



2017

Consolidated Reports
and Accounts

Banking that matters.





Chairman's message

“Today, UniCredit is a leading pan-European bank, well-equipped to address the future, and I thank all those who helped us achieve this result.”

Giuseppe Vita
Chairman

Dear Shareholders,

after six years as Chairman of UniCredit, I will be stepping down at the next Annual General Meeting, confident in the knowledge that UniCredit today is a much changed and stronger Group, poised for future growth and success. During my time here, the whole banking sector has faced unparalleled challenges and undergone a significant evolution. UniCredit has seized on this and taken the opportunity to undertake an in-depth long-term transformation of the Group, in order to create a true pan-European winner.

Having worked closely with all the UniCredit teams, I have developed an enormous respect and appreciation for the people within the Group. Thanks to them, UniCredit will be able to achieve its remarkable potential. The work of UniCredit's teams, under the strong leadership of our CEO Jean Pierre Mustier has made our Group one of Europe's most solid financial institutions. I would like to sincerely thank Jean Pierre for accelerating the transformation of our business model at a time when every company, including banks, must evolve. I greatly appreciate his constructive work

with the board to define a clear long-term strategy, which has been well-received by investors and all other stakeholders.

The past year saw an improved economic situation at both global and European level, and although interest rates remained persistently low, UniCredit experienced positive dynamics across the Group. Thanks to decisive actions, the Group is now significantly better positioned to address the future.

In 2017, UniCredit launched and began implementing its Transform 2019 plan, the start of a long-term process to ensure UniCredit becomes a true pan-European winner. I am pleased that the plan is already delivering tangible results by improving both our Group's profitability and capital base, by changing the way we work and by allowing our teams to focus even more on our customers. We redefined UniCredit's perimeter, while remaining one of the few true pan-European banks with a global reach. At the same time, we greatly reduced our portfolio of impaired loans, significantly improving our risk profile. The Group is making decisive strides forward in the area of technology, thanks to a series of key investments that will allow us to stay ahead of our customers' evolving behaviors and needs.

UniCredit's decisive actions benefitted all the Group's stakeholders and the entire Italian banking system as well as Italy as a whole.

Our progress has allowed us to announce a gradual increase of our dividend as of financial year 2019. In our dividend policy, we have taken into account the evolving regulatory framework, current monetary policies and the changing competitive scenario. Even as these factors have exerted greater pressure on the profitability of our sector, we are confident we have taken the best decisions for our investors, especially all our long-term shareholders.

We have charted a clear course toward change, and our progress was accelerated in 2017 by two extraordinary shareholders' meetings, which lay the groundwork for a new, stronger UniCredit.

The first meeting, in January 2017, saw the approval of the largest capital increase in history by a company based in Italy. I thank you for this act of trust in the bank, which helped us plan for the future with rigor and determination.

The second meeting, in December 2017, allowed for the improvement of UniCredit's governance, delivering far-reaching positive implications for the bank. The decision at that December meeting to empower the Board of Directors to submit its own list of candidates, to increase the number of board members drawn from the second list of candidates from one to two, to eliminate the 5 percent limit on voting rights, and to convert savings shares into ordinary shares aligned the Group with international best practices.

Among other notable changes was the cooptation of Fabrizio Saccomanni to our Board of Directors. I warmly welcome him to the board and I am certain that UniCredit will greatly benefit from his outstanding experience in the banking sector and his in-depth knowledge of European regulatory regimes.

These changes, like the others we have made in recent years, bring us closer to our ultimate goal: to make UniCredit a more efficient, more flexible and more profitable bank, able to seize opportunities to create sustainable value.

In light of what we have achieved and what we intend to accomplish, I am confident that the future will bring benefits to our shareholders and to all UniCredit's stakeholders. Thanks to our people, our bank possesses extraordinary strengths. Together, we will successfully ensure UniCredit is and remains a true pan-European winner.

Sincerely,

Giuseppe Vita
Chairman
UniCredit S.p.A.





Chief Executive Officer's message

“We are transforming through decisive actions. Everything we do is designed to make UniCredit a true pan European Winner.”

Jean Pierre Mustier
Chief Executive Officer

Dear Shareholders,

I would like to thank you for your ongoing support during our transformation. At UniCredit, we are taking decisive actions to become more competitive and build a strong, sustainable Bank, poised for future growth. We have executed on all our commitments in 2017, including a successful €13bn capital increase and the disposals of Pioneer Investments and Bank Pekao stakes. We concluded FINO Phase 1, with the sale of a €17.7bn portfolio. Everything we do is designed to make UniCredit a true pan European Winner.

Our strategy is to be One Bank, One UniCredit: a simple, successful, pan European commercial bank, with a fully plugged in CIB, delivering a unique Western, Central and Eastern European network to our extensive client franchise.

This strategy is long-term. What we are doing today to implement Transform 2019 - our strategic plan - is laying the groundwork for the future. It is changing the way we work to anticipate our clients' medium-term evolution, including their use of multiple channels.

Our investments in digital aim to improve the customer experience as we continue to optimise our processes and our cost base. New commercial dynamics are driving how we train and develop our people.

Our management is clear on this vision and their actions are underpinned by a strict long-term incentives structure based on the plan's key performing indicators. All our people are focused on the ongoing execution of Transform 2019. It is their energy, commitment and hard work which allow UniCredit to deliver tangible results.

As presented to investors at the 2017 Capital Markets Day in December, our performance is fully on track and we have confirmed all the Transform 2019 key targets, with a better risk profile and an improved dividend payout.

We have **strengthened our capital position**, resulting in a lower SREP Pillar 2 Requirement and an S&P upgrade to a BBB rating with a stable outlook. We have confirmed our 2019 CET1 ratio target whilst anticipating additional regulatory headwinds during the plan period. Post 2019, the CET1 ratio will remain above 12.5 per cent, thanks to an organic capital generation that will fully absorb the expected regulatory impacts.

In terms of **asset quality**, we signed binding agreements to reduce our stake in FINO to below 20 per cent. A more disciplined risk management strategy and underwriting processes are driving significant improvements in all our asset quality metrics. Finally, as announced, we are improving on our original Group Gross NPEs' target, cutting a further €4.0bn by the end of 2019. The full rundown of the Non Core portfolio, which will occur by end 2025, is entirely self-funded.

In terms of **transforming our operating model**, we have confirmed our overall revenues and cost targets. Our FTE and branch reductions are ahead of schedule and our digital and IT transformation is fully on track.

We continue to **maximise commercial bank value**, with the ongoing transformation resulting in higher productivity. Our activities in Western Europe continue to benefit from the revamped

network with new service models for retail and SME customers as well as a strong multichannel strategy. Cost reductions are progressing according to plan. In two other core divisions, CEE and CIB, we have further strengthened our leadership positions while keeping a strong focus on risk.

Finally, In terms of **adopting a lean but steering centre**, decisions taken at our latest EGM concerning, for example, a simplified share structure, position us as best in class in terms of European corporate governance.

Finally, on behalf of the Board of Directors and the whole Group, I would like to extend a special thanks to Giuseppe Vita, whose successful tenure as the Chairman of UniCredit is coming to a close. Giuseppe's significant contributions over the past six years have been very precious to our development. His vision and support have enabled UniCredit to grow into one of the few truly pan European commercial banks.

Sincerely,

Jean Pierre Mustier
Chief Executive Officer
UniCredit S.p.A.



One Bank, One UniCredit.

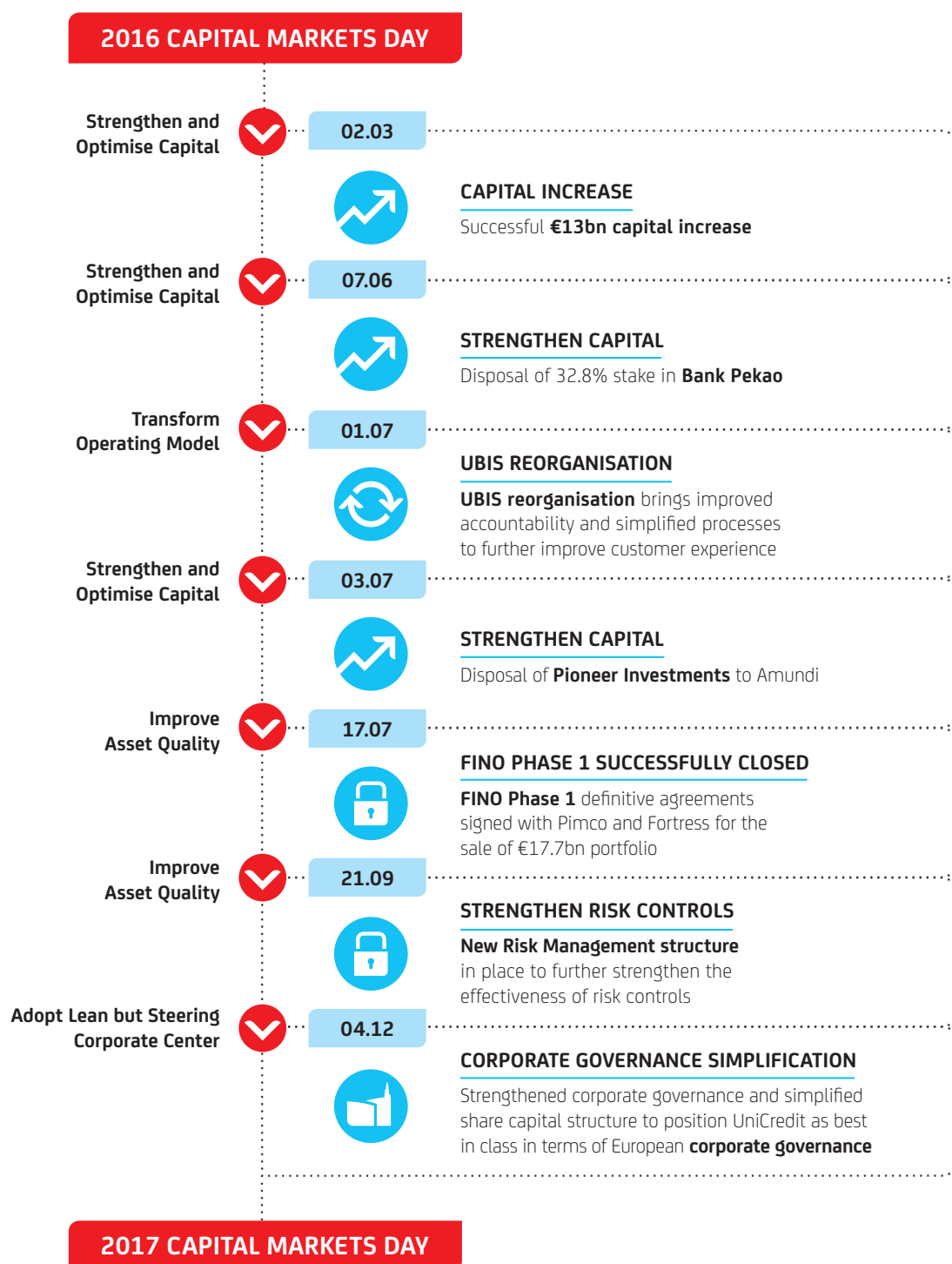


We are a simple, successful Pan European Commercial Bank, with a fully plugged-in CIB, delivering a unique Western, Central and Eastern European network to our extensive franchise of 25 million clients. Our strategy is long-term. We are transforming the Group through decisive actions to lay the groundwork for the future, changing the way we work to anticipate our clients' medium-term evolution. Everything we do is designed to make UniCredit a true Pan European Winner.

Transform 2019 Milestones

Transform 2019 - our strategic plan - is yielding tangible results.

Our strategy is to be One Bank, One UniCredit: a simple, successful, Pan European Commercial Bank, with a fully plugged in CIB, delivering a unique Western, Central and Eastern European network to our extensive client franchise.



Improve Asset Quality

The banking industry is evolving but our core business will always be to support client growth with a unique proposition linked to credit. It is our responsibility to provide advice and support so that companies can develop and globalise - while ensuring sustainable growth. This also means looking beyond purely economic returns, to drive investments with a positive impact on society.

In UniCredit, **“Improve Asset Quality”** is a key pillar of our strategic plan.

- We are focused on the proactive de-risking of our balance sheet
- A strong risk discipline safeguards the quality of future origination
- A new risk management structure further strengthens the effectiveness of our risk controls.

Key Asset Quality Metrics

	2016	2017	🎯 2019
Coverage ratio	55.6%	56.2%	>54%
Group Gross NPEs ratio	11.8%	10.2%	7.8%
FINO* portfolio disposal	FINO Phase 1 signed in December 2016	FINO Phase 1 concluded with € 17.7bn	FINO Phase 2 signed to sell down below 20%

Content

Introduction	10
Financial highlights	10
The management's report	11
The international economic and financial environment	11
Domestic macroeconomic developments	11
The performance of the Hungarian banking sector in 2016	12
UniCredit Bank's corporate social responsibility	13
Business reports	15
Report on the divisions	15
Corporate, Investment Banking and Private Banking Division	15
Retail Division	18
Human Resources	20
Report on UniCredit Jelzálogbank Zrt.	23
Financial reports	25
Independent Auditor's report	25
Financial statements	28
Consolidated statement of financial position (Balance Sheet)	28
Consolidated Income Statement	29
Consolidated statement of comprehensive income	30
Consolidated statement of changes in Shareholder's equity	31
Consolidated statement of cash-flows	32
Notes to the financial statements	33
Further information	80
Supervisory Board and Management Board	80
Calendar	84
Network units	87

Financial highlights

UniCredit Group Hungary – IFRS consolidated

Profit figures

(HUF million)

	2017	2016
Operating result	56,344	66,600
Profit before taxes	56,532	66,479
Profit after taxes	51,099	53,685

Balance Sheet figures

(HUF million)

	2017	2016
Balance Sheet Total	2,746,775	2,737,006
Loans and Advances to customers (net)	1,204,959	1,117,800
Deposits from customers	1,643,826	1,551,019
Shareholder Funds	338,844	299,153

Indicators

	2017	2016
Return on Equity before taxes	17.72%	24.24%
Return on Equity after taxes	16.02%	19.58%
Return on Average Assets (ROA) before taxes	2.06%	2.44%
Return on Average Assets (ROA) after taxes	1.86%	1.97%
Cost Income Ratio*	49.03%	40.03%
Net fee income in percentage of Total Operating Income	36.41%	33.62%

Indicators prescribed by NBH

(HUF million)

	2017	2016
Regulatory Capital**	289,676	261,875
Risk Weighted Assets	1,223,927	1,291,080
Total Capital Ratios	23.67%	20.28%

Other figures

	2017	2016
Headcount (FTE)	1,756	1,728
Number of locations	56	57
Number of branches	54	55

* Based on standard of Consolidated Financial Statement

Management report

International economic and financial environment

The recovery of the global economy continued in 2017, not least due to the fact that world trade growth surpassed the forecasts. Another favourable development was the consistently solid economic growth of developing and emerging regions coupled with significant improvement in advanced economies, whereas political and economic risks were somewhat moderated.

In Europe, the clear failure of populist and nationalist parties in France and the Netherlands and the results of the German elections have helped to mitigate concerns regarding the future of the European Union, even though numerous challenges and problems, such as Brexit and the refugee crisis, remain unresolved. As political risks fell and foreign trade grew, euro area GDP rose by 2.5 percent in 2017. By 2017 even the fundamentals of the euro area economy had improved significantly, which was reflected in continually improving confidence indices and the fact that actual figures consistently outperformed previous expectations. The stable fundamentals and the market expectation of tighter monetary policy underpinned the euro that has appreciated substantially against the US dollar since the middle of the year. In spite of the good growth figures, however, inflation last year was weak totalling 1.5 percent, and it fell well short of the 2 per cent inflation target of the European Central Bank (ECB). This posed a significant challenge for central bankers in the euro area. Even though the ECB, in line with the expectations of the market, announced in the autumn of 2017 that it would gradually phase out its asset purchase programme, interest rate normalization is unlikely to start in the near future.

The United States economy grew by 2.3 percent last year, performing similarly to the eurozone. Consumer demand increased thanks to stable wage growth, and investments rose with improving global outlook and recovery in the energy sector. The economic measures proposed by President Trump, such as tax reform and fiscal stimulus, also contributed to the optimism over growth, underpinning investor expectations for a more dynamic rate rise in the first half of the year. Market sentiment cooled significantly as the implementation of the election promises progressed very slowly and practically nothing was achieved in a large part of the year. In spite of good growth results and an economy operating with essentially full employment, prices rose less than the rate justified by macroeconomic fundamentals, and this was also reflected in the Fed's overall cautious interest rate policy. After three tightening steps during the year, the federal funds rate finished the year at 1.50 percent. The last rate rise took place in December, after the Trump administration managed to push through its program of tax cuts that may boost growth and thus inflation in 2018.

Favourable global environment and recovery in the European economy were behind the boom in the Central and Eastern European

(CEE) countries in 2017. The region's GDP growth was driven by exports, rising domestic demand and increasing lending. As a result, GDP grew faster than the potential growth rate in most of the countries. It was particularly the EU member states that performed above the average: being economies tightly integrated into global production and value chains, they profited most from growth in foreign trade and in the euro area. Increased transfers from the European Union have contributed significantly to the rise in capital investments, whereas labour shortages that were increasing in the Central European region as well, pushed wages higher and boosted consumer demand. In spite of an external environment of low inflation, with the tight labour market and the ensuing dynamic rise in wages triggered price rises as a result of which the inflation rate approximated and even reached central bank targets in many countries opening the way for the start of rate rise cycles.

Domestic macroeconomic developments

Hungarian economic trends were aligned with the regional ones. With low inflation in the euro area, a strong euro and the moderate rise of crude oil prices and Hungarian consumer price increase also fell short of earlier expectations in 2017 (2.4 percent), remaining well below the 4 percent upper limit of the inflation target band and even falling short of the 3 percent target set by the National Bank of Hungary (NBH). As a result, the NBH's policy in 2017 was shaped by the easing of monetary conditions through non-conventional instruments. This differed from the shift towards tightening by the central banks of advanced and CEE countries. The reference rate of the NBH remained unchanged at 0.90 percent.

The exchange rate of the forint to the euro was stable throughout the year, totalling about HUF 310. Nevertheless, in the middle of the summer a temporary but significant appreciation wave brought the exchange rate close to HUF 300. The NBH responded to this first with verbal intervention, later announced another easing envisaged in the autumn. In spite of the low interest rate environment, the macroeconomic fundamentals, the inflow of EU transfers and the positive assessment of the region by investors provide stable support for the exchange rate of the Hungarian currency.

The favourable external environment and the growth in world trade contributed significantly to the outstanding performance of the Hungarian economy last year, when GDP grew by as much as 4 per cent. Expansion was structurally balanced throughout the year. With the exception of agriculture, almost all sectors contributed to the increase in GDP, but primarily services and construction. In line with this, household consumption and investments grew dynamically last year. After a dramatic collapse in 2016, gross fixed investments recovered substantially with a 17 percent growth last year due largely to the continued housing market boom and new investments

Management report (CONTINUED)

in manufacturing. While fund inflows from the European Union remained below the expected level last year, generous state pre-financing made it possible to start projects contributing to the pickup of investment activity. Investments and consumption of households were the key drivers of GDP growth in 2017. All factors influencing household demand contributed to this. Low inflation environment, favourable financial conditions, record-high savings and strong wage rises encouraged both household consumption and demand on the housing market. Hence the boom on the Hungarian housing market continued in 2017, supported by low interest rates and yields as well as government subsidies. Supply is adjusting to the sudden rise in demand only gradually, leading to capacity constraints in construction. All these factors continue to push up prices in the Hungarian housing market.

The main pillars of economic growth, i.e. household consumption and investments were somewhat weakened by the rise in the related import demand and the fact that high pre-financing needs of EU projects redirected government funds from public consumption. As a result, government consumption had a no impact on GDP growth last year.

The labour market trends measured in 2016 reached new highs in 2017: the total number of employed exceeded 4.45 million and the unemployment rate fell below 4 percent. As a result of increasingly tight labour market, the lift of the minimum wage and public sector pays, gross wages rose by more than 10 percent.

The performance of the Hungarian banking industry in 2017

The positive developments that started in the Hungarian banking sector in 2016 continued last year. Less deleveraging, the end of the conversion of currency-denominated loans to forints, improving confidence and stronger domestic demand feeding increasingly into the performance of the economy enabled the banking industry to reach a turning point in profitability as well as lending. After years of negative profits, the sector reported major improvement in generating profits in 2016. This trend continued in 2017, when the industry reported net after-tax profits in the amount around 500 billion in 2017, around 50 percent more than a year earlier. Another positive development is that almost all market participants contribute to profitability. In 2017 the improvement in profitability, too, reflected the further significant reduction of the bank levy, progress in portfolio cleaning and the fall in the share of non-performing loans as a consequence of improving economic, labour market and wage trends that helped ease the provisioning pressure as well. As in 2016, the most important contribution to profitability was the write-back of impairments and risk provisions in 2017 as well. Last year, this atypical item generated one third of total accumulated pre-tax profits.

Meanwhile, the extremely low interest rate environment poses the greatest challenge for the sector. As deposit interest rates are still low, competition in the banking market intensified, and margins contracted yet further as the central bank's policy easing measures pushed the interbank rate to record lows.

The profit-lowering impact of the low interest rate environment was offset to some extent by continued rise in lending volumes. New lending rose by 30 percent in the corporate segment and by 22 percent in the retail one in 2017. This included a nearly 40 percent increase in new housing loan transactions, in line with the boom in the housing market. However, this positive trend is less discernible in housing loan portfolio figures, due in part to the increase in early repayments in cash and sales of bank portfolios.

Similarly to the previous year, in 2017, too, retail investors preferred government securities and investment funds offering higher returns to bank deposits against the background of the low interest rate environment. In addition, home buying became increasingly attractive as a form of investment, since the annual yield achievable on such an investments is around 15 per cent (estimation of the National Bank of Hungary). In spite of the low interest rate environment, growth of corporate deposits were nurtured by the disbursements of EU funds, whereas the household segment profited from a record level of household savings and strong wage dynamics. As the combined result of the factors mentioned above, the loan to deposit ratio fell further in the sector below 75 percent in 2017.

UniCredit Bank Hungary Zrt's performance and profits in 2017

After an extremely successful 2016, UniCredit Bank Hungary Zrt. closed another outstandingly profitable year in 2017. As of the end of 2017, the Bank's balance sheet was essentially equal to the 2016 year-end figure, with its net profits approaching the record 2016 level; being the third largest bank in Hungary.

Based on its consolidated balance sheet and profit and loss account prepared in accordance with the International Financial Reporting Standards (IFRS), total assets of UniCredit Bank Hungary Zrt. amounted to HUF 2747 billion at the end of 2017, representing 0.4 percent growth year-on-year.

Based on its balance sheet calculated in accordance with the Hungarian accounting standards, the Bank's market share reached 8.4 percent in 2017.

Given that margins shrank further as interest rates continued to decline in 2017, the Bank's after-tax profits of HUF 51.1 billion were outstanding and made a significant contribution to its 16

Management report (CONTINUED)

percent return on equity after tax (ROE). This excellent profitability is associated with our outstanding portfolio quality and one of the best cost-effectiveness indicators in the Hungarian banking industry. The Bank's cost/income ratio grew to 49 percent, which can be explained with the fact that UniCredit Bank Hungary grew dynamically even during the crisis, which had a significant impact on bank levy paid by the Bank in 2017.

The declining in net interest income reflects the impacts of the deteriorating interest environment. Net interest income was 7.3 percent lower in 2017 than a year before, even though the loan portfolio increased by 7.8 percent and deposits grew by 6.0 percent last year. The low interest income was partly offset by the 4.3 percent rise in commission income, while the Bank fell somewhat short of its excellent 2016 performance in trading results.

The Bank continually monitors the changes in the business environment and the needs of its clients, and it adjusts its business model. As a result, the Bank continued to focus on digital banking in 2017, and combined this with a series of developments aimed at providing a positive customer experience.

Provisions decreased by 95 percent in 2017. This steep fall was due to the sale of non-performing retail loans during the year and to the fact that the share of non-performing loans in the Bank's portfolio had been below the sectoral average traditionally and was improving further.

As a result of the aforementioned changes in the client portfolio, the loan to deposit ratio of UniCredit Bank Hungary Zrt. was 73 percent at the end of 2017.

As of the end of 2017, UniCredit Bank Hungary Zrt. was serving approximately 400,000 clients in its nation-wide branch network of 54 units.

Corporate Social Responsibility

In 2017 UniCredit Bank Hungary Zrt. reaffirmed its commitments in corporate social responsibility and, in accordance with its long-term strategy, it supported child healthcare, greater equality for disadvantaged groups of society, culture and financial culture. It also continued its existing environmental efforts.

At the beginning of the year the Bank financed the procurement of ten valuable child healthcare instruments: the recipients were seven paediatric wards of six hospitals across the country and one

child ambulance unit in the Northern region of the Great Hungarian Plain. These instruments will allow the comprehensive diagnosis and effective treatment of nearly ten thousand children. In summer 2017, the Bank helped the 2nd Department of Obstetrics and Gynaecology of Semmelweis University acquire an infant incubator that will enable parents to be involved in the care of their child from an earlier stage. After reopening its Szeged and Győr branch offices following their renovation, the Bank gave donations to three local child healthcare foundations to spend on the healthcare of children. In the Christmas period it gave a donation to the Go! Camp Anywhere scheme of Serious Fun Camp Hungary, helping the staff and the volunteers of the foundation to put a smile on the faces of children who may spend weeks or months in hospital.

Our commitment to culture was best demonstrated by our new patronage programme called Leave Your Mark, which aims to encourage young talent in arts, culture and other value creating fields, helping them to reach their potential. It is a core value of this programme and we believe that if we support new talents in achieving their goals, we are also helping the community at large.

The Bank continued its existing initiatives and implemented new ones in order to improve equality for disadvantaged groups. In late 2017, it announced for the third time its "Take a step with us!" social innovation programme, with an award of EUR 60,000 plus one-off professional support to the ten best applicants and a year-long personalized business skills development programme for the winners. The Bank also donated equipment with the aim of improving opportunities, as it sent furniture and computers in had used but still in excellent condition to one of the most disadvantaged small regions of Hungary. These donations now help the Real Pearl Foundation in its work of supporting children and families living in difficult circumstances.

We believe in developing financial culture and, in order to improve the financial knowledge of the young generations, our Bank's volunteers joined again in 2017 the Hungarian Money7 programme series connected to European Money Week. This event was launched in 2015 by the Hungarian Banking Association jointly with the Financial Compass Foundation and with professional assistance from the Ministry of Human Resources. The number of those involved grew to 1117 schools and over 16,000 students in 2017.

As a responsible corporation, UniCredit Bank Hungary Zrt. continually focuses on environmental awareness and sustainable operation; it continued its existing environmental initiatives in 2017. For the tenth time, it took part in the WWF's global initiative Earth Hour, during which the lights in the most important buildings are switched off for an hour to draw attention to the dangers of climate change.

Strengthen and optimise capital.



Following a € 13 billion capital increase, we confirmed a 2019 fully loaded CET1 ratio target above 12.5 percent and an organic capital generation that will fully absorb the expected regulatory impacts: our capital position is stronger and in line with best in class G-SIFIs.

Report on the divisions

Corporate and Investment Banking and Private Banking Division

2017 was one of the most successful years of the Corporate and Investment Banking and Private Banking Division. The Division remained the dominant segment of the bank in terms of both income and profit, due to its stringent cost management and low level of risk costs as well as remaining resilient to the challenges of the Banking market. The extraordinary low HUF – and in case of some for Hungary important currencies even negative – interest rate environment were the most evident aspects to face.

Despite the adverse effects of low interest rates revenue flow was outstanding in 2017, due to rapid growth of both loan and deposit volumes. Therefore our bank managed to retain its market positions in 2017 on a rapidly growing corporate market (12.70% of loans and 12.30% of deposits, EOP), moreover market share peaked at all-time records during the year (13.35% and 12.73% resp. in May). The key driver of the favourable trend in loan volume is our Division's robust capability of financing mid-sized domestic and foreign owned companies (acting as one of top lenders to this segment), our active role and presence at all major structured finance deals and our resilience to intra-year volatility of larger financing tickets of large multinationals and state-owned partners. The Market Based Lending Scheme of the National Bank of Hungary was dominant in SME loan financing of 2017, which we successfully took part in. As well as we did in the export and trade financing schemes refinanced by Hungarian Eximbank to targeted companies.

Our bank is one of the most successful corporate banks in Hungary not only because its excellent profitability indicators. It is also manifested in recognitions received from prestigious forums and – as a most important measure – in the feedback received from our corporate customers. Based on the objective satisfaction survey conducted among our customers, as a recognition of its high service level, the bank managed to achieve an outstanding result among the corporate clientele in 2017. Among others, the Euromoney and the Global Finance Award declared UniCredit to be the best domestic cash manager, real estate bank and private bank, while UniCredit group achieved best trade finance provider status in the CEE region.

Key to success lies within our five fundamentals. It comes, on the one hand, from the expertise and experience of our colleagues and, on the other one, from our up-to-date and full range of service proposition. Therefore, similar to previous years, we have highly focused on the quality of our service delivery to our clients and within this scope we have made several system enhancements to meet our clients' unique requests.

At Structured Finance 2017 was another very busy year full of challenge and success. Notwithstanding a very tight market and tough competition the area confirmed again its leading position in arranging and providing structured finance solutions to its clients.

We proudly took high profile roles such as co-ordinator or facility agent in several milestone club deals for our prime clients. In 2017 Structured Finance volumes increased by 22% while we maintained the excellent quality and profitability of our portfolio.

The year 2017 brought significant increase in volume and income for the Real Estate Financing Department compared to 2017. The share of the construction projects increased in the portfolio which could be the engine of a sustainable growth in the future. We are proud that we obtained significant role in two landmark deals such as the portfolio acquisition of CPI Group (Pólus and Campona shopping malls) and the refinancing of WestEnd City Center. In 2017 UniCredit Hungary's Real Estate team has won the Euromoney Best Bank award (in Overall category). In line with the growing housing market we are keen to finance large and medium-size residential projects mainly in Budapest. In addition we continue to offer full-scale service in the financing of hotels, shopping centres and logistics projects. In 2017 the portfolio quality of real estate financing improved significantly due to the decreasing share of non-performing loans.

We regard 2017 definitely as a year of execution of EU-funded investments both in public and private sector in Hungary. About 40% of the total seven-years facility allocated to Hungary was already transferred to beneficiaries until year-end 2017. Tender calls and results are regularly monitored by the European Competence Centre of the Bank in order to facilitate access to EU and national funds through professional financial advisory services. Our corporate customers may be potential beneficiaries of the competitiveness and rural development programs funded by EU, in this regard our aim is to facilitate to structure the most suitable financing solution for the related development project.

At the end of 2016 the European Investment Fund (EIF) and UniCredit have signed an InnovFin SME guarantee agreement to enhance access to finance for innovative small and medium-sized enterprises (SMEs) and mid-caps in eight countries, among them in Hungary. This transaction benefits from the support of Horizon 2020, the EU's Framework Programme for Research and Innovation, and the European Fund for Strategic Investments (EFSI), the heart of the Investment Plan for Europe.

The InnovFin SME Guarantee Facility provides guarantees on debt financing of between EUR 25,000 and EUR 7.5 million.

In 2017 our bank kept on focusing agribusiness as one of its strategic areas with the aim to optimize its services to agribusiness customers. The sector shows a substantial growth potential, our partners are stable, well capitalised SME companies. Agribusiness financing is dominated by special, tailor-made solutions offered to customers also taking into consideration sectoral specialties.

Report on the divisions (CONTINUED)

As a member of FCI (Factor Chains International) and the Hungarian Factoring Association UniCredit could increase its market share on the growing Hungarian factoring market in 2017. Turnover figures also reflect the outstanding second rank of our Bank which has been held compared to the previous year.

2017's biggest challenge was the continuous shrinking interest rate environment, which required enhanced adaptability from the GTB (Global Transaction Banking) Cash Management Department. Despite of the low market interest rate environment, the Bank continued to successfully increase its customer base. Clear evidences for this are the significant increase of payment and sight deposits volumes. Our high level of service is also recognized by the "Best Cash Management Provider" award from Euromoney.

Thanks to our reliable service level and high professional client service quality the card acquiring services showed a continuous growing tendency, resulted in an increasing market share; the number of terminals reached almost 7,000 by the end of the year. During 2017 the turnover of e-commerce retailers has grown further. This is reflected in the dynamic growth of the vPOS card acquiring turnover of the market which increased also our volumes on this channel. Based on the feedback from our customers we continuously improve the quality of our services and expand our product range. As a result from 2017 we can provide unique cash-storage and cash-handling solutions on the Hungarian market, and xml based account statements for our corporate customers.

UniCredit Bank Hungary Zrt's Trade Finance area closed a successful year in 2017 again. The share of guarantees and letters of credit within the trade finance portfolio has been increased. The growth in the guarantee revenues largely compensated the one-off negative effect resulting from the accrual of the guarantee fees. The trade related loan products refinanced by Eximbank within the portfolio continued to play an important role, meanwhile the structured trade finance loans related to agricultural products have been becoming more and more significant in the portfolio. In recognition of its performance in the field of trade finance, UniCredit Bank Hungary Zrt. has won the Hungarian Trade Finance market finance leader in the Euromoney Trade Finance survey at the beginning of 2018 and was ranked on the first place among the Hungarian banks in the category of "Best Service Provider" as well.

The Global Securities Services (GSS) business of UniCredit Bank Hungary Zrt. closed an extremely successful year in 2017. The business line strengthened its position, retained its market leadership and despite the strong competition, successfully could grow its clientele. Thanks to its stable client base and the favorable market conditions, the assets under custody managed by GSS increased compared to previous year, as well as the revenues earned by the business exceeded the revenues realized in 2016. The good results

achieved by GSS prove that it provides high quality and sustainable custody services to its clients. The GSS business develops its services in accordance with the unique needs of its clients, the constantly stricter legal regulations and capital market developments, it pays special attention to maintain client satisfaction and deems regulatory compliance very important.

Following the Central Bank of Hungary's decision in 2015 the HUF was introduced as a settlement currency in CLS. The bank has launched a successful project, as a result of which it has won more than 50 % of the mandates for „the HUF nostro agent services in CLS" (Continuous Linked Settlement) on the Hungarian market. In 2017 the bank has retained its leading position in this segment, while rendering the service helped to acquire new customers.

During 2017 CFA has successfully renewed the EUR 250 million share purchase and share option agreement with MOL Plc, and participated in the placement of bonds issued by MFB Bank Zrt as part of its EUR 500 million Bond Programme. With respect to M&A deals, CFA concluded a pre-IPO fundraising for a dynamically growing technology firm, with the deals financial closing deferred to 2018.

Our Bank's Markets division had closed a very successful 2017. Treasury Trading increased its revenues by 20%, while Treasury Sales managed to generate 28% higher revenues year on year. During 2017 market volatility had been extremely low both in the local market as well worldwide. Thanks to the continuous easing of the National Bank we saw historical record low yield levels in Hungary. This offered an ample opportunity for our clients to fix their long term interest rate exposure at very low levels. We had been actively advising our clients to fix their long term interest rate exposure, which allowed us to close significant volume of IRS transactions during the year. Our banks activity has significantly increased in commodity hedging. Similar to previous years our biggest business volumes had been traded in FX hedging products with our clients. In the past year we continued to advise our clients how to tackle market challenges, by reducing or eliminating market exposure, smoothing financial conditions for their enterprises and building shareholders value.

Our Bank's Treasury Trading activity was focused predominantly on Fx and rates trading. Despite of the low market volatility we could further increase our revenues with strategic position taking. Our Bank continues to be among the Top3 interbank Fx players. Our Trading units' prominent goal is to maintain its leading position in the Hungarian interbank market and taking hedging risk from our clients.

UniCredit Private Banking closed a successful business year in 2017. At year end we managed more than HUF 170 billion savings of more than 1,270 Private Banking clients. In 2017 both the domestic and the global environment featured low yields, while riskier markets

Report on the divisions (CONTINUED)

provided overall good investment opportunities and profits, with increased risks of market correction and negative impact geopolitical events. UniCredit Private Banking's asset allocation model, the Global Investment Strategy kept its leading role of responding to long term asset allocation needs of our clientele. For 2017 as a great external appreciation of our commitment to our clients, UniCredit Private Banking Hungary was named as Best Private Banking in Hungary by Global Finance Magazine.

In 2017 the Leasing Subgroup of UniCredit Bank Hungary achieved a 4th ranking on the market in the second consecutive year, increasing gross loans to customer by more than 25%. The major business segments are agricultural machines and tools, cars&LCV, trucks, equipment & machinery, IT and dealer financing. UniCredit Insurance Broker LLC, a member of UniCredit Leasing Group, provides insurance plans not only for the leased goods but also for the clientele of UniCredit Bank.

Report on the divisions (CONTINUED)

Retail and Small Business Division

In 2017 UniCredit Bank Hungary Zrt's Retail and Small Business Division continued to pay particular attention to flexibly adapting to market changes and to increasing the satisfaction of its customers in an economic environment of constant challenges.

Our business policy is centred on the establishment of long-term cooperation with clients, and on offering products and services built on client needs. Besides client acquisition, our Bank pays particular attention to client retention as well. By continuously updating our product range, we strive to satisfy client needs as fully as possible in the areas of daily banking transactions, savings, investments and mortgage lending. The success of our efforts is confirmed by a constant annual increase in the number of retail customers whose income is regularly transferred to their accounts in UniCredit Bank Hungary Zrt., and a large number of small business customers also consider UniCredit Bank Hungary Zrt. as their primary bank.

In accordance with its internal guidelines, the Division paid particular and continuous attention to the improvement of service quality, the training and professional support of branch network personnel and to the development of sales, and as a result, it achieved a high degree of client satisfaction. Customer satisfaction with UniCredit Bank Hungary Zrt. has been remarkably strong for years, allowing the Bank to be one of the market leaders in this regard. According to surveys made on services provided in our branches, our clients were especially satisfied, year after year, with the service quality, the advisors of UniCredit Bank Hungary Zrt., the financial advice tailored to the client's financial needs and with the consultations on the next steps to be taken. New customers also expressed great satisfaction with the helpfulness of our advisors and the atmosphere of our branches.

The surveys found that our customers' willingness to recommend our Bank is constantly high and that they are happy to recommend UniCredit Bank Hungary Zrt. to their acquaintances, family members and business partners.

As a result, the Division currently serves nearly 341,000 clients, including 49,000 small businesses. The retail lending market share was 3.9 per cent at the end of 2017, while the loan portfolio closed the year at HUF 245.6 billion. Activity was especially outstanding in retail mortgage loans, and based on the disbursement figures of 2017, the Bank achieved a market share of over 6 per cent in this product.

Our "Stabil Kamat" mortgage products continued to enjoy great popularity in 2017. The premium discounts introduced in 2016 helped our Bank further strengthen its competitiveness with the premium clientele and with the Active Plus interest rate discount launched on 1 March 2017 in the entire retail segment. The Bank started selling qualified consumer-friendly housing loans on 20 September 2017.

It offers a variety of interest rate periods and discounts to clients expressing interest in mortgages to finance their purchase of a used property. Our Bank also conducted a review of its existing mortgage products and modified the conditions and the procedure of applying for them taking into account the clients' preferences.

In April 2017 we introduced our own personal loan product called "Stabil kamat" personal loan. This fixed-rate product is to strengthen our competitiveness on the cash loan market.

The Retail and Small Business Division disbursed HUF 39.4 billion new mortgage loans in 2017, representing an increase of over 43 percent compared to 2016. Third party channels continued to make an important contribution to this result.

In 2017 the volume of investment loans for the small business clientele grew by nearly HUF 1 billion, primarily due to investment loans disbursed with customized conditions. The volume of Széchenyi investment loans disbursed under the Széchenyi Card Scheme also rose. In order to serve our clients' needs, we introduced our "Ritmusváltó" investment loan product. We achieved significant growth in our current account overdraft product sales as well. The trend turned around in 2017 when the volume of lending through our own "Hitelautomata Extra" overdraft facility product exceeded that of the Széchenyi Card overdraft facility. The successful sales were also underpinned by a large-scale campaign.

In 2017 the stock of savings of the Retail and Small Businesses Division increased by more than HUF 47 billion, closing the year at HUF 899 billion. The growing number of active small business clients and individuals with income transferred to their accounts made a major contribution to the 20 per cent increase in the portfolio of sight deposits. In addition, 2017 saw the continuation of a trend according to which in an environment of steadily falling deposit interest rates, clients are looking for investment opportunities with potential yields higher than those of deposits; they have found these primarily in securities. Among retail customers, government securities were no longer the only popular choices since an increasing number of clients expressed interest for investment fund products in 2017. Investment funds were the "bestseller products" in the retail clientele in 2017, also underpinned by the good performance of the funds. As a result, investment fund holdings of our retail clients grew significantly, by over HUF 19 billion last year. This helped us to increase our market share by more than 0.5 percentage points.

The Bank had a 4.6 percent market share in deposits and 4.9 percent in securities held by private individuals.

At the end of 2017, the number of debit and credit cards issued by UniCredit Bank Hungary Zrt. exceeded 312,000; 80 per cent of retail customers owned debit cards.

Report on the divisions (CONTINUED)

Keeping in mind the significant changes in customer needs and habits, we pay particular attention to the development of client-focused digital solutions, whereby we create value for our partners. In the fourth quarter of 2017 the Bank modified its website in line with UniCredit Group's standardization of the design of the websites in its foreign subsidiaries. The Bank also enhanced the navigation and communication solutions on the site. Partly thanks to the above, the unicreditbank.hu website had 1,689,534 visitors in 2017. 47 percent more inquiries were submitted in 2017 than in 2016. As the website is built flexibly and adjusts to the size and resolution of the device used for displaying it, 24 percent of all client inquiries were sent from mobile devices.

Over 90 per cent of the customers of the Retail and Small Business Division can conduct their banking transactions via the Telephone Banking channel. In an effort to provide clients with high quality services and maintaining their level, we achieved a client call response ratio of over 90 per cent in 2017.

80 per cent of all clients opted for convenient banking from home using SpectraNet Internet Banking that is available day and night. In the last quarter of 2017 the Bank started preparations for introducing a new internet banking service for private individual customers.

Under our Mobile First strategy, our Bank introduced in July 2015 its UniCredit Mobil application that was built around simplicity, client focus and the development of the financial culture of clients. Accordingly, our Bank continued updating its mobile application and also laid the groundwork for further solutions offering clients convenient digital methods for the transactions of their day-to-day finances. The postal order reader was introduced in the first quarter of 2017; it greatly simplifies payment by postal orders that are still widely used. Furthermore, thanks to the mToken function introduced in the second quarter of 2017 and the bank card limit modification implemented in the fourth quarter, our Mobile Banking density was more than three times higher than the volume of users of mobile application in the previous year.

In order to allow customers to deposit cash at any time of the day regardless of the opening hours of the branch offices, the Bank is continuously increasing the number of ATMs suitable for cash deposits. This convenience function was available at 81 ATMs at the end of 2017. Environmental protection is a key priority for our Bank, and an increasing number of customers are choosing e-statements instead of paper-based bank account statements. At the end of 2017, 65 percent of our clients used this service.

Report on the divisions (CONTINUED)

Human Resources

Strategy and participation

HR supports the Group with solutions that are innovative, sustainable over the long term and always focused on the value of human capital with maintaining and improving employee commitment and motivation, outstanding talent management schemes and stringent cost and staff management.

In 2017 the Bank launched a wide-ranging project to revise and optimize the remuneration system based on the preferences of its employees.

Supporting business processes

The HR Business Partner Model enables the thorough understanding and client-centred servicing of specific areas and activities in the Bank in terms of labour, compensation, training, development and selection.

Since UniCredit Bank Hungary Zrt. continues to pay special attention to employees' mobility within the organization and the utilization of their expertise both nationally and internationally, the Bank considers internal applications by colleagues first for any vacancies or newly opened positions, prior to evaluating any external applications.

The selection of our employees is assisted by a wide range of tools supporting in-depth assessment. Examples include competence-based and behavioural interviews, professional assignments and tests as well as personality, motivation and work attitude tests.

In 2017, the Bank hired 288 new employees. Through internal transfers and promotions, more than 287 (effectively 95) colleagues were offered new career opportunities. 10 colleagues worked in international positions in the UniCredit Group. 51 colleagues returned to the Bank from maternity leave. Annual bank-wide fluctuation was 13.5 percent.

Employee satisfaction surveys and the implementation of the subsequent action plans are of key importance for the Group as well as for UniCredit Bank Hungary Zrt. The 2017 survey was conducted with a high level of participation, as 85 per cent of employees expressed their opinion; the engagement index was 78 per cent. In 2017, employees participating in the talent programme continued their project work under the sponsorship of senior management, as part of which they formulated and implemented action plans for the areas to be developed.

HR also endeavours to increase employee satisfaction through the development of its own processes.

Training and development, succession management

HR continues to support the regular training of employees, the keeping of their knowledge up to date, the sharing of knowledge and the career management of employees in the Bank. The latter is implemented by relying on the annual appraisal system and talent management and manager training programmes.

Talent management is one of the most important elements of UniCredit Group's human resources strategy. The talent management programme is a group-level initiative, which was adopted by UniCredit Bank Hungary Zrt. more than ten years ago. Its goal is to identify in the organization people with outstanding potential, skills and professional knowledge, and to ensure that their career plans are implemented at both the national and international levels. In 2017 we continued our progress towards our chosen aims. In addition to innovative training methods, we retained all the elements (such as the Mentoring Programme) that had proved to be successful. Our digitalisation drive included the introduction of a new e-learning system in 2017 that offers our colleagues interactive and enjoyable learning methods by providing a much better user experience in their day-to-day work. Furthermore, in continuation of the FinTech and Innovation Conference held in 2016 we launched our Digital Afternoons initiative to which we invite external and internal experts to give talks aimed at enhancing digitalization attitudes in the organization.

Management training is just as important as the retention and training of employees who regularly perform at a high quality. UniCredit Bank Hungary Zrt launched its year-long manager development programme in 2017; the scheme focuses on managers placed in that position for the first time in their careers.

All employees are given the opportunity to participate in the training courses developed by the Bank's internal team of trainers. Primarily in response to the development needs of the organization, these training courses are focused on skills development and are very popular among employees. In 2017, nearly 540 employees participated in the training courses. The internal team of trainers added two new courses to its portfolio in 2017.

In addition to talent management and succession planning, knowledge sharing is one of the key values of UniCredit Bank Hungary Zrt. An increasing number of employees are given the opportunity to participate in international and national development programmes ranging from project work of a few months to assignments spanning several years.

Equal opportunity

As Hungary also joined the international Gender Balance Initiative, we adopted our Gender Balance Policy in 2013. The Policy is aimed at enforcing the principle of equal treatment in employee selection and promotion and the work-life balance. Changes implemented at the local level under the Policy continue to be monitored internationally. Reports of these indicators that are defined at the Group level, are regularly presented to the senior management as well.

In 2017 UniCredit Bank Hungary Zrt. launched a sensitization training scheme for its employees in client management positions. Three internal trainers of the Bank also completed the training and will provide our colleagues with the continued opportunity for learning. An e-learning material is also being written and will be available to all employees at the organization.

What to expect in 2018?

The 2018 HR strategy is shaped by continued strong management support, strategic workforce planning, the development of participants in the management programme, internal client satisfaction, reinforced employee commitment and cost-aware behaviour by the use of additional innovative solutions related to digitalization in order to ensure the enhanced efficiency and long-term sustainability of operations.

The Bank remains committed to ensuring that the organization employs people with the right qualities. In order to do so, it is improving the efficiency of its recruitment and selection activities and lays special emphasis on the continued development of colleagues and on the creation of an inspiring workplace environment where colleagues can find all the support they need for their personal and professional development.

As a pillar of its employer brand, the Bank is working on a reform of its remuneration system that will be introduced

Improve asset quality.



We addressed Italian legacy issues through the sale of a € 17 billion portfolio (FINO) and proactive bad loans management. A more disciplined risk management strategy and underwriting processes are driving significant improvements in all our asset quality metrics.

Report on UniCredit Jelzálogbank Zrt.

A mortgage bank operating as a specialised credit institution, UniCredit Jelzálogbank Zrt. was established on 8th June, 1998 with a registered capital of HUF 3 billion by Bayerische Vereinsbank AG. Since 22 December 2006, the sole shareholder of UniCredit Jelzálogbank Zrt. has been UniCredit Bank Hungary Zrt.

The main activity of UniCredit Jelzálogbank Zrt. is the issue of mortgage bonds and unsecured bonds which typically provide medium- and long-term funding to its own and refinanced loan portfolios. Mortgage loans are primarily secured by first mortgage, independent lien or seceded lien registered on the property financed, located on the territory of Hungary.

In order to increase efficiency, since 2008 UniCredit Jelzálogbank Zrt. has continuously outsourced some of its supporting activities (such as banking operations, human resources, IT, accounting, etc.) to UniCredit Bank Hungary Zrt. Since 1 April 2009, the tasks of specific business areas of UniCredit Jelzálogbank Zrt. have also been performed by UniCredit Bank Hungary Zrt. as outsourced activities, under agency contracts. Accordingly, all administration related to the financing of commercial real estate and home buyers and to estate development and land financing is performed by UniCredit Bank Hungary Zrt. The issue of mortgage bonds and unsecured bonds serving as the basis for the lending activity and refinancing activity continue to be the responsibility of UniCredit Jelzálogbank Zrt.

In line with its practice to date, UniCredit Jelzálogbank Zrt. obtains the typically medium- and long-term funding for its own and refinanced loan portfolios by issuing mortgage bonds, and through money-market and long-term borrowing. It may also raise the funds required for general operations by issuing unsecured bonds; however, no such issuance has been taken place in recent years. The issue of mortgage bonds and unsecured bonds typically takes place as part of mortgage bond offering programmes, in the context of which UniCredit Jelzálogbank Zrt. raises long-term HUF and foreign currency funds from the capital market.

In the current business and market environment, the frequency and volume of mortgage bond issues primarily depend on the structure of the bank's assets and liabilities, the composition of the collateral book, the maturity structure of mortgage bonds, developments in the market yield environment and changes in the regulatory requirements. Mortgage bonds and unsecured bonds may be issued in a number of forms. The form of the issuance and the instruments to be issued are specified in the prevailing base prospectus. In the case of a private offering, mortgage bonds and unsecured bonds are sold to a specific group of investors. In the case of a public offering, the terms of the mortgage bond and unsecured bond issue are laid down in the programme's base prospectus and in the final terms and conditions of each series.

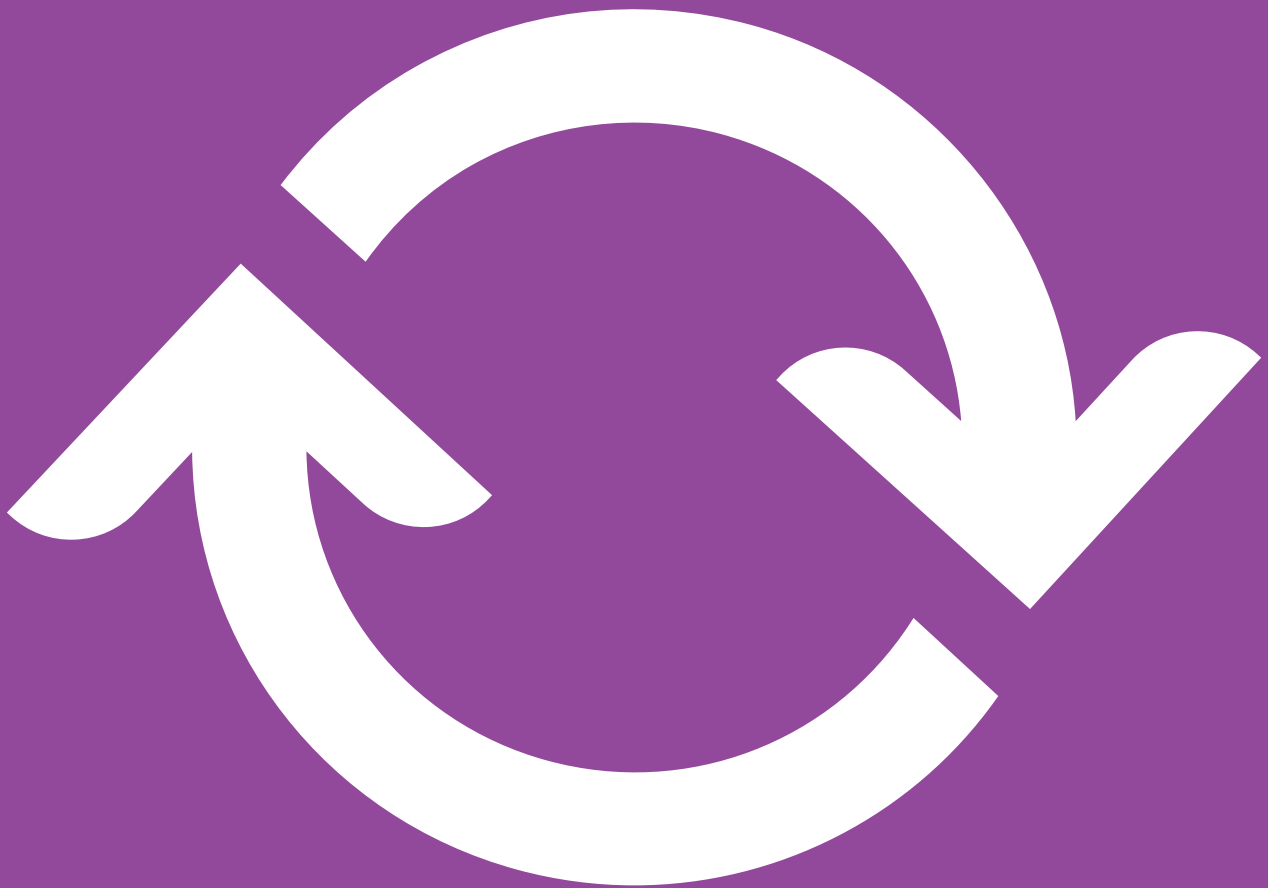
In November 2017, UniCredit Bank Hungary issued a Payment Undertaking in relation to any payment obligation due under Debt Instruments of UniCredit Jelzálogbank Zrt.

As a part of the sale of the non-performing loan portfolio of UniCredit Group and UniCredit Bank Hungary Zrt., UniCredit Jelzálogbank also published that it concluded an agreement about the sale of a retail loan portfolio in 2017. During the transaction, UniCredit Jelzálogbank Zrt. has sold the majority of its non-performing retail loan portfolio which resulted in a reduced credit risk and an improved performance.

In 2017, UniCredit Jelzálogbank renewed its earlier collaboration with the internationally recognized credit rating agency called Moodys Investors Service. Consequently, Moody's assigned a definitive 'Baa1' long-term rating to the mortgage bonds issued by UniCredit Jelzálogbank Zrt on 12th January, 2018. According to the rating methodology of Moody's the assigned rating belongs to the investment grade.

Based on its balance sheet drawn up according to the International Financial Reporting Standards (IFRS), total assets of UniCredit Jelzálogbank amounted to HUF 218.24 bn, profits after taxes to HUF 3.07 bn as of the end of fiscal year 2017.

Transform operating model.



The transformation of our operating model is fully on track, including cost discipline and efficiency measures to reduce the cost income ratio. Our FTE and branch reductions are ahead of schedule – as we further improve on customer focus, services and products. The digital and IT transformation is fully on track, investments supporting the business transformation with digitalization as a key enabler.

Independent Auditor's report



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Cg.: 01-09-071057

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INDEPENDENT AUDITOR'S REPORT

To the Shareholder of UniCredit Bank Hungary Zrt.

Opinion

The summary consolidated financial statements included on pages from 28 to 81 in the annual report for 2017 of UniCredit Bank Hungary Zrt. (the "Bank"), which comprise the summary consolidated statement of financial position as at December 31, 2017, the summary consolidated income statement, the summary consolidated statement of recognized income, summary consolidated statement of changes in Shareholder's equity and summary consolidated statement of cash flows for the year then ended, and related notes ("summary consolidated financial statements"), are derived from the audited consolidated financial statements of UniCredit Bank Hungary Zrt. for 2017.

In our opinion the accompanying summary consolidated financial statements are consistent, in all material respects, with the audited consolidated financial statements for 2017.

Summary consolidated financial statement

The summary consolidated financial statements do not contain all the disclosures required by the International Financial Reporting Standards as adopted by the European Union. Reading the summary consolidated financial statements and the auditor's report thereon, therefore, is not a substitute for reading the audited consolidated financial statements of the Bank. The summary consolidated financial statements and the audited consolidated financial statements for 2017 do not reflect the effect of the events occurred subsequent to the date of our report on the audited consolidated financial statements.

The Audited Statutory Financial Statements and Our Report Thereon

We expressed an unmodified audit opinion on the audited consolidated financial statements in our report dated February 6, 2018. The auditor's report on audited consolidated financial statements also contains the key audit matters identified during the audit of consolidated financial statements for 2017.

Responsibilities of Management and Those Charged with Governance for the Summary Financial Statements

Management is responsible for the preparation of the summary consolidated financial statements in the annual report for 2017 in accordance with relevant information included by the audited consolidated financial statements.

Independent Auditor's report (CONTINUED)

The Auditor's Responsibilities for the Audit of the Summary Financial Statements

Our responsibility is to express an opinion on whether the summary consolidated financial statements are consistent, in all material respects, with the audited consolidated financial statements for 2017 based on our procedures which were conducted in accordance with National Standard on Auditing "810 Engagements to Report on Summary Financial Statements".

Budapest, 22 June 2018



Nagyváradiné Szépfalvi Zsuzsanna
on behalf of Deloitte Auditing and Consulting Ltd.
and as a statutory registered auditor

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1068 Budapest, Dózsa György út 84/C.
Registration number: 000083
Registration number of statutory registered auditor: 005313

Banking that matters.



In this era of unprecedented change customers are looking for companies they can trust and that can play a tangible positive role in their everyday lives. UniCredit has a simple and successful Pan European Commercial banking model delivering relevant solutions to the real needs and wants of today's customers.

Financial statements

Consolidated statement of financial position (Balance Sheet) – 31 December 2017

Assets

	NOTE	2017	2016
		HUF MILLION	HUF MILLION
Cash and unrestricted nostros with Central Bank	15	21,655	15,184
Financial assets held for trading	16	112,595	76,278
Available-for-sale financial assets	17	704,065	648,836
Held-to-maturity investments	18	433	436
Placements with, and loans and advances to banks	19	607,456	797,156
Loans and advances to customers	20	1,204,959	1,115,455
Hedging derivative assets	21	44,395	31,297
Equity investments	22	–	–
Investment properties	23	10,330	10,787
Property, plant and equipment	24	20,645	20,380
Intangible assets	25	6,806	3,800
Current tax assets	14	59	1,111
Deferred tax assets	14	128	134
Assets, held for sale	14	–	115
Other assets	26	13,249	16,037
Total assets		2,746,775	2,737,006

Liabilities

	NOTE	2017	2016
		HUF MILLION	HUF MILLION
Deposits and loans from banks	27	555,151	729,254
Deposits from customers	28	1,643,826	1,546,005
Subordinated loans	29	–	21,218
Issued bonds	30	78,225	23,168
Financial liabilities held for trading	16	65,425	68,419
Hedging derivative liabilities	21	32,011	25,100
Current tax liabilities	14	1	–
Deferred tax liabilities	14	3,157	1,870
Other liabilities	31	25,787	20,307
Other provisions		4,156	2,339
Total liabilities		2,407,739	2,437,680

Equity

	NOTE	2017	2016
		HUF MILLION	HUF MILLION
Share capital	32	24,118	24,118
Capital reserve		3,900	3,900
Retained earnings		181,629	154,880
Statutory reserves	33	38,707	33,771
Valuation reserves		39,399	28,799
Net profit for the year		51,091	53,685
Total Equity attributable to the equity holder of the Bank		338,844	299,153
Minority interest		192	173
Total Equity		339,036	299,326
Total Liabilities and Equity		2,746,775	2,737,006

The accompanying notes (1-50) form an integral part of these financial statements.

Financial statements (CONTINUED)

Consolidated Income Statement – 31 December 2017

	NOTE	2017	2016
		HUF MILLION	HUF MILLION
Interest and similar income	6	79 863	91 180
Interest expense and similar charges	6	(21 552)	(28 274)
Net interest income	6	58 311	62 906
Fee and commission income	7	50 572	48 718
Fee and commission expense	7	(9 000)	(8 865)
Net fee and commission income	7	41 572	39 853
Dividend income	8	187	185
Net trading income	9	13 350	13 108
Net gain and loss on other financial instruments	10	755	2 493
Operating income		114 175	118 545
Impairment and losses on credit products	34	(317)	(6 681)
Net financial activity result		113 858	111 864
Personnel expenses	11	(18 646)	(17 939)
General operating expenses	12	(42 460)	(37 711)
Other provision	34	(1 536)	2 194
Amortization and impairment on property, plant and equipments	24	(921)	(1 277)
Amortization and impairment on intangible assets	25	(270)	(1 498)
Other income	13	6 319	10 971
Operating costs		(57 514)	(45 260)
Gain / (losses) on investments	22	54	(86)
Gain / (losses) on investment properties		134	(35)
Profit before tax		56 532	66 483
Income tax expense	14	(5 433)	(12 794)
Net profit for the year		51 099	53 689
Attributable to:			
Shareholder of the Group		51 091	53 685
Minority interests		8	4

The accompanying notes (1-50) form an integral part of these financial statements.

These figures have been recalculated to EUR using the closing HUF/EUR rate published by the Hungarian National Bank on the last business day of the respective years.

Financial statements (CONTINUED)

Consolidated statement of comprehensive income – 31 December 2017

(HUF million)

	NOTE	2017	2016
Net profit for the year		51,099	53,689
Other comprehensive results that will be subsequently reclassified to profit or loss:			
Movement in fair value reserve (available-for-sale financial assets)		10,498	6,838
Income tax on fair value reserve	14	(944)	(140)
Net movement in fair value reserve		9,554	6,698
Movement in cash-flow hedge reserve		1,149	1,747
Income tax on cash-flow hedge reserve	14	(103)	1,674
Net movement in cash-flow hedge reserve		1,046	3,421
Total comprehensive income for the year		61,699	63,808

The accompanying notes (1-50) form an integral part of these financial statements.

Financial statements (CONTINUED)

Consolidated statement of changes in Shareholder's equity – 31 December 2017

(HUF million)

	ORDINARY SHARES	CAPITAL RESERVE	RETAINED EARNINGS	STATUTORY RESERVES	VALUATION RESERVE	RESERVES Hedging reserve	NET PROFIT	TOTAL	NON- CONTROLLING INTEREST	TOTAL EQUITY
Balance at 1 January 2016	24,118	3,900	134,518	29,432	3,850	14,830	38,701	249,349	220	249,569
Net profit for the previous year	–	–	38,701	–	–	–	(38,701)	–	–	–
Total comprehensive income for the year	–	–	–	–	6,698	3,421	53,685	63,804	4	63,808
Dividend to equity holder	–	–	(14,000)	–	–	–	–	(14,000)	–	(14,000)
Business combination	–	–	–	–	–	–	–	–	(51)	(51)
Appropriations Transfer to retained earnings	–	–	(4,339)	4,339	–	–	–	–	–	–
Balance at 31 December 2016	24,118	3,900	154,880	33,771	10,548	18,251	53,685	299,153	173	299,326
Net profit for the previous year	–	–	53,685	–	–	–	(53,685)	–	–	–
Total comprehensive income for the year	–	–	–	–	9,554	1,046	51,091	61,691	8	61,699
Dividend to equity holder	–	–	(22,000)	–	–	–	–	(22,000)	–	(22,000)
Business combination	–	–	–	–	–	–	–	–	11	11
Appropriations Transfer to retained earnings	–	–	(4,936)	4,936	–	–	–	–	–	–
Balance at 31 December 2017	24,118	3,900	181,629	38,707	20,102	19,297	51,091	338,844	192	339,036

The accompanying notes (1-50) form an integral part of these financial statements.

Financial statements (CONTINUED)

Consolidated statement of cash-flows – 31 December 2017

Cash flows from operating activities

(HUF million)

	NOTE	2017	2016
Profit before tax		56,532	66,479
Items not involving movement of cash:			
Depreciation and amortisation	24, 25	1,191	2,775
Scrapped and transferred fixed assets		–	–
Profit on disposal of property, plant and equipment		(252)	(17)
Net impairment and losses in credit products		(3,126)	(9,653)
Net loss/gain from cashflow hedging assets		(5,038)	8,974
Foreign exchange loss on subordinated loans		–	(143)
Fair value change of investment properties		(135)	35
Foreign exchange loss/ (gain) on investment properties		(110)	41
Business combination		(8)	–
Income tax paid	14	(5,433)	(12,794)
Cash flows from operating profits before changes in operating assets and liabilities		43,621	55,697
Change in financial assets held for trading		(36,317)	(7,460)
Change in current tax assets		1,059	(90)
Change in other assets		2,788	1,203
Change in asset held for sale		115	–
Change in current tax liabilities		240	2,266
Change in other liabilities		5,382	(2,955)
Change in loans and advances to customers		(84,444)	(52,054)
Change in deposits with other banks		189,700	107,545
Change in deposits from customers		97,821	46,194
Change in deposits from other banks		(174,103)	(100,248)
Change in subordinated loans		(21,218)	–
Change in financial liabilities held for trading		(2,994)	6,038
Net cash from operating activities		(21,971)	439

Cash-flows from investing activities

(HUF million)

	NOTE	2017	2016
Proceeds on sale of property, plant and equipment		44	121
Other movement in property, plant and equipment and intangible assets		–	–
Addition of property, plant and equipment		(977)	(780)
Addition of intangible assets		(3,276)	(2,599)
Change in equity investments		–	–
Change in held to maturity investments		3	2
Change in available for sale financial assets		(44,731)	(66,595)
Change in investment properties		701	3,220
Net cash used in investing activities		(48,236)	(66,631)

Cash-flows from financing activities

(HUF million)

	NOTE	2017	2016
Change in issued bonds		55,057	19,652
Dividend paid		(22,000)	(14,000)
Net cash from financing activities		33,057	5,652
Net Increase in cash		6,471	(4,843)
Cash at the beginning of the year	15	15,184	20,027
Cash at the end of the year	15	21,655	15,184

The accompanying notes (1-50) form an integral part of these financial statements.

Notes to the financial statements

1. General

UniCredit Bank Hungary Zrt. ("UniCredit" or "the Bank") is registered as a joint-stock company under Hungarian law and is licensed to conduct universal banking activities in Hungary. The address of the Bank's registered head office is H-1054 Budapest, Szabadság tér 5-6. The Bank is a wholly owned subsidiary of UniCredito Italiano S.p.a.

Transactions with members of the UniCredit Group include credit relationships, where the related parties are borrowers or guarantors, and deposit relationships. Such transactions are conducted under substantially the same terms and conditions as are applied to third parties, unless otherwise stated.

These financial statements were approved by the Supervisory Board on 6 February 2018.

2. Basis of preparation

a.) Statement of compliance

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB"), and all applicable interpretations issued by the International Financial Reporting Interpretations Committee of the IASB ("IFRIC"), as adopted by the EU.

b.) Basis of measurement

The financial statements are presented in millions of Hungarian Forint ("HUF").

These consolidated financial statements are presented in Hungarian Forints, the currency of the primary economic environment in which the Group operates ("functional currency"). The accounting records of the Group are also maintained in this currency. Except as indicated, financial information presented in Hungarian Forints has been rounded to the nearest million.

These consolidated financial statements consolidate the accounts of the following entities: UniCredit Bank Hungary Zrt., UniCredit Jelzálogbank Zrt. ("Mortgage bank"), Arany Pénzügyi Lízing Zrt., Sas-Reál Kft., UniCredit Leasing Hungary Zrt., UniCredit Biztosításközvetítő Kft., UniCredit Operatív Lízing Kft. as subsidiaries and Europa Investment Fund as a special purpose vehicle (together the "Group").

These consolidated financial statements have been prepared on a fair value basis for derivative financial instruments, trading financial assets and liabilities and available-for-sale financial assets, except those for which a reliable measurement of fair value is not available. The latter items are stated at either amortised or historical cost.

Other financial assets and liabilities and non-financial assets and liabilities are stated at amortised cost, net of accumulated impairment losses (if applicable) or historical cost.

3. Significant accounting policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

a.) Consolidation principles

All entities directly or indirectly controlled by the Bank have been consolidated into these consolidated financial statements. These consolidated financial statements are based on the stand-alone reporting packages of the consolidated subsidiaries, which have also been prepared in accordance with IFRS.

Investments in associated companies, which are neither indirectly nor directly controlled by the Bank, but over which it can exercise significant influence, are accounted for using the equity method.

Notes to the financial statements (CONTINUED)

Investments in shares in companies, which are not consolidated are classified as available for sale investments and recognised at their fair values, when that fair value is reliably measurable. Changes in fair values are thus directly recognised in other comprehensive income. In cases where the fair value cannot be reliably determined, shares are carried at cost. When there is objective evidence that a financial asset is impaired, a loss is recorded in the consolidated income statement. As soon as the circumstances which led to the impairment cease to exist, the recovery in the fair value of the impaired available-for-sale equity security is recognised directly in equity.

b.) Consolidation procedures

When a subsidiary or associated company is acquired, the acquirer determines the related goodwill, which is recognised in the statement of financial position. Subsequently, goodwill is measured at cost less accumulated impairment losses.

Intra-group balances, and income and expenses arising from intra-group transactions are eliminated in preparing these consolidated financial statements.

c.) Comparatives

Certain items previously reported in the prior years' financial statements are restated and reclassified to provide consistency for presentation purposes, if applicable.

d.) Cash and cash equivalents

Cash and cash equivalents include nostros with the Central Bank and are carried at cost in the statement of financial position.

The amount of cash in the statement of cash flows is equal to the cash on hand from statement of financial position item Cash and unrestricted nostros with the Central Bank (see Note 15).

e.) Financial instruments

i) Classification

Financial assets and financial liabilities, held for trading are those that the Group principally holds for the purpose of short-term profit taking. These include shares, bonds, certain purchased loans and derivative contracts that are not designated as effective hedging instruments. All non-hedge derivatives in a net receivable position (positive fair value), are classified as financial assets, held for trading. All trading derivatives in a net payable position (negative fair value), are classified as financial liabilities, held for trading. The Group decided not to use the possibility of the optional, irrevocable classification of its financial instruments as financial instruments at fair value through profit or loss.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, and which are created by the Group with no intention of short term profit taking. Loans and receivables consists of loans and advances to banks and customers.

Held-to-maturity investments are financial assets with fixed or determinable payments and fixed maturity that the Group has the positive intent and ability to hold to maturity, and which are not designated as at fair value through profit or loss or as loans and receivables and if they don't meet the definition of loans and receivables. These include certain debt instruments.

Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. Available-for-sale instruments include certain debt and equity investments.

Hedging instruments. There are certain derivatives that are designated as hedging instruments in cash-flow hedges. They serve as hedges against the variability of cash flows within the framework of the Group's asset-liability management activities. For the purpose of cash-flow hedge, IRS transactions are entered into for hedging the risk as part of risk management strategy. Variable-rate interest receivables and payments on variable-rate assets and liabilities are swapped for fixed-rate interest payments, primarily by means of interest rate swaps. Interest rate swaps are also used to hedge the exposure to changes in the fair values of fixed rate available-for-sale debt securities attributable to changes in market interest rates.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognized in other comprehensive income and accumulated under the heading of cash flow hedging reserve. The gain or loss relating to the ineffective portion is recognized immediately in profit or loss, and is included in the 'other gains and losses' line item.

Notes to the financial statements (CONTINUED)

Amounts previously recognized in other comprehensive income and accumulated in equity are reclassified to profit or loss in the periods when the hedged item affects profit or loss, in the same line as the recognized hedged item. However, when the hedged forecast transaction results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously recognised in other comprehensive income and accumulated in equity are transferred from equity and included in the initial measurement of the cost of the non-financial asset or non-financial liability.

When a derivative is designated as the hedging instrument in a hedge of the change in fair value of a recognised asset or liability or a firm commitment that could affect profit or loss, changes in the fair value of the derivative are recognised immediately in profit or loss together with changes in the fair value of the hedged item that are attributable to the hedged risk.

Hedge accounting is discontinued when the Group revokes the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting. Any gain or loss recognised in other comprehensive income from the period when the cash flow hedge was effective remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the gain or loss accumulated in equity is recognised immediately in profit or loss. In a fair value hedge relationship, any adjustment to a hedged item for which the effective interest method is used, is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

ii) Recognition and de-recognition

The Group recognises financial assets and liabilities on the trade date. A financial asset or financial liability is initially measured at fair value plus (for an item, that is not subsequently measured at fair value through profit or loss) transaction costs that are directly attributable to its acquisition or issue.

From this date any gains and losses arising from changes in fair value of the assets are recognised either in income statement or in equity in case of assets measured at fair value through profit or loss and available for sale assets. All loans and receivables are recognised when cash is advanced to the counterparty.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all risks and rewards of ownership. (If the Group neither transfers nor retains substantially all the risks and rewards of ownership of the financial asset, the Group shall determine whether it has retained control of the financial asset. In this case, if the Group has not retained control, it shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer.

Financial liabilities are derecognised when the contractual obligations are discharged, cancelled or expire.

iii) Measurement

Initial measurement

Financial instruments are measured initially at fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue.

Subsequent measurement

Subsequent to initial recognition all trading and hedging financial assets and liabilities and all available-for-sale financial assets are measured at fair value, except that, where no quoted market price exists in an active market and fair value cannot be reliably measured, these are carried at cost less impairment.

Loans and receivables and held-to-maturity investments are measured at their amortised cost less accumulated impairment losses. Premiums and discounts are included in the carrying amount of the related instrument and are amortised. Financial assets, with the exception of loans which are reviewed monthly, are reviewed at each reporting date to determine whether there is objective evidence of impairment. If any such indicator of impairment exists, the asset's recoverable amount is determined and compared with its carrying amount to assess the amount of any impairment.

Fair value measurement principles

The fair value measurement principles, applied by the Group, are described in Note 5.

Gains and losses on subsequent measurement of FVTPL assets and available for sale assets

Gains and losses arising from a change in the fair value of trading financial assets and financial liabilities are recognised in the income statement. Gains and losses arising from a change in the fair value of available-for-sale financial assets are recognised in the Available-for-sale reserve, except for those designated as hedged items in qualifying fair value hedge relationships, where changes in fair value attributable to the risk being hedged are recognised in the income statement. Gains and losses arising from a change in the fair value of derivatives, designated as effective hedging instruments in a cash flow hedge relationship are recognised in the Cash flow hedge reserve. Any impairment loss on available-for-sale financial assets is recognised in the income statement.

Notes to the financial statements (CONTINUED)

f.) Transactions in foreign currency

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in equity as qualifying cash flow hedges.

g.) Equity investments

Equity investments that the Group holds for the purpose of short-term profit taking are classified as trading financial assets. Other equity investments are classified as available-for-sale financial assets. The measurement of these equity investments is stated in Note 3.(e.) except for equity investments in associated companies that are measured based on Note 3.(a.).

h.) Property, plant and equipment

Items of property, plant and equipment are measured at historical cost less accumulated depreciation and accumulated impairment losses.

i.) Intangible assets

Intangible assets are stated at historical cost less accumulated amortisation and accumulated impairment losses. The Group has no intangible assets with an indefinite useful life.

j.) Depreciation and amortisation

Depreciation is charged to write off the cost of all such assets which are to be depreciated to the income statement over their anticipated useful lives. All of the below assets are depreciated on a straight line basis. The annual rates of depreciation used are as follows:

Depreciation Rate (%)	
Buildings	2 – 6
Property rights	10
Office equipment	14.5 – 33
Hardware	25
Motor vehicles	20
Rental rights	10
Licenses	10
Software	20

Land and assets under construction are not depreciated.

k.) Impairment on non-financial assets

If there is objective evidence that a non-financial asset (Property, Plant and Equipment or Intangible asset) has been impaired, the carrying amount of the asset is compared with its recoverable value, equal to the greater of its fair value less selling cost and its value in use, i.e., the present value of future cash flow expected to originate from the asset. Any value adjustment (if recoverable value is estimated to be less than its carrying value) is recognised in the income statement. Items which are considered to have no further value are impaired in full.

If the value of a previously impaired asset is restored, its increased carrying amount cannot exceed the net carrying amount it would have had if there had been no impairment losses recognised in prior years.

l.) Investment properties

The Group measures its investment properties at fair value. The fair value of these investment properties is based on a valuation carried out by Grant Thornton Valuation Kft., an independent valuator company, not related to the Group. Valuation professionals have completed the valuation as independent appraisers and possess the necessary qualifications for the valuation of the subject real estate properties.

The fair value was determined in accordance with the requirements set forth by the International Financial Reporting Standards IFRS 13. The valuation premise used to measure the fair value of the income generating properties is the highest and best use. Valuation techniques applied are the market sales comparison and/or the income approach to value the real estate properties. The applied technique depends on the type of the property.

Notes to the financial statements (CONTINUED)

The inputs to valuation techniques are of the level 3 in the fair value hierarchy for real estate, therefore sensitivity analyses were performed during the valuation.

The capitalisation rate adopted is made by reference to the yield rates observed by the market players for similar properties or by using the build-up method based on a risk-free return, e.g. the long-term Hungarian Treasury bond, and adding risk premiums related to macro- and micro economics, the general and specific real estate market, location and actual usage of the properties.

There has been no change to the valuation technique during the year.

In estimating the fair value of the properties, the highest and best use of the properties is their current use.

m.) Loans and advances

Loans and advances originated by the Group are classified as loans and receivables. Purchased loans that the Group has the intent and ability to hold to maturity are also classified as loans and receivables.

Loans and advances are reported net of impairments for credit losses to reflect the estimated recoverable amounts.

Income for the period on loans and advances is determined using the effective interest method. The effective interest rate is established individually for all loans and advances. When calculating the effective interest rate, all contracted cash-flows are taken into account including fees commissions, as well as possible premiums or discounts. Estimated future credit losses are however not included. The result of this calculation is charged to the income statement.

n.) Leasing

Leases are classified as finance leases, whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Amounts due from lessees under finance leases are recognised as receivables at the amount of the Group's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant, periodic rate of return on the Group's net investment outstanding in respect of the leases.

o.) Impairment and losses on credit products

It is the policy of the Group to review periodically its portfolio of loans and advances to make provisions for impairment, where necessary. Impairment is based on an individual assessment of the recoverability of outstanding amounts. Increases and decreases in the provisions for impairments are charged to the income statement. Further details on loan assessment are provided under the Risk Management Policies.

p.) Deposits from banks and customers

Deposits are cash amounts, accepted by the Group from other banks and its customers, and they serve as funds to the active side of the business. Deposits are initially measured at fair value, and subsequently at their amortised cost. The Group does not classify or designate any deposits as financial liability at fair value through profit and loss.

q.) Issued bonds

The Mortgage Bank's primary source of funds is generated from the issuance of mortgage bonds. Mortgage bonds are secured bonds. The Mortgage bank may issue such bonds only if it has sufficient collateral, which may include independent mortgage rights and other securities such as government bonds and treasury bills.

Issued bonds are classified as financial liabilities, initially recognised at issue price, plus directly attributable transaction costs and subsequently measured at amortised cost.

Notes to the financial statements (CONTINUED)

r.) Equity elements

i) Statutory reserves

General reserve

In accordance with Section 83 of Hungarian Act No. CCXXXVII of 2013, a general reserve equal to 10% of the net post tax income (based on the Bank's financial statements, prepared in accordance with the local GAAP) is required to be made in the Hungarian statutory accounts. The general reserve is set aside to offset potential future losses according to Hungarian Accounting and Banking Rules. Increases in the general reserve are treated as appropriations from retained earnings, and are not charged against income.

Tied-up reserve

This reserve is an appropriation from the retained earnings, for future purchases of tangible or intangible assets, in order to obtain tax benefits. It is released to retained earnings in line with the expenditure for such assets.

ii) Valuation reserves

Valuation reserves are part of Shareholder's equity. Under the IFRS principles the valuation reserves include exclusively the cash-flow hedge reserve and available-for-sale instrument reserve less deferred tax as stated in Note 3.(e.) above.

s.) Derivative financial instruments

The Group uses the following derivative financial instruments: futures, interest rate swaps, options, forward rate agreements and spot and forward foreign exchange contracts to manage its exposure to foreign exchange, interest rate and market risks arising from operational, financing and investment activities.

The recognition of income/expenses relating to non-hedge derivative transactions are on a mark-to-market basis, and changes in value are immediately recognised in the income statement.

Quantitative information on the hedging derivatives is presented under Note 40.

The Group holds certain embedded derivative instruments. Their recognition and valuation rules are identical with those of the non-embedded derivatives.

t.) Financial Guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. The Group normally issues either short-term guarantees, with an initial payment, or long term guarantees, for which it receives regular fee income. Financial guarantees are reviewed quarterly, and a provision is created in the amount of any expected payment. These provisions are included within other liabilities.

u.) Income

Net Interest income

Interest income and interest expense for the year are recognised on an accruals basis, together with the application of the effective interest rate method on all instruments measured at amortised cost.

For loans and advances, the effective interest rate is established individually. When calculating the effective interest rate, all contracted cash-flows are taken into account including fees commissions, as well as possible premiums or discounts. Estimated future credit losses are however not included.

Dividend income

Dividend income is recognised in the income statement on the date that the Group's right to receive payment has been established.

Net fee and commission income

Net fee and commission income consists of income from services, provided on a fee and commission basis as well as expenses incurred for services provided by third parties and related to the Group's fee-earning business. Net commissions and fees are included in the income statement as they are received and paid.

Notes to the financial statements (CONTINUED)

Net trading income

Net trading income includes gains and losses arising from disposals and changes in the fair value of trading financial assets and liabilities.

Net gain and loss on other financial instruments

Net gain and loss on other financial instruments is related to non-trading financial assets and equity investments and includes the realized result at derecognition.

Gains and losses on other equity investments

Gains and losses on other equity investments include the net result arising from capital transactions from equity investments related to associated companies.

v.) Income tax

Income tax on the profit or loss for the year consists of current and deferred tax.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted at the reporting date. The profit for the year is adjusted according to the relevant tax regulations to calculate the taxable income.

Deferred tax is provided using the balance sheet liability method, in respect of which temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes are recognised in full. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the difference between the carrying amounts of assets and liabilities in the IFRS statement of financial position and in the balance sheet for local tax purposes.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the unused tax losses and credits can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax assets and liabilities are offset in the statement of financial position after the analysis, carried out according to IAS 12.

w.) Events after the reporting date

Events after the reporting date are those events, favourable and unfavourable, that occur between the reporting date and the date when the financial statements are authorised for issue. These events fall into two categories: those that provide evidence of conditions that existed at the reporting date (adjusting events after the reporting date); and those that are indicative of conditions that arose after the reporting date (non-adjusting events after the reporting date).

All adjusting events after reporting date have been taken into account in the preparation of the consolidated financial statements of the Group. Where there were material non-adjusting events that occurred after the reporting date, the appropriate disclosure thereof has been made in the consolidated financial statements.

x.) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, whose operating results are reviewed regularly by the Group to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

The Group's format for segment reporting is based on business segments and the Group's management and internal reporting structure.

Notes to the financial statements (CONTINUED)

The Group separates the following main business segments:

- CIB (Corporate and Investment Banking)
 - Includes the loans, deposits and other transactions and balances with corporate customers (excludes small enterprises) together with the results of trading activities and equity sales activities with customers.
 - Includes the custody service transactions and balance.
- Retail
 - Includes the loans, deposits and other transactions and balances with retail customers (includes small enterprises).
- Private Banking
 - Includes the loans, deposits and other transactions and balances with private banking customers.
- Others
 - Includes Assets Liabilities Management activities that contain the Group's funding and centralised risk management activities through borrowings, use of derivatives for risk management purposes and investing in liquid assets such as short-term placements and corporate and government debt securities.
- Leasing
 - Includes the leasing transactions.

The result of each segment also includes the head office costs (indirect and overhead) allocated on a reasonable basis. The business segment report is presented in Note 44.

y.) New standards and interpretations

Standards and Interpretations effective in the current period

The following amendments to the existing standards and new interpretation issued by the International Accounting Standards Board (IASB) and adopted by the EU are effective for the current reporting period:

- Amendments to IAS 7 "Statement of Cash Flows" – Disclosure Initiative (endorsed on 6 November 2017, effective for annual periods beginning on or after 1 January 2017).
- Amendments to IAS 12 "Income Taxes" – Recognition of Deferred Tax Assets for Unrealised Losses (endorsed on 6 November 2017, effective for annual periods beginning on or after 1 January 2017).

The adoption of these amendments to the existing standards has not led to any changes in the Group's accounting policies.

Standards and Interpretations issued by IASB and adopted by the EU but not yet effective

At the date of authorisation of these consolidated financial statements the following standards, amendments to the existing standards and interpretations issued by IASB and adopted by the EU were in issue but not yet effective:

- Amendments to IFRS 4 "Insurance Contracts" – Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (endorsed on 3 November 2017, effective for annual periods beginning on or after 1 January 2018).

The Group anticipates that the adoption of these amendments to the existing standards will have no material impact on the financial statements of the Group in the period of initial application.

- IFRS 15 "Revenue from Contracts with Customers" including amendments to IFRS 15: Effective date of IFRS 15 (endorsed on 22 September 2016, effective for annual periods beginning on or after 1 January 2018).
- Clarifications to IFRS 15 "Revenue from Contracts with Customers" (endorsed on 31 October 2017, effective for annual periods beginning on or after 1 January 2018).

The Group anticipates that the adoption of these standards, amendments to the existing standards and interpretations will have no material impact on the financial statements of the Group in the period of initial application.

- IFRS 16 "Leases" (endorsed on 31 October 2017, effective for annual periods beginning on or after 1 January 2019).
- IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases. The Group has completed an initial assessment of the potential impact on its consolidated financial statements but has not yet completed its detailed assessment. Based on the initial assessment the new lease standard will not have significant impact on the consolidated financial statements of the Group.

- IFRS 9 "Financial Instruments": In July 2014, the International Accounting Standards Board issued the final version of IFRS 9 Financial Instruments, and in November 2016 the EU has adopted it. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. The Bank currently plans to apply IFRS 9 initially on 1 January 2018.

The Group is currently working on the estimation of the actual impact of adopting IFRS 9 on the Group's consolidated financial statements in 2018, as it will be dependent on the financial instruments that the Group holds and economic conditions at that time as well as accounting elections and judgements that it will make in the future. The new standard will require the Group to revise its accounting processes and internal controls related to reporting financial instruments and these changes are not yet complete.

Notes to the financial statements (CONTINUED)

i. Classification – Financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

The Group has determined the business model on a level that reflects how financial assets are managed to achieve a particular business objective. However, the determination is not dependent on management's intentions for an individual instrument, this condition is not an instrument-by-instrument approach and made on a higher level of aggregation. However, the Group has more than one business model for managing its financial instruments.

The following business models were identified for IFRS 9 classification and measurement purposes:

- **Held to Collect (HTC):** Financial instrument is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and are managed to realise cash flows by collecting contractual payments over the life of the instrument. There is no need to hold all of those instruments until maturity. Sale is permitted if the Group sells financial assets when there is an increase in the assets' credit risk, because the credit quality of financial assets is relevant to the Group's ability to collect contractual cash flows. In addition, sales may be consistent with the objective of this business model if the sales are made due to an increase in the credit risk of the concentration or close to the maturity of the financial assets.
- **Both Held to Collect and for Sale (HTCS):** the objective is achieved by both collecting contractual cash flows and selling financial assets. The objective of the business model beside of the collecting for the contractual cash flows is to realise profit from the growth of the fair value of the instruments, and to minimise the losses arising from the increase of the fair value changes of the instruments in mid- or long-term. Compared to a HTC business model, this business model will typically involve greater frequency and value of sales.
- **Held to Benefit from Changes in Fair Value (e.g.: TRADING):** mainly trading securities, with the objective of realising cash flows through the sale of the assets. This business model is a residual category.

The business model assessment refers to the expectations of the Group, not just its intention but its ability to manage its financial assets. Consequently, this assessment is not performed on the basis of scenarios that the entity does not reasonably expect to occur, such as so-called 'worst case' or 'stress case' scenarios.

Therefore if the Group plans to sell a certain portfolio or financial assets in a 'stress case' scenario, it does not affect the business model assessment, if the Group does not reasonably expect it to occur.

The Group's limits about the value of sales that are not in connection with the increase in the assets' credit risk:

HTC business model:

- annual turnover of the portfolio $\leq 1\%$ – is consistent with HT business model,
- annual turnover of the portfolio is between 1% and 5% – further analysis is required in connection with the average turnover,
- annual turnover of the portfolio $\geq 5\%$ – not consistent with HTC business model.

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost (AC), fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). The standard eliminates the existing IAS 39 categories of held to maturity (HTM), loans and receivables (L&R) and available for sale (AFS).

Based on the current portfolio, IFRS 9 has no material impact on the effective interest rate calculation. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are no longer bifurcated. Instead, the hybrid financial instrument as a whole is assessed for classification and most likely fails the SPPI test.

In the assessment of the SPPI criteria's the Group analyses whether the contractual cash flows of loan commitments and other debt assets only contains solely payments of principal and interest. For the SPPI assessment the Group is using a tailor-suited IFRS 9 SPPI tool. In connection with the new IFRS 9 classification and measurement approach the Group anticipates the following modifications in its financial instruments.

Notes to the financial statements (CONTINUED)

The anticipated modifications in the financial assets in connection with IFRS 9 are:

Amortised cost

(HUF million)

	IAS 39 BOOK VALUE 31.12.2017	TRANSFER	REVALUATION	IFRS 9 BOOK VALUE 01.01.2018
Securities				
Gross carrying amount	433	11,615	–	12,048
Expected credit loss	–	–	(120)	(120)
Net book value	433			11,928
Placements with, and loans and advances to other banks				
Gross book value	607,456	(2,492)	–	604,964
Expected credit loss	–	–	(424)	(424)
Net book value	607,456			604,540
Loans and advances to customers				
Gross book value	1,251,714	(41,115)	(4,375)	1,206,224
Expected credit loss	(46,755)		(1,087)	(47,842)
Net book value	1,204,959			1,158,382

FV OCI

(HUF million)

	IAS 39 BOOK VALUE 31.12.2017	TRANSFER	REVALUATION	IFRS 9 BOOK VALUE 01.01.2018
Securities				
Gross book value/Fair value	704,065	(492)	–	703,573
Expected credit loss	–	–	(371)	(371)
Net book value	704,065			703,202

FV PL

(HUF million)

	IAS 39 BOOK VALUE 31.12.2017	TRANSFER	REVALUATION	IFRS 9 BOOK VALUE 01.01.2018
Securities				
Gross book value/Fair value	–	492	–	492
Placements with, and loans and advances to other banks				
Gross book value/Fair value	–	2,492	(149)	2,343
Loans and advances to customers				
Gross book value/Fair value	–	29,500	(3,692)	25,808

One equity instrument was transferred from AFS category to FV PL category with the following data at 31 December 2017:

INSTRUMENTUM	GROSS BOOK VALUE (IAS 39 AND IFRS 9) 31.12.2017 AND 01.01.2018	AMOUNT IN OCI AT 12.31.2017
VISA Inc. security	1,901,434 USD	612,188 USD

ii. Impairment – Financial assets and contract assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with 'expected credit loss' (ECL) model. This will require the management's judgement as to how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. The new impairment model will apply to financial assets measured at amortised cost and FVOCI, except for investments in equity instruments, lease receivables and to contract assets.

Under IFRS 9, loss allowances will be measured on either of the following bases:

- 12-month ECLs. These are ECLs that result from possible default events within the 12 months after the reporting date; and
- lifetime ECLs. These are ECLs that result from all possible default events over the expected life of a financial instrument.

During the financial year 2017 UniCredit Group proceeded with the development of business and risk concepts addressing the changes in accounting and methodological framework.

Notes to the financial statements (CONTINUED)

New methodology for ECL measurement (multi-year PD, LGD, EAD) and transfer logic was finalised and documented on UniCredit Group level and customised based on local peculiarities in 2017. In order to support Group and regulatory requirements IFRS9 compliant IT tool was developed and tested throughout 2017 based on the detailed business requirement documents and functional specifications.

The Group believes that impairment losses are likely to increase and become more volatile for assets in the scope of the IFRS 9 impairment model.

(HUF million)

MEASUREMENT CATEGORY	LOAN LOSS ALLOWANCE UNDER IAS 39/ PROVISION UNDER IAS 37	RECLASSIFICATION	REMEASUREMENT	LOAN LOSS ALLOWANCE UNDER IFRS 9
Loans and receivables (IAS 39)/Financial assets at amortised cost (IFRS 9)				
Cash and balances with central banks	–	–	–	–
Loans and advances to banks	–	–	424	424
Loans and advances to customers	46,755	–	1,087	47,842
Investment securities	–	–	–	–
Total	46,755	–	1,511	48,266
Held to maturity (IAS 39)/Financial assets at amortised cost (IFRS 9)				
Investment securities	–	–	120	120
Available for sale financial instruments (IAS 39)/Financial assets at FVOCI (IFRS 9)				
Investment securities	–	–	371	371
Loan commitments and financial guarantee contracts				
Provisions (loan commitments)	1,398	–	558	1,956
Provisions (financial guarantees)	470	–	443	913
Total	1,868	0	1,492	3,360

(HUF million)

	STAGE 1	STAGE 2	STAGE 3	POCI	
ASSETS TO BE MEASURED AT AMORTISED COST	12-MONTH ECL	LIFETIME ECL	LIFETIME ECL	PURCHASED OR ORIGINATED CREDIT-IMPAIRED	TOTAL
Gross carrying amount per asset type					
Cash and balances with central banks	–	–	–	–	–
Loans and advances to banks	557,889	25,686	–	–	583,575
Loans and advances to customers	1,090,898	46,877	62,746	4,443	1,204,964
Investment securities	13,832	–	–	–	13,832
Total gross carrying value	1,662,619	72,563	62,746	4,443	1,802,371
Loss allowance under IFRS 9 per asset type					
Cash and balances with central banks	–	–	–	–	–
Loans and advances to banks	423	–	–	–	423
Loans and advances to customers	3,304	1,671	41,420	1,447	47,842
Investment securities	120	–	–	–	120
Total loss allowance under IFRS 9	3,847	1,671	41,420	1,447	48,385

The Group intends to make ongoing impact assessment simulations to analyse effects from first time adoption throughout 2018.

iii. Classification – Financial liabilities

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, under IAS 39 all fair value changes of liabilities designated as at FVTPL are recognised in profit or loss, whereas under IFRS 9 these fair value changes are generally presented as follows:

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss.

Standards and Interpretations issued by IASB but not yet adopted by the EU

Notes to the financial statements (CONTINUED)

At present, IFRS as adopted by the EU do not significantly differ from regulations adopted by the International Accounting Standards Board (IASB) except from the following new standards and amendments to the existing standards, which were not endorsed for use in EU as at date of publication of these financial statements (the effective dates stated below is for IFRS in full):

- IFRS 17 “Insurance Contracts” (effective for annual periods beginning on or after 1 January 2021).
- IFRIC 22 “Foreign Currency Transactions and Advance Consideration” (effective for annual periods beginning on or after 1 January 2018).
- IFRIC 23 “Uncertainty over Income Tax Treatments” (effective for annual periods beginning on or after 1 January 2019).
- Amendments to IFRS 2 “Share-based Payment” – Classification and Measurement of Share-based Payment Transactions (effective for annual periods beginning on or after 1 January 2018).
- Annual Improvements to IFRS Standards 2014-2016 Cycle (Amendments to IAS 28 effective for annual periods beginning on or after 1 January 2017, Amendments to IFRS 1 effective for annual periods beginning on or after 1 January 2018).
- Amendments to IAS 40 “Investment Property” – Transfers of Investment Property (effective for annual periods beginning on or after 1 January 2018).
- Amendments to IFRS 9 “Financial Instruments” – Prepayment Features with Negative Compensation (effective for annual periods beginning on or after 1 January 2019).
- Amendments to IAS 28 “Investment in Associates and Joint Ventures” – Long-term Interests in Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2019).

The Group anticipates that the adoption of these standards, amendments to the existing standards and interpretations will have no material impact on the financial statements of the Group in the period of initial application. At the same time, hedge accounting regarding the portfolio of financial assets and liabilities, whose principles have not been adopted by the EU, is still unregulated.

4. Risk Management Policies

The most significant business risks to which the Bank is exposed are: credit risk, liquidity risk, market risk (includes interest rate and foreign exchange rate risks) and operational risks. The Group takes a group-wide approach to manage risk, tailored for specific Hungarian legal and business requirements. Integrated and on-line systems ensure constant, timely monitoring of risk.

The Group's policies for managing each of the major financial risks are reviewed regularly by the respective business areas, internal audit, senior management and the Management Board.

j) Credit risk

Credit risk is the risk of financial loss occurring as a result of a default by counterparty in their contractual obligation to the Group.

Credit regulations including the approval process, portfolio limit concentration guidelines, approval of discretionary limits, formulation of standards for the measurement of credit exposures and the risk rating of clients based on the assessment of management quality and financial statements, as well as the definition of eligible collaterals and the rules of their valuation are submitted, as well as the definition of eligible collaterals and the rules of their valuation by the Credit Risk Officer and approved in general by the Management Board, in details by the Chief Executive Officer.

Client and transaction classification

All outstanding loans are reviewed in general monthly, in-depth at least quarterly on an individual basis or – below a certain threshold – within a collective assessment.

Clients are classified at least yearly based on a rating system, which incorporates qualitative and quantitative factors, or in case of retail clients the classification is done at the time of loan application and afterwards on a monthly basis based on scorecards.

The Group applies a rating master-scale consisting of 26 notches within 10 rating classes. Thereof three notches serve for the defaulted customers, the others for the performing ones. Ratings refer to the probability of default (PD) according to the (group-wide used) master-scale. (Certainly, in case of defaulted clients PD is 100%).

Client classification is not equivalent to 'loans' classification.

Collateral

Principles and methods for the valuation of collateral securing the transactions of the Group involving risk-taking, as well as certain legal stipulations affecting the collateral applied by the Group and the principles for the monitoring of collateral are set out in the collateral valuation rules.

Notes to the financial statements (CONTINUED)

General principle is that the collateral:

- shall be legally binding and recoverable;
- shall be directly accessible and;
- appropriate to be liquidated in time.

The Group accepts and registers in its system the following types of collateral:

- Financial collateral held at own bank;
- Financial collateral held with other institutions;
- Insurance;
- Personal collateral – direct;
- Personal collateral – indirect;
- Real estate collateral;
- Assignment of receivables, pledge on receivables;
- Movable property collateral;
- Other collateral.

The basis for the valuation of collateral is the market value adjusted by the following factors:

- Collateral haircut: a percentage showing the expected loss (in %) of the market value in case of realisation of the collateral. Haircut is separately defined for every collateral type,
- Currency haircut: in case of mismatch between the currency of the loan and that of the collateral, the Group applies currency haircut to take into account currency risk,
- Maturity haircut: maturity mismatch occurs on exceptional basis, if the term of the collateral/collateral agreement is shorter than that of the agreement for the commitment. In such cases a haircut must be applied.

In case of real estate collateral, the value is established by a technical expert who is independent from the credit process. The value of real estate shall be reviewed regularly, in compliance with the legal provisions: at least once a year for non-residential real estate and once every 3 years for residential real estate. In case of residential real estate the Group applies statistical revaluation.

The price/value of financial collateral is updated daily in the collateral system.

Eligibility of guarantees and surety is subject to proper evaluation of the guarantor according to the respective internal rules.

Loan classification

The Group assesses whether there is objective evidence that loans and advances are impaired. Loans and advances are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash-flows of the asset that can be estimated reliably.

Objective evidence that loans and advances are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications, that a borrower will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers, or economic conditions that correlate with defaults in the Group.

Assets obtained by the Group during the year by taking possession of collateral held as security against loans and advances have to be evaluated as well, taking into account the possibility of expected loss at the sale of that asset. However, the Group's policy is to pursue timely realisation of the collateral in an orderly manner. The Group generally does not use the non-cash collateral for its own operation.

Loans are classified in general monthly and going into details at least quarterly, individually or (below a certain threshold) collectively.

Individual classification is necessary if the total exposure of the client exceeds a certain limit predefined in the relevant internal regulation. In this case the classification has to be based on the expected cash-flows, evaluated and revised according to the following aspects:

- a) the credit rating of the customer or the partner: the financial position, stability and income-generating capacity of the customer or partner affected by the financial or investment service and issuer of the security, and any changes thereto;
- b) compliance with the rules of repayment (delay): delays in the repayment of the principal and its interests arising in connection with the repayment of the receivable;
- c) the country risk relating to the customer (in respect of both political and transfer risks) and any changes thereto;
- d) the value of collateral pledged in security, their liquidity and accessibility, and any changes therein;
- e) the re-saleability and liquidity of the item (the market conditions of supply and demand, the available market prices and participation in the issuer's equity capital in proportion to the investment);
- f) the future payment obligation recognized as a loss arising from the item.

Notes to the financial statements (CONTINUED)

For the purpose of evaluation, the criterion set out in point e) applies to the classification of investments, stocks received in payment for claims and off-balance sheet liabilities, and the criterion set out in point f) typically applies to the classification of off-balance sheet liabilities. In the process of classifying items, all of the criteria indicated above have to be taken into consideration in a way where the amount of loss expected in the future in relation to the item shall be assessed on the basis of points a)-c) and points e)-f) as a result of the lack of return, the future payment obligations recorded as a loss, and the expected costs of enforcement of the collateral. Subsequently, the value of collaterals relating to the given item shall be deducted from the probable future loss, following the order of enforcement. Time effect of the future cash-flows has also to be taken into consideration during the evaluation.

Collective impairment can be applied if the total exposure of the client does not reach the predefined limit. Impairment is calculated in this case also at individual level, but with a simplified – standardized – method: taking into account the overdue days and certain – statistically estimated – parameters of both the client and the loan. Any deviation from this result is allowed only by taking over the item into individual classification.

Distressed restructuring

Restructuring is to be considered distressed (and thus resulting in a default event) in case of restructuring of principal and interest which is necessary because of the client's poor financial situation, and which results in a certain degree of debt forgiveness (that of principal, interests or fees, deferred payments), i.e. if the net present value of the loan is negatively affected by the restructuring, and if without the restructuring the customer would have got defaulted with high probability. Restructuring or re-aging for business considerations (e.g. the adjustment of the repayment schedule to the cash-flow of the client) does not constitute a default signal.

Impaired loans and securities

Impaired loans and securities are loans and securities for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loans or securities agreements.

Past due but not impaired loans

Loans and securities, where the contractual interests and principal payments are past due but the Group believes that impairment is not necessary on the basis of the level of security/collateral available or collection of outstandings.

Impairment loss

The Group allocates impairment losses that represent its estimate of the incurred losses in its loan portfolio. The main components of this impairment loss are an individual specific loss component that relates to individually significant exposures, and collective specific loan impairment losses allocated for individually non-significant loans based on internal policies.

The Group allocates impairment for incurred but not reported loss (IBNR) according to IFRS based on the parent Group guidelines.

For predefined sub-portfolios expected loss is calculated based on the following formula:

$$EL = EaD \times PD \times LGD$$

Where

EL	is expected loss,
EaD	is exposure at default,
PD	is probability of default (within one year), and
LGD	is loss given default.

Also at sub-portfolio level the loss confirmation period (LCP) is defined (ranging 4-12 months), which shows the average time period between the deterioration of the client's financial situation and its detection by the Group.

IBNR is calculated by multiplying EL by LCP, and increase/decrease is booked accordingly.

Write-off policy

The Group writes-off a loan or security balance (and any related impairment losses balance) when they prove to be uncollectible.

Current tendencies in lending

The industrial sector analysis and collateral details of loan portfolios are presented in Note 20 and the details of exposure of credit risk are presented in Note 45.

As for new retail loans, the Group applies selectivity, meaning more focus on products and segments with lower risk profile, also in accordance with Holding Policies and Guidelines, the legal provisions about responsible lending (implemented in 2010) and the legal provisions on debt to income and loan to value ratios (implemented in 2015, modified in 2016). Thanks to this the quality of newly disbursed portfolio is very good.

Notes to the financial statements (CONTINUED)

The Group lays strong emphasis on all elements of collection and – in addition to the programs prescribed by law or recommendation (etc. 1/2016 of the National Bank of Hungary (III.11.) No. recommendation for payment of past due mortgage loans restoration) – it continuously offers the possibility of renegotiation to its private individual clients in payment delay due to financial problems (e.g. termination of employment) or unfavourable economic conditions. The Group fulfilled the NBH. 14/2012 (XII.13.) and the 1/2016. (III.11.) No. recommendation and implemented it in the processes.

The Group maintained actively its contract signed in 2012 with the National Asset Management Company (Nemzeti Eszközkezelő, NET) and, on basis of individual assessment and decision, allows debtors fulfilling the criteria set forth in the respective legal regulations to participate in the program whereby the NET purchases the mortgaged real estate, pays the purchase price to the Bank as repayment to the outstanding loan and the Bank releases the rest of the loan, with the debtor continuing to remain in the property as renter.

In 2017 the Group had a special one-off offer for a segment of impaired retail clients with mortgage loans: after the sale of the collateralized real estate property and payment of the purchase price into the loan the bank waives the remaining debt.

In 2017 the Group launched a project to decrease the retail impaired mortgage loan portfolio. Significant part of this portfolio was sold in March and December.

In the corporate segment in 2017 the strengthening of our financing activity was still in focus. Parallel we continued to lay special emphasis on the monitoring, restructuring and collection activity. In case of corporate portfolio the Group's lending policy is differentiated by sectors and it defines a selective risk approach for new transactions in the most endangered sectors. Thanks to the successful collection activity real estate deals decreased in the problem loans portfolio in 2017, however, a significant part of the problem loans are still related to real estate financing deals stemming from the preceding years. Thanks to our prudent risk taking policy the portfolio composition in the other sectors is still balanced regarding both the problem-free exposures and transactions handed over to special treatment in 2017.

ii) Liquidity risk

Liquidity risk arises if the bank is unable to meet due obligations associated with its financial liabilities in time in any currency.

The objective of prudential liquidity management is to ensure that the Group has the ability to generate sufficient funds to meet all cash flow obligations as these fall due. Effective liquidity management is gaining importance in recent years ensuring market confidence, and protect the capital base while permitting effective growth. UniCredit Group has created its own short term and structural liquidity models similar to the efforts of the Basel Committee. The Group takes into account also the local legal requirements of foreign funding adequacy and mortgage funding adequacy ratio limitations and monitors the Basel III liquidity ratios besides its own internal regulations in managing liquidity.

Limits regarding the maximum net outflow of funds in a particular period (typically short-term) and in a particular currency and all currencies are in place and are monitored daily. Long-term funding plan and structural liquidity is approved and monitored by the Banks' Asset Liability Committee ('ALCO').

In line with UniCredit Group-wide standards, the Group deals with liquidity risk as a central risk in banking business by introducing and monitoring short-term and medium-term liquidity requirements. In this context the liquidity situation for the next few days and also for longer periods is analysed against a standard scenario and against scenarios of several general and bank-specific liquidity crisis. The degree of liquidity of customer positions and proprietary positions is analysed on an ongoing basis. Procedures, responsibilities and reporting lines in this area have been laid down in the liquidity policy, which includes a contingency plan in the event of a liquidity crisis.

Short-term and structural liquidity limits of the Group were observed continuously in 2017. The degree to which accumulated liquidity outflows are covered by accumulated inflows within the following month and year is determined on an ongoing basis. It was used as a key figure in managing the Group's liquidity and funding. Beyond the limits on ratios, absolute gap limits are in place to decrease central funding and liquidity dependency.

The liquidity structure of statement of financial positions for 2016 and 2017 are represented in Note 37 and the maturity analyses of derivative financial instruments are represented in Notes 39 and 40.

iii) Market risk

Market risk is the risk that changes in market prices, such as interest rates, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's/issuer's default) will affect the Group's income or the fair value of its holdings of financial instruments.

Market risk management encompasses all activities in connection with Group's International Markets (Treasury) Management ("ALM") operations and management of the statement of financial position structure. Risk positions are aggregated at least daily, analysed by the independent risk management unit and compared with the risk limits set by the Management Board and the ALCO designated by the Management Board. At the Group market risk management includes ongoing reporting on the risk position, limit utilisation, and the daily presentation of results of Markets' operations.

Notes to the financial statements (CONTINUED)

The Group uses the risk management procedures of UniCredit Group's Internal Model (IMOD). These procedures provide aggregate data and make available the major risk parameters for the various trading operations daily. Besides Value at Risk ("VaR"), other factors of equal importance are stress-oriented volume and position limits. Additional elements of the limit system are loss-warning level limits and options-related limits applied to trading and positioning in non-linear products.

IMOD, the UniCredit Group-wide pure historic VaR model implemented in the "UGRM" system of UniCredit Group.

Internal risk model is used for computing economic capital in Hungary, but the Pillar 1 capital requirement is calculated by the regulatory standard method. The system comprises all major risk categories: interest rate risk, credit spread risk, equity position risk (both general and specific risk) and exchange rate risk. The VaR position of the Group is presented in Note 47.

Regular and specific stress scenario calculations complement the information provided to ALCO and the Management Board. Stress scenarios are based on assumptions of extreme movements in individual market risk parameters. The Group analyses the effect of such fluctuations and a liquidity disruption in specific products and risk factors on the Group's results.

In addition to the risk model results, income data from market risk activities are also calculated and communicated on a daily basis. Such data are compared with current budget figures. Reporting includes marking to market of all investment positions regardless of their treatment/classification in the IFRS-based financial statements ("total return"). The results are reported directly to the Group's trading and risk management units, and also via the access-protected web application "ERCONIS" consolidated on group level.

The Group uses the "MARCONIS" web-based system to comprehensively and systematically review the market conformity of its transactions.

The daily reporting also includes details of volume-oriented sensitivities which are compared with the respective limits. The most important detailed presentations include: basis point values (interest rate/spread changes of 0.01%) by re-pricing band, FX sensitivities and sensitivities in equities and emerging-market/high-yield positions (by issue, issuer and market) by delta equivalents. Risk management is performed with details varying according to the risk-takers. In the interest rate sector, for example, basis point limits per currency and re-pricing band, basis point totals per currency and/or per re-pricing segment (total of absolute Basis Point Values – BPV) are used for risk management. By analogy to the detailed presentation of basis point positions in the interest rate sector, daily reporting presents details of credit spread by issue and re-pricing band. The BPV and credit spread points analysis are presented in Note 48. The interest rate re-pricing analysis is presented in Note 38.

Management of statement of financial position structure

Interest rate risk and liquidity risk from customer transactions is attributed to Group's treasury operations through a matched funds transfer pricing system applied throughout the UniCredit Group. This makes it possible to attribute credit, market and liquidity risk and contribution margins to the bank's business divisions in line with the principle of causation. ALCO ensures that the Group's overall maturity structure is optimised.

Products for which the material interest-rate and capital maturity is not defined, such as variable-rate sight and savings deposits, are modelled in respect of investment period and interest rate sensitivity by means of analyses of historical time series, and taken into account in the Group's overall risk position.

Interest rate sensitivities are determined and taken into account in hedging activities, which results in a positive contribution to profits from customer business.

Foreign exchange rate risk

The Group has assets and liabilities (on and off-balance sheet) denominated in several foreign currencies, and it is therefore exposed to foreign exchange rate risk. Foreign exchange rate risk arises when a mismatch occurs in the spot and forward asset/liability structure within a currency.

The statement of foreign exchange exposures (currency structure of assets and liabilities) is presented in Note 36.

iv) Compliance with CRD IV/CRR (Basel III)

The successful implementation of CRDIV/CRR from 2014 was managed as a group issue, and is covered mainly with group-wide solutions.

The Group started with standardised approach of the Basel II in 2008, and received the licence to apply foundation internal based approach (F-IRB) from 1st July, 2011 for the large corporate, mid-corporate, and bank portfolio.

- The IRB roll-out is being carried out locally. Model development is carried out partially centrally and partially locally.
- The decentralized approach means that the development of models complying with the requirements of A-IRB is done locally by the Group with the support of UniCredit S.p.A., they give support during the implementation by providing guidelines and standards and in terms of coaching and advice. The Group is responsible for the use and development of methods and local models, and the compliance to local regulatory requirements, while for UniCredit Group wide models it is the task of UniCredit Group.

Notes to the financial statements (CONTINUED)

The approval of the developed models and methods under IRB have to be confirmed (by a non-binding opinion), and the processes and data quality has to be validated by unit independent from the business, and are audited by Internal Audit as well.

v) Operational risk

Operational risk is the risk of loss due to errors, infringements, interruptions, damages caused by internal processes or personnel or systems, or caused by external events.

Operational risk events are those resulting from inadequate or failed internal processes, personnel and systems or from systemic and other external events: internal or external fraud, employment practices and workplace safety, client claims, products distribution, fines and penalties due to regulation breaches, damage to Group's physical assets, business disruption and system failures, process management.

Strategic risk, business risk and reputational risk are different from operational risk, whereas legal, conduct, and compliance risk are included in the operational risk definition.

UniCredit Bank Hungary is permitted and has used the Advanced Measurement Approach (AMA) since 1st July 2009, complying with all quantitative and qualitative requirements set by laws and regulations, the supervisor or even by internal Group rules.

The Group's Management Board is responsible for the effective oversight over operational risk exposure. The operational risk office (i.e. Operational and Reputational Risk Controlling) notifies the Management Board (partly via the Internal Control Business Committee, a.k.a. ICBC) about considerable operational risks, their changes as well as relevant breaches to policies and limits. The Management Board shall have an overall understanding of the operational risk control framework and of how operational risk affects the Group.

The Group's Management Board ensures that:

- the operational risk control process is sound and fully communicated and implemented in specific policies process and procedures within the business units taking into account the appropriateness and effectiveness;
- operational risk managers in the business lines are appointed, coming in for adequate support in order to perform their duties;
- the relevant committees are informed on changes in risk profiles and exposure, supported by the Operational and Reputational Risk Controlling;
- major operational risk drivers are identified, also examining reports from the Operational and Reputational Risk Controlling unit, Compliance and Internal Audit.

The Group's Management Board is responsible for approving all the material aspects of the operational risk framework, including the appointment of the office responsible for its implementation and control.

In the Group, the Operational and Reputational Risk Committee shall act as a decision-making body for issues arising from and connected with operational and reputational risks.

Members of the Committee are

- the Chief Risk Officer,
- the Divisional Operational Risk Managers, and
- the Head or deputy Head of Identity & Communication.

Permanent invitees of the Operational and Reputational Risk Committee meetings are: the Head of Organization, the representative(s) of Internal Audit, the internal auditor of UniCredit Jelzálogbank Zrt. (UniCredit Mortgage Bank – concerning Mortgage Bank issues of the agenda), resp. the Operational Risk Manager of UniCredit Leasing Hungary Zrt. and UniCredit Operatív Lizing Kft. (concerning leasing companies issues of the agenda).

The Operational and Reputational Risk Committee (OpRRiCo) holds its meeting regularly, once a quarter. The extraordinary meeting of the Committee may be summoned by any of the members as required or initiated by Operational and Reputational Risk Controlling and Internal Audit with the specification of the associated reasons.

Detection, monitoring, and mitigation of operational risk, and set up of action plans are supported by the Permanent Workgroup having its sessions quarterly, as well. Topics and proposals discussed in the Workgroup are the base for presentations towards OpRRiCo and ICBC.

Internal Audit is responsible for evaluating periodically (annually) the operational risk management system and measurement functionality and effectiveness, as well as its compliance with the regulatory requirements. Internal Audit monitors also the process of data collection and data management.

The centralized Operational and Reputational Risk Controlling unit has to operate the framework and to coordinate the decentralized activity of operational risk management, carried out by the nominated (divisional and administrative) operational risk managers in each business unit.

Notes to the financial statements (CONTINUED)

Operational and Reputational Risk Controlling annually prepares a self-assessment on the compliance of the local operational risk management, control and measurement system with the UniCredit Group standards and internal rules. UniCredit Group Internal Validation unit gives a non-binding opinion on the self-assessment, and local Internal Audit checks it, as well. At last it has to be approved by the Management Board of the Group.

Exposure to credit risk

General remarks:

- All categories are considered at client level,
- Past due days are defined according to the Basel III definition.

The categories for loan classification are as follows:

Performing loans: Loans belonging to client, who have no overdue debt or it does not exceed 90 days, and who have no default event.

Impaired loans:

Impaired Past due: Loans belonging to clients, who have an overdue amount greater than 90 days on any of their loans, and who have no other “unlikely to pay” default event.

UTP other than Bad loans: Loans belonging to client, who has an “unlikely to pay” default event (excluding work-out and 90 days overdue defaults).

Bad loans: Loans belonging to client are in the work-out phase.

5. Use of estimates and judgements

These disclosures supplement the commentary on risk management policy.

i.) Impairment for credit losses

Assets accounted for at amortised cost are evaluated for impairment on a basis described in accounting policy 3.(m.), (n.) and risk management policy 4.(i.).

ii.) Determining fair value

As far as valuation prices and techniques of financial instruments are concerned, the Group follows a measurement using a three-level fair valuation hierarchy, which reflects the significance of the inputs used in measuring fair values and contains the following three levels:

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices observed in non-active markets) or indirectly (i.e. derived from prices observed for similar assets or liabilities);

Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The classification of financial instruments is described in Note 39.

Fair Valuation is supplemented by a Fair Valuation Reserve that inter alia covers the effect of widened bid-ask spreads and the deteriorated liquidity of respective securities.

The fair value valuation techniques for loans and advances, and deposits are described in Note 43.

In accordance with IFRS requirements the Bank books CVA (Credit Valuation Adjustment) as an adjustment to the fair value of its OTC derivative trades. The CVA calculation is performed centrally by Bank Austria on a quarterly basis.

iii.) Fair value measurement principles

The fair value of financial instruments is based on their quoted price in an active market for that instrument at the reporting date without any deduction for transaction costs. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis. If a quoted market price is not available or the market is not active, the fair value of the instrument is estimated using pricing models or discounted cash-flow techniques.

Notes to the financial statements (CONTINUED)

Where discounted cash-flow techniques are used, the estimated future cash-flows are based on management's best estimates and the discount rate is a market related rate at the reporting date for an instrument with similar terms and conditions. Where pricing models are used, inputs are based on market related measures at reporting date.

The fair value of derivatives that are not exchange-traded are estimated at the amount that the Group would receive upon normal business conditions to terminate the contract at the reporting date taking into account current market conditions and the current creditworthiness of the counterparties.

The Group makes fair value adjustments which arise from close out costs and less liquid positions. Trading assets and available-for-sale assets are adjusted by fair value adjustments figures.

For performing loans the fair value is taken from Bank Austria's model, while for non-performing loans we make the assumption that the book value is the fair value. For the calculation of the performing loans' FV the liquidity profiles of Bank Austria and the Bank are used, as well as the risk adjusted zero coupon curve. For the discount factors of Assets the sum of the risk free rate, the expected loss and unexpected loss, for the liabilities the sum of the risk free rate and own credit spread (liquidity spread) are used, in line with the Group methodology.

The fair values for loans and deposits are shown at an aggregated product level and are not available on individual item level.

iv.) Effects of sovereign debt crisis and earlier credit crunch in valuations

- Debt securities classified as Available for Sale, were not impaired, as the Group doubts neither the issuers' (Hungarian Government, local Mortgage Banks) ability, nor their willingness to fulfill their due payments. The few price losses observed through market prices, hence, were realised in the available-for-sale Reserves in the Statement of changes in Shareholder's Equity.
- The Group was not engaged in securitization, nor does it possess financial instruments particularly hit by the 2008 market, nor the Greek default, such as credit derivatives or structured OTC products (e.g. CDOs, SIV), or assets affected by recent sovereign crises. The mortgage bonds issued by Jelzálogbank are covered bonds, the assets staying in the mortgage bank's portfolio and complying with the standards of the mortgage bank law, thus qualifying for the state subsidy schemes.
- The Group is exposed towards the Hungarian Government, but the vast majority of those exposures are liquidity reserves, mostly short term government bonds, and bills.
- The major effect of the long lasting crisis and the recent Hungary-specific concerns are that the liquidity charges (CDS of the Group) and the country spread of Hungary has widened, HUF yields have risen. These impact the Bank through re-pricing of its funding mix, and incorporated in the net interest income of loans and deposits, in tandem with the corresponding hedging instruments, such as cross-currency basis swaps (designated as cash flow hedge) that do cause swings in the equity but do smooth the yearly income statements.

6. Net interest income

	(HUF million)	
	2017	2016
Interest and similar income		
Interest income from Central Bank	813	2,899
Interest income from banks	2,606	3,770
Interest income from customers	35,973	40,113
Interest income on Trading financial instruments	945	384
Interest income on Hedge derivatives	25,680	30,034
Interest income on Available-for-sale financial assets	13,472	13,074
Interest income on Held-to-maturity assets	35	36
Interest income other	339	870
Total	79,863	91,180
Interest expense and similar charges		
Interest expense to Central Bank	164	(417)
Interest expense to banks	(738)	(1,855)
Interest expense related to hedge derivatives	(18,310)	(21,220)
Interest expense to customers	(1,611)	(5,283)
Interest expense on Subordinated loans	(1)	(15)
Interest expense on issued bonds	(1,056)	516
Total	(21,552)	(28,274)
Net interest income	58,311	62,906

Notes to the financial statements (CONTINUED)

7. Net fee and commission income

(HUF million)

	2017	2016
Fees and commission income		
Payment transaction fees	40,160	38,056
Custody service fees	3,691	3,510
Brokerage	4,294	5,125
Financial guarantee fees	1,482	1,659
Other financial fees and commissions	945	368
Total	50,572	48,718
Fees and commission expense		
Payment transaction fees	(7,142)	(6,343)
Custody service fees	(827)	(750)
Brokerage	(97)	(157)
Financial guarantee fees	(421)	(637)
Other financial fees and commissions	(513)	(978)
Total	(9,000)	(8,865)
Net fee and commission income	(41,572)	39,853

8. Dividend income

(HUF million)

	2017	2016
Dividends on investments	187	185
Total	187	185

9. Net trading income

(HUF million)

	2017	2016
Gain/(Loss) on foreign exchange, net	13,926	13,033
Gain/(Loss) on trading interest rate swaps, net	(944)	245
Gain/(Loss) on debt securities, net	190	119
Gain/(Loss) on equities, net	—	(52)
Gain/(Loss) on trading FRAs, net	67	(314)
Other trading income	111	77
Total	13,350	13,108

Notes to the financial statements (CONTINUED)

10. Net gain and loss on other financial instruments

(HUF million)

	2017	2016
Gain		
Available for sale debt securities	4,056	22,248
Available for sale investments	–	1,690
Gain on repurchased issued Mortgage Bonds	86	–
Total	4,142	23,938
Loss		
Available-for-sale debt securities	(3,286)	(21,445)
Loss on repurchased issued Mortgage Bonds	(101)	–
Total	(3,387)	(21,445)
Net gain on other financial instruments	755	2,493

11. Personnel expenses

(HUF million)

	2017	2016
Wages and salaries	13,955	12,931
Statutory social-security contributions	2,790	3,235
Other employee benefits	1,500	1,339
Employer's contributions	401	434
Total	18,646	17,939

The number of employees (in full time equivalent) was 1,756.4 on 31 December 2017 (2016: 1,727.9).

12. General operating expenses

(HUF million)

	2017	2016
Indirect tax expense and fees to authorities	30,628	26,325
Renting costs and operating expenses of property	2,113	2,002
Advertising	674	441
Information technology costs	5,626	5,771
Material and office equipment costs	251	233
Other administrative expenses	3,168	2,939
Total	42,460	37,711

Notes to the financial statements (CONTINUED)

13. Other income and expenses

(HUF million)

	2017	2016
Operating income		
Income related to foreign currency loans converted to HUF	5,141	10,196
Renting activity	1,008	1,178
Service transfer fees received	80	4
Indemnity received	47	32
Gain on sale of leasing assets	11	–
Other	666	272
Total	6,953	11,682
Operating expenses		
Expenses related to rented investment properties	(220)	(296)
Indemnity paid	(87)	(59)
Cost of Workout	(28)	(84)
Damage	(132)	–
Other	(167)	(272)
Total	(634)	(711)
Net other operating income	6,319	10,971

14. Taxation

The tax charge for the year is based on the profit for the year according to the statutory accounts of the Bank as adjusted for relevant taxation regulations. The corporate income tax rate was for the year of 2017 9% in Hungary. The supplementary tax (what the Bank had to pay to the income earned on special loans) has ceased from 1 January 2017.

14.1 Tax expense for the year

(HUF million)

	2017	2016
Current tax expense	5,112	9,991
Adjustments for prior years	76	253
Total	5,188	10,244
Deferred tax expense	245	2,550
Total income tax expense in income statement	5,433	12,794

14.2 Reconciliation of effective tax rate

	2017		2016	
	%	(HUF MILLION)	%	(HUF MILLION)
Profit before tax		56,532		66,483
Income tax using the domestic corporate tax rate	9.0	5,088	18.8	12,489
Supplementary corporate tax for banks	–	–	0.2	152
Adjustments for prior years	0.1	41	0.0	15
Tax effects of income/expenses exempt from corporate tax	0.0	25	(0.8)	(547)
Changes in tax rates	–	–	1.8	1,171
Other	0.5	279	(0.7)	(486)
Total	9.6	5,433	19.3	12,794

Notes to the financial statements (CONTINUED)

14.3 Balances, related to taxation

(HUF million)

	2017			2016		
	ASSETS	LIABILITIES	NET	ASSETS	LIABILITIES	NET
Current tax assets/(liabilities) at year-end	59	(1)	58	1,111	–	1,111
Deferred tax assets/(liabilities)						
Available-for-sale securities	–	(1,988)	(1,988)	(1)	(1,042)	(1,043)
Cash flow hedges	–	(1,908)	(1,908)	–	(1,805)	(1,805)
Property and equipment from tied up capital	106		106	199	(24)	175
IFRS transition adjustment	219	(36)	183	609	(12)	597
Effect of items, increasing/(decreasing) the local tax base	693	(115)	578	606	(266)	340
Netting effect	(890)	890	–	(1,279)	1,279	–
Total deferred tax assets/(liabilities)	128	(3,157)	(3,029)	134	(1,870)	(1,736)
Total tax assets/(liabilities)	187	(3,158)	(2,971)	1,245	(1,870)	(625)

14.4 Movements in temporary differences during the year – 2017

(HUF million)

	OPENING BALANCE	RECOGNISED IN THE CONSOLIDATED INCOME STATEMENT	RECOGNISED IN OCI	CLOSING BALANCE
Available-for-sale securities	(1,043)		(945)	(1,988)
Cash flow hedges	(1,805)		(103)	(1,908)
Property and equipment from tied up capital	175	(69)	–	106
IFRS transition adjustment	–	183	–	183
Effect of items, increasing/(decreasing) the local tax base	597	(19)	–	578
Netting	340	(340)	–	–
Total deferred tax assets / (liabilities)	(1,736)	(245)	(1,048)	(3,029)

14.5 Movements in temporary differences during the year – 2016

(HUF million)

	OPENING BALANCE	RECOGNISED IN THE CONSOLIDATED INCOME STATEMENT	RECOGNISED IN OCI	CLOSING BALANCE
Available-for-sale securities	(903)	–	(140)	(1,043)
Cash flow hedges	(3,479)	–	1,674	(1,805)
Allowances for loans (IBNR)	737	(737)	–	–
Property and equipment from tied up capital	177	(2)	–	175
IFRS transition adjustment	–	597	–	597
Effect of items, increasing/(decreasing) the local tax base	2,748	(2,408)	–	340
Total	(720)	(2,550)	1,534	(1,736)

15. Cash and unrestricted balance with the Central Bank

(HUF million)

	2017	2016
Cash on hand	18,349	15,173
Unrestricted balance with the Central Bank	3,306	11
Total	21,655	15,184

Notes to the financial statements (CONTINUED)

16. Financial instruments held for trading

(HUF million)

	2017	2016
Financial assets held for trading		
State treasury bills	10,193	625
State bonds	41,081	3,631
Other bonds	631	584
Equity securities	–	4
<i>Positive fair value of derivatives</i>		
FX derivatives	7,367	9,195
Interest rate derivatives	50,385	59,519
Commodity derivatives	2,938	2,720
Total	112,595	76,278
Financial liabilities held for trading		
<i>Negative fair value of derivatives</i>		
FX derivatives	6,675	4,823
Interest rate derivatives	55,813	60,876
Commodity derivatives	2,937	2,720
Total	65,425	68,419

17. Available-for-sale financial assets

(HUF million)

	2017	2016
State treasury bills	–	7,484
State bonds	572,405	597,794
Other bonds	130,845	42,853
Equities	815	705
Total	704,065	648,836
Impairment	–	–
Total	704,065	648,836

18. Held-to-maturity investments

(HUF million)

	2017	2016
Mortgage bonds	433	436
Total	433	436

The market value of the held-to-maturity securities portfolio as at 31 December 2017 is HUF 444 million (2016: HUF 441 million).

Notes to the financial statements (CONTINUED)

19. Placements with, and loans and advances to banks

(HUF million)

	2017	2016
Placements with Central Bank		
Maturity less than one year	218,352	186,766
Loans and advance to other banks		
Nostros with other banks	10,971	12,899
Maturity less than one year	361,491	534,383
Maturity more than one year	16,642	63,108
Total	607,456	797,156

20. Loans and advances to customers

(HUF million)

	2017	2016
Private and commercial:		
Maturity less than one year	442,652	446,167
Maturity more than one year	797,447	707,260
Securities, recognised as loans	11,615	14,002
Total	1,251,714	1,167,429
Provision for impairment and losses on credit products (Note 34)	(46,755)	(51,974)
Total	1,204,959	1,115,455

A. Analysis by industrial sector

	2017		2016	
	(HUF MILLION)	%	(HUF MILLION)	%
Private clients	221,125	17.67	240,430	20.59
Real estate finance	190,801	15.25	183,743	15.74
Trade	155,994	12.46	130,923	11.21
Transportation	111,419	8.90	127,129	10.89
Machine industry	106,813	8.53	73,349	6.28
Financial activities	83,778	6.69	105,345	9.02
Food processing	63,236	5.05	52,750	4.52
Chemicals/Pharmaceutical	53,476	4.27	45,726	3.92
Metallurgy	51,456	4.11	35,317	3.03
Construction	50,495	4.03	47,710	4.09
Community	49,389	3.95	33,459	2.87
Agriculture	34,079	2.72	30,475	2.61
Light industry	19,824	1.58	19,630	1.68
Electric energy industry	12,574	1.01	15,706	1.35
Catering trade	4,190	0.33	3,552	0.30
Communication	3,493	0.28	2,655	0.23
Mining	443	0.04	430	0.04
Other	39,129	3.13	19,100	1.64
Total	1,251,714	100.00	1,167,429	100.00

Notes to the financial statements (CONTINUED)

The acceptance value of collateral and other security pledges for loans were as follows (the acceptance value of the collaterals is reviewed periodically):

B. Collateral for the above loans

(HUF million)

	2017	2016
Against individually impaired	16,903	20,195
Warrant and guarantees	2,087	1,175
Cautions	448	491
Property	14,225	17,225
Debt securities	0	–
Equities	0	–
Others	143	1,304
Against collectively impaired	7,645	18,860
Warrant and guarantees	140	262
Cautions	70	154
Property	7,279	18,414
Debt securities	0	–
Equities	2	2
Others	154	28
Against past due, but not impaired	2,894	2,077
Warrant and guarantees	13	13
Cautions	1	5
Property	1,204	2,059
Debt securities	0	–
Equities	0	–
Others	1,676	–
Against neither past due nor impaired	552,955	436,316
Warrant and guarantees	127,432	84,052
Cautions	16,574	30,257
Property	319,007	299,871
Debt securities	4,508	933
Equities	955	992
Others	84,519	20,211
Total:	580,397	477,448

Loans and advances to customers are presented in the above structure in Note 45.

The above collaterals also cover the credit facilities, granted not disbursed. Those are detailed in Note 35.

21. Hedging derivative instruments

(HUF million)

	2017	2016
Derivative assets held for risk management purposes		
Interest rate swaps	44,395	31,294
Forward rate agreements	–	3
Total	44,395	31,297
Derivative liabilities held for risk management purposes		
Interest rate swaps	32,008	25,019
Forward rate agreements	3	81
Total	32,011	25,100

Further details on hedging derivatives are disclosed in Note 40. Specific details of the cash flow hedging principles and effectiveness tests are summarized in a separate document.

Notes to the financial statements (CONTINUED)

22. Equity investments

As at 31 December 2017 investments in consolidated subsidiaries were as follows:

(HUF million)

NAME OF INVESTMENT	GROSS BOOK VALUE	SHAREHOLDER'S EQUITY
UniCredit Jelzálogbank Zrt.	3,761	22,100
Arany Pénzügyi Lízing Zrt.	453	4,715
Sas-Reál Kft.	750	802
UniCredit Leasing Hungary Zrt.	672	542
UniCredit Operatív Lízing Kft.	3	14
UniCredit Biztosításközvetítő Kft.	41	210

All above investments are in companies incorporated in Hungary. Apart from these investments, the Bank holds majority interest in an SPV, Europa Investment Fund.

The Fund is consolidated in these financial statements, since the Group has the power to govern it, and is exposed to the volatility of its returns.

23. Investment properties

(HUF million)

	2017	2016
Investment property in usage	10,330	10,787
Total	10,330	10,787

The Group's investment properties are held within Europa Investment Fund, of which, 98.7 % (2016: 98.8%) of the units is owned by the Bank. The investment properties are regularly valued by an independent real estate appraiser company, as required by the respective law. The valuation methods, applied by the appraiser company are compliant with the regulations in IFRS 13. The investment properties, in usage are valued at fair market value. These properties earned HUF 744 million rental income in 2017 (2016: HUF 992 million).

24. Property, plant and equipment

Movement in property, plant and equipment

(HUF million)

	ACQUISITION COST AT THE BEGINNING OF THE YEAR	ACCUMULATED DEPRECIATION AT THE BEGINNING OF THE YEAR	BUSINESS COMBINATION	ADDITIONS	DISPOSALS NET	OTHER MOVEMENT	DEPRECIATION & AMORTISATION	CARRYING AMOUNT AT THE END OF THE YEAR
2017								
Land and buildings	24,995	(5,473)	–	374		–	(522)	19,374
Office equipment	8,375	(8,051)	–	805		–	(314)	815
Motor vehicles	574	(336)	–	323	(35)	–	(85)	441
Capital work in progress	296	–	–	969	(1,250)	–	–	15
Total	34,240	(13,860)	–	2,471	(1,285)	–	(921)	20,645
2016								
Land and buildings	25,330	(5,191)	–	123	88	(115)	(537)	19,522
Office equipment	8,558	(7,893)	–	324	–	–	(665)	324
Motor vehicles	562	(292)	–	59	16	–	(75)	238
Capital work in progress	22	–	–	780	506	–	–	296
Total	34,472	(13,376)	–	1,286	610	(115)	(1,277)	20,380

Notes to the financial statements (CONTINUED)

25. Intangible assets

Movement in intangible assets

(HUF million)

	ACQUISITION COST AT THE BEGINNING OF THE YEAR	ACCUMULATED DEPRECIATION AT THE BEGINNING OF THE YEAR	BUSINESS COMBINATION	ADDITIONS	DISPOSALS NET	OTHER MOVEMENT	DEPRECIATION & AMORTISATION	CARRYING AMOUNT AT THE END OF THE YEAR
2017								
Rental rights	235	(234)	–	5	–	–	–	6
Licenses	1,048	(279)	–	663	–	–	(70)	1,362
Software	12,206	(9,176)	–	2,609	(1)	–	(200)	5,438
Total	13,489	(9,689)	–	3,277	(1)	–	(270)	6,806
2016								
Rental rights	274	274	–	5	–	–	(4)	1
Licenses	740	327	–	411	–	–	(55)	769
Software	13,231	10,945	–	2,183	–	–	(1,439)	3,030
Total	14,245	11,546	–	2,599	–	–	(1,498)	3,800

26. Other assets

(HUF million)

	2017	2016
Leasehold improvements	272	311
Trade receivables, advances and other receivables	1,429	4,094
Accrued income and prepaid expenses	7,293	1,805
Items in transit	2,423	8,030
Receivables from State Treasury	1,426	1,537
Other	489	307
Total	13,332	16,084
Impairment losses	(83)	(47)
Total	13,249	16,037

27. Deposits and loans from banks

(HUF million)

	2017	2016
Loans from Central Bank		
Maturity less than one year	28,257	29,034
Maturity more than one year	77,904	89,958
Total	106,161	118,992
Loans and deposits from other banks		
Maturity less than one year	31,862	118,494
Maturity more than one year	417,128	491,768
Total	448,990	610,262
Total	555,151	729,254

Notes to the financial statements (CONTINUED)

28. Deposits from customers

(HUF million)

	2017	2016
Maturity less than one year	1,625,192	1,534,527
Maturity more than one year	18,634	11,478
Total	1,643,826	1,546,005

The above balances include customer transit accounts. Amounts included in customer transit accounts are held pending clarification and completion of transactions with customers undertaken in the ordinary course of business.

29. Subordinated loans

(HUF million)

	2017	2016
Bank Austria AG	–	10,563
Bank Austria AG	–	10,655
Total subordinated loans	–	21,218

The amount due to the parent company consisted of two separate loans, one of ATS 200 million received in July 1994 and another of DEM 38 million received in 1997. On 19 December 2001 the loans were consolidated and converted into EUR.

The annual extension of the above loans was discontinued in 2013. Their final maturity was end of 2017.

30. Issued mortgage bonds

(HUF million)

	2017	2016
Maturity less than one year	3,218	475
Maturity more than one year	75,007	22,693
Total	78,225	23,168

31. Other liabilities

(HUF million)

	2017	2016
Accrued expenses and prepaid income	10,833	7,983
Provision on guarantees and unutilised loans	1,868	1,752
Trade payable	2,231	2,009
Other taxes payable	2,745	2,934
Items in transit	7,719	5,014
Other	391	615
Total	25,787	20,307

Notes to the financial statements (CONTINUED)

32. Share capital

(HUF million)

	2017	2016
Authorised and issued share capital	24,118	24,118

Share capital consists of 4,823,644 ordinary shares with a par value of HUF 5,000 each.
100% of the issued shares are held by UniCredito Italiano S.p.a.

33. Statutory reserves

(HUF million)

	GENERAL RESERVE	TIED-UP RESERVE	TOTAL
Balance at 31 December 2016	33,506	265	33,771
Appropriations from retained earnings	5,201	(265)	4,936
Balance at 31 December 2017	38,707	–	38,707

34. Impairments and provisions

34.1 Impairments and provisions on credit products

(HUF million)

	LOANS	GUARANTEES AND UNUTILISED LOANS	TOTAL FINANCIAL INSTRUMENTS
Balance 31 December 2016	51,974	1,751	53,725
Write-offs	(6,644)	–	(6,644)
Amounts released	(14,519)	(1,353)	(15,872)
Additional impairment and provisions	16,102	1,470	17,572
Effect of FX rate fluctuation	(158)	–	(158)
As at 31 December 2017	46,755	1,868	48,623
Net movement in impairment and provisions	(5,061)	117	(4,944)
Write-offs	6,644	–	6,644
Net amount charged to the income statement	1,583	117	1,700
Receivables written-off	(1,383)	–	(1,383)
Total charged to the income statement, excluding the effect of f/x rate fluctuation	200	117	317

34.2 Other impairments and provisions

(HUF million)

	PROVISION MOVEMENT ON NON-CREDIT RISK ITEMS
Balance 31 December 2016	2,339
Write-offs	(71)
Amounts released	(316)
Additional impairment provisions	2,206
Effect of FX rate	(2)
As at 31 December 2017	4,156
Net movement in impairment provisions	1,819
Write-offs	71
Net amount charged to the income statement	1,890

The methods and assumptions applied in the calculation of provisions are described in points 3. m) and 4.

Notes to the financial statements (CONTINUED)

35. Commitments and contingent liabilities

At 31 December 2017, the Group had the following commitments and contingent liabilities (in nominal values):

(HUF million)

	2017	2016
Loan and overdraft facilities granted not disbursed	781,158	885,664
Financial guarantees	311,656	200,029
Letters of credit	34,216	27,906
FX spot sales (notional)	238,734	166,830
Other contingent liabilities	5,025	25

As at 31 December 2017, the total face value of client assets held in safe custody by the Group was 3,552,402 HUF million (2016: 3,554,847 HUF million).

36. Currency structure of assets and liabilities

The currency structure of assets and liabilities as at 31 December 2017 is as follows:

CURRENCY	ASSETS	LIABILITIES AND EQUITY	OFF BALANCE SHEET NET	TOTAL NET F/X EXPOSURE LONG / (SHORT)
Euro	1,002,451	851,973	(135,005)	15,473
Swiss Francs	3,576	4,559	1,230	247
United States Dollars	100	106,143	67,293	(38,750)
Japanese Yen	142	371	231	2
Polish Zloty	764	4,881	3,741	(376)
British Pounds	423	3,178	2,757	2
Czech Crowns	462	1,682	1,294	74
Other	43,161	4,928	1,356	39,589
Total foreign currency:	1,051,079	977,715	(57,103)	16,261
Hungarian Forint	1,695,696	1,769,060	59,589	(13,775)
Total	2,746,775	2,746,775	2,486	2,486

The currency structure of assets and liabilities as at 31 December 2016 is as follows:

CURRENCY	ASSETS	LIABILITIES AND EQUITY	OFF BALANCE SHEET NET	TOTAL NET F/X EXPOSURE LONG / (SHORT)
Euro	1,062,587	932,048	(1,910)	128,629
Swiss Francs	7,841	6,323	103	1,621
United States Dollars	32,449	74,627	(184)	(42,362)
Japanese Yen	492	629	—	(137)
Polish Zloty	698	6,393	—	(5,695)
British Pounds	572	6,644	—	(6,072)
Czech Crowns	48,792	39,451	—	9,341
Other	1,437	4,952	—	(3,515)
Total foreign currency:	1,154,868	1,071,067	(1,991)	81,810
Hungarian Forint	1,582,138	1,665,939	(3,793)	(87,594)
Total	2,737,006	2,737,006	5,784	5,784

Notes to the financial statements (CONTINUED)

37. Residual contractual maturities of financial assets and liabilities

Residual contractual maturities of financial assets and liabilities 31 December 2017

(HUF million)

	CARRYING AMOUNT	GROSS NOMINAL INFLOW / (OUTFLOW)	LESS THAN 1 MONTH	1-3 MONTHS	3 MONTHS TO 1 YEAR	1-5 YEARS	MORE THAN 5 YEARS
<i>Non-derivative assets</i>							
Cash and cash equivalents	21,655	21,655	21,655	–	–	–	–
Trading securities	112,595	114,506	60,692	25	11,830	36,038	5,921
Investment securities	704,498	738,329	2,027	2,776	50,059	584,528	98,939
Loans and advances to banks	607,456	638,184	268,956	28,234	271,390	51,755	17,849
Loans and advances to customers	1,204,959	1,341,492	271,786	42,370	111,518	608,556	307,262
Total	2,651,163	2,854,166	625,116	73,405	444,797	1,280,877	429,971
<i>Non-derivative liabilities</i>							
Trading liabilities	–	–	–	–	–	–	–
Deposits from banks	(555,151)	1,006,381	122,537	20,757	53,784	440,568	368,735
Deposits from customers	(1,643,826)	1,652,654	1,546,141	50,200	36,850	18,187	1,276
Debt securities issued	(78,225)	151,604	–	8,348	21,785	120,362	1,109
Subordinated liabilities	–	–	–	–	–	–	–
Total	(2,277,202)	2,810,639	1,668,678	79,305	112,419	579,117	371,120
<i>Cash flows from derivative positions</i>							
Trading:	(4,721)	(4,090)	(3,748)	2,298	(158)	(1,871)	(611)
Risk management:	12,384	18,673	3,388	1,396	(2,710)	16,009	590
Total	7,663	14,583	(360)	3,694	(2,868)	14,138	(21)
Unrecognised loan commitments	–	(1 127 030)	(5 495)	(72 411)	(247 407)	(269 909)	(531 808)

Residual contractual maturities of financial assets and liabilities 31 December 2016

(HUF million)

	CARRYING AMOUNT	GROSS NOMINAL INFLOW / (OUTFLOW)	LESS THAN 1 MONTH	1-3 MONTHS	3 MONTHS TO 1 YEAR	1-5 YEARS	MORE THAN 5 YEARS
<i>Non-derivative assets</i>							
Cash and cash equivalents	15,184	15,184	15,184	–	–	–	–
Trading securities	76,278	76,374	71,629	503	1,980	1,991	271
Investment securities	649,272	690,462	(1,030)	2,441	35,482	417,088	236,481
Loans and advances to banks	797,156	837,380	245,452	128,402	356,274	84,723	22,529
Loans and advances to customers	1,115,455	1,274,869	261,882	254,645	217,860	270,495	269,987
Total	2,653,345	2,894,269	593,117	385,991	611,596	774,297	529,268
<i>Non-derivative liabilities</i>							
Trading liabilities	–	–	–	–	–	–	–
Deposits from banks	(729,254)	1,115,893	81,159	38,981	41,935	536,817	417,001
Deposits from customers	(1,546,005)	1,564,125	1,413,254	88,879	38,617	19,867	3,508
Debt securities issued	(23,168)	25,012	–	37	443	24,500	32
Subordinated liabilities	(21,218)	21,183	–	–	21,183	–	–
Total	(2,319,645)	2,726,213	1,494,413	127,897	102,178	581,184	420,541
<i>Cash flows from derivative positions</i>							
Trading:	3,015	5,524	(1,000)	4,155	3,745	(1,215)	(161)
Risk management:	6,198	23,524	2,165	1,457	2,646	17,263	(7)
Total	9,213	29,048	1,165	5,612	6,391	16,048	(168)
Unrecognised loan commitments	–	(1,112,339)	(26,386)	(118,712)	(323,127)	(252,018)	(392,096)

Notes to the financial statements (CONTINUED)

38. Exposure to interest rate risk – non-trading portfolios

(HUF million)

	CARRYING AMOUNT	LESS THAN 1 MONTH	1-3 MONTHS	3 MONTHS TO 1 YEAR	1-5 YEARS	MORE THAN 5 YEARS	NOT INTEREST RATE SENSITIVE
31 December 2017							
Cash and cash equivalents	21 655	21 655	–	–	–	–	–
Loans and advances to banks	607 456	482 335	47 408	63 477	14 236	–	–
Loans and advances to customers	1 204 959	358 381	571 027	221 207	52 476	1 868	–
Investment securities	704 498	6 554	2 174	17 521	545 624	97 449	35 176
Total	2 538 568	868 925	620 609	302 205	612 336	99 317	35 176
Deposits from banks	(555 151)	(361 006)	(63 538)	(52 419)	(45 831)	(32 357)	–
Deposits from customers	(1 643 826)	(1 543 344)	(52 772)	(32 955)	(14 755)	–	–
Debt securities issued	(78 225)	(3 219)	(2 649)	–	(72 357)	–	–
Subordinated liabilities	–	–	–	–	–	–	–
Total	(2 277 202)	(1 907 569)	(118 959)	(85 374)	(132 943)	(32 357)	–
Effect of derivatives held for risk management	2 596 528	109 822	266 019	(219 863)	(359 958)	206 133	–
Total	2 857 894	(928 822)	767 669	(3 032)	119 435	273 093	35 176

The re-pricing techniques and principles, applied for qualification by the Group are described in details in Note 4.

(HUF million)

	CARRYING AMOUNT	LESS THAN 1 MONTH	1-3 MONTHS	3 MONTHS TO 1 YEAR	1-5 YEARS	MORE THAN 5 YEARS	NOT INTEREST RATE SENSITIVE
31 December 2016							
Cash and cash equivalents	15 184	15 184	–	–	–	–	–
Loans and advances to banks	797 156	504 675	156 596	88 596	47 289	–	–
Loans and advances to customers	1 115 455	338 040	338 923	392 286	47 352	(3 491)	2 345
Investment securities	649 272	75 901	4 949	12 109	284 168	266 392	5 753
Total	2 577 067	933 800	500 468	492 991	378 809	262 901	8 098
Deposits from banks	(729 254)	(503 515)	(83 063)	(56 872)	(60 542)	(25 262)	–
Deposits from customers	(1 546 005)	(1 405 875)	(92 918)	(33 747)	(13 345)	(120)	–
Debt securities issued	(23 168)	(175)	(2 650)	(300)	(20 012)	(31)	–
Subordinated liabilities	(21 218)	–	(10 564)	(10 654)	–	–	–
Total	(2 319 645)	(1 909 565)	(189 195)	(101 573)	(93 899)	(25 413)	–
Effect of derivatives held for risk management	1 189 507	29 642	64 580	(268 115)	89 351	84 299	–
Total	1 449 945	(943 107)	375 853	123 303	374 261	321 787	8 098

The re-pricing techniques and principles, applied for qualification by the Group are described in details in Note 4.

Notes to the financial statements (CONTINUED)

39. Derivative financial instruments held for Trading

31 December 2017

(HUF million)

	NOTIONAL AMOUNT WITH REMAINING LIFE OF			TOTAL	FAIR VALUES (NET)	FVA
	LESS THAN 3 MONTHS	3 MONTHS – 1 YEAR	OVER 1 YEAR			
Interest rate derivatives						
Forward Rate Agreements (bought)	–	200,000	50,000	250,000	(135)	–
Forward Rate Agreements (sold)	–	100,000	–	100,000	184	–
Interest Rate Swaps (SC IRS)	138,080	140,623	1,198,660	1,477,363	(4,393)	(45)
Interest Rate Swaps (DC IRS)	–	96,919	273,632	370,551	(920)	–
Multicallable swap	–	–	–	–	–	–
Forward Exchange&Swap*	1,601,431	842,094	66,908	2,510,432	2,104	–
Options (sold amounts)						
Barrier (European)						
Long Call	–	6,683	5,103	11,786	198	–
Short Call	–	6,451	4,885	11,336	(198)	–
Long Put	–	6,451	4,885	11,336	149	–
Short Put	–	6,683	5,103	11,786	(149)	–
FX (European)*						
Long Call	366	–	366	732	19	–
Long Call (embedded)	1,017	–	–	1,017	–	–
Long Put	–	–	–	–	–	–
Long Put (embedded)	133	–	–	133	–	–
Short Call	1,371	–	372	1,743	(19)	–
Short Put	129	–	–	129	–	–
IR Options						
CAP (bought)	–	–	3,296	3,296	42	–
CAP (sold)	–	–	3,296	3,296	(42)	–
FLOOR (bought)	–	–	–	–	–	–
FLOOR (sold)	–	–	–	–	–	–
Equity Options	–	–	–	–	–	–
Commodity						
Commodity forward&swap (bought)	580	2,551	316	3,447	2,901	–
Commodity forward&swap (sold)	580	2,551	316	3,447	(2,900)	–

*: without HUF and option delta

Notes to the financial statements (CONTINUED)

31 December 2016

(HUF million)

	NOTIONAL AMOUNT WITH REMAINING LIFE OF			TOTAL	FAIR VALUES	FVA
	LESS THAN 3 MONTHS	3 MONTHS – 1 YEAR	OVER 1 YEAR		(NET)	
Interest rate derivatives						
Forward Rate Agreements (bought)	–	100,000	–	100,000	(164)	–
Forward Rate Agreements (sold)	–	155,510	–	155,510	9	–
Interest Rate Swaps (SC IRS)	100,030	163,408	1,113,370	1,376,808	(166)	(37)
Interest Rate Swaps (DC IRS)	–	4,702	386,256	390,958	(1,465)	–
Multicallable swap	–	–	7,042	7,042	–	–
Forward Exchange&Swap*	1,648,920	261,192	12,191	1,922,303	4,888	–
Options (sold amounts)						
Barrier (European)						
Long Call	1,944	5,443	–	7,387	64	–
Short Call	1,866	5,225	–	7,091	(64)	–
Long Put	1,866	5,225	–	7,091	252	–
Short Put	1,944	5,443	–	7,387	(252)	–
FX (European)*						
Long Call	1,451	856	–	2,307	15	–
Long Call (embedded)	233	–	–	233	–	–
Long Put	1,400	529	–	1,929	32	–
Long Put (embedded)	208	–	–	208	1	–
Short Call	1,628	840	–	2,468	(15)	–
Short Put	1,620	527	–	2,147	(33)	–
IR Options						
CAP (bought)	–	23	3,819	3,842	53	–
CAP (sold)	–	23	3,819	3,842	(53)	–
FLOOR (bought)	–	23	–	23	–	–
FLOOR (sold)	–	23	–	23	–	–
Equity Options						
Commodity	–	–	–	–	–	–
Commodity forward&swap (bought)	924	237	159	1,320	2,695	–
Commodity forward&swap (sold)	924	237	159	1,320	(2,695)	–

*:without barrier options

40. Derivative financial instruments held for Hedging purposes

(HUF million)

	NOTIONAL AMOUNT WITH REMAINING LIFE OF			TOTAL	FAIR VALUES	FVA
	LESS THAN 3 MONTHS	3 MONTHS – 1 YEAR	OVER 1 YEAR		(NET)	
31 December 2017						
Interest Rate Swaps (DC IRS)	161,882	156,044	1,910,002	2,227,928	13,486	(480)
Interest Rate Swaps (SC IRS)	8,713	8,521	302,154	319,387	(1,561)	–
Forward Rate Agreements (bought)	–	60,000	–	60,000	(3)	–
Forward Rate Agreements (sold)	–	–	–	–	–	–
31 December 2016						
Interest Rate Swaps (DC IRS)	225,720	143,298	1,577,089	1,946,107	8,797	–
Interest Rate Swaps (SC IRS)	4,361	35,191	207,527	247,079	(1,868)	–
Forward Rate Agreements (bought)	–	296,849	–	296,849	(78)	–
Forward Rate Agreements (sold)	–	–	–	–	–	–

Notes to the financial statements (CONTINUED)

41. Fair valuation hierarchy¹

FINANCIAL ASSETS/ FINANCIAL LIABILITIES	FAIR VALUE IN HUF MILLION AS AT		FAIR VALUE HIERARCHY	VALUATION TECHNIQUE(S) AND KEY INPUT(S)	SIGNIFICANT UNOBSERVABLE INPUT(S)	RELATIONSHIP OF UNOBSERVABLE INPUT(S) TO FAIR VALUE
	31.12.2017	31.12.2016				
Forward Rate Agreements	Trading purpose: 49 Hedging purpose: (3)	Trading purpose: (155) Hedging purpose: (78)	Level 2	Discounted cash flow method is used. The two future cash flows are estimated based on forward interest rate (from observable yield curves at the end of the reporting period) and the contractual interest rate and are both discounted. Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and Unicredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none
Interest Rate Swaps (SC IRS)	Trading purpose: (4,393) Hedging purpose: 13,486	Trading purpose: (166) Hedging purpose: 8,797	Level 2	Discounted cash flow method is used. The future cash flows are estimated based on forward interest rates (from observable yield curves at the end of the reporting period) and contractual interest rate and are discounted. The FV includes both the market value and the accrued interest. Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and Unicredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none
Interest Rate Swaps (DC IRS)	Trading purpose: (920) Hedging purpose: (1,561)	Trading purpose: (1,465) Hedging purpose: (1,868)	Level 2	Discounted cash flow method is used. The future cash flows are estimated based on forward interest rates (from observable yield curves at the end of the reporting period) and contractual interest rate and are discounted. The FV includes both the market value, the accrued interest but excludes the effect of the revalued principals (recognized as forward exchange). Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and Unicredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none
Multicallable swap	—	—	Level 2	Discounted cash flow method is used. The future cash flows are estimated based on forward interest rates (from observable yield curves at the end of the reporting period) and contractual interest rate and are discounted, taking into account the Bermudan option feature of the product. The FV includes both the market value and the accrued interest. Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and Unicredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none

¹ FV of derivatives does not contain the Fair Value corrections (FVA; CVA), FV of securities does not contain the accrued interest.

Notes to the financial statements (CONTINUED)

FINANCIAL ASSETS/ FINANCIAL LIABILITIES	FAIR VALUE IN HUF MILLION AS AT		FAIR VALUE HIERARCHY	VALUATION TECHNIQUE(S) AND KEY INPUT(S)	SIGNIFICANT UNOBSERVABLE INPUT(S)	RELATIONSHIP OF UNOBSERVABLE INPUT(S) TO FAIR VALUE
	31.12.2017	31.12.2016				
Forward Exchange & Swap	2,104	4,888	Level 2	Discounted cash flow method is used. Future cash flows are estimated based on forward exchange rates (from observable forward exchange rates at the end of the reporting period) and contractual forward rates and are discounted. Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and UniCredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none
FX Options	–	–	Level 2	The European options calculation uses the standard Garman-Kohlhagen form of the Black-Scholes formula. Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and UniCredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none
IR Options	–	–	Level 2	The options calculation uses the Black-Scholes model.	none	none
Equity Options	–	–	Level 2	The options calculation uses the Black-Scholes model.	none	none
Commodity forward & swap	1	–	Level 2	Discounted cash flow method is used. The future cash flows are estimated based on forward commodity rates (from observable commodity index curve at the end of the reporting period) and contractual commodity price and are discounted. Credit valuation adjustments (CVAs) and debit valuation adjustments (DVAs) are incorporated into derivative valuations to reflect the impact on fair value of counterparty credit risk and UniCredit own credit quality respectively. Financial model based FVA is used for the valuation of derivatives (close-out risk) as well.	none	none
Bonds	590,800	527,127	Level 1	Marked-to-market valuation based on quotation prices observed in active markets (e.g. Reuters). Liquidity and close-out fair value adjustments apply.	none	none
Bonds	21,961	16,698	Level 2	Marked-to-model valuation based on a curve consisting of liquid bonds of the same sector or sovereign. Liquidity and close-out fair value adjustments apply.	none	none
Corporate bonds	20,299	19,317	Level 1	Marked-to-market valuation based on quotation prices observed in active markets (e.g. Reuters). Liquidity and close-out fair value adjustments apply.	none	none
Corporate bonds	36,550	20,725	Level 2	Marked-to-model valuation based on a curve consisting of liquid bonds of the same sector or sovereign. Liquidity and close-out fair value adjustments apply.	none	none
Investment Certificates	15,756	15,084	Level 2	Marked-to-market valuation based on NAV published by Association of Hungarian Investment Fund and Asset Management Companies.	none	none

Notes to the financial statements (CONTINUED)

FINANCIAL ASSETS/ FINANCIAL LIABILITIES	FAIR VALUE IN HUF MILLION AS AT		FAIR VALUE HIERARCHY	VALUATION TECHNIQUE(S) AND KEY INPUT(S)	SIGNIFICANT UNOBSERVABLE INPUT(S)	RELATIONSHIP OF UNOBSERVABLE INPUT(S) TO FAIR VALUE
	31.12.2017	31.12.2016				
Equities	492	386	Level 1	Marked-to-market valuation based on quotation prices observed in active markets (e.g. Budapest Stock Exchange).	none	none
Equities	323	323	Level 3	Fair market value of the Visa Inc. share (Stock Exchange price).	none	none
Mortgage bonds	72,639	1,729	Level 2	Marked-to-model valuation based on a curve consisting of liquid covered bonds. Liquidity and close-out fair value adjustments apply.	none	none

Reconciliation of Level 3 fair value measurements

(HUF million)

	CORPORATE BONDS	MORTGAGE BONDS	FORWARD EXCHANGE&SWAP	OTHERS	TOTAL
31 December 2017					
Opening balance	–	–	–	323	323
Total gains or losses:					
– in profit or loss	–	–	–	–	–
– in other comprehensive income	–	–	–	–	–
Transactions:					
– purchases	–	–	–	–	–
– issues	–	–	–	–	–
– disposals/settlements	–	–	–	–	–
Transfer to level 3	–	–	–	–	–
Transfers out of level 3	–	–	–	–	–
Closing balance	–	–	–	323	323
31 December 2016					
Opening balance	–	–	–	1,472	1,472
Total gains or losses:					
– in profit or loss	–	–	–	–	–
– in other comprehensive income	–	–	–	–	–
Transactions:					
– purchases	–	–	–	–	–
– issues	–	–	–	–	–
– disposals/settlements	–	–	–	–	–
Transfer to level 3	–	–	–	(1,149)	(1,149)
Transfers out of level 3	–	–	–	–	–
Closing balance	–	–	–	323	323

Notes to the financial statements (CONTINUED)

42. Balances outstanding and transactions with related parties

(HUF million)

	2017	2016
Assets		
Financial assets held for trading	40,811	49,322
Loans and receivables with banks	328,922	514,335
Loans and receivables with customers	6,647	11,481
Derivatives used for hedging	38,300	26,057
Intangible assets	2,345	–
Other assets	13	2,129
Total assets	417,038	603,324
Liabilities		
Deposits from banks	224,265	343,338
Loans subordinated	–	21,218
Deposits from customers	6,131	7,960
Financial liabilities held for trading	46,386	40,373
Derivatives used for hedging	24,377	15,260
Other liabilities	1,891	943
Total Liabilities and Shareholder's Funds	303,050	429,092
Commitments, contingencies, derivatives		
Loan and overdraft facilities granted not disbursed	19,689	20,964
Financial guarantees	20,093	24,609
Derivatives notional amount	4,207,641	3,843,022
Income Statement		
Interest and similar income	2,003	2,561
Interest expense and similar charges	(287)	(1,203)
Fee and commission income	1,136	1,694
Fee and commission expense	(1,687)	(1,815)
Net trading income	3,107	3,167
Fair value adjustment in hedge	72	199
General operating expenses	(4,817)	(5,052)
Other income/(expenses)	405	448
Total	(68)	(1)

The above balances and transactions are outstanding with:

Bank Austria Wien, UniCredit Bank SA., UniCredit Luxembourg SA., UniCredit Bank Czech Republic and Slovakia AS., UniCredit Banka Slovenija DD., Bank Pekao SA., Zagrebacka Banka DD., UniCredit Bank AG., UniCredit SPA., UniCredit Bulbank, Pioneer Global Asset Management S.p.A., UniCredit Bank Serbia JSC., Pioneer Befektetési Alapkezelő Zrt., UniCredit Business Integrated Solutions SCPA., UniCredit Business Integrated Solutions Austria GmbH., Európa Befektetési Alapkezelő Zrt., UniCredit Turn-Around Management CEE GmbH., UniCredit Leasing Hungary, UCTAM Hungary Kft., PEKAO Investment Banking SA., AO UniCredit Bank Moscow, UniCredit Insurance Management CEE GmbH., YAPI ve KREDİ BANKASI.

Notes to the financial statements (CONTINUED)

43. Fair value information

(HUF million)

	2017		2016	
	FAIR VALUE	CARRYING AMOUNT	FAIR VALUE	CARRYING AMOUNT
Cash and unrestricted nostros with Central Bank	21,655	21,655	15,184	15,184
Financial assets held for trading	112,595	112,595	76,278	76,278
Available-for-sale financial assets	704,065	704,065	648,836	648,836
Held to maturity investments	474	433	501	436
Placements with, and loans and advances to banks	607,127	607,456	808,728	797,156
Loans and advances to customers	1,293,976	1,204,959	1,222,218	1,115,455
Hedging derivatives assets	44,395	44,395	31,297	31,297
Equity investments	–	–	–	–
Total financial assets	2,784,287	2,695,558	2,803,042	2,684,642
Deposits and loans from banks	530,824	555,151	688,613	729,254
Deposits from customers	1,643,936	1,643,826	1,549,942	1,546,005
Subordinated loans	0	–	21,113	21,218
Issued bonds	80,313	78,225	23,689	23,168
Financial liabilities held for trading	65,425	65,425	68,419	68,419
Hedging derivative liabilities	32,011	32,011	25,100	25,100
Total financial liabilities	2,352,509	2,374,638	2,376,876	2,413,164

Estimation of fair values for the Fair Value Report to the Notes

The following description summarises the major methods and assumptions used in estimating the fair values of financial instruments reflected in the table.

Loans and advances: Fair value is calculated based on discounted expected future principal and interest cash flows. Loan repayments are assumed to occur at contractual repayment dates, where applicable. (Credit card advances, overdrafts and similar very short term receivables are deemed to be the receivable on demand at the balance sheet date). Expected future cash flows are estimated taking into account credit risk and any indication of impairment. Expected future cash flows, even for homogeneous categories of loans, are estimated on a single deal basis and discounted at a rate taking into account the risk free rate, the expected loss and unexpected loss. The estimated fair values of loans also reflect changes in interest rates.

Investments carried at cost and derivatives: Fair value is based on quoted market prices at the balance sheet date without any deduction for transaction costs, where available. If a quoted market price is not available, fair value is estimated using pricing models or discounted cash flow techniques, where applicable. For investments and fixed assets, where no reliable market price or model price is available, the book value is taken as fair value.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate for a similar instrument at the balance sheet date. Where other pricing models are used, inputs are based on market related data at the balance sheet date.

Bank and customer deposits: For demand deposits and deposits with no defined maturities, fair value is deemed to be the amount payable on demand at the balance sheet date. The estimated fair value of fixed-maturity deposits, including certificates of deposit, is based on discounted cash flows using a rate consisting of the risk free rate and own credit spread (liquidity spread). The value of long-term relationships with depositors is not taken into account in estimating fair values.

Long-term debt: The fair value is based on quoted market prices, if available. For debt instruments without quoted prices the fair value is estimated as the present value of future cash flows, discounted at market interest rates available at the balance sheet date.

Notes to the financial statements (CONTINUED)

44. Segment report

(HUF million)

	TOTAL BANK		RETAIL		PRIVATE BANKING	
	2017	2016	2017	2016	2017	2016
Total Net Interest Income	58,498	63,091	12,274	14,005	235	200
Net fee and commission income	41,572	39,853	20,465	19,450	1,026	916
Trading profit	14,105	15,601	3,248	3,094	82	80
Other operating income/expenses	6,319	10,967	1,674	453	0	–
Total non-interest income	61,996	66,421	25,387	22,997	1,108	996
REVENUES	120,494	129,512	37,661	37,002	1,343	1,196
Direct Expenses	(62,250)	(58,198)	(22,062)	(21,153)	(634)	(488)
Indirect and overhead expenses	0	–	(6,792)	(6,752)	(175)	(157)
OPERATING EXPENSES	(62,250)	(58,198)	(28,854)	(27,905)	(809)	(645)
GROSS OPERATING RESULT	58,244	71,314	8,807	9,097	534	551
Provision for risk and charges	(1,740)	2,225	(1,809)	2,330	0	2
Result and impairment on loans	(317)	(6,681)	2,334	(1,742)	(11)	(4)
Gain/ (losses) on other equity investments	188	(120)	0	–	0	–
Integration costs	157	(259)	157	(259)	0	–
RESULT BEFORE TAXES	56,532	66,479	9,489	9,426	523	549
Income taxes	(5,433)	(12,794)	–	–	–	–
NET PROFIT FOR THE YEAR	51,099	53,685	–	–	–	–
Customer loans net	1,204,959	1,117,800	233,508	237,763	791	563
Deposits from Customers	1,643,826	1,551,019	512,298	480,013	47,502	39,351

(HUF million)

	CORPORATE AND INVESTMENT BANKING		LEASING		OTHERS	
	2017	2016	2017	2016	2017	2016
Total Net Interest Income	23,233	24,589	1,850	1,280	20,906	23,017
Net fee and commission income	20,495	20,065	151	174	(565)	(752)
Trading profit	12,432	11,958	(22)	(13)	(1,635)	482
Other operating income/expenses	1	(33)	99	262	4,545	10,285
Total non-interest income	32,928	31,990	228	423	2,345	10,015
REVENUES	56,161	56,579	2,078	1,703	23,251	33,032
Direct Expenses	(24,126)	(21,805)	(1,541)	(1,483)	(13,887)	(13,269)
Indirect and overhead expenses	(6,148)	(5,885)	0	–	13,115	12,794
OPERATING EXPENSES	(30,274)	(27,690)	(1,541)	(1,483)	(772)	(475)
GROSS OPERATING RESULT	25,887	28,889	537	220	22,479	32,557
Provision for risk and charges	13	(20)	12	9	44	(96)
Result and impairment on loans	(2,527)	(4,779)	(113)	(156)	0	–
Gain/ (losses) on other equity investments	(13)	72	0	–	201	(192)
Integration costs	0	–	0	–	0	–
RESULT BEFORE TAXES	23,360	24,162	436	73	22,724	32,269
Income taxes	–	–	–	–	–	–
NET PROFIT FOR THE YEAR	–	–	–	–	–	–
Customer loans net	888,232	846,476	80,180	63,997	2,248	(30,999)
Deposits from Customers	1,062,587	1,005,877	580	487	20,859	(25,291)

Notes to the financial statements (CONTINUED)

45. Exposure to credit risk

General remarks:

- All categories are considered at client level,
- Past due days are defined according to the Basel III definition.

The categories for loan classification are as follows:

Performing loans:

Loans belonging to client, who have no overdue debt or it does not exceed 90 days and who have no default event.

Impaired loans:

- **Impaired Past due:** Loans belonging to clients, who have an overdue amount greater than 90 days on any of their loans, and who have no other “unlikely to pay” default event.
- **UTP other than Bad loans:** Loans belonging to client, who has an “unlikely to pay” default event (excluding work-out and 90 days overdue defaults).
- **Bad loans:** Loans belonging to client are in the work-out phase.

Notes to the financial statements (CONTINUED)

(HUF million)

	LOANS AND ADVANCES TO CUSTOMERS		PLACEMENTS WITH, AND LOANS AND ADVANCES TO BANKS		INVESTMENTS	
	2017	2016	2017	2016	2017	2016
Individually impaired						
Grade 1 – Performing	0	–	–	–	–	–
Grade 2 – Impaired Past Due	56	137	–	–	–	–
Grade 3 – UTP other than Bad	37,494	41,813	–	–	–	–
Grade 5 – Bad	14,698	14,590	–	–	–	–
Gross amount	52,248	56,540	–	–	–	–
Allowance for impairment	(33,767)	(32,454)	–	–	–	–
Carrying amount	18,481	24,086	–	–	–	–
Collectively impaired						
Grade 1 – Performing	0	–	–	–	–	–
Grade 2 – Impaired Past Due	3,984	6,903	–	–	–	–
Grade 3 – UTP other than Bad	3,327	6,885	–	–	–	–
Grade 5 – Bad	7,248	18,112	–	–	–	–
Gross amount	14,559	31,900	–	–	–	–
Allowance for impairment	(10,590)	(17,154)	–	–	–	–
Carrying amount	3,969	14,746	–	–	–	–
Past due but not impaired						
Grade 1 – Performing	4,390	4,769	–	–	–	–
Grade 2 – Impaired Past Due	0	–	–	–	–	–
Grade 3 – UTP other than Bad	0	–	–	–	–	–
Grade 5 – Bad	0	–	–	–	–	–
Gross amount	4,390	4,769	–	–	–	–
Allowance for impairment	(75)	(73)	–	–	–	–
Carrying amount	4,315	4,696	–	–	–	–
Past due comprises	–	–	–	–	–	–
0-30	3,678	3,792	–	–	–	–
30-60	595	659	–	–	–	–
60-90	117	313	–	–	–	–
90-180	0	4	–	–	–	–
over 180 days	0	1	–	–	–	–
Gross amount	4,390	4,769	–	–	–	–
Allowance for impairment	75	(73)	–	–	–	–
Carrying amount	4,315	4,696	–	–	–	–
Neither past due nor impaired						
Grade 1 – Performing	1,180,517	1,076,565	–	802,841	–	649,272
Grade 2 – Impaired Past Due	0	–	–	–	–	–
Grade 3 – UTP other than Bad	0	–	–	–	–	–
Grade 5 – Bad	0	–	–	–	–	–
Gross amount	1,180,517	1,076,565	–	802,841	–	649,272
Allowance for impairment	(2,323)	(2,293)	–	–	–	–
Carrying amount	1,178,194	1,074,272	–	802,841	–	649,272
Total	1,204,959	1,117,800		802,841		649,272

Notes to the financial statements (CONTINUED)

46. Exposure to market risks – trading and non-trading portfolios

Exposures to interest rate risk

The daily management of interest rate risk is based on BPV and VaR limits. BPV sensitivities are split to re-pricing time buckets and currencies. Both regular and ad-hoc sensitivity analyses are prepared with standard and occasional scenarios.

The standard scenarios are parallel shifts and turns in the yield curve below 10y tenor. Currency-wise both HUF yield shocks and all relevant foreign currency yield curve shocks are analyzed. Similar to last year, the applied standard magnitudes are 300bps for HUF and 200bps for other currencies. In the results the effect of flooring is not reflected, which is visible in the symmetric +/- shocks. Below scenarios describe a sudden, permanent change in the market; revalued immediately along NPV approach and accrued interest approach where applicable.

					(HUF million)
		INCOME	EQUITY	OTHER (NOTES ONLY)	TOTAL
2017					
HUF only	shift up	(4,097)	(48,644)	6,802	(45,939)
	shift down	4,097	48,644	(6,802)	45,939
	turn up	(1,720)	(29,708)	3,158	(28,270)
	turn down	1,720	29,708	(3,158)	28,270
All yields	shift up	(4,459)	(46,924)	6,786	(44,596)
	shift down	4,459	46,924	(6,786)	44,596
	turn up	(1,812)	(29,689)	3,750	(27,751)
	turn down	1,812	29,689	(3,750)	27,751
Worst of the above		(4,459)	(48,644)	(6,802)	(45,939)
2016					
HUF only	shift up	(3,160)	(53,498)	14,279	(42,379)
	shift down	3,160	53,498	(14,279)	42,379
	turn up	(918)	(31,413)	7,930	(24,401)
	turn down	918	31,413	(7,930)	24,401
All yields	shift up	(1,918)	(52,755)	12,991	(41,682)
	shift down	1,918	52,755	(12,991)	41,682
	turn up	272	(31,418)	8,172	(22,975)
	turn down	(272)	31,418	(8,172)	22,975
Worst of the above		(3,160)	(53,498)	(14,279)	(42,379)

Fair value fluctuations in both the Available for Sale portfolio and the Cash Flow Hedge derivatives affect Equity directly; while trading position and other derivatives affect Income Statement. NPV changes of positions booked against Equity will migrate to Income Statement as their Cash Flows mature. General interest rate positions and HTM bond holdings do not impact Income or Equity, their effect is shown under Other.

FX Sensitivity

Year-end FX open position sums up to 8,1 bn HUF, less than 10% of Solvency Capital. The total open FX position is limited at 60mn EUR, ca. 18 bn HUF. A 10% FX shock (HUF appreciation) would have about 0,8 bn HUF effect. Positions reported as they are managed and show the bank's overall risks including all on-balance and off-balance items, underlying and derivatives.

All market value change from FX revaluation impacts P&L.

FX risk in general is out of scope of hedge accounting except for derivative transactions where both IR and FX components influence the fair value at the same time (i.e. cross-currency IRS). As hedging relationship must be designated for a hedging instrument in its entirety, FX part of these derivatives is subject to fair value hedge with FX revaluation impact in P&L.

Notes to the financial statements (CONTINUED)

47. Summary of VaR position

The internal model based VaR (1 day, confidence level of 99 %) for 2017 moved in a range of HUF 1,895 million and HUF 3,933 million, following a moderately volatile path during the year. The average VaR was HUF 2,924 million; less than the year before. Credit spread risk and Interest rate risk were the main drivers of the VaR. The fx risk was far below the other components although also contributed the total market risk of the Group.

(HUF million)

RISK CATEGORY	YEAR-END	AVERAGE	MINIMUM	MAXIMUM
VaR as at 31 December 2017				
Exchange rate risk	46	107	4	288
Interest rate risk	1,716	1,677	876	2,339
Credit spread	2,102	2,698	2,071	4,021
Vega risk	0	0	0	1
Equity risk	0	1	0	6
Overall	1,913	2,924	1,895	3,933
VaR as at 31 December 2016				
Exchange rate risk	127	92	–	213
Interest rate risk	1,933	2,040	1,731	2,434
Credit spread	4,448	4,188	3,611	4,636
Vega risk	–	–	–	1
Equity risk	–	–	–	5
Overall	3,794	3,542	2,741	4,200

In addition to VaR, risk positions of the Group are limited through volume & sensitivities limits. As part of the daily risk reporting, detailed Market Risk Reports are prepared for all risk-taking departments, with updated and historical information made available to all risk-takers and the respective heads of departments.

48. Summary of interest sensitivity

As at 31 December 2017 and 2016, the entire interest rate position of the Group (trading and investment) for major currencies was composed as follows:

Basis Point Value ("BPV") for main currencies

							ANNUAL STATISTICS		
CURRENCY	UP TO 3 MONTHS	3 MONTHS TO 1 YEAR	1 YEAR TO 3 YEARS	3 YEARS TO 10 YEARS	OVER 10 YEARS	TOTAL	MAXIMUM	MINIMUM	ABSOLUTE AVERAGE
As at 31 December 2017									
CHF	(0.04)	0.02	(0.04)	(0.02)	(0.00)	(0.09)	0.17	(0.09)	0.06
EUR	1.33	1.84	3.57	0.92	(0.09)	7.57	12.65	(5.13)	2.34
GBP	0.00	0.02	(0.00)	(0.00)	0.00	0.02	0.02	(0.15)	0.04
HUF	(8.67)	2.74	(9.02)	(128.41)	(10.11)	(153.48)	(123.37)	(154.05)	138.44
JPY	0.00	0.00	0.00	0.00	0.00	0.00	0.01	(0.01)	0.00
USD	0.15	(1.49)	0.29	0.07	0.00	(0.98)	0.75	(6.77)	3.13
Total*	10.30	6.33	12.92	129.42	10.20	162.34			
As at 31 December 2016									
CHF	(0.08)	0.22	(0.01)	(0.03)	0.00	0.10	0.32	(0.26)	0.12
EUR	(2.93)	3.07	(0.56)	1.30	(0.14)	0.74	9.50	(9.63)	3.91
GBP	0.01	(0.02)	(0.01)	(0.00)	0.00	(0.02)	0.00	(0.10)	0.05
HUF	(13.22)	0.88	(7.22)	(110.61)	(5.74)	(135.91)	(105.35)	(140.52)	124.77
JPY	0.00	(0.00)	(0.00)	(0.00)	0.00	0.00	0.00	(0.00)	0.00
USD	(0.04)	(3.30)	(0.10)	0.01	0.00	(3.43)	2.85	(4.04)	1.12
Total	16.46	7.52	7.90	111.94	5.88	140.41			

*Total contains risk taking in all reported currencies

Notes to the financial statements (CONTINUED)

During 2017, the Group had major interest rate positions only in HUF. The BPV positions raised in 2016 mainly due to the changing market environment and not purely stemming from the increased risk appetite. The risk-taking departments and the management are daily informed about the development of the interest rate risks from the BPV monitoring reports.

By analogy to the detailed presentation of basis point positions in the interest rate sector, daily reporting presents details of credit spread by issuer and maturity.

(HUF million)

SEGMENTS	SECTOR	CREDIT SPREAD BASIS POINTS
Spread Points as at 31 December 2017		
Corporate	Energy BB	(9.70)
Financial	BB banks	(29.60)
Financial	A banks	–
Financial	BBB banks	–
Treasury	Treasuries – Local	(222.37)
Spread Points as at 31 December 2016		
Corporate	Energy BB	(10.71)
Financial	BB banks	(0.26)
Financial	A banks	–
Financial	BBB banks	–
Treasury	Treasuries – Local	(234.77)

Government and local mortgage banks of investment grade account for the largest part of the Group's credit spread positions. Credit spread positions slightly changed in 2017 although longer duration Hungarian Government Bonds were purchased. Credit spread positions are also limited on a total level of about HUF 280 million.

Capital requirements for market risk

Market risk, counterparty- and settlement risk of trading positions have to be reported together. The quarterly average capital requirement of the trading book was HUF 3.5 billion (in 2016 HUF 4.1 billion), the highest quarterly capital requirement was HUF 4.1 billion (in 2016: HUF 5.0 billion) mostly stemming from the counterparty risk of OTC derivatives and the position risk of bonds.

49. Compensation of key management personnel

The remuneration of directors and other members of key management personnel during the year was HUF 549 million (2016: HUF 442 million).

The key management consists of the Board of Directors, the Managing Directors, and the members of the Supervisory Board. No loans are granted for the key management personnel.

Based on the proportionality principle of the Hungarian Act No. CCXXXVII of 2013, the compensation above the limit is made in shares, with deferred time, taking into account Group's principals by the Group.

Notes to the financial statements (CONTINUED)

50. Regulatory capital

The EU Regulation No 575/2013 (Capital Requirements Regulations – CRR) has introduced common reporting standards for institutions in relation to capital (COREP – Common Reporting) from 1 January 2014 and financial reporting (FINREP) from 30 September 2014.

The Bank implemented Basel III from 1 January 2014. The Bank complies with the requirements and methods according to the Hungarian Banking Law (Law CCXXXVII of 2013 on credit institutions and financial enterprises, Hpt.) implementing Directive 2013/36/EU and the Capital Requirements Regulations (EU No. 575/2013).

The local Banking Group implemented Basel II Standard method from 1 January 2008. The Bank follows the instructions, requirements and methods given by the national regulator and its parent bank. The purpose of Basel II was to create more risk sensitive standards and regulations on defining regulatory capital requirement of capital financial institutions. Banks need to put aside capital to reduce the risks associated with its investing and lending practices. The most significant business risks to which the Bank is exposed are credit, liquidity, market (including interest and foreign exchange rate risks) and operational risk. Integrated and on-line systems ensure constant, timely monitoring of risk. The Bank's policies and processes for managing the major financial risks are reviewed regularly by the respective business areas, internal audit, senior management and the Boards of Directors.

UniCredit Bank Hungary Zrt. switched to internal rating based IRB method in its capital requirement calculation from the 1st July 2011.

Solid capital situation is an important element of the Bank's policy in order to maintain investor, creditor and market confidence and to sustain future business development. The impact of the level of capital on shareholders' return is also recognized and the Bank pays special attention to balance between the higher returns that might be possible with gearing and the advantages and security of a sound capital position.

One of the main blocks of COREP reporting templates is capital adequacy: an overview of regulatory capital and, total risk exposure amount.

The reporting templates of capital adequacy overview include information about Pillar 1 capital requirement and regulatory own funds. They are structured in CA1-4 templates as of below:

CA1	contains the amount of own funds of the institutions
CA2	summarizes the total risk exposure amounts
CA3	contains capital ratios and capital levels
CA4	contains memorandum items needed for calculating items in CA1 as well as information with regard to the Hpt./CRD capital buffers

Own funds components:

- Common Equity Tier 1 (CET 1): Ordinary share capital, Share premium, General reserve, Profit reserve, Profit for the year, Other Comprehensive Income, Deduction from CET1 capital due to prudential filters (mains itemes, Intangible assets, Cash Flow hedge reserve, IRB shortfall of credit risk adjustments to expected losses);
- Additional Tier 1;
- Tier 2 capital (T 2): Subsidiary loan capital, IRB Excess of provisions over expected losses eligible.

The minimum regulatory capital requirement is at 8% of total risk exposure amount.

National Bank of Hungary gave the permission to use 0% risk weight for capital requirement calculation for the exposures to the fully consolidated members of the Hungarian local banking Group.

Capital Management

Bank's risk Division has been responsible for Internal Capital Adequacy Assessment Process reporting since 1 January 2013, which also includes the comparison of Pillar 1 and Pillar 2 capital requirements on a quarterly basis, ICAAP is performed on local consolidated level.

The Bank calculates its planned capital requirements based on Basel II Pillar 1 and 2 methodology on local consolidated level once in a year as part of the yearly budgeting process. Should the figures of the financial budget change, capital plan is also modified if required.

Notes to the financial statements (CONTINUED)

The Group's regulatory Capital position at 31 December 2017 and 2016 was as follows:

(HUF million)

	2017	2016
Tier 1 Capital		
Ordinary share capital	24,118	24,118
Share premium	3,900	3,900
Retained earnings	180,312	153,982
P/L according to the balance sheet	25,005	53,265
Accumulated other comprehensive income	42,099	30,889
Other reserves	38,708	33,771
Adjustments to CET1 due to prudential filters	(19,412)	(18,066)
Goodwill included in the valuation of significant investments	0	(22)
Intangible assets	(6,806)	(3,799)
Deferred tax liabilities associated to intangible assets	0	24
IRB shortfall of credit risk adjustments to expected losses	(1,927)	(1,985)
Excess of deduction from AT1 items over AT1 Capital	0	–
Other transitional adjustments to CET1 Capital	0	–
Tier 1 Total	285,997	276,077
Tier 2 Capital		
Qualifying subordinated liabilities	0	4,235
Reserves for IRB position	3,679	3,541
Other transitional adjustments to T2 Capital	0	–
Tier 2 Total	3,679	7,776
Guarantee capital	289,676	283,853
RWA	1,223,927	1,291,080
Credit risk	1,049,575	1,078,939
Total risk exposure amount for position, foreign exchange and commodities risks	39,394	63,045
Operational risk	125,428	140,617
Total risk exposure amount for credit valuation adjustment	9,530	8,479
Capital adequacy (%)	23.67	21.99
Guarantee capital for legal limits	289,676	283,853

Supervisory Board and Management Board

UniCredit Bank Hungary Zrt.

SUPERVISORY BOARD

DR. ERICH HAMPEL

Chairman

SILVANO SILVESTRI

Members

TATJANA ANTOLIC JASNIC

ANDREA DIAMANTI

IVAN VLAHO

DR. PETTKŐ-SZANDTNER JUDIT

BOLYÁN RÓBERT

BERKI ANDRÁS RÓBERT

BOARD OF DIRECTORS

DR. PATAI MIHÁLY

Chairman and Chief Executive Officer

Members

MARCO INNACCONE

Deputy CEO

ALEKSANDRA CVETKOVIC

Head of Retail Division

TÓTH BALÁZS

**Head of Corporate, Investment Banking and
Private Banking Division**

ALEN DOBRIC

Head of Risk Division

LJILJANA BERIC

Head of Financial Division

MÁTYÁS SÁNDOR

Head of Global Banking Services

Supervisory Board and Management Board (CONTINUED)

UniCredit Jelzálogbank Zrt.

BOARD OF DIRECTORS

FARKAS BÁLINT MÁRTON	Chairman
KECSKÉSNÉ PAVLICS BABETT MÁRIA AGNIESZKA FRANECZEK	Members

SUPERVISORY BOARD

MARCO IANNACCONE	Chairman
LJILJANA BERIC ALEKSANDRA CVETKOVIC ALEN DOBRIC TÓTH BALÁZS	Members

Maximise commercial bank value.



We continue to maximise commercial bank value, with the ongoing transformation resulting in higher productivity. Our activities in Western Europe are benefitting from the revamped network with new service models for retail and SME customers as well as a strong multichannel strategy. We have further strengthened our leadership positions in CEE and CIB, while keeping a strong focus on risk.

Calendar

January 2017

The European Investment Fund and UniCredit Bank Hungary Zrt. signed an InnovFin SME guarantee agreement to improve the access of innovative small and medium-sized enterprises and small mid-caps to finance in eight countries.

January 2017

The leading international financial magazine Euromoney named UniCredit as “Best Trade Finance Service Provider” in Central and Eastern Europe as well as Western Europe. Euromoney also awarded the best trade finance services provider title to UniCredit Bank Hungary Zrt.

February 2017

UniCredit Bank Hungary Zrt. financed the procurement of 10 different instruments highly valuable in child healthcare, for 7 paediatric wards in 6 hospitals across the country and for a child ambulance unit operating in the Northern Great Hungarian Plain. The instruments purchased with the donation will allow the comprehensive diagnosis and effective treatment of nearly 10,000 children per year.

March 2017

UniCredit Bank donated furniture and computers to Real Pearl Foundation that supports children and families living in difficult circumstances. The furniture will be used in communal spaces in the village of Told in Hajdú-Bihar County. The donations were delivered by the market leader transport company Waberer's International Zrt., the business partner of the Bank.

March 2017

UniCredit took part, for the 10th time, in the global WWF initiative Earth Hour that aims to raise awareness of the perils of climate change. In 2017, the lights went out for one hour in the main UniCredit buildings in 12 countries, including Hungary.

April 2017

UniCredit Bank Hungary Zrt. launched its general-purpose Stable Interest Loan with interest rates fixed for 10, 15 or 20 years that is a novelty on the market. It also introduced the Exclusive Bronze account package, a new product for its small business clients.

April 2017

In Szeged we welcomed clients to our renovated and redecorated branch office. At the opening ceremony, donations in the amount of HUF 500,000 each were given to two local foundations: the Arrived Earlier Foundation helping premature babies, and the Music for Children with Cancer Foundation.

June 2017

By courtesy of UniCredit Bank Hungary Zrt., the Perinatal and Intensive Care Centre of Semmelweis University's 2nd Department of Obstetrics and Gynaecology received an infant incubator. Worth HUF 2.2 million, the equipment helps parents to be involved in the care of the new-borns as early as possible.

Calendar (CONTINUED)

July 2017

At the gala event for “Awards for Excellence” in 2017, Euromoney recognized UniCredit Group’s performance in five categories of excellence, including “Best Bank in Italy”, “Best Bank in Croatia”, “Best Bank for Wealth in Central & Eastern Europe” and “Best Bank for Transaction Services in Central & Eastern Europe”. It also awarded the distinguished title “Banker of the Year 2017” to the Bank’s Chief Executive Officer Jean Pierre Mustier.

August 2017

UniCredit Bank Hungary Zrt. introduced its “Change of Rhythm” investment loan that is available in an accelerated procedure and even without collateral, for small business clients intending to expand their equipment or machinery pool in order to improve their competitiveness.

September 2017

Consumer-friendly housing loans with a 3-year or 5-year interest rate period and fixed interest rates during the entire term of 10 and 15 years were launched by UniCredit Hungary Zrt. on 20th September after the National Bank of Hungary approved the Bank’s proposal.

September 2017

Euromoney ranked UniCredit Group number one in 11 countries in its cash management survey in 2017. These 11 first places represent significant progress as UniCredit achieved 5 first places in 2016. In Hungary, UniCredit Bank Hungary Zrt. earned the title “Best Cash Management Service provider”.

October 2017

UniCredit Bank Hungary Zrt. launched its new patronage programme “Leave Your Mark”. This programme highlights excellent performance and invites the Bank’s clients and the public at large to use an independent online platform and support these talented young people who stand out in various areas of life. This patronage and excellence mission is represented by ambassadors, who are famous Hungarians with outstanding achievements in their own fields.

November 2017

Held for the 12th time in 2017, the Mastercard – Bank of the Year competition was a prestigious review of the Hungarian banking industry, where Dr. Mihály Patai, Chairman-CEO of UniCredit Bank Hungary Zrt. won the title “Banker of the Year”. This is an award granted by the banking profession to recognize outstanding performance in the sector: the category winner is selected by the executives of the banks from among themselves.

November 2017

At the Global Finance Award 2017, UniCredit Bank Hungary Zrt. earned the title “Best Private Bank in Hungary in 2017”.

November 2017

UniCredit Bank Hungary Zrt. and UniCredit Foundation published their call for proposals directed to social non-profit organizations for the third time. In the “Take a step with us!” social innovation programme, the Bank provides an award of EUR 60,000 plus one-off professional support to the 10 best applicants and a year-long personalized business skill development programme for the 3 winning organizations.

November 2017

At the Website of the Year competition organized by the Hungarian Marketing Association, the Leave Your Mark patronage programme microsite of UniCredit Bank Hungary Zrt. won the award for Creative Solution of the Year as well as the overall Website of the Year 2017 award.

December 2017

In accordance with its “One Bank, One UniCredit” approach, UniCredit Bank Hungary Zrt. introduced its new slogan: “Banking that matters”. Since the announcement, the slogan has been used by the Group in its communications, in advertising campaigns, brand communication and marketing materials in all countries.

December 2017

The branch office of UniCredit Bank Hungary Zrt. in Győr was refurbished. At the opening ceremony, the Bank donated HUF 1 million to the Foundation for Intensive Child Healthcare Therapy.

Network units

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On 31 December 2017 UniCredit Bank's network consisted of 54 units throughout Hungary, from which 21 branches were located in Budapest, while 33 in the country.

Network units (CONTINUED)

Branches in Budapest

Bécsi úti fiók

1023 Budapest, Bécsi út 3-5.

Mammut II. fiók

1024 Budapest, Margit krt. 87-89. (Mammut II.)

Pesthidegkúti fiók

1028 Budapest, Hidegkúti út 167. (Széphalom Üzletközpont)

Lajos utcai fiók

1036 Budapest, Lajos u. 48-66.

Ferenciek tere fiók

1053 Budapest, Ferenciek tere 2.

Alkotmány utcai fiók

1054 Budapest, Alkotmány u. 4.

Szabadság téri fiók

1054 Budapest, Szabadság tér 5-6. (UniCredit Bank székház)

Nagymező utcai fiók

1065 Budapest, Nagymező u. 44.

Oktogon fiók

1067 Budapest, Teréz krt. 21.

Boráros téri fiók

1095 Budapest, Boráros tér 7.

Lurdy Ház fiók

1097 Budapest, Könyves Kálmán krt. 12-14. (Lurdy Ház)

Lágymányosi úti fiók

1111 Budapest, Lágymányosi u. 1-3.

Fehérvári úti fiók

1117 Budapest, Fehérvári út 23.

Alkotás úti fiók

1123 Budapest, Alkotás u. 50.

Duna Plaza Fiók

1138 Budapest, Váci út 178. (Duna Plaza)

Örs vezér téri fiók

1148 Budapest, Örs vezér tere 24. (Sugár Üzletközpont)

Mátyásföldi fiók

1165 Budapest, Veres Péter út 105-107.

Pestszentlőrinci fiók

1182 Budapest, Üllői út 455.

Europark fiók

1191 Budapest, Üllői út 201. (Europark)

KÖKI Terminál fiók

1191 Budapest, Vak Bottyán út 75 a-c

Campona fiók

1222 Budapest, Nagytétényi út 37-43. (Campona)

Network units (CONTINUED)

Branches in the country

Békéscsabai fiók

5600 Békéscsaba, Andrásy út 37-43. (Csaba Center)

Budakeszi fiók

2092 Budakeszi, Fő út 139.

Budaörsi fiók

2040 Budaörs, Szabadság út 49.

Ceglédi fiók

2700 Cegléd, Kossuth tér 4.

Debreceni fiók

4024 Debrecen, Kossuth Lajos u. 25-27.

Dunakeszi fiók

2120 Dunakeszi, Fő út 70.

Dunaújvárosi fiók

2400 Dunaújváros, Dózsa György út 4/D

Egri fiók

3300 Eger, Törvényház u. 4.

Érdi fiók

2030 Érd, Budai út 13. (Stop.Shop)

Esztergomi fiók

2500 Esztergom, Kossuth Lajos u. 14.

Gödöllői fiók

2100 Gödöllő, Dózsa György út 13.

Gyöngyösi fiók

3200 Gyöngyös, Péter Kis Szaléz u. 22.

Győri fiók

9021 Győr, Árpád út 45.

Kaposvári fiók

7400 Kaposvár, Dózsa György u. 1.

Kecskeméti fiók

6000 Kecskemét, Kisfaludy u. 8.

Miskolci fiók

3530 Miskolc, Hunyadi u. 3.

Mosonmagyaróvári fiók

9200 Mosonmagyaróvár, Fő u. 6.

Nagykanizsai fiók

8800 Nagykanizsa, Fő út 8.

Nyíregyházi fiók

4400 Nyíregyháza, Dózsa György út 1-3.

Pécs – Árkád Üzletház fiók

7621 Pécs, Rákóczi út 58. (Árkád Üzletház)

Salgótarjáni fiók

3100 Salgótarján, Rákóczi út 13.

Siófok

8600 Siófok, Fő u. 174-176.

Soproni fiók

9400 Sopron, Várkerület 1-3.

Szegedi fiók

6722 Szeged, Kossuth Lajos sugárút 18-20.

Székesfehérvári fiók

8000 Székesfehérvár, Budai út 1.

Szekszárdi fiók

7100 Szekszárd, Arany János u. 15-17.

Szentendrei fiók

2000 Szentendre, Dobogókői út 1. (Városkapu Üzletház)

Szigetszentmiklósi fiók

2310 Szigetszentmiklós, Bajcsy-Zsilinszky u. 26.

Szolnoki fiók

5000 Szolnok, Baross Gábor út 27.

Szombathelyi fiók

9700 Szombathely, Kőszegi út 30-32.

Tatabánya – Vértess Center fiók

2800 Tatabánya, Győri út 7-9. (Vértess Center)

Veszprémi fiók

8200 Veszprém, Ady E. u.1.

Zalaegerszegi fiók

8900 Zalaegerszeg, Kovács Károly tér 1/a

Adopt lean but steering center.



We have created a lean but steering center to drive Group-wide performance and ensure accountability. Through leaner support functions and transparent cost allocation, we focus on efficiency and simplification. We are positioned as best in class in terms of European corporate governance.

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