation of the merger transaction, the impaired loans of the former BPM Group and the related hedging targets have always been represented by showing separately the gross nominal value of the loans and the relative adjusting entries. The same approach was followed in all market communications (press releases, presentations to analysts) as well as in the ordinary management of impaired loans.

Consequently, in the tables below showing gross exposure and adjusting entries separately, impaired loans pertaining to the former BPM Group acquired as part of the business combination are shown as "opening balances"—in the gross exposure, their nominal value and in the adjustment entries, the difference between the aforementioned nominal value and the value attributed to loans as part of the Purchase Price Allocation process.

(in thousands of euro)	30/06/2018		01/01/2018		31/12/2017		Change on 31/12/2017	
	Net exposure	**% impact**	**Net exposure**	**% impact**	**Net exposure**	**% impact**	**ass.**	**%**
Bad loans	3,613,074	3.4%	5,241,780	4.9%	6,487,624	6.0%	(2,874,550)	(44.3%)
Unlikely to pay	5,808,344	5.4%	6,273,529	5.9%	6,458,818	6.0%	(650,474)	(10.1%)
Past due - non-performing	71,767	0.1%	80,426	0.1%	80,425	0.1%	(8,658)	(10.8%)
Non-performing loans	**9,493,185**	**8.9%**	**11,595,735**	**10.9%**	**13,026,867**	**12.1%**	**(3,533,682)**	**(27.1%)**
Performing loans	**97,237,717**	**91.1%**	**94,512,506**	**89.1%**	**94,715,812**	**87.9%**	**2,521,905**	**2.7%**
Total loans to customers	**106,730,902**	**100.0%**	**106,108,241**	**100.0%**	**107,742,679**	**100.0%**	**(1,011,777)**	**(0.9%)**

(in thousands of euro)	30/06/2018				31/12/2017				Change in gross exposure	Change in gross exposure %	Change in total value adjustments
	Gross exposure	Total value adjustments	Net exposure	Coverage	Gross exposure	Total value adjustments	Net exposure	Coverage			
Bad loans	10,690,810	(7,077,736)	3,613,074	66.20%	15,793,632	(9,306,008)	6,487,624	58.92%	(5,102,822)	(32.3%)	(2,228,272)
Unlikely to pay	8,659,003	(2,850,659)	5,808,344	32.92%	9,545,664	(3,086,846)	6,458,818	32.34%	(886,661)	(9.3%)	(236,187)
Past due - non-performing	88,603	(16,836)	71,767	19.00%	95,394	(14,969)	80,425	15.69%	(6,791)	(7.1%)	1,867
Non-performing loans	**19,438,416**	**(9,945,231)**	**9,493,185**	**51.16%**	**25,434,690**	**(12,407,823)**	**13,026,867**	48.78%	(5,996,274)	(23.6%)	(2,462,592)
of which: forborne	*5,976,558*	*(2,106,022)*	*3,870,536*		*7,225,055*	*(2,538,408)*	*4,686,647*		(1,248,497)	(17.3%)	(432,386)
Performing loans (*)	**97,635,059**	**(397,342)**	**97,237,717**	**0.41%**	**95,018,344**	**(302,532)**	**94,715,812**	**0.32%**	**2,616,715**	**2.8%**	**94,810**
of which: first stage	83,794,695	(137,156)	83,657,539	0.16%							
of which: second stage	13,840,364	(260,186)	13,580,178	1.88%							
of which: forborne	*2,223,159*	*(64,824)*	*2,158,335*		*2,430,545*	*(30,715)*	*2,399,830*		(207,386)	(8.5%)	34,109
Total loans to customers	**117,073,475**	**(10,342,573)**	**106,730,902**	**8.83%**	**120,453,034**	**(12,710,355)**	**107,742,679**	**10.55%**	**(3,379,559)**	**(2.8%)**	**(2,367,782)**

(*) Includes senior securities related to Project Exodus for 1,654.2 million euro (1,656.5 million euro of gross exposure and 2.3 million euro of value adjustments).

The figures in the table above correspond to the reclassified Balance Sheet item "Loans to customers" and, as indicated above, also include the senior securities subscribed by Banco BPM as part of Project Exodus, which included the disposal of bad loans for approximately 5 billion euro gross.

Without considering this reclassification, the net amount indicated corresponds to the item "Loans" reported in table 4.2 of the Consolidated condensed interim financial statements "Financial assets designated at amortised cost: breakdown by product for loans to customers".

Net non-performing loans (bad loans, unlikely to pay and past due and/or non-performing overdue) amount to 9.5 billion euro as at 30 June 2018, a decrease of 3.5 billion euro (-27.1%) compared to 31 December 2017. The reduction in the aggregate derives from the increase in value adjustments on bad loans (+1.2 billion euro) recognised on the first time adoption of the IFRS 9 accounting standard, from the subsequent disposal at the end of the half year through the securitisation operation known as the Project Exodus and from the continuation of work out activities.
An analysis of the individual items shows the following changes:

- net bad loans of 3.6 billion euro, a decrease of 44.3% compared to 31 December 2017 due to the Exodus disposal and IFRS 9 adjustments;
- net unlikely to pay of 5.8 billion euro, a decrease of 10.1% compared to 31 December 2017;
- net exposures past due amounting to 72 million euro, down by 10.8% compared to 31 December 2017.

The coverage rate for the entire impaired loans aggregate was 51.2%, up compared to 48.8% at 31 December 2017.
More specifically, at 30 June 2018, the coverage rate was as follows:

- bad loans 66.2%, (58.9% as at 31 December 2017);
- unlikely to pay 32.9% (32.3% at 31 December 2017);
- past due 19.0% (15.7% at 31 December 2017).

It should be noted that at the end of the period, the new valuation process for bad loans took into account the disposal scenario included in the NPL Strategy and approved by the Board of Directors, in line with the indications of IFRS 9. Taking into account the disposals already completed as at 30 June 2018, the disposals projected by the aforementioned plan that are to be implemented by 2020 amount to a nominal value of approximately 3.4 billion euro.

The coverage rate of performing loans was 0.41% compared to 0.32% at 31 December 2017. Net of repurchase agreements, which are essentially risk free, the coverage level for performing loans rose to 0.44% (0.34% at 31 December 2017). The increase in hedging is mainly due to the adoption of the new impairment model provided for by IFRS 9.

Financial assets amount to 41.0 billion euro, an increase of 18.9% compared to 34.5 billion euro as at 31 December 2017. This aggregate mainly includes debt securities amounting to 36.1 billion euro, equity securities and UCIT units amounting to 2.4 billion euro and the fair value of derivatives amounting to 2.2 billion euro; furthermore, following the introduction of IFRS 9, financial assets (equalling 0.3 billion euro) also include loans to customers which must be measured at fair value.
The overall increase compared to the end of 2017 was due to the growth in debt securities classified in the "Hold to Collect" (+1.8 billion euro), "Hold to Collect & Sell" (+2.6 billion euro) and "Trading" (+1.2 billion euro) portfolios. Government securities were 30.4 billion euro (+5.2 billion euro compared to 31 December 2017) in total; within this context diversification continued, with the Italian government securities sector falling to 62.2% of total government securities compared to 82.1% in December 2017 and coming to 56% if only government securities classified within the "Hold to Collect & Sell" category are considered.
As at 30 June 2018, the valuation reserves, gross of tax effects, on all the securities classified in the "Hold to Collect & Sell" portfolio were negative by a total of 188 million euro, with a decrease in the second quarter of 2018 of 490 million euro mainly attributable to the negative performance of the implicit rates of return on Italian government securities and the consequent repercussions on the market prices of other financial assets listed on the Italian market.

Exposure to sovereign risk

At the beginning of the period, the financial markets were characterised by an optimistic climate, fuelled by several factors: expectations of robust economic growth in the main world economies, the rallying of the American stock market within an environment of extremely low volatility and a calm climate in the trading of peripheral euro zone government securities, also in the wake of the alleviated fears of populist tendencies in the area as a result of the 2017 election results in the Netherlands, France and—above all—Germany. The predominant sentiment towards Italy at the beginning of the year was substantially positive, despite the approaching election with relatively uncertain results. It was only in the run-up to the Italian general elections held on 4 March that the spread between ten-year BTPs and ten-year German Bunds—after having reached a low at the beginning of February (127 bps)—entered into moderate tension, reaching 156 bps at the end of the month.

The ballot box returned a partially unexpected result, which made it difficult to identify a parliamentary majority. After three rounds of consultations by the Italian President, an alliance between the 5 Star Movement and the Lega emerged. After several weeks of negotiations, the two political powers outlined a programme of government, by way of an unprecedented contract formula, and came to an agreement on the prime ministerial candidate, Professor Giuseppe Conte, who was tasked with forming the government. However, the new administration was not formed immediately. Indeed, the Italian President did not appoint the candidate for Minister of Economy and Finance indicated by the appointed Prime Minister, and both resigned from office. This was followed by a rather tense political phase, in which an unsuccessful attempt was made to form an administration to take the country back to the polls after the approval of the annual budget law. Afterwards, on 31 May, the newly appointed Prime Minister, Giuseppe Conte, presented a new list of ministers, with some changes from the previous list, and the Government was formed.

Under these circumstances, the volatility of Italian bond and share prices increased significantly, favouring the return of moderate turbulence on European sovereign risks. Indeed, there were widespread fears amongst participants regarding the more spending-orientated and permissive policy approach of the new government's Maastricht parameters. Consequently, the BTP to Bund spread reached a maximum (daily average) of 283 bps at the end of May. During the most critical phases of the negotiations for forming the new government, the yield on ten-year BTPs was actually driven beyond 3.1%, while two-year securities quickly went from negative values to a peak of over 2.0% within a couple of weeks.

In the weeks that followed, partly due to the active supervision of the ECB, tensions eased somewhat, and the effect of European sovereign debt on the market remained limited, both in terms of intensity and in time. The spread for ten-year Spanish Bonos compared to German Bund, after reaching its lowest for the period of 66 bps at the beginning of April, reached 134 bps at the end of May, due in part to the political crisis that hit the Rajoy government in Spain. The spread on similar Portuguese bonds reached 190 bps (a low of 87 bps during the last ten days of April). The BTP-Bund spread closed the period at around 250 bps.

At the end of the period, an additional element contributed to ease the tensions on the sovereign risks of the euro zone: Greece, with an historic agreement within the Eurogroup, finally completed the financial assistance program provided by the ESM (European Stability Mechanism), obtaining a 10-year deferral on the interest of its public debt (at 180% of GDP), as well as the last tranche of the € 15 billion loan granted by the European authorities.

The Group’s total exposure in sovereign debt securities as at 30 June 2018 was euro 30,446.9 million, and is provided below, broken down by country (in thousands of euro):

Countries	Debt securities
Italy	18,939,544
Spain	1,779,087
Germany	2,436,606
France	4,328,729
Austria	139,089
Other EU countries	148,111
Total EU Countries	**27,771,166**
USA	2,675,748
Argentina	7
Total other countries	**2,675,755**
Total	**30,446,921**

The exposure is represented almost exclusively by debt securities issued by central and local governments, mostly issued by EU Member States. This position is mostly held by the Parent Company Banco BPM, which, as at 30 June, held a total of 28,874.3 million euro.

Investments in sovereign debt securities with EU countries are classified in the portfolio of financial assets at fair value through profit or loss for approximately 7%, in the portfolio of financial assets at fair value with an impact on comprehensive income for 52%, while the remaining 41% is classified in the segment of financial assets designated at amortised cost.

The tables below provide more detailed information about the breakdown by accounting portfolio, residual life brackets and fair value hierarchy.

Financial assets designated at fair value through profit and loss

Country	Maturing by 2018	Matures between 2018 and 2022	Matures between 2022 and 2027	Matures beyond 2027	Total fair value as at 30/06/2018	Total fair value by hierarchy		
						LEVEL 1	LEVEL 2	LEVEL 3
Italy	866,209	113,731	582,191	2,967	1,565,098	1,563,469	1,627	2
Spain	-	-	84,671	19,180	103,851	103,851	-	-
France	-	-	136,676	59,800	196,476	196,476	-	-
Other EU countries	-	45	43	4	92	77	11	4
Total	**866,209**	**113,776**	**803,581**	**81,951**	**1,865,517**	**1,863,873**	**1,638**	**6**

Financial assets designated at fair value through other comprehensive income

Country	Maturing by 2018	Matures between 2018 and 2022	Matures between 2022 and 2027	Matures beyond 2027	Total fair value as at 30/06/2018	Net FVTOCI Reserve	Value adjustments	Total fair value by hierarchy		
								LEVEL 1	LEVEL 2	LEVEL 3
Italy	52,447	5,190,730	2,891,823	285,370	8,420,370	(175,733)	-	8,420,370	-	-
Spain	-	-	397,846	504,745	902,591	1,990	-	902,590	-	-
France	-	-	1,181,405	2,130,884	3,312,289	44,095	-	3,312,289	-	-
Germany			178,340	1,684,625	1,862,965	23,453		1,862,966		
Total	**52,447**	**5,190,730**	**4,649,414**	**4,605,624**	**14,498,215**	**(106,195)**	**-**	**14,498,215**	**-**	**-**

Financial assets designated at amortised cost

Country	Maturing by 2018	Matures between 2018 and 2022	Matures between 2022 and 2027	Matures beyond 2027	Total book value as at 30/06/2018	Total fair value	Total fair value by hierarchy		
							LEVEL 1	LEVEL 2	LEVEL 3
Italy	-	3,555,297	5,398,779	-	8,954,076	8,671,152	8,671,152	-	-
Spain	-	-	696,973	75,672	772,645	786,054	786,054	-	-
France	-	-	-	819,964	819,964	837,276	837,276	-	-
Ireland	-	-	-	19,808	19,808	20,198	20,198	-	-
Germany			425,365	148,274	573,639	588,008	588,008		
Other EU countries	-	-	267,302	-	267,302	271,040	271,040	-	-
Total	**-**	**3,555,297**	**6,788,419**	**1,063,718**	**11,407,434**	**11,173,728**	**11,173,728**	**-**	**-**

Key financial highlights of the main Group companies

A summary of the main investments in Group companies is presented below, with an indication of the most significant balance sheet, income statement and operating balances as at 30 June 2018.

(in millions of euro)	Asset Total	Shareholders' equity (*)	Direct Funding	Indirect Funding	Net Loans	Profit (Loss)
Banks						
Banca Popolare di Milano	45,756.7	3,901.3	26,963.8	24,979.3	31,514.0	118.9
Banca Aletti & C.	16,515.6	963.6	2,225.0	24,907.7	1,790.7	90.3
Banca Akros	2,492.6	191.1	711.7	-	244.2	2.1
Banca Aletti & C. (Suisse)	128.2	28.8	97.9	392.2	10.7	(0.7)
Bipielle Bank (Suisse)	84.6	43.2	4.2	-	-	(0.9)
Financial companies						
Aletti Fiduciaria	10.4	7.9	-	997.9	1.6	(0.1)
Release	1,963.9	344.7	6.8	-	1,054.1	(23.4)
Other companies						
Bipielle Real Estate	1,123.1	1,102.0	-	-	7.1	9.8
Holding di Partecipazioni Finanziarie Banco Popolare	842.0	838.0	-	-	-	322.1
Società Gestione Servizi - BP	380.4	122.5	-	-	1.1	0.2
Tecmarket Servizi	37.8	20.6	-	-	-	3.9
Ge.Se.So.	1.6	0.4	-	-	-	0.1

(*) amount includes the income (loss) for the period.

RISK MANAGEMENT

Information on risks is provided in the illustrative notes to the consolidated condensed interim financial statements, to which reference should be made.

DISCLOSURE ON TRANSACTIONS WITH RELATED PARTIES

The information on transactions with related parties is included in the illustrative notes to the consolidated condensed interim financial statements, to which reference is made.

OUTLOOK FOR BUSINESS OPERATIONS

The slowdown in foreign trade and the weaker trend in investment expectations have not stopped the expansionary trend of the European and Italian economies. For the rest of the year, expectations are oriented towards maintaining this growth, which is also favoured by a monetary policy that will remain strongly expansionary, at least until the end of 2019, despite the planned interruption of the APP. One significant risk to the domestic scenario includes the effects of the public finance program framework that will be established by the Italian government starting from September/October. Specifically, the effects on the yield on government securities caused by the reaction of international investors to possible fiscal measures that may increase the public deficit will be significant.
Loan volume should continue to grow within this environment. However, growth will be slowed down by the abundant liquidity of the most dynamic companies, which will turn less to loans; by the low profitability of loans to large companies, determined by the competition between intermediaries; and by the selectivity of the offer, also in light of the new IFRS 9 accounting principle that came into effect, which entails greater provisions for high-risk loans. A positive contribution will continue to come from loans to households, motivated by the progressive stabilisation of the real estate market and by recent signs of its greater dynamism. Due to the rapid and significant reduction in non-performing loans because of the reduction in loan default rates, sale to third-parties and recovery actions, the speedy improvement of credit quality should continue during the second quarter of the year, thereby further freeing up additional resources on the bank assets side.
Bank funding over the year should continue to fall, albeit marginally. This decrease is mainly due to the ongoing erosion of the bond component, accompanied by the change in composition of technical items in favour of current accounts. At the same time, the cost of funding will also fall, driven by the aforementioned change in composition. Thus, the spread between bank asset and liability rates will tend to close marginally, putting pressure on net income from customers and on net interest income, which should increase to an extremely limited extent due to the effect of volume. In view of the insufficient trend in net fee and commission income, which was also penalised by the reduction in profit from trading and valuation at fair value, net interest and other banking income is expected to remain stable at 2017 levels.

Having already completed a significant number of projects in the 2016-2019 Strategic Plan, including, in particular, the implementation of the organisational unit dedicated to the management of non-performing loans, IT integration, the definition of the structure of partnerships in asset management and bancassurance, and the reorganisation of the commercial network, the Group will focus its attention on streamlining its private and investment banking activities, the digital transformation project, the simplification of the Group's scope and the optimisation of its territorial presence.
Furthermore, as it can leverage the positive outcome of the completed NPL disposal transactions, it will continue with its overall derisking action, in full compliance with the new ambitious objectives that have been announced.
Over the next few quarters, ordinary operations will continue to be based on recovering profit margins, which will reap the benefits of the synergies resulting from the merger.
Although competitive pressures on margins remain, the performance of revenues will benefit from an acceleration in lending volumes, a further containment of the average cost of funding, due to the residual margins to optimise its mix, and the positive contribution of the investee companies, while the trend in commissions, specifically those deriving from management, brokerage and advisory services, should not deviate significantly from the values of the first half of the year, also due to the foreseeable uncertainty and volatility of the markets.
The limitation of operating expenses by improving efficiency, carrying out specific actions intended to optimise spending and streamlining the organisational functions will continue to be one of the factors receiving the greatest attention.
The rates of coverage of non-performing loans will remain high, and the reduction in stocks will continue through internal workouts and, as noted, through the implementation of the actions provided for in the derisking plan.

Consolidated condensed interim financial statements

DISCLOSURE ON THE FIRST ADOPTION OF THE IFRS 9 ACCOUNTING STANDARDS FINANCIAL INSTRUMENTS AND IFRS 15 REVENUE FROM CONTRACTS WITH CUSTOMERS

Introduction

Regulation (EU) no. 2067 of 22 November 2016 endorsed the new international accounting standard IFRS 9 "Financial Instruments", which is mandatory as of 1 January 2018 and governs the steps of classification and measurement, impairment and hedge accounting related to financial Instruments, replacing the accounting standard IAS 39 "Financial Instruments: Recognition and Measurement".

Regulation no. 1905 of 22 September 2016 endorsed the accounting standard IFRS 15 "Revenue from Contracts with Customers" with mandatory application from 1 January 2018. This introduced a single reference framework for recognising revenues originating from contracts with customers and replaces the accounting standards IAS 18 "Revenues" and IAS 11 "Construction Contracts" and their relative interpretations (IFRIC 13, IFRIC 15, IFRIC 18, SIC 31).

Regarding the presentation of the effects of the first time adoption of the new accounting standards (hereinafter also referred to as FTA - First Time Adoption), it should be noted that in the first financial statements of application, the Banco BPM Group did not restate the comparison figures, but rather made use of the option provided for in the transitional provisions. The adoption of the new accounting standards, therefore, resulted in an adjustment to opening shareholders' equity on 1 January 2018, which showed an overall reduction of 1,071.4 million euro.
The table below shows the balance sheet which was prepared in compliance with the fifth update of the Bank of Italy Circular no. 262:

- balances at 31 December 2017 reclassified on the basis of the new standards and accounting for the new classification criteria for IFRS 9;
- the impacts related to the adoption of IFRS 9 deriving from the new measurement criteria and the IFRS 15 standard;
- the balances at 1 January 2018 restated following the adoption of the above-mentioned standards.

For further details on how the balances at 31 December 2017 and the impact of FTA are presented, please refer to the paragraphs below.

Asset items (in thousands of euro)	31/12/2017 IAS 39 balances Reclassifications	Impact of IFRS 9	1/1/2018 IFRS 9	Impact of IFRS 15	01/01/2018 IFRS 9 + IFRS 15
10. Cash and cash equivalents	976,686	-	976,686		976,686
20. Financial assets designated at fair value through profit and loss	6,192,182	(18,908)	6,173,274		6,173,274
a) financial assets held for trading	4,894,433	-	4,894,433		4,894,433
b) financial assets designated at fair value	-	-	-		-
c) other financial assets mandatorily at fair value	1,297,749	(18,908)	1,278,841		1,278,841
30. Financial assets measured at fair value through other comprehensive income	16,698,472	51,600	16,750,072		16,750,072
40. Financial assets measured at amortised cost	124,080,610	(1,318,220)	122,762,390		122,762,390
a) due from banks	5,168,138	(2,987)	5,165,151		5,165,151
b) loans to customers	118,912,472	(1,315,233)	117,597,239		117,597,239
50. Hedging derivatives	243,810	-	243,810		243,810
60. Fair value change of financial assets in macro fair value hedge portfolios (+/-)	54,531	-	54,531		54,531
70. Equity investments	1,349,191	(92,348)	1,256,843		1,256,843
80. Technical reserves of reinsurers	-	-	-		-
90. Property, plant and equipment	2,735,182	-	2,735,182		2,735,182
100. Intangible assets	1,297,160	-	1,297,160		1,297,160
of which:	-	-	-		-
- goodwill	76,389	-	76,389		76,389
110. Tax assets	4,520,189	371,598	4,891,787	5,610	4,897,397
a) current	319,462	-	319,462		319,462
b) deferred	4,200,727	371,598	4,572,325	5,610	4,577,935
120. Non-current assets and asset disposal groups held for sale	106,121	-	106,121		106,121
130. Other assets	2,952,631	-	2,952,631		2,952,631
Total assets	**161,206,765**	**(1,006,278)**	**160,200,487**	**5,610**	**160,206,097**

Liability and shareholders' equity items (*in thousands of euro*)	**31/12/2017 IAS 39 balances Reclassifications**	**Impact of IFRS 9**	**1/1/2018 IFRS 9**	**Impact of IFRS 15**	**01/01/2018 IFRS 9 + IFRS 15**
10. Financial liabilities measured at amortised cost	131,455,963	15,254	131,471,217		131,471,217
a) due to banks	27,199,304	-	27,199,304		27,199,304
b) due to customers	87,848,146	-	87,848,146		87,848,146
c) debt securities issued	16,408,513	15,254	16,423,767		16,423,767
20. Financial liabilities held for trading	7,942,063	(3,618)	7,938,445		7,938,445
30. Financial liabilities designated at fair value	3,253,190	-	3,253,190		3,253,190
40. Hedging derivatives	765,903	-	765,903		765,903
50. Fair value change of financial liabilities in macro fair value hedge portfolios (+/-)	8,535	-	8,535		8,535
60. Tax liabilities	669,494	22,229	691,723	-	691,723
a) current	14,493	-	14,493		14,493
b) deferred	655,001	22,229	677,230		677,230
70. Liabilities associated with assets held for sale	35	-	35		35
80. Other liabilities	3,567,581	-	3,567,581		3,567,581
90. Employee termination indemnities	408,160	-	408,160		408,160
100. Provisions for risks and charges:	1,172,301	16,451	1,188,752	20,400	1,209,152
a) commitments and guarantees given	119,472	16,451	135,923		135,923
b) retirement benefits and similar commitments	166,847	-	166,847		166,847
c) other provisions for risks and charges	885,982	-	885,982	20,400	906,382
110. Technical reserves	-	-	-		-
120. Valuation reserves	251,706	(78,229)	173,477		173,477
130. Redeemable shares	-	-	-		-
140. Equity instruments	-	-	-		-
150. Reserves	1,946,308	(972,622)	973,686	(14,790)	958,896
160. Share premium reserve	-	-	-		-
170. Share capital	7,100,000	-	7,100,000		7,100,000
180. Treasury shares (-)	(14,146)	-	(14,146)		(14,146)
190. Minority interests (+/-)	63,310	(5,743)	57,567		57,567
200. Income (Loss) for the period (+/-)	2,616,362	-	2,616,362		2,616,362
Total liabilities and shareholders' equity	**161,206,765**	**(1,006,278)**	**160,200,487**	**5,610**	**160,206,097**

DISCLOSURE ON THE FIRST ADOPTION OF THE IFRS 9 - ACCOUNTING STANDARDS FOR FINANCIAL INSTRUMENTS

As of 1 January 2018, the Banco BPM Group has reclassified and measured its financial assets and liabilities in accordance with the new IFRS 9 standard and the fifth update of the Bank of Italy Circular no. 262, without prejudice to the treatment of impacts caused by changes to its own credit risk on financial liabilities designated at fair value, for which the Group had implemented early adoption since 2017.

As noted in the introduction, with reference to the way in which the effects of the first time adoption of the accounting standard (hereinafter also referred to as FTA - First Time Adoption) are represented, the Banco BPM Group did not restate the comparison figures, but rather made use of the option provided for in the transitional provisions (IFRS 9, paragraph 7.2.15). The adoption of IFRS 9 has therefore resulted in an adjustment to the opening shareholders' equity on 1 January 2018.

In order to allow for an assessment of the effects brought about by the adoption of the new accounting rules, this section provides an illustration of the main regulatory requirements set forth by the IFRS 9 standard and the related choices made by the Group, the effects on the book value of shareholders' equity and on the own funds of the Banco BPM Group. It also provides:

- reconciliation between the latest approved financial statements (IAS 39) and the first IFRS 9 financial statements, prepared in accordance with Bank of Italy regulations and in reclassified form;
- detailed information, in keeping with the disclosure requirements of the IFRS 7 accounting standard regarding the first time adoption of IFRS 9: reconciliation schedules between the balances of the former IAS 39 as at 31 December 2017 and those recalculated based on the new IFRS 9 standard, by individual accounting category and by individual type of financial instrument, reconciliation schedules between the adjusting entries of IAS 39/IAS 37 and the adjusting entries of IFRS 9;
- credit quality at 1 January 2018 for all financial assets subject to the IFRS 9 impairment model.

Lastly, this section describes how the Banco BPM Group has decided to present the equity balances of the previous year/period for comparative purposes.

Explanation of regulatory requirements and the Group’s main choices

Governance

Please note that the first time adoption of the new accounting standard IFRS 9 required significant implementations—in terms of processes, procedures, methodologies and IT systems, which were governed by the establishment, as of 2016—of a specific project led by the Administration and Budget Function Head, with the support of the Special Projects and Monitoring Function and the active involvement of representatives from the Risk, Loans, Commercial, Organisation, IT, Finance, Planning & Control, Audit and NPL Unit, Audit and Internal Validation functions.

The main decisions for the project were made by a Steering Committee (consisting of the Managing Director, the General Manager, the Joint General Managers, the Project Manager and the Head of the Special Projects and Monitoring Function), and brought to the attention of the Board of Directors.

The results of the activities performed were periodically brought to the attention of the Operating Committee, comprised of all of the function heads involved directly and indirectly in the implementation of the new rules.

The models for calculating expected losses, relating to both performing and non-performing exposures, were validated by the Internal Validation function, a function independent of business structures and the structures responsible for developing and implementing the model.

Considering the significance of the impacts, with particular reference to calculating the expected losses on both performing and non-performing loans, please note that the valuation models, the parameters used and the relative assumptions were submitted for approval by the competent corporate bodies.

To ensure the correct classification of financial instruments and their measurement and impairment, the Group's administrative and accounting processes were adapted to reflect the main activities required by the new IFRS 9 standard (with particular reference to the SPPI test and the new impairment model) and related controls.

During the first half of 2018, the data and information produced by the new systems and processes underwent intense verification, including by the internal control bodies and the independent auditors, after which the calculation methods, processes, procedures and, lastly, IT systems were adapted as required. As of the date of preparing this interim report, the aforementioned verification activities have been completed and, therefore, the impact on the balance sheet of the adoption of the new IFRS 9 standard has been definitively determined.
In this regard, please note that the impact as quantified above differs only marginally from that communicated to the market on 9 May 2018, on a provisional basis, when the results for 31 March 2018 were disseminated. Specifically, the definitive transition to IFRS 9 resulted in a higher debit to consolidated shareholders' equity of 18.7 million euro. The effect on shareholders' equity at 1 January 2018, which was negative overall, therefore amounted to 1,406.0 million euro, as better illustrated in Table 1 below. This difference is explained by the fact that during the second quarter a series of in-depth analyses was carried out on the methodology and scope of the adoption of the impairment model, which made it possible for the estimate of expected losses on performing exposures to be refined. A few limited anomalies were found in the expected losses calculation that were, in any case, insignificant and the availability of updated information on the indirect effects of certain investments in associates and companies subject to joint control was taken into consideration. However, the analysis and the main methodological choices made by the Group with reference to the classification and measurement of financial instruments—as already illustrated in the Annual Financial Report of the Banco BPM Group as at 31 December 2017 and referred to in the aforementioned press release—were confirmed.
In the second half of 2018, the Group will continue with its activities related to the adoption of the new IFRS 9 standard and evaluate the opportunity to intervene in the refinement of loss calculation models, in the strengthening of control systems and, more generally, in the improvement of the overall governance required by the implementation of the aforementioned standard.

Classification and measurement requirements for financial assets and financial liabilities in accordance with IFRS 9

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

- the entity's business model:, which reflects the objectives that company management intends to pursue by holding financial assets. More specifically:
  - Hold to Collect (HTC), when the objective is to collect contractual cash flows, maintaining the financial instrument until maturity;
  - Hold to Collect and Sell (HTC&S), when the financial assets are held with a view to collecting contractual cash flows for the duration of the asset, as well as collecting the proceeds from its sale;
  - Other, when the objectives are different from those described in the points above, for example, which are attributable to the desire to collect cash flows through trade (Sell).
- Contractual characteristics of the cash flows: depending on whether the cash flows are based exclusively on principle and interest (Solely Payments of Principal and Interest, or SPPI) or if, otherwise, they also depend on other variables (for example: profit sharing, such as dividends, or repayment of the invested capital depending on the issuer's financial performance, etc.). The checks carried out to ascertain the contractual characteristics of cash flows are referred to as test SPPI or SPPI test.

The following accounting categories can be identified on the basis of the combinations between the business model and the contractual characteristics of the cash flows:

- financial assets designated at amortised cost: these include debt instruments (loans and securities) with a Hold to Collect business model, the contractual terms of which are represented solely by the payment of principle and interest (SPPI test passed);
- financial assets designated at fair value through other comprehensive income, with recycling in the income statement of the components of measurement and realisation: these include debt instruments (loans and securities) with a Hold to Collect and Sell business model, the contractual terms of which are represented solely by the payment of principal and interest (SPPI test passed);
- financial assets designated at fair value through profit and loss: these include all trading assets, including non-hedging derivative instruments and, regardless of the business model, those assets that must be measured at fair value as the cash flows do not represent only the payment of principal and interest (failure to pass the SPPI test). All equity instruments are therefore included, unless the entity chooses the irrevocable option of classifying them in the category of financial assets designated at fair value through other

comprehensive income, without any recycling in the income statement of the components of valuation and realisation (with the exception of dividends which continue to be recognised in the income statement).

In addition to the categories illustrated above, the accounting category of financial assets designated at fair value through profit or loss is also an option; this option is irrevocable and is allowed only to eliminate or significantly reduce an inconsistency in valuation or recognition that would otherwise result from the valuation of the assets or liabilities or from the recognition of the related gains and losses on different bases (accounting mismatch).
Regarding the new classification rules based on the characteristics of cash flows, IFRS 9 eliminates the rules for separating embedded derivatives from financial assets not designated at fair value through profit and loss.

Given the above, during the transition to IFRS 9, the Banco BPM Group defined the classification of financial instruments according to the new accounting categories provided for by IFRS 9 - taking into account the business model at 1 January 2018 and the characteristics of the contractual cash flows of the instrument at the date of its origin - and conducted a new measurement of the same on the basis of the respective valuation criteria.

The definition of the business model, which was conducted at both Group and legal entity level, took into consideration all relevant information, including historical data relating to past sales, methods for measuring and reporting the performance of financial assets, methods for managing and measuring risks that may affect the performance of financial assets, and remuneration policies for top management. Thus, specific guidelines were prepared in order to define the Group's business model and any changes to the same. In regard to the portfolio of financial assets designated at amortised cost, considering that the objective of the business model is the collection of the related cash flows, the criteria for the eligibility of sales in the event of the occurrence of specific circumstances (such as, a significant increase in credit risk or near-maturity sales) or in relation to their insignificance in terms of amount or frequency, have been defined.
With regard to the SPPI test, the Group's methodological approach was defined and target models were implemented, in terms of procedures and processes, for carrying out the test for all financial assets, whether represented by debt securities or by loans. As part of this methodological approach, a specific procedure was defined to ascertain whether the Benchmark Cash Flow Test had been passed, which is necessary when financial instruments have a modified time value of money, represented, for example, by a mismatch between the frequency of setting the interest rate for the payment of the respective instalment (fixing) and the reference rate (tenor).
Below is the analysis that was conducted with special internally developed tool, based on a check list of indicators designed to ascertain whether the SPPI test will be passed, rather than on the basis of information from external providers.

For the portfolio of debt securities outstanding as at 31 December 2017 held with a Hold to Collect business model, rather than Hold to Collect and Sell business model, the SPPI test was carried out to verify the possibility of classifying the securities in question in the accounting categories of “Financial assets designated at amortised cost” and “Financial assets designated at fair value through other comprehensive income”. The analysis illustrated that a limited percentage of debt instruments, both in number and in value, represented by structured or asset-backed securities were not exceeded; these instruments were therefore classified in the accounting category of “other financial assets mandatorily at fair value through profit and loss”.
With regard to financial instruments represented by loans, the approach adopted for the analysis varied depending on whether they referred to standard products classified as such on the basis of catalogues or product information sheets, common to the retail, small business and mid-corporate areas, rather than tailor made disbursements[3]. For the first type of financial instruments, the analysis focused on an examination of the sheets describing the products currently for sale. For the second type of financial instruments, the analysis focused on the precise examination of the individual loan agreements. The analysis conducted led to specific types of standard products being identified (regarding a marginal number of financial instruments with respect to the Group’s total exposure), as well as several tailor made contracts which, due to specific contractual clauses, would not pass the test.
The assets represented by UCIT units have been classified under “other financial assets mandatorily at fair value”, also on the basis of the clarifications provided by the IFRIC, which will be described in greater detail below.

[3] The scope of tailor made products—subject to analysis for the purposes of the SPPI test—includes all the exposures overseen by specialised Group structures that can be traced back to personalised disbursements on the basis of the specific financial needs of typically corporate customers and to exposures subject to restructuring, the specific features of which required the intervention of the aforementioned specialised structures.

For equity securities held with the intention of making a strategic investment and not held for trading and not qualifying as investments in subsidiaries, associates and entities under joint control, the option to designate instruments at fair value through other comprehensive income may be used.

With reference to financial liabilities, the new accounting standard IFRS 9 confirms the classification and measurement rules provided for by IAS 39, on the basis of which they are subject to measurement at amortised cost, with the exception of financial liabilities held for trading, including derivative liabilities, and financial liabilities for which the option to designate at fair value through profit and loss is used. In relation to the last type of liability, the IFRS 9 standard states that the fair value changes associated with its creditworthiness must be recognised as a balancing entry to a specific shareholders' equity reserve, rather than in the income statement as required by the IAS 39 standard, unless this treatment will create or amplify an accounting mismatch in the income statement. In the latter case, the entire fair value change of the liability must be recognised in the income statement.
In this regard, it should be noted that the Banco BPM Group has exercised the right to adopt changes in the accounting treatment of its creditworthiness for financial liabilities designated at fair value in advance, since its 2017 financial statements. Considering that the IFRS 9 standard substantially adopted the classification and measurement criteria of IAS 39, during the transition to the new standard, the Banco BPM Group reallocated to the new accounting items, verifying the need to revoke this designation for liabilities designated at fair value as at 31 December 2017, since there was no problem of accounting mismatch with the management hedge derivative that had motivated the original designation at fair value, since it had expired in the interim.

For details on the allocation of financial instruments to the new IFRS 9 accounting categories, please refer to be to tables 4, 5 and 6 below.

IFRS 9 impairment methodology based on expected credit losses (ECL)

According to IFRS 9, all financial assets not measured at fair value through profit or loss, represented by debt securities and loans, and off-balance sheet exposures (commitments and guarantees given) must be subject to the new impairment model based on expected losses (ECL – Expected Credit Losses). The new approach aims to ensure a more timely recognition of losses than the previous IAS 39 model, according to which losses should only be recognised if there is objective evidence that took place after the initial recognition of the asset (the incurred losses model).
Specifically, the impairment model introduced by the IFRS 9 accounting standard is based on the concept of forward-looking valuation, i.e. on the concept of Expected Credit Loss, whether calculated at 12 months (Stage 1) or for the entire residual lifetime of the instrument (lifetime loss for Stage 2 and Stage 3). In particular, the model establishes that financial assets should be classified into three separate stages, corresponding to different measurement criteria:

- Stage 1: to be measured on the basis of an estimate of expected forward-looking loss with reference to a time horizon of one year. Stage 1 includes performing financial assets for which no significant impairment of credit risk has been observed with respect to the date of initial recognition;
- Stage 2: to be measured on the basis of an estimate of expected forward-looking loss with reference to a time horizon corresponding to the entire residual life of the financial assets. Stage 2 includes the financial assets that have undergone significant impairment of credit risk with respect to initial recognition;
- Stage 3: to be measured on the basis of an estimate of expected forward-looking loss, based on a 100% likelihood of default. Stage 3 includes financial assets that are considered non-performing.

According to the Expected Credit Losses calculation model, losses must be recorded not only with reference to objective evidence of impairment losses that had already occurred at the reporting date, but also on the basis of expectations of future impairment that is not yet manifest, which must reflect:

- the likelihood of different scenarios occurring;
- the effect of discounting using the effective interest rate;
- historical experience and current and future valuations.

In order to implement the above requirements:

- the reference framework was defined to ascertain whether or not there has been a significant deterioration in credit risk (the Framework Stage Assignment) and performing exposures were consequently classified from Stage 1 to Stage 2;
- models have been developed – including forward-looking information – to be used both for the purposes of stage assignment (lifetime DP) and for the calculation of the expected credit loss at one year and lifetime.

Framework stage assignment

In order to allocate exposures to the various stages, the Banco BPM Group has classified them as follows:

- performing loans in Stages 1 and 2;
- non-performing loans in Stage 3. The analysis has led to the conclusion that the relative scope is in line with that of non-performing loans, determined according to the definitions contained within current supervisory provisions[4] (bad loans, unlikely to pay, past due), since they are deemed consistent with the accounting regulations in terms of objective evidence of impairment. For further details on this scope, please refer to Part "A.2 - Key financial statement items" of this Interim Report.

In regard to performing loans, the significant deterioration in creditworthiness was defined at the single relationship level by comparing the credit risk associated with the financial instrument at the time of valuation and at the time of initial disbursement or acquisition. This comparison will be made on the basis of quantitative and qualitative criteria. For the staging of debt securities that are characterised by more than one purchase transaction for the same ISIN, the Group has decided to use the First In-First Out (FIFO) method to calculate the original creditworthiness of the quantities subject to valuation.

More specifically, in order to identify the existence of a significant deterioration in credit quality and the subsequent transfer of the financial instrument from Stage 1 to Stage 2, the Group has identified the following criteria:

- relative quantitative criteria, based on statistical observations, considered an indication of a significant increase in credit risk over time;
- absolute qualitative criteria, represented by the identification of trigger events or the exceeding of absolute thresholds as part of the credit monitoring process. Specifically, these criteria were selected with reference to the indicators contained in the watch list for identifying anomalous loans, which are deemed to represent a deterioration in creditworthiness. This includes all exposures affected by forbearance measures which have this attribute still active, regardless of whether the current probation period is regular or not;
- backstop indicators, i.e. factors of credit delinquency, the existence of which gives rise to the presumption that there has been a significant increase in credit risk, unless there is evidence to the contrary. Presumably, except in exceptional cases attributable to specific types of counterparties, such as Public Administrations, the Group believes that the credit risk of the exposure should be considered significantly increased if past due/delinquent for more than 30 days, without prejudice to the application of the thresholds of significance provided for by supervisory regulations.

With particular reference to the quantitative criterion applicable to credit exposures to customers, the Banco BPM Group has chosen to take the change between the default probability (DP) at the date of origin of the financial instrument and the same probability measured at the reporting date as a reference. The development of the model has led to the identification of specific internal thresholds of variation between the default probability detected at the origin of the contractual relationship and the default probability detected at the valuation date, differentiated by risk segment, rating class and residual life. Exceeding these thresholds represents a significant increase in credit risk and the consequent transfer of the individual line of credit from Stage 1 to Stage 2. The determination of these thresholds, developed based on the Banco BPM Group's historical observations, underwent a calibration process to identify the scope of the positions to be classified in Stage 2 before the transition to impaired exposure, as well as the scope of the positions to be classified in Stage 1, as it is considered an expression of an improvement in credit risk.
Additionally, in order to compare the lifetime DP curves at the reporting date with the date of origin, forward-looking information was considered, such as macroeconomic factors and other elements represented by the type of market, the sector of activity, the type of financial instrument and the residual lifetime of the financial instrument itself.
For the portfolios of loans to banking counterparties and debt securities that do not have an investment grade rating, the relative quantitative criterion is based on a change in the default probability at twelve months, rather than over the residual lifetime of the instrument. This simplified approach, taking account of the type of counterparty/issuer, is justified by the insignificance of the difference in impact compared to the more complex model used on the portfolio of exposures represented by loans to customers.

Debt securities with an investment grade rating at the reporting date, which are mainly attributable to government securities, are classified as Stage 1 because the Banco BPM Group has made use of the Low Credit Risk Exemption

[4] Definitions contained in the Bank of Italy Circular no. 272 of 30 July 2008 and subsequent updates, on the basis of which the scope of non-performing loans corresponds to that of the Non-Performing Exposures of Implementing Regulation (EU) 680/2014, with which the EBA's ITS was incorporated (EBA/ITS/2013/rev1 of 24/07/2014).

for this category and this category only. This exemption represents the convenient expedient of not conducting the test related to the significant deterioration of credit risk with exposures whose credit risk is considered low.

With reference to the functioning of the model, the Banco BPM Group has decided to adopt a symmetrical reclassification model from Stage 2 to Stage 1. In cases where the conditions triggering the significant deterioration in credit risk cease to exist at a later valuation date, the financial instrument returns to being measured based on the expected loss over twelve months. It should also be noted that in the event of a return under Stage 3, there is no mandatory transfer of the counterparty's relationships to Stage 2. The classification of performing exposures into stages (Stage 1 or Stage 2) will therefore depend on the automatic application of the framework stage assignment that was illustrated previously.

<u>Expected Credit Loss – Stage 1 and Stage 2</u>
With reference to the Expected Credit Loss (ECL) calculation model for measuring the impairment of instruments classified under Stages 1 and 2, it should be noted that its development was based on the new internal model for measuring credit risk, which was approved by the Supervisory Authority in February 2018, with its extension to credit exposures acquired by the former BPM Group as part of the business combination from which Banco BPM originated.

Based on this model, with specific adjustments, new IFRS 9 compliant risk parameters have been developed, in terms of:
- one-year and lifetime default probability (DP): the probability of moving from performing status to non-performing status over the course of a year (1-year DP) or over the entire lifetime of the exposure (lifetime DP);
- Loss Given Default (LGD): the percentage of loss in the event of default on the basis of historical experience over a given observation period;
- Exposure at Default (EaD): the amount of exposure at the time of default.

In defining the scope of the model, with respect to the regulatory parameters, we have taken into account:
- the conditions of the current economic cycle (Point-in-Time risk measures);
- forecast information regarding the future trends in market factors (forward-looking risk measures) on which the expected lifetime loss depends. This forecast information refers to a defined time period (typically the expected duration of the credit exposure under assessment).

Additionally, factors that are only relevant for regulatory purposes (such as the down turn component considered in the regulatory LGD calculation to account for the adverse economic cycle) were removed, while the risk parameters over the entire lifetime of the instrument were considered.

As noted, the definition of default adopted is in line with that used for regulatory purposes.

In addition, in compliance with the requirements of the standard, according to which the estimate of the ECL must be the result of weighting a series of possible forward-looking scenarios (unbiased and probability weighted), the Group has developed a methodology for generating multiple macroeconomic scenarios with the associated probability of their occurrence. More specifically, in addition to the most likely (50%) baseline scenario (i.e. the forecast macroeconomic scenario on the basis of which the Group develops its projections for economic/asset and risk data over the short and medium term), alternative scenarios were developed to be better (positive with 20% probability and very positive with 5% probability) and worse (severe with 20% probability and very severe with 5% probability).

More detailed information on the way in which the Group has determined the aforementioned IFRS 9 compliant risk parameters is provided below.

Estimating the DP parameter
As illustrated above, the probability of default must be estimated not only in the twelve months following the reporting date, but also in future years in order to allow lifetime provisions to be calculated.
For the Group, the DP curves were constructed by multiplying the PiT migration matrices of the various risk segments defined by the internal rating models (Large Corporate, Mid Corporate, Mid Corporate Plus, Small Business, Private) which are conditioned on the economic cycle. The main methodological steps used to estimate the lifetime DP parameter are provided below:

- the construction of historical PiT migration matrices for each risk segment defined by the rating models and on the basis of the average of these matrices and the attainment of the long-term matrices (TTC) for each risk segment;
- the determination of future PiT matrices for the first three years following the reporting date, obtained on the basis of PiT matrices conditioned on the basis of selected macroeconomic scenarios, to which the respective probability of occurrence is associated, using satellite models (the Merton method) capable of expressing the sensitivity of the DP measures to changes in the main income statement items. These satellite models are differentiated by geo-sectoral clusters (e.g. industry, financial companies, consumer households) and use cluster-specific variables;
- obtaining cumulative DP by rating class, multiplying the future PiT matrices as previously calculated for the first three years, while from the fourth year onwards the TTC matrix is used. When the TTC matrix differs significantly from the last future PiT matrix, calculated for each selected scenario, a Smoothing Phase is provided;
- the generation of the cumulative lifetime DP curve as the average of the cumulative DP curves of each selected macroeconomic scenario weighted by the respective probability of occurrence.

Estimating the LGD parameter

In addition to the removal of adjustments used for regulatory purposes (indirect costs and down turn factor), from a forward-looking perspective, the estimate of this parameter takes into account the impact of the economic cycle on both the value associated with real estate guarantees through the property price index (thus changing the ratio between the residual debt and the value of the guarantee) and the component represented by the probability of bad loans via a specific scaling factor obtained by simulating the default cycles with the migration matrices between statuses.

EAD Estimation

To calculate the parameter in question, the exposure considered at each future payment date is represented by the residual debt, based on the amortisation plan, increased by any instalments due/past due.
For off-balance-sheet exposures (guarantees and commitments to disburse funds, whether irrevocable or revocable), the EAD is equal to the nominal value weighted by a specific credit conversion factor (CCF).

Expected Credit Loss – Stage 3

With reference to non-performing loans, corresponding to assets classified in Stage 3, although substantially in line with the scope of non-performing loans based on the previous IAS 39 standard, a specific methodology was developed to include forward-looking elements related to sales scenarios, in addition to the scenario that provides for the recovery of cash flows through internal management (the multi-scenario approach). As expressly provided for by the ITG[5] of the IASB, it is possible to consider the flows recoverable through sale when determining the expected losses, to the extent that it is possible to develop expectations and assumptions inferred on the basis of reasonable and demonstrable information (please see the following document on this subject: Meeting Summary – 11 December 2015 - Inclusion of cash flows expected from the sale on default of a loan in the measurement of expected credit losses).

The Group set objectives to achieve in terms of reducing the incidence of bad loans and total impaired loans compared to the total amount of loans to customers when defining its NPL Strategy. The achievement of these objectives presupposes that the amount of impaired loans may be reduced as a result of recovery activity. Given that the recovery forecasts through management within the Group would not have guaranteed the achievement of objectives, the Group has planned, as part of its NPL Strategy, to dispose of a total nominal amount of 8.5 billion euro in outstanding bad loans as at 1 January 2018. In light of the above, it was deemed that the conditions existed for considering the sales scenario approved and made public in determining the new valuation of bad loans at the date of transition to the new IFRS 9 standard.
Given the above, a new valuation model has been developed on the basis of which two different estimates of the cash flows that the Group expects to receive are associated for each bad loan:
- the first is determined assuming recovery from the debtor based on internal activity, in line with the valuations conducted pursuant to the IAS 39 accounting standard (workout scenario);
- the second is calculated assuming recovery by assigning the receivable (sale scenario).

[5] This is the IFRS Transition Resource Group for impairment of financial instruments, a working group established to support the implementation of certain issues relating to the new IFRS 9 impairment model.

Taking into account that at first time adoption, as well as when fully operational, the loans likely to be sold cannot be individually identified, the model provides that each loan is associated with a probability of sale.
The forecasts for expected losses are therefore equal to the weighted average of the estimate of the recoverable cash flows in the two scenarios (workout and sale), based on the probability of their occurrence. Probability is assigned to the various scenarios assuming the segmentation of the Group's total portfolio of bad loans, in accordance with the main characteristics that influence the value attributed by the market to loans of this type (for example: vintage, amount of exposures, type of product, presence of collateral and type, customer segment).
The probability assigned to the various clusters was guided by the amount of the level of target disposals approved by the Board of Directors and, as noted, equal to a nominal amount of 8.5 billion euro between 2018-2020. In other words, the probabilities have been assigned to the various clusters in such a way that the sum of the total nominal values of each cluster multiplied by the relative probability of transfer (hereinafter also "expected transfer value") amounts to 8.5 billion euro. More specifically, the probabilities assigned to the various clusters range from a minimum value of 2%—assigned to the cluster that the Group deems less convenient and therefore less likely to sell—up to a maximum value of 85%, which is assigned to the cluster that the Group deems more likely to sell. In this regard, please note that, at first time adoption, this last cluster was populated with the exposures that the Group deemed most likely to be included in the portfolio of disposals relating to the Exodus project, which was scheduled to be completed by the end of the first half of 2018, as illustrated in the significant events of the Interim Report on Operations (5.1 billion euro in expected transfer value corresponding to a population of exposures that amounts to a nominal value of 6 billion euro).
The valuation method used to calculate the recovery flows through sale is based on a discounting process for the recoverable cash flows (discounted cash flows), which takes into account the main parameters that are normally considered by potential buyers when defining the purchase price.

Hedge Accounting

In regard to hedge accounting, the new rules introduced by IFRS 9 aim to ensure greater alignment between the accounting representation of the hedges and the underlying management logic (risk management). However, these rules do not concern the macro hedging model for which an ad hoc and separate project has been implemented with respect to IFRS 9, which currently has not led to any accounting standard.
At first time adoption, the Group decided to opt-out to avail itself of the possibility of continuing to manage hedging transactions in accordance with the hedge accounting rules provided for by IAS 39 which are currently endorsed (in the carve-out version). This choice will be re-evaluated for reporting after 2018.

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

Impacts of IFRS 9 on the book value of shareholders' equity at 1 January 2018

With the adoption of IFRS 9, the consolidated shareholders' equity of the Banco BPM Group decreased by 1,056.6 million euro net of tax effects, falling from 11,963.5 million euro to 10,906.9 million euro. Specifically, this reduction is due to the following:

- -1,245.8 million euro due to the increase in adjusting entries because of the adoption of the new impairment model for impaired loans (bad loans);
- -90.1 million euro due to the increase in adjusting entries after the adoption of the new impairment model for non-performing loans and debt securities (classified under Stage 1 and Stage 2);
- -16.5 million euro due to the increase in liability provisions linked to the valuation of guarantees given and commitments to disburse funds, whether irrevocable or revocable;
- + 38.8 million euro following the adoption of the new rules for the classification and measurement of financial assets and liabilities, excluding the impact originating from the new model for calculating expected losses, as described above;

- -92.3 million euro due to the reduction in the value of investments in associates and companies subject to joint control that were measured with the equity approach, following the overall negative impact on shareholders' equity recorded by the same associates on the first time adoption of IFRS 9[6];
- +349.3 million euro due to the recognition of higher deferred tax assets relating to tax losses being processed as a result of the reduction in the book value of shareholders' equity described above[7].

The effects noted previously resulted in a reduction of 78.2 million euro in valuation reserves and 978.4 million euro in other equity reserves.

These impacts are highlighted in even greater detail in the following reconciliation schedule between shareholders' equity at 31 December 2017, determined in compliance with the former IAS 39 accounting standard, and shareholders' equity restated at 1 January 2018 due to the adoption of the new accounting standard.

[6] These impacts are attributable to the equity investments held in Agos Ducato S.p.A., Alba Leasing S.p.A., SelmaBipiemme Leasing S.p.A. And Factorit S.p.A.. Conversely, the equity investments held in Vera Vita S.p.A. and Vera Assicurazioni S.p.A were not affected, as these companies continue to apply the IAS 39 accounting standard, having opted for the deferral approach pending the entry into force of the new international accounting standard for insurance contracts (IFRS 17). In this regard, note that insurance companies have the right to postpone (however, no later than 2021) the entry into force of the IFRS 9 standard (the deferral approach) or to suspend the increased volatility introduced by the new standard to individual securities in shareholders' equity (the overlay approach).

[7] The Decree issued by the Ministry of Economy and Finance on 10 January 2018 established that the negative equity impact caused by the adoption of the new impairment model introduced by the IFRS 9 accounting standard can be deducted from the taxable income for IRES and IRAP for 2018. Consequently, at the date of first time adoption, a tax loss was generated for the Group's biggest companies, which is being processed. Pursuant to current legislation, IRES tax losses can be carried forward and can be recovered by generating taxable income in subsequent years without any time limit. However, IRAP tax losses cannot be carried forward. Given this legislation, tax assets recorded by the FTA are almost exclusively attributable to IRES taxation.

Table 1: Reconciliation schedule between shareholders' equity at 31 December 2017 (IAS 39) and shareholders' equity at 1 January 2018 (IFRS 9)

Imports in thousands of euro -			of which IFRS FTA impact 9 on item "120. Valuation reserves"	of which IFRS FTA impact 9 on item "150. Reserves"
A	**Consolidated shareholders' equity at 31 December 2017 (formerly IAS 39)**	**11,963,540**		
	of which: Group shareholders' equity	11,900,230		
	of which: minority interests in shareholders' equity	63,310		
B	**Impact of IFRS 9 measurement of expected credit losses (ECL) on impaired financial assets (Stage 3)**	**(1,245,844)**	**-**	**(1,245,844)**
	Fin. assets designated at amortised cost - Loans to customers	(1,245,844)		(1,245,844)
C	**Impact of IFRS 9 for the measurement of expected credit losses (ECL) on non-impaired financial assets (Stage 1 and Stage 2)**	**(90,089)**	**7,137**	**(97,226)**
	Fin. assets designated at amortised cost - Loans to customers	(73,898)		(73,898)
	Fin. assets designated at amortised cost - Loans to banks	(2,716)		(2,716)
	Fin. assets designated at amortised cost - Debt securities	(13,475)		(13,475)
	Fin. assets designated at fair value through other comprehensive income	-	7,137	(7,137)
D	**Impact of IFRS 9 for measuring expected credit losses (ECL) on off-balance sheet exposures**	**(16,451)**	**-**	**(16,451)**
	Guarantees and commitments	(16,451)		(16,451)
E	**Impact of IFRS 9 classification & measurement (excluding ECL measurement)**	**38,769**	**(80,210)**	**118,979**
	Fin. assets designated at FV through IS - debt securities	(12,237)	(6,823)	(5,414)
	Fin. assets designated at FV through IS - equity instruments and UCIT	-	(128,042)	128,042
	Assets designated at FV through IS - Loans to customers	(6,671)		(6,671)
	Fin. assets designated at fair value through OCI - debt securities	51,600	51,859	(259)
	Assets designated at amortised cost - Debt securities	17,713	17,504	209
	Financial liabilities designated at fair value	(15,254)	(14,708)	(546)
	Financial liabilities held for trading	3,618		3,618
F	**Impact of IFRS 9 on investments in associates (equity method)**	**(92,348)**	**-**	**(92,348)**
	Investments in associates	(92,348)		(92,348)
G=B+C +D+E+F	**Total impact of IFRS 9 on consolidated shareholders' equity at 1 January 2018 (before tax)**	**(1,405,963)**	**(73,073)**	**(1,332,890)**
H	**Tax impact as at 1 January 2018**	**349,369**	**(5,156)**	**354,525**
I=G+H	**Total impact of IFRS 9 on consolidated shareholders' equity at 1 January 2018 (after tax)**	**(1,056,594)**	**(78,229)**	**(978,365)**
	of which: impact of IFRS 9 on group shareholders' equity	(1,050,851)	(78,229)	(972,622)
	of which: impact of IFRS 9 on minority interests in shareholders' equity	(5,743)		(5,743)
A+I	**Consolidated shareholders' equity at 1 January 2018 (IFRS 9)**	**10,906,946**		
	of which: Group shareholders' equity	10,849,379		
	of which: minority interests in shareholders' equity	57,567		

Key:
FV: *Fair Value*
IS: Income statement
OCI: Other Comprehensive Income

In this regard, please note that the adoption of the new IFRS 9 measurement and impairment rules has, at times, led to the need to make a mere reclassification between valuation reserves (item 120) and other retained earnings (item 150), with an overall zero impact on the total Group shareholders' equity. Indeed, valuation reserves decreased by 114.6 million euro overall, yet were offset by a corresponding increase in profit reserves.

More specifically:

- the adoption of the new impairment rules for debt securities classified as "financial assets designated at fair value through other comprehensive income" led to a negative effect on profit reserves that amounted to 7.1 million euro (4.8 million euro after tax), offsetting a corresponding increase in valuation reserves;
- the reclassification of debt securities previously classified as financial assets available for sale to the new category of "other financial assets mandatorily at fair value" led to the crediting of profit reserves amounting to 6.8 million euro (4.6 million euro after tax), offsetting the debit of a corresponding amount to valuation reserves;
- the reclassification of UCIT units and equity instruments previously classified as financial assets available for sale to the new category of "other financial assets mandatorily at fair value" led to the crediting of

profit reserves amounting to 128.0 million euro (115.0 million euro after tax) offsetting the debit of a corresponding amount to valuation reserves;
- the reclassification of debt securities previously classified as financial assets designated at fair value through profit and loss to the new category of financial assets designated at fair value through other comprehensive income led to the reallocation of the positive effects (0.3 million euro) to valuation reserves, offsetting the charge to the profit reserve (0.2 million euro after tax).

Impact of IFRS 9 on own funds as at 1 January 2018

At the level of the capital ratios, the impacts at 1 January 2018 illustrated in the previous paragraph led to a reduction of 182 bps in the CET 1 ratio fully phased, which fell from 11.92%—the value before the first time adoption of the new accounting standard—to 10.10%.
These impacts do not account for the option exercised by the Group for the full adoption of the transitional rules introduced by the new article 473-bis of EU Regulation no. 575/2013, which phases in the impact on equity resulting from the adoption of the new impairment model introduced by the new accounting standard.
This transitional regulation offers the possibility of including a positive transitory component in Tier 1 capital for a percentage of the increase in provisions for expected losses on loans as a result of the application of IFRS 9 accounting standards. For off-balance-sheet exposures represented by guarantees and commitments, for which—at 31 December 2017—there were adjusting entries in accordance with the IAS 37 standard, the amount to be included in CET1 is not limited to the increase in the adjusting entries, but rather is equal to the absolute value of the adjusting entries for IFRS 9 expected losses[8].

This percentage will decrease over five years, as shown below:
- period from 1 January to 31 December 2018: 95% of the increase in provisions for expected credit losses due to the adoption of the IFRS 9 accounting standard. The expected negative impact deriving from the adoption of the new impairment model to own funds is consequently reduced to 5% of the impact that will be recorded on the book value of shareholders' equity as of 1 January 2018;
- period from 1 January 2019 to 31 December 2019: 85% of the increase in provisions for expected credit losses;
- period from 1 January 2020 to 31 December 2020: 70% of the increase in provisions for expected credit losses;
- period from 1 January 2021 to 31 December 2021: 50% of the increase in provisions for expected credit losses;
- period from 1 January 2022 to 31 December 2022: 25% of the increase in provisions for expected credit losses.

From 1 January 2023, the impact deriving from the first time adoption of the IFRS 9 accounting standard will be fully reflected in the calculation of own funds.
In addition to the possibility of phasing in the impact deriving from the first time adoption of the accounting standard on 1 January 2018, the transitional regulation provides for the possibility of phasing in any impacts that the adoption of the new impairment model will produce in the first few years following the first time adoption of the new accounting standard, albeit limited to those arising from the measurement of performing financial assets.

Taking into account the transitional regulations and the treatment of the adjusting entries relating to off-balance sheet exposures, as illustrated above, the impact of the first time adoption of IFRS 9 on CET1 for the entire 2018 financial year was up by 5 bps.

[8] In this regard, please refer to the EBA Q&A no. 2018/3923 of 25 May 2018.

Consolidated balance sheet - reconciliation between the balances at 31 December 2017 (IAS 39) and at 1 January 2018 (IFRS 9)

The following table shows the balance sheet format prepared in accordance with the items established by the fifth update of Circular no. 262. Specifically, the above schedule provides a reconciliation between the balances as at 31 December 2017, which were calculated on the basis of IAS 39, and those restated on 1 January 2018, on the basis of the IFRS 9 standard, with separate reporting:

- the reclassified IAS 39 balances in relation to the new classification criteria introduced by IFRS 9 ("31/12/2017 Reclassified IAS 39 balances" column), without the adoption of the new valuation criteria associated with the new accounting categories (different basis of measurement of value and relative impairment);
- The impacts deriving from the new measurement criteria (" Measurement Impact" column) and the new impairment model ("ECL Impact" - Expected Credit Losses column).

In order to come to a better understanding of the transition between the accounting categories of IAS 39 and IFRS 9 financial assets and liabilities, the balances resulting from the financial statements published at 31 December 2017 were reclassified based on the new frameworks of Circular no. 262, in accordance with certain conventional criteria that are described below:

- item "20. Financial assets designated at fair value through profit and loss: a) financial assets held for trading" corresponds to item "20. Financial assets held for trading" in the financial statements published on 31 December 2017;
- item "20. Financial assets designated at fair value through profit and loss: b) financial assets designated at fair value" corresponds to item "30. Financial assets designated at fair value" in the financial statements published on 31 December 2017;
- in item "30. Financial assets designated at fair value through other comprehensive income", the balance of item "40. Financial assets available for sale" was reclassified in the financial statements published on 31 December 2017;
- item "40. financial assets designated at amortised cost" includes the balances of items "50. Investments held to maturity", "60. Due from banks". "70. Loans to customers" shown in the financial statements published as at 31 December 2017;
- for the remaining items, the balances shown correspond to those originally published, although the numbering of the financial statement items differs due to the changes introduced in the IFRS 9 compliant financial statements.

Therefore, the "31/12/2017 IAS 39 balances" column provides the balances at 31 December 2017 (IAS 39) based on the conventional criteria described previously; the "Reclassifications" column gives the differences between the IAS 39 balances restated on the basis of the aforementioned conventional criteria and the same balances restated on the basis of the new classification criteria introduced by the new IFRS 9 standard, guided by the business model and by the characteristics of the cash flows.
In this regard, please note that the reclassification of liabilities from item "80. Other liabilities" to item "100. Provisions for risks and charges" refers to the adjusting entries on guarantees and commitments to be transferred back to the provisions for risks and charges, based on the new provisions introduced by the fifth update of Circular no. 262.

For further details of the transition between the old and new portfolios of financial assets and liabilities, please refer to the following section.

Table 2: reconciliation schedule between total assets at 31 December 2017 (IAS 39) and total assets at 1 January 2018 (IFRS 9)

Asset items (*in thousands of euro*)	**31/12/2017 IAS 39 balances**	**Reclassifications**	**31/12/2017 IAS 39 balances Reclassifications (a)**	**Measurement Impact (b)**	**ECL Impact (c)**	**01/01/2018**	**Impact of IFRS 9 (b+c)**
10. Cash and cash equivalents	976,686		976,686			976,686	-
20. Financial assets designated at fair value through profit and loss	4,940,776	1,251,406	6,192,182	(18,908)	-	6,173,274	(18,908)
a) financial assets held for trading	4,911,824	(17,391)	4,894,433			4,894,433	-
b) financial assets designated at fair value	28,952	(28,952)	-			-	-
c) other financial assets mandatorily at fair value	-	1,297,749	1,297,749	(18,908)		1,278,841	(18,908)
30. Financial assets measured at fair value through other comprehensive income	17,128,622	(430,150)	16,698,472	51,600		16,750,072	51,600
40. Financial assets measured at amortised cost	124,901,866	(821,256)	124,080,610	17,713	(1,335,933)	122,762,390	(1,318,220)
a) due from banks	5,164,715	3,423	5,168,138		(2,987)	5,165,151	(2,987)
b) loans to customers	119,737,151	(824,679)	118,912,472	17,713	(1,332,946)	117,597,239	(1,315,233)
50. Hedging derivatives	243,810		243,810			243,810	-
60. Fair value change of financial assets in macro fair value hedge portfolios (+/-)	54,531		54,531			54,531	-
70. Equity investments	1,349,191		1,349,191	(92,348)		1,256,843	(92,348)
80. Technical reserves of reinsurers	-		-			-	-
90. Property, plant and equipment	2,735,182		2,735,182			2,735,182	-
100. Intangible assets	1,297,160		1,297,160			1,297,160	-
of which:	-		-			-	-
- goodwill	76,389		76,389			76,389	-
110. Tax assets	4,520,189	-	4,520,189	923	370,675	4,891,787	371,598
a) current	319,462		319,462			319,462	-
b) deferred	4,200,727		4,200,727	923	370,675	4,572,325	371,598
120. Non-current assets and asset disposal groups held for sale	106,121		106,121			106,121	-
130. Other assets	2,952,631		2,952,631			2,952,631	-
Total assets	**161,206,765**	**-**	**161,206,765**	**(41,020)**	**(965,258)**	**160,200,487**	**(1,006,278)**

a) Balances as at 31 December 2017 on the basis of the IAS 39 standard, classified according to the new criteria for IFRS 9 financial assets and liabilities

b) IFRS 9 FTA impacts arising from the new measurement criteria for items related to financial assets and financial liabilities (excluding ECL), including indirect consequences resulting from the restatement of the equity of investments in associates and companies subject to joint control under IFRS 9

c) FTA impacts of IFRS 9 arising from the new Expected Credit Losses (ECL) model

Table 3: Reconciliation schedule between total liabilities and shareholders' equity at 31 December 2017 (IAS 39) and total liabilities and shareholders' equity at 1 January 2018 (IFRS 9)

Liability and shareholders' equity items (*in thousands of euro*)	31/12/2017 IAS 39 balances	Reclassifications	31/12/2017 IAS 39 balances Reclassifications (a)	Measurement Impact (b)	ECL Impact (c)	01/01/2018	Impact of IFRS 9 (b+c)
10. Financial liabilities measured at amortised cost	131,295,593	160,370	131,455,963	15,254	-	131,471,217	15,254
a) due to banks	27,199,304		27,199,304			27,199,304	-
b) due to customers	87,848,146		87,848,146			87,848,146	-
c) debt securities issued	16,248,143	160,370	16,408,513	15,254		16,423,767	15,254
20. Financial liabilities held for trading	7,942,063		7,942,063	(3,618)		7,938,445	(3,618)
30. Financial liabilities designated at fair value	3,413,560	(160,370)	3,253,190			3,253,190	-
40. Hedging derivatives	765,903		765,903			765,903	-
50. Fair value change of financial liabilities in macro fair value hedge portfolios (+/-)	8,535		8,535			8,535	-
60. Tax liabilities	669,494	-	669,494	21,037	1,192	691,723	22,229
a) current	14,493		14,493			14,493	-
b) deferred	655,001		655,001	21,037	1,192	677,230	22,229
70. Liabilities associated with assets held for sale	35		35			35	-
80. Other liabilities	3,687,053	(119,472)	3,567,581			3,567,581	-
90. Employee termination indemnities	408,160		408,160			408,160	-
100. Provisions for risks and charges:	1,052,829	119,472	1,172,301	-	16,451	1,188,752	16,451
a) commitments and guarantees given	-	119,472	119,472		16,451	135,923	16,451
b) retirement benefits and similar commitments	166,847		166,847			166,847	-
c) other provisions for risks and charges	885,982		885,982			885,982	-
110. Technical reserves	-		-			-	-
120. Valuation reserves	251,706		251,706	(83,005)	4,776	173,477	(78,229)
130. Redeemable shares	-		-			-	-
140. Equity instruments	-		-			-	-
150. Reserves	1,946,308		1,946,308	9,312	(981,934)	973,686	(972,622)
160. Share premium reserve	-		-			-	-
170. Share capital	7,100,000		7,100,000			7,100,000	-
180. Treasury shares (-)	(14,146)		(14,146)			(14,146)	-
190. Minority interests (+/-)	63,310		63,310		(5,743)	57,567	(5,743)
200. Income (Loss) for the period (+/-)	2,616,362		2,616,362			2,616,362	-
Total liabilities and shareholders' equity	**161,206,765**	**-**	**161,206,765**	**(41,020)**	**(965,258)**	**160,200,487**	**(1,006,278)**

a) Balances as at 31 December 2017 on the basis of the IAS 39 standard, classified according to the new criteria for IFRS 9 financial assets and liabilities
b) FTA impacts of IFRS 9 arising from the new measurement criteria for items related to financial assets and financial liabilities (excluding ECL)
c) FTA impacts of IFRS 9 arising from the new Expected Credit Losses (ECL) model

Portfolio of financial assets and liabilities - reconciliation between the balance sheet items published as at 31 December 2017 (IAS 39) and the balance sheet items provided in the new IFRS 9 balance sheet

The tables below provide detailed information on the reconciliation between:

- the items of IAS 39 financial assets and liabilities, as represented in the balance sheet prepared based on the criteria established in the fourth update of Bank of Italy Circular no. 262, which was originally published on 31 December 2017;
- the same financial assets and liabilities, which were restated based on the balance sheet items introduced by the fifth update of the Bank of Italy Circular no. 262, on the basis of the new classification, measurement and impairment criteria provided by IFRS 9.

Specifically, in line with the disclosure requirements established by IFRS 7 with reference to the first time adoption of the standard:

- table 4 illustrates that the balances of the financial assets relating to each IAS 39 accounting category have been reclassified to the new accounting categories in accordance with the reclassifications that were made necessary by the classification criteria introduced by IFRS 9 (IAS 39 reclass. values), as well as the related impacts on measurement and expected losses (Imp. Measurement" and ECL impact);
- table 5 shows the impact of the first time adoption of IFRS 9 on each type of financial instrument (debt securities, equity securities and UCIT units);
- table 6 illustrates the methods used to reclassify the balances of the financial liabilities relating to each IAS 39 accounting category to the new IFRS 9 accounting categories and their relative measurement impact;
- table 7 illustrates, with reference to cash exposures and off-balance-sheet exposures represented by financial guarantees given and commitments to disburse funds, the reconciliation between the adjusting entries for incurred losses determined on the basis of the previous accounting standards IAS 39 and IAS 37 and the adjustments for expected losses calculated on the basis of the new IFRS 9 impairment model.

In this regard, please note that the tables shown above do not furnish any evidence of financial assets and liabilities represented by hedging derivatives as they were not affected by the transition to the new IFRS 9 standard.

Table 4: reconciliation between the accounting categories of financial assets as at 31 December 2017 (IAS 39 values) and the accounting categories of financial assets as at 1 January 2018 (IFRS 9 compliant values) showing the reclassified amounts and the C&M and ECL impacts

FINANCIAL ASSET ITEMS as at 31/12/2017 - IAS 39 Values		FINANCIAL ASSET ITEMS AS AT 01/01/2018 - IFRS 9 compliant values						IFRS 9 FTA IMPACT ON CONSOLIDATED SHAREHOLDERS' EQUITY AS AT 01/01/2018		
(A)		(B)						(C) = (B) - (A)		
		20. Fin. assets designated at FV through IS: a) trade	20. Fin. assets designated at FV through IS: b) designated at FV	20. Fin. assets designated at FV through IS: c) mandatorily at fair value	30. Fin. assets designated at FV through other comprehensive income	40. Fin. assets designated at amortised cost: a) due from banks	40. Fin. assets designated at amortised cost: b) Loans to customers	FTA IFRS 9 impact on Group shareholders' equity as at 01/01/2018	*- of which FTA IFRS 9 impact on "valuation reserves" as at 01/01/2018*	*- of which IFRS FTA impact 9 on "Reserves" as at 01/01/2018*
20. Fin. assets held for trading	**4,911,824**	**4,894,433**					**15,991**	**-1,400**		**-1,400**
- IAS 39 reclass. values	*-4,911,824*	*4,894,433*					*17,391*			
- imp. measurement							*209*	*209*		*209*
- ECL impact							*-1,609*	*-1,609*		*-1,609*
30. Fin. assets designated at fair value	**28,952**			**20,960**	**7,992**			**0**	**275**	**-275**
- IAS 39 reclass. values	*-28,952*			*20,960*	*7,992*					
- imp. measurement								*0*	*259*	*-259*
- ECL impact								*0*	*16*	*-16*
40. Fin. assets available for sale	**17,128,622**			**832,072**	**14,290,445**		**2,023,403**	**17,298**	**-110,404**	**127,702**
- IAS 39 reclass. values	*-17,128,622*			*832,072*	*14,290,445*		*2,006,105*			
- imp. measurement							*17,504*	*17,504*	*-117,361*	*134,865*
- ECL impact							*-206*	*-206*	*6,957*	*-7,163*
50. Fin. assets held to maturity	**11,560,769**				**2,451,635**	**3,423**	**9,155,664**	**49,953**	**51,764**	**-1,811**
- IAS 39 reclass. values	*-11,560,769*				*2,400,035*	*3,423*	*9,157,311*			
- imp. measurement					*51,600*			*51,600*	*51,600*	*0*
- ECL impact							*-1,647*	*-1,647*	*164*	*-1,811*
60. Due from banks	**5,164,715**					**5,161,728**		**-2,987**		**-2,987**
- IAS 39 reclass. values	*-5,164,715*					*5,164,715*				
- ECL impact						*-2,987*		*-2,987*		*-2,987*
70. Loans to customers	**108,176,382**			**425,809**			**106,402,181**	**-1,348,392**		**-1,348,392**
- IAS 39 reclass. values	*-108,176,382*			*444,717*			*107,731,665*			
- imp. measurement				*-18,908*				*-18,908*		*-18,908*
- ECL impact							*-1,329,484*	*-1,329,484*		*-1,329,484*
Total financial assets	**146,971,264**	**4,894,433**	**0**	**1,278,841**	**16,750,072**	**5,165,151**	**117,597,239**	**-1,285,528**	**-58,365**	**-1,227,163**
- IAS 39 reclass. Values - securities	*-34,289,362*	*4,894,433*		*983,051*	*16,698,472*	*225,492*	*11,484,491*			
- IAS 39 reclass. Values - loans	*-112,681,902*			*314,698*		*4,939,223*	*107,427,981*			
- imp. measurement				*-18,908*	*51,600*		*17,713*	*50,405*	*-65,502*	*115,907*
- ECL impact						*-2,987*	*-1,332,946*	*-1,335,933*	*7,137*	*-1,343,070*

Table 5: reconciliation between the accounting categories of financial assets as at 31 December 2017 (IAS 39 values) and the accounting categories of financial assets as at 1 January 2018 (IFRS 9 compliant values) by type of financial instrument

FINANCIAL ASSET ITEMS as at 31/12/2017 - IAS 39 Values		FINANCIAL ASSET ITEMS AS AT 01/01/2018 - IFRS 9 compliant values						IFRS 9 FTA IMPACT ON CONSOLIDATED SHAREHOLDERS' EQUITY AS AT 01/01/2018		
(A)		(B)						(C) = (B) - (A)		
		20. Fin. assets designated at FV through IS: a) trade	**20. Fin. assets designated at FV through IS: b) designated at FV**	**20. Fin. assets designated at FV through IS: c) mandatorily at fair value**	**30. Fin. assets designated at FV through other comprehensive income**	**40. Fin. assets designated at amortised cost: a) due from banks**	**40. Fin. assets designated at amortised cost: b) Loans to customers**	**FTA IFRS 9 impact on Group shareholders' equity as at 01/01/2018**	***- of which FTA IFRS 9 impact on "valuation reserves" as at 01/01/2018***	***- of which IFRS FTA impact 9 on "Reserves" as at 01/01/2018***
20. Fin. assets held for trading	**4,911,824**	**4,894,433**					**15,991**	**-1,400**		***-1,400***
- debt securities	*2,283,911*	*2,266,520*					*15,991*	*-1,400*		*-1,400*
- equity instruments	*693,004*	*693,004*								
- UCITS units	*29,661*	*29,661*								
- derivatives	*1,905,248*	*1,905,248*								
30. Fin. assets designated at fair value	**28,952**			**20,960**	**7,992**			**0**	***275***	***-275***
- debt securities	*9,412*			*1,420*	*7,992*			*0*	*275*	*-275*
- equity instruments	*579*			*579*						
- UCITS units	*18,961*			*18,961*						
40. Fin. assets available for sale	**17,128,622**			**832,072**	**14,290,445**		**2,023,403**	**17,298**	***-110,404***	***127,702***
- debt securities	*15,716,663*			*179,445*	*13,531,113*		*2,023,403*	*17,298*	*17,638*	*-340*
- equity instruments	*993,472*			*234,140*	*759,332*			*0*	*-112,391*	*112,391*
- UCITS units	*418,487*			*418,487*	*0*			*0*	*-15,651*	*15,651*
50. Fin. assets held to maturity	**11,560,769**				**2,451,635**	**3,423**	**9,155,664**	**49,953**	***51,764***	***-1,811***
- debt securities	*11,560,769*				*2,451,635*	*3,423*	*9,155,664*	*49,953*	*51,764*	*-1,811*
60. Due from banks	**5,164,715**					**5,161,728**		**-2,987**		***-2,987***
- loans	*4,939,223*					*4,936,507*		*-2,716*		*-2,716*
- debt securities	*225,492*					*225,221*		*-271*		*-271*
70. Loans to customers	**108,176,382**			**425,809**			**106,402,181**	**-1,348,392**		***-1,348,392***
- loans	*107,742,679*			*308,027*			*106,108,239*	*-1,326,413*		*-1,326,413*
- debt securities	*433,703*			*117,782*			*293,942*	*-21,979*		*-21,979*
Total financial assets	**146,971,264**	**4,894,433**		**1,278,841**	**16,750,072**	**5,165,151**	**117,597,239**	**-1,285,528**	***-58,365***	***-1,227,163***

Effects of the first time adoption of IFRS 9 – Classification, measurement and impairment of financial assets

Based on the information provided in the tables above, the measurement criteria of the new IFRS 9 accounting categories—into which the outstanding instruments at the transition date have been classified—are substantially in line with those of the previous IAS 39 categories, with the exception of a few instances caused by changes in the business model, the intrinsic characteristics of financial instruments and the adoption of accounting choices permitted by the standard. In this regard, please note that the portfolio represented by UCIT units has been entirely reclassified under "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value", as the related flows are not comprised solely of the payment of principal and interest. For these instruments, also on the basis of the clarifications provided by the IFRIC (IFRS Interpretation Committee) in May 2017, the possibility of using the category of financial assets designated at fair value through other comprehensive income was not deemed possible. This was due to the fact that these UCIT units are not normally comparable to equity instruments as they entail a contractual obligation to deliver certain financial assets or a net asset in the event of liquidation or a redemption request from the subscriber.

More specifically, on the date of first time adoption, the classification of the portfolio of financial assets, based on the existing business model as at 1 January 2018, was carried out in accordance with the following guidelines:

- the IAS 39 portfolio of "Financial assets held for trading" (4,911.8 million euro) was almost entirely classified within the IFRS 9 accounting category of "Financial assets designated at fair value through profit and loss: a) financial assets held for trading" (4.894,4 million euro), with the exception of a debt security issued by a corporate counterparty, which was classified in the "Financial assets designated at amortised cost" category. The measurement at amortised cost (16.0 million euro) compared to fair value (17.4 million euro) led to the debiting of shareholders' equity during FTA that amounted to 1.4 million euro, due to the combined effect of the reversal of valuation losses (+0.2 million euro) and the recognition of expected losses (-1.6 million euro);
- the IAS 39 portfolio of "Financial assets designated at fair value" (29.0 million euro) was largely reclassified to the IFRS 9 accounting category of "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value", (21.0 million euro) and, for residual positions only, to the category of "Financial assets designated at fair value through other comprehensive income" (8.0 million euro). The reclassification to "Other financial assets required to be measured at fair value", which mainly concerns UCIT units, is due to failure to pass the SPPI test. At first time adoption, this classification did not affect total shareholders' equity, since fair value is the measurement criterion for the financial assets in question, both on the basis of IAS 39 and IFRS 9. As at 1 January 2018, there were no financial instruments for which the Group choose to use the option to designate at fair value through profit and loss;
- the IAS 39 portfolio of debt securities included in the "Financial assets available for sale" category (15,716.7 million euro) was mainly classified in the IFRS 9 accounting category of "Financial assets designated at fair value through other comprehensive income" (13,531.1 million euro), with the exception of certain government securities (2,006.1 million euro) which were classified in the IFRS 9 category of "Financial assets designated at amortised cost", due to the way in which these assets were managed at the transition date. This choice had a positive impact of 17.5 million euro on shareholders' equity, equal to the difference between the book value at 31 December 2017, represented by fair value (2,006.1 million euro), and the value resulting from application of the amortised cost (2,023.4 million euro), net of expected losses (-0.2 million euro). Additionally, there were certain debt instruments, of a limited number and value (179.4 million euro), which, under the IFRS 9 standard, had to be classified in "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value", due to failure to pass the SPPI test;
- the IAS 39 portfolio of equity instruments included in the category of "Financial assets available for sale" (993.5 million euro) was mainly classified (759.3 million euro) within "Financial assets designated at fair value through other comprehensive income", due to the option permitted by the standard for instruments held for non-trading purposes. The remaining amount (234.1 million euro) was classified in the IFRS 9 category of "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value". This classification did not affect total shareholders' equity and accounted for the fact that the aforementioned assets were and continue to be designated at fair value;
- the IAS 39 portfolio of "Investments held to maturity" (11,560.8 million euro) was almost entirely reclassified to the IFRS 9 accounting category of "Financial assets designated at amortised cost" (9,160.7

million euro), except for certain positions in government securities (2,400.0 million euro) which were reclassified to the IFRS 9 portfolio of "Financial assets designated at fair value through other comprehensive income", in line with the objectives for which they are held. In regard to these last securities, the first time adoption had a positive impact on shareholders' equity (51.6 million euro) amounting to the difference between the book value as at 31 December 2017 represented by the amortised cost (2,400.0 million euro) and the respective fair value measured as at 1 January 2018 (2,451.6 million euro). In regard to the securities reclassified in the amortised cost category, the expected losses were also calculated with a consequent negative impact on FTA shareholders' equity of 1.6 million euro;

- the positions classified in the IAS 39 portfolio of "Due from banks", amounting to 5,164.7 million euro, were entirely classified in the IFRS 9 category of "Financial assets designated at amortised cost: a) due from banks", in line with the objectives for which they are held. At FTA, the measurement of expected losses led to an increase in adjusting entries of 3.0 million euro;
- the positions classified under the IAS 39 portfolio of "Loans to customers", amounting to 108,176.4 million euro, were classified—for 107,731.7 million euro—in the IFRS 9 category of "Financial assets designated at amortised cost: b) loans to customers"; the measurement of expected losses on the basis of the new impairment model had a negative impact on shareholders' equity of 1,329.5 million euro, of which 1,245.8 million euro was related to bad loans (Stage 3). Exposures amounting to 444.7 million euro (consisting of loans amounting to 314.7 million euro and debt securities amounting to 130.0 million euro) are exceptions to the aforementioned rule, which failed the SPPI test and had to be reclassified to the portfolio of "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value". In regard to the last positions, the impact on shareholders' equity due to the different measurement criterion was negative by 18.9 million euro (6.7 million euro for loans and 12.2 million euro for debt instruments).

Given that the impact of the classification and measurement of financial assets at FTA—which is not attributable to the new impairment criterion—is insignificant overall, it should be noted that the increase in securities designated at fair value through profit and loss, with particular reference to the equity instruments and UCIT units previously classified in the "Financial assets available for sale" portfolio, will, with all other conditions being equal, cause greater volatility in the financial results recognised as from 1 January 2018.

Disclosure on portfolio transfers at FTA

Provided below is the information required by IFRS 7 (paragraphs 42M and 42N) on the effects of the reclassification of financial instruments reclassified at amortised cost—from accounting categories measured on the basis of a different criterion compared to amortised cost—and for instruments reclassified from assets designated at fair value through other comprehensive income, previously designated at fair value through profit and loss. Specifically, for the first accounting period in which IFRS 9 is applied, the following indications must be provided: the fair value of the reclassified financial instruments, of the profits or losses that would have been recorded in the income statement or in the valuation reserves if the instruments had continued to be valued on the basis of the previous fair value criterion, and the interest recorded on the reclassified financial instruments on the basis of the effective interest rate.

As made evident in table 4, for the Banco BPM Group the only noteworthy instruments that have been reclassified are government securities, which were previously classified in the portfolio of "Financial assets available for sale" (2,006.1 million euro), and which have been reclassified to "Financial assets designated at amortised cost" (2,023.4 million euro), in relation to the method of management of these securities that is substantially based on the collection of contractual flows.
As at 30 June 2018, the fair value of these securities amounted to 1,981.2 million euro; if not reclassified within securities at amortised cost, the measurement at fair value would have led to the debiting of valuation reserves in the period amounting to 41.2 million euro. Interest recognised during the first half of 2018 on the basis of the effective interest rate was 19.3 million euro, in line with the amounts that would have been recognised in the same period without reclassification.

Table 6: reconciliation between the accounting categories of financial liabilities as at 31 December 2017 (IAS 39 values) and the accounting categories of financial liabilities as at 1 January 2018 (IFRS 9 compliant values)

FINANCIAL LIABILITY ITEMS as at 31/12/2017 - IAS 39 Values		FINANCIAL LIABILITY ITEMS AS AT 01/01/2018 - IFRS 9 compliant values					FTA IFRS 9 IMPACT ON CONSOLIDATED SHAREHOLDERS' EQUITY AS AT 01/01/2018		
(A)		(B)					(C) = (B) - (A)		
		10. Fin. liab. designated at amortised cost: a) due to banks	10. Fin. liab. designated at amortised cost: b) due to customers	10. Fin. liab. designated at amortised cost: a) debt securities issued	20. Fin. liab. held for trading	30. Fin. liab. designated at FV	FTA IFRS 9 impact on Group shareholders' equity as at 01/01/2018	*- of which FTA IFRS 9 impact on "valuation reserves" as at 01/01/2018*	*- of which IFRS FTA impact 9 on "Reserves" as at 01/01/2018*
10. Due to banks	**27,199,304**	**27,199,304**					-		
20. Due to customers	**87,848,146**		**87,848,146**				-		
30. Debt securities issued	**16,248,143**			**16,248,143**			-		
40. Financial liabilities held for trading	**7,942,063**				**7,938,445**		**3,618**		**3,618**
- due to banks	**6,176**				**6,176**		-		
- due to customers	**816,729**				**816,729**		-		
- debt securities	**3,953,232**				**3,953,232**		-		
- derivative instruments	**3,165,926**				**3,162,308**				
- IAS 39 reclass. values	*3,165,926*				*3,165,926*				
- imp. measurement					*(3,618)*		***3,618***		*3,618*
50. Financial liabilities designated at FV	**3,413,560**			**175,624**		**3,253,190**	**(15,254)**	**(14,708)**	**(546)**
- IAS 39 reclass. values	*3,413,560*			*160,370*		*3,253,190*			
- imp. measurement				*15,254*			***(15,254)***	*(14,708)*	*(546)*
Totals	**142,651,216**	**27,199,304**	**87,848,146**	**16,423,767**	**7,938,445**	**3,253,190**	**(11,636)**	**(14,708)**	**3,072**
- IAS 39 reclass. values	*6,579,486*			*160,370*	*3,165,926*	*3,253,190*			
- imp. measurement				*15,254*	*(3,618)*		*(11,636)*	*(14,708)*	*3,072*

With reference to financial liabilities, the Banco BPM Group has exercised the right to adopt changes in the accounting treatment of its creditworthiness for financial liabilities designated at fair value in advance, since its 2017 financial statements. Therefore, no FTA impact is attributable to the presentation of the effects related to the different ways in which the creditworthiness of a company is measured. Considering that the IFRS 9 standard substantially adopted the classification and measurement criteria of IAS 39, the transition to the new standard did not affect shareholders' equity, with the exception of two obligations classified in the IAS 39 portfolio of "Financial liabilities designated at fair value through profit and loss" for which, accounting for the transitional provisions of the standard, a reclassification to "Financial liabilities designated at amortised cost" was necessary, as it was impossible to justify the previous valuation with the need to eliminate an outstanding accounting mismatch on the date of transition to the new standard[9]. Financial liabilities were therefore recognised on the basis of amortised cost, which amounted to 175.6 million euro, compared to the previous fair value of 160.4 million euro. The subsequent recognition of a higher value under liabilities consequently negatively affected total shareholders' equity, which amounts to 15.2 million euro.

Lastly, the decrease in 3.6 million euro in "Financial liabilities held for trading" was due to the reversal of the derivative implicit in some loan agreements, accounting for the new IFRS 9 rules for the separation of derivatives from financial assets and the fact that the aforementioned assets were reclassified to the item "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value" after failing to pass the SPPI test.

[9] The derivative contract hedging the risks connected with the aforementioned liabilities that motivated the original designation at fair value was subsequently derecognised.

Table 7: Reconciliation schedule of the adjustments for IAS 39 credit risk and of the provisions as per IAS 37 (balances as at 31 December 2017) and the adjustments for credit risk as at 1 January 2018 (IFRS 9 compliant)

ITEMS IN IAS 39 BALANCE SHEET	ITEMS IN THE IFRS 9 BALANCE SHEET	31/12/2017 Total adjustments for IAS 39 credit risk		Effect of reclassification		Effect of loss remeasurement		01/01/2018 Total adjustments for IFRS 9 credit risk	
		Non-performing assets	Performing assets	Non-performing assets Stage 3	Performing assets Stage 1 and 2	Non-performing assets Stage 3	Performing assets Stage 1 and 2	Non-performing assets Stage 3	Performing assets Stage 1 and 2
40. Fin. assets available for sale	**20. Fin. assets designated at FV through IS: c) other fin. assets mandatorily at FV**	**39,251**		**-39,251**					
- securities	- securities	39,251		-39,251					
70. Loans to customers	**20. Fin. assets designated at FV through IS: c) other fin. assets mandatorily at FV**	**152,259**	**16,849**	**-152,259**	**-16,849**				
- securities	- securities	15,032	16,380	-15,032	-16,380				
- loans	- loans	137,227	469	-137,227	-469				
30. Financial assets designated at fair value through profit and loss	**30. Fin. assets designated at FV through other comprehensive income**						**16**		**16**
- securities	- securities						16		16
40. Fin. assets available for sale	**30. Fin. assets designated at FV through other comprehensive income**						**6,957**		**6,957**
- securities	- securities						6,957		6,957
50. Fin. assets held to maturity	**30. Fin. assets designated at FV through other comprehensive income**						**164**		**164**
- securities	- securities						164		164
20. Fin. assets held for trading	**40. Fin. assets designated at amortised cost**						**1,609**		**1,609**
- securities	- securities						1,609		1,609
40. Fin. assets available for sale	**40. Fin. assets designated at amortised cost**						**206**		**206**
- securities	- securities						206		206
50. Fin. assets held to maturity	**40. Fin. assets designated at AC: b) loans to customers**						**1,647**		**1,647**
- securities	- securities						1,647		1,647
60. Due from banks	**40. Fin. assets designated at AC: a) due from banks**	**1,530**	**1,337**				**2,987**	**1,530**	**4,324**
- securities	- securities						271		271
- loans	- loans	1,530	1,337				2,716	1,530	4,053
70. Loans to customers	**40. Fin. assets designated at AC: b) loans to customers**	**12,270,694**	**302,064**			**1,245,844**	**83,640**	**13,516,538**	**385,704**
- securities	- securities						9,742		9,742
- loans	- loans	12,270,694	302,064			1,245,844	73,898	13,516,538	375,962
On-balance-sheet financial assets		**12,463,734**	**320,250**	**-191,510**	**-16,849**	**1,245,844**	**97,226**	**13,518,068**	**400,627**
100. Other liabilities	**100. Provisions for risks and charges - a) provisions for risks and charges**	**119,472**				**16,451**		**135,923**	
- guarantees given and commitments	- guarantees given and commitments	119,472				16,451		135,923	
Off-balance-sheet exposures		**119,472**				**16,451**		**135,923**	

Effects of the first time adoption of IFRS 9 – Impact on value adjustments

On the FTA date, total adjustments to credit risk on exposures to undergo expected losses amounted to 14,054.6 million euro, of which:

- 13,918.7 million euro related to the accounting portfolios of financial assets designated at amortised cost and financial assets designated at fair value through other comprehensive income (13,518.1 million euro relating to non-performing loans—Stage 3—and 400.6 million to performing loans—Stage 1 and Stage 2);
- 135.9 million euro related to off-balance sheet exposures represented by financial guarantees given and commitments to disburse funds of an irrevocable and revocable nature.

The increase in adjusting entries for financial assets of 1,134.7 million euro compared to the figures at 31 December 2017 (amounting to 12,784.0 million euro), is due to the combined effect of the following factors:

- with reference to non-performing loans:
  - the reduction of value adjustments resulting from reclassifications to the new accounting category not subject to the impairment model represented by "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value", specifically:
    - 39.3 million euro relating to certain impaired debt securities (41.5 million euro gross), previously recognised within "Financial assets available for sale";
    - 152.2 million euro relating to: 15.0 million euro to the reclassification of securities (20.5 million euro gross) and 137.3 million euro to the reclassification of loans (323.5 million euro gross) previously recognised within "Loans to customers" which did not pass the SPPI test;
  - an increase of 1,245.8 million euro in the loan portfolio of "Financial assets designated at amortised cost: b) loans to customers" as a result of the new calculation model;
- with reference to performing loans:
  - the reduction in value adjustments of 16.4 million euro on reclassifications of debt securities (140.9 million euro gross) and 0.4 million euro on loans (128.9 million euro gross), previously recognised within "Loans to customers" and reclassified to the new accounting category not subject to the impairment model represented by "Financial assets designated at fair value through profit and loss: c) other financial assets required to be measured at fair value";
  - value adjustments on debt securities classified in the portfolio of "Financial assets designated at fair value through other comprehensive income" amounting to 7.1 million euro (no adjustment entries existed as at 31 December 2017 on the basis of the incurred loss model);
  - value adjustments on debt securities classified in the "Financial assets designated at amortised cost" portfolio, amounting to 13.5 million euro, (no adjustment entries existed as at 31 December 2017 on the basis of the incurred loss model);
  - the new model of expected losses on loans classified as "Financial assets designated at amortised cost" with respect to the model of expected losses of 76.6 million euro compared to the previous incurred losses model;
- with regard to off-balance-sheet exposures represented by financial guarantees given and commitments to disburse funds, the measurement of provisions on the basis of expected losses led to an increase in adjusting entries of 16.5 million euro, mainly attributable to the extension of the impairment model to the scope of revocable margins (15.2 million euro). As at 1 January 2018, the adjusting entries amounted to 136.0 million euro and are shown in balance sheet liability item "100. Provisions for risks and charges a) guarantees given and commitments".

Effects of the first time adoption of IFRS 9 - Credit quality

Based on the above, tables 8 and 9 below provide an analysis of credit quality as at 1 January 2018 for all exposures subject to the IFRS 9 impairment model, i.e. for "Financial assets designated at fair value through other comprehensive income" and for "Financial assets designated at amortised cost" – loans to banks and customers", divided between exposures represented by debt securities and loans.
Specifically, credit quality is expressed in two form: closing-balance exposures and opening-balance exposures.
The representation of credit quality in closing balances is a consequence of the business combination of the former BPM Group on 1 January 2017, which made it necessary to display the net purchase value in the consolidated financial statements as gross exposure, without accounting for the outstanding adjusting entries at the acquisition date.
In order to allow for an assessment of the coverage of exposures, with particular reference to impaired exposures, an opening-balance representation is also provided, which shows the total value adjustments recorded on loans from the date of their disbursement, in line with the credit management and monitoring processes.

Table 8: Credit quality as at 1 January 2018 (IFRS 9) – Closing-balance exposures

The following table displays the breakdown of the exposures subject to the IFRS 9 impairment model by stage (Stage 1, Stage 2 and Stage 3), illustrating the gross exposure, the total adjustment value and the net exposure.

	Gross exposure				Total value adjustments				Net exposure			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
30. Financial assets measured at fair value through other comprehensive income	**15,891,003**	**106,875**	**-**	**15,997,878**	**(5,041)**	**(2,097)**	**-**	**(7,138)**	**15,885,962**	**104,778**	**-**	**15,990,740**
- securities	15,891,003	106,875	-	**15,997,878**	(5,041)	(2,097)	-	**(7,138)**	15,885,962	104,778	-	**15,990,740**
40. Financial assets measured at amortised cost	**98,929,482**	**12,529,308**	**22,694,583**	**134,153,373**	**(63,590)**	**(228,613)**	**(11,098,780)**	**(11,390,983)**	**98,865,892**	**12,300,695**	**11,595,803**	**122,762,390**
a) due from banks	**4,452,582**	**715,488**	**1,598**	**5,169,668**	**(1,914)**	**(1,073)**	**(1,530)**	**(4,517)**	**4,450,668**	**714,415**	**68**	**5,165,151**
- loans	4,223,668	715,488	1,598	**4,940,754**	(1,645)	(1,073)	(1,530)	**(4,248)**	4,222,023	714,415	68	**4,936,506**
- securities	228,914	-	-	**228,914**	(269)	-	-	**(269)**	228,645	-	-	**228,645**
b) loans to customers	**94,476,900**	**11,813,820**	**22,692,985**	**128,983,705**	**(61,676)**	**(227,540)**	**(11,097,250)**	**(11,386,466)**	**94,415,224**	**11,586,280**	**11,595,735**	**117,597,239**
- loans	83,171,805	11,616,712	22,692,985	**117,481,502**	(58,208)	(217,803)	(11,097,250)	**(11,373,261)**	83,113,597	11,398,909	11,595,735	**106,108,241**
- securities	11,305,095	197,108	-	**11,502,203**	(3,468)	(9,737)	-	**(13,205)**	11,301,627	187,371	-	**11,488,998**
Total	**114,820,485**	**12,636,183**	**22,694,583**	**150,151,251**	**(68,631)**	**(230,710)**	**(11,098,780)**	**(11,398,121)**	**114,751,854**	**12,405,473**	**11,595,803**	**138,753,130**

The quality of credit relating to non-performing loans (Stage 3) is described in greater detail below and is divided into bad loans, unlikely to pay and past due - non-performing.

Stage 3 - Loans - credit quality	Gross exposure				Total value adjustments				Net exposure			
	Bad loans	Unlikely to pay	Past due - non-performing	Stage 3 Total	Bad loans	Unlikely to pay	Past due - non-performing	Stage 3 Total	Bad loans	Unlikely to pay	Past due - non-performing	Stage 3 Total
a) due from banks	**1,598**	**-**	**-**	**1,598**	**(1,530)**	**-**	**-**	**(1,530)**	**68**	**-**	**-**	**68**
- loans	1,598			**1,598**	(1,530)			**(1,530)**	68	-	-	**68**
b) loans to customers	**14,038,805**	**8,558,786**	**95,394**	**22,692,985**	**(8,797,025)**	**(2,285,257)**	**(14,968)**	**(11,097,250)**	**5,241,780**	**6,273,529**	**80,426**	**11,595,735**
- loans	14,038,805	8,558,786	95,394	**22,692,985**	(8,797,025)	(2,285,257)	(14,968)	**(11,097,250)**	5,241,780	6,273,529	80,426	**11,595,735**
Total	**14,040,403**	**8,558,786**	**95,394**	**22,694,583**	**(8,798,555)**	**(2,285,257)**	**(14,968)**	**(11,098,780)**	**5,241,848**	**6,273,529**	**80,426**	**11,595,803**

Table 9: Credit quality as at 1 January 2018 (IFRS 9) – Opening-balance exposures

The following table displays the breakdown of the exposures subject to the IFRS 9 impairment model by stage (Stage 1, Stage 2 and Stage 3), illustrating the gross exposure, the total adjustment value and the net exposure.

	Gross exposure				Total value adjustments				Net exposure			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
30. Financial assets measured at fair value through other comprehensive income	**15,891,003**	**106,875**	**-**	**15,997,878**	**(5,041)**	**(2,097)**	**-**	**(7,138)**	**15,885,962**	**104,778**	**-**	**15,990,740**
- securities	15,891,003	106,875	-	**15,997,878**	(5,041)	(2,097)	-	**(7,138)**	15,885,962	104,778	-	**15,990,740**
40. Financial assets measured at amortised cost	**98,985,821**	**12,574,254**	**25,113,870**	**136,673,945**	**(119,929)**	**(273,559)**	**(13,518,067)**	**(13,911,555)**	**98,865,892**	**12,300,695**	**11,595,803**	**122,762,390**
a) due from banks	**4,452,754**	**716,653**	**1,598**	**5,171,005**	**(2,086)**	**(2,238)**	**(1,530)**	**(5,854)**	**4,450,668**	**714,415**	**68**	**5,165,151**
- loans	4,223,840	716,653	1,598	**4,942,091**	(1,817)	(2,238)	(1,530)	**(5,585)**	4,222,023	714,415	68	**4,936,506**
- securities	228,914	-	-	**228,914**	(269)	-	-	**(269)**	228,645	-	-	**228,645**
b) loans to customers	**94,533,067**	**11,857,601**	**25,112,272**	**131,502,940**	**(117,843)**	**(271,321)**	**(13,516,537)**	**(13,905,701)**	**94,415,224**	**11,586,280**	**11,595,735**	**117,597,239**
- loans	83,227,972	11,660,493	25,112,272	**120,000,737**	(114,375)	(261,584)	(13,516,537)	**(13,892,496)**	83,113,597	11,398,909	11,595,735	**106,108,241**
- securities	11,305,095	197,108	-	**11,502,203**	(3,468)	(9,737)	-	**(13,205)**	11,301,627	187,371	-	**11,488,998**
Total	**114,876,824**	**12,681,129**	**25,113,870**	**152,671,823**	**(124,970)**	**(275,656)**	**(13,518,067)**	**(13,918,693)**	**114,751,854**	**12,405,473**	**11,595,803**	**138,753,130**

As illustrated in the table above, almost all exposures represented by debt securities are classified in Stage 1, as the majority are government securities with an investment grade rating.

However, in regard to performing exposures represented by loans to banks and customers, please note that these are classified for approximately 88% under Stage 1, with the remaining 12% under Stage 2. Note that approximately 77% of the exposures classified as Stage 2 are attributable to the increase in the probability of default compared to set thresholds rather than backstop indicators represented by the presence of a past due/delinquent for more than 30 days.

By focusing the analysis on the portfolio of loans classified as loans to customers, the coverage of performing loans was 0.4%; more specifically, it was 0.14% for Stage 1 and 2.24% for Stage 2.

The quality of credit relating to non-performing loans (Stage 3) is described in greater detail below and is divided into bad loans, unlikely to pay and past due - non-performing.

Stage 3 - Loans - credit quality	Gross exposure				Total value adjustments				Net exposure			
	Bad loans	Unlikely to pay	Past due - non-performing	Stage 3 Total	Bad loans	Unlikely to pay	Past due - non-performing	Stage 3 Total	Bad loans	Unlikely to pay	Past due - non-performing	Stage 3 Total
a) due from banks	**1,598**	**-**	**-**	**1,598**	**(1,530)**	**-**	**-**	**(1,530)**	**68**	**-**	**-**	**68**
- loans	1,598			**1,598**	(1,530)			**(1,530)**	68	-	-	**68**
b) due from customers	**15,793,632**	**9,223,246**	**95,394**	**25,112,272**	**(10,551,852)**	**(2,949,717)**	**(14,968)**	**(13,516,537)**	**5,241,780**	**6,273,529**	**80,426**	**11,595,735**
- loans	15,793,632	9,223,246	95,394	**25,112,272**	(10,551,852)	(2,949,717)	(14,968)	**(13,516,537)**	5,241,780	6,273,529	80,426	**11,595,735**
Total	**15,795,230**	**9,223,246**	**95,394**	**25,113,870**	**(10,553,382)**	**(2,949,717)**	**(14,968)**	**(13,518,067)**	**5,241,848**	**6,273,529**	**80,426**	**11,595,803**

Effects of the first time adoption of IFRS 9 – Recognition of deferred tax assets (DTA)

As illustrated in table 1 above, the first time adoption of IFRS 9 led to the debiting of shareholders' equity to the amount of 1,406.0 million euro, gross of the tax effect, mainly due to the new impairment model on credit exposures.
With reference to the relative taxation, it should be noted that the Decree issued by the Ministry of Economy and Finance on 10 January 2018 established that the negative equity impact caused by the adoption of the new impairment model introduced by the IFRS 9 accounting standard can be deducted from the taxable income for IRES and IRAP for 2018.
Consequently, at the date of first time adoption, a tax loss was generated for the Group's biggest companies, which is being processed.
Pursuant to current legislation, IRES tax losses can be carried forward and can be recovered by generating taxable income in subsequent years without any time limit. However, IRAP tax losses cannot be carried forward.
Given this aforementioned legislation, deferred tax assets (DTA) of 349.4 million euro were recognised, almost entirely attributable to IRES tax losses.
To verify the conditions for the recognition of these DTAs, the estimates made in the 2017 financial statements were updated with reference to future income forecasts, which showed that the DTAs are recoverable within a reasonably defined time period.

Method of presenting balances from previous periods for comparison

As indicated in the introduction to this section, the Banco BPM Group has made use of the exemption from the obligation to recalculate comparative values provided for in paragraph 7.2.15 of IFRS 9 and paragraphs E1 and E2 of IFRS 1 "First-Time Adoption of International Financial Reporting Standards", based on which the first financial statements that adopt the new standard do not envisage the mandatory restatement of comparative figures on a uniform basis.
Consequently, the balance sheet and income statement balances for the previous year are not fully comparable with the new accounting categories and the related valuation criteria introduced by the new IFRS 9 standard, as they were prepared in accordance with the previous IAS 39 accounting standard.
For this reason, and also taking into account that the Supervisory Authority left the form and content of the information relating to the transition to IFRS 9 to the independence of the competent corporate bodies when issuing the fifth update of Circular no. 262, the Banco BPM Group decided not to compare the items affected by IFRS 9, as the balances—both the balance sheet and income statement balances—for the previous year were not determined and thus would not allow for a comparison to be made on a completely consistent basis.
Therefore, in order to present the balances relating to the previous year/period, the Banco BPM Group chose to:

- reconcile the balances relating to the balance sheet and income statement items not affected by IFRS 9 into a single statement;
- prepare a separate indication of the balance sheet items intended to record the balance sheet and income statement balances of the financial instruments that fall within the scope of IFRS 9, which will continue to be included in the items published in the latest approved financial statements (interim financial statements).

A reconciliation between the items in the balance sheet as at 31 December 2017 is found below, prepared on the basis of the fourth update of Circular 262 and the new items in the balance sheet introduced by the fifth update of Circular 262, showing comparable items (albeit with different numbering) and items for which no comparison is provided as they were prepared on a inconsistent basis and are therefore not comparable. This reconciliation is provided in order to furnish an immediate understanding of the balance sheet and income statement reported in the Consolidated condensed interim financial statements of this Report.

Consolidated balance sheet

Reconciliation between items before and after IFRS 9

Asset items	
Asset statement as at 30/06/2018 (IFRS 9)	**Asset statement as at 31/12/2017 (IAS 39)**
10. Cash and cash equivalents	10. Cash and cash equivalents
20. Financial assets designated at fair value through profit and loss	
a) financial assets held for trading	
b) financial assets designated at fair value	
c) other financial assets mandatorily at fair value	
30. Financial assets measured at fair value through other comprehensive income	
40. Financial assets measured at amortised cost	
a) due from banks	
b) loans to customers	
	20. Financial assets held for trading
	30. Financial assets designated at fair value through profit and loss
	40. Financial assets available for sale
	50. Investments held to maturity
	60. Due from banks
	70. Loans to customers
50. Hedging derivatives	80. Hedging derivatives
60. Fair value change of financial assets in macro fair value hedge portfolios (+/-)	90. Fair value change of financial assets in macro fair value hedge portfolios (+/-)
70. Equity investments	100. Equity investments
80. Technical reserves of reinsurers	110. Technical reserves of reinsurers
90. Property, plant and equipment	120. Property, plant and equipment
100. Intangible assets	130. Intangible assets
of which:	of which:
- goodwill	- goodwill
110. Tax assets	140. Tax assets
a) current	a) current
b) deferred	b) deferred
120. Non-current assets and asset disposal groups held for sale	150. Non-current assets and asset disposal groups held for sale
130. Other assets	160. Other assets
Total assets	**Total assets**

Liability and shareholders' equity items	
Liability statement as at 30/06/2018 (IFRS 9)	**Liability statement as at 31/12/2017 (IAS 39)**
10. Financial liabilities measured at amortised cost	
a) due to banks	10. Due to banks
b) due to customers	20. Due to customers
c) debt securities issued	
	30. Debt securities issued
20. Financial liabilities held for trading	40. Financial liabilities held for trading
30. Financial liabilities designated at fair value	
	50. Financial liabilities designated at fair value through profit and loss
40. Hedging derivatives	60. Hedging derivatives
50. Fair value change of financial liabilities in macro fair value hedge portfolios (+/-)	70. Fair value change of financial liabilities in macro fair value hedge portfolios (+/-)
60. Tax liabilities	80. Tax liabilities
a) current	a) current
b) deferred	b) deferred
70. Liabilities associated with assets held for sale	90. Liabilities associated with assets held for sale
80. Other liabilities	
	100. Other liabilities
90. Employee termination indemnities	110. Employee termination indemnities
100. Provisions for risks and charges:	
a) commitments and guarantees given	
	120. Provisions for risks and charges:
b) retirement benefits and similar commitments	a) retirement benefits and similar commitments
c) other provisions for risks and charges	b) other provisions
110. Technical reserves	130. Technical reserves
120. Valuation reserves	140. Valuation reserves
130. Redeemable shares	150. Redeemable shares
140. Equity instruments	160. Equity instruments
150. Reserves	170. Reserves
160. Share premium reserve	180. Share premium reserve
170. Share capital	190. Share capital
180. Treasury shares (-)	200. Treasury shares (-)
190. Minority interests (+/-)	210. Minority interests (+/-)
200. Income (Loss) for the period (+/-)	220. Income (Loss) for the period (+/-)
Total liabilities and shareholders' equity	**Total liabilities and shareholders' equity**

Consolidated income statement

Reconciliation between items before and after IFRS 9

Income statement items	
Income statement as at 30/06/2018 (IFRS 9)	**Income statement as at 31/12/2017 (IAS 39)**
10. Interest and similar income	
	10. Interest and similar income
20. Interest and similar expense	20. Interest and similar expense
30. Interest margin	
	30. Interest margin
40. Fee and commission income	40. Fee and commission income
50. Fee and commission expense	50. Fee and commission expense
60. Net fee and commission income	**60. Net fee and commission income**
70. Dividends and similar income	70. Dividends and similar income
80. Profits (losses) on trading	
	80. Profits (losses) on trading
90. Fair value adjustments in hedge accounting	90. Fair value adjustments in hedge accounting
100. Profits (losses) on disposal or repurchase of:	100. Profits (losses) on disposal or repurchase of:
a) financial assets measured at amortised cost	
b) financial assets designated at fair value through other comprehensive income	
c) financial liabilities	d) financial liabilities
	a) loans
	b) financial assets available for sale
	c) investments held to maturity
110. Profits (losses) on other financial assets and liabilities designated at fair value through profit and loss	
a) financial assets and liabilities designated at fair value	
b) other financial assets mandatorily at fair value	
	110. Profits (losses) on financial assets and liabilities designated at fair value through profit and loss
120. Net interest and other banking income	
	120. Net interest and other banking income
130. Net losses/recoveries on credit risk relating to:	
a) financial assets measured at amortised cost	
b) financial assets designated at fair value through other comprehensive income	
	130. Net losses/recoveries on impairment of:
	a) loans
	b) financial assets available for sale
	c) investments held to maturity
	d) other financial transactions
140. Profit/loss from contractual changes without derecognition	
150. Net income from banking activities	
	140. Net income from banking activities
160. Net premiums	150. Net premiums
170. Balance of other income/expense from insurance activities	160. Balance of other income/expense from insurance activities
180. Net income from banking and insurance activities	
	170. Net income from banking and insurance activities
190. Administrative expenses:	180. Administrative expenses:
a) personnel expenses	a) personnel expenses
b) other administrative expenses	b) other administrative expenses
200. Net provisions for risks and charges	
a) commitments and guarantees given	
b) other net provisions	190. Net provisions for risks and charges

Income statement items	
Income statement as at 30/06/2018 (IFRS 9)	**Income statement as at 31/12/2017 (IAS 39)**
210. Net adjustments to/recoveries on property and equipment	200. Net adjustments to/recoveries on property and equipment
220. Net adjustments to/recoveries on intangible assets	210. Net adjustments to/recoveries on intangible assets
230. Other operating expenses/income	220. Other operating expenses/income
240. Operating expenses	
	230. Operating expenses
250. Profits (losses) on investments in associates and companies subject to joint control	240. Profits (losses) on investments in associates and companies subject to joint control
260. Profits (losses) from the fair value designation of property, plant and equipment and intangible assets	250. Profits (losses) from the fair value designation of property, plant and equipment and intangible assets
270. Value adjustments on goodwill	260. Value adjustments on goodwill
280. Profits (losses) on disposal of investments	270. Profits (losses) on disposal of investments
290. Profit (loss) before tax from continuing operations	
	280. Profit (loss) before tax from continuing operations
300. Income (loss) before tax from continuing operations	290. Income (loss) before tax from continuing operations
310. Income (loss) after tax from continuing operations	
	300. Income (loss) after tax from continuing operations
320. Profit (loss) from discontinued operations, net of taxes	310. Profit/(loss) on asset disposal groups held for sale after tax
330. Income (Loss) for the period	
	320. Income (Loss) for the period
340. Income (loss) attributable to minority interests	330. Income (loss) attributable to minority interests
350. Parent Company's net income (loss)	
	340. Parent Company's net income (loss)

DISCLOSURE ON THE FIRST ADOPTION OF THE IFRS 15 ACCOUNTING STANDARD - REVENUE FROM CONTRACTS WITH CUSTOMERS

The standard, published by the IASB on 28 May 2014, introduces a single model for the recognition of all revenues originating from contracts with customers and replaces the previous standards/interpretations on revenues (IAS 18, IAS 11, IFRIC 13, IFRIC 15, IFRIC 18, SIC 31).
On the basis of this model, the entity must recognise revenues on the basis of the fee that it expects to receive for the assets or the services provided in the ordinary course of business. In detail, the recognition of revenues must take place on the basis of the following five steps:

- identify the contract, defined as an agreement with commercial substance between two or more parties able to generate rights and obligations;
- identify the performance obligations in the contract;
- determine the transaction price, namely the amount to which an entity expects to be entitled in exchange for the transfer of goods and services;
- allocate the transaction price to each performance obligation on the basis of the stand-alone selling price;
- recognise the revenues allocated to the single performance obligation when the same is satisfied, namely when the customer obtains control of the goods or the services. This recognition takes into account the fact that some services may be rendered at a specific point in time or over a period of time.

Services that involved the recognition of commission income in the income statement were analysed with the aim of verifying the correct method of recognising revenues. Specifically, the analysis focused on the potentially variable revenue components and on those that may be derecognised, particularly those relating to the provision of asset management services and placement activities.
The analyses revealed that the methods for recognising revenues introduced by the new accounting standard were substantially in line with the previous accounting treatment.
Taking into account that the IFRS 15 accounting standard makes explicit the need to record a liability for the amounts collected but which may be reversed (refund liabilities), an estimate was made of the above liability, which in the Group is attributable to the specific case of the placement of certain single-premium insurance products for which, in the presence of the early extinction of the products, the placement bank is required to return part of the placement fees collected in proportion to the residual duration.
The quantification of this liability, which was carried out with reference to historical observation of early repayment, amounted to 20.4 million euro. Considering the related tax effect, amounting to 5.6 million euro, the reduction in shareholders' equity amounts to 14.8 million euro.
For more immediate evidence of the above impacts on the Group's financial position, reference should be made to the reconciliation table between the balance sheet as at 31 December 2017 and that restated as at 1 January 2018, as reported in the introduction to this chapter.

In addition to the quantitative impacts, the new standard requires more information on the nature, amount, timing and uncertainty of revenues, as well as on the cash flows deriving from contracts with customers.
With regard to this consolidated half-year financial report, IFRS 15—which amended IAS 34 relating to interim financial statements—introduced, as a disclosure requirement, the need to provide a breakdown of revenues by operating segments, in accordance with IFRS 8. Specifically, for the bank, the revenues from contracts with customers are represented by commission income which is shown by type of service provided, considered to be the most suitable criterion for representing the nature of the revenue.
For the relative information, please refer to section "Part L - Segment reporting" of this interim consolidated financial Report.

FINANCIAL STATEMENTS

Consolidated balance sheet

Asset items (*in thousands of euro*)	**30/06/2018**	**31/12/2017 (*)**
10. Cash and cash equivalents	796,466	976,686
20. Financial assets designated at fair value through profit and loss	7,800,964	
a) financial assets held for trading	6,522,922	
c) other financial assets mandatorily at fair value	1,278,042	
30. Financial assets designated at fair value through other comprehensive income	19,017,645	
40. Financial assets designated at amortised cost	126,094,384	
a) due from banks	5,489,437	
b) loans to customers	120,604,947	
Financial assets held for trading (former IAS 39)		4,911,824
Financial assets designated at fair value through profit and loss (former IAS 39)		28,952
Financial assets available for sale (former IAS 39)		17,128,622
Investments held to maturity (former IAS 39)		11,560,769
Due from banks (former IAS 39)		5,164,715
Loans to customers (former IAS 39)		108,176,382
50. Hedging derivatives	176,497	243,810
60. Fair value change of financial assets in macro fair value hedge portfolios (+/-)	48,577	54,531
70. Equity investments	1,355,065	1,349,191
90. Property, plant and equipment	2,733,275	2,735,182
100. Intangible assets	1,295,196	1,297,160
of which: goodwill	76,389	76,389
110. Tax assets	4,903,767	4,520,189
a) current	308,562	319,462
b) deferred	4,595,205	4,200,727
120. Non-current assets and asset disposal groups held for sale	44,861	106,121
130. Other assets	2,762,381	2,952,631
Total assets	**167,029,078**	**161,206,765**

(*) Balances resulting from the financial statements published at 31 December 2017 as illustrated in the paragraph "Method of presenting balances from previous periods for comparison" contained in the section "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers".

Liability and shareholders' equity items (*in thousands of euro*)	**30/06/2018**	**31/12/2017 (*)**
10. Financial liabilities designated at amortised cost	134,335,338	
a) due to banks	31,550,552	27,199,304
b) due to customers	87,659,619	87,848,146
c) debt securities issued	15,125,167	
Debt securities issued (former IAS 39)		16,248,143
20. Financial liabilities held for trading	8,210,839	7,942,063
30. Financial liabilities designated at fair value	2,720,813	
Financial liabilities designated at fair value (former IAS 39)		3,413,560
40. Hedging derivatives	753,379	765,903
50. Fair value change of financial liabilities in macro fair value hedge portfolios (+/-)	36,830	8,535
60. Tax liabilities	606,246	669,494
a) current	13,737	14,493
b) deferred	592,509	655,001
70. Liabilities associated with assets held for sale	4,212,805	35
80. Other liabilities	3,734,255	
Other liabilities (former IAS 39)		3,687,053
90. Employee termination indemnities	396,185	408,160
100. Provisions for risks and charges	1,135,843	
a) commitments and guarantees given	120,664	
Provisions for risks and charges: (former IAS 39)		1,052,829
b) retirement benefits and similar commitments	159,489	166,847
c) other provisions for risks and charges	855,690	885,982
120. Valuation reserves	(178,829)	251,706
150. Reserves	3,573,442	1,946,308
170. Share capital	7,100,000	7,100,000
180. Treasury shares (-)	(13,155)	(14,146)
190. Minority interests (+/-)	52,510	63,310
200. Income/Loss for the period	352,577	2,616,362
Total liabilities and shareholders' equity	**167,029,078**	**161,206,765**

(*) Balances resulting from the financial statements published at 31 December 2017 as illustrated in the paragraph "Method of presenting balances from previous periods for comparison" contained in the section "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers".

Consolidated income statement

Items (*in thousands of euro*)		1st half 2018	1st half 2017 (*)
10.	Interest and similar income	1,480,257	
	Interest and similar income (former IAS 39)		1,499,205
20.	Interest and similar expense	(300,148)	(513,413)
30.	**Interest margin**	**1,180,109**	**985,792**
40.	Fee and commission income	983,320	1,079,633
50.	Fee and commission expense	(55,807)	(60,254)
60.	**Net fee and commission income**	**927,513**	**1,019,379**
70.	Dividends and similar income	40,576	44,625
80.	Profits (losses) on trading	(66,287)	
90.	Fair value adjustments in hedge accounting	(460)	(1,125)
100.	Profits (losses) on disposal or repurchase of:	(131,771)	
	a) financial assets designated at amortised cost	(260,552)	
	b) financial assets designated at fair value through other comprehensive income	129,783	
	c) financial liabilities	(1,002)	
110.	Profits (losses) on other financial assets and liabilities designated at fair value through profit and loss	5,689	
	a) financial assets and liabilities designated at fair value	(22,433)	
	b) other financial assets mandatorily at fair value	28,122	
	Profits (losses) on trading (former IAS 39)		23,223
	Profits (losses) on disposal or repurchase of: (former IAS 39)		(64,263)
	a) loans (former IAS 39)		(94,681)
	b) financial assets available for sale (former IAS 39)		37,011
	d) financial liabilities (former IAS 39)		(6,593)
	Profits (losses) on financial assets and liabilities designated at fair value (former IAS 39)		2,474
120.	**Net interest and other banking income**	**1,955,369**	**2,010,105**
130.	Net losses/recoveries on credit risk relating to:	(424,073)	
	a) financial assets designated at amortised cost	(420,875)	
	b) financial assets designated at fair value through other comprehensive income	(3,198)	
	Net losses/recoveries on impairment of: (former IAS 39)		(556,990)
	a) loans (former IAS 39)		(489,135)
	b) financial assets available for sale (former IAS 39)		(78,951)
	d) financial liabilities (former IAS 39)		11,096
140.	Profit/loss from contractual changes without derecognition	-	
150.	**Net income from banking activities**	**1,531,296**	**1,453,115**
180.	**Net income from banking and insurance activities**	**1,531,296**	**1,453,115**
190.	Administrative expenses:	(1,534,180)	(1,562,911)
	a) personnel expenses	(880,353)	(907,123)
	b) other administrative expenses	(653,827)	(655,788)
200.	Net provisions for risks and charges	(45,671)	
	a) commitments and guarantees given	15,189	
	Net provisions for risks and charges (former IAS 39)		(9,137)
	b) other net provisions	(60,860)	(9,137)
210.	Net adjustments to/recoveries on property and equipment	(56,012)	(55,653)
220.	Net adjustments to/recoveries on intangible assets	(52,838)	(70,267)
230.	Other operating expenses/income	313,022	3,293,173
240.	**Operating expenses**	**(1,375,679)**	**1,595,205**
250.	Profits (losses) on investments in associates and companies subject to joint control	250,654	93,617
280.	Profits (losses) on disposal of investments	3,894	1,623
290.	**Profits (Losses) from current operations gross of taxes**	**410,165**	**3,143,560**
300.	Taxes on income from continuing operations	(61,182)	(26,378)
310.	**Profits (Losses) from current operations net of taxes**	**348,983**	**3,117,182**

Items (*in thousands of euro*)	1st half 2018	1st half 2017 (*)
320. Profit (loss) from discontinued operations, net of taxes	4	45,793
330. Income (Loss) for the period	**348,987**	**3,162,975**
340. Income (loss) attributable to minority interests	3,590	7,394
350. Parent Company's net income (loss)	**352,577**	**3,170,369**
Basic EPS (euro)	0.233	2.098
Diluted EPS (euro)	0.233	2.098

(*) Balances resulting from the consolidated interim financial report as at 30 June 2017 restated pursuant to IFRS 5. For further details, please refer to the paragraph entitled "Method of presenting balances from previous periods for comparison" contained in the section "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers" and in the "Notes for a proper comparison of the comparative financial statements and comparative information" in "Part A - Accounting policies".

Statement of consolidated comprehensive income

Items	30/06/2018	30/06/2017 (*)
10. Income (Loss) for the period	**348,987**	**3,162,975**
Other comprehensive income after tax without reclassification to		
20. Equity instruments designated at fair value through other comprehensive income	(19,069)	
30. Financial liabilities designated at fair value - changes in own creditworthiness	7,690	(7,373)
70. profit or loss Defined benefit plans	4,080	2,519
90. Share of valuation reserves related to investments in associates carried at equity	(10)	14
Other comprehensive income after tax with reclassification to		
100. Foreign investment hedges	(238)	342
110. Exchange rate differences	820	(1,411)
120. Cash flow hedges	(2,437)	(2,735)
130. Hedging instruments (non-designated items)		
140. Financial assets (other than equity instruments) designated at fair value through other comprehensive income	(337,686)	
Financial assets available for sale (former IAS 39)		87,629
160. Share of valuation reserves related to investments in associates carried at equity	(5,451)	14,375
170. Total other comprehensive income after tax	**(352,301)**	**93,360**
180. Comprehensive Income (Items 10+130)	**(3,314)**	**3,256,335**
190. Consolidated comprehensive income attributable to minority interests	3,585	7,390
200. Consolidated comprehensive income attributable to the Parent Company	**271**	**3,263,725**

(*) The data for the previous period were prepared in accordance with IAS 39 classification and measurement criteria and are therefore not fully comparable with the data for the current period.

Statement of changes of consolidated shareholders' equity

30 June 2018	Balance as at 31/12/2017	Changes in opening balance (*)	Balance as at 01/01/2018	Allocation of net income from previous year		Changes in the period									Shareholders' equity as at 30/06/2018	Group shareholders' equity as at 30/06/2018	Minority interests as at 30/06/2018
							Operations on shareholders' equity										
				Reserves	Dividends and other allocations	Changes in reserves	Issue of new shares	Purchase of treasury shares	Extraordinary distribution of dividends	Changes in equity instruments	Derivatives on treasury shares	Stock options	Changes in equity investments	Comprehensive income for the year			
Share capital:	**7,164,561**	**-**	**7,164,561**	**-**		**-**	**-**	**-**					**(100)**		**7,164,461**	**7,100,000**	**64,461**
a) ordinary shares	7,164,561	-	7,164,561	-		-	-	-					(100)		7,164,461	7,100,000	64,461
b) other assets	-	-	-	-		-	-	-					-		-	-	-
Share premium reserve	**1,216**	**-**	**1,216**	**-**		**-**	**-**	**-**					**(1,115)**		**101**	**-**	**101**
Reserves:	**1,953,356**	**(987,412)**	**960,201**	**2,606,512**		**(740)**	**(1,137)**	**-**	**-**		**-**		**(5)**		**3,564,831**	**3,573,442**	**(8,611)**
a) retained earnings	1,456,946	(987,412)	463,791	2,606,512		1,252	(1,137)	-	-				(66)		3,070,352	3,078,961	(8,609)
b) other	496,410	-	496,410	-		(1,992)	-	-			-		61		494,479	494,481	(2)
Valuation reserves	**251,849**	**(78,229)**	**173,620**	**-**		**-**							**1**	**(352,301)**	**(178,680)**	**(178,829)**	**149**
Equity instruments	**-**	**-**	**-**							**-**					**-**	**-**	**-**
Treasury shares	**(14,146)**	**-**	**(14,146)**			**-**	**991**	**-**							**(13,155)**	**(13,155)**	**-**
Income (Loss) for the period	**2,606,704**	**-**	**2,606,704**	**(2,606,512)**	**(192)**									**348,987**	**348,987**	**352,577**	**(3,590)**
Shareholders' equity	**11,963,540**	**(1,065,641)**	**10,892,156**	**-**	**(192)**	**(740)**	**(146)**	**-**	**-**	**-**	**-**		**(1,219)**	**(3,314)**	**10,886,545**	**10,834,035**	**52,510**
- of the Group	**11,900,230**		**10,834,589**	**-**	**-**	**(740)**	**(146)**	**-**	**-**	**-**	**-**		**61**	**271**	**10,834,035**		
- of minority interests	**63,310**	**(5,743)**	**57,567**	**-**	**(192)**	**-**	**-**	**-**					**(1,280)**	**(3,585)**	**52,510**		

(*) These are the impacts of the First Time Adoption (FTA) due to the adoption of the IFRS 9 and IFRS 15 accounting standards as described in detail in the section of the condensed interim financial statements "Disclosure on the first adoption of the accounting standards IFRS 9 Financial instruments and IFRS 15 Revenue from contracts with customers".

30 June 2017 *(in thousands of euro)*	Balance as at 31/12/2016	Changes in opening balance (*)	Balance as at 01/01/2017	Allocation of net income from previous year		Changes in the period									Shareholders' equity as at 30/06/2017	Group shareholders' equity as at 30/06/2017	Minority interests as at 30/06/2017
							Operations on shareholders' equity										
				Reserves	Dividends and other allocations	Changes in reserves	Issue of new shares	Purchase of treasury shares	Extraordinary distribution of dividends	Changes in equity instruments	Derivatives on treasury shares	Stock options	Changes in equity investments	Comprehensive income for the year			
Share Capital:	**7,200,332**	**-**	**7,200,332**	**-**		**134**	**10,660**	**-**					**(16,058)**		**7,195,068**	**7,100,000**	**95,068**
a) ordinary shares	7,200,332	-	7,200,332	-		134	10,660	-					(16,058)		7,195,068	7,100,000	95,068
b) other assets	-	-	-	-		-	-	-					-		-	-	-
Share premium reserve	**-**	**-**	**-**	**-**		**1,112**	**-**	**-**					**-**		**1,112**	**-**	**1,112**
Reserves:	**2,121,665**	**(27,513)**	**2,094,152**	**(1,704,935)**		**1,514,239**	**(1,590)**	**-**	**-**		**-**		**6,198**		**1,908,064**	**1,943,888**	**(35,824)**
a) retained earnings	2,077,009	-	2,077,009	(396,237)		(259,418)	(1,590)	-	-				6,198		1,425,962	1,461,675	(35,713)
b) other	44,656	(27,513)	17,143	(1,308,698)		1,773,657	-	-			-		-		482,102	482,213	(111)
Valuation reserves	**28,949**	**27,513**	**56,462**	**-**		**26,310**							**1**	**93,360**	**176,133**	**175,975**	**158**
Equity instruments	**-**	**-**	**-**							**-**					**-**	**-**	**-**
Treasury shares	**(1,590)**	**-**	**(1,590)**			**-**	**1,590**	**-**							**-**	**-**	**-**
Income (Loss) for the period	**(1,704,508)**	**-**	**(1,704,508)**	**1,704,935**	**(427)**									**3,162,975**	**3,162,975**	**3,170,369**	**(7,394)**
Shareholders' equity	**7,644,848**	**-**	**7,644,848**	**-**	**(427)**	**1,541,795**	**10,660**	**-**	**-**	**-**	**-**		**(9,859)**	**3,256,335**	**12,443,352**	**12,390,232**	**53,120**
- of the Group	**7,575,280**		**7,575,280**	**-**	**-**	**1,540,567**	**10,660**	**-**	**-**	**-**	**-**		**-**	**3,263,725**	**12,390,232**		
- of minority interests	**69,568**	**-**	**69,568**	**-**	**(427)**	**1,228**	**-**	**-**					**(9,859)**	**(7,390)**	**53,120**		

(*) This is the restatement relating to the different accounting treatment adopted by the Group, from 1 January 2017, for the representation of profits and losses associated with changes in the creditworthiness of financial liabilities under the fair value option.

Consolidated cashflow statement

Indirect method

A.	Operating activities	30/06/2018	30/06/2017 (*)
	1. Cash flow from operations (**)	**1,100,125**	**3,922,839**
-	Net income (loss) for the period (+/-)	352,577	3,170,369
-	gains/losses on financial assets held for trading and on other financial assets/liabilities designated at fair value through profit and loss (-/+)	182,055	110,080
-	capital gain/loss on hedging activities (-/+)		-
-	Net adjustments to/recoveries on credit risk (-/+)	424,073	556,990
-	net value adjustments to/recoveries on plant and equipment and intangible assets (+/-)	108,850	126,094
-	allocations to provisions for risks and charges and other costs/revenues (+/-)	56,668	11,745
-	net premiums not collected (-)		-
-	other insurance income/expenses not collected (-/+)		-
-	duties, taxes and tax credits not settled (+/-)	51,900	29,500
-	net adjustments to/recoveries from discontinued operations net of the taxes (-/+)		-
-	other adjustments (+/-)	(75,998)	(81,939)
	2. Cash flow from/used in financial assets	**(7,583,077)**	**(48,908,245)**
-	financial assets held for trading	(1,812,782)	
-	financial assets designated at fair value	(22,880)	
-	other financial assets mandatorily at fair value	25,917	
-	financial assets designated at fair value through other comprehensive income	(2,270,771)	
-	financial assets designated at amortised cost	(3,754,714)	
-	*financial assets (former IAS 39)*		(47,271,251)
-	other assets	252,153	(1,636,994)
	3. Cash flow from/used in financial liabilities	**6,424,449**	**47,123,444**
-	financial liabilities designated at amortised cost	2,864,121	41,541,311
-	financial liabilities held for trading	272,394	589,463
-	financial liabilities designated at fair value	(532,377)	(1,478,873)
-	other liabilities	3,820,311	6,471,543
	Net cash flow from/used in operating activities	**(58,503)**	**2,138,038**
B.	**Investing activities**		
	1. Cash flow from:	**818,625**	**7,429**
-	sales of investments in associates and companies subject to joint control	813,691	-
-	dividends collected on investments in associates and companies subject to joint control		-
-	sales of property and equipment	4,934	7,429
-	sales of intangible assets	-	-
-	sales of subsidiaries and business branches		-
	2. Cash flow used in:	**(940,534)**	**(2,013,759)**
-	purchases of investments in associates and companies subject to joint control	(803,409)	(254,314)
-	purchases of property and equipment	(86,308)	(986,561)
-	purchases of intangible assets	(50,817)	(772,884)
-	purchases of subsidiaries and business branches		-
	Net cash flow from/used in investing activities	**(121,909)**	**(2,006,330)**
C.	**Financing activities**		
-	issues/purchases of treasury shares		10,660
-	issues/purchases of equity instruments		-
-	dividend distribution and other allocations	192	(427)
-	Third-party sales/purchases		(427)
	Net cash flow from/used in financing activities	**192**	**10,233**
	Net cash flow from/used during the period	**(180,220)**	**141,941**

(*) *The data for the previous period were prepared in accordance with IAS 39 classification and measurement criteria* and are therefore not fully comparable with the data for the current period.

(**) *The figures for the previous period have been reclassified to the new items in the cash flow statement in accordance with the classification and measurement criteria set out in IAS 39.*

(***) *The item "Financial assets (former IAS 39)" includes the cash used in all former IAS 39 financial assets, including financial assets held to maturity, which in the previous cash flow statement were classified as investment activities, in order to ensure as consistent a comparison as possible with the current period.*
Specifically, cash flow from/used in financial assets was as follows:
- FA held for trading: (1,611,120)
- FA designated at fair value: 1,479
- FA available for sale: (8,083,384)
- loans to customers: (34,089,853)
- due from banks: (338,200)
- FA held to maturity: (3,150,173)

	Reconciliation	30/06/2018	30/06/2017
-	Cash and cash equivalents at the beginning of the year	976,686	648,255
-	Net cash flow from/used in activities during the year	(180,220)	141,941
-	Cash and cash equivalents: foreign exchange effect		-
	Cash and cash equivalents at the end of the period	**796,466**	**790,196**

ILLUSTRATIVE NOTES

Please note that these Illustrative Notes have been prepared with reference to the structure of the notes required by Bank of Italy Circular 262 for the financial statements for the year, albeit with limited information, as these are consolidated condensed interim financial statements. For ease of reading, the numbering provided for in the aforementioned Circular has been maintained, although some parts, sections or tables may be omitted for the reasons explained above.

PART A - ACCOUNTING POLICIES

A.1 GENERAL PART

General preparation principles

This interim consolidated financial Report (hereinafter also "Interim Report" or "Report"), drawn up pursuant to Art. 154-*ter* of Italian Legislative Decree no. 58 dated 24 February 1998 (CFL) and subsequent updates, comprises the consolidated condensed interim financial statements and is accompanied by an interim report on operations, which contains significant events during the half year, a disclosure on related party transactions and a description of the main risks and uncertainties, also with relation to the business outlook.

The consolidated condensed interim financial statements (hereinafter also "consolidated financial statements") comprise the balance sheet, income statement, statement of comprehensive income, statement of changes of shareholders' equity, cash flow statement and the illustrative notes and comments on the results for the period.

The financial statements have been prepared in keeping with the provisions of the Bank of Italy in Circular no. 262 of 22 December 2005 "Bank Financial Statements: Layouts and Rules for Preparation" and the subsequent updates (most recently, the fifth update published on 22 December 2017).
The financial statements provide not only the accounting data as at 30 June 2018, but also the comparative balances relating to the same period in the previous year, with the exception of the balance sheet, which is compared with the last set of financial statements approved as at 31 December 2017.
Given the First Time Adoption of IFRS 9 and IFRS 15, please note that the Banco BPM Group has made use of the option provided for in the transitional provisions of the cited standards not to restate the comparative figures; the effects relating to the first adoption are therefore reflected through an adjustment to the opening consolidated shareholders' equity balances at 1 January 2018. With particular reference to the first adoption of IFRS 9, it should be noted that the balance sheet and income statement balances for the previous year, as prepared in compliance with the previous IAS 39, are therefore not fully comparable with the new accounting categories and with the relative valuation criteria introduced by the new standard. In regard to the exposure of the balances of the previous year/period, to ensure as consistent a comparison as possible for comparable items, Banco BPM Group has opted to:

- reconcile the balances relating to the balance sheet and income statement items not affected by IFRS 9 into a single statement;
- prepare a separate indication of the balance sheet items intended to record the balance sheet and income statement balances of the financial instruments that fall within the scope of IFRS 9, which will continue to be included in the items published in the latest approved financial statements (interim financial statements). The balance as at 30 June 2018 is therefore not provided for these items, but will be presented on the basis of the new items in the financial statements.

For this reason, the tables contained in the fair value disclosure and in the illustrative notes, in addition to the figure as at 30 June 2018, will only show comparative balances for items that have a restated balance for both the current and the previous period in the financial statements.
Otherwise, the tables will be proposed in a double version (tables at 30 June 2018 and, separately, tables at 31 December 2017 for the balance sheet and at 30 June 2017 for the income statement) as they are not fully comparable.

For further details on the methods of presenting comparative balances, please refer to the previous chapter "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers".

The reclassified balance sheet and income statement have been drawn up on the basis of these statements, based on the criteria described in the next section dedicated to the "Results". The reclassified statements, based on operational criteria, are meant to provide a more direct illustration of developments in cash flows, the balance sheet and income during the half.

The Consolidated condensed interim financial statements, approved by the Board of Directors of Banco BPM on 3 August 2018, are subject to a limited audit by independent auditors PricewaterhouseCoopers S.p.A., in application of the engagement assigned to this company with the shareholders' resolutions of Banco Popolare Soc. Coop. and Banca Popolare di Milano S.c. a r.l. of 15 October 2016.

This document has been prepared adopting the euro as its main currency; the amounts are stated, unless otherwise specified, in thousands of euro.

Statement of compliance with the international accounting standards

The consolidated financial statements as at 30 June 2018 have been prepared in accordance with the international accounting standards (IAS/IFRS) and relative interpretations (IFRIC) validated by the European Union and in force at the time of its approval, as established by European Union Regulation no. 1606 of 19 July 2002.

These standards have changed from those adopted for the preparation of the 2017 financial statements, following the mandatory application, as of 1 January 2018, of the IFRS 9 and IFRS 15 international accounting standards, as illustrated in greater detail in the specific chapter at the beginning of these financial statements.

For a description of the accounting standards adopted in order to prepare this report, reference should be made to Part "A.2 - Key financial statement items" below.

With regard to the disclosure provided, the consolidated financial statements as at 30 June 2018 have been prepared in a condensed format, as envisaged by accounting standard IAS 34 regarding "Interim financial reporting".

The estimation processes used to draft the interim consolidated financial statements are those normally adopted when the annual accounts are drafted, with greater recourse to estimation particularly with reference to certain types of administrative expenses.

The consolidated condensed interim financial statements as at 30 June 2018 were prepared on the basis of the assumption that the Group will continue as a going concern, as the directors have not identified any circumstances relating to operations or to the evolution of the equity and financial situation that could cast doubts as to the ability of Group companies to be able to continue to operate as usual, and according to the principle of the recognition of costs and revenues on an accrual basis, privileging the prevalence of substance over form.

The consolidated condensed interim financial statements are drawn up clearly and provide a true and fair view of the equity and financial situation and economic result of Banco BPM and its subsidiaries as at 30 June 2018, as illustrated in the paragraph entitled "Scope of consolidation and methods".

New accounting standards/interpretations or amendments or changes to existing standards approved by IASB/IFRIC

An illustration of the new accounting standards or the amendments to existing standards approved by the IASB are given below, as well as new interpretations or amendments to existing ones, published by IFRIC, with separate disclosure of those applicable in 2018 from those applicable in subsequent years.

IAS/IFRS accounting standards and related SIC/IFRIC interpretations endorsed that must be applied when preparing the 2018 financial statements

Regulation no. 1905 of 22 September 2016 - IFRS 15 "Revenue from contracts with customers" and subsequent clarifications endorsed with Regulation no. 1987 of 31 October 2017
The IFRS 15 standard, published by the IASB on 28 May 2014, introduces a single model for the recognition of all revenues originating from contracts with customers and replaces the previous standards/interpretations on revenues (IAS 18, IAS 11, IFRIC 13, IFRIC 15, IFRIC 18 and SIC 31).

Regulation no. 2067 of 22 November 2016 - IFRS 9 "Financial instruments"
The IFRS 9 standard, issued by the IASB in July 2014, governs the steps of classification and measurement of financial instruments, as well as the relative impairment processes, replacing the previous accounting standard IAS 39.

Regulation no. 1988 of 3 November 2017 – "Joint application of IFRS 9 Financial instruments and IFRS 4 Insurance contracts". The objective of the amendments is to resolve, for insurance companies, the problems related to the application of IFRS 9, before the implementation of the standard (IFRS 17 which will enter into force on 1 January 2021) which will replace IFRS 4 on insurance contracts.

Regulation no. 182 of 7 February 2018 – "Annual Improvement Cycle to IFRS 2014 – 2016". The aim is to provide some clarifications in order to resolve certain methodological inconsistencies or clarifications.

Regulation no. 289 of 26 February 2018 – "Amendments to IFRS 2". The amendments aim to clarify the valuation and recognition criteria to be adopted for certain types of share-based payment transactions.

Regulation no. 400 of 14 March 2018 – "Amendments to IAS 40 – Changes in the use of investment property". The amendments clarify the time of transfer of an asset from/to the category of "investment property", identified as "change in use".

Regulation no. 519 of 28 March 2018 – "IFRIC 22 Interpretation – Foreign currency transactions and advances". The interpretation clarifies the accounting for transactions involving the receipt or payment of advances in foreign currency.

With the exception of the first time adoption of the IFRS 9 and IFRS 15 accounting standards, for which reference should be made to the specific chapter "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers", the other amendments and interpretations did not have a significant impact on the Group's balance sheet and income statement.

IAS/IFRS accounting standards and SIC/IFRIC interpretations approved, the application of which takes effect after 30 June 2018

The following paragraphs illustrate the main accounting standards/interpretations or amendments of the same issued by the IASB/IFRIC and validated by the European Commission, which will be applicable on a mandatory basis subsequent to FY 2018.

Regulation no. 1986 of 31 October 2017 - IFRS 16 "Leasing".
The standard was published by the IASB on 13 January 2016, with the aim of improving the accounting reporting of leasing contracts. The mandatory application is expected starting 1 January 2019.
More specifically, the standard introduces new rules for the accounting recognition of lease contracts for both lessors and lessees, replacing the previous standards/interpretations (IAS 17, IFRIC 4, SIC 15 and SIC 27). A lease is defined as a contract whose execution depends on the use of an identified asset and that conveys the right to control the use of the asset for a period of time in exchange for consideration.
IFRS 16 establishes the principles for recognition, measurement, presentation and disclosure of leases. The aim is to ensure that lessees and lessors provide appropriate information in a manner that faithfully represents transactions. The information provides users of financial statements with the elements for assessing the effect of the lease on the entity's financial position, financial performance and cash flows.

The Standard applies to all contracts that contain a right to use an asset for a certain period of time in exchange for a certain fee. IFRS 16 applies to all transactions involving a right to use the asset, regardless of the contractual form, i.e. finance or operating leases, rent or lease.
The main change concerns the representation in the balance sheet of the lessee with reference to the right of use and the commitment made with regard to operating leases, through the recording of an asset and a liability. Specifically, the lessee shall recognise a liability on the basis of the present value of future instalments, as a balancing entry to recognising the right to use the asset covered by the leasing contract among the assets.
After the initial registration:

- the right of use will be subject to amortisation over the duration of the contract or the useful life of the asset (on the basis of IAS 16) or measured using an alternative fair value method (IAS 16 or IAS 40);
- the liability will be gradually reduced as a result of the payment of the instalments and the interest to be charged to the income statement will be recognised on it.

Contracts of less than 12 months or which have a new unit value of the leased asset of modest value are excluded from IFRS 16.
As regards the lessor, the IAS 17 accounting rules for lease contracts are substantially confirmed and differentiated on the basis of whether it is an operating or finance lease. In the case of a finance lease, the lessor will continue to recognise a receivable for future lease payments in the balance sheet.
In this regard, please note that the Group will start an assessment of the impact in the second half of 2018, with a view to establishing the scope and relative accounting treatment of the assets used under lease contracts and related IT implementations; on the basis of a preliminary analysis, the main impacts are related to the right to use real estate through rental contracts.
As far as leased assets are concerned, no significant impact is expected, as the accounting rules established by the current accounting standard IAS 17 are substantially confirmed for the lessor.

Regulation no. 498 of 22 March 2018 – "Amendments to IFRS 9 Financial Instruments – Items of prepayment with negative compensation". These amendments aim to clarify the classification of certain financial assets that are redeemable in advance when applying IFRS 9. In particular:

- for financial assets: contemplates the option of also valuing at amortised cost loans which, in the event of early repayment, require payment by the grantor;
- for financial liabilities: in the event of a change in the contractual terms of a liability that does not entail derecognition, it is expected that the effect of the change on amortised cost will be recognised in the income statement at the date of the change.

Accounting standards IAS/IFRS and SIC/IFRIC interpretations issued by IASB/IFRIC, awaiting validation

For the sake of completeness, below is a list of additional standards or interpretations, issued by the IAS/IFRIC but not yet validated, which, although of potential interest to the Group, are not retained as having any significant impact on the Group's equity or income situation or on financial statement disclosures:

- Interpretation IFRIC 23 -"Uncertainty over Income Tax Treatments" issued by the IFRIC on 7 June 2017, with a view to providing clarifications on how to apply the recognition and measurement criteria laid out in IAS 12 in the case of uncertainty regarding treatments for the determination of income tax.
- Amendments to IAS 28 – "Long-term Interests in associated companies and joint ventures" issued by the IASB on 12 October 2017, in order to clarify that an entity applies IFRS 9 to medium/long-term interests in associated companies or joint ventures for which it does not use the equity approach.
- Projects to improve several IFRS "2015-2016" (IFRS 3, IFRS 11, IAS 12 and IAS 23) issued by the IASB on 12 December 2017, to provide several clarifications that seek to resolve some inconsistencies or illustrate methods.
- Amendments to IAS 19 - "Changes, reductions or settlement of pension plans" issued by the IASB on 7 February 2018, with the aim of specifying how an entity must determine pension expenses in the event of changes in a defined benefit plan.
- Amendments to the "Conceptual Framework" issued on 29 March 2018 concerning the revision of the document issued in 2010 regarding the definitions and fundamental criteria on the basis of which the accounting standards are prepared.

Lastly, on 18 May 2017, the IASB issued the new IFRS 17 accounting standard governing policies issued by insurance companies, which is expected to be applied from 1 January 2021. Direct impacts on the Group's operations are not expected, as neither the Parent Company nor the subsidiaries carry out insurance activities.

Uncertainties with regard to the use of estimates for drawing up the consolidated condensed interim financial statements

The application of certain accounting standards necessarily involves the use of estimates and assumptions which affect the values of the assets and liabilities recorded in the financial statements and the disclosures made on potential assets and liabilities.
The assumptions underlying the estimates made take into account the information available as of the date of preparation of this Interim report, as well as the assumptions considered reasonable in the light of past experience and the current state of the financial markets. In this regard, note that the situation caused by the economic and financial crisis has made it necessary to make assumptions concerning future performance characterised by significant uncertainty.
Precisely in consideration of the uncertain situation, it cannot be excluded that the hypotheses adopted, however reasonable, might not be confirmed by future scenarios in which the Group finds itself operating. The results which will be achieved in the future could therefore differ from the estimates made for the purpose of drawing up this Interim report and could consequently make adjustments necessary which at present cannot be foreseen or estimated with respect to the book value of the assets and liabilities recorded in the financial statements.

The following paragraphs illustrate the estimation processes considered most critical to the truthful and correct portrayal of the Group’s equity, economic and financial situation, both in terms of the materiality of the values in the financial statements affected by said processes and the high level of judgement required for valuations that envisage the use of estimates and assumptions by Company management:

- determining the impairment on loans disbursed recognised in the balance sheet assets;
- estimated impairment losses in relation to intangible assets with an indefinite useful life and investments in associates;
- determining the fair value of financial assets and liabilities;
- estimating the recoverability of deferred tax assets;
- estimating provisions for risks and charges;
- estimating the recoverable value of real estate held for investment purposes;
- estimating obligations relating to employee benefits.

Determining the impairment on loans disbursed recognised in the balance sheet assets

Loans represent one of the items subject to estimates most exposed to choices made by the Group in terms of disbursement and risk management and monitoring.
More specifically, the Group manages the risk of default of borrowers by continuously monitoring customer accounts in order to assess their ability to repay the amount borrowed, based on their economic-financial situation. This monitoring activity is designed to detect signs of deterioration in loans, also with a view to a timely classification within the perimeter of impaired loans and a precise estimate of the relative total value adjustments. This estimate can be made, depending on the size of the exposure being measured, on an analytical basis based on recoverable cash flows, or on a lump-sum basis based on statistical parameters of the losses historically recorded on loans with similar characteristics.
With regard to loans for which no objective evidence of impairment has been individually identified, i.e. for performing loans, the new impairment model, based on expected losses, requires the implementation of adequate monitoring systems aimed at identifying whether or not there has been a significant deterioration since the date of initial recognition of the exposure. The IFRS 9 impairment model requires that losses be determined with reference to the time horizon of one year for financial assets that have not suffered a significant deterioration in their creditworthiness with respect to initial recognition (Stage 1) rather than with reference to the entire life of the financial asset if a significant deterioration is found (Stage 2).

On the basis of the above, it follows that losses on receivables must be recorded with reference not only to the objective evidence of impairment already seen at the reporting date, but also on the basis of expectations of future impairment losses not yet evident, which must be reflected:

- the likelihood of different scenarios occurring;
- the effect of discounting expected cash flows using the effective interest rate;
- historical experience and current and future valuations.

It follows that the determination of expected losses is a complex exercise that requires significant judgements and estimates. More specifically:

- the calculation of the significant deterioration in creditworthiness with respect to the date of initial recognition of the exposure is based on the identification of adequate qualitative and quantitative criteria, which also consider forward-looking information. Any amendment or refinement of the above criteria could therefore lead to significant changes in the size of the exposures to be classified as Stage 2, with consequent impacts on the total amount of the related expected losses;
- the result of the impairment model must reflect an objective estimate of the expected loss, obtained by evaluating a range of possible results. This implies the need to identify possible scenarios, based on assumptions about future economic conditions, to which the relative probability of occurrence must be associated. The selection of different scenarios and probability of occurrence and changes in the set of macroeconomic variables to be considered in the forecast time horizon could have significant effects on the calculation of expected losses;
- the determination of expected losses requires the use of estimation models:
  - the cash flows that individual debtors (or portfolios of debtors that are similar in terms of risk) are expected to be able to generate in order to satisfy, in whole or in part, the obligations undertaken with regard to the Group. With regard to impaired loans for which a disposal plan exists, the expected losses must be quantified also on the basis of the estimate of the recoverable flows through the disposal scenario, to be considered as an alternative scenario to the one based on the internal management of the recovery activity (work out) according to the multi scenario approach described above,
  - recovery time;
  - the estimated realisable value of property and collateral.

Within the range of possible approaches relating to estimation models permitted by the reference international accounting standards, the use of a method or the selection of certain estimation parameters may have a significant influence on the valuation of loans. These methods and parameters are necessarily updated through a continuous process with the aim of arriving at a best estimate in order to best represent the estimated realisable value of the credit exposure. It should also be noted that, in line with the new impairment model introduced by IFRS 9, any changes in the objectives of the NPL Strategy on the sales scenarios considered or any refinement of the statistical models on which the calculation parameters of expected losses on non-performing loans are based could also have significant impacts on the total amount of expected losses.

Given the above, it cannot be excluded that alternative monitoring criteria or different methodologies, parameters or assumptions in determining the recoverable value of the Group's credit exposures - influenced, however, also by possible alternative strategies for their recovery approved by the competent corporate bodies as well as by the evolution of the economic and financial context and reference regulations - may result in valuations different from those conducted for the purposes of the preparation of the consolidated condensed interim financial statements as at 30 June 2018.

Estimated impairment losses in relation to intangible assets with an indefinite useful life and investments in associates

Pursuant to IAS 36, all intangible assets with an indefinite useful life must undergo impairment testing at least once a year to verify the recoverability of their value. In addition, the standard establishes that the results of the annual test may be considered valid for subsequent tests, provided that the probability that the recoverable value is less than the book value of the intangible assets is considered remote. This opinion may be based on the analysis of the events which have occurred and the circumstances which have changed subsequent to the most recent annual impairment test.
Based on the provisions of the cited standard, the Banco BPM Group has opted to conduct impairment testing of intangible assets with an indefinite useful life on 31 December of each year, assessing exclusively for subsequent

interim situations, the possible existence of new impairment indicators that could cast doubt on the recoverability of the book values.
At 30 June 2018, the Group's intangible assets with an indefinite useful life amounted to 580.7 million euro, aligned with the figures at 31 December 2017, and were represented by 76.4 million euro of goodwill attributable to the “Bancassurance Protezione” cash generating unit (CGU) and the “Bancassurance Vita” CGU and 504.3 million euro of brands recognised following the business combination with the former Banca Popolare di Lodi Group (222.2 million euro) and the former BPM Group (282.1 million euro).
As illustrated in the section “Intangible assets – item 100” contained in "Part B – Consolidated balance sheet disclosure of these Illustrative notes", to which reference should be made for further details, during the period a survey was carried out to exclude the possible existence of further impairment indicators than those already considered for the purposes of the test conducted as at 31 December 2017, such as to cast doubt on the recoverability of the book values, also relying on the sensitivity analysis produced for the 2017 financial statements.
In this regard, it should be noted that the verification of the recoverability of these intangible assets is a complex exercise, the results of which are affected by the valuation methods adopted, as well as by the underlying parameters and assumptions, which may need to be modified to take account of new information or developments that could not be foreseen when this Report was prepared.
As regards equity investments, note that the non availability, as at the date of preparation of the consolidated condensed interim financial statements, of the balance sheets and income statements of the investee companies and of their updated forecast business plans, could introduce further elements of uncertainty in the process of assessing the value of equity investments. In these circumstances, we can therefore not exclude the possibility that the value attributed to the equity investments based on the information available may possibly differ from subsequent assessments made in light of different available information.

Determination of the fair value of financial assets and liabilities

In the event of financial instruments that are not listed on active markets or illiquid and complex instruments, adequate valuation processes need to be set in place, characterised by a certain amount of subjective judgement as regards the choice of the valuation model and of the relative input parameters, which sometimes cannot be observed in the market.
There are margins of subjectivity in the valuation with regard to whether certain parameters are observable or not, and in the consequent classification in correspondence with the fair value hierarchy levels.
For qualitative and quantitative information on the methods adopted to measure the fair value of instruments recognised at fair value through profit and loss in the financial statements and for those values at amortised cost, please refer to “Part A.4 - Fair value disclosure” below.

Estimating the recoverability of deferred tax assets

The Group has significant deferred tax assets among its assets, mainly deriving from temporary differences between the income statement recognition date of given business costs and the date when said costs may be deducted, and also resulting from tax losses carried forward. The recognition of these assets and the subsequent maintenance in the balance sheet entails a judgement as to the potential recoverability of the same. Said judgement of recoverability is also based on the legislative tax provisions in force on the date of preparation of this report. These provisions permit deferred tax assets that meet the requirements established by Law no. 214 of 22 December 2011 to be transformed into tax credit in the event that a statutory loss, a tax loss for IRES purposes, or a net negative value of production, for IRAP purposes, is recorded, therefore making their recovery certain, regardless of the ability to generate future profits. With regard to deferred tax assets resulting from tax losses for IRES purposes, current legislation allows the same to be carried forward without any time restriction. For said deferred tax assets and for the residual assets resulting from temporary differences other than those previously cited, the judgement of probability is based on the income forecasts that can be inferred on the basis of the approved strategic and forecast plans.
In this regard, it is important to note that verifying the recoverability of the recognition values of deferred tax assets is a valuation that requires significant elements of judgement.
The recoverability could also be negatively influenced by circumstances that are not foreseeable at the present time, such as changes to the current tax legislation or changes in the macroeconomic or market scenario, which would then require an update of the income forecasts used as a basis to estimate future taxable income. For this reason, the recoverability of the DTA that cannot be transformed into tax credit is continuously monitored with regard to changes in tax legislation and in the results recorded, which may be negatively influenced by the economic and market scenario.

Estimating provisions for risks and charges

The companies belonging to the Group are defendants in a wide range of lawsuits and tax disputes and are also exposed to a number of types of contingent liabilities. The complexity of the situations and corporate deals that underlie the outstanding disputes, along with the difficulties in the interpretation of applicable law, require significant elements of judgement to estimate the liabilities that may result when pending lawsuits are settled. The difficulties lie in assessing if and what may be due and how much time will elapse before liabilities materialise and are particularly evident when the proceedings are at the initial stage and/or the relative preliminary analysis is underway. The specific nature of the matter disputed and the consequent absence of case law relating to similar disputes, not to mention the differing opinions expressed by judgement bodies both at the various levels of the proceedings and by bodies at the same level over time, make a valuation of the potential liabilities difficult even when the provisional rulings relating to the courts of first instance are available. Previous experience demonstrates that in a number of cases, the rulings made by the judges in the courts of first instance were then completely overturned on appeal or in the supreme court, which may be in favour or not in favour of Group companies. On the basis of the above, the classification of potential liabilities and the consequent valuation of the provisions needed is based on subjective elements of judgement which require recourse to estimation processes which can be highly complex. It cannot therefore be ruled out that following the issue of the final rulings, allocations made to provisions for risks and charges on the basis of the potential liabilities of lawsuits and tax disputes may turn out to be lacking or surplus to requirements.
Information on the main risk positions of the Group relating to legal disputes (clawback actions and lawsuits in progress) and tax disputes with the tax authorities is provided in the section ”Liability provisions – item 90 and 100” in "Part B – Consolidated balance sheet disclosure of these Illustrative Notes".

Estimating the recoverable value of real estate assets held for investment purposes

The Group possesses real estate for investment purposes, mostly originating from properties repossessed to close an original credit position (*datio in solutum* - acceptance in lieu) or from an agreement to settle a dispute. For these assets, in the event of indicators that could potentially show an impairment loss, the recoverable value has to be established, recognising a write-down if said value should be lower than the book value. The estimation of recoverable value, conducted using external appraisals, was impacted by an inevitable component of subjectivity in certain circumstances, amplified by the specific characteristics of each property. In this regard, note that the difficulties related to this estimation process are particularly evident in the current scenario of the Italian property market, the reference market for almost all of the Group’s properties. Therefore, in the future, the possibility of a further reduction in the recoverable value cannot be excluded if the performance of the real estate sector should worsen and, consequently, the values expressed by the market should be lower than the situation existing at the date of the appraisals.

Estimating obligations relating to employee benefits

The calculation of the liabilities associated to employee benefits, with specific reference to defined benefit plans and to long-term benefits, implies a certain degree of complexity; the outcome of assessments depends, to a large extent, on the actuarial assumptions used in both demographic terms (such as mortality rates and employee turnover) and financial terms (such as discounting rates and rates of inflation). The judgement expressed by management is therefore fundamental when selecting the most suitable technical bases for the assessment in question, which is influenced by the socio-economic climate in which the Group operates, as well as the performance of the financial markets.

The main actuarial assumptions used by the Group at 30 June 2018, compared with those used at 31 December 2017, are given below:

Demographic assumptions	
Employee mortality rate	30/06/2018: IPS55 Demographic basis for annuity insurance 31/12/2017: IPS55 Demographic basis for annuity insurance
Frequency and amount of advances on employee termination indemnities	30/06/2018: up to 1.5% 31/12/2017: up to 1.5%
Frequency of turnover	30/06/2018: 1.0%-3.5% 31/12/2017: 1.0%-3.5%

Financial assumptions	
Yearly discounting rate (*)	30/06/2018: Iboxx Euro Corporate AA index, with the time reference corresponding to the average duration of defined benefit plans (social security, employee termination indemnities and seniority bonuses)
	31/12/2017: Iboxx Euro Corporate AA index, with the time reference corresponding to the average duration of defined benefit plans (social security, employee termination indemnities and seniority bonuses)
Annual inflation rate	30/06/2018: 1.50%
	31/12/2017: 1.50%

(*) At June 30, 2018, the Iboxx Euro AA 7-10 year Corporate Index was 0.98% (0.88% at 31 December 2017), and the Iboxx Euro AA 10+ Corporate Index was 1.45% (1.30% at 31 December 2017)

The list of valuation processes shown above is included simply to provide readers with a better understanding of the main areas of uncertainty, and it should in no way be considered as implying that, to date, alternative assumptions can prove more appropriate. In addition, valuations are based on the going concern assumption: the directors, in fact, have a reasonable expectation that the Group will continue its current activity in the foreseeable future and have prepared the interim financial statements on the assumption of going concern. Information on risks and related controls can be found in "Part E –Information on risks and related hedging policies" of these Illustrative Notes, as well as in the Group's interim report on operations.

Notes for a proper comparison of the comparative financial statements and comparative information

In addition to what is shown in the initial section dedicated to illustrating the impacts of the first time adoption of the IFRS 9 and IFRS 15 accounting standards, which makes the balances at 30 June 2018 not fully comparable with those of the previous financial year/period, it should be noted that the income statement balances at 30 June 2017—contained in the financial statements and in the tables of the illustrative notes—have been restated with respect to those originally published, in order to retrospectively reflect the contribution of the subsidiary Aletti Gestielle SGR S.p.A. pursuant to IFRS 5. Starting from the third quarter of 2017, the investee company in question was classified as a discontinued operation, following negotiations with Anima Holding which were completed with the sale of the investee company on 28 December 2017. Due to the aforementioned standard, the positive contribution of Aletti Gestielle SGR S.p.A., amounting to 45.4 million euro, which in the previous year's financial statements was represented in the various items of the income statement as a result of the line-by-line consolidation, was reclassified to the summary item of the income statement "320. Profit (loss) from discontinued operations, net of taxes".
A reconciliation schedule between the income statement for the first half of 2017, restated as described above, and the originally published income statement are attached.

Application of the Group's accounting policies to completed transactions or events during the period

Non-recourse assignment of "Project Exodus" bad loans

As illustrated in the "Significant events during the period" section of the Interim report on operations, in June 2018 the sale of a portfolio of loans classified as bad loans was completed through a securitisation transaction aimed at obtaining a state guarantee for senior securities (the Guarantee Securitisation of Non-performing loans - GACS pursuant to Decree no. 18 of 14 February 2016 converted into Law no. 49 of 8 April 2016 and the subsequent MEF decree of 3 August 2016).
More specifically, on 1 June 2018 this operation, called "Project Exodus", involved the transfer of a portfolio of bad loans, for a gross nominal amount of approximately 5 billion euro, to a SPE set up for this purpose, not belonging to the Banco BPM Group (Red Sea SPV S.r.l.).

The payment of the purchase price by the SPE was financed on 15 June 2018 through the issue of three classes of notes, which were initially fully subscribed by the originating banks (Banco BPM and BPM S.p.A.), for a nominal value of approximately 1.9 billion euro, distributed as follows:

- senior securities (Class A) for 1,656.5 million euro. These securities hold an Investment Grade rating (Moody's: Baa2; Scope: BBB (SF) and its yield is equal to the 6-month Euribor plus an annual spread of 0.6%;
- Mezzanine securities (Class B) securities 152.9 million euro. These unrated securities provide for a yield equal to 6-month Euribor plus an annual spread of 6 %;
- junior (Class J) securities amounting to 51 million euro. These securities, which are not rated, provide for variable remuneration depending on the performance of the securitisation.

Subsequently, on 29 June 2018, in compliance with the retention rule established by supervisory regulations, the Group transferred 95% of its junior shares and 95% of its mezzanine shares to third parties, i.e. the shares that bear the first loss and that may benefit from the excess spread of the transaction; the consideration paid at the time of the sale totalled 54.7 million euro.

Following this sale, on 29 June 2018, the conditions were met for the derecognition of the portfolio of bad loans transferred to be derecognised, since the rights and benefits of the sold financial assets were substantially transferred.

Regarding the transferred loans, it should also be noted that the Group has no power—neither in fact nor in law—to manage the relevant activities of the SPE, represented by the activities aimed at recovering the credit. Based on the reference regulations for GACS discussed previously, the recovery of the transferred bad loans was entrusted to an external servicer and the Group does not maintain any form of involvement.

The economic effects of the disposal, quantified on the basis of the difference between the book value at the beginning of the year and the net amount received, including the new assets acquired, were negative and equal to 221 million euro. Taking into account the reversal of the discounting of the loans sold, due to the passage of time and recognised in interest margin up to the date of sale, the losses recognised in item "100 a) Gains/losses on the disposal of financial assets" amounts to approximately 276 million euro.

In the light of the above, as at 30 June 2018 the Group holds:

- all senior securities classified as the portfolio of "Financial assets designated at amortised cost: b) loans to customers". Taking into account the impairment model based on expected losses, the book value amounts to 1,654.2 million euro;
- 5% of mezzanine securities and 5% of junior securities classified in the portfolio of "Financial assets designated at fair value through profit and loss" at the book value of 2.9 million euro. The valuation at fair value was based on the price of the sale transaction completed on 29 June 2018 (level 3 in the fair value hierarchy).

For the sake of full disclosure, financial assets designated at amortised cost include a limited recourse loan granted to the SPE amounting to 72.4 million euro. The purpose of this loan was to establish a cash reserve equal to 4% of the nominal value of the senior and mezzanine securities. In this regard, it should be noted that this loan does not represent any form of credit support to the securitisation; in the waterfall payments, the repayment of the loan in question is different from the payment of the principal of the senior securities and the payment of the principal and interest of the mezzanine securities.

Fee to guarantee the convertibility of DTA - legislative changes to Decree Law no. 59/2016

Please recall that article 11 of Italian Decree Law no. 59 of 3 May 2016, converted with amendments into Italian Law no. 119 of 30 June 2016, introduced an optional regime by virtue of which the guarantee on the convertibility into tax credits of deferred tax assets (DTA) which meet the requirements laid out in Law no. 214 of 22 December 2011 is subject to the payment of a fee, due for the years starting from 31 December 2015 until 31 December 2029, to be determined on an annual basis.

On 21 February 2017, the law (Law no. 15 of 17 February 2017) converting the *Salva Risparmio* Decree Law was published in the Official Gazette; in detail, Art. 26 *bis*, paragraph 4, amended Article 11 of Decree Law 59/2016, postponing the period for which the annual fee is due, which is now from 31 December 2016 until 31 December 2030.

Pursuant to these regulatory references, the exercise of this option, which was carried out in 2016 by both groups involved in the merger, is considered irrevocable.

In more detail, the annual fee to be paid to ensure the convertibility of the above-mentioned deferred tax assets into tax credits must be determined on an annual basis by applying the rate of 1.5% to a base obtained by adding the difference between the convertible deferred tax assets recognised in the financial statements for the previous year and the corresponding deferred tax assets recognised in the 2007 financial statements, to the amount of conversions of the same deferred tax assets carried out from 2008 until the previous year, and subtracting the taxes set forth in the Decree and paid with reference to the above-mentioned tax periods (base also referred to as "type 2 DTA"). The fees are deductible for both IRES and IRAP purposes in the year in which they are paid.
In accordance with the above regulatory provisions, in the income statement item "190.b) Other administrative expenses" in the first half of 2018, a charge of 12.6 million euro was charged, corresponding to fees relating to the first six months of the annual fee for 2018, as determined above (13.4 million euro was the amount charged to the income statement for the first half of 2017).

TLTRO II – Targeted Longer Term Refinancing Operations

As at 30 June 2018, the ECB funding transactions, consisting entirely of TLTRO II loans, amount to euro 21.4 billion, of which euro 15 billion relating to the parent company Banco BPM and euro 6.4 billion relating to the subsidiary BPM S.p.A.
For each TLTRO II transaction, with a fixed maturity of four years from the time of disbursement (which took place on the basis of four quarterly auctions starting from June 2016), the reference rate is that applied to the main refinancing transactions at the date of each allotment, equal to zero. In any event, there was also the possibility to benefit from the more favourable interest rate on deposits with the ECB, to the maximum extent of 0.4%, if, between 1 February 2016 and 31 January 2018, the net eligible loans exceed a given benchmark level by at least 2.5%.
As at 31 January 2018, it was confirmed that both Banco BPM and the subsidiary BPM S.p.A. had reached the benchmark level. The application of a negative interest rate of up to 0.4% on the funding transactions in question is therefore confirmed, in line with the reference rate used for the recognition of fees as from 2017.
In this regard, it should be noted that interest for the first half of 2018 amount to 43.1 million euro.
Interest accrued in the first half of 2017 amounted to 71.7 million euro and included 31.7 million euro of amounts not recognised in the previous year, in the absence of conditions for their recognition.
This interest, even if referring to financial liabilities, is recorded in the income statement under "interest income".

Contributions to deposit guarantee schemes and resolution mechanisms

With Directives 2014/49/EU (Deposit Guarantee Schemes Directive – DGSD) of 16 April 2014 and 2014/59/EU (Bank Recovery and Resolution Directive – BRRD) of 15 May 2014 and the creation of the Single Resolution Mechanism (EU Regulation no. 806/2014 of 15 July 2014), significant changes were made to European law concerning the governance of banking crises, with the strategic purpose of strengthening the single market and ensuring system-wide stability. Following the assimilation of these directives into national legislation, from 2015, credit entities must provide the financial resources needed to finance the Interbank Deposit Guarantee Fund (IDGF) and the National Resolution Fund, merged into the Single Resolution Fund (SRF) from 2016, by paying ordinary and, where necessary, extraordinary contributions.
In compliance with the DGSD directive, the IDGF has envisaged that Italian banks must pay ordinary annual contributions until the target level is reached, corresponding to 0.8% of total guaranteed deposits of the Italian banks that are members of the IDGF. Said level must be reached by 3 July 2024. The extent of the contribution requested of the individual bank is proportional to the amount of its guaranteed deposits as at 30 September of each year, with respect to the total guaranteed deposits of the Italian member banks of the IDGF and the degree of risk relating to the member bank with guaranteed deposits with respect to the level of risk of all of the other member banks of the IDGF.
As envisaged by the BRRD, Italian banks must make annual ordinary contributions until the SRF has acquired financial resources that are at least 1% of the total guaranteed deposits of all authorised credit entities in all participating Member States. This level must be reached by 1 January 2024. The contributions from each entity are calculated based on the ratio of the amount of their liabilities (net of guaranteed deposits and own funds, for entities belonging to a group, of intergroup liabilities) to the total liabilities (net of guaranteed deposits and own funds) of Italian banks and of the relative level of risk of each credit entity to the level of risk of all other Italian banks.
Note that if the available financial resources of the IDGF and/or of the SRF are insufficient, respectively to guarantee reimbursement to depositors or to fund the resolution, it is envisaged that the credit entities must then make extraordinary contributions.

The ordinary contribution was recognised under item "190. b) Other administrative expenses" in application of IFRIC 21 interpretation "Levies", on the basis of which the liability relating to the payment of a levy - the contributions in question have been considered the equivalent of a levy for accounting purposes - emerges from the time at which the "obligating event" arises, namely at the time of the obligation to pay the annual fee. With regard to the contribution in question, the time the obligating event arises has been identified in the first quarter for the SRF and in the third quarter for the IDGF.
Specifically, the ordinary contribution to the SRF for 2018 amounted to 68.0 million euro, entirely charged to the income statement in the first quarter (62.4 million euro was the ordinary contribution for 2017). In this regard, please note that in 2018, as in the previous year, the Group did not avail itself of the option of fulfilling the request by entering into an irrevocable commitment to pay (IPC).
In addition, in May 2018, the Bank of Italy called in additional contributions to the National Resolution Fund for 25.5 million euro, in relation to the financial requirements connected with the termination measures carried out prior to the launch of the SRF; this amount was charged in the period under item "190. b) Other administrative expenses" (in 2017 no additional contributions were requested).

Scope of consolidation and methods

(A) Subsidiary companies

The consolidated condensed interim financial statements include the balance sheet and income statement results of the Parent Company Banco BPM S.p.A. and its direct and indirect subsidiaries, including structured entities, in accordance with that envisaged by accounting standard IFRS 10. Based on the cited standard, the requirement of control is the basis for the consolidation of all types of entity, including structured entities, and is met when an investor simultaneously:

- has the power to direct the relevant activities of the entity;
- is exposed to or benefits from variable returns resulting from its involvement with the entity;
- has the ability to use its power to affect the amount of said returns (link between power and returns).

IFRS 10 establishes therefore that, in order to possess control, the investor must have the ability to direct the relevant activities of the entity, by virtue of a legal right or of a mere state of fact, and must also be exposed to changes in the results that result from said power.

The Group therefore consolidates all types of entity when all three control elements are present.

Generally, when an entity is considered direct by virtue of voting rights, control results from holding over half of the voting rights.
In the other cases, establishing the scope of consolidation requires all factors and circumstances that give the investor the practical ability to unilaterally conduct the relevant activities of the entity (actual control). To this end, a set of factors has to be considered, such as, merely by way of example:

- the purpose and the design of the entity;
- the identification of the relevant activities and how they are managed;
- any right held by means of contractual arrangements which awards the power to direct the relevant activities, such as the power to establish the financial and operating policies of the entity, the power to exercise majority voting rights in the decision-making body or the power to appoint or remove the majority of the body with decision-making functions;
- any voting rights that may potentially be exercised and that are considered substantial;
- involvement with the entity in the role of agent or principal;
- the nature and dispersion of any rights held by other investors.

The following paragraphs provide further details on the scope of entities controlled exclusively as at 30 June 2018, broken down into companies controlled through voting rights and structured entities.

Companies controlled through voting rights

With reference to the Group's situation as at 30 June 2018, companies in which a majority of voting rights in the ordinary shareholders meeting is held are considered to be exclusively controlled, insofar as there is no evidence that other investors have the practical ability to direct the relevant activities.
As regards companies in which half or a lower amount of voting rights are held, as at 30 June 2018, there are no arrangements, statutory clauses, or situations able to establish that the Group has the practical ability to unilaterally direct the relevant activities.

Consolidated structured entities

The control of structured entities, namely entities for which voting rights are not considered relevant to establish control, is retained to exist where the Group has contractual rights to manage the relevant activities of the entity and is exposed to the variable returns of the same. On this basis, at 30 June 2018 the consolidated structured entities recognised by the Group are represented by the SPEs for securitisation transactions.

Special Purpose Entities for securitisation transactions

With regard to Special Purpose Entities for securitisation transactions, the elements retained as relevant for the purpose of identifying control and therefore the need for any consolidation, are represented by:
- the purpose of said SPEs;
- exposure to the outcome of the transaction;
- the ability to structure transactions and to direct the relevant activities and take critical decisions through servicing contracts;
- the ability to arrange for their liquidation.

Line-by-line consolidation method

Controlled entities are consolidated from the date on which the Group acquires control, according to the purchase method, and cease to be consolidated from the moment in which a situation of control no longer exists, as described in the "Business combinations, goodwill and changes in interest holdings" section below under "A.2 - Key financial statement items", which should be referred to.

Full consolidation consists of the "line-by-line" acquisition of the balance sheet and income statement aggregates of subsidiary entities. For consolidation purposes, the book value of the equity investments held by the Parent Company or by the other Group companies is eliminated against the acquisition of the assets and liabilities of the investees, as a balancing entry to the corresponding portion of shareholders' equity attributable to the Group and the portion held by minority interests, also taking into account the purchase price allocation upon acquisition of control.

For subsidiary entities, the portion of shareholders' equity, income (loss) for the year and comprehensive income pertaining to minority interests is indicated as a separate item in the respective schedules of the consolidated financial statements (respectively in items: "190. Minority interests", "340. Income (loss) attributable to minority interests", "190. Consolidated comprehensive income attributable to minority interests").
In this regard, please note that there is no effect on the balance sheet, the income (loss) or comprehensive income pertaining to minority interests resulting from the consolidation of the separate equities held by the SPEs for securitisations originated by the Group, not subject to derecognition in the separate financial statements of the assigning Group banks. For a description of the effects of the consolidation of these equities, please refer to the information contained in part "A.2. Key financial statement items" below, section "16 - Other information, Securitisations - derecognition from financial statements of financial assets transferred".

The costs and revenues of the subsidiary entity are consolidated from the date on which control was acquired. The costs and revenues of a subsidiary sold are included in the income statement up until the date of the disposal; the difference between the sale price and the book value of the net assets of the same is recognised under the income statement item "280. Profits (losses) on disposal of investments". In the event of the partial disposal of a subsidiary entity, which does not result in a loss of control, the difference between the sale price and the relative book value is recognised as a balancing entry of shareholders' equity.

The assets, liabilities, off-balance sheet transactions, income and expenses relating to transactions between consolidated companies are eliminated in full.

The balance sheet and income statement results of the consolidated companies whose operating currency is different from the Euro are translated based on the following rules:

- the balance sheet assets and liabilities are converted at the exchange rate in effect at the end of the period;
- the revenues and costs on the income statement are converted at the average exchange rate for the period.

All exchange rate differences originated by the conversion are recognised in a specific valuation reserve under shareholder's equity. Said reserve is eliminated through a concurrent debit/crediting of the income statement when the investment is disposed of. Changes in value of the valuation reserve due to exchange differences are included in the Statement of comprehensive income.

In order to prepare the consolidated condensed interim financial statements as at 30 June 2018, all of the exclusively controlled companies have prepared a balance sheet and income statement in accordance with the Group's accounting principles.

Investments in associates and companies subject to joint control held for sale are recorded in compliance with the reference international accounting standard IFRS 5, which regulates the recording of non-current assets held for sale. In this case, the assets and liabilities held for sale are included in the balance sheet items "120. Non-current assets and asset disposal groups held for sale" and "70. Liabilities associated with non-current assets and asset disposal groups held for sale". As regards the income statement, expenses and income associated with assets and liabilities classified as held for sale, net of taxes, have been recognised in the separate item "320. Profit (loss) from discontinued operations, net of taxes". If the fair value of the assets and liabilities held for sale, net of selling costs, turns out to be lower than the book value, a value adjustment is recognised in the income statement.

List of equity investments in exclusively controlled companies

Company name	Operational headquarters	Registered office	Type of relationship (1)	Investment relationship		Available % of votes (2)
				Participating Undertaking	% held	
Banco BPM S.p.A.	**Verona**	**Milan**	**Parent Group**			
1. Agriurbe S.r.l. (in liquidation)	Milan	Milan		Banco BPM	100.000%	100.000%
2. Aletti & C. Banca di Investimento Mobiliare S.p.A.	Milan	Milan	1	Banco BPM	100.000%	100.000%
3. Aletti Fiduciaria S.p.A.	Milan	Milan	1	Banca Aletti & C.	100.000%	100.000%
4. Arena Broker S.r.l.	Verona	Verona	1	Holding di Partecipazioni	57.300%	57.300%
5. Banca Akros S.p.A.	Milan	Milan	1	Banco BPM	100.000%	100.000%
6. Banca Aletti & C. (Suisse) S.A.	CH - Lugano	CH - Lugano	1	Banca Aletti & C.	100.000%	100.000%
7. Banca Popolare di Milano S.p.A.	Milan	Milan	1	Banco BPM	100.000%	100.000%
8. Bipielle Bank (Suisse) S.A. (In liquidation)	CH - Lugano	CH - Lugano	1	Banco BPM	100.000%	100.000%
9. Bipielle Real Estate S.p.A.	Lodi	Lodi	1	Banco BPM	100.000%	100.000%
10. BPM Covered Bond S.r.l.	Rome	Rome	1	Banco BPM	80.000%	80.000%
11. BPM Covered Bond 2 S.r.l.	Rome	Rome	1	Banco BPM	80.000%	80.000%
12. BRF Property S.p.A.	Parma	Parma	1	Partecipazioni Italiane	51.114%	51.114%
				Banco BPM	14.314%	14.314%
13. BP Covered Bond S.r.l.	Milan	Milan	1	Banco BPM	60.000%	60.000%
14. BP Property Management Soc. Consortile a r.l.	Verona	Verona	1	Banco BPM	92.309%	99.462%
				Bipielle Real Estate	4.615%	
				Banca Aletti & C.	1.000%	
				S.G.S. BP	1.000%	
				Holding di Partecipazioni	0.538%	
15. BP Trading Immobiliare S.r.l.	Lodi	Lodi	1	Bipielle Real Estate	100.000%	100.000%
16. Consorzio AT01	Lodi	Lodi	1	Sviluppo Comparto 8	95.000%	95.000%
17. FIN.E.R.T. S.p.A. (in liquidation)	Rome	Rome	1	Banco BPM	80.000%	80.000%
18. Ge.Se.So. S.r.l.	Milan	Milan	1	Banco BPM	100.000%	100.000%

Company name	Operational headquarters	Registered office	Type of relationship (1)	Investment relationship		Available % of votes (2)
				Participating Undertaking	% held	
19. Holding di Partecipazioni Finanziarie Banco Popolare S.p.A.	Verona	Verona	1	Banco BPM	100.000%	100.000%
20. Immobiliare Marinai d'Italia S.r.l.	Lodi	Lodi	1	Banco BPM	100.000%	100.000%
21. Liberty S.r.l. (in liquidation)	Lodi	Lodi	1	Banco BPM	100.000%	100.000%
22. Lido dei Coralli S.r.l.	Sassari	Sassari	1	Bipielle Real Estate	100.000%	100.000%
23. Manzoni 65 S.r.l.	Milan	Milan	1	Bipielle Real Estate	100.000%	100.000%
24. Mariner S.r.l. (*)	Lodi	Lodi	1	Bipielle Real Estate	100.000%	100.000%
25. Meleti S.r.l.	Lodi	Lodi	1	Perca	100.000%	100.000%
26. Milano Leasing S.p.A. (in liquidation)	Milan	Milan	1	Banco BPM	99.999%	99.999%
27. Partecipazioni Italiane S.p.A. (in liquidation)	Milan	Milan	1	Banco BPM	99.966%	100.000%
28. Perca S.r.l.	Lodi	Lodi	1	Immobiliare Marinai d'Italia	100.000%	100.000%
29. P.M.G. S.r.l. (in liquidation)	Milan	Milan	1	Banco BPM	84.000%	84.000%
30. ProFamily S.p.A.	Milan	Milan	1	Banco BPM	100.000%	100.000%
31. Release S.p.A.	Milan	Milan	1	Banco BPM	85.387%	85.387%
32. Sagim S.r.l. Società Agricola	Asciano (Siena)	Asciano (Siena)	1	Agriurbe	100.000%	100.000%
33. Sirio Immobiliare S.r.l.	Lodi	Lodi	1	Bipielle Real Estate	100.000%	100.000%
34. Società Gestione Servizi BP Soc. Consortile p.az.	Verona	Verona	1	Banco BPM	68.334%	99.562%
				Banca Akros	4.093%	
				Banca Aletti & C.	8.753%	
				Banca Popolare di Milano	17.506%	
				Bipielle Real Estate	0.438%	
				Holding di Partecipazioni	0.438%	
35. Sviluppo Comparto 6 S.r.l.	Lodi	Lodi	1	Bipielle Real Estate	100.000%	100.000%
36. Sviluppo Comparto 8 S.r.l.	Lodi	Lodi	1	Bipielle Real Estate	100.000%	100.000%
37. Tecmarket Servizi S.p.A.	Verona	Verona	1	Banco BPM	100.000%	100.000%
38. Terme Ioniche S.r.l.	Cosenza	Lodi	1	Bipielle Real Estate	100.000%	100.000%
39. Terme Ioniche Società Agricola S.r.l.	Cosenza	Cosenza	1	Bipielle Real Estate	100.000%	100.000%
40. Tiepolo Finance S.r.l.	Lodi	Lodi	1	Banco BPM	60.000%	60.000%
41. BP Mortgages S.r.l. (**)	Milan	Milan	4	-	0.000%	
42. BPL Mortgages S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	-	0.000%	
43. BPM Securitisation 2 S.r.l. (**)	Rome	Rome	4	-	0.000%	
44. BPM Securitisation 3 S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	-	0.000%	
45. Erice Finance S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	-	0.000%	
46. Italfinance Securitisation VH 1 S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	Banco BPM	9.900%	9.900%
47. Italfinance Securitisation VH 2 S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	-	0.000%	
48. Leasimpresa Finance S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	-	0.000%	
49. Profamily Securitisation S.r.l. (**)	Conegliano V. (Treviso)	Conegliano V. (Treviso)	4	-	0.000%	

(1) Type of relationship:
1 = majority of voting rights in the ordinary shareholders' meeting
4 = other forms of control
(2) Availability of votes in the ordinary shareholders' meeting, distinguishing between actual and potential
(*) Company undergoing disposal as per IFRS 5.
(**) Special Purpose Entity for securitisation transactions originated by the Group.

(B) Investments in companies subject to joint control and subject to significant influence

The table below provides information on investments in companies subject to joint control and significant influence by the Banco BPM Group.

Company name	Registered office	Operational headquarters	Type of relationship (a)	Investment relationship		Available % of votes
				Holder	% held	
A. Companies subject to joint control						
N/A						
B. Companies subject to significant influence						
1. Agos Ducato S.p.A.	Milan	Milan	1	Banco BPM	39.000%	39.000%
2. Alba Leasing S.p.A.	Milan	Milan	1	Banco BPM	39.189%	39.189%
3. Aosta Factor S.p.A.	Aosta	Aosta	1	Banco BPM	20.690%	20.690%
4. Arcene Immobili S.r.l. (in liquidation)	Lodi	Lodi	1	Banco BPM	50.000%	50.000%
5. Arcene Infra S.r.l. (in liquidation)	Lodi	Lodi	1	Banco BPM	50.000%	50.000%
6. Bipiemme Vita S.p.A. (*)	Milan	Milan	1	Banco BPM	19.000%	19.000%
7. Bussentina S.c.a r.l. (in liquidation)	Rome	Rome	1	Bipielle Real Estate	20.000%	20.000%
8. Calliope Finance S.r.l. in liquidation	Conegliano V. (Treviso)	Conegliano V. (Treviso)	1	Banco BPM	50.000%	50.000%
9. Etica SGR S.p.A. (*)	Milan	Milan	1	Banco BPM	19.444%	19.444%
10. Factorit S.p.A.	Milan	Milan	1	Banco BPM	39.500%	39.500%
11. GEMA Magazzini Generali BPV-BSGSP S.p.A.	Castelnovo Sotto (Reggio Emilia)	Castelnovo Sotto (Reggio Emilia)	1	Banco BPM	33.333%	33.333%
12. HI-MTF SIM S.p.A.	Milan	Milan	1	Banca Aletti	25.000%	25.000%
13. Immobiliare Centro Milano S.p.A.	Milan	Milan	1	Release	33.333%	33.333%
14. Motia Compagnia di Navigazione S.p.A.	Venice	Venice	1	Banco BPM	25.000%	25.000%
15. SelmaBipiemme Leasing S.p.A.	Milan	Milan	1	Banco BPM	40.000%	40.000%
16. S.E.T.A. Società Edilizia Tavazzano S.r.l. (in liquidation)	Milan	Milan	1	Banco BPM	32.500%	32.500%
17. Vera Assicurazioni S.p.A.	Milan	Milan	1	Banco BPM	35.000%	35.000%
18. Vera Vita S.p.A.	Novara	Novara	1	Banco BPM	35.000%	35.000%

(a) Type of relationship:
1 = investment in share capital
(*) Companies subject to significant influence based on partnership agreements or shareholders' agreements with other shareholders.

For a description of the classification, recognition, equity method measurement and derecognition criteria, reference should be made to Part "A.2 - Key financial statement items" below - section "5. Investments in associates and companies subject to joint control".

Changes in the scope of consolidation

In the sector of companies consolidated on a line-by-line basis, the only change in the consolidation scope during the period was due to the completion of the liquidation procedure and the consequent cancellation of the subsidiary Pami Finance S.r.l. from the competent company register.

With reference to the perimeter of associated companies, please note that as part of the reorganisation of the Bancassurance business unit, in March Banco BPM completed the acquisition of 50% + 1 share of Avipop Assicurazioni and Popolare Vita, bringing its stake in the share capital of the two companies to 100%. On the same date, Banco BPM completed the sale to Cattolica Assicurazioni of 65% of the share capital of Avipop Assicurazioni and Popolare Vita. As a result of these transactions, the Group holds 35% of the share capital of the two companies which, in May, changed their corporate names to Vera Assicurazioni and Vera Vita respectively. Such interests continue to be classified as investments in associates and companies subject to joint control and accounted for using the equity approach.

Lastly, the associate Renting Italease S.r.l. left the investments in associates and companies subject to joint control carried at equity segment valued using the equity method, following the completion of the sale to third parties of the interest held by Bipielle Real Estate, equal to 50% of the share capital.

For further details, please refer to the section that illustrates the significant events that occurred during the period.

A.2 - KEY FINANCIAL STATEMENT ITEMS

The following accounting standards adopted to prepare the 30 June 2018 consolidated condensed interim financial statements, effective from 1 January 2018, are described below by financial statement item, with reference to the phases of classification, recognition, measurement and derecognition of the various asset and liability items, as well as the methods for recognising revenue and costs.

1 - Financial assets designated at fair value through profit and loss

Classification criteria

This category includes financial assets other than those classified under "Financial assets designated at fair value through other comprehensive income" and "Financial assets designated at amortised cost". This includes:

- the debt securities or loans to which an Other business model is connected, i.e. a method of managing financial assets that is not aimed at collecting contractual cash flows (Hold to collect business model) or at collecting contractual cash flows and selling financial assets (Hold to Collect and Sell business model);
- debt securities, loans and UCIT units for which the contractual terms do not exclusively provide for the repayment of principal and payment of interest on the amount of principal to be repaid (i.e. which do no pass the SPPI test);
- equity instruments, that do not qualify as investments in subsidiaries, associates and entities under joint control, held for trading or for which, during initial recognition, the option of classifying them as "Financial assets designated at fair value through other comprehensive income" was not implemented.

More detailed information is provided below on the three sub-items making up this category, represented by: "a) Financial assets held for trading", "b) Financial assets designated at fair value through profit and loss", "c) Other financial assets that must be measured at fair value".

a) Financial assets held for trading

A financial asset (debt securities, equity instruments, loans, UCIT units) is classified as held for trading if it is managed with a view to collecting cash flows through sale, i.e. if it is associated with the Other business model, as:

- it is acquired for the purpose of being sold in the near future;
- it is part of a portfolio of financial instruments that are jointly managed and for which there is a proven strategy for short-term profit.

It also includes derivative contracts with a positive fair value, not designated as part of a recognised hedge. Derivative contracts include those embedded in structured financial instruments, in which the host contract is a financial liability, that have been recognised separately because:

- their economic characteristics and risks are not closely related to those of the host contract;
- a separate instrument with the same terms as the embedded derivative would meet the definition of derivative;
- the hybrid instruments to which they belong are not designated at fair value with changes in fair value through profit or loss with the related changes recorded in the income statement.

A derivative is considered to be a financial instrument or other contract that has the following characteristics:

- its value changes in response to changes in an interest rate, in the price of a financial instrument, in a commodity price, in the exchange rate in foreign currency, in a price or rate index, in a credit rating or in a credit index or in another pre-established variable (the underlying) provided that, in the case of a non-financial variable, the underlying is not specific to a party to the contract;

- it does not require an initial net investment or requires a lower initial net investment than would be required for other types of contracts that would be expected to respond similarly to changes in market factors;
- it is settled at a future date.

b) Financial assets designated at fair value
A financial asset (debt securities and loans) may be designated at fair value upon initial recognition, with the measurement results recognised in the income statement, only when such designation makes it possible to provide better information because it eliminates or considerably reduces inconsistency in the valuation or measurement that would otherwise be caused by measuring assets or liabilities or recognising the associated gains and losses on different bases (accounting mismatch).

c) Other financial assets mandatorily at fair value
Other financial assets that must be measured at fair value represent a residual category and are made up of financial instruments that do not meet the business model or cash flow requirements to be classified as assets designated at amortised cost or at fair value through other comprehensive income. More specifically, these include:

- debt securities, loans held as part of an Other business model, which do not belong to the trading portfolio;
- debt securities, loans or UCIT units for which the contractual terms do not exclusively provide for the repayment of principal and payment of interest on the amount of principal to be repaid (i.e. which do no pass the SPPI test);
- equity instruments not held for trading, for which no use was made of the option of classifying them among the assets designated at fair value through other comprehensive income.

Recognition criteria

Financial assets are initially recognised on the settlement date in case of debt securities, equity instruments and UCITS units, on the disbursement date for loans and on the subscription date for derivative contracts.
Upon their initial recognition, financial assets designated at fair value through profit and loss are recorded at fair value, which generally corresponds to the price paid, excluding transaction costs or revenues directly attributable to the financial instruments, which are recognised in the income statement.

Income item measurement and recognition criteria

Subsequent to initial recognition, financial assets designated at fair value through profit and loss are recorded at fair value, with recognition of changes as a matching balance to the income statement. For derivative instruments, if the fair value of a financial asset becomes negative, that item is accounted for as a financial liability held for trading.

To determine the fair value of financial instruments listed on an active market, market listings at the reporting date are used. In the absence of an active market, estimate methods and valuation models are used that take into account all the risk factors associated with the instruments and that are based on market inputs, such as methods based on the valuation of other listed instruments that are substantially the same, discounted cash flow analysis, option pricing models, and values recognised in recent comparable transactions. In the event that no reliable estimate of the fair value is possible for equity instruments and related derivatives, the cost criterion is used as an estimate of the fair value only on a residual basis and limited to a few cases (non-applicability of the above methods or in the presence of a range of possible fair value valuations, of which cost represents the most significant estimate).
Please refer to "Part A.4 – Fair value disclosure" for details on how fair value is determined.

Trading profits or losses and gains or losses as a result of the valuation of the trading portfolio, including derivatives connected to financial liabilities/assets designed at fair value, are recognised in the income statement in the item "80. Profits (losses) on trading"; the same economic effects associated with financial assets designated at fair value and financial assets that must be measured at fair value are recorded under item "110. Profits (losses) on financial assets and liabilities designated at fair value through profit and loss".

Derecognition criteria

Financial assets are derecognised when the contractual rights to receive the cash flows generated by the assets have expired or when the financial assets are disposed of and all risks and benefits of ownership of the assets have been

substantially transferred. In the event that the substantial transfer of risks and benefits cannot be verified, financial assets are derecognised from the financial statements if control of the assets has been relinquished.
Lastly, sold assets are derecognised if the contractual right to receive the cash flows of the assets is maintained, but at the same time a contractual obligation is assumed to pay these flows to a third party without delay and only to the extent of those received.

For financial assets other than equity instruments, derecognition may also occur following reclassification to the "Financial assets measured at fair value through other comprehensive income" and "Financial assets designated at amortised cost" categories. This reclassification can occur in the very rare circumstance that an entity decides to modify its business model for managing financial assets. The transfer value is represented by the fair value on the date of its reclassification and prospectively from that date. In this instance, the effective interest rate of the reclassified financial asset is determined on the basis of its fair value on the date of reclassification, which is the date of initial recognition for the allocation of the various stages of credit risk (stage assignment) for the purpose of impairment.

2 - Financial assets designated at fair value through other comprehensive income

Classification criteria

This category includes financial assets (debt securities and loans) when both of the following conditions are met:

- the objective of their possession is represented by both the collection of contractual cash flows and their sale (Hold to collect and Sell business model);
- the related contractual flows are represented solely by payments of principal and interest on the capital to be repaid (i.e. that they foresee passing the SPPI test - Solely Payment of Principal and Interest test).

This category also includes equity instruments, not held for trading and not qualifying as investments in subsidiaries, associates and entities under joint control, for which the option of classifying them among financial assets measured at fair value through other comprehensive income is applied. This option may be exercised at the time of initial recognition of the individual financial instrument and is irrevocable.

Recognition criteria

Financial assets are initially recognised on the settlement date for debt securities and equity instruments and on the disbursement date for loans.
Upon their initial recognition, assets are designated at fair value, which generally corresponds to the price paid, including transaction costs or revenues directly attributable to the instruments.

Income item measurement and recognition criteria

Subsequent to initial recognition, assets classified at fair value through other comprehensive income, consisting of debt securities and loans, continue to be measured at fair value, with recognition of the portion of interest in the income statement on the basis of the effective interest rate criterion, exchange rate revaluation effects and expected losses (impairment). Gains and losses deriving from the measurement at fair value are instead recorded in a specific shareholders' equity reserve, which will be recycled in the income statement when the financial asset is derecognised.
Specifically, at each balance sheet or interim reporting date, the aforementioned assets are subject to impairment in order to estimate the expected losses in value relating to credit risk (Expected Credit Losses), based on the impairment model also established for "Financial assets designated at amortised cost". These adjustments are recorded in the income statement under item "130. Net value adjustments/recoveries for credit risk" as a balancing entry to a specific shareholders' equity valuation reserve ("120. Valuation reserves"); the same applies to recoveries of part or all of the write-downs from previous financial years. For more information on the impairment model, please refer to paragraph "16 - Other information, Methods for determining impairment losses on financial assets" below.

Equity instruments that have been classified in this category are designated at fair value; profits and losses from measurement at fair value are recognised with a matching entry in a specific equity reserve. ("120. Valuation reserves"). These reserves will never be recycled in the income statement, even if carried out through the sale of the asset. In this instance, it will be necessary to reclassify them as another shareholders' equity item ("150. Reserves"). Additionally, no write-down loss is recognised on the income statement for these assets, as they are not subject to any impairment process. Dividends collected are the only component recognised in the income statement.

For information about how fair value is determined, please refer to the criteria previously explained for "Financial assets designated at fair value through profit and loss" and the subsequent "Part A.4 – Fair value disclosure".

Derecognition criteria

Financial assets are derecognised when the contractual rights to receive the cash flows generated by the assets have expired or when the financial assets are disposed of and all risks and benefits of ownership of the assets have been substantially transferred. In the event that the substantial transfer of risks and benefits cannot be verified, financial assets are derecognised from the financial statements if control of the assets has been relinquished.
Lastly,sold assets are derecognised if the contractual right to receive the cash flows of the assets is maintained, but at the same time a contractual obligation is assumed to pay these flows to a third party without delay and only to the extent of those received.

For financial assets other than equity instruments, derecognition may also occur following reclassification to the "Financial assets designated at fair value through profit and loss" and "Financial assets designated at amortised cost" categories. This reclassification can occur in the very rare circumstance that an entity decides to modify its business model for managing financial assets. The transfer value is represented by the fair value on the date of its reclassification and prospectively from that date.
In the event of a reclassification to "Financial assets designated at amortised cost", the cumulative profit or loss in the valuation reserve is eliminated as a balancing entry to an adjustment to the fair value of the financial asset at the reclassification date.
In the event of reclassification under "Financial assets designated at fair value through profit and loss", the cumulative profit or loss in the valuation reserve is reclassified from shareholders' equity to the income statement.

3 - Financial assets designated at amortised cost

Classification criteria

This category includes financial assets (loans and debt securities) when both of the following conditions are met:
- the objective of their possession is to collect contractual cash flows (Hold to Collect business model);
- the related contractual flows are represented solely by payments of principal and interest on the capital to be repaid (i.e. that they foresee passing the SPPI test).

Specifically, it includes loans granted to customers and banks—in any form—and debt securities that meet the requirements described in the paragraph above.
Loans originated through financial leases are also included in this item, in line with IAS 17, and are recognised according to the "financial method", including values associated with assets waiting to be granted under financial lease, including real estate under construction.
Also included are repurchase agreements with the obligation to sell securities at a future date and "securities lending" transactions with a cash guarantee deposit which is fully available to the lender, for the spot amount paid, if the characteristics of these transactions do not entail recognition in the proprietary portfolio of the security being carried over or lent, since no risk or benefit has been acquired from them.
Lastly, this category also includes operating receivables connected with the provision of financial services as defined in the Consolidated Banking Law and in the Consolidated Finance Law.

Recognition criteria

Financial assets are initially recognised on the settlement date for debt securities and on the date of disbursement for loans. Upon their initial recognition, financial assets classified in this category are designated at fair value, which generally corresponds to the price paid, including any transaction costs or revenues directly attributable to the instrument.

Specifically, loans are initially recognised on the disbursement date based on the fair value of the financial instrument. Recognition is usually equal to the amount disbursed or the subscription price, including costs/income directly associated with the individual loan and that can be determined from the start of the transaction, although settled at a later time. Costs are excluded that, although having the above characteristics, are repaid by the borrowing counterparty or fall under normal internal administrative costs.

If the date on which the credit contract is signed and the date on which the funds are disbursed are not the same, a commitment to disburse funds is recognised, which will be closed out upon the effective disbursement of the loan.

Income item measurement and recognition criteria

After initial recognition, the financial assets in question are measured at amortised cost, equal to the initial recognition value decreased by repayments of principal, decreased/increased by the amortisation—calculated according to the effective interest rate method—of the difference between the amount disbursed and the amount repayable at maturity, typically comparable to the costs/income directly associated to the individual loan.
The effective interest rate is determined by calculating the rate that equates the asset's present value of future principal and interest cash flows to the amount disbursed, including costs/income associated with the asset. The estimate of cash flows must consider all contractual provisions which could influence the amounts and maturities, without considering the expected loss on the asset. This accounting method, based on financial logic, spreads the economic effect, throughout the residual life of the asset, of all transaction costs, commissions, bonuses or discounts considered an integral part of the effective interest rate method. The amortised cost method is not used for short-term assets whose limited life span makes the application of discounting immaterial. Such assets are measured at historical cost, and any costs/income are recognised in the income statement on a straight-line basis throughout the loan contract life. The same measurement criterion is used for assets without a defined maturity or demand loans.

The book value of the financial assets designated at amortised cost is adjusted to account for any provisions on expected losses. At each balance sheet date or interim reporting date, the aforementioned assets are subject to impairment to estimate the expected value loses associated with credit risk (ECL - Expected Credit Losses). These losses are recognised in the income statement under item "130. Net losses/recoveries for credit risk".

More specifically, the impairment model provides for the classification of assets into three distinct stages (Stage 1, Stage 2, Stage 3), based on changes to the debtor's creditworthiness, corresponding to different criteria for measuring expected losses:

- Stage 1 includes performing financial assets for which there has been no significant deterioration in credit risk since the date of initial recognition or for which the credit risk is considered low. Impairment is based on an estimate of the expected loss over one year (expected loss resulting from possible default on the financial asset within one year from the reference date);
- Stage 2 includes performing financial assets that have undergone significant impairment of credit risk with respect to the initial recognition. Impairment is proportional to the estimate of expected loss over the entire residual life of the financial asset;
- Stage 3 includes non-performing financial assets (100% default probability), measured by estimating the expected loss over the entire life of the instrument.

For performing assets, expected losses are determined using a collective process based on certain risk parameters, namely the Default Probability (DP), the Loss Given Default (LGD) and the Exposure at Default (EAD), deriving from internal models for calculating regulatory credit risk that are suitably adjusted to account for the specific requirements set out in accounting regulations.

Non-performing assets, i.e. assets for which, in addition to a significant increase in credit risk, there is objective evidence of impairment, are measured with an analytical or lump-sum measurement process based on uniform risk categories, designed to establish the current value of expected future recoverable cash flows, discounted on the basis of the original effective interest rate.
Non-performing assets include exposures to which the status of bad loan, probable default or past-due accounts/debts in excess of ninety days has been attributed in accordance with the definitions established by the supervisory provisions in force (Bank of Italy Circular no. 272 "Matrix of accounts") and referred to by Bank of Italy Circular no. 262 "Matrix of Accounts", as they are considered to be consistent with the IFRS 9 accounting standard for objective evidence of impairment.

Expected cash flows consider expected recovery times and the estimated net realisable value of any guarantees.
For fixed rate positions, the original effective rate used to discount the expected recovery flows, determined as illustrated above, remains unchanged over time, even if there is a change in the contractual rate due to financial difficulties of the debtor.
For loans with variable interest rates, the rate used for discounting cash flows is updated in relation to the indexing parameters (Euribor, for example), while on the other hand, the originally established spread is kept constant.

The original value of financial assets is reinstated in subsequent years, due to an improvement in the credit quality of the exposure compared to that which had led to the previous write-down. Recoveries are recognised in the income statement and cannot exceed the asset's amortised cost had no adjustments been carried out in the past.
For more information on the impairment model, please refer to paragraph "16 - Other information, Methods for determining impairment losses on financial assets" below.

For non-performing loans, accrued interest is calculated on the basis of amortised cost, based on the exposure—determined using the effective interest rate—adjusted for expected losses. For non-performing loans that do not accrue contractual interest, such as bad loans, this interest corresponds to the reversals of the impairment losses related to discounting the recovery forecasts due to the simple passing of time.

Derecognition criteria

Financial assets are derecognised when the contractual rights to receive the cash flows generated by the assets have expired or when the financial assets are disposed of and all risks and benefits of ownership of the assets have been substantially transferred. In the event that the substantial transfer of risks and benefits cannot be verified, financial assets are derecognised from the financial statements if control of the assets has been relinquished.
Lastly, sold assets are derecognised if the contractual right to receive the cash flows of the assets is maintained, but at the same time a contractual obligation is assumed to pay these flows to a third party without delay and only to the extent of those received.

The derecognition of impaired financial assets may occur upon recognising that the exposure is irrecoverable and the consequent conclusion of the recovery process (final derecognition) and involves a reduction in the nominal and gross book value of the loan. This is the case where settlement agreements with the debtor result in a reduced loan amount (in full and final settlement) or in specific situations, for example:

- the final judgment declaring that part or all of the loan has been extinguished;
- the conclusion of insolvency or enforcement proceedings against the principal debtor and the guarantors;
- the conclusion of all possible judicial and extra-judicial means for recovering the debt;
- the completion of a mortgage restriction on an asset as collateral, with the consequent derecognition of the credit guaranteed by the restricted mortgage, in the absence of additional specific guarantees or other actions that may be taken to recover the exposure.

These specific situations may lead to the total or partial derecognition of the exposure, yet do not necessarily entail waiving the legal right to recover the debt.

In addition, non-performing financial assets may be derecognised by writing them off after acknowledging that no reasonable expectations of their recovery exist, even while continuing with actions aimed at their recovery. Such write-off shall be made during the financial year in which the debt or part of it is deemed irrecoverable—even while legal proceedings are under way—and may occur before the legal debt recovery proceedings against the debtor and the guarantors have come to a close. This does not imply a waiver of the legal right to recover the loan and is carried out when the credit documentation contains reasonable financial information indicating that the debtor is unable to repay the debt. In this instance, the nominal gross value of the loan remains unchanged, but the gross book value is reduced by an amount equal to the amount written off, which may be related to the entire exposure or to a portion of it. The amount written off cannot be subject to subsequent recoveries in impairment losses, following an improvement in the recovery forecasts, but only after the amount is actually collected.

Lastly, the derecognition of the financial assets in question may also occur following their reclassification into the categories "Financial assets measured at fair value through other comprehensive income" and "Financial assets designated at fair value through profit and loss". This reclassification can occur in the very rare circumstance that an entity decides to modify its business model for managing financial assets. The transfer value is represented by the fair value on the date of its reclassification and prospectively from that date. Gains or losses resulting from the difference between the amortised cost of the financial asset and its fair value are recognised:

- in the income statement, in the event of reclassification under "Financial assets designated at fair value through profit and loss";
- in shareholders' equity to a specific valuation reserve, in the event of reclassification to "Financial assets measured at fair value through other comprehensive income".

4 - Hedging transactions

It should be noted that Gruppo Banco BPM avails itself of the IFRS 9 option to continue to fully apply the hedge accounting rules set forth by IAS 39, in the version approved by the European Commission (the carved out version).

Classification criteria

Asset and liability items include financial hedging derivatives, which, at the date of the financial statements or interim report, showed a positive and negative fair value respectively.

Hedges seek to neutralise potential losses attributed to a specific risk recognisable on a given financial instrument or a group of financial instruments by offsetting them with the gains recognisable on a different financial instrument or group of financial instruments in the event that the risk should actually materialise.
The following types of hedges are provided:

- fair value hedges, which seek to hedge exposure to changes in the fair value, attributable to a specific risk, of a financial statement asset or liability. It is also possible to activate macro fair value hedging, with the goal of reducing fair value fluctuations, attributable to interest rate risk, of monetary amounts deriving from a portfolio of financial assets and liabilities (including core deposits). Net amounts deriving from the mismatch of assets and liabilities cannot be subject to macro hedging;
- cash flow hedges, which seek to hedge the exposure to changes in future cash flows attributable to specific risks associated with financial statement items or a highly likely expected transaction;
- hedges of foreign currency transactions, which seek to hedge the risks of investment in a foreign company expressed in a currency other than the Group's reference currency (euro).

At the level of the consolidated financial statements, only derivatives entered into with an external counterparty to the Group may be designated as hedging instruments. The results associated with internal transactions carried out between various Group entities are eliminated.

Derivatives can be designated as hedges, provided that the hedging relationship between the hedged instrument and the hedging instruments is formally documented and it is effective at the time the hedge is originated and prospectively throughout its entire life. The hedge's effectiveness depends on the extent to which the changes in the fair value or in the expected cash flows of the hedged instrument are actually offset by those of the hedging instrument. Therefore, effectiveness is measured by comparing such changes, while considering the aim pursued by the company when the hedge was established.
A hedge is effective (within the limits established as a range of 80% to 125%) when changes in the fair value (or in the cash flows) of the hedging instrument almost completely neutralise the changes in the hedged instrument attributable to the hedged risk. Hedging effectiveness is assessed at each balance sheet date or interim reporting date using:

- prospective tests justifying the application of hedging accounting, in that they demonstrate its expected effectiveness;
- retrospective tests demonstrating the hedge's actual effectiveness achieved over the period being examined. In other words, these tests measure how far the actual results deviate from perfect hedging.

Recognition criteria

Derivative hedging instruments are recognised at fair value at the date on which the relative contracts are entered into.

Income item measurement and recognition criteria

Subsequent to the initial recognition, hedging derivatives continue to be designated at fair value. In particular:

- for fair value hedges, the changes in fair value of the hedged element are offset by the changes in fair value of the hedging instrument. Such offsetting is recognised by charging the changes in value, referring both to the hedged element (referring to the changes generated by the underlying risk factor) as well as to the hedging instrument, to the income statement, in item "90. Fair value adjustments in hedge accounting". Any resulting difference, which represents the partial ineffectiveness of the hedge, represents the net effect on the income statement. If the hedging relationship ends, the hedged instrument reacquires the original measurement approach of the class to which it belonged; for instruments measured at amortised cost, the cumulative revaluations/write-downs recognised as a result of changes in fair value of the hedged risk are recognised in the income statement under interest income and expense throughout the residual life of the hedged item, on the basis of the effective interest rate. If the hedged item is sold or repaid, the share of fair value not yet amortised is recognised immediately in the income statement;
- for cash flow hedges, the portion of changes in the fair value of the derivative determined to be an effective hedge is recognised directly at equity (item "120. Valuation reserves"), while it is recognised through profit and loss only when changes in cash flows to be offset arise in the hedged item. The portion of gains or losses of the hedging instrument considered ineffective is charged to the income statement (item "90. Fair value adjustments in hedge accounting"). This portion is equal to any difference between the cumulative fair value of the hedging instrument and the cumulative fair value of the hedged instrument. In any event, the fluctuations in fair value of the hedged item and the related hedge must lie within the 80%-125% range. If the cash flow hedge is no longer considered effective or the hedging relationship is terminated, the total amount of profits or losses on the hedging instrument, previously recognised in "Valuation reserves", is recognised in the income statement only when the hedged transaction will take place or when it is no longer deemed possible that the transaction will take place; in this last circumstance, the profits or losses are transferred from the shareholders' equity item to the income statement item "90. Fair value adjustments in hedge accounting";
- hedges of investments in foreign currency are accounted for using the same method as for cash flow hedges.

Derecognition criteria

Should the above tests fail to confirm the effectiveness of the hedging, both retrospectively and prospectively, hedge accounting, as described above, is discontinued. In this case, the hedging derivative contract is reclassified under "Financial assets designated at fair value through profit and loss" and, specifically, under "Financial assets held for trading".
Additionally, the hedging relationship stops when:

- the derivative expires, is discharged or exercised;
- the hedged item is sold, expires or is repaid;
- it is no longer highly likely that the future hedged transaction will be carried out.

5 - Investments in associates and companies subject to joint control

Classification criteria

This item includes investments in associates or companies subject to joint control, which are carried at equity.
Associates are non-subsidiary companies upon which the Group has a significant influence. The company exercises a significant influence in all cases where it holds 20% or more of voting rights in the investee, and irrespective of the shareholding percentage, whenever it has the power to participate in investee business and financial decisions by virtue of specific legal relations, such as shareholders' agreements, the purpose of which is to ensure that the members of the agreement are represented in the management bodies and to safeguard a consistent management approach without controlling it.
Companies subject to joint control are enterprises where the joint control is based on a contract or other agreement whereby it is necessary to obtain the unanimous consensus of all the parties sharing the control to make strategic financial and operating decisions. This takes place when the voting rights and control over investee economic activity are shared jointly by Banco BPM and another party. In addition, an equity investment is qualified as under

joint control when, even though voting rights are not shared jointly, the unanimous consent of all parties sharing control is required to make decisions regarding significant activities.

Recognition criteria

Financial assets are initially recognised on the settlement date. Upon their initial recognition, financial assets classified in this category are carried at cost, including any goodwill paid for at the time of acquisition, which, therefore, is not independently or separately recorded.

Income item measurement and recognition criteria

The book value is subsequently increased or decreased to reflect the share of profit or loss of the investees attributable to the Group generated after the acquisition date, as a matching entry to the consolidated income statement item "250. Profits (losses) on investments in associates and companies subject to joint control". Dividends received from an investee are deducted from the investee's book value.
Should it be necessary to carry out adjustments due to changes in the investee's shareholders' equity that have not been recognised in the investee's income statement (for example, as a result of the designation at fair value of "Financial assets designated at fair value through other comprehensive income", as a result of the valuation of actuarial gains/losses on defined benefit plans), the share of the above changes attributable to the Group is recognised directly in the shareholders' equity item "120. Valuation reserves".
When applying the equity approach, the most recent available financial statements of the associated company or company subject to joint control are used, suitably adjusted to take into account any significant events or transactions that have taken place between the investee company's last available financial statements and the reference date of the consolidated financial statements. If the investee company adopts accounting standards that are different than the Group's, changes are made to the investee's financial statements.

After applying the equity approach, investments in associates or jointly controlled entities are tested for impairment when there is objective evidence of impairment that could have an impact on the investee's cash flows and consequently on the recoverability of the book value of the investment.
The process of recognising any impairment, therefore, involves checking for possible indicators that are considered to show objective evidence of impairment, such as:

- significant financial difficulties of the investee company (for example, significant negative changes in the book value of shareholders' equity, reduction or interruption of the distribution of dividends, achievement of operating results below a physiological threshold, compared to the objectives of the budget or the long-term plan or down compared to previous years or compared to the situation that existed on the acquisition date of the investment);
- breach of contract, for example the investee's default or failure to make payment;
- the extension of allowances for economic or legal reasons relating to the financial difficulties of the investee, which otherwise would not have been taken into consideration;
- the announcement or notice of a financial restructuring plan or the existence of a high probability that the investee may announce restructuring operations or may be declared bankrupt;
- the disappearance of an active market relating to the investment held due to the financial difficulties of the investee;
- significant changes that adversely affect the investment in the technological, market, economic or legal environment in which the investee operates;
- a significant or prolonged decrease in fair value below cost. The Group considers a fall in fair value of over 30% below the purchase cost to be a significant decrease. The Group considers a continuous decrease in fair value for an uninterrupted period of more than 24 months to be a prolonged decrease.

If there is evidence that the value of an equity investment may have decreased, its recoverable value is estimated, which is the higher of its fair value, net of selling costs, and its value in use. Value in use is determined by discounting future cash flows that the investment will generate, including the final disposal value of the investment. An impairment loss is recognised in the income statement when the book value, including goodwill, is lower than the recoverable amount. If the reasons for an impairment loss cease to apply due to an event that occurs after the impairment was recognised, write-backs are recognised in the income statement up to the amount of the impairment loss previously recognised.

Derecognition criteria

Investments in associates and companies subject to joint control are derecognised when there is a disposal in which all of the associated risks and rewards have been substantially transferred.
If there is a situation resulting in the loss of significant influence or joint control, any remaining equity investment is reclassified to the portfolios of IAS 9 financial assets, normally that of "Financial assets designated at fair value through other comprehensive income", on the basis of the relative fair value. Derecognition from the item "Investments in associates and companies subject to joint control" may also take place if there are circumstances causing control to be obtained (step acquisitions). For more information please refer to paragraph 16 below entitled "Other information, Business combinations, goodwill and changes in interest holdings".

6 - Property and equipment

Classification criteria

Property and equipment include land, operating property, works of art, real estate investments, technical plants, furniture, fittings and equipment of any type. More specifically:

- assets held for use in the production or supply of goods and services are classified as "property and equipment used in operations" and recognised in accordance with IAS 16;
- property held for rental to third parties or for capital appreciation through sale is classified as "property and equipment held for investment" and follows the rules set out in IAS 40;
- property held to enhance the value of the investment through renovation or requalification for its subsequent sale is classified as inventories and follows the rules of IAS 2.

Property and equipment also include assets related to finance lease contracts which returned to the company's ownership following the termination of the contracts and the concurrent closure of the original credit position. This item also includes assets used under finance lease contracts, provided that the legal ownership of the assets rests within the leasing company.
This item also includes leasehold improvements and incremental expenses incurred on third party assets, whenever they are identifiable and distinguishable tangible assets. More specifically, these are costs to renovate rented property, sustained to render them suitable for their intended use. These costs are classified in the specific category to which they refer (e.g. technical plant, equipment).

Recognition criteria

Property and equipment are initially carried at cost, which includes the purchase price and all accessory charges directly attributable to the acquisition of the asset and bringing it to working conditions. Extraordinary maintenance costs which entail an increase in future economic benefits are included in the asset's book value, while other ordinary maintenance costs are charged to the income statement.
Property withdrawn following the closure of the original credit position (*datio in solutum* - transfer in lieu of payment) will be recognised at the lower of the gross loan value recognised at the time of withdrawal of the asset, and:

- the "market value" deriving from a specific appraisal, if the property is not expected to be classified under "non-current assets and asset disposal groups held for sale" within a short time;
- the "immediate sale value" deriving from a specific appraisal, which adjusts the market value for prospective sale in the very short term, when it is known at the termination date that the property will be subsequently allocated under "non-current assets and asset disposal groups held for sale";
- the price during trading, if on initial recognition concrete negotiations for sale are in course, demonstrated by commitments undertaken by the interested parties to the negotiations.

Income item measurement and recognition criteria

Subsequent to initial recognition, property and equipment, with the exception of those covered by the IAS 2 standard, are carried at cost, less any depreciation and impairment.

Property and equipment are systematically depreciated throughout their useful life, using the straight-line method, with the exception of:

- land, whether purchased separately or as part of the value of the buildings standing on it, in that land has an unlimited life. If its value is embedded in the value of the buildings built on it, in virtue of the application of the component approach, land is considered a separate asset from the building. At the acquisition date, the separation of the value of the land and the value of the building is based on appraisals by independent experts;
- works of art, because the useful life of a masterpiece cannot be estimated and its value normally is destined to increase with time.

At each balance sheet or interim reporting date, if there is any indication that an asset may be impaired, the asset's book value is compared with its recoverable amount, that is, equal to the higher of the asset's fair value, net of costs to sell, and its value in use, understood as the present value of future cash flows originated by the asset. Any adjustments are charged to the income statement. Whenever the reasons for the impairment loss are no longer valid, recoveries are recognised, which must not exceed the asset's value had no impairment taken place in the past, net of accrued depreciation.

Property and equipment recognised in accordance with IAS 2 are designated at the lower of the book value and net realisable value, which is the estimated sale price less estimated completion costs and other costs necessary to make the sale.

Derecognition criteria

Property and equipment is derecognised from the balance sheet at the time of disposal or when the asset is permanently withdrawn from use and no future economic benefits are expected from its disposal. Capital gains and losses deriving from the liquidation or disposal of property and equipment are calculated as the difference between the net sale consideration and the book value of the asset and are recognised in the income statement on the day of derecognition.

7 - Intangible assets

Classification criteria

Intangible assets are non-monetary, identifiable and non-physical assets originating from legal or contractual rights owned to be used on a long-term basis and which are likely to generate future economic benefits. Intangible assets also include goodwill, which is the difference between the price paid for a business combination and the fair value of the net identifiable assets purchased, as illustrated in greater detail in paragraph "16 – Other information, Business combinations, goodwill and changes in interest holdings".

Recognition criteria

Intangible assets are carried at cost, adjusted to account for accessory charges, only if it is likely that the future economic benefits attributable to the asset will be realised, and if the cost of the asset can be reliably determined. Otherwise, the cost of the intangible asset is recognised in the income statement during the year it was incurred.

Income item measurement and recognition criteria

The cost of intangible assets, with definite useful life, is amortised on a straight-line basis over their useful life. If the useful life is undefined, no amortisation is carried out, only periodic assessments of the adequacy of the book value. At each balance sheet date or interim reporting date, if there is evidence of impairment, the asset's recoverable amount is estimated. The amount of the loss, recognised in the income statement, is equal to the difference between the asset's book value and recoverable value.
Intangible assets include software, intangible assets linked to the valuation of client relationships or the valuation of trademarks recognised during business combinations.

Goodwill is not amortised, but must be regularly tested for impairment to verify the adequacy of its book value. Specifically, goodwill must be tested any time there is evidence of impairment and at least once a year. To this end, the cash-generating unit to which the goodwill is allocated is identified. This unit represents the lowest level at which goodwill is monitored for internal management purposes and should not be larger than the operating segment determined in compliance with IFRS 8.
The amount of any impairment is determined based on the difference between the book value of the goodwill and its recoverable amount, if lower. This recoverable amount is equal to the larger of the fair value of the cash-generating unit, net of costs to sell, and its value in use. The value in use is the present value of future cash flows expected from cash-generating units to which goodwill was allocated. The resulting adjustments are charged to the income statement.
No subsequent recoveries can be recognised.

Derecognition criteria

Intangible assets are derecognised from the balance sheet at the time of disposal or when future economic benefits are no longer expected.

8 - Non-current assets and asset disposal groups held for sale

Classification criteria

Non-current assets/liabilities and asset/liability groups are classified under the asset item "Non-current assets and asset disposal groups held for sale"—and under the liability item "Liabilities associated with non-current assets and asset disposal groups held for sale"—for which their book value will presumably be recovered through sale rather than continuous use.
In order to be classified under the above items, the assets or liabilities (or discontinuation group) must be immediately available for sale, and there must be active and concrete programmes which show that their disposal within the short term is highly probable.

Income item measurement and recognition criteria

After they are classified in the above-mentioned category, these assets are designated at the lower of the book value and their fair value, net of costs to sell, with the exception of certain types of assets—such as all financial instruments falling within the scope of IFRS 9—for which the valuation criteria of the reference accounting standard must continue to be applied.
If the non-current assets held for sale can be amortised/depreciated, the amortisation/depreciation process ceases from the year the assets are classified under non-current assets held for.
Expenses and income attributable to assets and liabilities associated with disposal groups are shown in the income statement under item "320. Profit (loss) from discontinued operations", net of taxes, while those relating to individual non-current assets held for sale are recorded under the most appropriate income statement item.

Derecognition criteria

Non-current assets and asset disposal groups held for sale are derecognised from the balance sheet upon disposal.

9 - Current and deferred taxation

These items include current and deferred tax assets, and current and deferred tax liabilities relating to income taxes.

Income taxes, calculated in compliance with current tax regulations, are accounted for based on the accrual principle, consistent with the recognition of the costs and revenues that generated the taxes in the financial statements. Therefore, this represents the tax charge, equal to the balance of current taxes and deferred tax assets and liabilities, relating to the income for the year. Income taxes are charged to the income statement, with the exception of those relating to items charged or credited directly to shareholders' equity, as they as well are consistently recognised directly through shareholders' equity.

In particular, current tax liabilities (assets) for the current and previous years reflect the amount of income taxes that are expected to be paid/recovered to/from the tax authorities, based on a prudent estimate, applying the tax rates and tax regulations in force at the reporting date (interim reporting). Current tax assets and liabilities are shown as a net balance in the balance sheet, in case the settlement is executed based on the net balance, owing to the existence of a legal right to offsetting.

Deferred tax assets and liabilities are calculated based on temporary differences arising between the tax values of the individual assets and liabilities and their book values, without any time limits.
Deferred tax assets are recognised in the financial statements or the interim reports when it is likely that they can be recovered, which is assessed based on the ability of the company concerned and of the Group, as a result of the "tax consolidation" scheme, to continue to generate positive taxable income in future financial years, also taking account of the tax provisions in force at all times, such as Law no. 214/2011, which permits the transformation of certain deferred tax assets meeting specific conditions into credits. Deferred tax liabilities are recognised in the financial statements or interim reports, with the sole exceptions of assets recognised in the financial statements at an amount higher than the value recognised for tax purposes and of reserves subject to tax on distribution, where it is reasonable to believe that no operations will be performed deliberately that would trigger taxation.
Recognised deferred tax assets and liabilities are systematically measured to account for any changes in regulations or tax rates, as well as for any changes in the subjective positions of the Group companies.

10 - Provisions for risks and charges

Provisions for risks and charges: guarantees given and commitments
The sub-item in question includes provisions for credit risk for commitments to disburse the funds and guarantees given, which are subject to impairment rules pursuant to IFRS 9, as is the case for "Financial assets designated at amortised cost" and "Financial assets measured at fair value through other comprehensive income". For more information on the impairment model, please refer to paragraph "16 - Other information, Methods for determining impairment losses on financial assets" below.
In addition, this sub-item also includes provisions for risks and charges established for other types of commitments and guarantees given that, because of their specific characteristics, do not fall within the scope of impairment pursuant to IFRS 9.

Provisions for risks and charges: retirement benefits and similar commitments
As explained in the paragraph below "16 - Other information, Employee termination indemnities and other employee benefits", the sub-item "company retirement plans and similar obligations" includes defined-benefit plans, namely pension funds backed by a capital repayment and/or return guarantee in favour of beneficiaries. Benefits to be paid in the future are measured by an external actuary, using the "projected unit credit method", as required by IAS 19.
Actuarial gains and losses, defined as the difference between the book value of the liability and the present value of the commitments at the end of the period, are accounted for in full to shareholders' equity under the item "Valuation reserves".

Provisions for risks and charges: other provisions for risks and charges
The sub-item "Other provisions for risks and charges" includes allocations recognised for estimated outlays for legal or implicit obligations deriving from past events. These outlays may be contractual in nature, such as allocations for incentive system for staff, early retirement incentives, indemnity required under contractual clauses when specific events take place, or for compensation and/or restitution, such as those against possible losses on lawsuits, including clawback actions, estimated outlays for customer complaints regarding securities brokerage and tax disputes.

Provisions for risks and charges consist of liabilities whose amount or expiry are uncertain and are recognised in the financial statements only if:
- there is a current obligation (legal or implicit) as a result of a past event;
- it is likely that an outflow of resources will be required to produce economic benefits to settle the obligation;
- the amount of the probable future outflow can be reliably estimated.

The amount of the provision recognised represents the best estimate of the financial outlay required to meet the obligation existing at the reporting date and reflects the risks and uncertainties inherent in the facts and circumstances under examination. Whenever the time factor is significant, provisions are discounted using current market rates. The provision and the effect of discounting are recognised in the income statement under item "200. Net provisions for risks and charges", as well as the increase in the provision due to the passage of time.
The provisions allocated are re-examined at each date of the financial statements and adjusted to reflect the best current estimate. When the outflow of resources to produce economic benefits to settle the obligation is unlikely, the allocation is reversed.
In addition, each provision must be used to pay for outlays for which the provision itself had been originally set aside.

11 - Financial liabilities measured at amortised cost

Classification criteria

"Financial liabilities measured at amortised cost" include the sub-items "Due to banks", "Due to customers" and "Debt securities issued" and consist of various forms of interbank and customer loans and funding carried out through certificates of deposit and bonds outstanding.
These also include loans recorded by lessees as part of financial leases, as well as funding repurchase agreements and securities lent against collateral in cash, to which the lender has full access. Also included are operating payables connected with the provision of financial services as defined in the Consolidated Banking Law and in the Consolidated Finance Law.

Recognition criteria

These liabilities are initially recognised when the amounts collected are received or the debt securities are issued and are carried out on the basis of their fair value, which is generally equal to the amount received or the issue price, increased by any additional costs/income directly attributable to the individual funding or issue transaction and not paid back by the lending counterparty. Internal administrative costs are excluded.
Repurchase agreements with the obligation to repurchase are recognised as funding transactions for the spot amount paid.

Income item measurement and recognition criteria

Subsequent to initial recognition, the financial liabilities that emerged, net of any redemptions and/or repurchase, are measured at amortised cost, using the effective interest rate method. Short-term liabilities are an exception, if the time factor is immaterial. These are stated at their received value, and any incurred costs are charged to the income statement on a straight-line basis over the contractual life of the liability. Moreover, funding instruments under an effective hedge are measured based on the standards established for hedging transactions.

For structured instruments that incorporate an embedded derivative—in accordance with IFRS 9 and illustrated in the previous item "Financial assets held for trading"—the embedded derivative is separated out from the host contract. In that instance:
- the embedded derivative is classified as an asset or liability held for trading and is measured at fair value;
- the host contract is classified under liabilities valued at amortised cost.

Derecognition criteria

Financial liabilities are derecognised from the financial statements or interim reports when expired or cancelled. Derecognition also takes place in the event of repurchases of securities issued. The difference between the book value of liabilities and the purchase price paid is recorded in the income statement. The subsequent placement of own securities following their repurchase is accounted for as a new issue, recognised at the new placement price, with no effects on the income statement.

12 - Financial liabilities held for trading

Classification criteria

The item in question includes:
- financial liabilities issued with the intention of repurchasing them in the short term;
- liabilities that are part of a portfolio of financial instruments that are managed together and for which there is a proven short-term profit strategy;
- derivative contracts with a negative fair value and not designated as hedging instruments, including those linked to assets or liabilities designated at fair value through profit or loss and embedded derivatives separated out from liabilities valued at amortised cost.

Also included are liabilities arising from technical overdrafts generated by trading in securities and own certificate issues.

Recognition criteria

Financial liabilities held for trading are initially recognised on the settlement date for cash liabilities and on the subscription date for derivative contracts.
Initial recognition is based on the fair value of liabilities, which generally corresponds to the collected amount, excluding transaction costs or income directly associated with the instruments, which are directly charged to the income statement.
Please refer to "Part A.4 – Fair value disclosure" for details on how fair value is determined.

Income item measurement and recognition criteria

Gains and losses from changes in fair value and/or from the sale of trading instruments are recognised in the income statement. For derivative instruments, if the fair value of a financial liability becomes positive, that item is accounted for under "Financial assets designated at fair value through profit and loss: a) financial assets held for trading".
Trading profits or losses and gains or losses as a result of the valuation of the trading portfolio are recognized in income in the item "80. Profits (losses) on trading".

Derecognition criteria

Financial liabilities held for trading are derecognised when the contractual rights to the relative cash flows expire or when the financial liability is transferred, with the substantial transfer of all risks and benefits arising from its ownership.

13 - Financial liabilities designated at fair value

Classification criteria

On initial recognition, financial liabilities are designated at fair value through profit and loss only if the following circumstances exist:
- it eliminates or considerably reduces the inconsistency in valuation which would otherwise be caused by measuring assets or liabilities or recognising the associated gains and losses on different bases ("accounting mismatch");
- a group of financial assets, financial liabilities or both is managed, and its performance designated at fair value according to a documented risk management or investment strategy, documented internally by executives with strategic responsibilities;
- there is a hybrid contract containing one or more embedded derivatives, and the embedded derivative significantly changes the cash flows which would otherwise be expected from the contract.

The option to designate a liability at fair value is irrevocable and is made on the individual financial instrument and does not require the same application to all instruments with similar characteristics. However, it is not possible to

designate at fair value only one part of a financial instrument attributable to a single risk component to which the instrument is subject.
For more details on the scope of Group liabilities under the fair value option and the method used to determine fair value and quantify its creditworthiness, please refer to paragraph "16 – Other information, Financial liabilities designated at fair value through profit and loss and determination of own creditworthiness", and the subsequent "Part A.4 - Fair value disclosure".

Recognition criteria

The financial liabilities in question are designated at fair value from initial recognition. Initial income and expenses are immediately charged to the income statement.

Income item measurement and recognition criteria

Subsequent to initial recognition, financial liabilities are measured at their current fair value. The change in fair value is recognised in the income statement, with the exception of the effects resulting from changes in own credit risk, which are recognised in a specific valuation reserve (item "120. Valuation reserve"), unless this treatment creates or amplifies an accounting mismatch in the income statement. An accounting mismatch is created or amplified when the recognition of the effects of own credit risk in an equity reserve entails a more significant mismatch in the income statement than what would arise from recognising the entire change in fair value of the liability in the income statement. In this last case, the entire change in fair value of the liability, including the effect of the change in own credit risk, must be recognised in the income statement.
The effects correlated with the change in own credit risk are presented in the statement of comprehensive income, net of the relative tax effect, under other comprehensive income without reclassification to profit or loss.
The amount recognised in the specific shareholders' equity reserve (item "120. Valuation reserves") will never be reversed in the income statement, even if the liability should have expired or been extinguished. In this instance, it will be necessary to reclassify the cumulative income (loss) in the specific valuation reserve to another item of shareholders' equity ("150. Reserves")

Derecognition criteria

Financial liabilities are derecognised from the financial statements or interim reports when expired or cancelled. For financial liabilities represented by securities issued, derecognition is carried out also in case of repurchase. The difference between the book value of the liability and the purchase price is recorded in the income statement, with the exception of profits/losses connected to the change in own credit risk, which are recorded in a shareholders' equity reserve, as described above. The subsequent placement of own securities following their repurchase is considered as a new issue, recognised at the new placement price, with no effects on the income statement.

14 - Foreign currency transactions

Classification criteria

Assets and liabilities in foreign currency include those denominated explicitly in a currency other than the euro, as well as those which establish financial indexing clauses linked to the exchange rate between the euro and a specific currency or a specific basket of currencies.

To determine the conversion procedures to be used, assets and liabilities in foreign currency are broken down between monetary and non-monetary items.

Monetary elements consist of sums in cash and assets and liabilities expressing the right to receive or the obligation to pay fixed or determinable amounts in cash (receivables, debt securities, financial liabilities). Non-monetary elements (such as equity instruments) are assets or liabilities that do not contemplate the right to receive or the obligation to pay fixed or determinable amounts in cash.

Recognition criteria

Upon initial recognition, foreign currency transactions are recorded in the functional currency, and the exchange rate applied to the amount expressed in foreign currency is the one in effect at the date of the transaction.

Income item measurement and recognition criteria

At each balance sheet date or interim reporting date, items expressed in foreign currencies are measured as follows:
- cash items are translated at the exchange rate in effect at the closing date;
- non-cash items carried at their historical cost are translated at the exchange rate in effect at the transaction date;
- non-cash items designated at fair value are converted at the exchange rate in effect at the closing date.

Exchange rate differences originated by the settlement of cash items or by the translation of cash items at rates other than the initial ones or by the conversion of the previous financial statements are charged to the income statement at the time they arise.

When a gain or loss from a non-cash item is carried at equity, the relevant exchange rate difference is also carried at equity. Conversely, when a gain or loss on a non-monetary element is recognised in the income statement, the associated exchange rate difference is also recognised in the income statement.

For information about the conversion of the financial statements of foreign subsidiaries that use a currency other than the reference currency of the Group's Parent Company (euro), please refer to "Accounting policies - Scope of consolidation and methods", contained in "A.1 - General part".

15 - Insurance assets and liabilities

No insurance companies are included in the scope of consolidation.

16 - Other information

a) Contents of other financial statement items

Cash and cash equivalents

This item includes legal tender, including foreign banknotes and coins and demand deposits with the Central Bank of the country or countries where the Group operates through its companies or branches, with the exception of the minimum reserve.
The item is recognised at face value. The face value of foreign currencies is translated into euro at the closing exchange rate at the period-end date.

Fair value change of financial assets and financial liabilities in macro fair value hedge portfolios

These items include, respectively, changes in financial assets or liabilities subject to macro hedging of interest rate risk, based on the respective balance, whether positive or negative.

Other assets

This item includes assets not attributable to the other balance sheet asset items. For example, this item may contain:
- gold, silver and precious metals;
- accrued income other than that capitalised on the related financial assets, including those deriving from contracts with customers pursuant to the IFRS 15 standard;
- receivables associated with providing non-financial goods or services;
- payable tax items other than those recognised in "110. Tax assets".

Leasehold improvements and incremental expenses incurred on third party assets other than those attributable to the item "90. Property and equipment" are also included, insofar as they cannot be separated from the assets to which they refer and therefore cannot be used independently (e.g. building work). These costs are recognised in this item because the lease contract represents a form of control over the assets for the lessee, the use of which is expected to produce economic benefits. These costs are recognised to the income statement in the shortest period between that in which the improvements and the additional expenses may be used and the residual duration of the rental agreement, including the renewal period, if there is evidence in this regard.
These may also include any remainders (of the "borrower's balance") of items in transit or suspended not attributed to the specific accounts, because they are of immaterial amounts.

Other liabilities

This item records liabilities not attributable to the other balance sheet liability items.
For example, this item contains:

- payment agreements that under IFRS 2 must be classified as payables;
- payables associated with the payment of non-financial goods or services received;
- accrued liabilities other than those to be capitalised on the related financial liabilities, including those deriving from contracts with customers pursuant to the IFRS 15 standard;
- various receivable tax items other than those recognised in item "60. Tax liabilities" connected, for example, to withholding agent activities.

Employee termination indemnities and other employee benefits

According to IAS 19, employee termination indemnities represent a post-employment benefit.
Following the supplementary pension reform under Italian Legislative Decree no. 252 of 5 December 2005, new regulations were introduced for employee termination indemnities accrued beginning from 1 January 2007, recognised for accounting purposes.
In particular, for companies which had at least 50 employees in 2006, from an accounting perspective, employee termination indemnities accrued from 1 January 2007 are considered a defined contribution plan; the charge is limited to the benefits established under the Italian Civil Code, without applying any actuarial methodology.
Otherwise, the provisions for employee termination indemnities accrued up to 31 December 2006 will continue to be accounted for as a defined benefit plan.
In general terms, the post-employment plans—which include, beyond the Provisions for employee severance indemnities, Pension funds—are classified into two categories, defined benefits and defined contributions, based on their relative characteristics.
More specifically, in defined contribution plans, the cost is represented by contributions accrued during the year, since the company only has the obligation to pay the contributions defined by contract to a fund and therefore has no legal or implicit obligation to pay other amounts in addition to said contributions in the event that the fund does not have sufficient assets to pay all the benefits to employees.
In defined benefit plans, the actuarial and investment risk, namely the risk that contributions are insufficient or that the assets in which contributions are invested do not generate a sufficient return, is borne by the company. The liability is calculated by an external actuary using the Projected unit credit method. Based on this method, all future disbursements have to be estimated on the basis of demographic and financial assumptions and are then discounted to account for the time that will pass before actual payment and to be re-proportioned on the basis of the ratio of the years of service accrued and the theoretical seniority estimated at the time the benefit is disbursed. The actuarial value of the liability calculated in this way must then be adjusted by the fair value of any assets underlying the plan (net liabilities/assets).
The actuarial gains and losses that originate from changes in the previous actuarial assumptions as a result of the actual experience or as a result of changes to the actuarial assumptions themselves lead to the re-measurement of the net liability and are recognised as a balancing entry of a net equity reserve. These gains and losses are recorded in the "Statement of comprehensive income".
The change in the liability resulting from an amendment or a reduction in the plan is recognised in the income statement as a gain or loss. Specifically, an amendment is made when a new plan is introduced, rather than if an existing plan is withdrawn or amended. On the other hand, there is a reduction when there is a significant decrease in the number of employees included in the plan, such as in the case of redundant headcount reduction plans (access to the Solidarity Fund).

The Projected unit credit method described above, is also used to measure long-term benefits, such as seniority bonuses awarded to employees. Unlike that described for defined benefit plans, actuarial gains and losses relating to the measurement of long-term benefits are recognised immediately in the income statement.

Valuation reserves

This item includes valuation reserves associated with equity instruments designated at fair value through other comprehensive income, financial assets (other than equity instruments) designated at fair value through other comprehensive income, foreign investment hedging, cash flow hedging and for foreign currency conversion differences, as well as for individual assets and discontinued operations, the portion of valuation reserves of investments carried at equity, actuarial gains (losses) on defined benefit plans and profit/loss connected to the change in own credit risk relating to fair value option liabilities. It also includes the revaluation reserves recognised in compliance with special revaluation regulations, also if subject to tax exemption.

Share capital and treasury shares

Share capital includes common and preferred stock issued by the bank net of any capital already subscribed but not yet paid up at the balance sheet or interim reporting date. This item includes any treasury shares held by the bank. The latter are recognised in the financial statements in their own item as a negative component of shareholders' equity.
The original cost of repurchased treasury shares and the gains or losses originated by their subsequent sale are recognised as changes to shareholders’ equity.
Transaction costs relating to operations on share capital, such as share capital increases, are recorded as a decrease in shareholders’ equity, net of any related tax benefits.
Dividends on ordinary shares are recognised as a reduction from shareholders' equity in the year in which the Shareholders' Meeting approves their distribution. Any advances on dividends disbursed to shareholders are recognised in the balance sheet liability item “Advances on dividends” with a negative sign.

Minority interests

This item shows the portion of consolidated shareholders’ equity attributable to shares owned by minority shareholders, calculated based on equity ratios. The amount is calculated net of any treasury shares repurchased by consolidated companies.

b) Illustration of other significant accounting treatments

Dividends and revenue and cost recognition

Revenue from contracts with customers (IFRS 15)

Revenue is the gross inflow of economic benefits that flow to the entity as payment for its obligation to transfer to the customer a wide range of goods and services that are part of ordinary activities.
Revenues from contractual obligations with customers are recognised in profit or loss when it is probable that the entity will receive the payment to which it is entitled in exchange for the goods or services transferred to the customer. This payment must be allocated to the single obligations covered by the contract and must be recognised as revenue in the income statement based on the timing of fulfilment of the obligation. Specifically, revenue may be recognised in the income statement:

- at a particular point in time, when the entity settles its positive duty to act by transferring the promised good or service to the customer or
- over time, as the entity settles its positive duty to act by transferring the promised good or service to the customer.

This positive duty to act is considered fulfilled when the customer takes control of the transferred good or service.
The amount promised in the contract with the customer may include fixed amounts, variable amounts or both. Specifically, the contract amount may vary as a result of redemptions, discounts, refunds, incentives, performance bonuses or similar items. The variability of the consideration may also depend on whether or not a future event

occurs. In the presence of variable fees, the recording of the revenue in the income statement is carried out when it is possible to estimate the revenue reliably and only if it is highly probable that this amount will not subsequently have to be reversed in the income statement, in whole or in a significant part.
If the entity receives a payment from the customer that it expects to reimburse the customer, in whole or in part, for the revenue received, a liability should be recognised for the expected future redemptions. The estimate of this liability is updated at each balance sheet date or interim reporting date and is carried out based on the portion of the amount that the entity expects not to be entitled to.
Costs associated with obtaining and fulfilling contracts with customers are recognised in the income statement in the periods in which the corresponding revenues are accounted for. Costs that are not directly associated with revenues are immediately charged to the income statement.

Income and charges relating to financial instruments

With reference to income and charges relating to financial assets/liabilities, it should be noted that:

- interest is recognised pro-rata temporis on the basis of the contractual interest rate or the effective interest rate if the amortised cost method is used. In the latter case, any marginal costs and incomes, considered an integral part of the return of the financial instrument, are calculated in the effective interest rate and recognised as interest. The item "interest income (or interest expense)" also includes the positive (or negative) spreads or margins accrued until the reporting date, relating to financial derivative contracts:
  - hedging financial assets and liabilities that generate interest;
  - classified in the balance sheet in the trading portfolio, but operationally connected with financial assets and/or liabilities designated at fair value (Fair Value Option);
  - operationally connected with assets and liabilities classified in the trading portfolio and which envisage the settlement of spreads or margins at multiple maturities;
- default interest, if provided for by contract, is recorded in the income statement only when actually collected;
- dividends are recognized in the income statement when the legal right to collect them ensues, and therefore when their distribution is resolved;
- profits and losses from the initial recognition of the fair value of financial instruments are recognised in the income statement at the time of recognition of the transaction, based on the difference between the price paid or collected and the fair value of the instrument, only when the fair value can be determined by referring to current observable market transactions or using valuation techniques whose inputs are observable market parameters; otherwise, these profits and losses are distributed over time, taking the nature and the term of the instrument into account;
- gains and losses deriving from the sale of financial instruments are recognised in the income statement when the sale is completed, with the relative transfer of the risks and benefits, based on the difference between the amount received and the book value of the instruments.

Share-Based Payments

Share-based payments are payments made to employees, as a consideration for work performed, settled with equity-linked instruments, which may, for example, consist of the assignment of:

- stock options;
- rights to receive shares when specific objectives are reached.

Considering how difficult it is to directly estimate the fair value of work received in exchange for the assignment of shares, it is possible to indirectly measure the value of services received, by referring to the fair value of the equity-linked instruments at their assignment date. The fair value of payments settled through the issue of shares is recognised on the basis of the accrual principle in item "190 a). Personnel expenses", with a matching entry as an increase in item "150. Reserves".
In detail, when assigned shares cannot be immediately "used" by the employee but can be used when the employee has completed a given term of service, the company shall pay the cost as a consideration for the service provided throughout the vesting period.

Repurchase agreements, securities lending and sell/buy back agreements

Repurchase or forward agreements whereby the Group sells securities to third parties with the obligation to repurchase them upon maturity of the transactions at a predetermined price are recognised in payables to banks or to customers, depending on the counterparty. Likewise, repurchase or forward agreements whereby the Group acquires securities from third parties with the obligation to resell them upon maturity of the transactions at a predetermined price are recognised in receivables from banks or customers (accounting categories of the "Financial assets designated at amortised cost"), depending on the counterparty. The difference between the spot and forward price of the above-mentioned transactions is recognised as interest (expense or income depending on the case) on an accrual basis throughout the life of the transaction. Securities lending transactions in which the guarantee is represented by cash which is fully available to the lender are recognised in the financial statements like the above-mentioned repurchase agreements.

In the case of securities lending transactions with a guarantee consisting of other securities, or with no guarantee, the lender and the borrower continue to recognise the security subject to the loan and any security provided as a guarantee, respectively, in the balance sheet assets. The remuneration of this transaction is recognised by the lender in item "40. Fee and commission income" and by the borrower in item "50. Fee and commission expense".

Offsetting financial instruments

In accordance with IAS 32, paragraph 42, financial assets and financial liabilities may be offset, and the net balance may be reported in the financial statements if the entity:

- has a legally enforceable right to make said offsets, currently exercisable in all circumstances, where they refer to regular business operations or to situations of default, insolvency or bankruptcy of the parties;
- intends either to settle the transactions on a net basis, or to settle the same on a gross basis, the substantial effects of which are equivalent to a settlement on a net basis.

For derivative instruments covered by offsetting arrangements, which meet the requirements illustrated above, Circular 262 establishes that all trading derivatives and all hedging derivatives may be offset. If the imbalance of trading derivatives is the opposite sign of the imbalance of all hedging derivatives, the imbalances are to be reported on a net basis. Usually, the net balance is allocated to the trading portfolio rather than as hedging derivatives, depending on the prevailing absolute value of the imbalance of trading derivatives compared to the hedging derivatives.

Securitisations - derecognition from financial statements of financial assets transferred

In securitisation transactions put in place by the Group, the transfer of financial assets to an SPE (special purpose entity), even if with recourse entails the derecognition of these assets from the financial statements, only if there is a substantial transfer of the risks and the benefits. In the event that the substantial transfer of risks and benefits cannot be verified, the transferred assets are derecognised if the Group relinquishes all control over them. In the event of such circumstances, the difference between the carrying value of the assets sold and the amount received, including the new assets acquired, is recognised as a gain or loss in the income statement.
Otherwise, the financial statements are not derecognised if the Group has maintained the risks and rewards associated with the securitised portfolio, even though it has been sold without recourse, for example via the comprehensive subscription of a tranche of junior securities or securities that bear the risk of the initial losses or through the assumption of similar exposures. Consequently, the transferred receivables must continue to be recognised in the separate financial statements of the originator bank as "Assets sold and not derecognised", while the amount collected from the transfer is recognised as a balancing entry to the payable owed to the SPE, net of the securities subscribed by the bank in question. In the consolidated financial statements, the main impact of the consolidation of the SPE and of the relative capital from the securitisation, if the requirements of control established by IFRS 10 are fulfilled, is that the securities issued by the SPE and subscribed by entities not belonging to the Group are recorded in the consolidated balance sheet.
Tiepolo Finance is the only exception to the above-described general rule, for which on first-time adoption of the international accounting standards, the Group made use of the option not to recognise in the financial statements assets underlying securitisations performed before 1 January 2004, which had been derecognised based on the previous accounting standards. As at June 30 2018, the junior security issued by Tiepolo Finance, classified in the

portfolio of "Financial assets designated at fair value through profit and loss: c) Other financial assets required to be measured at fair value", was recorded with a value of zero, insofar as entirely written down.

Business combinations, goodwill and changes in interest holdings

A business combination involves the union of businesses or separate business activities in a single entity obliged to prepare financial statements.
A combination may give rise to an investment relationship between the purchasing Parent Company and the subsidiary acquired. In such circumstances, the purchaser applies standard IFRS 3 in the consolidated financial statements, while in the separate financial statements, the interest holding acquired as an investment in the subsidiary is recorded, applying accounting standard IAS 27 "Separate financial statements".
A combination may also include the purchase of another entity's net assets, including any eventual goodwill, or the acquisition of the capital of another entity (mergers, conferrals, business segment acquisitions). A combination of this type does not translate into an investment relationship similar to that which exists between the parent and subsidiary company, and therefore, in this case, accounting standard IFRS 3 applies also in the separate financial statements of the purchaser.
Business combinations are recognised using the purchase method, which requires: (i) the identification of the acquirer; (ii) the calculation of the cost of the business combination; (iii) purchase price allocation (PPA).

Identification of the acquirer

For all business combinations, IFRS 3 requires the identification of an acquirer, identified as the party that obtains control over another entity, meaning the power to establish the financial and operational policies of that entity in order to obtain benefits from its business activities. For business combinations that result in the exchange of shareholdings, the identification of the acquirer must consider factors such as: (i) the number of new ordinary shares with voting rights issued with respect to the total number of ordinary shares with voting rights which will constitute the share capital of the company existing after the combination; (ii) the fair value of the entities that participate in the combination; (iii) the composition of the new corporate bodies, (iv) the entity that issues the new shares.

Calculation of the cost of the business combination

The price transferred in a business combination equates to the fair value, as of the acquisition date, of the assets transferred, the liabilities incurred and the equity instruments issued by the purchaser in exchange for obtaining control over the entity acquired. The price the acquirer transfers in exchange for the entity acquired includes any asset or liability emerging from an agreement on the potential price, to be recorded as of the acquisition date on the basis of the fair value. Changes to the transferred price are possible if they derive from additional information on events or circumstances which existed as of the acquisition date and are recognisable within the business combination measuring period (or rather within twelve months of the date of acquisition, as will be specified further on). Any other change which derives from events or circumstances subsequent to the acquisition, such as that acknowledged to the seller linked to achievement of specific income-related performances, must be recognised in the income statement.
The costs relating to the acquisition, which include brokerage commission, advisory, legal, accounting and professional costs and general administrative expenses, are recorded in the income statement at the time they are incurred, with the exception of the costs for issuing shares and debt securities which are recorded on the basis of the matters set forth by standards IAS 32 and IFRS 9.

Purchase Price Allocation (PPA)

On the basis of the acquisition method, at the acquisition date, the acquirer must allocate the cost of the business combination (the Purchase Price Allocation or PPA) to the identifiable assets acquired and the liabilities assumed, measured at the relative fair values at that date, also recognising the value of the minority interests of the acquired entity. Therefore, it is necessary to draw up a balance sheet for the acquired company at the acquisition date, calculating at fair value the identifiable assets acquired (including any intangible assets not previously recognised by the acquired entity) and the identifiable liabilities assumed (including contingent).
With regard to each business combination, the minority interests can be recorded at fair value or in proportion to the portion held in the identifiable net assets of the company acquired.

In addition, if control is achieved by means of subsequent acquisitions (business combinations carried out in several phases), the shareholding previously held is measured at fair value as of the acquisition date, and the difference with respect to the previous book value must be recorded in the income statement.
At the acquisition date, the acquirer must therefore determine the difference between:

- the sum of:
  - the cost of the business combination;
  - the amount of any minority interests as described above;
  - the fair value of any shareholdings previously held by the acquirer;
- the fair value of the net identifiable assets acquired, including contingent liabilities.

Any positive difference must be recognised as goodwill; otherwise, any negative difference must be recognised in the income statement of the entity resulting from the business combination as profit deriving from a bargain purchase (negative goodwill or badwill), after making a new measurement to ascertain the proper process for identifying all assets acquired and liabilities assumed.
Identification of the fair value of the assets and liabilities must be finalised definitively within a maximum period of twelve months as from the acquisition date (measuring period).

Once control has been obtained and the acquisition method previously described applied, any further increase or decrease in the shareholding in a subsidiary company which continues to be controlling is recorded as a transaction between shareholders. Therefore, the book value of the group and minority shareholders' equity must be adjusted to reflect the changes in the holding in the subsidiary. Any difference between the value for which the minority interests are adjusted and the fair value of the price received or paid must be recorded directly in the group shareholders' equity.

In the presence of an event that results in a loss of control, the effect to be recognised in the income statement is equal to the difference between (i) the sum of the fair value of the price received and of the fair value of the residual interest held and (ii) the prior book value of the assets (including goodwill), of the liabilities of the subsidiary, and any minority shareholder's equity. The amounts previously recognised in the statement of comprehensive income (such as the revaluation reserves of financial assets available for sale designated at fair value through other comprehensive income) must be recorded in the same way as required in the event that the parent company has directly disposed of the assets and the related liabilities (by means of reclassification in the income statement or shareholders' equity.
The fair value of any shareholding held in the former controlling investment must be considered equal to the fair value at the time of initial recognition of a financial asset on the basis of IFRS 9 or, if appropriate, equal to the cost at the time of initial recognition in an associated company or a jointly-controlled entity.

Reorganisation transactions between two or more businesses or corporate assets forming part of the Group are not considered to be business combinations. The international accounting standards do not govern transactions under joint control which are recorded at the same values as the entity acquired in the financial statements of the acquirer if they do not present a significant influence on future cash flows. This is in compliance with the matters established by IAS 8 paragraph 10, which requires, in the absence of a specific standard, the use of one's own judgement when applying an accounting standard for the purpose of providing relevant, reliable, prudent disclosure which reflects the economic essence of the transaction.

Methods for determining impairment losses on IFRS 9 Financial Instruments

At each balance sheet or interim reporting date, loans and debt securities classified under "Financial assets designated at amortised cost" and "Financial assets measured at fair value through other comprehensive income"—as well as off-balance sheet exposures represented by commitments to disburse funds and the guarantees given—must be subject to impairment in order to estimate expected losses in value due to credit risk (ECL - Expected Credit Losses).

General features of the impairment model
According to the Expected Credit Losses calculation model, losses must be recorded not only with reference to objective evidence of impairment losses that had already occurred at the valuation date, but also on the basis of expectations of future impairment that has not yet occurred.

In particular, the ECL model states that the aforementioned instruments must be classified into three distinct stages, according to their absolute or relative credit quality or compared to the initial disbursement, to which different criteria correspond for measuring the expected losses. More specifically:

- Stage 1 includes both originated or acquired performing financial assets that display no significant deterioration in credit risk (SICR - Significant Increase in Credit Risk) with respect to the initial recognition date;
- Stage 2 includes performing financial assets with significant deterioration in credit risk on the valuation date compared to the initial recognition, albeit not impaired;
- Stage 3 includes all exposures for which one or more events capable of negatively impacting cash flows are found (evidence of impairment), i.e. exposures that are considered non-performing.

For Stage 1 exposures, the expected loss is accounted for, on the date of initial recognition and on each subsequent reporting date, for up to one year; for Stage 2 and 3 exposures, expected losses are recognised over the entire residual lifetime of the instrument.
An exception to the foregoing is represented by financial assets that are considered non-performing from the time of their acquisition or origin (POCI - Purchased or Originates Credit Impaired). Please refer to the paragraph below for more information on this.

For the Banco BPM Group, the scope of the exposures classified in Stage 3 corresponds to that of non-performing loans, identified in accordance with the definitions established by the supervisory provisions in force (Bank of Italy Circular no. 272 "Matrix of accounts") and referred to by Bank of Italy Circular no. 262 "Bank financial statements: layouts and rules for preparation", insofar as retained consistent with IAS/IFRS standards in terms of objective evidence of impairment. Based on the above-mentioned circulars, the scope of non-performing loans corresponds to the "Non-Performing Exposure" aggregate defined by Regulation (EU) 2015/227, which incorporated the EBA's "Implementing Technical Standards (ITS) on Supervisory reporting on Forbearance and Non-Performing exposure" (EBA/ITS/2013/03/rev1 24/7/2014). Specifically, the circulars identify the following categories of non-performing assets:

- Bad Loans: these represent the set of cash and off-balance-sheet exposures for a party in a state of insolvency (even if not ascertained in court) or in substantially equivalent situations, regardless of any loss forecasts developed by the bank;
- Unlikely to pay: these represent cash and off-balance-sheet exposures for which the conditions are not met for the classification of the debtor under bad loans and for which it is deemed unlikely that the borrower will meet its credit obligations (for principal and/or interest) in full without recourse to actions such as the enforcement of guarantees. This assessment is carried out regardless of the presence of any amounts (or instalments) past due and unpaid. Classification as unlikely to pay is not necessarily linked to the explicit presence of anomalies, such as non-repayment, but it is linked to the existence of elements indicative of a situation of risk of default by the borrower (for example, a crisis in the industrial sector in which the borrower operates);
- Past due and/or non-performing overdue exposures: cash exposures, other than those classified as bad or unlikely to pay loans which, at the reference date, have a past due and/or overdue position for more than 90 days, in accordance with the thresholds of significance provided for by law. For the Banco BPM Group, past due and/or non-performing overdue exposures are determined by making reference to the position of the individual borrower.

In addition, in line with EBA standards, Bank of Italy regulations have introduced the definition of forborne exposures. In particular, these are exposures benefiting from measures of tolerance, which consist of concessions, in terms of changes to and/or the refinancing of an existing loan, granted only to customers in financial difficulty, or to prevent the financial difficulty of the same, which could have a negative effect on the customer's ability to fulfil the original contractual obligations. They are not granted to a debtor with the same risk profile but who is not in financial difficulty. These tolerance measures must be identified in terms of individual credit lines and may regard the exposures of debtors classified both as performing and non-performing.
For exposures with forbearance measures classified as a unlikely to pay, the return to performing exposures can occur only after one year has elapsed since it was granted (the probation period) and all the other conditions laid out in paragraph 157 of the EBA's ITS are met.
In any event, renegotiated exposures must not be considered forborne when the debtor is not in a situation of financial difficulty; these are renegotiations granted for commercial reasons.

Impairment losses on performing financial instruments

Regarding performing financial assets, i.e. for those assets not considered impaired, it is necessary to assess, at the single relationship level, the existence of a significant deterioration in credit risk (SICR), by comparing the credit risk associated with the financial instrument at the time of valuation and at the time of initial disbursement or acquisition. This comparison is made on the basis of quantitative and qualitative criteria. More specifically, in order to identify the existence of a significant deterioration in credit quality and the subsequent transfer of the financial instrument from Stage 1 to Stage 2, the Banco BPM Group has identified the following criteria (Stage Assignment):

- relative quantitative criteria, based on statistical observations, considered an indication of a significant increase in credit risk over time;
- absolute qualitative criteria, represented by the identification of trigger events or the exceeding of absolute thresholds as part of the credit monitoring process. This includes all exposures affected by forbearance measures which have this attribute still active, regardless of whether the current probation period is regular or not;
- backstop indicators, i.e. factors of credit delinquency, the existence of which gives rise to the presumption that there has been a significant increase in credit risk, unless there is evidence to the contrary. Presumably, except in exceptional cases attributable to specific types of counterparties, such as Public Administrations, the Group believes that the credit risk of the exposure should be considered significantly increased if past due/delinquent for more than 30 days, without prejudice to the application of the thresholds of significance provided for by supervisory regulations.

With particular reference to the quantitative criterion applicable to credit exposures to customers, the Banco BPM Group has chosen to take the change between the default probability (DP) at the date of origin of the financial instrument and the same probability measured at the reporting date as a reference. The development of the model has led to the identification of specific internal thresholds of variation between the default probability detected at the origin of the contractual relationship and the default probability detected at the valuation date, differentiated by risk segment, rating class and residual life. Exceeding these thresholds represents a significant increase in credit risk and entails the consequent transfer of the individual line of credit from Stage 1 to Stage 2. The determination of these thresholds, developed based on the Group's historical observations, underwent a calibration process to guarantee the effective capacity for discrimination of the stage assignment model.

For the portfolios of loans to banks and debt securities, the relative quantitative criterion is based on a change in the default probability at twelve months, rather than over the residual lifetime of the instrument. This simplified approach, taking account of the type of counterparty/issuer, is justified by the insignificance of the difference in impact compared to the more complex model used on the portfolio of loans to customers.

Regarding debt securities, in order to measure the significant increase in credit risk, the Group applies the Low Credit Risk Exemption, i.e. the practical expedient that consists in assuming that credit risk has not increased significantly compared to the initial recognition of the instrument when the credit risk was judged as being “low”. This exemption applies to securities rated as investment grade at the valuation date, in full compliance with IFRS 9. In addition, considering the presence of more than one purchase transaction for the same International Securities Identification Number (ISIN), it was necessary to identify a method to pinpoint the tranches sold in order to determine the residual quantities associated with the credit quality at the date of initial recognition to be compared with that at the valuation date; this method of movement is based on the FIFO method (First In - First Out).

With regard to the functioning of the model, the Banco BPM Group has decided to adopt a symmetrical reclassification model from Stage 2 to Stage 1. In cases where the conditions triggering the significant deterioration in credit risk cease to exist at a later valuation date, the financial instrument returns to being measured based on the expected loss over twelve months. It should also be noted that in the event of a return amongst the performing exposures under Stage 3, there is no mandatory transfer of the counterparty's relationships to Stage 2 i. The classification of performing exposures into stages (Stage 1 or Stage 2) will depend on the automatic application of the stage assignment framework.

In the case of forbearance exposures, any return to the calculation of the expected loss at one year is made in accordance with the probation period, in line with the time frames set out in the EBA’s aforementioned ITS, which has been transposed into supervisory provisions.

Once the allocation to the various stages of credit risk has been defined, the expected losses (ECL) are determined by assigning the following risk parameters to each individual transaction or tranche:

- DP (Default Probability): represents the probability that a performing exposure can move to impaired status over the course of one year. This factor is quantified using internal exposure rating models or on the basis of average segment/portfolio data;
- LGD (Loss Given Default): the percentage of loss in the event of default, quantified on the basis of historical experience of recoveries discounted on the basis of impaired practices;
- (EAD - Exposure At Default): the exposure at the moment of default.

Value adjustments for expected losses are then quantified as a product of DP, LGD and EAD.
The models used to estimate these parameters employ the same parameters used for regulatory purposes, making specific adjustments to account for the different requirements and purposes of the accounting regulations compared to prudential regulations. In keeping with the impairment model of IFRS 9, the main adjustments aim to:

- remove the margins of conservatism required solely for prudential purposes;
- account for the conditions of the current economic cycle (PiT - Point-in-Time) instead of the measurement of the parameters through the economic cycle (TTC - Through the cycle), which is required for regulatory purposes;
- introduce forecast information regarding future trends in macroeconomic factors (forward-looking) considered potentially capable of influencing the debtor's situation;
- to extend risk parameters to a long-term perspective, accounting for the lifetime of the credit exposure to be assessed.

Specifically, the DPs calculated over the lifetime of the instrument are obtained on the basis of the regulatory DPs, which account for the entire TTC economic cycle, appropriately calibrated, by means of satellite models to reflect the default rates based on current (PiT) and prospective (forward-looking) conditions.
LGD values are assumed to be equal to the regulatory recovery rates calculated through the economic cycle (TTC) and suitably adjusted in order to remove some of the conservatism margins of the regulatory models, which are represented by indirect costs and the component associated with the adverse economic cycle (the down turn component), as well as to reflect the most current recovery rates (PiT) and expectations concerning future (forward-looking) trends. Specifically, the estimate of this parameter takes into account the impact of the economic cycle on both the value associated with real estate guarantees through the property price index—thus changing the ratio between the residual debt and the value of the guarantee—and the component represented by the probability of bad loans via a specific scaling factor obtained by simulating the default cycles with the migration matrices between statuses.
To calculate the EAD lifetime, the exposure at each future payment date is represented by the residual debt, based on the amortisation plan, increased by any instalments due/past due. For off-balance-sheet exposures (commitments to disburse funds and guarantees given), the EAD is equal to the nominal value weighted by a specific credit conversion factor (CCF).
Forecasts for forward-looking macroeconomic indicators are quantified based on five possible future scenarios which are assigned the respective probability of occurrence determined internally by the Group. More specifically, in addition to the most likely baseline scenario (i.e. the forecast macroeconomic scenario on the basis of which the Group develops its projections for economic/asset and risk data over the short and medium term), alternative scenarios were developed to be better (positive and very positive) and worse (severe and very severe).

Lastly, for the estimate of expected losses over the lifetime of the instrument, the reference time period is represented by the contractual maturity date. For instruments without maturity, the estimate of expected losses refers to a time frame of one year from the reporting date.

Impairment losses on non-performing financial instruments
As illustrated above, for non-performing financial assets, to which a 100% default probability is associated, the amount of adjustments for expected losses relating to each loan is equal to the difference between its book value (interim situation) at the time of valuation (amortised cost) and the present value of expected future cash flows, calculated by using the original effective interest rate (or a close substitute when not available). Cash flows are estimated on the basis of expected recovery over the entire lifetime of the asset, taking into account the estimated net realisable value of any guarantees.

To estimate future cash flows and related collection times, the loans in question consisting of significant unit amounts are subject to an analytical valuation process. For some similar categories of non-performing loans with insignificant unit amounts, the assessment processes establish that the loss forecasts are based on a forfeit/statistical calculation method, to be applied analytically to each individual position. The scope of exposures subject to forfeit/statistical calculation, based on LGD management grids and differentiated according to segment and risk status (vintage), is represented by:

- bad loans and probable defaults with exposures below or equal to an established threshold of 300 thousand euro;
- the total number of past due exposures impaired, regardless of the relevant exposure threshold. In particular, these are loans which show uninterrupted overdrafts or late payments, automatically identified by the Group's IT procedures, based on the cited rules of the Supervisory Authority.

Depending on the deterioration status and type of exposure, the recovery value is determined using a going concern approach rather than a gone concern approach.
The going concern approach is implemented if it is considered that the debtor's operating activity may continue to generate, in the foreseeable future, cash flows to be used for the payment of financial debts to all creditors, based on expected repayment schedules. The approach in question establishes, as a source of redemption, the profitability available deriving from the customer's operating activity or from other financial sources, as well as the estimated amount deriving from the enforcement of any collateral or personal guarantees (for the portion not covered by the available profitability). The available profitability assessment is carried out prudentially using different analyses, depending on the type of customer and the data acquired by it.
The gone concern approach is used when the customer's operating activity is found or is expected to cease and the main source of repayment is the amount deriving from the enforcement of collateral (pledge or mortgage), as is the case for all exposures classified as non-performing. In addition, possible redemption flows from seizable assets owned by the debtor or any guarantor must be evaluated.

Regarding bad loans, the quantification of expected losses includes forward-looking elements correlated with specific sales scenarios, where the Group's NPL strategy establishes that the aforementioned loans may be recovered through sale on the market.
Consequently, the estimate of the expected losses from bad loans varies depending not only on the expected flows recoverable from internal management activities (work out), but also on the estimated flows recoverable through their sale on the market (the multi scenario approach).
As expressly provided for by the ITG[(1)] of the IASB, it is possible to consider the flows recoverable through sale when determining the expected losses, to the extent that it is possible to develop expectations and assumptions inferred on the basis of reasonable and demonstrable information (please see the following document on this subject: Meeting Summary – 11 December 2015 - Inclusion of cash flows expected from the sale on default of a loan in the measurement of expected credit losses).
Given the above, a new valuation model has been developed on the basis of which two different estimates of the cash flows that the Group expects to receive are associated for each exposure:

- the first is determined assuming recovery from the debtor based on internal activity, according to the ordinary valuation guidelines followed by the Group as illustrated above (workout scenario);
- the second is calculated assuming recovery by assigning the receivable (sale scenario).

Taking into account that loans likely to be sold cannot be individually identified on the reporting date, the model provides that each loan is associated with a probability of sale.
The expected loss for the loans in question is therefore equal to the weighted average of the probabilities assigned to the two scenarios of the estimated cash flows recoverable in the two scenarios (workout and sale).
Probability is assigned to the various scenarios assuming the segmentation of the Group's total portfolio of bad loans, in accordance with the main characteristics that influence the value attributed by the market to loans of this type (for example: vintage, amount of exposures, type of product, presence of collateral and type, customer segment).
The probability assigned to the various clusters was guided by the amount of target disposals approved by the Board of Directors when defining and updating the NPL Strategy. In other words, the probabilities have been assigned to the various clusters in such a way that the sum of the total nominal values of each cluster multiplied by the relative probability of transfer (hereinafter also "expected transfer value") amounts to the aforementioned amount of target disposals approved by the Board of Directors. The probabilities assigned to the various clusters vary over time and can range from a minimum value of 2%, assigned to the cluster that is deemed less convenient and therefore less likely to sell, up to a maximum value of 85%, which is assigned to the cluster that includes the loans deemed more

[(1)] This is the IFRS Transition Resource Group for impairment of financial instruments, i.e. a working group established to support the implementation of certain issues relating to the new IFRS 9 impairment model.

likely to sell. The composition of the clusters also varies over time depending on the trend of market appetite for the various types of exposures (e.g. secured vs unsecured) and the consequent assessments of convenience made by the competent bank bodies.
The valuation methodology used to calculate the recovery flows through sale is based on a discounting process for the recoverable cash flows (discounted cash flows), which takes into account the main parameters that are normally considered by potential buyers when defining the purchase price, suitably calibrated in order to take into account the comparable transactions observed on the market.

Acquired or originated non-performing financial assets

If at the time of initial recognition a credit exposure classified under items"Financial assets designated at fair value through other comprehensive income" or "Financial assets designated at amortised cost" is deemed impaired, it qualifies as "Acquired or originated non-performing financial assets" (POCI - Purchased or Originates Credit Impaired).
An asset is deemed non-performing at the time of initial recognition when the credit risk is extremely high and, in the instance of acquisition, it is acquired with significant discounts compared to the residual contractual debt.
Regarding the criteria for initial recognition, measurement and derecognition, please refer to the information given for the asset items under which they can be classified, except as specified below, concerning the methods adopted to measure the amortised cost and impairment.
Specifically, the amortised cost and, consequently, interest income are calculated considering the credit-adjusted effective interest rate. With regard to calculating the credit-adjusted effective interest rate, the adjustment for the credit consists of considering the estimate of future cash flows, including the credit losses expected over the entire residual lifetime of the asset.
Additionally, the assets in question also entail special treatment with regard to the impairment process, as they are always subject to the calculation of the loss expected over the lifetime of the financial instrument. Therefore, subsequent to initial recognition, the loss or gain deriving from any change in the losses expected throughout the entire lifetime of the credit, compared to initial losses must be recorded in the income statement. Thus, it is not possible for the expected losses to be calculated on the basis of one year.

Within the Group's consolidated financial statements, non-performing loans acquired as part of the business combination with the former BPM Group fall within the item in question.

Renegotiations

If a financial asset is renegotiated (i.e. when the original contractual conditions are amended by the parties), it must be verified whether the financial asset should continue to be recorded in the financial statements, or if this is not the case, the original financial asset should be derecognised and a new financial instrument recognised.
To this end, it is necessary to evaluate whether the amendments made to the contractual terms of the renegotiation are substantial.
If the changes are substantial, the entity must derecognise the financial instrument that is subject to change and proceed to recognise a new financial asset on the basis of the new contractual provisions, whether the renegotiation is formalised through the signing of a new contract or by way of amendment to an existing contract. Specifically, renegotiations introducing specific objective elements which affect the characteristics and/or cash flows of the financial instrument (such as, a change in the currency of denomination or the introduction of indexing to equity or commodity parameters) are held to be substantial. This takes into consideration the significant impact expected on original cash flows or which are made to customers without financial difficulties, with the objective of adjusting the cost of the contract to current market conditions. In the latter case, it should be noted that if the bank does not grant the renegotiation of the contractual conditions, the customer would be able to borrow from another intermediary with the consequent loss of the revenue flows provided by the renegotiated contract for the bank. In other words, it is deemed that there is no loss for the bank that must be recognised in the income statement as a result of realigning to the best current market conditions for its customers for commercial renegotiations.
Otherwise, for non-substantial renegotiations, the gross value is restated by calculating the present value of the cash flows resulting from the renegotiation, based on the original rate of exposure existing before the renegotiation. The difference between this gross value and the gross book value prior to the change is recognised in the income statement as a gain or loss from contractual changes without derecognition (modification accounting). Non-substantial renegotiations include modifications granted to counterparties with financial difficulties (concessions of forbearance measures) relating to the bank's attempt to maximise the recovery of the original exposure, the risks and

benefits of which, however, continue to be retained by the bank. This does not apply to modifications that introduce substantial objective elements into the contract that could result in the derecognition of the financial asset, as described above.

Financial liabilities designated at fair value

To obtain funding, the Group issues different types of bonds, both at a fixed rate and structured types (index-linked to share components, to exchange rates, to interest rate structures, inflation rates or similar indices). The risks resulting from such issues are hedged by the Group as part of its overall market risk management and also by entering into derivative contracts.

From an accounting perspective, some of these contracts are designated as hedges, according to the rules of hedge accounting and in particular for the fair value hedge, as illustrated previously in paragraph "4. Hedging transactions".
Conversely, for other contracts, for which the hedging is not qualified according to hedge accounting rules, asymmetric accounting would be created, between the financial liability and the hedging transaction, resulting from the different measurement criteria applied to the bond issue—valued at amortised cost—and to the operational hedge derivative instrument, measured at fair value. The Group overcomes this asymmetry by designating bond issues subject to operational hedging at fair value (Fair Value Option). In addition to simplifying the administrative and accounting management of hedges, with specific reference to structured issues, the adoption of the fair value option instead of hedge accounting is closely linked to the actual methods the Group uses to carry out its hedging policies, by managing its market exposure globally and not through a discrete relation with the issued bond.
Unlike hedge accounting, whose accounting rules require that only fair value changes attributable to the hedged risk be recognised on hedged instrument, the fair value option requires the recognition of all fair value changes, regardless of the hedged risk factor.

For the issues in question, fair value is measured first by making recourse to prices observable in markets considered active, such as regulated markets, electronic trading networks (like Bloomberg) or organised trading systems or equivalent.
Lacking prices observable in active markets, the measurement is based on the prices of recent transactions on the same instrument in non-active markets rather than on valuation techniques based on a cash flow discounting model, which must consider all factors deemed significant by market participants in determining a hypothetical trade. In particular, to determine creditworthiness, the spreads implicit in the comparable issues of the same issuer obtained on active markets are used rather than the curve of the credit default swaps in the name of Banco BPM with an equal degree of subordination as the security subject to the assessment. The impact resulting from the change in the Bank's creditworthiness, between the issue date and the valuation date, is quantified by calculating the difference between the fair value obtained, considering all risk factors to which the bond is exposed, including credit risk, and the fair value obtained considering the same factors, excluding the change in credit risk arising during the period.
For further details on how fair value is determined, please refer to the detailed information in the specific paragraph in "Part A.4 – Fair value disclosure".

With regard to recognition criteria for balance sheet and income statement components, note that:

- derivatives that are associated operationally with liabilities designated at fair value are classified as "Financial assets designated at fair value through profit and loss: a) Financial assets held for trading" or "Financial liabilities held for trading";
- the spreads and the margins accrued on the derivatives up until the valuation date are recorded, depending on the balance, under "interest income" or "interest expense", consistent with the accrual recorded for the bond issues subject to operational hedges;
- the profits and losses resulting from the disposal or valuation of bonds issued under the fair value option are recognised under the income statement item "110. Profits (losses) on other financial assets and liabilities designated at fair value through profit and loss", with the exception of valuation and realisation effects correlated with the change in own credit risk, which are recognised as a balancing entry to a specific equity reserve (item "120. Valuation reserves"), unless this treatment creates or amplifies a mismatch in the income (loss), as described in more detail in section "13. Financial liabilities designated at fair value";
- the results of the valuation of derivatives connected with the fair value option loans are recognised in the income statement under the item "80. Profits (losses) on trading".

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

During the period there were no transfers between portfolios of financial assets.

A.4 FAIR VALUE DISCLOSURE

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market operators, under current market conditions on the valuation date in the main market or in a more advantageous market (exit price). Underlying the fair value measurement is the presumption that the entity is considered a going concern, i.e., that it is in a fully operational situation and it does not therefore intend to liquidate or considerably reduce its operations or undertake transactions under unfavourable conditions. Therefore, the fair value is not the amount that the entity would receive or pay in the case of forced transactions or below-cost sales.

Fair value is a market valuation approach not specifically referring to estimates concerning possible future cash flows developed by the individual company; indeed, fair value must be determined by adopting the assumptions that market participants would use in determining the price of assets and liabilities, presuming that they are acting in their own best economic interest.
To measure the fair value of financial and non-financial assets and liabilities, IFRS 13 establishes a three-tiered fair value hierarchy, based on the source and quality of the inputs used:

- **Level 1**: the inputs are represented by listed (non-adjusted) prices in active markets for identical assets or liabilities;
- **Level 2**: the inputs are represented by:
  - listed prices in active markets for similar assets or liabilities;
  - listed prices in non-active markets for identical or similar assets or liabilities;
  - parameters observable in the market or corroborated by market data (for example, interest rates, credit spreads, implicit volatilities and exchange rates) and used in the valuation technique;
- **Level 3**: the inputs used are not observable in the market.

For financial instruments designated at fair value in the financial statements, the Group has established a "Fair Value Policy", which assigns the maximum priority to the prices listed on active markets (level 1) and lower priority to the use of inputs which cannot be observed (level 3), in that they are more discretionary, in line with the above-described fair value hierarchy. More specifically, this policy defines:

- the rules to identify market data, the selection/hierarchy of information sources and the price configurations needed to measure the value of the financial instruments in active markets, classified as level 1 of the fair value hierarchy ("Mark to Market Policy");
- the valuation techniques and the relative input parameters in all cases in which the Mark to Market Policy cannot be adopted ("Mark to Model Policy").

Mark to Market

To determine fair value, the Group uses information based on market data, whenever available, obtained from independent sources, insofar as this is considered the best evidence of fair value. In this case, the fair value is the market price of the same instrument assessed, meaning without changes in or restructuring of the instrument, which can be taken from the listings expressed by an active market (and classified as level 1 in the fair value hierarchy). A market is considered active when the list prices express actual and regular market transactions and are readily and regularly available through stock markets, brokers, intermediaries, sector companies, listing services or authorised entities.

Mark to Model

When the Mark to Market Policy is not applicable, because there are no prices directly observable on active markets, it is necessary to use valuation techniques that maximise the use of information available on the market, based on the following valuation approaches:

1. Comparable approach: in this case, the instrument's fair value is derived from the prices observed in recent transactions on similar instruments in active markets, suitably adjusted to take into account differences in

the instruments and in the market conditions, rather than from the prices of recent transactions on the same instrument as that subject to valuation not listed in active markets;

2. Valuation Model: in the absence of observable transaction prices for the instrument being measured or similar instruments, it is necessary to apply a valuation model. The model must provide proven reliability in estimating hypothetical "operational" prices and therefore must be generally accepted by market participants.

This was classified in level 2 instead of level 3 as significant inputs used for the purpose of determining the fair value were observed on the market. A financial instrument must be classified in its entirety in a single level. Therefore, when the measurement technique uses input from multiple levels, the entire measurement must be classified in the level of the hierarchy where the lowest level of input is classified, where it is deemed significant for calculating the fair value as a whole.

The following types of investment are normally considered as level 2:

- OTC financial derivatives whose fair value is obtained through pricing models, which may use both observable and non-observable input. However, the latter parameters are judged to be insignificant in calculating the overall fair value;
- equity instruments that are not listed on active markets, measured using market multiple techniques, referring to a selected sample of companies that are comparable to the company being valued, rather than measured based on actual transactions executed in a time frame that is reasonably near the reference date;
- third party or own debt securities that are not listed on active markets, whose input, including credit spreads, is taken from market sources;
- hedge funds featuring significant transparency and liquidity, measured based on the NAV provided by the management company/fund administrator.

The following financial instruments are generally considered level 3:

- hedge funds characterised by significant levels of illiquidity, and for which the process to evaluate the equity of the fund requires a considerable amount of assumptions and estimates. The fair value is measured on the basis of the NAV. Said NAV may be suitably corrected to account for the fund's diminished liquidity, i.e., the period of time between the date of the request for redemption and that of the actual redemption, as well as for possible exit commissions relating to the investment;
- real estate funds measured on the basis of the last available NAV;
- private equity funds measured on the basis of the last available NAV, adjusted if necessary to take into account events that were not recognised in the measurement of the price or to reflect a different valuation of the assets underlying the fund in question;
- illiquid stock for which no recent or comparable transactions have been observed, usually measured on the basis of the equity model;
- debt securities characterised by complex financial structures, for which sources that are not publicly available are typically used. These are non-binding quotations and moreover not corroborated by market data;
- debt securities issued by parties in financial difficulty, for which the management has to use its own judgement to establish the "recovery rate", as no significant prices can be observed on the market;
- OTC derivative financial instruments for which the non-observable input parameters used by the pricing model are deemed significant in order to measure the fair value;
- medium/long-term loans (performing and non-performing) measured on the basis of expected cash flows determined using models that vary according to the status of the counterparty and discounted at an interest rate considered representative from the perspective of the potential buyer.

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

Financial assets and liabilities designated at fair value on a recurring basis

For the Banco BPM Group, assets and liabilities measured at fair value on a recurring basis are represented by financial assets and liabilities. For these instruments, in the absence of prices directly observable in active markets, the fair value must be determined using the "Comparable Approach" valuation approach or the "Model Valuation", as described in the previous paragraph. A description is provided below of the main valuation techniques adopted for each type of financial instrument.

Debt securities

These are measured by discounting expected cash flows (Discounted Cash Flow Method), suitably adjusted to account for issuer risk. The sources of information used to determine the spread deemed expressive of issuer risk are, in hierarchical order: i) the cash credit spread curve drawn from the prices of securities of the same issuer, characterised by the same seniority and currency, listed on markets considered active; (ii) the "Credit Default Swap" curve of the issuer with an equal seniority; (iii) the credit spread curve of debt securities listed in active markets relating to comparable issuers; (iv) the rating/sector cash credit spread curves; (v) the sector credit default swap curve.

Loans that do not pass the SPPI test

The techniques used for loans are illustrated below, which are required to be measured at fair value since the contractual cash flows do not exclusively envisage repayment of the principal and payment of interest on the principal to be repaid (i.e. they do not pass the SPPI test), either because of clauses originally envisaged in the contract or subsequent amendments.

More specifically:

- for loans that do not pass the SPPI test due to the presence of contractual clauses originally provided for in the contract, the fair value is determined on the basis of cash flows, suitably adjusted for expected losses, based on DP and LGD parameters. These flows are then discounted using a market interest rate, adjusted to take account of a premium considered to express risks and uncertainties. In the presence of implicit optional components, such as the possibility of changing the interest rate, the fair value also takes into account the valuation of these components;
- for loans that do not pass the SPPI test as a result of contractual changes due to restructuring agreements (these are in the form of non-performing forborne exposures) , the fair value measurement takes as its initial reference the cash flow forecasts expressed by the operator, in line with the method used to determine the impairment of loans at amortised cost. These flows shall be adjusted to take account of the likelihood or otherwise of the success of the forbearance rate granted to the counterparty and of the legal and management costs considered upfront from the perspective of the potential buyer. The estimated recovery flows are discounted on the basis of interest rates, obtained by relying on those observed on the market in transactions involving impaired loans, considered as consistent as possible with respect to the assets to be valued.

Unlisted equity instruments

These are measured by referring to direct transactions of the same security or similar securities observed over a suitable time frame as compared to the valuation date, using the comparably company market multiples method, and subordinately using financial, income and equity valuation methods.

Investments in UCIT units, other than open-ended harmonised UCIT

These are measured on the basis of the NAV made available by the fund administrator or by the management company. These investments typically include private equity funds, real estate funds and hedge funds.

Over The Counter (OTC) Derivatives

These are measured on the basis of multiple models, depending on the type of instrument and input factors (interest rate risk, volatility, exchange rate risk, price risk, etc.) which affect their valuation. For future cash flow discounting purposes, the risk-free interest rate refers to the OIS ("Overnight Indexed Swap") curve.

In detail, for non-option instruments (such as interest rate swaps, forward rate agreements, overnight interest swaps and domestic currency swaps), the valuation techniques adopted belong to the category of "discount cash flow models", based on certain or trend-based cash flow discounting.

For option instruments, models generally accepted in market practice, such as Black & Scholes, Black-like and Hull & White, are used. In particular:

- for plain vanilla options, the methodologies most used fall within the forward risk-neutral framework and are based on analytical black-like formulas, in which volatility depends on maturity and the strike (volatility skew);
- for more complex options (such as exotic options, barrier options and autocallable options), the methodologies most used, again within the risk-neutral sphere, are based on Monte Carlo simulations, according to which the option pay-off is evaluated through simulations for a sufficiently high number of repetitions relating to the evolution over time of the risk factors underlying the option. Such models estimate the likelihood that a specific event will take place by incorporating assumptions such as the volatility of estimates or the price of the underlying instrument. The price of the derivative is therefore obtained as the discounted arithmetic average of the values obtained for each scenario.

For instruments that contain different option and non-option derivative components, the valuation is conducted by applying the appropriate valuation methodology to each instrument component.

In addition, in order to measure the fair value, several fair value adjustments are considered in order to best reflect the sale price of an actually possible market transaction. These adjustments are specifically model risk, liquidity risk and counterparty risk, illustrated here below.

<u>Model risk:</u> this adjustment is made to cover the risk that the pricing models, though validated, may generate fair values not directly observable or not immediately comparable with market prices. In general, this is the case for structured products, whose valuation is highly complex and for which the break down into elementary components which can be "summed" (host instrument and embedded derivative) may generate imprecisions in the valuation, or in the event of pricing algorithms or types of pay-offs that are particularly "exotic", which do not have a suitable degree of dissemination on the market, or in the presence of models that are highly sensitive to variables that are difficult to observe on the market.

<u>Liquidity risk</u>: this adjustment is made to take account of the size of the "bid/ask spread", i.e., the actual cost of unfreezing positions in OTC derivatives in markets with low efficiency. The effect of the liquidity risk adjustment is greater the more the product is structured, due to the related hedging/unfreezing costs, where the valuation model is not sufficiently confirmed and disseminated among operators, because this makes the valuations more random.

<u>Counterparty risk:</u> adjustments to the market value of OTC derivative instruments, classified as performing, are made in order to reflect:

- the risk of possible default by the counterparty; in this case, the adjustment is called Credit Valuation Adjustment (CVA);
- the risk of non-fulfilment of one's own contractual obligations (own credit risk), in order to calculate the Debt Valuation Adjustment (DVA).

The consideration of own credit risk in the designation of a financial liability at fair value is consistent with the valuation made for an entity that holds the same instrument as a financial asset, and is expressly envisaged by IFRS 13 (non-performance risk).

CVA and DVA are determined for each separate legal entity belonging to the Group, on the basis of the expected future exposure of the derivative instruments, the probability of default (DP) of the parties, and the relative losses (LGD). More specifically, the calculation of expected exposure takes into account the effects resulting from the existence of netting and collateral agreements, which are able to mitigate counterparty risk. Specifically, the "Credit Support Annex" (CSA) contracts negotiated with counterparties for derivative transactions govern the procedures for settling financial collateral, based on mark-to-market trends.

When estimating DP, maximum use of market parameters is made, referring to Credit Default Swap quotations, where available, against internal parameters.

The table below summarises the main types of derivatives existing in the Group, indicating the related valuation models and the main inputs.

Derivative category	Product	Valuation models	Main input of the model
Financial derivatives on interest rates	Swap	Discounted Cash Flow and Libor Convexity adjustment	Interest rate curves, interest rate volatility, interest rate correlation
	Cap - Floor	Bachelier - Analytical	
	European Swaption	Bachelier - Analytical	
	Bermuda Swaption	Hull-White one-factor mixture – Trinomial tree	
	CMS Spread Option	Bachelier - Analytical	
	CMS cap/floor/swap	Bachelier and CMS Convexity adjustment (Hagan)	
	FRA	Discounted Cash Flow – Analytical	
	Interest Rate Futures	Analytical with Hull-White one-factor convexity adjustment	
	Bond Option	Black - Analytical	
	Discounted Cash Flow - Analytical	Bond Futures and Bond Repo	
	Bond Futures option	Binomial tree	
Derivatives on inflation rates	Swap, Cap - Floor	Lognormal Forward Inflation Model - Analytical	Interest rate and inflation rate curves, interest/inflation rate volatility/correlation, calibrated on market prices
Derivatives on shares / equity indices / exchange rates	Single asset plain vanilla options	Black and Scholes - Analytical	Equity/forex volatility, interest rate and exchange rate curves, spot prices of equity indices, dividends, repo rates
	Single asset American options	Black and Scholes – Binomial tree (equity) – trinomial tree (forex)	
	European options on controlled volatility index	Local Volatility – Monte Carlo	Equity/forex volatility, interest rate and exchange rate curves, spot prices of equity indices, repo rates
	Exotic options	Black and Scholes – Monte Carlo	Equity/forex volatility, interest rate and exchange rate curves, spot prices of equity indices, dividends, repo rates, correlations
	European options on baskets	Black and Scholes /Black and Scholes Mixture - Analytical	Equity/forex/interest rate volatility, correlations, interest rates, exchange rates, spot prices of equity indices, dividends, repo rates
	American Barrier Options	Local Volatility – Monte Carlo	
	American Barrier Options on exchange rate	Trinomial tree	
	Autocallable options	Hybrid Black and Scholes, two-factor Hull and White – Monte Carlo	
	Dividend Swap and Total Return Swap	Discounted Cash Flow - Analytical	Interest rates, exchange rates, dividends, repo rates
Credit derivatives	Credit Default Swap	Discounted Cash Flow - Analytical	Interest rates, Credit Default Swap curve

The techniques and parameters for determining fair value and the criteria for assignment under the fair value hierarchy are defined and formalised in a specific fair value policy adopted by the Group. The reliability of the fair value measurements is also guaranteed by the verifications carried out by a Risk Management department. This department, which is independent from the Front Office units that hold the positions, periodically reviews the list of pricing models to be used under the Fair Value Policy: these models must represent market standards or best practices and the related calibration techniques must guarantee a result in line with valuations capable of reflecting the "current market conditions". Specifically, to correctly determine the fair value, each product is associated to a pricing model generally accepted by the market and selected based on the characteristics and market variables underlying said product. For highly complex products or in the event that the existing valuation model for the products is deemed lacking or inadequate, an internal process is launched to supplement the current models. Based on this process, the Risk Management department conducts an initial stage of validation of the pricing models, which may be native to the position keeping system or issued by a specific internal department. This is followed by a stage conducted by the same department, to guarantee constant reliability of the previously validated model.
In detail, the validation aims at verifying the theoretical robustness of the model through independent repricing, possible calibration of the parameters and comparison with counterparties' prices. If the validation is successful, the

use of the models is still subordinate to approval by specific internal committees of the Group. Following the validation stage, continuous revision is planned in order to confirm the accuracy and adherence to the market of the pricing models used by the Group, through suitable actions, if necessary, on the models and the related underlying theoretical assumptions. In order to cover the risk that the pricing models, though validated, may generate fair values not immediately comparable with market prices, a suitable adjustment will be made for "Model risk", as described above.

Financial assets and liabilities measured at amortised cost in the financial statements

For financial assets and liabilities recognised in the financial statements based on amortised cost, classified in the accounting categories of "Financial assets designated at amortised cost" (due from banks and customers) and "Liabilities designated at amortised cost" (due from banks and customers and debt securities issued), fair value is determined for reporting purposes only as required by the applicable accounting standard IFRS 7. In particular:

- for performing medium/long-term loans (mostly mortgage loans and leases), fair value is determined on the basis of cash flows, suitably adjusted for expected losses, on the basis of DP and LGD parameters. These flows are discounted using a market interest rate adjusted to take account of a premium considered to express risks and uncertainties;
- fair value for non-performing loans (bad loans, unlikely to pay and past due) is recorded as net book value. In this regard, it should be noted that the impaired loans market is characterised by significant illiquidity and a high degree of price dispersion according to the specific characteristics of the loans. The absence of observable parameters that could serve as a reference for measuring the fair value of exposures comparable to those being measured could therefore lead to a wide range of possible fair values; for this reason, for the purposes of financial reporting, the fair value of impaired loans is set at the carrying value;
- for debt securities classified in the portfolio of "Due from banks or customers" or "Debt securities", the fair value is measured by using prices obtained on active markets or valuation models, as described above in the previous paragraph "Assets and liabilities measured at fair value on a recurring basis".

For demand or short-term receivables and payables, the book value is considered a good approximation of fair value, as permitted by IFRS 7.

With regard to medium-long term performing and non-performing loans, note that the methods and the assumptions used to estimate fair value are based on subjective valuations; for this reason, the fair value shown in the financial statements for disclosure purposes only, could be significantly different to the values calculated for different purposes, just as it may not be comparable to those provided by other financial institutions.

A.4.2 Processes and sensitivity of valuations

For an examination of the techniques, inputs and valuation processes adopted by the Group for the instruments classified in level 3 of the fair value hierarchy, please refer to the previous paragraph.
Level 3 exposures amount to 1,242.9 million euro, and roughly 67.7% are represented by equity instruments and UCITS units for which no quantitative sensitivity analysis of the fair value was conducted, with respect to the change in non-observable inputs, insofar as the fair value was acquired from external sources without making any adjustment or was generated by a model with inputs specific to the entity under assessment (for example, the company's capital values) and for which alternative values cannot be reasonably envisaged.

Level 3 exposures also include, among other things, approximately 337 million euro in loans to customers which, due to their contractual characteristics, have not passed the SPPI test and must therefore be designated at fair value.
The determination of the fair value of most of these loans is based on repayment assumptions often confirmed by specific plans prepared and approved for which it would not be appropriate to envisage alternative scenarios, while the financial component linked to the discount rates applied is not very significant. Consequently, no sensitivity analysis was carried out for these loans either.

A.4.3 Fair value hierarchy

For the purpose of preparing the disclosure on transfers between levels set out in the following paragraphs, it is noted that, for securities in the hierarchy as at 30 June 2018 which had a different level of fair value than as at 1

January 2018, it was assumed that the transfer between levels occurred with regard to the balances at the beginning of the reference period.

A.4.4 Other information

It must be specified that the Group did not use the option of measuring the fair value at overall net level, in order to fully calculate the counterparty risk associated with positions in derivative contracts grouped in the same Netting, as described in the paragraph above entitled "A.4.1 Fair value levels 2 and 3: valuation techniques and input used". In the presence of collateral agreements (CSA), the exposure associated with the individual derivative is determined in relation to its marginal contribution to the expected net exposure generated by all the contracts stipulated with a given counterparty within the same CSA.

QUANTITATIVE INFORMATION

A.4.5 Fair value hierarchy

Financial assets and liabilities designated at fair value on a recurring basis

Given the above, the table below provides a breakdown of the financial assets and liabilities measured at fair value on a recurring basis, in the fair value hierarchy. As established by the previously cited standard IFRS 13, recurring valuations refer to those assets or liabilities measured at fair value in the balance sheet, on the basis of that envisaged or permitted by the relevant international accounting standards.
In this regard, note that for the Banco BPM Group, the only assets and liabilities measured at fair value on a recurring basis are financial assets and liabilities.

Financial assets/liabilities designated at fair value	30/06/2018		
	L1	L2	L3
1. Financial assets designated at fair value through profit and loss, of which	4,794,622	2,132,064	874,278
- Financial assets held for trading	4,551,299	1,970,539	1,084
- Financial assets designated at fair value	-	-	-
c) Other financial assets mandatorily at fair value	243,323	161,525	873,194
2. Financial assets designated at fair value through other comprehensive income	18,303,666	345,367	368,612
3. Hedging derivatives	-	176,497	-
Total	**23,098,288**	**2,653,928**	**1,242,890**
1. Financial liabilities held for trading	1,263,362	6,945,877	1,600
2. Financial liabilities designated at fair value	2,461,882	258,931	-
3. Hedging derivatives	-	753,379	-
Total	**3,725,244**	**7,958,187**	**1,600**

The table below, while not fully comparable, shows the fair value hierarchy of financial assets and liabilities measured at fair value on a recurring basis at 31 December 2017, in compliance with the IAS 39 accounting standard, prepared in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

	31/12/2017		
	Level 1	Level 2	Level 3
1. Financial assets held for trading	3,079,405	1,798,733	33,686
2. Financial assets designated at fair value through profit and loss	7,991	19,389	1,572
3. Financial assets available for sale	15,761,099	624,079	743,444
4. Hedging derivatives	-	243,810	-
Total	**18,848,495**	**2,686,011**	**778,702**
1. Financial liabilities held for trading	987,343	6,951,183	3,537
2. Financial liabilities designated at fair value	3,065,348	348,212	-
3. Hedging derivatives	-	765,903	-
Total	**4,052,691**	**8,065,298**	**3,537**

Financial assets designated at fair value on a recurring basis

Instruments measured significantly on the basis of non-observable parameters (Level 3) include 70.3% instruments classified in the portfolio of assets required to be measured at fair value, mainly as a result of failing the SPPI test, and 29.7% equity instruments classified in the category of "Financial assets designated at fair value through other comprehensive income"; the remainder is classified in trading assets.
More specifically, level 3 financial assets amounted to 1,242.9 million euro and are represented by the following types of investment:

- unlisted equity instruments of 581.4 million euro, mostly valued on the basis of internal equity models;
- UCIT units of 260.2 million euro, represented almost entirely by private equity funds (162.2 million euro), real estate funds (79.9 million euro) and bond funds (18.1 million euro); these funds are characterised by significant levels of illiquidity, and for which the process to evaluate the equity of the fund requires a considerable amount of assumptions and estimates;
- loans to customers of 337.4 million euro. These loans are also able to explain the increase in assets measured at fair value on a recurring basis of level 3 compared to those existing at 31 December 2017, following the application of the new classification rules provided for by the IFRS 9 accounting standard (failure to pass the SPPI test);
- debt securities amounting to 63.3 million euro, consisting mainly of structured debt securities amounting to 54 million euro;
- Over the Counter (OTC) derivatives of 0.6 million euro for which the non-observable input parameters used by the pricing model are deemed significant in order to measure the fair value.

Financial assets include 2,243.6 million euro in derivative instruments held for trading and hedging, of which almost entirely classified in hierarchy levels 1 and 2 (2,243.0 million euro equal to 99.97%). In particular:

- listed derivatives (futures and options) corresponding to 151.2 million euro, are measured on the basis of the prices provided by the Clearing Houses (level 1);
- Over The Counter (OTC) derivatives, which amount to 2,091.8 million euro, are measured on the basis of models, which use observable market parameters to a significant extent, or on the basis of prices originating from independent sources (level 2).

Financial liabilities designated at fair value on a recurring basis

Financial liabilities held for trading classified as level 1 refer to listed derivatives amounting to 164.7 million euro and to technical overdrafts on securities listed in active markets of 1,098.6 million euro; the remaining financial liabilities held for trading, corresponding to 3,850 million euro, were almost entirely classified as level 2.

Financial liabilities designated at fair value are represented by own bond issues subject to hedging by means of derivative instruments, for which the fair value option has been activated. More specifically, the securities classified as level 1, which as at 30 June 2018 represented 90.5% of the total liabilities measured at fair value (item 30 of balance sheet liabilities), consist of issues for which it was deemed that there is an active market (regulated market, electronic trading network, organised trading systems or equivalent).
Hedging derivatives have a negative fair value of 753.4 million euro and are fully classified as level 2.

Transfers between fair value levels (Level 1 and Level 2) of financial assets/liabilities designated at fair value through profit and loss on a recurring basis

In the first half of 2018, transfers from level 1 to level 2 concerned only the portfolio of "financial assets held for trading", and refer to a limited number of debt securities, amounting to 4.6 million euro (at year-end value), for which as at 30 June the conditions required by the Group's Fair Value Policy to be able to take an quoted price on an active market had not been met, as had been the case at the beginning of the year.

During the same period, transfers were made from level 2 to level 1 amounting to 55.5 million euro (value at beginning of the year) of financial assets belonging mostly (50.3 million euro) to a debt security that also belonged to the portfolio of "financial assets held for trading" and for 10.8 million euro (value at the beginning of the year) for financial liabilities related to the single issue of the parent group belonging to the portfolio of "financial liabilities designated at fair value".
This refers to a limited number of bonds for which, as at 30 June 2018, it was possible to rely on prices observed in markets considered active.

Period changes in financial assets designated at fair value on a recurring basis (level 3)

The following table shows the changes during the period in relation to financial instruments measured at fair value classified in level 3 of the fair value hierarchy. It should be noted that the opening balances reflect the balances at 1 January 2018 restated on the basis of the classification and measurement criteria introduced by the new IFRS 9 accounting standard.

	Financial assets designated at fair value through profit and loss				Financial assets designated at fair value through other comprehensive income	Hedging derivatives
	Total	of which: a) financial assets held for trading	of which: b) financial assets designated at fair value	of which: c) other financial assets mandatorily at fair value		
1. Opening balance	**768,958**	**16,297**	**-**	**752,661**	**380,398**	**-**
2. Increases	**270,219**	**5,542**	**-**	**264,677**	**1,312**	**-**
2.1. Purchases	79,424	4,965	-	74,459	145	-
2.2. Profits charged to:	66,160	10	-	66,150	1,145	-
2.2.1. Income statement	66,160	10	-	66,150	153	-
- of which capital gains	63,312	1	-	63,311	-	-
2.2.2. Shareholders' equity	-	X	X	-	992	-
2.3. Transfers from other levels	80,958	564	-	80,394	-	-
2.4. Other increases	43,677	3	-	43,674	22	-
3. Decreases	164,899	20,755	-	144,144	13,098	-
3.1. Sales	55,909	4,969	-	50,940	2,771	-
3.2. Redemptions	25,472	4	-	25,468	-	-
3.3. Losses charged to:	30,362	203	-	30,159	10,173	-
3.3.1. Income statement	30,362	203	-	30,159	13	-
- of which capital losses	30,014	203	-	29,811	-	-
3.3.2. Shareholders' equity	-	X	X	-	10,160	-
3.4. Transfers from other levels	20,565	15,565	-	5,000	-	-
3.5. Other decreases	32,591	14	-	32,577	154	-
4. Closing balance	**874,278**	**1,084**	**-**	**873,194**	**368,612**	**-**

Period changes in financial liabilities designated at fair value on a recurring basis (level 3)

	Financial liabilities held for trading	Financial liabilities designated at fair value	Hedging derivatives
1. Opening balance	**3,537**	**-**	**-**
2. Increases	**34**	**-**	**-**
2.1 Issues	-	-	-
2.2. Losses charged to:	22	-	-
2.2.1. Income statement	22	-	-
- of which capital losses	21	-	-
2.2.2. Shareholders' equity	X	-	-
2.3. Transfers from other levels	-	-	-
2.4. Other increases	12	-	-
3. Decreases	**1,971**	**-**	**-**
3.1. Redemptions	-	-	-
3.2. Buy-backs	76	-	-
3.3. Profits charged to:	4	-	-
3.3.1. Income statement	4	-	-
- of which capital gains	4	-	-
3.3.2. Shareholders' equity	X	-	-
3.4. Transfers to other levels	1,891	-	-
3.5. Other decreases	-	-	-
4. Closing balance	**1,600**	**-**	**-**

Fair value disclosure on financial assets and liabilities measured at cost

With reference to the fair value disclosure, required by IFRS 7, paragraphs 25 and 26, referred to by standard IAS 34, regarding the fair value of financial assets and liabilities recognised in the financial statements at amortised cost, please refer to the relevant tables showing the breakdown of financial assets and liabilities valued at amortised cost in “Part B – Consolidated balance sheet disclosure”.

A.5 Disclosure on day one profit/loss

Pursuant to IFRS 7 paragraph 28, please note that within financial instruments of the Group the impact in the year of the recognition of the Day 1 Profit, meaning the difference between the fair value measured upon initial recognition (transaction price) and the amount determined at that same date using a valuation technique, is of an intangible amount and is due to the issue of certificates by Banca Akros. Revenues suspended at 30 June 2018 amount to 18 thousand euro and relate to a single issue in 2016 maturing in 2021.

Disclosure on structured credit products

Note that as at 30 June 2018, the Group’s exposure to structured credit securities amounted to 1,713.6 million euro and referred to Asset Backed Securities (ABSs) deriving from third-party securitisations. In this case:

- 1,657.1 million euro in securities issued by the SPE Red Sea SPV, which the Group holds following the GACS securitisation of bad loans completed in June 2018 (senior tranche of 1,654.2 million euro; mezzanine tranche of 2.9 million euro). For more details, please refer to to the section “Application of the Group's accounting policies to completed transactions or events during the period” in Part A of Illustrative notes to the consolidated condensed interim financial statements;
- 56.5 million euro for securities relating to third-party securitisations (junior tranche for 39.7 million euro; mezzanine tranche for 5.4 million euro; senior tranche for 11.4 million euro). It should be noted that the junior exposure is almost exclusively attributable to the security issued by the company BNT Portfolio SPV (38.4 million euro); it refers in particular to the vehicle set up in 2014 to complete the securitisation of agricultural loans of Banca della Nuova Terra, financed by the issue of a single tranche of securities.

PART B - CONSOLIDATED BALANCE SHEET DISCLOSURE

The following tables are presented in the manner described in the paragraph “General preparation principles” in “A.1 - General part”.

ASSETS

Financial assets designated at fair value through profit and loss – item 20

2.1 Financial assets held for trading: breakdown by product

Items/Amounts	Total 30/06/2018		
	L1	L2	L3
A. Cash assets			
1. Debt securities	3,477,958	55,204	48
1.1 Structured securities	49,805	32,441	37
1.2 Other debt securities	3,428,153	22,763	11
2. Equity instruments	917,777	-	22
3. UCIT units	4,340	-	451
4. Loans	-	-	-
4.1 Repurchase agreements	-	-	-
4.2 Other	-	-	-
Total (A)	**4,400,075**	**55,204**	**521**
B. Derivative instruments	-	-	-
1. Financial derivatives	151,224	1,915,335	563
1.1 held for trading	151,224	1,897,965	563
1.2 connected with the fair value option	-	17,150	-
1.3 other	-	220	-
2. Credit derivatives	-	-	-
2.1 held for trading	-	-	-
2.2 connected with the fair value option	-	-	-
2.3 other	-	-	-
Total (B)	**151,224**	**1,915,335**	**563**
Total (A+B)	**4,551,299**	**1,970,539**	**1,084**

2.3 Financial assets designated at fair value: breakdown by product

As at 30 June 2018 the Group does not hold financial assets designated at fair value.

2.5 Other financial assets mandatority at fair value: breakdown by product

Items/Amounts	Total 30/06/2018		
	L1	L2	L3
1. Debt securities	46,753	116,332	63,231
1.1 Structured securities	-	-	9,200
1.2 Other debt securities	46,753	116,332	54,031
2. Equity instruments	4,804	30,912	212,829
3. UCIT units	191,766	14,281	259,741
4. Loans	-	-	337,393
4.1 Repurchase agreements	-	-	-
4.2 Other	-	-	337,393
Total	**243,323**	**161,525**	**873,194**

Financial assets designated at fair value through other comprehensive income – item 30

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

Items/Amounts	Total 30/06/2018		
	L1	L2	L3
1. Debt securities	18,050,879	231,842	-
1.1 Structured securities	-	-	-
1.2 Other debt securities	18,050,879	231,842	-
2. Equity instruments	252,787	113,525	368,612
3. Loans	-	-	-
Total	**18,303,666**	**345,367**	**368,612**

Financial assets designated at amortised cost – item 40

4.1 Financial assets designated at amortised cost: breakdown by product of loans due from banks

Transaction type/Amounts	Total 30/06/2018					
	Book value			Fair value		
	First and Second Stage	Third Stage	of which: originated or acquired impaired	L1	L2	L3
A. Due from central banks	**2,050,979**	**-**	**-**	**-**	**11,876**	**2,039,103**
1. Fixed-term deposits	-	-	-	X	X	X
2. Minimum reserve	2,018,043	-	-	X	X	X
3. Repurchase agreements	-	-	-	X	X	X
4. Other	32,936	-	-	X	X	X
B. Due from banks	**3,438,388**	**70**	**-**	**4,565**	**170,076**	**3,261,083**
1. Loans	3,258,891	70	-	-	-	3,261,083
1.1 Current accounts and sight deposits	1,022,284	70	-	X	X	X
1.2. Fixed-term deposits	137,383	-	-	X	X	X
1.3. Other loans:	2,099,224	-	-	X	X	X
- Reverse repurchase agreements	313,798	-	-	X	X	X
- Financial leases	2,236	-	-	X	X	X
- Other	1,783,190	-	-	X	X	X
2. Debt securities	179,497	-	-	4,565	170,076	-
2.1 Structured securities	-	-	-	-	-	-
2.2 Other debt securities	179,497	-	-	4,565	170,076	-
Total	**5,489,367**	**70**	**-**	**4,565**	**181,952**	**5,300,186**

4.2 Financial assets designated at amortised cost: breakdown by product of loans to customers

Transaction type/Amounts	Total 30/06/2018					
	Book value			Fair value		
	First and Second Stage	Third Stage	of which: originated or acquired impaired	L1	L2	L3
1. Loans	**95,583,531**	**9,493,185**	**1,370,131**	**-**	**-**	**109,855,718**
1.1. Current accounts	10,932,155	1,267,392	289,785	X	X	X
1.2. Reverse repurchase agreements	7,126,565	-	-	X	X	X
1.3. Mortgage loans	56,033,410	4,721,772	863,894	X	X	X
1.4. Credit cards, personal loans and salary-backed loans	2,131,518	20,095	4,093	X	X	X
1.5. Financial leases	1,200,905	1,215,979	-	X	X	X
1.6. Factoring	94,630	83	83	X	X	X
1.7. Other loans	18,064,348	2,267,864	212,276	X	X	X
2. Debt securities	**15,528,231**	**-**	**-**	**13,246,660**	**279,257**	**1,734,477**
2.1. Structured securities	-	-	-	-	-	-
2.2. Other debt securities	15,528,231	-	-	13,246,660	279,257	1,734,477
Total	**111,111,762**	**9,493,185**	**1,370,131**	**13,246,660**	**279,257**	**111,590,195**

As at 30 June 2018, the breakdown into risk stages of loans to customers is given in the table below:

Exposure types/risk stages	First Stage	Second Stage	Third Stage	Total
Bad loans	-	-	3,613,074	3,613,074
Unlikely to pay	-	-	5,808,344	5,808,344
Past due - non-performing	-	-	71,767	71,767
Non-performing loans	**-**	**-**	**9,493,185**	**9,493,185**
Performing loans	**82,003,353**	**13,580,178**	**-**	**95,583,531**
Total loans to customers	**82,003,353**	**13,580,178**	**9,493,185**	**105,076,716**

The tables below, while not fully comparable, show the breakdown by product of the portfolios of IAS 39 financial assets at 31 December 2017, prepared in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

Financial assets held for trading: breakdown by product

Items/Amounts	31/12/2017		
	L1	L2	L3
A. Cash assets			
1. Debt securities	2,223,393	42,230	18,288
1.1 Structured securities	80,398	20,293	18,175
1.2 Other debt securities	2,142,995	21,937	113
2. Equity instruments	692,974	-	30
3 UCIT units	29,009	-	652
4. Loans	-	-	-
4.1 Reverse repurchase agreements	-	-	-
4.2 Other	-	-	-
Total A	**2,945,376**	**42,230**	**18,970**
B. Derivative instruments			
1. Financial derivatives:	134,029	1,756,503	14,716
1.1 held for trading	134,029	1,710,374	14,716
1.2 connected with the fair value option	-	46,121	-
1.3 other	-	8	-
2. Credit derivatives:	-	-	-
2.1 held for trading	-	-	-
2.2 connected with the fair value option	-	-	-
2.3 other	-	-	-
Total B	**134,029**	**1,756,503**	**14,716**
Total (A+B)	**3,079,405**	**1,798,733**	**33,686**

Financial assets designated at fair value: breakdown by product

Items/Amounts	Total 31/12/2017		
	L1	L2	L3
1. Debt securities	7,991	-	1,421
1.1 Structured securities	-	-	1,421
1.2 Other debt securities	7,991	-	-
2. Equity instruments	-	579	-
3. UCIT units	-	18,810	151
4. Loans	-	-	-
4.1 Structured	-	-	-
4.2 Other	-	-	-
Total	**7,991**	**19,389**	**1,572**

Financial assets available for sale: breakdown by product

Items/Amounts	31/12/2017		
	L1	L2	L3
1. Debt securities	15,312,293	400,657	3,712
1.1 Structured securities	-	-	1,420
1.2 Other debt securities	15,312,293	400,657	2,292
2. Equity instruments	275,632	223,422	494,419
2.1 Designated at fair value	275,632	223,422	491,713
2.2 Designated at cost	-	-	2,706
3. UCIT units	173,174	-	245,313
4. Loans	-	-	-
Total	**15,761,099**	**624,079**	**743,444**

Investments held to maturity: breakdown by product

	Total 31/12/2017			
	Book value	Fair Value		
		Level 1	Level 2	Level 3
1. Debt securities	11,560,769	11,685,005	-	-
- structured	-	-	-	-
- other	11,560,769	11,685,005	-	-
2. Loans	-	-	-	-
Total	**11,560,769**	**11,685,005**	**-**	**-**

Due from banks: breakdown by product

Transaction type/Amounts	Total 31/12/2017			
	Book value	Fair Value		
		Level 1	Level 2	Level 3
A. Due from Central Banks	**2,001,231**	**-**	**-**	**2,001,231**
1. Time deposits	-	X	X	X
2. Minimum reserve	1,992,298	X	X	X
3. Reverse repurchase agreements	-	X	X	X
4. Other	8,933	X	X	X
B. Due from banks	**3,163,484**	**-**	**228,807**	**2,927,937**
1. Loans	2,937,992	-	-	2,927,937
1.1 Current accounts and demand deposits	979,528	X	X	X
1.2 Time deposits	208,181	X	X	X
1.3 Other loans:	1,750,283	X	X	X
- Reverse repurchase agreements	94,612	X	X	X
- Financial leases	2,426	X	X	X
- Other	1,653,245	X	X	X
2. Debt securities	225,492	-	228,807	-
2.1 Structured securities	-	X	X	X
2.2 Other debt securities	225,492	X	X	X
Total	**5,164,715**	**-**	**228,807**	**4,929,168**

Loans to customers: breakdown by product

Transaction type/Amounts	Total 31/12/2017					
	Book value			Fair Value		
	Performing	Non-performing		L1	L2	L3
		Acquired	Other			
Loans	**94,715,812**	**-**	**13,026,867**	**-**	**-**	**109,600,355**
1. Current accounts	11,679,207	-	1,651,988	X	X	X
2. Reverse repurchase agreements	6,364,149	-	-	X	X	X
3. Mortgage loans	55,589,969	-	7,073,545	X	X	X
4. Credit cards, personal loans and salary-backed loans	2,077,127	-	22,816	X	X	X
5. Financial leases	1,203,993	-	1,416,729	X	X	X
6. Factoring	87,923	-	79	X	X	X
7. Other loans	17,713,444	-	2,861,710	X	X	X
Debt securities	**428,203**	**-**	**5,500**	**24,952**	**125,372**	**284,392**
8. Structured securities	-	-	5,000	X	X	X
9. Other debt securities	428,203	-	500	X	X	X
Total	**95,144,015**	**-**	**13,032,367**	**24,952**	**125,372**	**109,884,747**

Investments in associates and companies subject to joint control - item 70

Investments in associates and companies subject to joint control as at 30 June 2018 amounted to 1,355.1 million euro, compared with 1,349.2 million euro as at 31 December 2017.

Regarding the streamlining process of the Bancassurance sector, in March the purchase of 50% of Avipop Assicurazioni and Popolare Vita was completed, amounting to a total value of 803.4 million euro.
On the same date, the sale of 65% of the share capital of the same subsidiaries was completed for the amount, net of costs to sell, of 813 million euro, with a total economic effect of 174.7 million euro.
As at 31 December 2017, the interests held in the two companies were classified as 35% under "investments in associates and companies subject to joint control" and the remainder (15% of Popolare Vita and 14.999% of Avipop, for a total of 78.8 million euro) under "Non-current assets and asset disposal groups held for sale".

The other changes recorded in the half-year also include the impact resulting from the valuation of investments in associated companies using the equity approach, relating to the share of the results recorded by the same in the period (+76.0 million euro); the effects of the reduction of capital of Agos Ducato (-86.6 million euro), Vera Vita (-110.2 million euro), Vera Assicurazioni (-10.6 million euro), Bipiemme Vita (-3.5 million euro), Factorit (-2.3 million euro) and Etica Sgr (-0.6 million euro) following the distribution of dividends; as well as changes attributable to the Group in the reserves of these companies, relating to the FTA reserves relating to the impact of the introduction of IFRS 9 (-92.3 million euro) and valuation reserves (-3.6 million euro).

Property and equipment – item 90

9.1 Property and equipment used in operations: breakdown of assets designated at cost

Asset/Amounts	Total 30/06/2018	Total 31/12/2017
1. Owned assets	**1,458,404**	**1,477,052**
a) land	469,947	469,996
b) buildings	831,416	843,225
c) furniture	47,852	51,237
d) electronic systems	55,798	53,460
e) other	53,391	59,134
2. Assets acquired under financial lease	**261**	**268**
a) land	-	-
b) buildings	261	268
c) furniture	-	-
d) electronic systems	-	-
e) other	-	-
Total	**1,458,665**	**1,477,320**

9.2 Property and equipment held for investment purposes: breakdown of assets designated at cost

Asset/Amounts	Total 30/06/2018	Total 31/12/2017
Owned assets		
a) land	565,007	565,261
b) buildings	709,603	692,601
Total	**1,274,610**	**1,257,862**

Intangible assets – item 100

10.1 Intangible assets: breakdown by asset type

Asset/Amounts	Total 30/06/2018		Total 31/12/2017	
	Duration defined	Indefinite duration	Duration defined	Indefinite duration
A.1 Goodwill	**-**	**76,389**	**-**	**76,389**
A.1.1 attributable to the group	-	76,389	-	76,389
A.1.2 attributable to minority interests	-	-	-	-
A.2 Other intangible assets	**714,535**	**504,272**	**716,499**	**504,272**
A.2.1 Assets designated at cost	714,535	504,272	716,499	504,272
a) Internally generated intangible assets	-	-	-	-
b) Other assets	714,535	504,272	716,499	504,272
A.2.2 Assets designated at fair value	-	-	-	-
a) Internally generated intangible assets	-	-	-	-
b) Other assets	-	-	-	-
Total	**714,535**	**580,661**	**716,499**	**580,661**

Intangible assets with an indefinite useful life: impairment testing to determine whether there has been a permanent loss in value

As at 30 June 2018, the Group's residual intangible assets with an indefinite useful life amounted to 580.7 million euro, 76.4 million euro is represented by goodwill and 504.3 million euro by trademarks.

Goodwill as at 30 June 2018 was allocated to the "Bancassurance Protezione" (51.1 million euro) and "Bancassurance Vita" (25.1 million euro) CGUs (in addition to a marginal amount relating to the investee Arena Broker).

During the period there were no changes in the CGUs indicated and, therefore, these represent values in line with the residual values as at 31 December 2017.

For the purpose of this interim financial Report, a survey was carried out to identify the existence of any impairment indicators other than those already considered for the purposes of the test conducted at 31 December 2017.

Specifically, for the purpose of the impairment test of the insurance CGUs carried out at 31 December 2017, the fair value determined by the valuation implicit in the price agreed for the sale to Cattolica Assicurazioni of 65% of the equity investments in Popolare Vita (now Vera Vita) and Avipop Assicurazioni (now Vera Assicurazioni) was taken as reference.
Given the substantial confirmation of these values both at the time of the sale at the end of March and following the evidence that emerged from the process of price verification by the buyer, there are no elements that could constitute indicators of impairment of the goodwill recorded.

Other intangible assets with an indefinite useful life are represented by the value of trademarks allocated to the following CGUs:

- Commercial Network for 222 million euro
- BPM for 263 million euro
- Banca Akros for 19 million euro.

The trademark allocated to the Commercial Network refers to the merger transactions carried out in previous years by the former Banco Popolare and was valued, for the purposes of the impairment test conducted at 31 December 2017, together with the goodwill allocated to the same CGU using the Dividend Discount Model.
During the first half of 2018, the cost of capital, determined using the Capital Asset Pricing Model (CAPM) method, was 9.07%, slightly lower than at 31 December 2017 (9.22%).

The trademarks of BPM and Banca Akros (recognised during the Purchase Price Allocation process carried out following the merger between Banco Popolare and BPM) were valued at 31 December 2017 based on the royalties that the brand owner would receive from the sale of the brand to third parties.

From review illustrated above, no results emerged which would require early impairment testing; therefore, the estimated recovery value of intangible assets with an indefinite useful life has not been updated.

Note that assessing the existence or otherwise of effective impairment indicators, especially in a turbulent economic or market scenario such as the present one, is a particularly difficult exercise that requires a high level of judgement and that implies the use of estimates and assumptions, which may have to be changed in the future in the light of information that may become available or unexpected developments as at the date of preparation of this Report. In the second half of the year, the Group will conduct continuous monitoring in order to identify any facts or circumstances which could shed doubt on the recoverability of book values, in any event, the impairment test will be formally conducted at the time of preparation of the financial statements as at 31 December 2018.

LIABILITIES

Financial liabilities designated at amortised cost – item 10

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

Transaction type/Group components	Total 30/06/2018				Total 31/12/2017			
	BV	Fair Value			BV	Fair Value		
		L1	L2	L3		L1	L2	L3
1. Due to central banks	**21,281,339**	X	X	X	**21,383,001**	X	X	X
2. Due to banks	**10,269,213**	X	X	X	**5,816,303**	X	X	X
2.1 Current accounts and sight deposits	577,241	X	X	X	594,482	X	X	X
2.2 Fixed-term deposits	212,597	X	X	X	187,645	X	X	X
2.3 Loans	9,275,040	X	X	X	4,746,234	X	X	X
2.3.1 Repurchase agreements payable	8,157,457	X	X	X	3,534,794	X	X	X
2.3.2 Other	1,117,583	X	X	X	1,211,440	X	X	X
2.4 Payables for commitment to repurchase own capital instruments	-	X	X	X	-	X	X	X
2.5 Other payables	204,335	X	X	X	287,942	X	X	X
Total	**31,550,552**	**-**	**-**	**31,777,068**	**27,199,304**	**-**	**-**	**27,197,795**

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

Transaction type/Group components	Total 30/06/2018				Total 31/12/2017			
	BV	Fair Value			BV	Fair Value		
		L1	L2	L3		L1	L2	L3
1. Current accounts and demand deposits	77,231,654	X	X	X	77,390,766	X	X	X
2. Fixed-term deposits	2,690,423	X	X	X	3,598,192	X	X	X
3. Loans	6,956,952	X	X	X	5,296,507	X	X	X
3.1 repurchase agreements payable	5,820,312	X	X	X	4,180,122	X	X	X
3.2 Other	1,136,640	X	X	X	1,116,385	X	X	X
4. Payables for commitment to repurchase own capital instruments	-	X	X	X	-	X	X	X
5. Other payables	780,590	X	X	X	1,562,681	X	X	X
Total	**87,659,619**	**-**	**-**	**87,659,619**	**87,848,146**	**-**	**-**	**87,848,146**

1.3 Financial liabilities designated at amortised cost: breakdown by product for debt securities issued

Security type/Amounts	Total 30/06/2018			
	BV	Fair Value		
		L1	L2	L3
A. Securities				
1. Bonds	14,756,468	12,881,042	1,888,871	93,736
1.1 structured	-	-	-	-
1.2 other	14,756,468	12,881,042	1,888,871	93,736
2. Other securities	368,699	-	364,175	4,453
2.1 structured	-	-	-	-
2.2 other	-	-	-	-
Total	**15,125,167**	**12,881,042**	**2,253,046**	**98,189**

The table below, while not fully comparable, shows the breakdown by product of the IAS 39 debt securities issued at 31 December 2017, prepared in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

Debt securities issued: breakdown by product

Security type/Amounts	Total 31/12/2017			
	Book Value	Fair Value		
		Level 1	Level 2	Level 3
A. Securities				
1. Bonds	15,481,103	13,047,720	2,876,324	-
1.1 structured	-	-	-	-
1.2 other	15,481,103	13,047,720	2,876,324	-
2. Other securities	767,040	-	767,040	-
2.1 structured	-	-	-	-
2.2 other	767,040	-	767,040	-
Total	**16,248,143**	**13,047,720**	**3,643,364**	**-**

Financial liabilities held for trading – item 20

2.1 Financial liabilities held for trading: breakdown by product

Transaction type/Amounts	Total 30/06/2018					Total 31/12/2017				
	NV	Fair Value			Fair value *	NV	Fair Value			Fair value *
		L1	L2	L3			L1	L2	L3	
A. Cash liabilities										
1. Due to banks	2,839	3,661	-	-	3,661	2,126	6,176	-	-	6,176
2. Due to customers	1,091,138	1,094,953	-	-	1,094,953	775,890	816,729	-	-	816,729
3. Debt securities	3,911,997	-	3,848,464	1,592	3,850,056	4,002,847	-	3,951,586	1,646	3,953,232
3.1 Bonds	-	-	-	-		-	-	-	-	-
3.1.1 Structured	-	-	-	-	X	-	-	-	-	X
3.1.2 Other bonds	-	-	-	-	X	-	-	-	-	X
3.2 Other securities	3,911,997	-	3,848,464	1,592	3,850,056	4,002,847	-	3,951,586	1,646	3,953,232
3.2.1 Structured	3,911,997	-	3,848,464	1,592	X	4,002,847	-	3,951,586	1,646	X
3.2.2 Other	-	-	-	-	X	-	-	-	-	X
Total A	**5,005,974**	**1,098,614**	**3,848,464**	**1,592**	**4,948,670**	**4,780,863**	**822,905**	**3,951,586**	**1,646**	**4,776,137**
B. Derivative instruments										
1. Financial derivatives	X	164,748	3,096,264	8		X	164,438	2,996,770	1,891	
1.1 held for trading	X	164,748	3,074,089	-	X	X	164,438	2,942,754	1,891	X
1.2 connected with the fair value option	X	-	21,643	8	X	X	-	53,728	-	X
1.3 Other	X	-	532	-	X	X	-	288	-	X
2. Credit derivatives	X	-	1,149	-		X	-	2,827	-	
2.1 held for trading	X	-	1,149	-	X	X	-	2,827	-	X
2.2 connected with the fair value option	X	-	-	-	X	X	-	-	-	X
2.3 Other	X	-	-	-	X	X	-	-	-	X
Total B	**X**	**164,748**	**3,097,413**	**8**	**X**	**X**	**164,438**	**2,999,597**	**1,891**	**X**
Total (A+B)	**X**	**1,263,362**	**6,945,877**	**1,600**	**X**	**X**	**987,343**	**6,951,183**	**3,537**	**X**

(*) Fair value calculated excluding changes in value due to changes in the issuer's creditworthiness with respect to the issue date.

Financial liabilities designated at fair value – item 30

3.1 Financial liabilities designated at fair value: breakdown by product

Transaction type/Amounts	Total 30/06/2018				
	NV	Fair value			Fair value *
		L1	L2	L3	
1. Due to banks	**-**	**-**	**-**	**-**	**-**
1.1 Structured	-	-	-	-	X
1.2 Other	-	-	-	-	X
of which:					#RIF!
- commitments to disburse funds	-	X	X	X	X
- financial guarantees given	-	X	X	X	X
2. Due to customers	**-**	**-**	**-**	**-**	**-**
2.1 Structured	-	-	-	-	X
2.2 Other	-	-	-	-	X
of which:					-
- commitments to disburse funds	-	X	X	X	X
- financial guarantees given	-	X	X	X	X
3. Debt securities	**2,732,905**	**2,461,882**	**258,931**	**-**	**2,738,519**
3.1 Structured	-	-	-	-	X
3.2 Other	2,732,905	2,461,882	258,931	-	X
Total	**2,732,905**	**2,461,882**	**258,931**	**-**	**2,738,519**

(*) Fair value calculated excluding changes in value due to changes in the issuer's creditworthiness with respect to the issue date.

The table below, while not fully comparable, shows the breakdown by product of the IAS 39 financial liabilities designated at fair value at 31 December 2017, prepared in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

Financial liabilities designated at fair value: breakdown by product

Transaction type/Amounts	31/12/2017				
	NV	FV			FV*
		L1	L2	L3	
1. Due to banks	**-**	**-**	**-**	**-**	**-**
1.1 Structured	-	-	-	-	x
1.2 Other	-	-	-	-	x
2. Due to customers	**-**	**-**	**-**	**-**	**-**
2.1 Structured	-	-	-	-	x
2.2 Other	-	-	-	-	x
3. Debt securities	**3,454,501**	**3,065,348**	**348,212**	**-**	**3,435,418**
3.1 Structured	-	-	-	-	x
3.2 Other	3,454,501	3,065,348	348,212	-	x
Total	**3,454,501**	**3,065,348**	**348,212**	**-**	**3,435,418**

(*) Fair value calculated excluding changes in value due to changes in the issuer's creditworthiness with respect to the issue date.

Employee termination indemnities and provisions for risks and charges – items 90 and 100

As at 30 June, liability provisions amount to 1,532.0 million euro (figure of 1,461.0 million euro last 31 December) and include the provisions for employee severance indemnities of 396.2 million euro (408.2 million euro at the end of last year), retirement plans of 159.5 million euro (166.8 million euro as at 31 December 2017), risk provisions for commitments and guarantees given of 120.6 million euro (under the item "Other liabilities" in 2017 for 119.5 million euro) and other provisions for risks and charges of 855.7 million euro (figure of 886.0 million euro at the end of 2017).

The latter include:

- provisions for personnel expenses of 529.1 million euro, primarily attributable to allocations to the Solidarity Funds relating to agreements for voluntary personnel redundancy plans;
- the foreseeable charges connected with certain transactions linked with operations with customers and possible developments in the interpretation of certain regulations governing banking activities. Considering that a precise indication of the allocations could seriously prejudice the position of the company in the management of disputes connected with potential liabilities subject to valuation, as permitted by paragraph 92 of the international accounting standard of reference (IAS 37), for some cases no analytical indication has been provided regarding the amount of the allocations existing within the provisions for risks and charges and the allocations charged to the profit and loss account.

10.1 Provisions for risks and charges: breakdown

Items/Components	30/06/2018
1. Provisions for credit risk relating to commitments and financial guarantees given	67,925
2. Provisions for other commitments and guarantees given	52,739
3. Company pension funds	159,489
4. Other provisions for risks and charges	855,690
4.1 Legal and tax disputes	171,747
4.2 Personnel expenses	529,053
4.3 Other	154,890
Total	**1,135,843**

As at 31 December 2017, provisions for risks and charges were broken down as follows:

Items/Components	31/12/2017
1. Company pension funds	166,847
2. Other provisions for risks and charges	885,982
2.1 legal disputes	166,207
2.2 personnel expenses	611,208
2.3 other	108,567
Total	**1,052,829**

Details are provided below on the main pending legal proceedings and the main disputes outstanding with the Tax Authority.

Risks associated with pending legal proceedings

The Group operates in a legal and regulatory scenario, which exposes it to a wide variety of legal proceedings, relating, for example, to the conditions applied to its customers, to the nature and characteristics of the products and financial services it sells, to administrative irregularities, to clawback actions for bankruptcies, and to labour law disputes. The relative risks undergo a specific analysis by the Group, with a view to make specific allocations to provisions for risks and charges, if the disbursement is retained likely, on the basis of the information available. As indicated in the paragraph entitled "Uncertainties with regard to the use of estimates for drawing up the interim financial statements", to which we refer, the complexity of the situations and of corporate operations which are behind disputes imply considerable elements of subjective judgment, which may regard both what may be due and whether it is due and how much time will elapse before liabilities materialise.
The following paragraphs illustrate the main legal disputes in progress at the end of the half year, characterised by highly complex profiles and/or significant potential outlay, merely for the purpose of illustrating the maximum risk exposure, regardless of the Group's opinion as the likelihood of losing the dispute. For many of these proceedings, the Group actually believes that the risk profiles of the same are limited and therefore, as they regard possible liabilities, it has not made any allocation to provisions; with regard to liabilities considered probable, a disclosure of said judgment and on the amount of the allocation made is provided only if this will not prejudice the outcome of the dispute with the counterparty, in court or as regards the settlement. In this regard, we must emphasise that, although the estimates made by the Group are retained reliable and compliant with the reference accounting standards, we

cannot however exclude that the costs that will emerge to settle disputes may be different, also in regard to significantly higher amounts, than the allocations made.

Raffaele Viscardi S.r.l.

The law suit, notified on 30 April 2009 and which has a *petitum* of around 46 million euro, concerns the operations of a branch in Salerno relating to the granting of agricultural loans to the plaintiff company, which alleges that it was led to subscribe bank bonds to guarantee the sums disbursed and claims damages to its image due to reporting in the Italian Central Credit Register. On 5 May 2015, the Court of Salerno issued a ruling in favour of the bank, in response to which the opponent submitted an appeal.

Maflow SpA in Extraordinary Receivership

In a notice dated 14 April 2014, Maflow S.p.A., in extraordinary receivership, summoned the former Banco Popolare before the court, requesting: (i) a court order, together with others, to pay compensation for damages of 199 million euro, corresponding to the financial difficulties of Maflow, as calculated by the counterparty; (ii) a court order to return the amount allegedly received by the bank unlawfully from loans granted to Maflow from establishment to default. The above is all based on the assumption that the bank played a dominant role by influencing the financial management of Maflow.
In a ruling dated 14 December 2016, which was then appealed against, the Court of Milan totally rejected the claims of the petitioner in these Proceedings, also ordering the same to pay legal expenses.

Administrative Proceedings

On 17 July 2014, the former Banco Popolare received a formal written notice, insofar as jointly and severally obliged with those potentially responsible for the infringement, regarding the alleged infringement of anti-money laundering legislation (Italian legislative Decree no. 231/2007). The accusation regards the failure to report a transaction retained as suspicious, following inspections conducted by the Finance Police; the matter in question dates back to 2009 and regards the paying in of 41 non-transferable banker's drafts for a total amount of 10.1 million euro.

Porta Vittoria Bankruptcy

This company, part of the Coppola Group, was declared bankrupt by the Court of Milan on 29 September 2016. The bank's credit came to 225.1 million euro in total, 219.5 million euro of which was attributable to mortgage loans and 5.6 million euro to current account overdrafts generated by the differentials on a derivative instrument in place with Porta Vittoria. The bank submitted a petition to be admitted as a creditor, and the Bankruptcy Judge, in line with the proposal of the Receiver, admitted the mortgage credit with subordination to all the other creditors and with mortgage privilege only with respect to other subordinated creditors. The receivable from a derivative was regularly and fully admitted as unsecured. Deeming the measure groundless, the bank challenged the statement of liabilities, requesting the admission of its receivable from the mortgage loan without subordination.
The opposition to the statement of liabilities is still pending.

Bankruptcy of Tikal S.r.l. in liquidation/Release S.p.A.

On 5 April 2017, the Bankruptcy of Tikal S.r.l. in liquidation, former tenant of the property in which the activities of Hotel Cicerone in Rome were carried out, summoned Release and Cicerone S.a.r.l. (a company incorporated under the laws of Luxembourg belonging to the Coppola Group) before the court to obtain compensation for damages for tortious liability for a total of 19.9 million euro due to the non-recognition of goodwill indemnity and for the alleged loss in value of the company, due to the return of the leased property before the expiry of the rental agreement. The early return resulted from the expiry of the lease agreement in place between Release Spa and Cicerone S.a.r.l..
The summons was followed by the request of Release S.p.A. for admission as a creditor due to its occupancy compensation receivable; the demand was accepted by the Court, which recognised the receivable, in part also with preferential status.

Cicerone S.a r.l.

On 21 November 2017, Cicerone S.a r.l. summoned Release and Banco BPM, challenging the invalidity of the debt restructuring agreement entered into with Release on 19 October 2010, which originates from the leasing contract for the "Hotel Cicerone" hotel complex in Rome. The counterparty requested that the original finance lease dated 29 November 2004 be declared in force, in addition to compensation for the damages allegedly suffered, quantified at approximately 45 million euro. On 13 April 2018, the Bankruptcy of Porta Vittoria intervened in the proceedings, supporting the position of the plaintiff.

This lawsuit is in line with the action taken in August 2015 by Cicerone S.a.r.l. and Porta Vittoria S.p.A. against the same defendants, which was dismissed in March 2017 for failure to resume proceedings following the declaration of bankruptcy of Porta Vittoria.

Bankruptcy of Trafileria del Lario S.p.A. in liquidation

On 12 October 2017, the Bankruptcy of Trafileria del Lario S.p.A. in liquidation (formerly Trafilerie Brambilla S.p.A.) served a writ of summons citing independent claims for damages both against the company's former statutory auditors and directors and against Banco BPM and other credit institutions. The grievances referring to the banking class involved are substantiated in the alleged aggravation of the company failure, in collaboration with the directors and statutory auditors themselves, determined by the continuation of business activities in a situation of insolvency and abusive access to credit via false invoices. Based on the reconstruction of the treatment, this behaviour caused damages to the company to the tune of 25 million.

Lucchini S.p.A.

On 23 March 2018, the extraordinary receivership of Lucchini S.p.A. summoned a number of banks jointly and severally, including Banco BPM, to obtain damages totalling approximately 351 million euro.

The legal proceedings originate from the events that led to the economic and financial collapse of the company, which culminated in it being placed under extraordinary receivership in December 2012. Specifically, the banks are retained responsible for the alleged damages caused to Lucchini following the signing and execution of the restructuring agreement pursuant to Art. 182-*bis* of the bankruptcy law, which was formalised in December 2011 and approved by the Court of Milan in February 2012.

Civil and criminal proceedings relating to the Bankruptcies of the Dimafin Group

The Banco BPM Group has been involved in a number of civil disputes brought by the receivers, the former members of the Board of Directors and the owner of the Dimafin Group, as well as in criminal proceedings relating to the default of the same business group.

On 22 November 2017, a settlement agreement was finalised and then executed, allowing the 9 civil proceedings brought by the receivers of the Bankruptcy of the Di Mario Group and by the former management of the bankrupt companies to be dropped and also the revocation of the civil action, already formalised, in the criminal proceedings instituted following the default of the Di Mario group, with the release of the sums previously seized from the Bank at the request of the Rome Public Prosecutor's Office.

The scope of the transaction does not include the case filed by the owners of the Dimafin Group, represented by Mr. Raffaele Di Mario, against 23 parties, including numerous credit institutions, requesting that the same be found jointly liable for the alleged fraudulent and negligent conduct of the parties summoned, retained responsible for the financial difficulties of the Dimafin Group companies and the consequent bankruptcy of the same. According to the plaintiff, said conduct is alleged to have brought the value of the shareholdings held by the claimant to zero, which is why Mr. Di Mario is claiming compensation of 700 million euro.

Furthermore, in December 2017, the Bankruptcy of Mr. Raffaele Di Mario, as owner and lender of the parent company Dimafin S.p.A., served a summons to Banco BPM and Release, as well as other credit institutions, to acknowledge the liability of the banks for aggravating Mr. Raffaele Di Mario's state of insolvency. According to the plaintiff's, the greatest instability was caused by the granting of credit to companies for which Di Mario had issued guarantees. The grievances therefore show damages, estimated at 8.9 million euro, allegedly caused to all the creditors of the insolvent for the lower satisfaction of their claims. The citation also aims to obtain a declaration of invalidity for the guarantees issued by the entrepreneur, linked to the restructuring plan drawn up for the Dimafin Group.

Ittierre S.p.A. former Banco Popolare

The company was placed under extraordinary receivership. By means of a summons, both the former Banca Popolare di Lodi (BPL) and the former Banca Popolare di Novara S.p.A. (BPN) were requested to return, pursuant to Art. 67 of the Finance Law, the total sum of 16.6 million euro for the principal creditor and 4.9 million euro for the secondary creditor. An objection was raised as to the erroneous duplication of the request, which in reality referred to the same current account migrated from BPL to BPN following the swap of branches. Furthermore, the grounds of the request were challenged, due to the imprecision of the same insofar as the counterparty had not specified which remittances were being disputed. As regards the former BPN dispute, the judge is still currently being replaced and for the other, a court-appointed expert witness excluded the existence of revocable remittances to return the amounts, which was a positive development for the outcome of the case. Pending the negotiations, the hearing for the conclusions was postponed. Last March, a comprehensive settlement agreement was finalised with the Extraordinary Receivership procedures of Ittierre S.p.A., It Holding S.p.A. and Malo S.p.A. to settle all the revocation proceedings pending between the parties with a total disbursement of 200,000 euro.

Ittierre S.p.A former Banca Popolare di Milano
The company was placed under extraordinary receivership. The extraordinary receivership submitted a petition requesting the return of 30.9 million euro pursuant to Art. 67 of the Bankruptcy Law. The court-appointed expert witness in accounting deemed remittances of only 35,000 euro revocable, a positive development for the outcome of the case. The hearing for the conclusions was postponed, pending negotiations.

Impresa S.p.A former Banca Popolare di Milano
Company in Extraordinary Receivership. The extraordinary receivership procedure called the pool of banks, in which BPM participated to an extent of only 8%, as well as the directors of the company, before the Court of Rome for compensation for damages quantified jointly and severally at 166.9 million euro. The hearing for the submission of evidence is scheduled for the end of October 2018.

Send S.r.l.
The company went bankrupt in 2009. The receivable results from a pool operation of 49.5 million euro with the Unicredit head office, addressed to the construction of a shopping centre in Vicenza and secured by a mortgage at the same level on the property complex funded. The former Banco's share was 28.80%. The pool receivables (and therefore also the former Banco's) have been regularly admitted to the bankruptcy proceedings due to the mortgage privilege.
The bankruptcy receiver filed a claim for damages against the Pool Banks for the amount of the loan. In 2015, the Court assigned to the receivership stated its lack of jurisdiction. The receivership proceedings resumed before the Court of Venice, business section, the conclusions were set out and the case was held back by a decision.

Risks associated with current disputes with the Tax Authority

Banco BPM, the companies that merged to form the same, the incorporated subsidiary companies and the subsidiary companies underwent various inspections by the Tax Authority in 2018 and in previous years. These activities concerned the taxable income declared for the purpose of income tax, VAT, registration tax, and more generally the manner in which the tax legislation in force at the time was applied. As a consequence of said inspections, the Banco BPM Group is involved in numerous legal proceedings.

The potential liabilities relating to tax disputes under way that involve Banco BPM and its subsidiaries amounted to 333.4 million euro as at 30 June 2018 (332.7 million euro as at 31 December 2017), of which 306.8 million euro relate to notices of assessment, tax demands and payment notices and 26.6 million euro relate to formal reports on findings served or to be served (based on the daily reports on findings for the inspection currently under way). In this regard, note that the estimate of said potential liabilities relating to the notices of assessment does not consider any interest (with the exception of the assessments relating to 2005 of the former Banca Popolare Italiana and for liabilities classified as likely), while the estimate of potential liabilities relating to formal reports on findings served or to be served does not include interest or fines, insofar as they are not indicated in the latter document (with the exception of liabilities classified as likely).

Developments during the period

No new disputes arose during the period and no existing ones were terminated or settled.
The following paragraph provides a breakdown of the main tax disputes outstanding at 30 June 2018.

Disputes relating to Banco BPM

- Banco BPM (former Banca Popolare di Verona e Novara Soc. Coop.) - tax demand regarding IRAP tax paid to the Regional headquarters for Veneto for 2006. The claim refers to the application of the ordinary rate of 4.25% to the net value of production resulting from business activities performed in Veneto and in Tuscany, instead of the higher rate of 5.25% and amounts to a total of 7.1 million euro. An appeal has been submitted for this tax demand. The Provincial Tax Commission partially admitted the appeal and declared that the fines requested were not due. The Regional Tax Commission confirmed the ruling of the court of first instance, therefore cancelling the tax claim relating to higher IRAP regarding the Tuscany Regional Authority. An appeal submitted to the Supreme Court is still pending.
- Banco BPM (former Banca Popolare Italiana Soc. Coop.) - notice of settlement regarding registration tax relating to the reclassification of the disposal of a portfolio of securities made in 2002 between Cassa di Risparmio di Pisa and Banca Popolare Italiana as a business segment disposal. The claims amount to 14.5 million euro. In a ruling dated 18 October 2011, the Regional Tax Commission of Florence fully upheld the appeal submitted by the former Banco Popolare. An appeal submitted to the Supreme Court is still pending.
- Banco BPM (former Banca Popolare Italiana Soc. Coop.) - notices of assessment relating to tax year 2005 regarding the claimed non-deductibility for IRES and IRAP purposes of costs and value adjustments to receivables relating to facts or actions classified as offences (it regards offence of false corporate reporting, obstacles to supervision and market turbulence alleged to have been committed by Banca Popolare Italiana with relation to the attempted takeover of Banca Antonveneta). The claims amount to 199.8 million euro (including interest and collection commission). In separate rulings filed on 15 October 2014, no. 8562 (IRES) and no. 8561 (IRAP), the Provincial Tax Commission of Milan, Section 22, fully rejected the appeals submitted by the Bank, although providing no reasons underlying its confirmation of the tax claim. We have appealed against the above ruling to the Regional Tax Commission of Lombardy. On 6 May 2015, the appeals lodged on 3 February 2015 were heard before the Milan Regional Tax Commission, section 2. By ruling no. 670, handed down on 19 May 2015, the Commission rejected the combined appeals submitted and confirmed the challenged rulings, also without adequate reasoning. An appeal has been submitted to the Supreme Court of Cassation.
- Banco BPM (former Banca Popolare Italiana Soc. Coop.) - notices of assessment served on 22 December 2014 relating to the formal report on findings dated 30 June 2011 for tax years 2006-2009. These notices also regard the claimed non-deductibility for IRES and IRAP purposes of costs retained as relating to facts or actions classified as offences. More specifically, they regard value adjustments on loans already disputed with reference to tax year 2005. Said value adjustments, although recognised by Banca Popolare Italiana in its financial statements for 2005, were deductible on a straight line basis over the following 18 financial years pursuant to the version in effect at the time of Art. 106, paragraph three, of Italian Presidential Decree no. 917 of 22 December 1986. The notices of assessment serviced therefore dispute the claimed non-deductibility of the quotas of the above-cited adjustments on loans deducted in 2006, 2007, 2008 and 2009. Total claims amount to 15.8 million euro. An appeal was presented to the Provincial Tax Commission. The commission suspended the proceedings until the judgment of the Supreme Court of Cassation on the crime costs for 2005, which were referred to in the previous point, has become final.
- Banco BPM - notices of assessment and formal written notices of the fines relating to the finding regarding the failure to apply the withholding tax set forth in Art. 26, paragraph 5 of Italian Presidential Decree 600/1973, to interest due on deposits made by foreign subsidiaries resident in the US State of Delaware relating to 2013, 2014 and 2015. The claims amount to 25.0 million euro. These disputes are included in the out-of-court settlement made with the Tax Authority, which in 2016 and in 2017 resulted in the closure of similar disputes relating to other years and other incorporated companies without the application of any fine.
- Banco BPM - notices of assessment served on 23 December 2014 regarding 2009 for the former subsidiaries Banca Popolare di Lodi, Credito Bergamasco and Efibanca. The total claim amounts to 58.4 million euro. The Provincial Tax Commission has upheld all of the appeals submitted, cancelling the notices of assessment. The Tax Authority has appealed. On 5 October 2017, the appeals were heard before the Milan Regional Tax Commission. The Commission confirmed the first instance decisions in favour of the bank. The appeal to the Supreme Court filed by the Tax Authority is pending.
- Banco BPM - the audit report delivered on 7 August 2017 regarding the 2012, 2013, 2014 and 2015 financial years containing remarks on the failure to pay IRES and IRAP with reference to certain economic

relationships between Banca Italease S.p.A. and the subsidiary Banca Italease Funding LLC as part of the capital enhancement operations implemented through the issue of preference shares. The total claim amounts to 1.7 million euro.

- Banco BPM (Former Banca Italease) – Settlement notices to recover the mortgage and cadastral taxes on a loan stipulated in 2006. The claim amounts to a total of 3.2 million euro. The appeal submitted by Banca Italease was upheld in the first and second instance. An appeal submitted to the Supreme Court is still pending.

In addition to the aforementioned disputes, note that with reference to the two reimbursement refusal measures issued by the Tax Authority - Provincial Office of Novara relating to IRPEG and ILOR tax receivables requested for reimbursement by the former Banca Popolare di Novara S.c.a r.l. for 1995 for a total amount of 86.5 million euro, the Turin Regional Tax Commission accepted both the combined appeals and also ordered that the Tax Authority pay legal costs. The Tax Authority has appealed this decision to the Supreme Court.

Disputes relating to other subsidiary companies

- Aletti Fiduciaria - notice to recover taxes due by the fiduciary company pursuant to the personal liability of the shareholder under Art. 36, paragraph 3, of Italian Presidential Decree no. 602/1973. The claim amounts to 7.9 million euro. The company’s appeal was fully upheld in the first and second instance. The appeal to the Supreme Court filed by the Tax Authority is pending.
- Banca Aletti - with reference to Banca Aletti's credit position with the Swiss Tax Authorities relating to tax credits on foreign dividends requested for reimbursement on a conventional basis, on 9 March 2018 the Swiss Federal Administration formalised its refusal to reimburse credits accrued in 2008 and 2009. The refused net receivable recorded in the financial statements of the subsidiary, and thus also in the consolidated financial statements, amounts to 38.2 million Swiss francs, equivalent to approximately 33 million euro. In view of the position expressed by the Helvetic Administration, Banca Aletti challenged the administrative measure before the competent authorities in order to assert its rights.

<u>Classification and valuation of potential liabilities in accordance with the provisions of accounting standard IAS 37</u>

Potential liabilities associated with the proceedings regarding the claimed non-deductibility of costs relating to the attempted takeover of Banca Antonveneta by the former Banca Popolare Italiana

The potential liability regarding only the year 2005 amounts to 199.8 million euro, in addition to the potential liability relating to the associated notices of assessment for the years 2006, 2007, 2008 and 2009, estimated at 15.8 million euro, excluding interest and collection commissions.
With regard to the dispute, as at 31 December 2017, tax credits amounting to 201.9 million euro were due from the Tax Authority, following payments made provisionally. The amount paid is recognised in the financial statements under “Other assets”. In this regard, we must emphasise that said payments are not retained such as to impact the risk of losing the dispute, which have been valued on the basis of the provisions of IAS 37: in fact, these amounts are paid as part of an automatic mechanism, which is unrelated to the groundlessness or otherwise of the related tax claims, and which will be known only after the ruling of the highest court.

The aforementioned potential liabilities were carefully assessed in light of the negative rulings made in the courts of the first two instances.
It is deemed that the decisions taken during the first and second instances are unlawful.
First and foremost, it should be noted that, in the parallel criminal proceedings initiated against the signatories of the tax declarations for the crime of false tax declaration (a crime based on the same charges contained in the assessment notices in question), the judge acquitted the defendants “due to lack of evidence”. While the criminal proceedings are separate from administrative disputes, it should be noted that, in the operative part of the judgment, the criminal judge used the same arguments to justify their decision as those put forward by the bank in its defence in the appeals presented in the administrative proceedings described above.
Furthermore, an analysis of the order and the content of the ruling of the Regional Tax Commission shows that the Commission’s decision on the merits of the case contains no specific justification and is based on a mere reference to the Authority’s claims, with no express indication of the reasons for its decision not to accept the precise arguments laid out by Banco Popolare in support of its appeal.

On this basis, it is believed that there are grounds to challenge the ruling before the Supreme Court, as it is possible to re-submit to the court all defensive arguments regarding aspects of legitimacy not considered by the judges in the first and second instances.
On 18 December 2015, the appeal was submitted to the Supreme Court.
The detailed analyses carried out on this situation with the support of the advisers engaged to prepare the appeal, as well as the additional opinion requested from another authoritative expert on the topic, have confirmed the conviction that the Tax Authority's claim is illegitimate and that it is still possible for the defensive arguments to be considered and accepted in the case before the Supreme Court. These same analyses led the Board of Directors to confirm the classification of the potential liability as possible but not probable.
In light of the evaluations carried out, no provision has been recognised for the potential liabilities in question in the financial statements as at 30 June 2018.

Potential liabilities associated with other outstanding proceedings

The remaining potential liabilities associated with tax disputes amount to a total of 117.8 million euro.

In the light of the successful outcomes in the courts of first instance and/or the existence of valid grounds on which to challenge the claims made by the Tax Authority with regard to proceedings under way and also considering the specific opinions issued by authoritative external firms, the potential liabilities classified as possible but unlikely amount to a total of 87.7 million euro.
The potential liabilities classified as probable amount in total to 30.1 million euro and were fully debited from the income statement when the tax demands received were paid or are entirely covered by provisions allocated to the item Provisions for risks and charges.

Inspections under way as at 30 June 2018

As at 30 June 2018, an audit for direct tax purposes for the year 2013 is under way against Banco BPM (the former Banco Popolare).
The audit was launched on 29 November 2017 by the Verona Tax Police Branch of the Finance Police and was extended on 27 December 2017 to cover the years 2014, 2015 and 2016.
Currently, the auditors have started the contradictory procedure with reference to a single point. This concerns the economic treatment of the guarantees previously issued by the former Banca Popolare Italiana and the former Banca Italease to their subsidiaries resident in the state of Delaware. These guarantees aimed to raise financial resources through preferred shares. The auditors did not provide information on the quantification of the potential issue. On 27 February 2018, pursuant to and for the purposes of articles 10 and 12 of the Taxpayer's Statute, the bank gave the auditors a memorandum of its own in which it expressed the reasons for which it considers that the potential issue is unfounded. The audit was suspended after this memorandum was submitted.

Group shareholders' equity – Items 120, 130, 140, 150, 160, 170 and 180

The Group's consolidated shareholders' equity as at 30 June 2018, including valuation reserves and net income for the period, amounted to 10,834.0 million euro, compared to the figure at the end of 2017 of 11,900.2 million euro.
The comprehensive income recorded as at 30 June 2018, in terms of the share pertaining to the Group, was a positive 0.3 million euro due to the net profit of period of 352.6 million euro and the negative change in valuation reserves of 352.3 million euro.

The following table shows the breakdown of valuation reserves.

(in thousands of euro)	30/06/2018	31/12/2017
Financial assets designated at fair value through other comprehensive income	(127,263)	
Financial assets available for sale (former IAS 39)		297,875
Property, plant and equipment	217	217
Foreign investment hedges	1,567	1,805
Cash flow hedges	(10,619)	(8,182)
Exchange rate differences	19,098	18,278
Financial liabilities designated at fair value through profit or loss (changes to its own credit risk)	12,361	14,517
Actuarial gains/(losses) on defined benefit pension plans	(75,361)	(79,436)
Share of valuation reserves related to investments in associates carried at equity	(1,143)	4,318
Special revaluation laws	2,314	2,314
Total	**(178,829)**	**251,706**

Valuation reserves at 30 June were negative and amounted to 178.8 million euro compared to the positive figure of 251.7 million euro as at 31 December 2017.
The decrease of 78.2 million euro is attributable to the introduction of the IFRS 9 accounting standard. More specifically, this negative change amounts to the combined effect:

- of a reduction in valuation reserves of 114.6 million euro, offset by a corresponding increase in other profit reserves;
- of an increase in valuation reserves of 36.4 million euro, which translated into a corresponding increase in shareholders' equity.

For more information on the impacts described above, please refer to the section "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers".
The additional decrease in the period amounted to -352.3 million euro and was largely attributable to the negative performance of government security spreads recorded in the second half of 2018, which were recognised within assets designated at fair value through other comprehensive income. Indeed, as at 30 June 2018, the reserves on these assets were down by 127.3 million euro, net of the related tax (the reserves were positive with +297.9 million euro at 31 December 2017; the figure was +229.5 million euro at the beginning of the year, taking into account the impact of the first time adoption of IFRS 9 to assets of this kind, including the impacts described above).
Looking at the analysis of the trend in the second quarter, these reserves, gross of tax effects, went from a total positive balance of 302 million euro at 31 March 2018 to a total negative balance of 188 million euro at 30 June 2018. As already mentioned, this change is mainly attributable to the negative performance of implicit rates of return on Italian government securities and the consequent repercussions on the market prices of other financial assets listed on the Italian market.
Net of tax, the absolute negative change in valuation reserves recorded in the second quarter for the assets in question amounted to 342 million euro.

The following table provides a reconciliation between the Parent Company's shareholders' equity and net income (loss) for the period with the corresponding consolidated balances.

(in thousands of euro)	Shareholders' equity	Net income (loss) for the period
Balance as at 30/06/2018 as per the Parent Company's financial statements	**9,695,169**	**169,607**
Impact of the consolidation of subsidiaries	1,105,820	690,938
Impact of the valuation at net equity of associated companies	(19,618)	75,998
Cancellation of the dividends received during the period from subsidiaries and associates	-	(571,207)
Other consolidation adjustments	52,664	(12,759)
Balance as at 30/06/2018 as per the consolidated financial statements	**10,834,035**	**352,577**

For more information on the breakdown of own funds and capital ratios, please refer to section F "Consolidated shareholders' equity disclosure" below.

13.1 Share capital and treasury shares: breakdown

As at 30 June 2018, share capital was 7,100 million euro, consisting of 1,515,182,126 ordinary shares subscribed and fully paid up.

The "treasury shares" item is represented by 4,177,619 shares of the Parent Company for a book value of 14.1 million euro.

13.2 Share capital – number of shares of the Parent Group: Annual changes

	Ordinary	Other
A. Existing shares at the beginning of the period	**1,515,182,126**	**-**
- fully paid up	1,515,182,126	-
- not fully paid up	-	-
A.1 Treasury shares (-)	(4,492,254)	-
A.2 Outstanding shares: opening balance	**1,510,689,872**	**-**
A. Increases	**314,635**	**-**
B.1 New issues	-	-
for a fee:	-	-
- business combinations transactions	-	-
- bond conversion	-	-
- exercise of warrants	-	-
- other	-	-
without compensation:	-	-
- to employees	-	-
- to directors	-	-
- other	-	-
B.2 Sale of treasury shares	314,635	-
B.3 Other changes	-	-
C. Decreases	**-**	**-**
C.1 Cancellation	-	-
C.2 Purchase of treasury shares	-	-
C.3 Disposal of companies	-	-
C.4 Other changes	-	-
D. Outstanding shares: closing balance	**1,511,004,507**	**-**
D.1 Treasury shares (+)	4,177,619	-
D.2 Existing shares at the end of the period	1,515,182,126	-
- fully paid up	1,515,182,126	-
- not fully paid up	-	-

Information relating to issues and purchases/sales of shares issued by the Bank

During the half-year, there were no changes in the breakdown of the share capital.

Information relating to issues and purchases/sales of convertible bonds issued by the Bank

As at 30 June 2018, no convertible bond instruments issued by the bank were in circulation.

PART C - CONSOLIDATED INCOME STATEMENT DISCLOSURE

The following tables are presented in the manner described in the paragraph "General preparation principles" in "A.1 - General part".

Interest – items 10 and 20

1.1 Interest and similar income: breakdown

Items/Technical forms	Debt securities	Loans	Other loans	Total 30/06/2018
1. Financial assets designated at fair value through profit and loss	30,807	-	-	30,807
1.1 Financial assets held for trading	24,455	-	-	24,455
1.2 Financial assets designated at fair value	-	-	-	-
1.3 Other financial assets required to be measured at fair value	6,352	-	-	6,352
2. Financial assets designated at fair value through other comprehensive income	151,281	-	X	151,281
3. Financial assets designated at amortised cost	86,268	1,202,973	X	1,289,241
3.1. Due from banks	1,314	15,405	X	16,719
3.2. Loans to customers	84,954	1,187,568	X	1,272,522
4. Hedging derivatives	X	X	(59,272)	(59,272)
5. Other assets	X	X	3,417	3,417
6. Financial liabilities	X	X	X	64,783
Total	**268,356**	**1,202,973**	**(55,855)**	**1,480,257**
of which: interest on impaired financial assets	-	148,274	-	148,274

The table below, while not fully comparable, shows the breakdown of the interest at 30 June 2017 prepared in line with the classification and measuring criteria of the IAS 39 financial instruments, drafted in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

Interest and similar income: breakdown

Items/Technical forms	Debt securities (*)	Loans (*)	Other loans (*)	Total 30/06/2017 (*)
1. Financial assets held for trading	20,905	-	24,687	45,592
2. Financial assets designated at fair value through profit and loss	111	-	-	111
3. Financial assets available for sale	187,245	-	-	187,245
4. Investments held to maturity	94,522	15	-	94,537
5. Due from banks	1,124	14,558	86	15,768
6. Loans to customers	2,398	1,047,668	1,411	1,051,477
7. Hedging derivatives	X	X	-	-
8. Other assets	X	X	104,475	104,475
Total	**306,305**	**1,062,241**	**130,659**	**1,499,205**

(*) The figures relating to the previous period have been restated pursuant to IFRS 5.

1.3 Interest and similar expenses: breakdown

Items/Technical forms	Payables	Securities	Other loans	Total 30/06/2018	Total 30/06/2017 (*)
1. Financial liabilities designated at amortised cost	(80,555)	(196,030)	-	(276,585)	(416,195)
1.1 Due to central banks	-	X	X	-	-
1.2. Due to banks	(38,728)	X	X	(38,728)	(35,521)
1.3. Due to customers	(41,827)	X	X	(41,827)	(60,864)
1.4 Debt securities issued	X	(196,030)	X	(196,030)	(320,002)
2. Financial liabilities held for trading	(6,482)	-	(28,244)	(34,726)	(7,533)
3. Financial liabilities designated at fair value	-	(7,642)	-	(7,642)	(38,348)
4. Other liabilities and funds	X	X	(656)	(656)	(24,776)
5. Hedging derivatives	X	X	39,868	39,868	(26,369)
6. Financial assets	X	X	X	(20,407)	-
Total	**(87,037)**	**(203,672)**	**10,968**	**(300,148)**	**(513,413)**

(*) The figures relating to the previous period have been restated pursuant to IFRS 5.

Fees and commissions – items 40 and 50

2.1 Fee and commission income: breakdown

Service type/Amounts	Total 30/06/2018	Total 30/06/2017 (*)
a) guarantees given	38,829	42,897
b) credit derivatives	-	-
c) management, brokerage and advisory services	484,137	550,165
1. trading of financial instruments	19,215	15,074
2. trading of currency	1,772	3,750
3. portfolio management	15,233	18,285
3.1. Individuals	15,233	18,285
3.2 collective	-	-
4. securities custody and administration	3,292	6,414
5. custodian bank	9,396	9,339
6. placement of securities	324,107	367,289
7. receipt and transmission of orders	21,635	28,826
8. consulting	4,053	1,342
8.1 concerning investments	347	525
8.2 concerning financial structure	3,706	817
9. distribution of third party services	85,434	99,846
9.1. portfolio management	1,546	1,795
9.1.1 individuals	1,546	1,795
9.1.2 collective	-	-
9.2 insurance products	53,794	65,510
9.3 other products	30,094	32,541
d) collection and payment services	92,715	108,563
e) servicing for securitisations	448	46
f) factoring services	-	-
g) tax collection and treasury services	-	-
h) management of multilateral trading facilities	-	-
i) keeping and managing current accounts	113,236	110,668
j) other services	253,955	267,294
Total	**983,320**	**1,079,633**

(*) The figures relating to the previous period have been restated pursuant to IFRS 5.

2.2 Fee and commission expense: breakdown

Services/Amounts	Total 30/06/2018	Total 30/06/2017 (*)
a) Guarantees received	(2,559)	(2,221)
b) credit derivatives	-	-
c) management and brokerage services:	(18,929)	(16,913)
1. trading of financial instruments	(10,910)	(8,736)
2. trading of currency	-	-
3. portfolio management	(279)	(534)
3.1. own	(279)	(534)
3.2 delegated by third parties	-	-
4. securities custody and administration	(3,258)	(3,702)
5. placement of financial instruments	(1,470)	(585)
6. Off-site offer of financial instruments, products and services	(3,012)	(3,356)
d) collection and payment services	(5,900)	(19,433)
e) other services	(28,419)	(21,687)
Total	**(55,807)**	**(60,254)**

(*) The figures relating to the previous period have been restated pursuant to IFRS 5.

Profits (losses) on trading – item 80

4.1 Profits (losses) on trading

Transactions/Income components	Capital gains (A)	Profit from trading (B)	Losses (C)	Losses from trading (D)	Net result
1. Financial assets held for trading	**37,742**	**46,681**	**(112,339)**	**(34,702)**	**(62,618)**
1.1 Debt securities	9,998	18,912	(72,075)	(15,672)	(58,837)
1.2 Equity instruments (other than investments in associates and companies subject to joint control)	27,710	26,856	(40,062)	(18,221)	(3,717)
1.3 UCIT units	34	79	(202)	(731)	(820)
1.4 Loans	-	-	-	-	-
1.5 Other	-	834	-	(78)	756
2. Financial liabilities held for trading	**60,807**	**18,633**	**(25,119)**	**(37,934)**	**16,387**
2.1 Debt securities	31,764	10,365	(4,069)	(359)	37,701
2.2 Payables	57	2,648	(19)	(1,176)	1,510
2.3 Other	28,986	5,620	(21,031)	(36,399)	(22,824)
Financial assets and liabilities: conversion differences	**X**	**X**	**X**	**X**	**86,471**
3. Derivative instruments	**819,993**	**1,389,843**	**(965,377)**	**(1,261,745)**	**(106,527)**
3.1 Financial derivatives:	818,671	1,389,397	(965,310)	(1,260,125)	(106,608)
- on debt securities and interest rates	677,189	988,532	(779,618)	(872,452)	13,651
- on equity instruments and equity indices	137,688	398,179	(181,222)	(385,755)	(31,110)
- on currencies and gold	X	X	X	X	(89,241)
- Other	3,794	2,686	(4,470)	(1,918)	92
3.2 Credit derivatives	1,322	446	(67)	(1,620)	81
of which: natural hedges associated with the fair value option (IFRS 7, par. 9, let. d)	X	X	X	X	-
Total	**918,542**	**1,455,157**	**(1,102,835)**	**(1,334,381)**	**(66,287)**

Fair value adjustments in hedge accounting – item 90

5.1 Fair value adjustments in hedge accounting

Income components/Amounts	Total 30/06/2018	Total 30/06/2017
A. Revenue from:		
A.1 Fair value hedging derivatives	86,596	178,856
A.2 Hedged financial assets (fair value)	80,164	35,376
A.3 Hedged financial liabilities (fair value)	27,900	77,316
A.4 Cash flow hedging derivatives	356	-
A.5 Assets and liabilities in foreign currency	191	-
Total income from hedged assets (A)	**195,207**	**291,548**
B. Charges related to:		
B.1 Fair value hedging derivatives	(57,815)	(86,379)
B.2 Hedged financial assets (fair value)	(95,955)	(195,772)
B.3 Hedged financial liabilities (fair value)	(41,706)	(10,010)
B.4 Cash flow hedging derivatives	-	-
B.5 Assets and liabilities in foreign currency	(191)	(512)
Total charges from hedging activities (B)	**(195,667)**	**(292,673)**
C. Fair value adjustments in hedge accounting (A - B)	**(460)**	**(1,125)**

Profit (loss) on disposal/repurchase - item 100

6.1 Profit (loss) on disposal/repurchase: breakdown

Items/Income components	Total 30/06/2018		
	Income	Losses	Net result
Financial assets			
1. Financial assets designated at amortised cost	634,260	(894,812)	(260,552)
1.1. Due from banks	-	(1,662)	(1,662)
1.2. Loans to customers	634,260	(893,150)	(258,890)
2. Financial assets designated at fair value through other comprehensive income	174,198	(44,415)	129,783
2.1 Debt securities	174,198	(44,415)	129,783
2.2 Loans	-	-	-
Total assets	**808,458**	**(939,227)**	**(130,769)**
Financial liabilities designated at amortised cost	-	-	-
1. Due to banks	-	-	-
2. Due to customers	-	-	-
3. Debt securities issued	-	(1,002)	(1,002)
Total liabilities	**-**	**(1,002)**	**(1,002)**

The table below, while not fully comparable, shows the breakdown of profit (loss) on disposal/repurchase at 30 June 2017 prepared in line with the classification and measuring criteria of the IAS 39 financial instruments, drafted in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

Profit (loss) on disposal/repurchase: breakdown

Items/Income components	Total 30/06/2017		
	Income	Losses	Net result
Financial assets			
1. Due from banks	32	-	32
2. Loans to customers	78,911	(173,624)	(94,713)
3. Financial assets available for sale	39,852	(2,841)	37,011
3.1 Debt securities	24,223	(1,159)	23,064
3.2 Equity instruments	7,959	(120)	7,839
3.3 UCIT units	7,670	(1,562)	6,108
3.4 Loans	-	-	-
4. Investments held to maturity	-	-	-
Total assets	**118,795**	**(176,465)**	**(57,670)**
Financial liabilities			
1. Due to banks	-	-	-
2. Due to customers	-	-	-
3. Debt securities issued	(1,151)	(5,442)	(6,593)
Total liabilities	**(1,151)**	**(5,442)**	**(6,593)**

Profits (losses) on other financial assets and liabilities designated at fair value through profit and loss – item 110

7.1 Net change in value of other financial assets and liabilities designated at fair value through profit and loss: breakdown of financial assets and liabilities designated at fair value

Transactions/Income components	Capital gains (A)	Gains on disposal (B)	Losses (C)	Losses on disposal (D)	Net result
1. Financial assets held for trading	**-**	**-**	**-**	**-**	**-**
1.1 Debt securities	-	-	-	-	-
1.2 Loans	-	-	-	-	-
2. Financial liabilities	**7,303**	**624**	**(30,183)**	**(177)**	**(22,433)**
2.1 Debt securities issued	7,303	624	(30,183)	(177)	(22,433)
2.2. Due to banks	-	-	-	-	-
2.3. Due to customers	-	-	-	-	-
3. Financial assets and liabilities in foreign currencies: conversion differences	**X**	**X**	**X**	**X**	**-**
Total	**7,303**	**624**	**(30,183)**	**(177)**	**(22,433)**

7.2 Net change in value of other financial assets and liabilities designated at fair value through profit and loss: breakdown of other financial assets madatorily at fair value

Transactions/Income components	Capital gains (A)	Gains on disposal (B)	Losses (C)	Losses on disposal (D)	Net result [(A+B) - (C+D)]
1. Financial assets held for trading	**64,205**	**4,181**	**(39,087)**	**(1,177)**	**28,122**
1.1 Debt securities	543	2,645	(5,858)	(581)	(3,251)
1.2 Equity instruments	20,165	287	(1,857)	(274)	18,321
1.3 UCIT units	4,051	992	(8,271)	(322)	(3,550)
1.4 Loans	39,446	257	(23,101)	-	16,602
2. Financial assets: conversion differences	**X**	**X**	**X**	**X**	**-**
Total	**64,205**	**4,181**	**(39,087)**	**(1,177)**	**28,122**

Net value adjustments/recoveries on credit risk – item 130

8.1 Net value adjustments for credit risk related to financial assets designated at amortised cost: breakdown

Transactions/Income components	Value adjustments (1)			Value recoveries (2)		Total
	First and Second Stage	Third Stage		First and Second Stage	Third Stage	
		Write-off	Other			
A. Due from banks	380	-	(4)	1,469	-	1,845
- loans	464	-	(4)	1,449	-	1,909
- debt securities	(84)	-	-	20	-	(64)
of which: acquired or originated impaired credit	-	-	-	-	-	-
B. Loans to customers	(42,303)	(60,848)	(1,201,492)	20,062	861,861	(422,720)
- loans	(36,830)	(60,848)	(1,201,492)	12,601	861,861	(424,708)
- debt securities	(5,473)	-	-	7,461	-	1,988
of which: originated or acquired impaired credit	-	-	-	-	-	-
Total	**(41,923)**	**(60,848)**	**(1,201,496)**	**21,531**	**861,861**	**(420,875)**

8.2 Net value adjustments for credit risk related to financial assets designated at fair value through other comprehensive income: breakdown

Transactions/Income components	Value adjustments (1)			Value recoveries (2)		Total 30/06/2018
	Third Stage		First and Second Stage	Third Stage	First and Second Stage	
	Write-off	Other				
A. Debt securities	(5,028)	-	-	1,830	-	(3,198)
B Loans	-	-	-	-	-	-
- to customers	-	-	-	-	-	-
- to banks	-	-	-	-	-	-
of which: acquired or originated impaired loans	-	-	-	-	-	-
Total	**(5,028)**	**-**	**-**	**1,830**	**-**	**(3,198)**

The tables below, while not fully comparable, show the breakdown of the net adjustments for impairment of the portfolio of the IAS 39 financial instruments at 30 June 2017, drafted in accordance with the provisions of the previous version of Bank of Italy Circular 262 (fourth update).

Net value adjustments for credit impairment: breakdown

Transactions/Income components	Value adjustments			Value recoveries				Total 30/06/2017
	Specific		Portfolio	Specific		Portfolio		
	Cancellations	Other		A	B	A	B	
A. Due from banks	-	-	(55)	-	80	-	384	409
- Loans	-	-	(55)	-	80	-	384	409
- Debt securities	-	-	-	-	-	-	-	-
B. Loans to customers	(55,114)	(1,054,192)	(11,979)	157,860	454,331	-	19,550	(489,544)
Acquired deteriorated loans	-	-		-	-			-
- Loans	-	-	X	-	-	X	X	-
- Debt securities	-	-	X	-	-	X	X	-
Other loans	(55,114)	(1,054,192)	(11,979)	157,860	454,331	-	19,550	(489,544)
Loans	(55,114)	(1,054,192)	(9,881)	157,860	454,331	-	19,550	(487,446)
Debt securities	-	-	(2,098)	-	-	-	-	(2,098)
C. Total	**(55,114)**	**(1,054,192)**	**(12,034)**	**157,860**	**454,411**	**-**	**19,934**	**(489,135)**

Key:
A = From interest
B - Other recoveries

Net losses on impairment of financial assets available for sale: breakdown

Transactions/Income components	Value adjustments		Value recoveries		Total 30/06/2017
	Specific		Specific		
	Cancellations	Other	A	B	
A. Debt securities	-	(15,410)	-	1	(15,409)
B. Equity instruments	-	(1,924)	-	-	(1,924)
C. UCIT units	-	(61,618)	x	x	(61,618)
D. Loans to banks	-	-	x	-	-
E. Loans to customers	-	-	-	-	-
F. Total	**-**	**(78,952)**	**-**	**1**	**(78,951)**

Key:
A = From interest
B - Other recoveries

Net losses on impairment of financial assets held to maturity: breakdown

In the first half of 2017, no value adjustments were recognised on financial assets held to maturity.

Net losses on impairment of other financial transactions: breakdown

Transactions/Income components	Value adjustments			Value recoveries				Total 30/06/2017
	Specific		Portfolio	Specific		Portfolio		
	Cancellations	Other		A	B	A	B	
A. Guarantees given	-	(10,677)	(3,983)	-	25,433	-	958	11,731
B. Credit derivatives	-	-	-	-	-	-	-	-
C. Commitments to disburse funds	-	-	-	-	-	-	-	-
D. Other loans	-	(1,473)	-	-	838	-	-	(635)
E. Total	**-**	**(12,150)**	**(3,983)**	**-**	**26,271**	**-**	**958**	**11,096**

Key:
A = From interest
B - Other recoveries

Other operating expenses/income – item 230

16.1 Other operating expenses: breakdown

	Total 30/06/2018	Total 30/06/2017 (*)
Expenses on leased assets	(7,821)	(8,805)
Amortisation of leasehold improvements costs	(9,060)	(6,461)
Other	(34,471)	(24,693)
Total	**(51,352)**	**(39,959)**

(*) The figures relating to the previous period have been restated pursuant to IFRS 5.

16.2 Other operating income: breakdown

	Total 30/06/2018	Total 30/06/2017 (*)
Income on current accounts and loans	22,791	28,599
Recoveries on tax	125,900	130,412
Recoveries on expenses	21,039	25,315
Rents receivable on real estate	27,956	31,868
Other	166,688	3,116,938
Total	**364,374**	**3,333,132**

(*) The figures relating to the previous period have been restated pursuant to IFRS 5.

Earnings per share

	30/06/2018		30/06/2017	
	Basic EPS	**Diluted EPS**	**Basic EPS**	**Diluted EPS**
Weighted average of ordinary shares (number)	1,510,759,980	1,510,759,980	1,511,383,883	1,511,383,883
Attributable result (in thousands of euro)	352,577	352,577	3,170,369	3,170,369
EPS (euro)	**0.233**	**0.233**	**2.098**	**2.098**
Attributable result without badwill (in thousands of euro)	352,577	352,577	94,232	94,232
EPS (euro)	**0.233**	**0.233**	**0.062**	**0.062**
Annualised attributable result without badwill(*) (in thousands of euro)	705,154	705,154	188,464	188,464
EPS (euro)	**0.467**	**0.467**	**0.125**	**0.125**

(*) The annualised result does not represent a forecast of profits for the year.

As at 30 June 2018, Basic EPS coincides with Diluted EPS as there were no financial instruments with potential dilutive effects.

PART E – INFORMATION ON RISKS AND RELATED HEDGING POLICIES

Introduction

The Banco BPM Group implements the process for managing risks originated by banking and financial activities to pursue stable and sustainable growth objectives over time, in line with the general policies established by the Board of Directors.

Risk profile and risk management and measurement systems

During the first quarter of 2018, the Board of Directors of the Parent Company Banco BPM approved the new Risk Appetite Framework (RAF), on a consolidated level and as an individual legal entity, whereby the Body with Strategic Supervision Functions (*Organo con Funzione di Supervisione Strategica* - OFSS) approves the level of risk that the Group is willing to accept in pursuing its strategic objectives.
The new framework consists of the following basic elements:

1. Governance, which defines the roles and responsibilities of the players involved and the information flows between them;
2. the system of metrics, which summarise risk exposure;
3. the system of thresholds, which defines the risk appetite;
4. the escalation process, activated with different intensities and players when the various thresholds are reached;
5. the instruments and procedures which support the representation and operational management of the RAF, including Significant Transactions (ST);
6. the Risk Appetite Statement (RAS), in which the methods for calculating the thresholds and metrics are analysed.

The RAF is the instrument which makes it possible to establish, formalise, communicate and monitor in a unitary and synergistic manner the consistency of the risk profile (of the Group and of the individual relevant companies) with the risk appetite approved by the Board of Directors and constitutes a policy for the development of the main company processes. Compared to the previous year's framework, the RAF has been supplemented with new indicators in order to further monitor the risk areas identified.
The system of metrics takes into account the recent regulatory instructions on Risk Governance and leverages the internal Risk Identification process, which identified 5 risk areas as relevant for the Group for RAF purposes: First and Second Pillar Capital Adequacy, Liquidity Adequacy, Credit Quality, Profitability, Operational/Conduct.
The indicators selected for monitoring the Group's exposure in the risk areas noted above were broken down into 2 levels: strategic, as they enable the Board of Directors to guide the Group's strategic policies and operational, as they supplement the strategic indicators and, when possible, anticipate their trends through greater monitoring frequency.
The system of thresholds for the strategic indicators defines 4 thresholds: i) Risk Target (Medium/Long-Term Objective); ii) Risk Trigger, the surpassing of which activates the escalation processes laid out in the Framework; iii) Risk Tolerance (tolerance threshold); and iv) Risk Capacity (maximum risk that can be assumed). For the Operational indicators, on the other hand, only the Risk Trigger threshold is used to distinguish the stress area from the business as usual area.
The Risk Function develops the RAF to support the Managing Body (MB), in collaboration with the Planning Function and the other competent Functions, revising the framework at least annually based on changes in the internal and external conditions in which the Group operates.
Risk prevention activities are also carried out in the process of managing Significant Transactions (relating to credit, finance, disposal of bad loans transactions, etc.) which involves, firstly, the Risk Function, which is required to express a prior, non-binding opinion on all significant transactions.

The Group also provides specific and dedicated training activities and courses with a view to disseminating and promoting a solid and robust risk culture within the Bank. Particular mention should be made of certain initiatives, in recent years, aimed at all Group personnel, carried out through specific courses (in the classroom and online) concerning, for example, operational risks, compliance, safety, the banks' administrative responsibilities, the MiFID regulation, anti-money laundering, health and safety at work and work-related stress.

Monitoring and reporting activities

Risk monitoring and control activities carried out by the Risk Function are meant to ensure, at the Group and individual company levels, unitary oversight over the applicable risks, guaranteeing appropriate and timely information to the Corporate Bodies and the Organisational Units involved in risk management, ensuring the development and continuous improvement of risk measurement methodologies and models.
To this end, the Parent Company prepares reporting for the Corporate Bodies in line with the Group's internal policies. Within integrated risk reporting, the Risk Function conducts a periodic assessment of the Risk Profile of the RAF indicators, comparing it with the thresholds defined in the framework and providing historical and detailed analysis that explains the dynamics, points for attention and areas for improvement.
Benchmarking analysis of the main Italian and European banks allows Corporate Bodies and top management to gain a more integrated view of Group risks.

First and second pillar capital adequacy

In order to provide its management and the Supervisory Authority with a complete and knowledgeable disclosure that illustrates the adequacy of own funds, the first line of defence for covering the risks assumed, the Banco BPM Group evaluates its capital position on a current and prospective basis, from a First and Second Pillar perspective, based on the Basel III rules (which are applied through CRR/CRD IV) and the specific guidelines communicated to banks by the Supervisory Authority.
As concerns Pillar 1, the Group's capital adequacy is substantiated in the continuous monitoring and management of capital ratios, calculated by applying the rules established by Supervisory Regulations to verify compliance with regulatory limits and ensure the maintenance of the minimum levels of capitalisation required by Supervisory Regulations. These ratios are also estimated during the Budget or Strategic Plan preparation process and their consistency with the thresholds established in the Risk Appetite Framework and the estimates made in the Capital Plan is verified.
With regard to Pillar 2, the Risk Function coordinates the Group's internal capital adequacy assessment process, in line with the regulatory provisions, and prepares the current and prospective estimates summarised in the yearly ICAAP (Internal Capital Adequacy Assessment Process) report.
The ICAAP capital adequacy assessment takes place by monitoring specific capital indicators which take into account the economic capital originating from Pillar 2 risks, activating the escalation processes if limits are surpassed.
The outcome of the capital adequacy self-assessment, conducted on a long-term basis, takes into consideration the simulations carried out from a regulatory perspective and through the application of internal operating methods. The simulations are carried out under ordinary course of business conditions and also take into account the results deriving from the application of stress scenarios.
The capital adequacy self-assessment from the operating perspective hinges on the comparison between the Group's AFR (available financial resources) and the capital requirements calculated through advanced methodologies developed internally and validated by the competent corporate Function.
The current level of own funds and risk-weighted assets enables the Banco BPM Group to fully comply with regulatory thresholds and specific thresholds required by the Supervisory Authority at the end of the Supervisory Review and Evaluation Process (SREP).

Credit risk

The Banco BPM Group pursues lending policy objectives that seek to:

- support the growth of the business activities in its market territories, with the goal of overseeing and governing the evolution of the Group's positioning, in line with the policies of the Risk Appetite Framework and the budget objectives, focusing on the support and development of customer relationships;
- diversify its portfolio, limiting loan concentration on single counterparties/groups, on single sectors of economic activity or geographical areas;

- adopt a uniform and unique credit management model based on rules, methods, processes, IT procedures and internal regulations harmonised and standardised for all Group banks and companies.

With the aim of optimising credit quality and minimising the global credit risk cost for both the Group and the single companies, under the organisational model the Parent Company's Loans Function is in charge of lending policy guidelines for both the banks and companies of the Group.
Guidelines have also been set at Group level, defining how to behave with respect to credit risk-taking, to avoid excessive concentrations, limit potential losses and guarantee credit quality. In particular, in the loan approval phase, the Parent Company exercises the role of management, direction and support at the Group level.
The credit portfolio monitoring, carried out by the Function, is focused on the performance analysis of risk profile of economic sectors, geographical areas, customer segments and types of granted credit lines, as well as on other analysed spheres of action, allowing the definition of possible corrective actions at central level.
The role of the Parent Company's Risk Function is to provide support to Top Management in the planning and control of risk exposure and capital absorption, with a view to maintaining the stability of the Group, checking capital adequacy forecasts and in stress conditions and compliance with the RAF thresholds, the Group's risk limits and its propensity for risk. In particular, the Function's task is to develop, manage and optimise internal rating models (First Pillar), the loan portfolio model (Second Pillar) over time, and to supervise—as part of second level controls—the calculation of weighted risk assets using Advanced methods.
Portfolio risk monitoring is based on a default model that is applied on a monthly basis to credit exposures of the Banco BPM Group.

Credit quality

The Banco BPM Group uses an elaborate set of instruments to grant and manage credit and to monitor portfolio quality.
Rating plays a key role in loan granting, credit product disbursement, monitoring and management processes. In particular, it plays a role in deciding on the competent bodies to approve loans, influences the mechanism for the automatic renewal of uncommitted credit facilities, and contributes to determining automatic interception in the monitoring and management process (Watchlist).
The internal rating system, which is structured based on default probability (DP), loss given default (LGD) and exposure at default (EAD) risk parameters, is used not only to assess the counterparty when granting, monitoring and renewing credit lines, but also to collectively write down receivables in the financial statements.
The classification of non-performing exposures is conducted in line with the criteria established by the EBA.
To a great extent, the management of non-performing loans in the Group is based on a model that assigns the management of a specific set of loans (portfolio) to specialist resources. In particular, the Group established a unit (the NPL Unit) dedicated to managing non-performing positions, including through assigning portfolios, in keeping with the 2016-2019 Strategic Plan guidelines. The NPL Unit, reporting to the Managing Director, aims to manage non-performing loans with a view to optimising recovery efficiency and speed and creating opportunities for maximising value.
The credit assessment made to establish the amount of expected loss relating to non-performing loans establishes different procedures depending on the status and the size of the exposure. Expected losses evaluated by the manager are periodically reviewed.

Credit risk measurement models

When measuring credit risk, the bank uses an econometric model for management purposes, supplied with an extensive set of data and risk variables.
Using Credit-VaR (value at risk) metrics, the model makes it possible to define the probability distribution of losses within the loan portfolio, limited to performing loans, cash loans and endorsement credits, of resident financial and ordinary customers. This distribution is used to measure the maximum potential loss over a yearly time period and with a specific level of confidence.
Specifically, in order to obtain this distribution, the model's processing engine uses a Monte Carlo simulation, which simulates a sufficiently high number of scenarios as to provide a good empirical approximation of the theoretical distribution of credit portfolio losses.

The calculation of the maximum potential loss, which can be broken down into the traditional measures of Expected Loss and Unexpected Loss (Economic Capital), is affected by concentration risk (as a result of high levels of exposure to individual counterparties or to types of counterparties, which are similar in terms of geographical areas and/or economic sectors—single name concentration) and systematic risk (as a result of the impact of unexpected changes in macroeconomic factors on the likelihood of insolvency of individual counterparties—systemic risk), respectively.
The impact of these components on credit risk depends not only on the degree of concentration of the credit portfolio, but also on the relationship between macroeconomic factors and the default probability, which is in turn estimated using a quantitative stress testing model (developed and updated internally), capable of linking the deterioration rates of counterparties that are economically and geographically similar to a set of first-level (international and domestic) economic and financial factors.
Lastly, the portfolio model periodically undergoes stress testing to evaluate the Group portfolio's credit risk sensitivity to plausible extreme changes in one (sensitivity analysis) or more (scenario analysis) economic and financial factors.

On 30 June 2018, the expected loss, calculated on the Basel III performing validation perimeter (for which Banco BPM was authorised by the Bank of Italy to use internal rating systems to calculate the capital requirements on credit risks) was 0.69% of the exposure to default, while the overall loss (expected and unexpected loss measured using the C-VaR method with a 99.9% confidence level) amounted to 1.21% of the exposure to default.

The internal models for estimating DP and LGD are subject to an internal assessment process by the Internal Validation service and to a third-tier control by the Audit Function. The outcome of these processes is outlined in special reports submitted to the Corporate Bodies and sent to the European Central Bank/Bank of Italy.

Outcome of backtesting rating systems

In order to calculate capital requirements against Credit Risk and only on the scope of the Parent Company, the Banco BPM Group adopts internal estimates of Default Probability (DP) and of Loss Given Default (LGD) for Corporate and Private Customer portfolios.
The comparison between estimates and empirical data is made separately for DP on a six-monthly basis at least, for LGD on an annual basis, through backtesting conducted by the Internal Validation service. The last backtesting exercise regarded the updated DP and LGD models produced in December 2017.
With regard to DP models, the Banco BPM Group adopts performance measures to verify the discriminatory range of the estimates (accuracy ratio - AR) and calibration tests (classic binomial, multi-period and single-period tests and adjusted binomial tests, including those adjusted to account for the cyclical nature of the macroeconomic scenario in question) to compare default rates (DR) over an annual time horizon with estimated DP values.
Regarding the Corporate segment, the latest backtesting exercise showed a good discriminatory range of models, both in terms of single modules and final integrating ratings, which produced values comparable, and at times superior, to those obtained during the development phase.
With regard to the calibration, satisfactory values were found for the Large Corporate model.

With regard to the classic multi-period binomial test, the Mid Corporate Plus, Mid Corporate and Small Business segments showed a higher number of non-calibrated classes. These values are due to a general underestimation of the counterparties riskiness, which it is believed will be resolved following the adoption of the new internal models, re-estimated with a 90-day default definition. However, in relation to the yearly figure for the reference backtesting group, an improvement in the percentages of default by rating class is starting to be recorded, supported by the single-period binomial test, the number of non-calibrated classes for which is largely stable compared to the previous period. Overall, the model performed well for the Private customer segment. A number of modules performed the same or better than during development. However, there was a deterioration in performance for the sociological module which is only applied to a small number of counterparties out of the total portfolio. In terms of the calibration, the results of the multi-period and single-period binomial tests were satisfactory, while the adjusted test confirmed the Corporate segment's outcome.
In general, in 2017, the models were fine-tuned, mainly in order to make the definition of default compliant with regulatory requirements. The results of the conducted activities demonstrate that the calibration tests were passed in full. These aspects of improvement were discussed with the Supervisory Authority. Following the update of the time series, analyses were conducted on the LGD model in production, by comparing, for both the Corporate and private Segments, the parameters considered the most significant (Probability of Non-Performance, Performing/Closure Loss

Given Default, Loss Given Non-Performance), the estimated values obtained with those deriving from the update to highlight any deviations.
The updated values of the parameter “Probability of Non-Performance” were lower than those calculated in the development phase (model in production) for the Corporate and Private segments, showing prudence in estimates.
The LGD Performing/Closure, for the Corporate and Private segments, recorded declines for Performing and Past Due statuses; however, there were increases for the Unlikely to Pay status.
Lastly, as regards the “Loss Given Non-Performance” relating to the Corporate segment, there was a general increase for mortgage loans; however, the values relating to the residual products decreased. For current accounts, there was an increase in cases with personal guarantees. All drivers in the Private segment rose, except for instalment products lacking a personal guarantee. The LGN estimate drivers remained substantially stable in the backtesting sample.
Concerning LGD, modelling developments were made to make the utilised models more consistent with regulations regarding the calculation of the assets weighted for impaired positions. These aspects of improvement were discussed with the Supervisory Authority.

Counterparty Risk

Counterparty risk is defined as the risk that the counterparty in a transaction defaults before the final settlement of the cash flows of the transaction (EU Regulation no. 575/2013). As regards this type of risk, for operating purposes and to provide support for capital adequacy assessment processes (ICAAP process), the Parent Company and Banca Aletti use internal methods to estimate exposures to the risk of possible default of counterparties in OTC derivative transactions.
These methods are mostly based on statistical-quantitative approaches, partially linked to the techniques used for VaR (Value at Risk) estimates, which assess the impact that market risk factors may have on the positive future market value of the overall derivatives portfolio.
For the Parent Group and Banca Aletti, the estimate of exposure to counterparty risk for positions in OTC derivatives for counterparties with whom a collateral agreement has been signed (Credit Support Annex – CSA) is carried out using the simplified Shortcut Method simulation and assessed based on possible changes to the Mark to Market of the individual contracts underlying the same reference CSA,with a time horizon given by the risk margin period for each contract. The measurement is also implemented in the Parent Company and Banca Aletti lending process chain, with a daily monitoring and reporting system.
For the remainder of the derivative exposures, the estimation is calculated using an EPE (expected positive exposure) methodology (analytical or simplified formula). The exposure in Securities Financing Transactions (securities lending and repurchase agreements) is calculated using the standardised methodology adopted for supervisory reporting purposes.
For operational monitoring of counterparty risk arising from its operations not backed by CSA agreements, Banca Akros uses a measurement based on the net mark-to-market plus an add-on differentiated by maturity and asset class.
For the calculation of CVA/DVA (credit value adjustment/debit value adjustment), a simulative estimation model based on the forward evolution of market variables is adopted (Monte Carlo simulation).
The indirect membership (through Clearing Brokers) of a Clearing House for operations in OTC derivatives enabled the following objectives to be achieved:

- the mitigation of counterparty risk through netting mechanisms, leading to a reduction of credit facilities to market counterparties with regard to the plain vanilla swaps transferred to LCH;
- the reduction of capital requirements;
- compliance with the European Directive - European Market Infrastructure Regulation (EMIR);
- mitigation of operating risk.

In accordance with the Basel III Framework Regulation, additional capital requirements regarding the following are to be calculated:

- own funds for the CVA through the adoption of the standardised method, as established by (EU) Regulation no. 575/13 for banks that are not authorised to use the internal model method (IMM) for counterparty risk or the IMM for Incremental Risk Charge (IRC);
- exposures relating to operations with Qualified Central Counterparties (QCCP) by adopting the methods established by Arts. 306-308 of EU Regulation no. 575/2013.

In calculating exposure to counterparty risk, for Supervisory Reporting, the Group uses the standardised approach on the entire scope of reference (derivatives, repurchase agreements, securities lending and medium and long term loans).

Financial risks

Trading portfolio

The organisational model adopted by the Banco BPM Group for the trading portfolios exposed to interest rate risk and price risk requires:

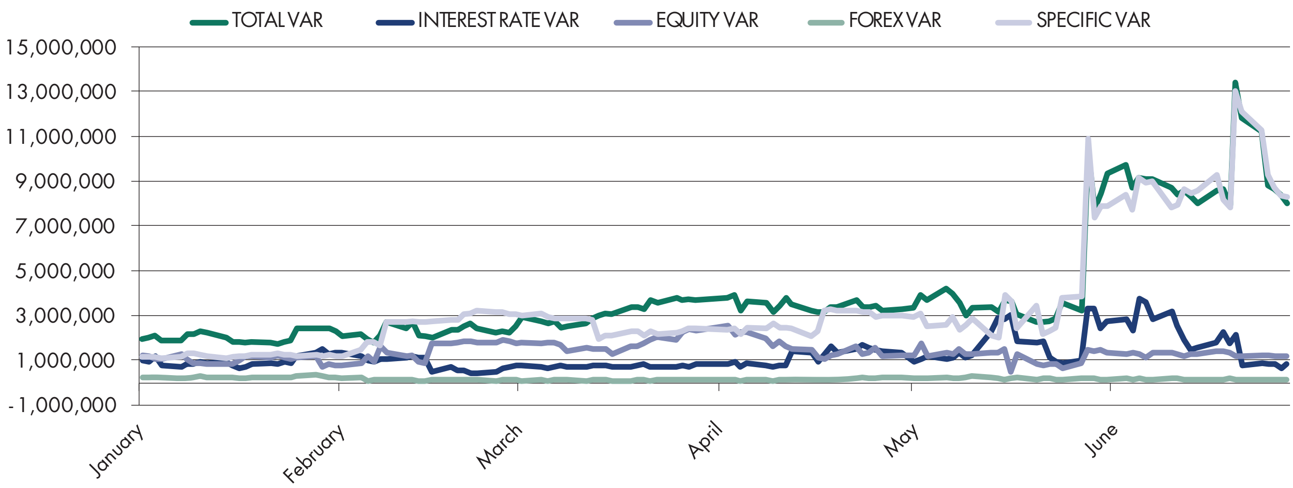
- the centralisation of the management of Treasury and of Proprietary Portfolio positions in Parent Group Finance;
- the centralisation in the subsidiary Banca Aletti of the risk positions and the operating flows associated with trading of securities, currency, OTC derivatives and other financial assets. In addition to this, there are the main interest rate risk exposures from the trading portfolio of Banca Aletti relating to operations on money markets and the associated listed or plain vanilla derivatives, on the markets of listed and OTC derivatives, and structured products;
- the management at Banca Akros of its trading portfolio, the exposures of which come from the activities carried out by the Bank as market maker on regulated markets and OTC for the various investment segments, in addition to the assumption of market risk on own account.

The function in charge of controlling the financial risk management, with the aim of identifying the types of risk, define the methods to measure risks, control limits at the strategic level and verify the consistency between trade limits and the risk/return targets assigned, is centralised in the Parent Company under the responsibility of the Risk Function for all Group banks.
Risk analyses of the Trading portfolio are carried out by means of indicators, both deterministic, such as the sensitivity to market risk factors, and probabilistic, such as VaR (Value at Risk), which measures the maximum potential loss of the portfolio over a certain time horizon and with a given level of confidence.
With respect to the scope of Banco BPM and Banca Aletti, risk capital estimates under the VaR approach are made using the historical simulation method and considering a time horizon of one working day and a statistical confidence interval of 99%. VaR is calculated by applying a Lambda coefficient (decay factor) of 0.99, so as to render the estimate more reactive to the most recent changes in market parameters, and by equal-weighting historic observations. If the latter is higher than the VaR calculated with the above decay factor, it is used for risk estimates.
Risk depends particularly on government securities positions existing in Banco BPM's proprietary portfolio, which generate interest rate risk as well as specific risk on debt securities.
For the measurement of the market risks of the trading portfolio and the quantification of the relative capital requirements, with reference to generic risks (interest rate, price, volatility, exchange rate), Banca Akros uses its own internal model based on VaR and recognised for regulatory purposes. The methodology for generating scenarios is based on the Monte Carlo simulation and the parameters of the VaR model adopted are: *lookback period:* 1 year; confidence interval: 99%: holding period: 1 day; decay factor: 0.992.
The capital requirement relating to the specific risk component is calculated using the standardised method for all Group banks.
Operationally, trading portfolio risks are measured using the Global Historical VaR, which includes all the risk factors to which the bank is exposed, and also extends to issuer risk.

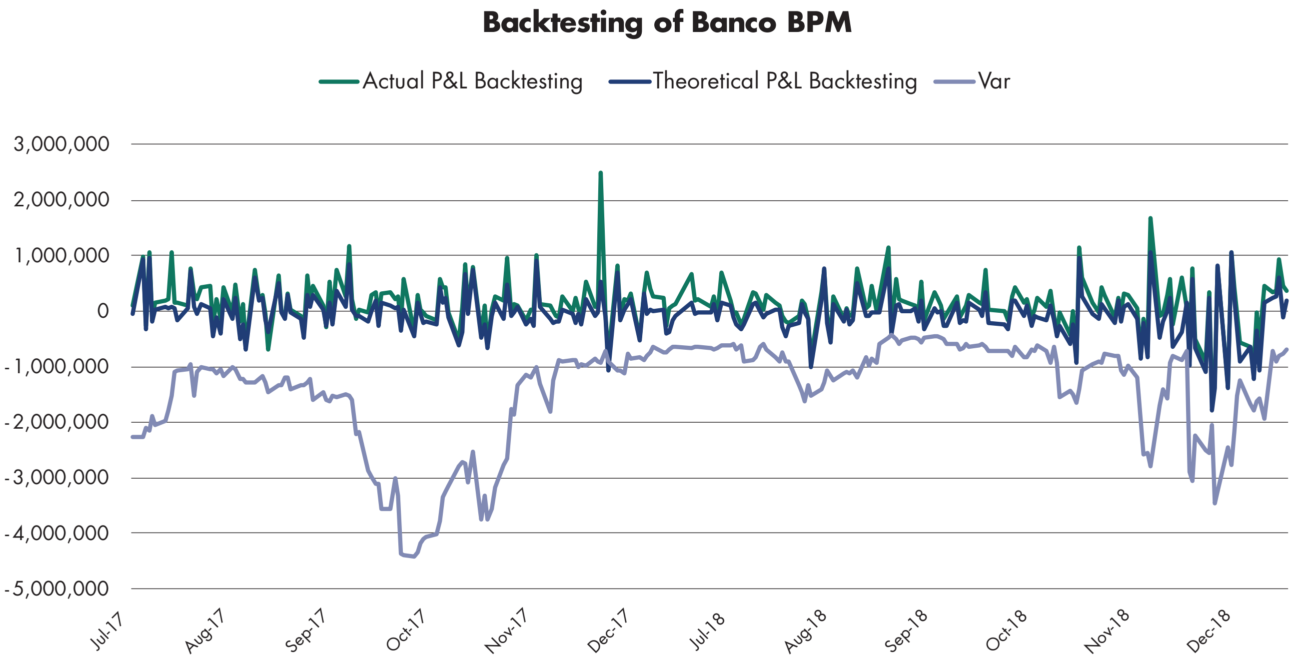
Below is the portfolio risk, in which the precise data relating to 29 June 2018 also include the risk positions present in the Banco BPM Group trading portfolio.

Regulatory trading portfolio *(in millions of euro)*	**29 June 2018**	**1st half 2018** average	maximum	minimum
Interest rate risk	0.827	*1.241*	*3.781*	*0.411*
Exchange rate risk	0.121	*0.157*	*0.338*	*0.087*
Equity risk	1.189	*1.369*	*2.550*	*0.487*
Dividends and Correlations	0.095	*0.275*	*0.554*	*0.014*
Total uncorrelated	*2.233*			
Diversification effect	*-0.881*			
Total Generic Risk	1.351	*1.921*	*3.446*	*1.124*
Specific Risk Debt Securities	8.270	*3.732*	*13.047*	*1.064*
Combined Risk	7.988	*4.156*	*13.419*	*1.729*

Daily VaR and VaR by risk factor
BANCO BPM GROUP: Regulatory trading portfolio



Following the validation of the internal model for the calculation of the capital requirement relating to market risks, backtesting is conducted on a daily basis, with a view to verifying the solidity of the VaR model adopted. These tests are conducted on the regulatory trading portfolio of the Parent Company Banco BPM, Banca Aletti and Banca Akros.
The graphs below show the backtesting of the Parent Company Banco BPM relating to the VaR method, calculated on the generic risk of debt securities, generic and specific equity risk, interest rate risk and exchange rate risk. For backtesting purposes, as established by supervisory regulations in force, we used the equal-weighted VaR measurement instead of using a decay factor used in operational approaches.



Banking portfolio

The interest rate risk relating to the banking portfolio is eminently associated with the core activity performed by the bank acting as an intermediary in the process of transformation of maturities. In particular, the issue of fixed rate bonds, the granting of fixed rate commercial loans and mortgages and funding from demand current accounts represent a fair value interest rate risk, while floating rate financial assets and liabilities represent a cash flow interest rate risk.
The Asset & Liability Management unit of the Parent Bank's Finance Function is responsible for managing interest rate risk and operates in compliance with the limits for exposure to interest rate risk defined by the RAF and the indications of the Finance Committee.
The Parent Company's Risk Function is in charge of monitoring and controlling the interest rate risk of the banking portfolio, also for the financial subsidiaries. This activity is performed on a monthly basis to verify that the limits in terms of changes in interest margin or equity or the economic value of the banking portfolio are complied with, as regards own funds.

As part of the monitoring of interest rate risk, in particular the risk measures used internally and subject to the RAF limit are:

- the change in the expected interest margin following a parallel shock of the spot rate curves of +/-40 basis points (income perspective) over twelve months;
- the change in economic value following a parallel shock of the spot rate curves of +/-200 basis points (capital perspective), as regards own funds;
- the value at risk of the banking portfolio based on the VaR methodology over 12 months and with a confidence interval of 99.9%.

In accordance with normal management practice and internal regulations, the Banco BPM Group conducts periodic stress tests, applying instant or variable shocks over time, both parallel or non-parallel, to the interest rate curves of the currencies in which the banking portfolio items are denominated. Additionally, during the ICAAP exercise, the impact of extreme yet plausible changes in risk factors on VaR is assessed from a capital adequacy perspective.

In the first half of 2018, interest rate risk exposure, from income and capital perspectives, continuously remained within the Risk Appetite Framework and operational risk limits.

The table below shows exposure to interest rate risk at the end of the first half of 2018 in accordance with operational risk measurements.

Risk ratios (%)	2018 financial year (1st half)			
	30 June	average	maximum	minimum
For shift of + 100 bps				
Financial margin at risk /Financial margin	19.4%	19.1%	19.9%	18.5%
For shift of - 100 bps (EBA floor)				
Financial margin at risk /Financial margin	-17.7%	-18.5%	-17.7%	-19.8%
For shift of + 100 bps				
Economic value at risk / Economic value of capital	-2.8%	-1.9%	-0.4%	-3.7%
For shift of - 100 bps (EBA floor)				
Economic value at risk / Economic value of capital	-0.8%	0.7%	1.9%	-0.8%

Operating Risk

Operating risk is the risk of suffering losses caused by inadequacy or failure attributable to procedures, human resources and internal systems or caused by external events. Losses resulting from fraud, human error, interruption of operations, non-availability of systems, contractual breaches and natural disasters are included in this type of risk. Operating risk also encompasses legal risk, while strategic and reputational risk are not included.
The Banco BPM Group was authorised by the European Supervisors to adopt for regulatory purposes a combination of the AMA (Advanced Measurement Approach), relating to the validated scope of the former Banco Popolare Group (Banco Popolare, Banca Aletti, Aletti Gestielle SGR, SGS BP and BP Property Management), the TSA (Traditional Standardised Approach) on the scope of the former Banca Popolare di Milano Group (BPM SpA, ProFamily and Banca Akros) and the BIA (Basic Indicator Approach) for the other remaining companies making up the Banco BPM Group. In this regard, please note that as of the date of the report on 30 June 2018, Banca Aletti will adopt the AMA methods in the private banking segments transferred to it by BPM and by Banca Akros.
The capital requirement, according to the AMA method, is determined by combining the risk measurement obtained by the model based on previous operating losses, both internal and external, with that obtained based on the model that uses elements of scenario analyses. Both of the models adopt an approach known as the Loss Distribution Approach, which is based on the modelling of aggregate annual loss, defined as the sum of loss amounts (severity) associated to each loss event that occurs over one year (frequency). The risk is estimated by measuring the Value at Risk with a confidence interval of 99.9% for one year. The capital requirement relating to the AMA scope takes into account any benefits from diversifying exposure to the different types of operating risk and envisages the deduction of provisions transferred to the income statement to the extent of the expected loss.
The Banco BPM Group is adopting a reporting model, consisting of a management IT system for the Corporate Bodies and Top Management (significant losses and related recoveries, overall assessment of the risk profile, capital absorption and risk management policies implemented and/or planned) and an operational reporting system, for the purposes of adequate risk management in the relevant areas.

Liquidity Risk

Liquidity risk refers to the risk that the Group may be unable to meet its certain or expected payment commitments with reasonable certainty. Normally there are two types of liquidity risk: Funding and Liquidity Risk, or the risk that the Group, in the short (liquidity) and long (funding) term, may not be able to meet its payment commitments and its obligations in an efficient manner due to its inability to obtain funds without harming its ordinary activities and/or its financial position; and Market Liquidity Risk, the risk that the Group may be unable to liquidate an asset without incurring capital losses as a result of little depth in the reference market and/or due to the timing with which it is necessary to carry out the transaction.
In the Banco BPM Group, liquidity and funding risk is governed by the "Liquidity, funding and ILAAP risk regulation", which establishes the roles and responsibilities of the corporate bodies and the corporate functions, the models and metrics used for risk measurement, the guidelines for the execution of stress testing and the Liquidity Contingency Plan.
Liquidity risk is managed and monitored within the internal liquidity adequacy assessment process (ILAAP), which is the process used by the Group to identify, measure, monitor, mitigate and report on the Group's liquidity risk profile. Within this process, the Group proceeds with an annual self-assessment of the adequacy of the overall framework for the management and measurement of liquidity risk, which also includes governance, methodologies, IT systems,

measurement instruments and reporting. The results of the risk profile adequacy assessment and the overall self-assessment are reported to the Corporate bodies and submitted for the attention of the Supervisory Authority.
Liquidity governance is centralised within the Parent Company. Operational liquidity management is coordinated by the Parent Company and takes place in a centralised manner. Although within the scope of the appropriate exceptions, some management can take place in a decentralised manner at individual entity level, however within the risk appetite defined by the Group.
Liquidity risk monitoring and control activities are carried out on a daily basis (short-term liquidity) and a monthly basis (structural liquidity) and aim to monitor the evolution of the risk profile, verifying its adequacy with respect to the Risk Appetite Framework and the established operating limits. On a quarterly basis, stress testing is conducted in order to test the Group's capacity to resist unfavourable scenarios, and the estimates of liquidity that can be generated with countermeasures (the Action Plan, an integral part of the Liquidity Contingency Plan) that may be activated in the presence of a stress scenario are updated.
In particular, the Group uses a monitoring system that includes short-term (time horizon from infra-day up to twelve months) and long-term (more than twelve months) liquidity indicators. To that end, both regulatory metrics (LCR, NSFR, ALMM) and metrics developed internally and which include the use of models for estimating behavioural and/or optional parameters are used.
In the first half of 2018, the liquidity profile of the new Banco BPM Group showed adequacy in the short and longer term, complying with the risk limits set forth internally and, when present, at regulatory level.

Covered bond transactions and securitisations

Significant events during the period

Under the BPM CB1 Programme, on 10 January 2018, the Fifth Series were fully redeemed early for the residual nominal value of 375 million euro. On the payment date of 15 January 2018, the subordinated loan granted to the SPE was also repaid for 350 million euro. On 26 April 2018, Banco BPM issued the Ninth Series of covered bonds (CB), fully subscribed by Banco BPM and used as collateral for refinancing transactions with the ECB, for a nominal value of 2.5 billion euro, a variable rate coupon equal to the 3-month Euribor plus 30 bps, maturing on 26 April 2021.

As part of the BPM CM2 programme, on 23 January 2018, Banco BPM issued the Fourth Series of CB for a nominal value of 750 million euro, placed with institutional investors, with a fixed interest rate coupon of 1%, maturing on 23 January 2025. The subordinated loan granted to the SPE was repaid for 200 million euro on the payment date of 18 January 2018 and for 150 million euro on the payment date of 18 April 2018.

As part of the BP CB1 programme, Banco BPM issued (i) on 25 January 2018 the Eleventh Series of CB for a nominal value of 1.5 billion euro, a variable rate coupon equal to the 1-month Euribor plus a spread of 100 bps, maturing on 30 June 2020 and (ii) on 28 March 2018 the Twelfth Series of CB for a nominal value of 1 billion euro, a variable rate coupon of 1-month Euribor plus a spread of 30 bps, maturing on 30 June 2021. Both securities were fully subscribed by Banco BPM and used as collateral for refinancing operations with the ECB. Additionally, on 31 March 2018 the retained Tenth Series of CB issued for a nominal value of 1 billion euro were fully repaid.

In March 2018, Banco BPM and BPM repurchased *en bloc* the positions classified as bad loans until 31 January 2018 included in the Group's CB programmes.

In order to streamline the Banco BPM Group's CB programmes, a number of measures were completed during the first half of 2018 with the signing of the relevant contracts. In particular, (i) the BP CB2 Programme was closed early (ii) Banco BPM repurchased three asset portfolios from the BP CB1 Programme and (iii) eligible assets were sold under the BPM CB1 Programme and BPM CB2 Programme.

Specifically, regarding the BP CB2 Programme, in April 2018 (i) full early repayment was made on the only outstanding Series (Fourth Series), held entirely by Banco BPM for a nominal value of 1.25 billion euro and (ii) Banco BPM repurchased the entire portfolio of assets, the amount for which was settled by offsetting the amount due by the SPE as early repayment of the subordinated loan granted by Banco BPM to the SPE. On 1 June 2018, an extraordinary Guarantor Payment Date was set for the SPE to make the final payments and, on the same date, a

Termination Agreement was concluded, terminating all the contracts signed and relationships entered into as part of the transaction.

With reference to the BP CB1 Programme, on 18 April 2018 Banco BPM repurchased three portfolios of mortgage loans previously transferred to the SPE for an overall residual debt of approximately 2.7 billion euro, settling the amount for the repurchase price of these mortgage loans by offsetting it against the early partial repayment of the subordinated loan granted by Banco BPM to the SPE. Following the repurchase of these three asset portfolios, on 3 July 2018, the three Mortgage Pool Swap contracts between the SPE and the counterparty Credit Suisse International, and the related back-to-back between the latter and Banco BPM, were closed early, with the consequent update of the programme documentation. Furthermore, on 2 July 2018, the SPE made an early partial repayment of the subordinated loan granted by Banco BPM amounting to 1.5 billion euro.

After modifying the contractual documentation to allow access to Banco BPM as Additional Seller and Additional Lender and to provide for new transfer criteria to also include commercial mortgage loans and disbursements to Group employees, and in regard to the BPM CB1 Programme, on 19 April 2018, Banco BPM and BPM sold a portfolio of eligible assets with total residual debt of approximately 3.9 billion euro to the SPE, BPM Covered Bond S.r.l.. This portfolio consisted of (i) eligible assets provided by Banco BPM (commercial mortgage loans, residential mortgage loans, including disbursements to Group employees) resulting from the repurchase of the entire portfolio of the BP CB2 Programme and part of the portfolio of the BP CB1 Programme, as well as the repurchase of the securitisation assets BPL Mortgages 7 and other eligible free assets (Banco BPM's First Portfolio) and (ii) eligible assets provided by BPM (commercial mortgage loans) resulting from the repurchase of the entire portfolio of the securitisation transaction BPM Securitisation 3 and other eligible free assets (BPM's Eighth Portfolio). To pay the purchase price for the new portfolio, the SPE used a subordinated loan granted by the Originating Banks.

On 29 May 2018, with the signing of the relative contracts, the sale to the SPE, BPM Covered Bond 2 S.r.l. of a new portfolio of eligible assets for a total residual debt of 1.13 billion euro, comprised of residential landed and mortgage loans originated by both Banco BPM (the Second Portfolio) and BPM (the Sixth Portfolio), was completed. To pay the purchase price for the new portfolio, the SPE used a subordinated loan granted by the Originating Banks.

As concerns the securitisation transactions, in March 2018, the BPM Securitisation 3 transaction was closed with the signing of the related contracts. In particular, BPM repurchased the entire residual portfolio of mortgage loans underlying this transaction, and on the extraordinary repayment date of 8 March 2018, the SPE made the early repayment of the securities still outstanding and fully subscribed by BPM.

As part of the restructuring of the BPL Mortgages 7 transaction, with the signing of the related contracts (i) on 9 March 2018, the SPE transferred non-performing loans to Banco BPM, as well as those loans that were eligible for Banco BPM's CB Programmes for a total residual debt of 586 million euro and (ii) on 19 March 2018, the sale by Banco BPM (third sale) was completed following amendment of existing contractual documentation, including by BPM (first sale) as Additional Seller, of an additional portfolio of loans consisting partly of performing credits resulting from the closure of the BPM Securitisation 3 transaction and partly of additional mortgage, land and buildings, and agricultural loans and other loans granted to small and medium-sized enterprises, for an overall residual debt of 3.7 billion euro.
In order to finance the purchase of loans, on 12 April 2018, the SPE increased the nominal value of the First Series asset-backed Securities; in particular (i) A1 (Senior) Securities were increased by 2,840.8 million euro, including 1,121.2 million euro subscribed by Banco BPM and 1,719.6 million euro subscribed by BPM (ii) B1 (mezzanine) securities were increased by 56.4 million euro fully subscribed by BPM and (iii) C1 (junior) securities were increased by 228.5 million euro fully subscribed by BPM. On the same date, after having subscribed to the Increase Notes, in order to rebalance the holding of the Senior, Mezzanine and Junior Securities with respect to the percentages of the composition of the total portfolio originated by each bank, Banco BPM and BPM transferred part of the First Series and Second Series Securities to each other. In addition, on the Increase Date of 12 April 2018, the DRBS rating agency downgraded the ratings of A1 and A2 Senior Securities from AA (high) to A and that of B1 Mezzanine and B2 Securities from A (high) to BBB (high), while Moody's confirmed its existing ratings. Senior securities are used by Banco BPM and BPM, each for their own share, as collateral for monetary policy transactions with the Eurosystem.
As part of the restructuring of the BPL Mortgages 7 transaction, on 12 April 2018 the cash reserve was increased by 91.4 million euro via the disbursement by BPM of a limited loan of the same amount, bringing the balance of the Cash Reserve Account to the new level of 257.8 million euro.

During the period, with the signing of the relative contracts, the securitisation transaction conducted through the SPE, Tiepolo Finance S.r.l. was closed. Specifically, on 21 May 2018, Banco BPM repurchased the entire residual portfolio of mortgage loans underlying this transaction and, on 25 June 2018, an extraordinary payment date was made on which the SPE closed the transaction and derecognised the Junior Securities (Class C) still outstanding and fully subscribed by Banco BPM (and totally written off by the same), on the basis of the applicable waterfall payments and within the limits of available funds, bringing forward their contractual maturity from 10 July 2018 to 25 June 2018. In addition, in June all contracts still outstanding regarding the transaction were closed with the signing of a Termination Agreement.

Lastly, with regard to securitisation transactions involving receivables deriving from leasing contracts originated by the former Banca Italease, the ITABEI securitisation transaction was closed in June 2018. The securities issued as part of the transaction were fully repaid in September 2016.
Specifically, on 12 June 2018, Banco BPM and the SPE Erice Finance signed a contract to repurchase the residual credit portfolio resulting from leasing contracts.
On 11 July 2018, all the counterparties to the transaction signed a Termination Agreement.

Significant events after the end of the interim period

As part of the BPM CB2 programme, on 25 July 2018, Banco BPM issued the Fifth Series of CB for a nominal value of 500 million euro, placed with institutional investors, a fixed interest coupon of 1.125%, maturing on 25 September 2023. The subordinated loan granted to the SPE was repaid for 170 million euro on the payment date of 18 July 2018.

In July, Banco BPM completed the purchase of 100% of the share capital of the SPEs, BPM Securitisation 3 S.r.l. and Leasimpresa Finance S.r.l..

PART F – CONSOLIDATED SHAREHOLDERS' EQUITY DISCLOSURE

Reference legislation and standards to follow

From 1 January 2014, the new harmonised regulations for banks and investment companies contained in (EU) Regulation no. 575/2013 (CRR) and in directive no. 2013/36/EU (CRD IV) dated 26 June 2013 came into force. These transpose the standards defined by the Basel Committee for banking supervision (so-called Basel 3 framework) to the European Union. The Regulation and its technical rules are directly applicable in national legal systems and constitute the Single Rulebook.

Please note that the minimum capital requirements for 2018 are as follows:
- a minimum common equity tier 1 capital ratio (Common Equity Tier 1 ratio: CET1 ratio): 4.5% + 2.5% Capital Conservation Buffer: CCB;
- a minimum Tier 1 capital ratio of: 6.0% + 2.5% of CCB;
- minimum total capital ratio of: 8% + 2.5% of CCB.

Note that on 4 October 2016, the Bank of Italy, in update 18 of Circular Letter 285, reduced the CCB to 1.875% for 2018.

In a communication dated 23 September 2017, the Bank of Italy confirmed that the countercyclical capital buffer (CCyB) was set at zero percent.

In its communication of 30 November 2017, the Bank of Italy identified the Banco BPM banking group as a systemically important institution (Other Systemically Important Institution, O-SII). The O-SII reserve is zero for 2018, while Banco BPM is required to gradually reach a reserve of 0.25% with linear increases from 1 January 2019 to 1 January 2022 (0.06% from 1 January 2019, 0.13% from 1 January 2020, 0.19% from 1 January 2021 and finally 0.25% from 1 January 2022).

On 27 December 2017, the European Central Bank (ECB) notified Banco BPM of its final decision on the minimum capital ratios to be complied with by the Banco BPM on an ongoing basis.
The decision is based on the supervisory review and evaluation process (SREP) conducted in compliance with Art. 4(1)(f) of Regulation (EU) no. 1024/2013.
Therefore, in compliance with At. 16 (2) (a) of the Regulation no. 1024/2013, which confers on the ECB the power to require supervised banks to hold own funds in excess of the minimum capital requirements laid down by current regulations, a requirement of 2.50% was introduced to be added to the requirements highlighted above.
Taking into account the aforementioned requirements deriving from the communication, at consolidated level the Banco BPM Group is required to meet the following capital ratios:
- CET1 ratio: 8.875%;
- Tier 1 ratio: 10.375%;
- Total Capital ratio: 12.375%.

With regard to the measurement of risk-weighted assets, note that the Banco BPM Group is authorised to use the following methods based on its own internal models:
- internal system to measure credit risk relating to corporate and retail customers, according to the advanced approach (Advanced IRB), to calculate the relative consolidated and separate capital requirements.
  The model applies only to the exposures presented in the financial statements of the Parent Company Banco BPM S.p.A. and the subsidiary Banca Aletti S.p.A.;
- internal model to measure market risk (generic and specific on equity instruments, generic on debt securities and position-related for UCIT units) to calculate the relative separate and consolidated capital requirements.
  The model applies only to the exposures presented in the financial statements of the Parent Company Banco BPM S.p.A. and the subsidiary Banca Aletti S.p.A.
  The exposures presented in the financial statements of the subsidiary Banca Akros S.p.A. are measured on the basis of a different internal model;
- internal model to measure operating risk (AMA) to calculate the relative separate and consolidated capital requirements.

The model applies to the Parent Company Banco BPM S.p.A., Banca Aletti S.p.A, SGS Soc. cons., BP Property Management S.c.a r.l. and the Parent Company's Leasing Division.

Within the due date (1 February 2018), Banco BPM informed the European Central Bank that it had exercised the option for the full adoption of the transitional rules introduced by the new Article 473-*bis* of EU Regulation no. 575/2013, which phases in the impact on equity resulting from the adoption of the new impairment model introduced by the new IFRS 9 accounting standard. The aforementioned transitional regulation offers the possibility of including a positive transitory component in Tier 1 capital for a percentage of the increase in provisions for expected losses on loans as a result of the application of IFRS 9 accounting standards. This percentage will decrease over five years, as shown below:

- period from 1 January to 31 December 2018: 95% of the increase in provisions for expected credit losses due to the adoption of the IFRS 9 accounting standard. The expected negative impact deriving from the adoption of the new impairment model to own funds is consequently reduced to 5% of the impact that will be recorded on the book value of shareholders' equity as of 1 January 2018;
- period from 1 January 2019 to 31 December 2019: 85% of the increase in provisions for expected credit losses;
- period from 1 January 2020 to 31 December 2020: 70% of the increase in provisions for expected credit losses;
- period from 1 January 2021 to 31 December 2021: 50% of the increase in provisions for expected credit losses;
- period from 1 January 2022 to 31 December 2022: 25% of the increase in provisions for expected credit losses.

From 1 January 2023, the impact deriving from the first time adoption of the IFRS 9 accounting standard will be fully reflected in the calculation of own funds.

In addition to the possibility of phasing in the impact deriving from the first time adoption of the accounting standard on 1 January 2018, the transitional regulation provides for the possibility of phasing in any impacts that the adoption of the new impairment model will produce in the first few years following the first time adoption of the new accounting standard, albeit limited to those arising from the measurement of performing financial assets.

Capital ratios at 30 June 2018

Applying the transitional rules in force as at 30 June 2018, the capital ratios calculated including the entire amount of the income earned until 30 June 2018[1] are as follows:

- Common Equity Tier1 (CET1) Ratio of 12.93% compared to the 12.36% of 31 December 2017;
- Tier 1 Capital Ratio of 13.13% compared to the value of 12.66% at the end of 2017;
- Total capital ratio of 15.77% compared to the 15.21% at the end of 2017.

The current level of own funds enables the Banco BPM Group to fully comply with the Regulators' requirements, both with respect to the calculation rules currently applicable in the transition period, as well as when the new capital requirements shall apply in full.

The CET1 ratio calculated on the basis of rules that will take effect at the end of the transitional period (so-called CET1 ratio fully phased) will be roughly 10.84%.

Communication concerning prudential filters relating to securities issued by the central governments of countries belonging to the European Union

As at 30 June 2018, the valuation reserve of the securities issued by central government authorities of countries belonging to the European Union, after tax, was fully taken into account in determining own funds.

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[1] Based on the provisions of Art. 26, paragraph 2 of EU Regulation no. 575/2013 of 26 June 2013 (CRR), the inclusion of interim profits in Common Equity Tier 1 Capital (CET1) is subject to the prior permission of the competent authorities (the ECB).
Pending the completion of the procedure by the authority and subject to the issue of the related authorisation, the capital ratios indicated in this document were calculated by including the entire amount of net profit for the first half of 2018 in CET1.

Liquidity position and leverage ratio

The Delegated Regulation (EU) no. 61/2015 came into force on 1 October 2015, and requires banks to maintain a certain level of liquidity measured with reference to a short-term horizon (Liquidity Coverage Ratio, LCR). The regulation establishes a gradual phase-in[1]. As at 30 June 2018, Banco BPM's LCR was higher than 130%.

In the near future, the introduction of a further liquidity requirement is envisaged, measured on a longer time horizon called the Net Stable Funding Ratio (NSFR). The above ratio, calculated in accordance with the most recent rules set by the Quantitative Impact Study and including protected capital certificates, is higher than 100%.

Lastly, as regards the leverage ratio, please note that from September 2016, the legislative changes set forth in the (EU) Delegated Regulation 2015/62 of 10 October 2014 and the new technical standards set forth in (EU) Implementing Regulation 2016/428 of 23 March 2016 came into force. Note that this ratio is currently not mandatory. Within a draft complete review of the CRR[2], the European Committee proposed a minimum level of 3%. The above-mentioned ratio, calculated in accordance with the rules in force during the transitional period, comes to 5.0% as at 30 June 2018. The same ratio, calculated by applying rules that will take effect at the end of the transitional period, is estimated at around 4.1%.

BREAKDOWN OF OWN FUNDS		**Total**	
		30/06/2018	**31/12/2017**
A.	Common Equity Tier 1 capital (CET1) before the application of prudential filters	10,798,870	11,868,333
	of which CET1 instruments subject to transitional provisions	-	-
B.	CET1 prudential filters (+/-)	(41,951)	(15,523)
C.	**CET1 before items to be deducted and before the effects of the transitional regime (A +/- B)**	**10,756,919**	**11,852,810**
D.	Items to be deducted from CET1	(3,544,304)	(2,821,609)
E.	Transitional regime - Impact on CET1 (+/-), including minority interest subject to transitional provisions	1,488,564	347,481
F.	**Total Common Equity Tier 1 capital (CET1) (C - D +/- E)**	**8,701,179**	**9,378,682**
G.	Additional Tier 1 capital (AT1) before items to be deducted and before the effects of the transitional regime	134,226	326,664
	of which AT1 instruments subject to transitional provisions	129,900	322,015
H.	Items to be deducted from AT1	-	-
I.	Transitional regime - Impact on AT1 (+/-), including instruments issued by subsidiaries and included in AT1 by virtue of transitional provisions	-	(97,004)
L.	Total Additional Tier 1 capital (AT1) (G - H +/- I)	134,226	229,660
M.	**Tier 2 capital (T2) before items to be deducted and before the effects of the transitional regime**	**1,864,115**	**2,113,716**
	of which T2 instruments subject to transitional provisions	27,344	71,533
N.	Items to be deducted from T2	(88,225)	(102,737)
O.	Transitional regime - Impact on T2 (+/-), including instruments issued by subsidiaries and included in T2 by virtue of transitional provisions	-	(75,053)
P.	**Total Tier 2 capital (T2) (M - N +/- O)**	**1,775,890**	**1,935,926**
Q.	**Total own funds (F + L + P)**	**10,611,295**	**11,544,268**

[1] 60% from 1 October 2015; 70% from 1 January 2016; 80% from 1 January 2017; 100% from 1 January 2018.
[2] Document "COM(2016) 850 final" of 23.11.2016.

CATEGORIES/AMOUNTS		Unweighted amounts		Weighted amounts/requirements	
		30/06/2018	31/12/2017	30/06/2018	31/12/2017
A.	**RISK ASSETS**				
A.1	Credit and counterparty risk				
	1. Standardised method	74,005,729	96,058,742	29,387,665	48,917,787
	2. Method based on internal ratings				
	2.1 Basic	-	-	-	-
	2.2 Advanced	96,380,347	74,440,541	28,029,607	18,381,207
	3. Securitisations	1,716,335	72,471	1,159,853	82,814
B.	**REGULATORY CAPITAL REQUIREMENTS**				
B.1	**Credit and counterparty risk**			4,686,171	5,390,544
B.2	Credit valuation adjustment risk			14,555	25,563
B.3	Settlement risk			1,295	1,708
B.4	**Market risk**				
	1. Standardised method			35,476	40,094
	2. Internal models			170,054	165,755
	3. Concentration risk			-	-
B.5	**Operating risk**				
	1. Basic method			13,244	13,244
	2. Standardised method			209,753	214,577
	3. Advanced method			252,461	220,230
B.6	**Other calculation items**				-
B.7	**Total prudential requirements**			5,383,009	6,071,715
C.	**RISK ASSETS AND CAPITAL RATIOS**				
C.1	Risk-weighted assets			67,287,612	75,896,441
C.2	Common Equity Tier 1 capital/Risk-weighted assets (CET1 capital ratio)			12.93%	12.36%
C.3	Total Tier 1 capital/ Risk-weighted assets (Tier 1 capital ratio)			13.13%	12.66%
C.4	Total own funds/Risk-weighted assets (Total capital ratio)			15.77%	15.21%

PART G - BUSINESS COMBINATIONS REGARDING COMPANIES OR DIVISIONS

Transactions carried out during the period

No business combination transactions were carried out outside the Group during the first six months of the year.

Business combinations after the reporting period

No business combination transactions were carried out outside the Group after the end of the six-month period.

PART H - TRANSACTIONS WITH RELATED PARTIES

Banco BPM adopted "Process rules for the management of related parties IAS 24". These Process rules, which are valid for Banco BPM and for all Group companies, establish the following operating criteria to identify related parties:

a) companies subject to significant influence and joint control: the entities in which the Parent Company Banco BPM or the subsidiary entities exercise significant influence pursuant to IAS 28 or joint control pursuant to IFRS 11. In particular, these are the "Investments in companies subject to joint control and subject to significant influence" specified in the section "Accounting policies - Scope of consolidation and methods";
b) executives with strategic responsibilities: the members of the Board of Directors, the acting members of the Board of Statutory Auditors, the General Manager and the Joint General Managers of the Parent Company and the Group companies are classified as such, as well as the top operations and management executives of Banco BPM, identified by a dedicated board resolution, the Manager responsible for preparing the Company's financial reports, the Head of the Compliance function, the Head of the Internal Audit function of Banco BPM, any additional structure heads identified by the Board of Directors of Banco BPM and any extraordinary liquidators;
c) close family members of executives with strategic responsibilities: only family members that are able to influence (or be influenced by) the party concerned in the relationship between the latter and Banco BPM or Group companies. The following are presumed to be as such, unless otherwise declared in writing by the executive, under the latter's own responsibility and containing adequate and analytical justification of the reasons that exclude any possible influence: spouses, common law spouses (including cohabitants whose status is not revealed in the family status certificate), offspring of the party, of the spouse or common law spouse, individuals dependent on the party, the spouse or common law spouse. Any other individual which the party believes may influence them (or be influenced by them) in their dealings with the bank or the other BPM Group companies is also a related party;
d) participative relations attributable to executives with strategic responsibilities and their close relatives: the following entities are considered to be related parties, those in which executives with strategic responsibilities or their close relatives have control pursuant to Article 2359, paragraph 1 of the Italian Civil Code, or joint control or exercise significant influence which is presumed when they hold, directly or indirectly, at least 20% of the voting rights which can be exercised during ordinary shareholders' meetings, or 10% if the company has shares listed on organised markets;
e) group pension funds: the pension funds for Group employees and any other related body;
f) holders of a significant equity investment: shareholders and the relative corporate groups (legal entities which are parent companies, subsidiaries or subject to joint control) which control the Parent Company, even jointly, or which exercise significant influence over Banco BPM, are considered related parties. As a minimum, a situation of significant influence is deemed to exist when the shareholder holds an interest with voting rights exceeding 10% of the share capital of Banco BPM. Parties not belonging to the Group who hold an interest in other Group companies greater than 20% of the voting rights that may be exercised in the shareholders' meeting, or 10% if the company has shares listed in organised markets, are also considered to be related parties;
g) parties who themselves are in a position to appoint members of the Board of Directors by virtue of the articles of association or shareholders' agreements.

Financial and commercial transactions between subsidiary companies and those subject to significant influence and joint control.

Financial and commercial transactions with related parties fall within the sphere of ordinary operations and have been conducted as arm's length transactions.

The tables below indicate the balance sheet and income statement transactions as at 30 June 2018 with the companies subject to significant influence, the joint ventures, management with strategic responsibilities (which include audit bodies) and other related parties.

(in thousands of euro)	Entities exercising significant influence (1)	Associated companies	Joint ventures	Executives with strategic responsibilities	Other related parties	TOTAL	% of consolidated total
Financial assets held for trading	-	5,492	-	-	759	6,251	0.10%
Due from banks	-	-	-	13	46,283	46,296	0.84%
Loans to customers	-	2,550,029	-	7,501	173,853	2,731,383	2.26%
Other assets	-	6,690	-	-	-	6,690	0.05%
Due to banks	-	-	-	-	273,451	273,451	0.87%
Due to customers	-	322,824	-	17,209	456,916	796,949	0.91%
Debt securities issued	-	-	-	2,439	2,818	5,258	0.03%
Financial liabilities held for trading	-	-	-	-	1,874	1,874	0.02%
Financial liabilities designated at fair value	-	-	-	99	1,760	1,859	0.07%
Other liabilities	-	2,061	-	293	56,955	59,309	0.59%
Guarantees given and commitments	-	555,018	-	3,029	224,101	782,148	1.41%

(1) Funds or other authorised parties who act as a Shareholder and who possess a shareholding greater than 10% of the share capital

(in thousands of euro)	Entities exercising significant influence (1)	Associated companies	Joint ventures	Executives with strategic responsibilities	Other related parties	TOTAL	% of consolidated total
Interest margin	-	11,498	-	24	174	11,696	0.99%
Net fee and commission income	-	73,711	-	15	4,307	78,033	8.41%
Administrative expenses/recoveries of expenses	-	948	-	(7,850)	5	(6,897)	0.45%
Other costs/revenues	-	16	-	(4)	(629)	(617)	0.23%

(1) Funds or other authorised parties who act as a Shareholder and who possess a shareholding greater than 10% of the share capital

Other transactions with other related parties

The table below discloses other transactions—supplies of goods and services and transactions on real estate—entered into with related parties, shown in the above table under "executives with strategic responsibilities" and "other related parties".

	Purchases and sales of goods and services	Rentals receivable	Rentals payable
a) Directors	-	-	-
b) Executives with strategic responsibilities	-	7	-
c) Close family members of the parties in letters a) and b)	-	-	-
d) Subsidiary, associated company or subject to significant influence by the parties in letters a) and b)	1,593	1,023	-

Other information

In regard to paragraph 8 of Art. 5 "Disclosures to the public on related party transactions" of the CONSOB (The Italian Securities and Exchange Commission) Regulation containing provisions for related party transactions (adopted by CONSOB with resolution no. 17221 of 12 March 2010 and then amended with resolution no. 19974 of 27 April 2017), the following paragraphs illustrate the most important transactions conducted in the first half of 2018, as well as those that are less important yet particularly significant.

Implementation of 2016-2019 Strategic Plan —Demerger of the Banca Akros Private Banking business unit to Banca Aletti

On 1 April 2018, the demerger of the Banca Akros Private Banking business unit to Banca Aletti was completed.
As a result of the demerger, Banca Akros transferred the business unit to Banca Aletti, comprising all the assets, resources and contractual relationships held by the Private Banking Department of Banca Akros.
In particular, the following were assigned to the beneficiary:

i) contractual relationships for the provision of investment services and activities and ancillary services (assets under administration) with customers in the Private Banking Department and related existing documentation;
ii) contractual management relationships for investment portfolios (asset management) with customers in the Private Banking Department and related existing documentation;
iii) current account contractual relationships and related assets and liabilities with customers in the Private Banking Department and existing related documentation;
iv) on the Effective Date, employment relationships with employees who operate within the business unit with all rights, including the employees severance fund (TFR), resulting from the employment relationship, within the limits provided for by law and by collective labour agreements, and, correspondingly, the amount of the relative Valuation reserves recognised in the financial statements of the demerged company to take account of actuarial gains (losses) relating to defined-benefit pension plans;
v) agency contracts with financial consultants authorised to make off-site offers who, on the Effective Date, operate within the business unit with all rights, including any pension funds, resulting from the respective contracts and from the applicable laws and collective agreements;
vi) the branch dedicated to private banking activities located in Rome with the relative leasing and ancillary contracts;
vii) all other contracts which are outstanding as at the Effective Date, relating to the business unit, including, by way of example, the distribution agreements of UCITs managed by third parties;
viii) furniture, fittings and equipment, including IT, tangible and intangible, for the functional use of the business unit;
ix) receivables from and payables due to banks (interbank);
x) sureties, guarantees, obligations and memorandum accounts of the business unit.

The demerger led to a 3.9 million euro reduction in Banca Akros' shareholders' equity through the reduction in reserves and a corresponding increase in Banca Aletti's shareholders' equity through an increase in reserves.
Differences in the amount of balance sheet assets and liabilities involved in the demerger between the reference date used to draft the demerger plan and the effective date of the demerger were settled by means of a monetary adjustment.

Banco BPM Business Plan. Approval of the merger plan by incorporation of the Banca Popolare di Milano S.p.A.

On 27 March 2018, the Board of Directors resolved to begin operations aimed at merging by incorporation BPM into the Parent Company by applying the simplified merger procedure, pursuant to art. 2505 of the Italian Civil Code, without the determination of an exchange rate and without the preparation of the explanatory report by the Board of Directors.
The merger transaction is part of the streamlining initiatives of the corporate and organisational structure provided for in the 2016/2019 Strategic Plan of the Banco BPM Group. This is the logical continuation of the actions already taken as part of the integration process between the two former Groups.
The proposal to merge BPM into the Parent Group aims to achieve the full benefits of the actions described above and is an important turning point for establishing the full identity of the new Group, allowing the full exploitation of its strong competitive position, characterised by a national market share of more than 8%, with over 4 million customers and a leadership position in the richest and most entrepreneurial regions in Italy. The transaction also contributes to achieving greater synergies compared to those originally planned, fostering better operating efficiency due to the simplification of the Group's governance and corporate structure, the more timely and effective implementation of commercial strategies and the optimisation of its physical presence across Italy.
It is therefore expected that the merger may produce effects, pursuant to Art. 2504 - *bis* of the Italian Civil Code, indicatively in the fourth quarter of 2018, after registering the deed of merger in the Companies' Register and prior authorisation by the Supervisory Authority. The transactions of the company being merged will be entered into the financial statements of the absorbing company as from the first day of the current financial year. Tax effects will apply from the same date.

The merger will have no impact on the consolidated ratios, since it is the merger of a bank wholly owned by the Parent Group.

Approval of the merger by incorporation of Società Gestione Servizi S.C.P.A. and BP Property Management S.C.A.R.L. into Banco BPM.

On 9 May 2018, the Board of Directors resolved to begin operations aimed at merging by incorporation Società Gestione Servizi BP and BP Property Management into the Parent Company, by applying the simplified merger procedure, pursuant to Art. 2505 of the Italian Civil Code, without the determination of an exchange rate and without the preparation of the explanatory report by the Board of Directors.
The merger transaction is part of the streamlining initiatives of the corporate and organisational structure and meets the need to simplify and streamline its structure, optimise and make the most of its resources and reduce costs.
Specifically, the merger operations in question should lead to following:

- greater efficiency in management processes;
- the reduction in activities outsourced by the Parent Company to its subsidiaries to only activities and functions that are objectively indispensable;
- the reduction in the complexity of processes and, consequently, of operating risks;
- additional cost synergies.

It is expected that the merger between the two companies may produce effects, pursuant to Art. 2504 - *bis* of the Italian Civil Code, indicatively with effect from January 2019 and prior to authorisation by the Supervisory Authority, after registration of the deed of merger in the Companies' Register and prior authorisation by the Supervisory Authority. The transactions of the companies being merged will be entered into the financial statements of the absorbing company as from the first day of the current financial year in which the legal effects are completed. Tax effects will apply from the same date.
The merger will have no impact on the consolidated ratios, since it is the merger of companies wholly owned by the Group or for which the Parent Company has signed option contracts for the repurchase of the equity investment.

The issue of Banco BPM bonds subscribed by Banca Aletti & C. S.p.A., with the use of the liquidity deriving from funding activities through the issue of Certificates —definition of ceilings and characteristics

The operation in question regards the issue of Banco BPM bonds, underwritten by Banca Aletti, using liquidity resulting from funding collected from the issuing of Certificates.
The Banco BPM bonds are issued at the same spread as the funding of the Certificates issued by Banca Aletti, whose economic conditions, on each occasion, are in line with those applied to retail products for fresh funding.
For the Banco BPM Group, this transaction is part of a strategy to diversify sources of funding and to stabilise the liquidity profile, which makes it possible to meet customer requirements by extending the range of products.
As at 30 June 2018, Banco BPM S.p.A. issued 9 bonds for a total of approximately 273 million euro, against a ceiling of approximately 600 million euro, established by the framework resolution updated on 19 December 2017 and valid for the period between January and December 2018.

Early closure of the BPM 3 securitisation transaction and the restructuring of the BPL7 securitisation transaction

This transaction approved by the Board of Directors on 7 February 2018 consists of the early closure of the SEC3 transaction and the restructuring of the BPL7 transaction. Specifically, it was agreed to proceed with:

i) the early closure of the SEC3 transaction through the relegation by the SPE to BPM of the entire SEC3 portfolio and the subsequent early repayment of the securities, without prejudice to the resolutions concerning BPM;
ii) any change in the BPL7 transaction contractual documentation to allow, as part of this transaction, the sale of an additional portfolio of loans granted to small and medium-sized enterprises by Banco BPM and BPM, without prejudice to resolutions concerning the latter, with total residual debt of approximately 4.6 billion euro and an increase in outstanding securities or the issue of new classes of asset-backed securities, as described above;
iii) the relegation of the non-performing loans in the BPL7 portfolio by SPV to Banco BPM;
iv) the relegation of loans in the BPL7 portfolio eligible for Banco BPM's CB programmes by SPV to Banco BPM;

v) the signing of all useful and/or necessary and/or appropriate contractual documentation relating to or in any way connected with the performance by Banco BPM of these functions and the performance of the aforesaid transactions and indicated in the attached documentation as contracts for early closure and contracts for restructuring.

In March 2018, the SEC3 transaction was closed early and, in order to proceed with the issue of securities resulting from the restructuring of BPL7, Banco BPM and BPM S.p.A. sold a portfolio of loans granted to small and medium-sized enterprises to the SPE BPL Mortgages S.r.l.; the total amount of the portfolio sold as at 31 March 2018 was approximately 3.8 billion euro.

On 12 April 2018, the SPE increased the notes issued in 2014 by approximately 3.1 billion euro, 1.1 billion euro of which was attributable to Banco BPM and 2 billion euro to BPM S.p.A..
On 28 May 2018, the Central Bank of Ireland made senior bonds issued as part of the transaction eligible for Eurosystem monetary policy transactions.

In April, close to the issue date of the securities, BPM S.p.A. issued a subordinated loan to the SPE, aimed at increasing the cash reserve of the transaction by 91.4 million euro.

On 27 March 2018, as part of the aforementioned restructuring of the securitisation and in order to close the transaction, the Board of Directors resolved to grant the following credit lines: (i) the granting by Banco BPM S.p.A. of new lines for the banking book for a total of 6.3 billion euro (ii) the granting by BPM S.p.A. of a new line for the banking book of 3.5 billion euro.

Covered Bond Issue Programme of the Banco BPM Group and relative issue proposals

On 27 February 2018, the Board of Directors agreed on the proposals described below in order to define the streamlining process for the Group's four covered bond programmes, with a view to reducing costs, increasing available collateral and issuing CBs as provided for in the 2018 funding plan. More specifically, the individual proposals relate to the following:

- the full early repayment of the retained Fourth Series issued under the BP CB2 programme, the repurchase of the entire asset portfolio of the BP CB2 programme and the termination of the BP CB2 programme;
- the repurchase from BP Covered Bond S.r.l. of the three asset portfolios of the BP programme; subject to the conclusion of legal assessments, the closing of the asset swaps named in the BP CB1 programme documentation, Mortgage Pool Swap, the mutual termination of the related ISDA Master Agreements and guarantee documents;
- access by Banco BPM to the BPM CB1 Programme as a new Originating Bank and lender to carry out the roles of Additional Seller and Additional Lender once the relative loan has been approved; the authorisation for BPM S.p.A. to approve the Amendments to the Documents for the sale of the BPM CB1 programme to include commercial and residential mortgage loans granted to Group employees; the sale to BPM Covered Bond S.r.l. of the First Portfolio of Banco BPM for a maximum amount of 4 billion euro of commercial and residential mortgage loans granted to Group employees; the authorisation for BPM S.p.A. to sell the Eighth Portfolio for a maximum of 500 million euro;
- the extension of the maturity date of the retained Tenth Series of the BP CB1 Programme for a maximum of 4 years;
- the renewal of BPM CB1 and subsequent updates, the issue of the Ninth Series or subsequent retained Series at variable rates up to a maximum of 3.5 billion euro with a maximum maturity of four years and a maximum coupon equal to Euribor + 100 basis points;
- the authorisation for BPM S.p.A. to approve the repurchase *en bloc* of all the positions classified as bad loans as at 31 January 2018, relating to the BPM CB1 and BPM CB2 issue programmes;
- as part of the BPM CB2 programme, Tap Series 4, i.e. the issue of one or more new series, in both cases, up to a maximum of 350 million euro, at a fixed rate, with a maximum maturity of 15 years and a spread not exceeding 70 basis points above the mid-swap reference rate;
- the sale by Banco BPM to the SPE BPM Covered Bond 2 S.r.l. of the Second Portfolio of eligible residential mortgage loans, up to a maximum of 1.5 billion euro; the authorisation for BPM S.p.A. to sell the Sixth Portfolio up to a maximum of 1 billion euro; the issue, within the current year, of the New 2018 Series, both as individual issues and through the issue of more series of covered bonds for a total maximum nominal amount of 2 billion euro, at a fixed rate, with a maximum maturity of 15 years and a maximum

spread on the swap rate of 70 basis points for maturities of up to 7 years and 100 basis points on other maturities.

In relation to that which was resolved:
- in April, the Fourth Series of the BP CB2 programme was repaid, the mortgage loan portfolio was subsequently repurchased, and the documentation closing the programme was signed on 1 June;
- on 18 April 2018, Banco BPM repurchased three portfolios of mortgage loans previously sold to the SPE BP Covered Bond for a total residual debt of approximately 2.7 billion euro, settling the amount for the repurchase price of these mortgage loans by offsetting it against the early partial repayment of the subordinated loan granted by Banco BPM to the SPE;
- as part of the BPM CB1 programme and subject to the amendment of the contractual documentation, on 19 April 2018, Banco BPM and BPM S.p.A. transferred to the SPE BPM Covered Bond S.r.l. a portfolio of eligible assets with a total residual debt of approximately 3.9 billion euro, financed by the SPE through the use of a subordinated loan granted by the originating banks, with the signing of the relative contracts;
- on 31 March 2018, the retained Tenth Series amounting to 1 billion euro of the BP CB1 programme was fully repaid;
- on 26 April 2018, Banco BPM issued the Ninth Series of BPM CB1 (fully subscribed by Banco BPM and used as collateral for refinancing transactions with the ECB) for a nominal value of 2.5 billion euro, a variable rate coupon equal to the 3-month Euribor plus 30 bps, maturing on 26 April 2021;
- in March 2018, BPM S.p.A. repurchased *en bloc* the positions classified as bad loans until 31 January 2018 in the BPM CB1 and BPM CB2 programmes;
- on 29 May 2018, with the signing of the relative contracts, the sale to the SPE, BPM Covered Bond 2 S.r.l. of a new portfolio of eligible assets for a total residual debt of 1.1 billion euro, comprised of residential landed and mortgage loans originated by both Banco BPM and BPM S.p.A. was completed. To pay the purchase price for the new portfolio, the SPE used a subordinated loan granted by the Originating Banks.

On 27 March 2018, as part of the aforementioned transactions to sell portfolios of loans to BPM Covered Bond S.r.l. and BPM Covered Bond 2 S.r.l., the Board of Directors resolved to grant credit lines to the SPEs BPM Covered Bond S.r.l. and BPM Covered Bond 2 S.r.l., with: (i) a loan granted by Banco BPM to BPM Covered Bond S.r.l. of 4.1 billion euro; (ii) a loan granted by Banco BPM to BPM Covered Bond 2 S.r.l. of 1.2 billion euro.

Alba Leasing S.p.A. – revision of credit lines

This transaction, approved by the Board of Directors on 23 January 2018, concerns (i) the confirmation of the reliability ceiling for direct risks of 1 billion euro and (ii) a reduction in total credit lines granted by the Banco BPM Group to Alba Leasing S.p.A. from 923.3 million euro to 898.3 million euro, combined with indirect risks of 3.0 million euro.

ProFamily S.p.A. – revision of credit lines

The transaction, approved by the Board of Directors on 27 February 2018, concerns the revision and restructuring of credit lines available from the Banco BPM Group for ProFamily S.p.A., which increased from 1,321.4 million euro to 1,621.4 million euro (plus 100 million euro for outstanding risks).

Credit Agricole risk group - Agos Ducato

The transaction, approved by the Board of Directors on 19 June 2018 with regard to the Credit Agricole Group, concerns:
i) the restructuring of the credit ceiling available from the Banco BPM Group for a total of 2,200 million euro for direct risks (together with a credit ceiling of 800 million euro for outstanding risks);
ii) an increase from 30 million euro to 50 million euro in the credit line for the purchase of bonds for the banking book granted;
iii) an increase from 1,521.7 million euro to 1,525.5 million euro in total credit lines;
iv) an increase from 1,993.3 million euro to 2,017.1 million euro in the total credit lines (combined with indirect risks of 1 million euro and outstanding risks of 750 million euro).

PART I - DISCLOSURE ON SHARE-BASED PAYMENT AGREEMENTS

1. Description of share-based payment agreements

A. QUALITATIVE INFORMATION

1. Remuneration linked to incentive systems: compensation plans based on shares

As the Parent Company, Banco BPM S.p.A. prepares the annual Report on Pay pursuant to the provisions in force on remuneration and incentive policies and practices of the Bank of Italy (Circular no. 285/2013, 7th update of 18 November 2014, Part I, Title IV, Chapter 2 "Pay and incentive policies and practices"), of Art. 123-*ter* of Italian Legislative Decree 58/1998 (Consolidated Finance Law or CFL) and of Art. 84-*quater* of CONSOB resolution no. 11971/1999 as amended (Issuer Regulations).
The remuneration policies (Policy) define—in the interest of all stakeholders—the guidelines of the Group's personnel remuneration and incentive systems with a view to favouring the pursuit of long-term strategies, targets and results in line with the general framework of governance and risk management policies and with liquidity and capital levels, while also attracting to and retaining in the Group parties with adequate professional skills and abilities to meet business requirements, for the benefit of competition and good governance, by pursuing fairness internally and with respect to the external labour market.
The Group's pay policies also aim to guarantee adequate remuneration for long-term performance, making it possible to leverage personnel, recognise individual contributions to the achievement of results and discourage unfair conduct in relationships with customers and in terms of compliance with regulations, or conduct which tends towards excessive risk exposure or results in regulatory violations.
The pay system of Group employees includes a variable component linked to annual incentive systems (bonus). The receipt of a bonus is subject to the activation of an incentive system by the Group company in which the employee works and meeting all predefined access conditions in full (access gateways).
The bonus for key personnel (or parties whose professional activity has or may have a significant impact on the Group's risk profile, identified based on Delegated Regulation (EU) 604/2014) is broken down into:

- an up-front portion, equal to 60% of the bonus;
- three annual instalments of equal amounts, totalling 40% of the bonus, deferred over the three-year period subsequent to the year in which the up-front portion is accrued.

When the bonus recognised exceeds 300,000 euro, the portion subject to the deferral period is equal to 60% of the bonus, paid in five annual instalments of equal amounts, deferred over the five-year period subsequent to the year in which the up-front portion is accrued.
Half of the up-front portion and half of the deferred instalments of the bonus are paid in Banco BPM ordinary shares.
In addition, in line with national banking system practices and in keeping with the spirit of provisions in force, if the bonus recognised is lower than or equal to the relevant threshold of 50,000 euro and at the same time lower than or equal to one-third of the individual gross fixed annual remuneration, it is paid in a lump sum in cash; this provision does not regard high-end key personnel[1] and personnel actually affected[2] by a ratio between variable and fixed remuneration of more than 100%, to whom, therefore, the regulations regarding the deferral and allocation of shares continue to apply in full.
Starting from 2017, a three-year long-term incentive (LTI) system was introduced in the Group (the LTI bonus) correlated with the targets of the 2016-2019 Strategic Plan. This decision was made to link part of the remuneration of top company managers to the interests of shareholders which demand the creation of value for the company over time.
The receipt of the LTI bonus is also subject to meeting all predefined access conditions in full (access gateways).
The LTI bonus is paid entirely in Banco BPM ordinary shares. (performance shares), broken down into:

- an up-front portion equal to 40% of the LTI bonus;

[1] High-end key personnel for 2018 are: The Managing Director, General Manager, Joint General Managers and Managers in the first line of management of the Parent Company, the Managing Director, General Manager, Joint General Manager and Deputy General Manager (when present) of Banca Popolare di Milano, Aletti & C. Banca d'Investimento Mobiliare, Banca Akros, ProFamily and Società Gestione Servizi BP.
[2] *Ex ante.*

- three annual instalments of equal amounts, totalling 60%, deferred over the three-year period subsequent to the year in which the up-front portion is accrued.

In both systems (annual and three-year), there is a retention period (sale restriction) on the shares accrued: two years for the up-front shares and one year for the deferred shares. For the latter, the retention period starts from the moment the deferred remuneration is accrued. The assignment of shares to the respective recipients (and therefore actual transfer of ownership) takes place at the end of the retention period.
Both up-front and deferred shares are subject to malus and claw-back mechanisms, as set forth in the Policy.
The Three-Year Plan—approved by the Ordinary Shareholders' Meeting of Banco BPM on 8 April 2017—which calls for the valuation of this variable component of the pay of the executive members of the Board of Directors and employees and collaborators of the Banco BPM Banking Group in the category of top Group managers, to be paid through the free assignment of ordinary shares of Banco BPM S.p.A. under the 2017-2019 long-term incentive system.
On 7 April 2017, the Ordinary Shareholders' Meeting of Banco BPM approved, pursuant to Art. 114-*bis* of the CFL and Art 84-*bis* of the Issuers' Regulations, the compensation plans based on shares of Banco BPM, as defined in the respective Disclosure Documents prepared for this reason by the Board of Directors on 27 February 2017, on the basis of the Policy—an Annual Plan that calls for the valuation of a share of the variable component of the pay of the Group's key personnel, to be paid through the free assignment of ordinary shares of Banco BPM S.p.A. under the 2018 annual incentive system.

In addition to the compensation plan based on Banco BPM S.p.A. shares, the Ordinary Shareholders' Meeting of Banco BPM on 7 April 2018 approved:

- 2018 remuneration and incentive policies,
- the maximum limit of 2:1 for the ratio between the variable and the fixed component of the remuneration for selected figures considered strategic,
- the criteria for calculating the compensation to be granted in the event of early termination of employment or early cessation of service, including the limits set on such compensation.

For more details, please refer to the following documents: The 2018 Report on Pay, the Disclosure Document on the 2018 Annual Plan and the Disclosure Document on the Three-year 2017-2019 Plan, available on www.bancobpm.it (Corporate Governance – Remuneration Policies section).

2. Share-based compensation plans of previous years

On 27 February 2018, the Banco BPM Board of Directors approved the opening of the access gateways for the 2017 Incentive System, as well as:

- the implementation of the 2017 Plan already approved by the Ordinary Shareholders' Meeting of Banco BPM on 8 April 2017, for a total value of 2.84 million euro (estimated total amount that can be disbursed);
- access to the deferred bonuses attributable to previous years, relative to the 2014 (3rd deferred share), 2015 (2nd deferred share) and 2016 (1st deferred share) Incentive Systems, defined as part of the annual remuneration policies approved by the Ordinary Shareholders' Meetings of the former Banca Popolare di Milano S.c. a r.l on 12 April 2014, 11 April 2015 and 30 April 2016, respectively.

With regard to the 2015 Incentive System of the former Banco Popolare Banking Group, whose compensation plan was approved by the Shareholders' Meeting on 19 March 2016, the deferred share of the bonus will mature in 2019 and will be subject to a one-year retention period.
In relation to the equity instalments attributable to previous years, the number of ordinary shares of the former Banca Popolare di Milano S.c. a r.l. recognised was converted into Banco BPM S.p.A. shares – due to the merger with the former Banco Popolare Soc. Coop. – based on the value established for the share swap equal to 1 Banco BPM share for every 6.386 shares of the former Banca Popolare di Milano S.c. a r.l.; also, the recognised ordinary shares of the former Banco Popolare Soc. Coop were converted into Banco BPM S.p.A. shares – due to the merger with Banca Popolare di Milano S.c. a r.l. – based on the value established for the share swap equal to one Banco BPM share for every share of the former Banco Popolare - Soc. Coop.
For more details on the procedures and the terms for the allocation of the shares under the above-illustrated Plans, please refer to the respective disclosure documents drawn up in accordance with art. 84-*bis* of the Issuers' Regulations, deposited at the registered office of Borsa Italiana S.p.A. and also available to the general public on

Banco BPM S.p.A.'s website. www.bancobpm.it (for 2017: Corporate Governance — Remuneration Policies section; for previous years: Corporate Governance — Historic Documentation — Shareholders' Meetings section).

3. Employee termination compensation

For some parties categorised as key personnel, in specific cases of termination of the employment relationship, they are entitled to agree—in accordance with the methods defined in the Policy—on golden parachutes to the maximum extent of two years of gross fixed annual pay up to the maximum limit of euro 2.4 million (employee gross amount).
Without prejudice to the exceptions set forth in the Bank of Italy Supervisory Instructions, the disbursement takes place in concurrent compliance with the following criteria:

- one up-front instalment equal to 60%, and three annual instalments of equal amounts, totalling 40%, for parties for whom the amount of the golden parachute is less than or equal to 600,000 euro;
- one up-front instalment equal to 40%, and five annual instalments of equal amounts, totalling 60%, for parties for whom the amount exceeds 600,000 euro;
- 50% of each instalment in cash and 50% in Banco BPM S.p.A. ordinary shares.

There is a retention period on matured shares of two years for the up-front shares and of one year for the deferred shares. For the latter, the retention period starts from the moment deferred remuneration is accrued.
Both up-front and deferred shares are subject to malus and claw-back mechanisms, as set forth in the remuneration policies in force.
The most significant personnel incentive plans described above, which involve payment based on the shares of the Parent Company, are equity settled plans in accordance with the provisions of IFRS 2. These share-based payments are recognised in the income statement under "Personnel expenses" with a balancing entry of an increase in "Reserves" in consolidated shareholders' equity and in the shareholders' equity of the Parent Company.
Subsidiaries, on the other hand, in their separate financial statements, record the cost for the period in the income statement item "Administrative expenses: Personnel expenses" as a balancing entry of an increase in the liability balance sheet item "Provisions for risks and charges", in that the most significant personnel incentive plans establish payment based on the shares of the Parent Company, which will be regulated by the individual subsidiaries and, therefore, are considered cash-settled transactions.

B. QUANTITATIVE INFORMATION

4. Annual changes

On 7 November 2017, the share warehouse was set up–through the repurchase of shares resulting from exercising the right of withdrawal connected with the merger between Banco Popolare - Soc. Coop. and Banca Popolare di Milano S.c. a r.l.–with 4,627,460 ordinary shares of Banco BPM S.p.A.
On 20 November 2017–in implementation of the remuneration and incentive policies of the former BPM Group - a total of 135,206 ordinary shares of Banco BPM S.p.A. were delivered, of which (i) 104,879 to 19 beneficiaries of the bonus recognised under the 2014 Incentive System, in relation to the up-front and the first deferred share, matured respectively in 2015 and 2016; (ii) 30,327 to a person who left the company for the golden parachute recognised in 2015, in relation to the up-front and first deferred share, which matured in 2015 and 2016 respectively.
The share warehouse balance at 1 January 2018 consisted of 4,492,254 ordinary shares of Banco BPM S.p.A.
During the first half of 2018—in implementation of the remuneration and incentive policies of the former BPM Group and the former Banco Popolare Group—a total of 314,635 ordinary shares of Banco BPM S.p.A. were delivered to 73 beneficiaries, in relation to the up-front portions of the respective 2015 Incentive Systems, which matured in 2016.
The share warehouse balance at 30 June 2018 consisted of 4,177,619 ordinary shares of Banco BPM S.p.A.

5. Other information

Regarding the 2017 Incentive System for key personnel, the surpassing of the access gateways relating to the 2017 performance year determined the equity component of remuneration of 2,055,645 euro overall (employee gross amount). Surpassing these access gateways also entailed the accrual of the following share portions (referring to amounts at a consolidated level):

- 2017 Incentive System—up-front share instalment—1,140,135 euro (employee gross amount);

- 2016 Incentive System for former BPM Banking Group—1st deferred equity instalment - 140,394 euro (employee gross amount);
- 2015 Incentive System for former BPM Banking Group - 2nd deferred equity instalment—150,379 euro (employee gross amount);
- 2015 Incentive System for former Banco Popolare Group—no equity instalments were accrued;
- 2014 Incentive System for former BPM banking group—3rd deferred equity instalment—113,676 euro (employee gross amount).

Regarding the long-term 2017-2019 Incentive System, international accounting standards were adopted, which require the vesting period of rights to be taken into account; therefore, an amount of 953,000 euro was set aside, corresponding to one third of the up-front portion of the ILT bonus that could reach maturity in 2020.
In relation to a golden parachute recognised in 2017 to one person classified as key personnel of the former BPM Banking Group, the 1st deferred equity instalment equal to 12,000 euro (employee gross amount) was accrued in 2018.

PART L - SEGMENT REPORTING

According to IFRS 8, companies must provide information enabling users of financial statements to assess the nature and the effects on the financial statements of their business activities and the economic contexts in which they operate.
Therefore, it is necessary to highlight the contribution of the various operating segments to the formation of the group’s income.

The identification of the operating segments of this Section is consistent with the procedures adopted by the Company Management to make operating decisions and is based on internal reporting, used for allocating resources to the various segments and the analysis of their performance.

For this reason, and in order to improve the representation of the Group's profitability, also highlighted are operating segments that are below the quantitative thresholds put forward in paragraph 13 of IFRS 8.

Due to the business combination between the Banco Popolare Group and the BPM Group in 2017, it was necessary to partially modify the operating segments previously identified by Banco Popolare (defined as the buyer from the accounting perspective). Subsequently, during the current financial year, further changes were introduced in order to fully implement the Group's business model, as set out in the 2017-2019 Strategic Plan. In particular, a new structure for the Commercial Network was defined. The changes in question were also made as a result of the extraordinary transactions, which profoundly changed the presence of the Banco BPM Group in asset management (disposal of Aletti Gestielle SGR at the end of December 2017) and in bancassurance and which will give a specialist connotation to Banca Akros S.p.A. and Banca Aletti S.p.A.. Therefore, compared to the structure of the Segment Reporting in 2017:

- the Commercial Network has been redefined into the new Retail, Corporate, Institutional and Private business lines (the latter was included in the Private&Investment Banking business line in 2017)
- the Private & Investment Banking business line, present during the previous financial year, was split into the Private segment (now concentrated in Banca Aletti) and the Investment Banking segment (represented by Banca Aletti's Investment Banking division and Banca Akros);
- the Strategic Partnership component (Agos Ducato S.p.A., Vera Vita S.p.A., Vera Assicurazioni S.p.A., Factorit S.p.A., SelmaBipiemme Leasing S.p.A. and Anima Holding S.p.A.) was separated from the Equity Investments segment, which in 2017 was located within the Corporate Centre;
- as a result of the aforementioned extraordinary transactions, concerning the Wealth Management sector, the latter was excluded from this Sector Information.

For 2018, the operating segments taken as a reference to provide the disclosure in question are as follows:

- Retail;
- Corporate;
- Institutional;
- Private;
- Investment Banking;
- Strategic Partnerships;
- Leasing;
- Corporate Centre.

Lastly, note that the justification for identifying leasing as an operating segment lies in the need to provide separate evidence of a run-off activity, the economic contribution indicated of which is, therefore, represented solely by the result deriving from the management of the progressive reduction in assets and liabilities of the former Banca Italease (today incorporated within Banco BPM) and the subsidiary Release.

In light of the new structure of the operating segments, illustrated above, the figures for 2017 have been restated, also in order to retroactively reflect the effects of presenting the contribution of Aletti Gestielle SGR in a separate item, in line with the requirements of IFRS 5.
However, it should be noted that, despite this restatement, the balances for the previous year are not fully comparable, as a result of the first time adoption of IFRS 9 as explained in more detail in the paragraph “Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers”.

Segment results – income statement figures

1st half. 2018	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Interest margin	1,180,109	620,542	237,514	29,616	(590)	47,352	(5,366)	27,012	224,029
Profits (losses) on investments in associates and companies subject to joint control carried at equity	75,998	-	-	-	-	-	74,792	-	1,206
Financial margin	**1,256,107**	**620,542**	**237,514**	**29,616**	**(590)**	**47,352**	**69,426**	**27,012**	**225,235**
Net fee and commission income	927,513	760,176	84,878	14,967	43,704	14,039	-	5	9,744
Other net operating income	154,179	3,319	458	2,637	(2,342)	(150)	-	9,330	140,927
Net financial result	109,490	6,953	25,405	118	8	(4,005)	8,354	(16)	72,673
Other operating income	**1,191,182**	**770,448**	**110,741**	**17,722**	**41,370**	**9,884**	**8,354**	**9,319**	**223,344**
Operating income	**2,447,289**	**1,390,990**	**348,255**	**47,338**	**40,780**	**57,236**	**77,780**	**36,331**	**448,579**
Personnel expenses	(879,149)	(586,400)	(25,786)	(3,831)	(25,798)	(12,222)	(917)	(3,447)	(220,748)
Other administrative expenses	(414,589)	(517,792)	(40,539)	(4,617)	(11,674)	(28,997)	(291)	(19,190)	208,511
Net value adjustments on property, plant and equipment and intangible assets	(96,946)	-	-	-	-	(557)	-	(8,157)	(88,232)
Operating expenses	**(1,390,684)**	**(1,104,192)**	**(66,325)**	**(8,448)**	**(37,472)**	**(41,776)**	**(1,208)**	**(30,794)**	**(100,469)**
Profit (loss) from operations	**1,056,605**	**286,798**	**281,930**	**38,890**	**3,308**	**15,460**	**76,572**	**5,537**	**348,110**
Net adjustments on loans to customers	(686,451)	(472,800)	(184,426)	(412)	(10)	75	-	(15,600)	(13,278)
Net adjustments on securities and other financial assets	635	-	-	-	-	51	-	-	584
Net provisions for risks and charges	(45,671)	(59,267)	10,066	718	(46)	5,884	-	(10,281)	7,255
Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments	178,550	-	-	-	-	-	174,656	(102)	3,996
Profit (loss) before tax from continuing operations	**503,668**	**(245,269)**	**107,570**	**39,196**	**3,252**	**21,470**	**251,228**	**(20,446)**	**346,667**
Taxes on income from continuing operations	(87,257)	67,449	(29,582)	(10,779)	(894)	(6,953)	9,798	2,520	(118,816)
Charges related to the banking system, net of taxes	(67,428)	(47,783)	(2,619)	(465)	(1,754)	(3,724)	-	-	(11,083)
Profit (loss) from discontinued operations	4	-	-	-	-	-	-	-	4
Income (loss) attributable to minority interests	3,590	-	-	-	-	-	-	3,421	169
Income (loss) for the period without Badwill	**352,577**	**(225,603)**	**75,369**	**27,952**	**604**	**10,793**	**261,026**	**(14,505)**	**216,941**
Merger difference (Badwill)	-	-	-	-	-	-	-	-	-
Parent Company's net income (loss)	**352,577**	**(225,603)**	**75,369**	**27,952**	**604**	**10,793**	**261,026**	**(14,505)**	**216,941**

The following table shows the breakdown of commission income by type of service provided and IFRS 8 operating segment, in line with the disclosure requirements introduced by IFRS 15 for interim financial reports.

Service type/amounts	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Distribution of savings products, order collection and trading of securities and currencies:	**436,700**	**346,742**	**480**	**2,770**	**43,931**	**33,299**	**-**	**-**	**9,478**
- administered, trading securities, currencies and acceptance of orders	72,448	35,216	140	864	3,426	32,382	-	-	420
- managements and funds	331,229	283,161	300	1,829	37,744	917	-	-	7,278
- bancassurance	33,023	28,365	40	77	2,761	-	-	-	1,780
Distribution of insurance products	**22,387**	**18,796**	**3**	**12**	**26**	**-**	**-**	**-**	**3,550**
Distribution of consumer credit products	**20,516**	**24,825**	**-**	**5**	**19**	**-**	**-**	**-**	**(4,333)**
Transactional banking services (e-money, portfolio and collection and payment services)	**158,465**	**138,261**	**16,124**	**6,609**	**670**	**8**	**-**	**-**	**(3,207)**
Current account management and loans:	**338,434**	**256,335**	**66,300**	**6,135**	**874**	**41**	**-**	**9**	**8,740**
- cash loans and unsecured loans	203,248	140,480	56,512	2,777	254	27	-	9	3,189
- current accounts, deposits and foreign	135,186	115,855	9,788	3,358	620	14	-	-	5,551
Other services	**6,818**	**6,892**	**1,633**	**228**	**22**	**2,901**	**-**	**-**	**(4,858)**
Fee and commission income	**983,320**	**791,851**	**84,540**	**15,759**	**45,542**	**36,249**	**-**	**9**	**9,370**
Fee and commission expense	(55,807)								
Net fee and commission income	**927,513**								

1st half 2017 (*)	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Interest margin	1,059,756	527,774	233,092	27,975	(3,254)	68,389	(7,655)	19,063	194,372
Profits (losses) on investments in associates and companies subject to joint control carried at equity	81,939	-	-	-	-	-	80,776	-	1,163
Financial margin	**1,141,695**	**527,774**	**233,092**	**27,975**	**(3,254)**	**68,389**	**73,121**	**19,063**	**195,535**
Net fee and commission income	1,019,379	837,872	88,367	19,973	39,548	11,749	-	4	21,866
Other net operating income	44,678	1,663	421	2,093	19	12	-	7,805	32,665
Net financial result	100,177	9,366	4,969	31	6	5,610	10,992	-	69,203
Other operating income	**1,164,234**	**848,901**	**93,757**	**22,097**	**39,573**	**17,371**	**10,992**	**7,809**	**123,734**
Operating income	**2,305,929**	**1,376,675**	**326,849**	**50,072**	**36,319**	**85,760**	**84,113**	**26,872**	**319,269**
Personnel expenses	(913,430)	(612,664)	(26,941)	(4,003)	(18,971)	(16,932)	(958)	(3,903)	(229,058)
Other administrative expenses	(431,348)	(483,789)	(36,336)	(4,303)	(11,095)	(24,059)	(296)	(19,715)	148,245
Net value adjustments on property, plant and equipment and intangible assets	(109,289)	-	-	-	-	(4,855)	-	(6,895)	(97,539)
Operating expenses	**(1,454,067)**	**(1,096,453)**	**(63,277)**	**(8,306)**	**(30,066)**	**(45,846)**	**(1,254)**	**(30,513)**	**(178,352)**
Profit (loss) from operations	**851,862**	**280,222**	**263,572**	**41,766**	**6,253**	**39,914**	**82,859**	**(3,641)**	**140,917**
Net adjustments on loans to customers	(647,020)	(392,297)	(180,909)	3,396	(33)	1,094	-	(78,289)	18
Net adjustments on securities and other financial assets	(79,177)	-	-	-	-	25	-	-	(79,202)
Net provisions for risks and charges	(9,137)	(4,288)	6,903	580	(1)	1,119	-	(37)	(13,413)
Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments	13,301	-	-	-	-	-	-	(10)	13,311
Profit (loss) before tax from continuing operations	**129,829**	**(116,363)**	**89,566**	**45,742**	**6,219**	**42,152**	**82,859**	**(81,977)**	**61,631**
Taxes on income from continuing operations	(43,776)	32,000	(24,631)	(12,579)	(1,710)	(13,271)	2,482	13,153	(39,220)
Charges related to the banking system, net of taxes	(45,008)	(49,954)	(3,752)	(444)	(58)	(3,110)	-	-	12,310
Profit (loss) from discontinued operations	45,793	-	-	-	-	-	-	-	45,793
Income (loss) attributable to minority interests	7,394	-	-	-	-	-	-	7,578	(184)
Income (loss) for the period without Badwill	**94,232**	**(134,317)**	**61,183**	**32,719**	**4,451**	**25,771**	**85,341**	**(61,246)**	**80,330**
Merger difference (Badwill)	3,076,137	-	-	-	-	-	-	-	3,076,137
Parent Company's net income (loss)	**3,170,369**	**(134,317)**	**61,183**	**32,719**	**4,451**	**25,771**	**85,341**	**(61,246)**	**3,156,467**

(*) The figures relating to the previous period have been restated to provide a like-for-like comparison.

Segment results – balance sheet figures

30/06/2018	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Loans to customers:	120,604,947	56,583,415	27,721,322	5,485,052	227,482	1,934,744	-	2,987,113	25,665,819
- loans to customers	105,076,716	56,583,415	27,621,322	5,485,052	227,482	1,934,744	-	2,987,113	10,237,588
- debt securities	15,528,231	-	100,000	-	-	-	-	-	15,428,231

31/12/2017 (*)	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Loans to customers	108,176,382	57,948,163	26,677,841	5,423,612	219,600	1,556,011	-	3,244,333	13,106,822

(*) The figures relating to the previous period have been restated to provide a like-for-like comparison.

30/06/2018	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Direct funding	105,505,599	70,005,127	7,278,926	10,365,316	3,072,378	1,285,877	-	6,760	13,491,216

31/12/2017 (*)	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Direct funding	107,509,849	70,167,867	8,341,857	8,881,274	2,894,188	1,638,771	-	9,047	15,576,845

(*) The figures relating to the previous period have been restated to provide a like-for-like comparison.

30/06/2018	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Equity investments	1,355,065	-	-	-	-	-	1,337,332	-	17,733

31/12/2017 (*)	Total	Retail	Corporate	Institutional	Private	Investment Banking	Strategic Partnerships	Leasing	Corporate Centre
Equity investments	1,349,191	-	-	-	-	-	1,331,320	-	17,871

(*) The figures relating to the previous period have been restated to provide a like-for-like comparison.

Note that the majority of the assets and operating income were generated in Italy, confirming the deep-seated presence in the national territory, considered to be the Group's primary sphere of operations. The weight of activities and operating income earned abroad is significantly below the threshold of 5%.

Certification of the consolidated condensed interim financial statements pursuant to art. 81-ter of Consob Regulation no. 11971 of 14 May 1999 and subsequent amendments and additions

CERTIFICATION OF THE CONSOLIDATED CONDENSED INTERIM FINANCIAL STATEMENTS PURSUANT TO ART. 81-*TER* OF CONSOB REGULATION NO. 11971 OF 14 MAY 1999 AND SUBSEQUENT AMENDMENTS AND ADDITIONS

1. The undersigned, Giuseppe Castagna, as Managing Director of Banco BPM S.p.A. and Gianpietro Val, as Manager responsible for preparing the company's financial reports of Banco BPM S.p.A. hereby certify, also in consideration of the provisions of Art. 154-*bis*, paragraphs 3 and 4, of Italian Legislative Decree no. 58 dated 24 February 1998:

   - the adequacy in relation to the characteristics of the company and
   - the effective application

   of the administrative and accounting procedures for the formation of the consolidated condensed interim financial statements in the first half of 2018.

2. The assessment of the adequacy and the verification of the effective application of the administrative and accounting procedures for the formation of the consolidated condensed interim financial statements as at 30 June 2018 were based on an internal model set in place by Banco BPM S.p.A., developed on the basis of the Internal Control – Integrated Framework (COSO)" and, for the IT component, the "Control Objectives for IT and related Technology (COBIT)", which represent the standard for the internal audit system generally accepted at international level.

3. We also hereby certify that:

   3.1 the consolidated condensed interim financial statements as at 30 June 2018:

   a) were drawn up in compliance with the applicable international accounting standards recognised in the European Community as per EC Regulation no. 1606/2002 of the European Parliament and Commission, dated 19 July 2002;

   b) comply with the results of the accounting records and journal entries;

   c) are suitable for providing a true and fair view of the balance sheet, income statement and financial situation of the issuer and of all the companies included within the scope of consolidation.

   3.2 The interim report on operations includes a reliable analysis of the important events which occurred during the first six months of the year and their impact on the consolidated condensed interim financial statements, together with a description of the main risks and uncertainties for the remaining six months of the year. The interim report on operations also includes a reliable analysis of the information on significant transactions with related parties.

Verona, 03 August 2018

signed by Giuseppe Castagna Managing Director	signed by Gianpietro Val Manager responsible for preparing the Company's financial reports

Independent Auditors' Report

REVIEW REPORT ON CONSOLIDATED CONDENSED INTERIM FINANCIAL STATEMENTS AS OF 30 JUNE 2018

To the shareholders of
Banco BPM SpA

Foreword

We have reviewed the accompanying consolidated condensed interim financial statements of Banco BPM SpA and its subsidiaries (Banco BPM Group) as of 30 June 2018, comprising the balance sheet, the income statement, the statement of comprehensive income, the statement of changes of shareholder's equity, cashflow statement and related illustrative notes. The Directors of Banco BPM SpA are responsible for the preparation of the consolidated condensed interim financial statements in accordance with International Accounting Standard 34 applicable to interim financial reporting (IAS 34) as adopted by the European Union. Our responsibility is to express a conclusion on these consolidated condensed interim financial statements based on our review.

Scope of review

We conducted our work in accordance with the criteria for a review recommended by Consob in Resolution No. 10867 of 31 July 1997. A review of consolidated condensed interim financial statements consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than a full-scope audit conducted in accordance with International Standards on Auditing (ISA Italia) and, consequently, does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion on the consolidated condensed interim financial statements.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying consolidated condensed interim financial statements of Banco BPM Group as of 30 June 2018 are not prepared, in all material respects, in accordance with International Accounting Standard 34 applicable to interim financial reporting (IAS 34) as adopted by the European Union.

Milan, 7 August 2018

PricewaterhouseCoopers SpA

Signed by

Pierfrancesco Anglani
(Partner)

This report has been translated into English from the Italian original solely for the convenience of international readers

Attachments

Reclassified consolidated balance sheet - reconciliation between the balances at 31 December 2017 and at 1 January 2018

In order to give a better understanding of the transition to the new IFRS 9 and IFRS 15 accounting standards, the following table provides the reconciliation between the balances at 31 December 2017 and at 1 January 2018 for each item on the reclassified balance sheet, with separate evidence of the changes attributable to the IFRS 9 and IFRS 15 accounting standards.
Regarding the IFRS 9 standard, the changes attributable to the new classification criteria and the impacts relating to the new measurement criteria (with separate indication of those relating to the new impairment model of expected losses ECL – Expected Credit Losses) are shown. To this end, the balances at 31 December 2017 (IAS 39) have been conventionally reclassified into the new accounting categories (column "31/12/2017 (IAS 39)"); the "IFRS 9 Reclassifications" column illustrates the IAS 39 balances reallocated according to the new classification rules provided for by IFRS 9 and the "IFRS 9 Measurement Impacts" and "IFRS 9 ECL Impacts" columns provide the impacts relating to the new measurement criteria (excluding the impacts of expected losses) and impairment respectively. With reference to IFRS 15, the "IFRS 15 Impacts" column shows the liability recorded in FTA with the related tax impact and the change in shareholders' equity.
For a better understanding of the impacts concerning the transition to the new IFRS 9 and IFRS 15 accounting standards, as well as the criteria for preparing the balance sheet in a reclassified form, please refer to:

- "Disclosure on the first adoption of the accounting standards IFRS 9 – Financial instruments and IFRS 15 – Revenue from contracts with customers" section, contained within these condensed interim financial statements;
- the disclosure contained within the "Results" section of the Interim Report on Operations.

(in thousands of euro)	31/12/2017 (IAS 39)	Reclassifications IFRS 9 (a)	31/12/2017 (IAS 39) reclassified	Measurement Impacts IFRS 9 (b)	ECL Impacts IFRS 9 (c)	ECL Impacts IFRS 15	01/01/2018
Cash and cash equivalents	976,686	-	976,686	-	-		976,686
Loans measured at Amortised Cost	112,681,902	(314,696)	112,367,206	-	(1,322,458)		111,044,748
- Loans to banks	4,939,223 (1)	-	4,939,223	-	(2,716)		4,936,507
- Loans to customers	107,742,679 (2)	(314,696)	107,427,983	-	(1,319,742)		106,108,241
Financial assets and hedging derivatives	34,533,172	314,696	34,847,868	50,405	(13,475)		34,884,798
- Designated at FV through IS	5,184,586	1,251,406	6,435,992	(18,908)	-		6,417,084
- Designated at FV through OCI	17,128,622 (3)	(430,150)	16,698,472	51,600	-		16,750,072
- Designated at AC	12,219,964 (4)	(506,560)	11,713,404	17,713	(13,475)		11,717,642
Investments in associates and companies subject to joint control (*)	1,349,191	-	1,349,191	(92,348)	-		1,256,843
Property, plant and equipment	2,735,182	-	2,735,182	-	-		2,735,182
Intangible assets	1,297,160	-	1,297,160	-	-		1,297,160
Tax assets	4,520,189	-	4,520,189	923	370,675	5,610	4,897,397
Non-current assets and asset disposal groups held for sale	106,121	-	106,121	-	-		106,121
Other assets	3,007,162	-	3,007,162	-	-		3,007,162
Total ASSETS	**161,206,765**	**-**	**161,206,765**	**(41,020)**	**(965,258)**	**5,610**	**160,206,097**
Due to banks	27,199,304	-	27,199,304	-	-		27,199,304
Direct funding	107,509,849	-	107,509,849	15,254	-		107,525,103
- Due to customers	87,848,146	-	87,848,146	-	-		87,848,146
- Securities and financial liabilities designated at FV	19,661,703	-	19,661,703	15,254	-		19,676,957
Other financial liabilities designated at FV	8,707,966	-	8,707,966	(3,618)	-		8,704,348
Liability provisions	1,580,461 (5)	-	1,580,461	-	16,451	20,400	1,617,312
Tax liabilities	669,494	-	669,494	21,037	1,192		691,723
Liabilities associated with assets held for sale	35	-	35	-	-		35
Other liabilities	3,576,116 (6)	-	3,576,116	-	-		3,576,116
Total LIABILITIES	**149,243,225**	**-**	**149,243,225**	**32,673**	**17,643**	**20,400**	**149,313,941**
Minority interests	63,310	-	63,310	-	(5,743)		57,567
Group shareholders' equity	11,900,230	-	11,900,230	(73,693)	(977,158)	(14,790)	10,834,589
CONSOLIDATED SHAREHOLDERS' EQUITY	**11,963,540**	**-**	**11,963,540**	**(73,693)**	**(982,901)**	**(14,790)**	**10,892,156**

Reclassification of IAS 39 balances on the basis of new items for financial assets and liabilities

a) FTA impacts of IFRS 9 arising from the new measurement criteria for items related to financial assets and financial liabilities (excluding ECL)

b) FTA impacts of IFRS 9 arising from the new Expected Credit Losses (ECL) model

(*) Impact on investments in associates and companies subject to joint control following the restatement of shareholders' equity based on IFRS 9 by investees.

(1) *Corresponds to the previous balance sheet item "due from banks" (5,164,715 thousand), net of assets represented by debt securities (225,492 thousand).*
(2) *Corresponds to the previous balance sheet item "loans to customers" (108,176,382 thousand), net of assets represented by debt securities (433,703 thousand).*
(3) *In the item "assets designated at FV through OCI" the portfolio pursuant to IAS 39 of "Financial assets available for sale" has been entirely reclassified.*
(4) *The item "Financial assets designated at amortised cost" includes the balance of the portfolio pursuant to IAS 39 of "Financial assets held to maturity" (11,560,769 thousand) and loans to customers and banks represented by debt securities, as illustrated in points 1) and 2) above (for a total of 659,195 thousand).*
(5) *The item "Liability provisions" includes the balances of the items pursuant to IAS 39 "Provisions for employee severance indemnity" and "Provisions for risks and charges", increased by the "Risk coverage for guarantees given and commitments", which was included in the item "Other liabilities" in the IAS 39 financial statements.*
(6) *The item "Other liabilities" is net of "Risk coverage for guarantees given and commitments" (119,472 thousand) reclassified under the item "Liability provisions".*

Reconciliation between the items in the consolidated income statement and the reclassified consolidated income statement schedule for the first half of 2018

1st half 2018	**Income statement**	**Reclassifications**		**Reclassified income statement**
Interest margin				**1,180,109**
10. Interest and similar income	1,480,257			
20. Interest and similar expense	(300,148)			
Profits (losses) on investments in associates and companies subject to joint control carried at equity				
250. Profits (losses) on investments in associates and companies subject to joint control		75,998	(a)	**75,998**
Financial margin				**1,256,107**
Net fee and commission income				**927,513**
40. Fee and commission income	983,320			
50. Fee and commission expense	(55,807)			
Other net operating income				154,179
230. Other operating expenses/income	313,022	9,060	(b)	
		(141,850)	(c)	
		(5,089)	(d)	
		(20,964)	(e)	
Net financial result				**109,490**
70. Dividends and similar income	40,576			
80. Profits (losses) on trading	(66,287)			
90. Fair value adjustments in hedge accounting	(460)			
100 Profits (losses) on disposal or repurchase	(131,771)	261,743	(f)	
110. Profits (losses) on other financial assets and liabilities designated at fair value through profit and loss	5,689			
Other operating income				**1,191,182**
Operating income				**2,447,289**
Personnel expenses				**(879,149)**
190 a) Personnel expenses	(880,353)	(3,885)	(g)	
190 b) Other administrative expenses		5,089	(d)	
Other administrative expenses				
190 b) Other administrative expenses	(653,827)	3,885	(g)	**(414,589)**
		141,850	(c)	
		93,503	(m)	
Net value adjustments on property and equipment and intangible assets				**(96,946)**
210. Net adjustments to/recoveries on property and equipment	(56,012)			
220. Net adjustments to/recoveries on intangible assets	(52,838)	20,964	(e)	
230. Other operating expenses/income		(9,060)	(b)	
Operating expenses				**(1,390,684)**
Profit (loss) from operations				**1,056,605**
Net adjustments on loans to customers				**(686,451)**
130 a) Net adjustments to/recoveries on credit risk related to financial assets designated at amortised cost	(420,875)	(1,909)	(h)	
		64	(i)	

1st half 2018	Income statement	Reclassifications		Reclassified income statement
		(1,988)	(l)	
		(261,743)	(f)	
Net adjustments on securities and other financial assets				**635**
130 b) Net adjustments to/recoveries from credit risk related to financial assets designated at fair value through other comprehensive income	(3,198)			
		1,909	(h)	
		(64)	(i)	
		1,988	(l)	
Net provisions for risks and charges				**(45,671)**
200. Net provisions for risks and charges	(45,671)			
Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments				178,550
250. Profits (losses) on investments in associates and companies subject to joint control	250,654	(75,998)	(a)	
280. Profits (losses) on disposal of investments	3,894			
Profit (loss) before tax from continuing operations				**503,668**
Taxes on income from continuing operations				**(87,257)**
300. Taxes on income from continuing operations	(61,182)	(26,075)	(m)	
Charges related to the banking system, net of taxes		(67,428)	(m)	**(67,428)**
Profit (loss) from discontinued operations				**4**
320. Profit (loss) from discontinued operations, net of taxes	4			
Income (loss) attributable to minority interests				**3,590**
340. Income (loss) after tax from discontinued operations	3,590			
Parent Company's net income (loss)	**352,577**	**-**		**352,577**

The letters shown beside the column "Reclassifications" have been included to give a better understanding of the reclassifications carried out.

With reference to the reconciliation provided above, please note that:

- The item **"Interest margin"** is represented by the algebraic balance of interest and similar income (item 10) and interest and similar expense (item 20);
- the item **"Profits (losses) on investments in associates and companies subject to joint control carried at equity"** shows the portion of profits (losses) pertaining to investee companies carried at equity (included in item 250) totalling 76.0 million euro (a), and together with the interest margin, the aggregate is defined as the **"Financial margin"**;
- The item "net fee and commission income" is represented by the algebraic balance of fee and commission income (item 40) and expense (item 50);
- the item **"Other net operating income"** is represented by the financial statement item "230 Other operating expense/income", (i) with the recoveries on indirect taxes, legal fees and other expenses, totalling 141.8 million euro (c), separated out, which, for reclassification purposes are shown in the item "Other administrative expenses" and (ii) with the recovery of training costs of 5.1 million euro (d), classified in "Personnel expenses", also separated out. The aggregate of "Other net operating income" does not include the amortisation charges on costs for improvements to third party assets of 9.1 million euro (b) (recognised in the reclassified item "Net value adjustments on property and equipment and intangible assets") and does include value adjustments to intangible assets with a definite useful life (client relationship) of 21.0 million euro (e) (taken from item 220 of the official schedule). The effect of the aforementioned reclassifications was -158.8 million euro;
- the income statement item "Net financial result" includes "Dividends and similar income" (item 70), "Profits (losses) on trading" (item 80), "Fair value adjustments in hedge accounting" (item 90), "Profits (losses) on financial assets and liabilities designated at fair value through profit and loss" (item 110). It also includes "Profits (losses) on disposal or repurchase" (item 100), with the exception of the loss of 261.7 million euro (f) relating to the disposal of loans not represented by debt securities, classified in the operational aggregate "Net adjustments on loans to customers";
- the item **"Personnel expenses"** is represented by the financial statement item "190 a) Personnel expenses" and by several charges functionally related to personnel, amounting to 3.9 million euro (g), recognised in the financial statements under item "190 b) Other administrative expenses" and by the recovery of training costs of 5.1 million euro (d), recorded under item "230 Other operating expense/income", as described above;

- the item **"Other administrative expenses"** is represented by the financial statement item 190 b), net of recoveries on indirect taxes, legal fees and other expenses, totalling 141.8 million euro (c), included in the item "230 Other operating expense/income", as described above, and of several charges connected to personnel, recognised in the reclassified item "Personnel expenses" for 3.9 million euro (g). Ordinary and extraordinary charges totalling 93.5 million euro (m) introduced for banks under the single and national resolution funds (SRF and NRF) and the deposit guarantee scheme (DGS) are also excluded and are shown, net of the related tax effect, in the separate item "Charges related to the banking system, net of taxes";
- the item **"Net value adjustments on property and equipment and intangible assets"** equals the balance sheet items 210 and 220, gross of the portion of amortisation on costs for improvements to third party assets, for 9.1 million euro (b), recognised in the item "230 Other operating expense/income" and net of the adjustments to intangible assets with definite useful lives (client relationship), grouped in the reclassified aggregate "Other net operating income", for 21.0 million euro (b). The overall effect of the aforementioned adjustments on the aggregate was a positive figure of 11.9 million euro;
- the total of **"Net adjustments on loans to customers**" and **"Net adjustments on securities and other financial assets"** starts from item 130 of the income statement "Net losses/recoveries for credit risk". Specifically, "Net adjustments on loans to customers" include adjustments to the value of exposures classified in the portfolio of financial assets designated at amortised cost - loans to customers - loans, as well as the negative result of the disposal of loans, amounting to 261,7 million euro (f) (included in item 100).
  The aggregate of "Net adjustments on securities and other financial assets" includes net adjustments on exposures classified in the portfolio of financial assets designated at amortised cost—loans to banks—loans (h), as well as net adjustments for impairment of exposures classified in the portfolio of financial assets designated at amortised cost consisting of debt securities (included in item 130) issued by banks (i) and by customers (l) totalling 1.9 million euro;
- the **"Net provisions for risks and charges"** corresponds to item 200 of the official income statement;
- **"Profits (losses) on disposal of investments in associates and companies subject to joint control and other investments"** correspond to item 280 of the official income statement and to the net income on the disposal of investments carried at equity (item 250 of the official income statement), net of the portion of profits (losses) of the investees valued at equity, overall a positive 76.0 million euro (a) included in the reclassified aggregate "Profits (losses) on investments in associates and companies subject to joint control carried at equity";
- the item **"taxes on income from continuing operations"** corresponds to item 300 of the official income statement, net of the tax effect of system expenses, amounting to 26.1 million euro (m), as previously illustrated;
- the item **"Charges related to the banking system, net of taxes"** includes the aforementioned ordinary and extraordinary charges for a total of 93.5 million euro (m) recognised in the accounts in item 190 b) of the official income statement, net of the related tax effect, amounting to 26.1 million euro (m).

Reconciliation between the items in the consolidated balance sheet and the reclassified consolidated balance sheet as at 30 June 2018

Asset items *(in thousands of euro)*		**30/06/2018**
10.	Cash and cash equivalents	796,466
	Cash and cash equivalents	**796,466**
40. a)	Financial assets designated at amortised cost: due from banks	5,489,437
	less: debt securities to banks at amortised cost	(179,494)
	Loans designated at AC: loans to banks	**5,309,943**
40. b)	Financial assets designated at amortised cost: loans to customers	120,604,947
	plus: senior securities relative to Project Exodus (GACS)	1,654,186
	less: debt securities to customers at amortised cost	(15,528,231)
	Loans designated at AC: loans to customers	**106,730,902**
20.	Financial assets designated at fair value through profit and loss	7,800,964
50.	Hedging derivatives	176,497
	Financial assets and hedging derivatives designated at FV through IS	**7,977,461**
30.	Financial assets designated at fair value through other comprehensive income	19,017,645
	Financial assets and hedging derivatives designated at FV through OCI	**19,017,645**
	debt securities to banks and customers at amortised cost	15,707,725
	less: senior securities relative to Project Exodus (GACS)	(1,654,186)
	Financial assets and hedging derivatives designated at AC	**14,053,539**
70.	Equity investments	1,355,065
	Equity investments	**1,355,065**
90.	Property, plant and equipment	2,733,275
	Property, plant and equipment	**2,733,275**
100.	Intangible assets	1,295,196
	Intangible assets	**1,295,196**
110.	Tax assets	4,903,767
	Tax assets	**4,903,767**
120.	Non-current assets and asset disposal groups held for sale	44,861
	Non-current assets and asset disposal groups held for sale	**44,861**
60.	Fair value change of financial assets in macro fair value hedge portfolios (+/-)	48,577
130.	Other assets	2,762,381
	Other assets	**2,810,958**
	Total assets	**167,029,078**

Liability items ***(in thousands of euro)***		**30/06/2018**
10. a)	Financial liabilities designated at amortised cost: due to banks	31,550,552
	Due to banks	**31,550,552**
10. b)	Financial liabilities designated at amortised cost: due to customers	87,659,619
10. c)	Financial liabilities designated at amortised cost: debt securities issued	15,125,167
30.	Financial liabilities designated at fair value	2,720,813
	Direct funding	**105,505,599**
20.	Financial liabilities held for trading	8,210,839
40.	Hedging derivatives	753,379
	Other financial liabilities designated at fair value	**8,964,218**
90.	Employee termination indemnities	396,185
100.	Provisions for risks and charges	1,135,843
	Liability provisions	**1,532,028**
60.	Tax liabilities	606,246
	Tax liabilities	**606,246**
70.	Liabilities associated with assets held for sale	4,212,805
	Liabilities associated with assets held for sale	**4,212,805**
50.	Fair value change of financial liabilities in macro fair value hedge portfolios (+/-)	36,830
80.	Other liabilities	3,734,255
	Other liabilities	**3,771,085**
	Total liabilities	**156,142,533**
190.	Minority interests (+/-)	52,510
	Minority interests	**52,510**
120.	Valuation reserves	(178,829)
150.	Reserves	3,573,442
170.	Share capital	7,100,000
180.	Treasury shares (-)	(13,155)
200.	Income/Loss for the period	352,577
	Group shareholders' equity	**10,834,035**
	Total liabilities and shareholders' equity	**167,029,078**

Reconciliation between the consolidated income statement for the first half of 2017 and the same restated for comparative purposes

Items *(in thousands of euro)*	1st half 2017	Reclassifications IFRS 5	1st half 2017 restated
10. Interest and similar income	1,499,246	(41)	1,499,205
20. Interest and similar expense	(513,221)	(192)	(513,413)
30. Interest margin	**986,025**	**(233)**	**985,792**
40. Fee and commission income	1,161,320	(81,687)	1,079,633
50. Fee and commission expense	(70,590)	10,336	(60,254)
60. Net fee and commission income	**1,090,730**	**(71,351)**	**1,019,379**
70. Dividends and similar income	44,625	-	44,625
80. Profits (losses) on trading	24,584	(1,361)	23,223
90. Fair value adjustments in hedge accounting	(1,125)	-	(1,125)
100. Profits (losses) on disposal or repurchase of:	(64,263)	-	(64,263)
a) loans	(94,681)	-	(94,681)
b) financial assets available for sale	37,011	-	37,011
d) financial liabilities	(6,593)	-	(6,593)
110. Profits (losses) on financial assets and liabilities designated at fair value through profit and loss	2,476	(2)	2,474
120. Net interest and other banking income	**2,083,052**	**(72,947)**	**2,010,105**
130. Net losses / recoveries on impairment of:	(556,990)	-	(556,990)
a) loans	(489,135)	-	(489,135)
b) financial assets available for sale	(78,951)	-	(78,951)
other financial transactions	11,096	-	11,096
140. Net income from banking activities	**1,526,062**	**(72,947)**	**1,453,115**
170. Net income from banking and insurance activities	**1,526,062**	**(72,947)**	**1,453,115**
180. Administrative expenses:	(1,569,994)	7,083	(1,562,911)
a) personnel expenses	(910,752)	3,629	(907,123)
b) other administrative expenses	(659,242)	3,454	(655,788)
190. Net provisions for risks and charges	(9,137)	-	(9,137)
200. Net adjustments to/recoveries on property and equipment	(55,769)	116	(55,653)
210. Net adjustments to/recoveries on intangible assets	(70,325)	58	(70,267)
220. Other operating income (expenses)	3,291,586	1,587	3,293,173
230. Operating expenses	**1,586,361**	**8,844**	**1,595,205**
240. Profits (losses) on investments in associates and companies subject to joint control	93,617	-	93,617
270. Profits (losses) on disposal of investments	1,623	-	1,623
280. Profit (loss) before tax from continuing operations	**3,207,663**	**(64,103)**	**3,143,560**
290. Taxes on income from continuing operations	(45,090)	18,712	(26,378)
300. Income (loss) after tax from continuing operations	**3,162,573**	**(45,391)**	**3,117,182**
310. Income (loss) after tax from discontinued operations	402	45,391	45,793
320. Income (Loss) for the period	**3,162,975**	**-**	**3,162,975**
330. Income (loss) attributable to minority interests	7,394	-	7,394
340. Parent Company's net income (loss)	**3,170,369**	**-**	**3,170,369**

Reconciliation between the reclassified consolidated income statement for the first half of 2017 and the same restated for comparative purposes

Reclassified income statement items (***in thousands of euro***)	**1st half 2017**	**Reclassifications IFRS 5**	**System expenses reclassification**	**1st half 2017 restated**
Interest margin	1,059,989	(233)		1,059,756
Profits (losses) on investments in associates and companies subject to joint control carried at equity	81,939	-		81,939
Financial margin	**1,141,928**	**(233)**	**-**	**1,141,695**
Net fee and commission income	1,090,730	(71,351)		1,019,379
Other net operating income	44,662	16		44,678
Net financial result	101,540	(1,363)		100,177
Other operating income	**1,236,932**	**(72,698)**	**-**	**1,164,234**
Operating income	**2,378,860**	**(72,931)**	**-**	**2,305,929**
Personnel expenses	(917,107)	3,677		(913,430)
Other administrative expenses	(498,731)	4,977	62,406	(431,348)
Net value adjustments on property, plant and equipment and intangible assets	(109,463)	174		(109,289)
Operating expenses	**(1,525,301)**	**8,828**	**62,406**	**(1,454,067)**
Profit (loss) from operations	**853,559**	**(64,103)**	**62,406**	**851,862**
Net adjustments on loans to customers	(647,020)	-		(647,020)
Net adjustments on receivables due from banks	(79,177)	-		(79,177)
Net provisions for risks and charges	(9,137)	-		(9,137)
Profits (Losses) on disposal of investments in associates and companies subject to joint control and other investments	13,301	-		13,301
Profit (loss) before tax from continuing operations	**131,526**	**(64,103)**	**62,406**	**129,829**
Taxes on income from continuing operations	(45,090)	18,712	(17,398)	(43,776)
Charges related to the banking system, net of taxes	-	-	(45,008)	(45,008)
Income (loss) after tax from discontinued operations	402	45,391		45,793
Income (loss) attributable to minority interests	7,394	-		7,394
Income (loss) for the period without Badwill	**94,232**	**-**	**-**	**94,232**
Merger difference (Badwill)	3,076,137	-		3,076,137
Parent Company's net income (loss)	**3,170,369**	**-**	**-**	**3,170,369**

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