Takarék Mortgage Bank Plc.

Consolidated Financial Statements in accordance with the International Financial Reporting Standards adopted by the European Union and Independent Auditor's Report

December 31, 2019

Consolidated Financial Statements in Accordance with the International Financial Reporting Standards adopted by the European Union – 31 December 2019

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GENERAL INFORMATION

Chairman of the Board of Directors

József Vida

External Members of the Board of Directors

Gábor Gergő Soltész
Éva Hegedűs
Pál Sass

Internal Members of the Board of Directors

Dr. Gyula László Nagy
Attila Mészáros

Chief Executive Officers

Dr. Gyula László Nagy (Chief Executive Officer from 26/04/2017)
Attila Mészáros (Deputy Chief Executive Officer from 11/10/2018)

Large Shareholders Liaison Officer and Secretary

Illés Tóth

Small Shareholders Liaison Officer

info@takarek.hu

Auditor

Deloitte Ltd.

Personally responsible auditor

Gábor Molnár

Seat of the Bank, central office

Budapest.
Magyar Tudósok körútja 9. G. ép
1117

Deloitte.

Deloitte Advisory and Management Consulting
Private Limited Company
H-1068 Budapest,
Dózsa György út 84/C, Hungary
H 1438 Budapest,
P.O.Box 471, Hungary
Branch office: H-4029 Debrecen,
Csapó utca 40., Hungary

Phone: +36 (1) 428-6800
Fax: +36 (1) 428-6801
www.deloitte.hu

Registered by the Capital Court of Registration
Company Registration Number: 01-10-044100

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Takarék Mortgage Bank Plc.

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the Consolidated Financial Statements of Takarék Mortgage Bank Plc. and its subsidiaries (the „Group") for the year 2019 which comprise the Consolidated Statement of Financial Position as at December 31, 2019 – which shows a total assets of MHUF 342,897 –, and the related Consolidated Statement of Profit or Loss, Consolidated Statement of Other Comprehensive Income – which shows a Profit for the year of MHUF 22,306 –, Consolidated Statement of Changes in Equity and Consolidated Statement of Cash Flows for the year then ended and notes to the Consolidated Financial Statements including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at December 31, 2019 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union (the „EU IFRS"), and the consolidated financial statements were prepared in all material respects in accordance with the provisions of the effective Hungarian Act C of 2000 on Accounting (the „Accounting Act") relevant to the entities preparing consolidated financial statements in accordance with EU IFRS.

Basis for Opinion

We conducted our audit in accordance with the Hungarian National Standards on Auditing and the effective Hungarian laws and other regulations on audits. Our responsibilities under these standards are further described in the "*The Auditor's Responsibilities for the Audit of the Consolidated Financial Statements*" section of our report.

We are independent of the Group in compliance with the relevant effective Hungarian regulations and the "Rules of conduct (ethical rules) of the auditor profession and the disciplinary process" of the Chamber of Hungarian Auditors and, in respect of matters not regulated therein, the "Code of Ethics for Professional Accountants" (the IESBA Code) issued by the International Ethics Standards Board for Accountants, and we have fulfilled our other ethical responsibilities in accordance with the same ethical requirements.

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

Key Audit Matters

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

Key Audit Matter	**How our audit addressed the matter**
Calculation of expected credit losses on loans assessed on portfolio-level	
(See Sections 20 of Notes to the Consolidated Financial Statements for the details) As at December 31, 2019 the Group shows net value of loans to customers at amortised cost in an amount of MHUF 57,828 (gross amount MHUF 58,816) in connection with MHUF 988 provision has been recognized. The calculation of expected credit losses of loans assessed on portfolio-level requires application of professional judgement and use of highly subjective assumptions by management. The most significant assumptions applied in provisioning calculation are the followings: - IFRS9 credit risk staging methodology and application - probability of default - loss given default - estimation of future cash-flows expected to be realized. Based on the significance of the above described circumstances the calculation of expected credit loss of loans assessed on portfolio-level was identified as a key audit matter.	The relevant audit procedures performed by us included the followings: - testing design and operative effectiveness of key controls relating to monitoring of loans and calculating and recording of impairment, - test of staging through portfolio level analysis and the staging methodology applied by the model, - robust challenge of management estimates related to the provisioning, - assess the collective model methodology and testing the calculations in terms of risk parameters (probability of default - PD, loss given default - LGD, expected credit loss - ECL, macroeconomic factors) applied by the collective models by involving of experts, recalculation of impairment, - comprehensive analysis of loan portfolio.

Other Information

Other information comprises the information included in the Responsible Corporate Governance Report and the consolidated business report of the Group for 2019, but does not include the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information and for the preparation of the consolidated business report in accordance with the relevant provisions of the Accounting Act and other regulations. Our opinion on the consolidated financial statements provided in the section of our independent auditor's report entitled *"Opinion"* does not apply to the other information.

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

Furthermore, in accordance with the Accounting Act, our responsibilities regarding the consolidated business report also include reviewing the consolidated business report to assess whether the consolidated business report was prepared in accordance with the relevant provisions of the Accounting Act and other regulations, if any, including the assessment whether the consolidated business report complies with the requirements of Section 95/B. (2) e) and f) of the Accounting Act, and to express an opinion on the above and on whether the consolidated business report is consistent with the consolidated financial statements. Furthermore, in accordance with the Accounting Act we shall make a statement whether the information referred to in Section 95/B. (2) a)-d), g) and h) has been provided in the consolidated business report.

In our opinion, the consolidated business report of the Group for 2019 corresponds to the consolidated financial statements of the Group for 2019 and the relevant provisions of the Accounting Act in all material respects. The information referred to in Section 95/B. (2) a)-d), g) and h) of the Accounting Act has been provided.

As the Group is not subject to additional requirements under any other regulation in connection with the consolidated business report, we have not formulated an opinion on this matter.

In addition to the above, based on the information obtained about the Group and its environment, we must report on whether we became aware of any material misstatements in the other information and, if so, on the nature of such material misstatements. We have nothing to report in this regard.

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

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

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

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

The auditor's responsibilities for the audit of the consolidated financial statements

Our objectives during the audit are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue, on the basis of the above, an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Hungarian National Standards on Auditing and the effective Hungarian laws and other regulations on audits will always detect a material misstatement when it exists. Misstatements can arise from fraud or error, and they are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with the Hungarian National Standards on Auditing and the effective Hungarian laws and other regulations on audits, we exercise professional judgment and maintain professional scepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in the auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify the opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

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

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

Report on Other Legal and Regulatory Requirements

In compliance with Article 10 (2) of Regulation (EU) No. 537/2014 of the European Parliament and the Council, we provide the following information in our independent auditor's report, which is required in addition to the requirements of International Standards on Auditing:

Appointment of the Auditor and the Period of Engagement
We were appointed as the auditors of Takarék Mortgage Bank Plc. by the General Meeting of Shareholders on April 25, 2019 and our uninterrupted engagement has lasted for 8 years.

Consistence with the Additional Report to the Audit Committee
We confirm that our audit opinion on the consolidated financial statements expressed herein is consistent with the additional report to the Audit Committee of Takarék Mortgage Bank Plc., which we issued on March 31, 2020 in accordance with Article 11 of Regulation (EU) No. 537/2014 of the European Parliament and the Council.

Provision of Non-audit Services
We declare that no prohibited non-audit services referred to in Article 5 (1) of Regulation (EU) No. 537/2014 of the European Parliament and the Council were provided by us to the Group. In addition, there are no other non-audit services which were provided by us to Takarék Mortgage Bank Plc. and its controlled undertakings and which have not been disclosed in the consolidated business report.

The engagement partner on the audit resulting in this independent auditor's report is the signatory of the report.

Budapest, March 31, 2020

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Gábor Molnár
on behalf of Deloitte Auditing and Consulting Ltd.
and as a statutory registered auditor

Deloitte Auditing and Consulting Ltd.
1068 Budapest, Dózsa György út 84/C.
Registration number: 000083

Registration number of statutory registered auditor: 007239

Consolidated Statement of Profit or Loss for the year ended 31 December 2019

	Notes	2019*	2018*
Interest income	4	8,899	9,693
Interest expense	4	(7,613)	(7,900)
Net interest income		**1,286**	**1,793**
Fee and commission income	5	1,813	383
Fee and commission expense	5	(389)	(502)
Net fee and commission income		**1,424**	**(119)**
Profit from foreign exchange transactions		71	5
Change in fair value of financial instruments	35	58	2,045
Gains from securities		733	1,566
Net result from investment services		-	-
Net trading result		**862**	**3,616**
Other operating income	6	841	1,821
Other operating expense	7	(902)	(692)
Operating income, net		**3,511**	**6,419**
Provision for impairment losses	20	155	1,736
General and administrative expenses	8	(2,658)	(3,449)
Profit before tax		**1,008**	**4,706**
Income tax expense	11	(219)	(82)
Profit from discontinued operations	17	21,517	1,964
Profit for the year		**22,306**	**6,588**
Attributable to: profit of shareholders of the Bank from continuing operations		789	4,935
Attributable to: non-controlling interests		-	(311)
Earnings per share (HUF 100 face value)	31		
Basic earnings per share (HUF)		**5.30**	**43.27**
Diluted earnings per share (HUF)		**5.30**	**43.27**

*The data in the table until the Profit from discontinued operations line are the individual data of Takarék Mortgage Bank consolidated with Takarék Commercial Bank.

All figures in tables are in HUF million except otherwise noted

Consolidated Statement of Other Comprehensive Income for the year ended 31 December 2019

	Notes	2019	2018
Profit for the year		22,306	6,588
Other comprehensive income			
Items that may be reclassified to profit or loss:			
Change in Cash-flow hedge reserve		(31)	25
Change in fair value of securities at fair value through other comprehensive income		66	(368)
Foreign currency translation reserve		-	-
Deferred tax effect for other comprehensive income		(3)	31
Other comprehensive (loss)/profit for the period net of taxes	12	32	(312)
Total comprehensive income for the year, net of income taxes		**22,338**	**6,276**
Attributable to: profit of shareholders of the Bank from continuing operations		821	5,105
Attributable to: non-controlling interests		-	(311)

All figures in tables are in HUF million except otherwise noted

Consolidated Statement of Financial Position as at 31 December 2019

	Notes	31 December 2019*	31 December 2018**
Assets			
Cash on hand		-	3,157
Balances with the National Bank of Hungary	14	915	2,073
Due from banks	15	17,566	61,664
Securities at fair value through other comprehensive income	16	43,734	192,142
Derivative financial assets	35	2,851	3,962
Securities at amortised cost	18	999	-
Refinanced mortgage loans	19	217,205	105,296
Loans and advances to customers at amortised cost and at fair value	20	57,8288	372,594
Tangible assets	21,23	157	2,171
Intangible assets	22	241	388
Deferred tax asset	11	0	679
Other assets	24	1,401	10,390
Total assets		**342,897**	**754,516**

*The data as of December 31, 2019 are the individual data of Takarék Mortgage Bank
***Data as of December 31, 2018 are Takarék Mortgage Bank Consolidated Data (includes Takarék Commercial Bank Consolidated Data)*

All figures in tables are in HUF million except otherwise noted

Consolidated Statement of Financial Position as at 31 December 2019

	Notes	31 December 2019*	31 December 2018**
Liabilities			
Due to banks	25	3,119	156,659
Deposits from customers	28	-	304,333
Derivative financial liabilities	35	423	2,371
Issued securities	26	265,929	214,389
Financial liabilities at fair value through profit or loss, except for derivatives	27	6,552	6,693
Lease liability	23	70	-
Deferred tax liabilities	11	93	-
Provisions	29	509	3,988
Other liabilities	30	1,159	10,847
Total liabilities		**277,854**	**699,280**
Shareholders' equity			
Share capital	31	10,849	10,849
Treasury shares	31	(207)	(207)
Retained earnings		24,556	2,479
Other reserve	31	29,845	29,598
Non-controlling interest	31	-	12,517
Total shareholders' equity		**65,043**	**55,236**
Total liabilities and shareholders' equity		**342,897**	**754,516**

*The data as of December 31, 2019 are the individual data of Takarék Mortgage Bank
***Data as of December 31, 2018 are Takarék Mortgage Bank Consolidated Data (includes Takarék Commercial Bank Consolidated Data)*

Budapest, 31 March 2020

Dr. Gyula László Nagy
CEO

Takarék Jelzálogbank Nyrt. 1117 Budapest, Magyar Tudósok körútja 9. G. ép. TAKARÉK JELZÁLOGBANK

Attila Mészáros
Deputy CEO

All figures in tables are in HUF million except otherwise noted

Consolidated Statement of Cash Flows for the year ended 31 December 2019

	Notes	2019	2018
Cash flow from operating activities			
Profit for the year from continuing operation		790	4,622
Profit for the year from discontinued operation		21,517	1,964
Non-cash adjustments to net profit/(loss) from:			
Depreciation and amortization from continuing operation	21,22	159	288
Depreciation and amortization from discontinued operation	21,22	114	-
Impairment of tangible assets	21,22	104	656
Release of provision for losses (contains the impact of implementation of IFRS 9 in 2018)		(2,111)	(5,923)
Release of other provision		(65)	(1,686)
Loss on tangible assets derecognized		16	119
Gain/ (loss) on intangible assets derecognized		-	284
Capitalized interest on loans and advanced to customers at amortised cost and fair value		137	567
Fair value adjustment of derivatives	35	(337)	(2,236)
Fair value adjustment on financial liabilities at fair value through profit or loss, other than derivatives		51	186
Operating loss before change in operating assets		**(1,142)**	**(1,160)**
Decrease/(Increase) in operating assets:			
Securities at amortised cost		999	-
Securities at fair value through profit or loss		-	46,651
Securities at fair value through other comprehensive income		(4,370)	(112,281)
Refinanced mortgage loans		(47,842)	(28,699)
Loans and advances to customers at amortised cost and at fair value		17,522	(58,553)
Other assets		(45 619)	(4,052)
Increase/(Decrease) in operating liabilities:			
Deposits from customers		-	(24,920)
Due to banks		(19,805)	(124,246)
Other liabilities		(391)	5,131
Net cash flow from operating activities		**(102,647)**	**(302,129)**

All figures in tables are in HUF million except otherwise noted

Consolidated Statement of Cash Flows for the year ended 31 December 2019 - continued

	Notes	2019	2018
Cash flow from investing activities			
Proceeds from sales of tangible assets		-	272
Purchase of tangible and intangible assets		2	(202)
Net cash outflow from investing activities		**2**	**70**
Cash flow from financing activities			
Proceed from issued securities		60,854	157,570
Principal repayment on issued securities		(21,577)	(120,636)
Repayment of long term loans		10,378	246,922
Repayment of leasing liabilities		(42)	-
Net cash outflow from financing activity		**49,614**	**283,856**
Decrease in cash and cash equivalents		(53,031)	(18,203)
Net effect of the sale of subsidiaries and joint venture	17	4,618	-
Opening balance of cash and cash equivalents		66,894	85,097
Closing balance of cash and cash equivalents		**18,481**	**66,894**
Breakdown of cash and cash equivalents:			
Cash on hand		-	3,157
Balances with the National Bank of Hungary		915	2,073
Due from banks with a maturity of less than 90 days		17,566	61,664
Closing balance of cash and cash equivalents		**18,481**	**66,894**
Supplementary data			
Interest received		*11,087*	*23,557*
Interest paid		*(8,385)*	*(8,462)*

All figures in tables are in HUF million except otherwise noted

Consolidated Statement of Changes in Equity for the year ended 31 December 2019

	Notes	Share capital	Treasury shares	Share premium	General reserve	Cash flow hedge reserve	Change in fair value of securities at fair value through other comprehensive income	Retained earnings	Non-controlling interest	Share-holder's equity
1 January 2018		**10,849**	**(207)**	**27,926**	**460**	**5**	**1,267**	**(2,796)**	**12,828**	**50,332**
IFRS 9 adjustment		-	-	-	-	-	-	(1,370)	-	(1,370)
Profit for the year		-	-	-	-	-	-	6,897	(311)	6,586
Other comprehensive income	12	-	-	-	-	23	(335)	-	-	(312)
Transfer to general reserve		-	-	-	252	-	-	(252)	-	-
1 January 2019		**10,849**	**(207)**	**27,926**	**712**	**28**	**932**	**2,479**	**12,517**	**55,236**
IFRS16 adjustment	41	-	-	-	-	-	-	(14)	-	(14)
1 January 2019 - Opening		**10,849**	**(207)**	**27,926**	**712**	**28**	**932**	**2,465**	**12,517**	**55,222**
Profit from the year from continuing operations		-	-	-	-	-	-	789	-	789
Profit for the year from discontinued operations		-	-	-	-	-	-	21,517	-	21,517
Other comprehensive income	12	-	-	-	-	(28)	60	-	-	32
Change in non-controlling		-	-	-	-	-	-	-	(12,517)	(12,517)
Transfer to general reserve		-	-	-	215	-	-	(215)	-	-
31 December 2019		**10,849**	**(207)**	**27,926**	**927**	**-**	**992**	**24,556**	**-**	**65,043**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

1 DESCRIPTION OF THE BANK

Takarék Mortgage Bank Public Limited Company (formerly FHB Mortgage Bank Plc., hereinafter "the Bank") was established on 21 October 1997 as a limited liability company with a share capital of HUF 3 billion.
The Bank provided mortgage-banking services through its Head Office and regional representative offices located within the Republic of Hungary. The Bank also refinances mortgage loans provided by commercial banks to their customers.

The Bank received its license on 6 March 1998 to operate as a specialized financial institution in accordance with the provisions of Act CXII of 1996 on Credit Institutions and Financial Enterprises and Act XXX of 1997 on Mortgage Loan Companies and on Mortgage Bonds. The Bank commenced operations as of 16 March 1998.

On 31 October 2003 the Hungarian Financial Supervisory Authority (HFSA) granted permission for Takarék Mortgage Bank to issue a prospectus to introduce its shares to the Budapest Stock Exchange. The ordinary shares were listed on the Budapest Stock Exchange on 24 November 2003.

The Bank introduced its New Strategic Plan in February 2006 to expand its banking activity and branch network. The Bank set up new subsidiaries, among them the Takarék Commercial Bank Ltd., thereby significantly expanding the range of services provided by the Group. At that time Takarék Mortgage Bank Plc. is the parent company of the group. (The Bank and its subsidiaries are jointly referred to as the Group, Bank Group.)

The strategic partnership program with Allianz was adopted by the Board of Directors of Takarék Mortgage Bank, the plan included the acquisition of the Allianz Bank, which merged into the Takarék Commercial Bank Ltd in 2011. This strategic partnership was terminated in 2018. The Board of Directors also approved "The bank of the families" concept, meaning a customer- and service-driven sales attitude.

In 2013, Takarék Mortgage Bank managed several acquisitions, there through broadened the Banking Group and the range of activities. It included the acquisition of Diófa Alapkezelő Zrt. (Diófa Fund Management Ltd.), the purchase of the Díjbeszedő Operational and Service Limited Liability Company, hereinafter the "DÜSZ"), that come into being after a demerge from Díjbeszedő Holding Ltd. (DBH), the Díjbeszedő Faktorház Co. Plc. ("DBF"), DíjNET Ltd., Díjbeszedő Informatikai Lld ("DBIT") and the portion of the ownership of the Magyar Posta (Hungarian Post).

Related to the transaction of the business shares, the Bank and the Magyar Posta (Hungarian Post) entered into a strategic cooperation, and in the scope of that they shall cooperate in the ownership and control of some of their jointly controlled companies, furthermore in course of the harmonization of their business activities.

Based on the Act CXXXV of 2013 on integration of cooperative financial institutions and modification of certain rules on economic issues (Szhitv), Takarék Mortgage Bank Plc. and under its qualifying holding and prudential supervisory Takarék Commercial Bank Ltd. became a member of Integration Organisation of Cooperative Credit Institution (SZHISZ) in September 2015, and also the member of the Guarantee Group of Cooperative Credit Institutions, and a member of the country's fourth largest banking group.

Notes to the Consolidated Financial Statements

Takarék Mortgage Bank Co. Plc. at the end of December 2015 increased its share capital with HUF 4,249 billion face value, or HUF 30.5 billion issue value. Capital increase was executed by issuing dematerialized dividend preference shares (Series "B") and registered, dematerialized ordinary shares (Series "C"). The new shares (Series "B" and Series "C") were not listed on the Budapest Stock Exchange, they were purchased by the members of the Integration.

As parent company of the Group, the Mortgage Bank exercised its rights over the Group companies until 2017, the rights were transferred to MTB Magyar Takarékszövetkezeti Bank Zrt. in 2017 according to the strategy of SZHISZ.

The satellite financial entities of the Group, including the fund management, the leasing and factoring services and the centralized debt collection were taken over in December 2017 by the MTB Magyar Takarékszövetkezeti Bank Zrt., the leader of the Integration. MTB Magyar Takarékszövetkezeti Bank Zrt. extended the provision of investment services also to the customers of the Group from 2017, supported by the Takarék Commercial Bank, as investment agent.

From the second quarter of 2018 the Takarék Mortgage Banks continues its operations purely as a refinancing mortgage bank, the Takarék Commercial Bank provides retail mortgage lending services to customers. However, the existing loan portfolio remains at Takarék Mortgage Bank until expiry.

On 30 November 2018, the General Meeting of MTB Magyar Takarékszövetkezeti Bank Zrt. adopted the Takarék Group's new business strategy for the period 2019-2023, which opens a new chapter in the one and a half century history of Savings Cooperatives. One of the most important elements of this is the foundation of a new, universal, commercial bank in which the savings cooperatives merge and the new bank will serve the customers of all savings. This new bank will be the national commercial bank of the Takarék Group.

In December 2017 the Bank sold the majority of their direct and indirect investments leaving Takarék Commercial Bank Ltd. amongst their shares unsold until the date 29 October 2019. Takarék Mortgage Bank Plc. sold 51 % investment in Takarék Commercial Bank to MTB Ltd. with that closing transaction. Takarék Commercial Bank is part of scope of consolidation of the parent company MTB Ltd.

The services previously provided by Mortgage Bank (full-fledged business administration services including accounting, taxation, HR, payroll accounting, statistics, statutory data provision and leasing activity), in 2019 are further provided by MTB to the Mortgage Bank and Takarék Commercial Bank Zrt., within the framework of service level agreement (SLA) contract. The Takarék Commercial Bank, as the agent of the Takarék Mortgage Bank Plc., were fully responsible for direct lending, furthermore performs loan aftercare and qualified loan management until the date 31 October 2019 then was merged into Takarékbank Ltd. Although, Takarék Commercial Bank, in order to have favourable funding costs, had part of their loans refinanced by the Takarék Mortgage Bank Plc.

The consolidated financial statements for the year ended 31 December 2019 were authorized for issue in accordance with a resolution of the Board of Directors on 31 March 2020. The final approval on the consolidated financial statements is provided by the General Meeting.

Notes to the Consolidated Financial Statements

2 ACCOUNTING POLICIES

2.1 Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for securities at fair value through other comprehensive income, derivative financial instruments, loans at fair value through profit or loss, financial liabilities at fair value through profit or loss, that are recorded at fair value

Statement of compliance
The consolidated financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

2.2 Change in accounting policies-

The effect of adopting new and revised International Financial Reporting Standards effective from 1 January 2019

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:

- **IFRS 16 "Leases"** – adopted by the EU on 31 October 2017 (effective for annual periods beginning on or after 1 January 2019),
- **Amendments to IFRS 9 "Financial Instruments"** - Prepayment Features with Negative Compensation – adopted by the EU on 22 March 2018 (effective for annual periods beginning on or after 1 January 2019),
- **IFRIC 23 "Uncertainty over Income Tax Treatments"** – adopted by the EU on 23 October 2018 (effective for annual periods beginning on or after 1 January 2019),
- **Amendments to IAS 28 "Investments in Associates and Joint Ventures"** - Long-term Interests in Associates and Joint Ventures – adopted by the EU on 8 February 2019 (effective for annual periods beginning on or after 1 January 2019),
- **Amendments to IAS 19 "Employee Benefits"** - Plan Amendment, Curtailment or Settlement – adopted by the EU on 13 March 2019 (effective for annual periods beginning on or after 1 January 2019),
- **Amendments to various standards due to "Improvements to IFRSs (cycle 2015 -2017)"** resulting from the annual improvement project of IFRS (IFRS 3, IFRS 11, IAS 12 and IAS 23) primarily with a view to removing inconsistencies and clarifying wording – adopted by the EU on 14 March 2019 (effective for annual periods beginning on or after 1 January 2019).

The adoption of these amendments to the existing standards has not led to any material changes in the Group's financial statements.

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

Notes to the Consolidated Financial Statements

- **Amendments to IAS 1 "Presentation of Financial Statements" and IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors"** - Definition of Material (effective for annual periods beginning on or after 1 January 2020),

- **Amendments to References to the Conceptual Framework in IFRS Standards** (effective for annual periods beginning on or after 1 January 2020).

The Group has elected not to adopt these new standards, amendments to existing standards and new interpretation in advance of their effective dates. The Group anticipates that the adoption of these standards, amendments to existing standards and new interpretations will have no material impact on the financial statements of the Group in the period of initial application.

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

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

- **IFRS 14 "Regulatory Deferral Accounts"** (effective for annual periods beginning on or after 1 January 2016) - the European Commission has decided not to launch the endorsement process of this interim standard and to wait for the final standard,

- **IFRS 17 "Insurance Contracts"** (effective for annual periods beginning on or after 1 January 2021),

- **Amendments to IFRS 3 "Business Combinations"** - Definition of a Business (effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2020 and to asset acquisitions that occur on or after the beginning of that period),

- **Amendments to IFRS 10 "Consolidated Financial Statements" and IAS 28 "Investments in Associates and Joint Ventures"** - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture and further amendments (effective date deferred indefinitely until the research project on the equity method has been concluded),

- **Amendments to IFRS 9 "Financial Instruments", IAS 39 "Financial Instruments: Recognition and Measurement" and IFRS 7 "Financial Instruments: Disclosures"** - Interest Rate Benchmark Reform (effective for annual periods beginning on or after 1 January 2020).

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

Hedge accounting for a portfolio of financial assets and liabilities whose principles have not been adopted by the EU remains unregulated.

Notes to the Consolidated Financial Statements

2.3 Currency of the consolidated financial statements

Unless otherwise stated, the consolidated financial statements are presented in million of Hungarian forint (HUF), the Hungarian forint is the functional and presentation currency used by Bank and its subsidiary with registered office in Hungary. The functional currency of the German branch of Takarék Commercial Bank Ltd. is the Euro (EUR).

2.4 Basis of Consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiary as at 31 December 2019.
Control is presumed to exist where the Bank holds, directly or indirectly, more than 50% of the registered capital or where the Bank can exercise more than 50% of the voting rights or where the Bank can appoint or dismiss the majority of the members of the Board of Directors.
Consolidation involves all of the subsidiaries as of the day of acquisition of control. Consolidation of the subsidiaries ceases when the Company loses control of the subsidiaries. Control achieved when the Bank has power over the investee, is exposed, or has rights, to variable returns from its involvement with investee, and has the ability to use its power to affect its return.

The list of the subsidiaries of the Bank as at 31 December 2018 is the following:

Companies included in the consolidation	Main shareholder**	Core business	Relation-ship *
Takarék Commercial Bank Ltd.	Takarék Mortgage Bank Plc. 51%	Universal banking services	S

** Relationship: "S"=subsidiary.*
*** % in the column = the ownership of the main shareholder*

The list of the subsidiaries of the Bank as at 31 December 2019 is the following:

Companies included in the consolidation	Main shareholder	Core business	Relation-ship
not any consolidated entity *			

**The investment in Takarék Commercial Bank Ltd. sold in 29 October 2019 to MTB. These consolidated financial statements include the profit from discontinued operations in separate line in Consolidates Statement of Profit or Loss in 2019 and 2018. The assets and liabilities do not include the Takarék Commercial Bank in the Consolidated Statement of Financial Position in 2019.*

Notes to the Consolidated Financial Statements

2.5 Rounding

When rounding to thousands, anything above the midpoint of HUF 500 is rounded up and anything below and including the midpoint is rounded down. When rounding to millions, anything above the midpoint of HUF 500,000 is rounded up and anything below and including the midpoint is rounded down.

2.6 Summary of significant accounting policies

2.6.1 Categories of financial instruments

The Bank groups the recognised financial assets as follows:

- **Cash and cash equivalents**
- **Financial assets held for trading**
  - Derivative financial assets
- **Non-trading financial assets mandatorily at fair value through profit or loss**
  - Loans and advances to customers at fair value
- **Financial assets at fair value through other comprehensive income**
  - Securities at fair value through other comprehensive income
- **Financial assets at amortised cost:**
  - Balances with the National Bank of Hungary
  - Due from banks
  - Refinanced mortgage loans
  - Loans and advances to customers at amortised cost

The Bank groups the recognised financial liabilities as follows:

- **Financial liabilities held for trading**
  - Derivative financial liabilities
- **Financial liabilities classified at fair value through profit or loss**
  - Financial liabilities at fair value through profit or loss, other than derivatives
- **Financial liabilities measured at amortised cost (other financial liabilities):**
  - Due to banks
  - Deposits from customers
  - Issued securities

2.6.2 Cash and cash equivalents

For the purpose of the Consolidated Statement of Cash Flows, cash and cash equivalents include cash at hand, receivables from the National Bank of Hungary, and receivables from banks with an original maturity of not more than 90 days.

2.6.3 Securities at fair value through other comprehensive income

Securities at fair value through other comprehensive income are held within a business model whose objective is achieved by both collecting of contractual cash flows and selling securities, and the contractual terms of these securities give rise on specified dates to cash flows that are solely payment of principal and interest on the principal amount outstanding. Investments in securities are accounted for on a settlement date basis and are initially measured at fair value. Securities at fair value through other comprehensive income are measured at subsequent reporting dates at fair value. Unrealized gains and losses (Fair value difference) on securities at fair value through other comprehensive income are recognized directly in other comprehensive income , interest and foreign exchange gains/losses on this items are recognized consolidated statement of profit or loss, unless such financial asset at fair value through other comprehensive income is part of an effective hedge. Such gains and losses will be reported when realized in consolidated statement of profit or loss for the applicable period.

2.6.4 Refinanced mortgage loans

The Bank has a substantial refinanced mortgage loans portfolio. As part of the refinancing arrangements, partner banks sell independent and separated liens (which are used as collateral for housing loans) to the Bank. The independent and separated liens are then sold back to the partner banks such way that the repurchase of the independent lien is scheduled to mirror the principal repayment schedule of the particular mortgage loan of the partner bank's customer. The instalment from the partner banks is due irrespective of whether or not the partner bank receives repayments from its customer.
The individual mortgage loans of the partner banks' customers that are refinanced are in conformity with the relevant statutory requirements (being that these loans are performing). The classification is made, impairment is reported and receivables from the clients is reported for these individual loans by the partner banks. Refinanced mortgage loans are classified as performing because by purchasing the independent and separated lien the Bank gives a long-term loan to the partner commercial bank and the client risk is entirely borne by the partner banks, the risk the Bank bear is the credit risk of the partner banks.
Refinanced mortgage loans are presented at amortized cost less impairment losses.

2.6.5 Loans and advances to customers at amortised cost

Loans provided directly to customers are reported as loans and advances to customers and are measured at amortized cost less any impairment losses. If there is objective evidence that an impairment loss has been incurred, the carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of profit or loss.
All loans and advances are recognized upon their disbursement.

2.6.6 Restructuring of loans

In cases of default the Bank favours renegotiating the loans to customers instead of foreclosure wherever possible. Renegotiated loans may be restructured by extending of the loan term and/or agreeing on new conditions. The Group doesn't measure any significant gain or losses on the restructuring loans.

The Bank management keeps track of renegotiated loans to ensure all terms and conditions are met and to secure future cash payments. Provision for impairment of restructured loans is set up on an individual as well as on a portfolio basis and with the application of the original effective interest rate of the loan.
In case of renegotiated loans the classification of the clients (and eventually the provision) may improve if the clients start to pay their instalments as scheduled. The new buffer account scheme and the converted HUF loans (under the State program) were dealt with the same process like other refinanced mortgage loans in spite of the originated loan has not got any payment problem.

When the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset, Bank shall recalculate the gross carrying amount of the financial asset and shall recognise a modification gain or loss in profit or loss. The gross carrying amount of the financial asset shall be recalculated as the present value of the renegotiated or modified contractual cash flows that are discounted at the financial asset's original effective interest rate.

When the contractual terms of a financial asset are modified and the modification does not result in derecognition, the Bank determines if the financial asset's credit risk has increased significantly since initial recognition. If the credit risk remains significantly higher than what was expected at initial recognition the loss allowance will continue to be measured at an amount equal to lifetime ECL. The loss allowance on restructured loans will generally only be measured based on 12-month ECL when there is evidence of the borrower's improved repayment behaviour following modification leading to a reversal of the previous significant increase in credit risk.

2.6.7 Impairment losses on loans

IFRS 9:
Impairment losses on loan and placement losses with other banks represent Management assessment for potential losses in relation to these activities.
Impairment losses on loans and placements with other banks is recognised by the Bank based on the expected credit loss model in accordance with IFRS 9. Based on the three stage model allowance for impairment is recognised at an amount equal to 12-month expected credit loss from the initial recognition, unless purchased or originated credit-impaired (POCI). On financial assets with significantly increased credit risk or credit impaired financial assets (based on objective evidences) provision for impairment is recognised in amount of lifetime expected credit loss.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant difficulty, the probability that they will enter bankruptcy or other financial reorganisation, default of delinquency in interest or principal payments and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Impairment on a particular loan or a group of similar loans is recognized if their book value is greater than the estimated recoverable amount. The recoverable amount is the present value of expected future cash flows, including amounts recoverable from guarantees and collaterals, discounted based on the loan's original effective interest rate. The impairment for significant loans is assessed individually. For those loans that are of insignificant in their individual amounts the Bank assesses impairment on a portfolio basis, taking into consideration the type and the classification of the loan, non-performance history and losses.
The Bank writes off loss on loans and advances when borrowers are unable to fulfil their obligations to the Bank and when relevant evidence has been obtained through the appropriate legal proceedings. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of profit or loss. The impairment of loans and advances are recognized as credit loss expenses. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a write-off is later recovered, the recovery is credited to the 'Credit loss expense'.
The Group applies individual evaluation for receivables from non-retail customers, reverse mortgage transactions.
In the course of individual evaluation the credit rating department and decisive management evaluate wholly all observable information during definition of rating classes and amount of impairment, mainly amount of receivables, default, foreclosures, debtor's payment discipline, attitude, etc.

The Group applies collective and statistical evaluation in cases of covered receivables from retail customers and overdraft receivables from retail customers.
The Group applies collective and simplified evaluation in cases of uncovered receivables except of overdraft receivables.

2.6.8 Leases

Determination of whether an agreement is a lease agreement or contains a lease transaction is based on its contents. The Bank analyses agreements to decide whether delivery under the agreement involves the use of a specific asset or assets and transfers the right to use such assets.

The Bank as lessee
In the context of operative lease schemes the lessor does not essentially transfer the Bank all risks and benefits associated with ownership. Lease payments pursuant to an operative lease transaction are recognized in the expense item on a straight-line basis throughout the terms of the lease. Contingent lease fees are recognised as expense when incurred.
Asset held under finance leases are initially recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the consolidated statement of financial position as a finance lease obligation.

The Bank as lessor
Leases where the Group transfers substantially all the risks and rewards incident to ownership of the asset to the lessee are classified as finance leases. The net investment in finance leases provided by the Group is included in loans and advances to customers. A receivable is recognized over the leasing period of an amount equalling the present value of the lease payment using the implicit rate of interest and including any guaranteed residual value. All income resulting from the receivable is included in interest income in the statement of profit or loss.

2.6.9 Acquisitions and goodwill

Business combinations are accounted for using the purchase method of accounting. This involves recognizing identifiable assets (including previously unrecognized assets) and liabilities (including contingent liabilities) of the acquired business at fair value. A negative difference is recognised directly in the earnings for the year of the acquisition. Goodwill is measured as the excess of the sum of the consideration transferred the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquire (if any) over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed.
Initially goodwill is measured at cost. Following initial recognition, the Bank runs an impairment test annually and measures goodwill at cost less any accumulated impairment.
An asset is identifiable if it is separable or arises from contractual or other legal rights, regardless of whether those rights are transferable or separable from the entity or from other rights and obligations.
If the subsidiaries acquired are later disposed of, the difference between the selling price and the net assets plus cumulated translation difference and goodwill is recognized in the statement of profit or loss.

2.6.10 Tangible and intangible assets

Tangible (fixed) and intangible assets are presented at cost, less accumulated depreciation, and less impairment if any. Depreciation is charged to the statement of profit or loss in the period to which it relates. Depreciation is computed using the straight-line method over the estimated useful lives of the assets considering residual value, as follows:

Real estate	2%
Leasehold improvement	6%
Equipment and furniture	9% - 33%
Software	10% - 33%
Rights representing assets	3.5% - 16.7%
Hardware	33% - 50%
Vehicles	20% - 33%
Other fixed assets	9% - 14.5%

Intangible assets have a definite useful life, excluding goodwill.

2.6.11 Impairment of non-financial assets

On the balance sheet date the Bank assesses if there is any indication of impairment. If there is, or in cases where an annual impairment test is required the Bank estimates the recoverable amount of the asset. Recoverable amount is the fair value of the asset net of the costs of sale, or the value in use, whichever is higher. Where the carrying amount of an asset exceeds its recoverable amount, the Bank recognises impairment on the asset, by this the carrying amount is written down to the recoverable amount. When determining value in use the estimated future cash flows are discounted to their present value considering current market assessment of the time value of money and the risks specific to the asset. The appropriate valuation method is applied for the determining fair value net of cost of sales. Several assessments are used to underpin these calculations such as listed share prices or other available fair value indicators.
Each asset is assessed annually, when any indication of a reversal or reduction of earlier impairment is performed. If there is such an indication the Bank estimates the recoverable value of the asset. Reversal of previously entered impairment is only done in cases where there has been a change in the estimates applied for determining the asset's recoverable value since the last reporting of impairment.
The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of profit or loss. Impairment losses relating to goodwill cannot be reversed in future periods.

2.6.12 Derivatives

A derivative transaction is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instrument, reference yield or index, it is settled in a future date and there is no or low initial investment.
Derivatives are recorded at fair value and carried as assets when their fair value is positive or as liabilities when their fair value is negative. Changes in the fair value of derivatives are included in 'Net trading result'. The resulting gain or loss is recognised immediately in 'Net trading result'.
Derivatives include forwards, futures, swaps and options.

2.6.13 Hedge transactions (according to IAS 39)

The Bank makes use of derivative instruments to manage exposures to interest rate, foreign currency and credit risk, including exposures arising from forecast transactions and firm commitments. In order to manage particular risks, the Bank applies hedge accounting for transactions which meet specified criteria.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Upon concluding the hedge contract the Bank drafts the hedge document that sets forth the relationship between the transaction and the instrument hedged. The document describes the nature of risk as well as the risk management goals and strategies. The document also sets forth the method of measuring hedge effectiveness.

Once the hedge is established as relationship, the Bank assesses whether the hedge transaction is expected to be effective in the long term in meeting the fair value attributable to the risk hedged or in offsetting cash flow changes. Hedges are reviewed by the responsible banking department on a quarterly basis. A hedge transaction is considered effective if, as a result, the fair value attributable to the risk hedged or the cash flow change offset by the hedge is within a range of 80-125% in the period to which the hedge refers.

For the purposes of hedge accounting, hedges are classified into two categories:

(a) Fair value hedges which hedge the exposure to changes in the fair value of a recognized asset or liability; and

(b) Cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognized asset or liability or a forecasted transaction.

There are no net investment hedges in foreign operations.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges and that prove to be highly effective in relation to the hedged risk, are recorded in the Consolidated Comprehensive Income Statement along with the corresponding change in fair value of the hedged asset or liability that is attributable to the specific hedged risk.

In relation to cash flow hedges, which meet the conditions for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognized initially in the other comprehensive income item. The gains or losses on effective cash flow hedges recognized initially in other comprehensive income are either transferred to the statement of profit or loss in the period in which the hedged transaction affects the statement in the profit or loss, or are included in the initial measurement of the cost of the non-financial related asset or liability. The ineffective portion is recognized in the statement of profit or loss.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. At that point in time, any cumulative gain or loss on the hedging instrument recognized in other comprehensive income remains in other comprehensive income until the forecasted transaction occurs. Where the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognized in other comprehensive income is transferred to the net profit/loss for the period.

For hedges, which do not qualify for hedge accounting (economic hedges), any gains or losses arising from changes in the fair value of the hedging instrument are taken directly to the statement of profit or loss for the period.

The following lines in the profit or loss statement contain the gains or losses in connection with the hedging instruments of hedges (swaps):

(a) Interest income or interest expense
(b) Gains or losses from foreign exchange transactions
(c) The remaining change from fair value adjustment in Change in fair value of derivatives

2.6.14 Current tax

Current taxes include the corporate income tax, local business tax and innovation contribution payable and refundable amounts and are measured at the amount expected to be recovered from or paid to the tax authorities. The rates applied are in accordance with the provisions of the Hungarian taxation law.

Notes to the Consolidated Financial Statements

2.6.15 Deferred taxes

Deferred tax is provided on temporary differences at the balance sheet date between the tax basis of assets and liabilities and their carrying amounts for financial reporting purposes. All deferred tax liabilities are recognized. Deferred tax assets are recognized only to the extent that it is probable that taxable profit will be available against which it can be utilized. Deferred tax assets and liabilities are measured at the enacted tax rates that are expected to apply in the year when the asset is realized or the liability is settled. Deferred tax assets and liabilities are offset if a legally enforceable right exists to set off current tax assets against current taxes liabilities and the deferred tax relate to the same company and the same tax authority.

2.6.16 Classification into financial liabilities or shareholders' equity

Financial liability is any liability that is:

- a contractual obligation:
    - to deliver cash or another financial asset to another entity; or
    - to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or
- a contract that will or may be settled in the entity's own equity instruments and is:
    - a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or
    - a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments.

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities.

2.6.17 Financial liabilities carried at amortized cost

The Bank has the following financial liabilities to finance its business: issued mortgage bonds, issued bonds, loans from the Hungarian state, interbank loans and customer deposits.

Financial liabilities, which are not designated at fair value through profit or loss, are classified as financial liabilities carried at amortized cost. At initial measurement, they are recognized at fair value. After initial measurement, they are carried at amortized cost using the effective interest rate. Amortized cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the effective interest rate.

2.6.18 Financial liabilities carried at fair value other than derivatives

On initial recognition the management designates the financial liabilities into financial liabilities classified at fair value through profit or loss category. Management may only designate an instrument at fair value through profit or loss upon initial recognition when the following criteria are met, and designation is determined on an instrument by instrument basis:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the liabilities or recognising gains or losses on them on a different basis;
- the liabilities are part of a group of financial liabilities, which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy;
- the financial instrument contains one or more embedded derivatives, which significantly modify the cash flows that otherwise would be required by the contract.

Such financial liabilities are issued mortgage bonds, bonds and interbank loans (that are economically closely related to the swaps, which are entered to mitigate risks). Financial liabilities at fair value through profit or loss are recorded in the statement of financial position at fair value. Changes in fair value are recorded in 'Change in fair value of derivatives'. Interest is earned or incurred is accrued in 'Interest income' or 'Interest expense', respectively, using the effective interest rate (EIR).

Included in this classification are mortgage bonds and bonds issued which are managed on a fair value basis, where the nominal value represents the contractually required payments. The change in fair value other than movement in portfolio or currency represents credit risk.

In case financial liabilities classified as measured at fair value through profit or loss because it eliminates or significantly reduces a measurement or recognition inconsistency (accounting mismatch) changes in fair value related to credit risk are recognised in consolidated statement of profit or loss.

2.6.19 Financial guarantee contracts

Financial guarantee contracts are those contracts that require a payment to be made to reimburse the holder for a loss incurred because the specified debtor fails to make a payment when it is due in accordance with terms of a debt instrument.
Financial guarantee contracts are initially recognised in the financial statements within 'Provisions' at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the amount recognised less cumulative amortisation, and the best estimate of expense required to settle any financial obligation arising as a result of the guarantee.
The financial guarantee fee received is recognised in the statement of profit or loss in 'Fee and commission income' on a straight line basis over the lifetime of the guarantee.
Any increase in the liability relating to financial guarantees is recorded in the statement of profit or loss in 'Credit loss expense'.

2.6.20 Derecognizing of financial instruments

A financial asset (or a part of a financial asset or a group of financial assets) is derecognized when

- the rights under contract related to the cash flows from the financial asset cease; or
- the rights under contract related to the cash flows from the financial asset are transferred; or an obligation is undertaken by virtue of a transfer agreement to pay the cash flows from the financial asset to third parties; and
- the Bank has transferred substantially all risks and rewards of the asset; or
- the Bank has not retained nor transferred substantially all risks and rewards associated with the asset but has transferred control of the asset.

If the Bank has not retained nor transferred substantially all risks and rewards associated with the asset but has retained control of the financial asset, it continues to recognize the transferred asset in proportion to its continuing involvement. The rate of continuing involvement in a transferred asset is the Bank's rate of exposure to the risks associated with changes in the value of the transferred asset.
When the Bank continues to report the transferred asset in proportion to its continuing involvement it also reports an associated liability.
A financial liability (or a part of a financial liability) is derecognized when it ceases, is executed or matured. Exchange or partial exchange of existing financial liabilities or a part thereof with significantly different terms and conditions or significant modification of its terms and conditions is also considered as cessation of the financial liability and is reported as a new financial liability, taking the relevant part of IFRS 9. The difference between the book value of, and the consideration paid for financial liabilities (or a part thereof) that ceased

or have been transferred to third parties is reported in the profit or loss. (see g) point about modification in contractual cash flow)

2.6.21 Repurchase and reverse repurchase transactions

The Bank purchases securities under agreements to resell at a specified future date, these securities are not recognised in the statement of financial position. The consideration paid, including accrued interest, is recorded in the statement of financial position, within ‘Due from banks’, reflecting the transaction’s economic substance as a loan by the Bank. The difference between the purchase and resale prices is recorded in ‘Net interest income’ and is accrued over the life of the agreement using the effective interest rate.
The Bank does not report securities provided to repo as a separate item in the balance sheet, only in the Notes.

2.6.22 Provisions

Provisions are recognized when the Bank has present obligation (legal or constructive) as a result of a past event and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Expense relating to lending provision is a part of provision for impairment losses on loan expense. On provision for contingent liabilities related to business combinations is recognized in other operating expense.

2.6.23 Short term employee benefits

Under the Bank’s policy, the employer must grant employees their paid leave in the period the leave is earned, except for the paid leave emerges during maternity leave. Deferment of the expected cost of leave is applicable to the Bank and its subsidiaries, but this cost is recognized only if it is material.

2.6.24 Long term employee benefit plans- pensions

In the normal course of business the Bank pays fixed contributions into the Hungarian State and private pension funds on its employees, which is recognized in social security contributions (mandatory contribution) and other personnel expenses (voluntary contribution) and which cannot be considered as employee benefit plan. The Bank itself does not offer a pension scheme or post-retirement benefit plan, and consequently has no legal or contractual obligation to make further contributions.

2.6.25 Repurchased treasury shares

Treasury shares represent the cost of shares of the Bank repurchased and are displayed as a reduction of shareholders’ equity. Treasury shares are accounted for at weighted average cost. Premiums and discounts on repurchase and subsequent disposal are credited and debited directly to retained earnings, no gain or loss is recognized in the statement of profit or loss.

2.6.26 Share-based payment

The Bank has developed a share option scheme to remunerate its Directors, executives and specific managers for their services. The scheme involves transfer of treasury shares at a discount.
The Bank reports share option benefits extended in shares at the fair value on the day the benefit was approved by the Annual General Meeting (AGM), calculated by means of the methodology described in Note 32, in accordance with IFRS 2, Share-base Payment. The fair value of shares involved in the share option scheme but not yet delivered is recognized as expense (other personnel costs) as a separate line item against share option reserve under shareholders’ equity for the period the benefit is earned.

Notes to the Consolidated Financial Statements

The cumulative expense on share option is based on the period earned until the balance sheet date and the Bank's estimate regarding the number of shares earned. In the case of treasury shares provided with market terms the Bank recognizes proceeds received from a party who meets all other requirements of earning irrespective of whether the market requirement is met or not.

2.6.27 Income and expense

Interest income and interest expense (the interest subsidy received from the Hungarian State or from the client) are recognized time-proportionately using the effective interest rate method. Interest income and interest expense include the amortization of discount or premium on securities.

The effective interest rate is the rate which exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Fees directly related to loans are reported in the calculation of effective interest rate. Fees referring only to a particular period are accrued. Fees attached to particular deliveries are considered as a lump sum once the criteria are met.

2.6.28 Interest subsidy

State interest subsidy

Interest subsidy is available to clients who have been granted loans in accordance with the specific provisions of the Hungarian legislation (Government Decree 12 of 2001). There are two types of interest subsidy: mortgage bond's interest subsidy and supplementary interest subsidy. Both methods are designed to reduce the interest payable by the client. The mortgage bond's interest subsidy being based indirectly on the bank's costs (mortgage bond's interest subsidy), and the supplementary interest subsidy on the actual amount of interest payable by the client (asset side subsidy).

Both types of subsidies are presented in the Bank's revenues, thus the Bank only passes on these subsidies to the clients as they pay a lower-than-market interest rate to the Bank. The interest subsidy is available for a period not exceeding the first 20 years of a loan.

A new Hungarian legislation became effective from 1 January 2007 under which a 5% withholding tax is to be paid for the interest income on subsidized mortgage loans. This additional tax is reported in 'General and administrative expenses'.

Those loans which connect interest subsidy are measured at amoritised cost, meet the requirement of the SPPI test, and the allowance is calculated according to expected credit loss model. (see the credit risk model in notes 36)

Mortgage bond interest subsidy

The mortgage bond interest subsidy is available for housing loans up to the stipulated amounts and based on conditions as specified in the government decree 12/2001 and calculated in accordance with the criteria set. The condition of the maximum interest percentage payable by the customer also has to be met. The subsidy is available for housing loans eligible for subsidy as specified in the decree such as:

- Mortgage loans granted by the Bank or with partner banks; and

- Independent and separated liens purchased by the Bank then repurchased by the partner bank under refinancing arrangements, and for receivables from the repurchased part(s) of lien packages.

The subsidy is available on a monthly basis up to the total of mortgage bonds outstanding in the given month. The underlying calculation is based on the daily balance of subsidized loans or mortgage bonds.

Supplementary interest subsidy
The amount of supplementary interest subsidy and the underlying calculation method thereof (reflecting the maximum interest) are laid down in the contract between the Bank and the client. The monthly interest subsidy is one-twelfth of the prevailing subsidized outstanding principal as determined by the amount of the non-due repayable principal as of the date of the transaction.

2.6.29 Contingent liabilities / contingent assets

Consequent to the Group's business, contingent liabilities are not recognized in the financial statements but are presented in the Notes. They are disclosed unless the possibility of an outflow of resources embodying financial gains is remote. Contingent liabilities are reported in the balance sheet when it becomes probable.
Likewise, a contingent asset is not recognized in the financial statements but disclosed when an inflow of financial gains is probable.

2.6.30 Post balance sheet events

Post-balance sheet events that provide additional information about a Group's position at the balance sheet date (adjusting events) are reflected in the financial statements. Post-balance sheet events that are not adjusting events are disclosed in the Notes when material.

2.6.31 Segment information

An operating segment is a component of an entity:
(a) that engages in business activities from which it may earn revenues and incur expenses;
(b) whose operating results are reviewed regularly by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance; and
(c) for which discrete financial information is available.

Operating segments can engage in business activities that have not yet generated income; for instance foundation related transactions can be pre-income operating segments.

The Bank takes the following factors into consideration when determining whether services are interconnected: nature of services, type or group of clients buying the services, methods applied in the course of service provision, and the regulatory environment. The Bank presents each segment whose contribution to (internal and external) revenue, earnings or balance sheet total is material, in consideration of other material provisions of IFRS 8 (Note 40). The data related to the business segments of own lending and refinancing, are separated in the balance sheet (under Notes 19 and 20) and in the statement of profit or loss (under Note 4).
Geographical segmentation has also been analyzed. Since the revenue, earnings or balance sheet total of the German branch office is under 10%, no presentation of geographical segmentation has been made.

2.6.32 Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, therefore, the related assets and liabilities are presented gross in statement of financial position.

2.6.33 Foreign currency translation

The reporting currency of the Bank is HUF referred to 2.3.
The Bank and its subsidiary recognize initially currency transactions in their functional currency valid on the transaction day. Monetary assets and liabilities denominated in currencies other than the company's functional currency are converted to the functional currency at the exchange rate on the balance sheet date. Any difference is reported in the profit or loss. Items other than monetary reported at cost are converted at the rate on the initial day of the transaction. Non-monetary items reported at fair value are converted at the rate on the date fair value was determined.
In the course of consolidation, assets and liabilities of foreign companies are converted to HUF on the reporting date at the NBH rate on the balance sheet date. Items of the profit or loss statement are converted at the annual weighted NBH rate. The currency difference is reported in other comprehensive income. The currency difference is released from other comprehensive income and transferred to profit or loss when the foreign company is dissolved or sold.

2.6.34 Trade date and settlement date accounting

A regular purchase or sale of a financial asset is recognized on the date of delivery. Exemptions are derivatives where recognition of purchase is done on the day when the deal is contracted. The date of settlement is the day on which the Bank Group takes possession of the asset. A regular sale or purchase transaction is a transaction where the asset sold and purchased must be delivered within a set interval prescribed by law or as customary in the market.

2.6.35 Bank tax

The credit institutions as financial institutions are taxable entities of the Act LIX of 2006 on the Introduction of Special Tax and Bankers' contribution intended to improve the Balance of Public Finances.
For tax years 2019 and 2018 the tax base is the total assets according to Hungarian Accounting Standards of the second financial year preceding the tax year (2017, 2016), which can be decreased by decreasing items under the Act.
The Bank tax is presented as other operating expense in the Consolidated Statement of Profit or Loss because it does not meet the definition of income tax according to IFRS.
The special tax for financial institutions liability defined in accordance with the amount of special tax for credit institutions paid by Takarék Mortgage Bank Ltd. and Takarék Commercial Bank Ltd. in 2018.

2.7 Significant accounting judgements and estimates

The preparation of financial statements in conformity with IFRS requires using of estimates and assumptions that affect the amounts reported in the financial statements and notes thereto. Although these estimates are based on management's best knowledge of current event and actions the actual results may differ from those estimates. Estimates are applied in the following areas:

Notes to the Consolidated Financial Statements

Going concern
The Bank's management assessed the Bank's capabilities to continue operation and found that the Bank has the resources necessary for continued operation in the foreseeable future. Furthermore, the management is not aware of any significant uncertainty that might raise serious doubts in respect of the Bank's ability to exist as a going concern.

Fair value of financial instruments
In cases where the fair value of financial assets and liabilities are not measured at marked to market, other kind of assessment model is necessary to be used to determine fair value. Wherever possible, the input of these models is observable market data. Where such data are not available the Bank uses valuation model to determine fair value. (Note 35)

Share-based payment
When establishing the fair value of shares involved in the share option scheme the Bank assesses the allocation condition, the allocation price, and compliance with the trading and profit objectives. (Note 32)

Deferred tax assets
Deferred tax assets are recognized in respect of tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Judgment is required to determine the amount of deferred tax asset that can be recognized, based upon the likely timing and level of future taxable profits, together with future tax planning strategies. (Note 11)

Loan impairment test and its result
The Group regularly assesses its financial instruments portfolio for impairment. Management determines the adequacy of the impairments based upon reviews of individual loans and placements, recent loss experience, current economic conditions, the risk characteristics of the various categories of loans and other pertinent factors.
The use of a new, three stage model was implemented for IFRS 9 purposes. The new impairment methodology (see notes 36) is used to classify financial instruments in order to determine whether credit risk has significantly increased since initial recognition and to identify the credit-impaired assets. For instruments with credit-impairment or significant increase of credit risk lifetime expected losses will be recognized.

Impairment of other assets
The Bank assesses the existence of possible impairment of assets. The Bank estimates the recoverable value of the asset. Recoverable value is the fair value of the asset net of the costs of sale, or the value in use, whichever higher.
When determining value in use expected cash is discounted in consideration of the time value of cash and asset-specific risks.
Each asset is assessed annually (except stated otherwise), when any indication of a reversal or reduction of earlier impairment is assessed. If there is such an indication the Bank estimates the recoverable value of the asset.
For more details see Notes 21 and 22.

Notes to the Consolidated Financial Statements

2.8 Reclassification and error

After the balance sheet date of the consolidated financial statements of 2018 there were no mistakes or errors discovered which are significant and affect the decision made by the users based on the financial statements.

2.9 Changes in the legal and regulatory environment and its effect on the financial statements of the Group

With its 20/2015. (VI.29.) regulation, the Hungarian National Bank from 30 September 2019 raised the minimum level of the Mortgage Financing Indicator from 0.2 to 0.25, and also started a mortgage bond purchase program, which lead to the raising of the refinancing portfolio of the Mortgage Bank.

3 CHANGE IN ESTIMATES

There are not any significant areas, where there is any material change in estimates.

4 INTEREST AND SIMILAR INCOME AND EXPENSE

	2019	2018
Interest income		
Loans and advances to customers at amortised cost and fair value	4,013	5,439
Refinanced mortgage loans	2,573	2,338
Due from banks	8	18
Interest income on assets carried at amortised cost	*6,594*	*7,795*
Securities at fair value through profit or loss		
Securities at fair value through other comprehensive income	549	759
Interest on derivative transactions	1,756	1,139
Interest income on assets carried at fair value	*2,305*	*1,898*
Total	**8,899**	**9,693**

Accrued interest receivable on stage 3 impaired loans amounted to HUF 21 million in 2019 according to IFRS 9. Accrued interest receivable on impaired loans amounted to HUF 62 million in 2018.

	2019	2018
Interest expense		
Mortgage bonds	6,344	6,070
Due to banks	19	31
Interest paid on deposits	0	0
Interest on bonds	175	361
Interest expense on leases	1	0
Interest expense on liabilities carried at amortised cost	*6,539*	*6,462*
Interest on derivative transactions	803	715
Mortgage bonds	271	723
Interest on bonds		
Interest expense on liabilities carried at fair value	*1,074*	*1,438*
Total	**7,613**	**7,900**

The interest income from loans and refinanced mortgage loans includes HUF 941 million interest subsidy in 2019 (2018: HUF 1,642 million).

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

5 FEE AND COMMISSION INCOME AND EXPENSE

	2019	2018
Fee and commission income		
Mortgage loans of the Bank	146	157
Refinanced mortgage loans	89	73
Handling commission	34	62
Real estate appraisal fee	136	89
Treasury services*	1,407	0
Other	-	2
Total	**1,813**	**383**

**gains from the closed derivatives transaction before maturity*

	2019	2018
Fee and commission expense		
Real estate appraisal fee	293	262
Agency fees and commissions	10	39
Treasury services	781	181
Fees and commissions to banks and to clearing house	8	7
Other	-	13
Total	**389**	**502**

6 OTHER OPERATING INCOME

	2019	2018
Reversal of provision*	58	642
Income from sold inventory and inventory	19	41
Rental income on property	2	-
Invoiced expenses and services	726	977
Tax refunds for previous years	-	105
Other	36	56
Total	**841**	**1,821**

*The main part of reversal of provision is connected to the change of the contractual obligation related to IT software, the booked fee increased the maintenance cost in 2018.

All figures in tables are in HUF million except otherwise noted

7 OTHER OPERATING EXPENSE

	2019	2018
Bank tax (detailed in a) below)	74	156
Other payable taxes and contributions*	182	150
Invoiced expenses and services	42	21
Extraordinary depreciation	113	-
Impairment of non-financial assets	-	3
Provision for expected liabilities (Note 30)	-	8
Expenses for the previous year	42	-
Tax penalty, late penalty	2	4
Supervisory and other fees	356	286
Loss on sold inventory	-	27
Loss on damages compensations paid	2	12
Other	89	25
Total	**902**	**692**

*Include the local business tax and the innovation contribution in 2018 and in 2019.

a) Bank tax

The amount of Bank tax booked for 2019 by group members is detailed in the following table:

	2019	2018
Takarék Mortgage Bank Plc.	74	156
Takarék Commercial Bank Ltd.*	-	2,781
Total	**74**	**2,937**

*Include the obligation of financial transaction levy, based on the Act CXVI. of 2012.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

8 GENERAL AND ADMINISTRATIVE EXPENSES

	Note	2019	2018
Staff costs	9	318	413
Marketing and advertising		127	2
General and administrative costs		717	509
Rental fee	10	21	533
Depreciation	21,22,23	167	117
Consultancy fees		333	875
Maintenance costs		836	851
Other taxes		6	9
Insurance fees		8	10
Database system usage		29	31
Other		76	99
Total		**2,658**	**3,449**

9 STAFF COSTS

	2019	2018
Wages and salaries	259	311
Social security contribution	50	75
Other personnel related payments	9	27
Total	**318**	**413**

Social security contribution is payable by the Bank based on gross wages and salaries paid to employees. The full time head count of the Bank at the end of the reporting period was 14 (2018: 724 consolidated, 36 non-consolidated).

All figures in tables are in HUF million except otherwise noted

10 RENTAL FEE (OPERATING LEASE)

Non-cancellable operating leases

The operating lease agreement of the registered office expires on 31 December 2019.

	31 December 2019	31 December 2018
	Minimum lease payments	Minimum lease payments
Within 12 month	-	2,403
Between 1 and 5 years	-	800
Over 5 years	-	758
Total	**-**	**3,961**

These lease agreements are connected to Takarék Commercial Bank Ltd, the investment in this subsidiary are sold in 2019, so the non-cancellable operating leases reduce to zero.

	Minimum lease payments	Contingent rents	Sublease payments	Total
Expense in the period 2019	21	-	-	21
Expense in the period 2018	927	-	(12)	914

All figures in tables are in HUF million except otherwise noted

11 INCOME TAX

	31 December 2019	31 December 2018
Current income tax	**-**	**-**
Corporate income tax*	-	-
Deferred tax expense from continuing operation	**219**	**82**
Deferred tax expense from discontinued operation	**-**	**81**
Total	**219**	**163**

*The local business tax and the innovation contribution are presented on the "Other operating expense" line in the Consolidated Statement of Profit or Loss in 2019 and in 2018.

Reconciliation of expected tax based on book earnings and actual tax paid is presented as follows:
The Act LXXXII of 2016 on the amendment of Act LXXXI of 1996 on Corporate Tax Act modified the tax rate from 19% to 9%.
Based on this information the Group calculated the deferred tax with the 9% tax rate in 2019 and in 2018.

Based on the business plans of the Management the profit of the Group in the foreseeable future will cover the accumulated deferred tax assets from tax loss carry forward. Based on the assumption the recognition of the deferred tax benefits is reasonable.

	31 December 2019	31 December 2018
Profit/ (Loss) before tax	*1,008*	*6,749*
Calculated corporate income tax (9%)	91	607
Items modifying the Hungarian tax base	117	(786)
Effect from discontinued operation	(368)	-
Effect of the reduction of the available taxable profit	379	274
Effect of other modifications	-	68
Total income tax expense/(benefit)	**219**	**163**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Deferred tax position

	31 December 2019				
	Deferred tax assets	Deferred tax liabilities	Deferred tax net position	Income statement effect	Deferred tax position in reserves
Effect of corporate tax of IFRS adoption	-	117	(117)	117	-
Items modifying corporate tax base	-	(24)	24	(1,014)	-
Disbursement fee	-	-	-	44	-
Derivatives	-	-	-	115	-
Impairment	-	-	-	(180)	-
Suspended interest	-	-	-	42	-
Cash-flow hedge	-	-	-	2	-
Effect of consolidation	-	-	-	319	-
AFS securities	-	-	-	(31)	
Effect of discontinued operation	-	-	-	367	-
Net deferred tax position	**-**	**93**	**(93)**	**(219)**	**-**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

	31 December 2018				
	Deferred tax assets	Deferred tax liabilities	Deferred tax net position	Income statement effect	Deferred tax position in reserves
Disbursement fee	(44)	-	(44)	(69)	-
Derivatives	(115)	-	(115)	(235)	-
Impairment	180	-	180	300	-
Suspended interest	(42)	-	(42)	115	-
Acquisition	-	-	-	38	-
Tax loss carried forward	(2)	-	(2)	-	(2)
Effect of consolidation	990	-	990	(274)	-
AFS securities	(319)	-	(319)	(50)	-
Deferred tax of foreign subsidiaries	31	-	31	12	33
Net deferred tax position	**679**	**-**	**679**	**(163)**	**31**

All figures in tables are in HUF million except otherwise noted

12 OTHER COMPREHENSIVE INCOME

Components of other comprehensive income

	31 December 2019	31 December 2018
Other comprehensive income		
Cash-flow hedge reserve	(31)	25
including: change in fair value	(31)	25
including: reclassification to profit or loss	(31)	-
Securities at fair value through other comprehensive income	66	(368)
including: change in fair value	(665)	(504)
including: reclassification to profit or loss	731	136
Foreign currency translation	-	-
Deferred tax effect	(3)	31
Total	**32**	**(312)**

Deferred tax effects relating to other comprehensive income

	31 December 2019			31 December 2018		
	Before tax amount	Deferred tax	Net of tax amount	Before tax amount	Deferred tax	Net of tax amount
Other comprehensive income						
Cash-flow hedge reserve	(31)	3	(28)	25	(2)	23
Securities at fair value through other comprehensive income	66	(6)	60	(368)	33	(335)
Total	**35**	**(3)**	**32**	**(343)**	**31**	**(312)**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

13 FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The Banking Group has introduced the new IFRS 9 standard since 1 January 2018, the classification and the reconciliation of carrying amounts of financial assets and liabilities to IFRS 9 are reported below:

Classification of carrying amounts of financial assets and liabilities according to IFRS 9

	Notes	31. December 2018
Financial assets		
Cash and cash equivalents		*3,157*
Financial assets held for trading		*3,962*
- Derivative financial assets	35	3,962
Non-trading financial assets mandatorily at fair value through profit or loss		*164*
- Loans and advances to customers at fair value	20	164
Financial assets at fair value through other comprehensive income		*192,142*
- Securities at fair value through other comprehensive income	16	192,142
Financial assets at amortised cost		*541,463*
- Balances with the National Bank of Hungary	14	2,073
- Due from banks	15	61,664
- Refinanced mortgage loans	19	105,296
- Loans and advances to customers at amortised cost	20	372,430
Total financial assets		**740,888**
Financial liabilities		
Financial liabilities held for trading		*2,371*
- Derivative financial liabilities	35	2,371
Financial liabilities classified at fair value through profit or loss		*6,693*
- Financial liabilities at fair value through profit or loss, other than derivatives	27	6,693
Financial liabilities measured at amortised cost (other financial liabilities)		*675,381*
- Due to banks	25	156,659
- Deposits from customers	28	304,333
- Issued securities	26	214,389
Total financial liabilities		**684,445**

All figures in tables are in HUF million except otherwise noted

14 BALANCES WITH THE NATIONAL BANK OF HUNGARY

	31 December 2019	31 December 2018
Short term deposits	-	-
Nostro account at National Bank of Hungary	915	2,071
Accrued interest for the period	-	2
Total	**915**	**2,073**

15 DUE FROM BANKS

	31 December 2019	31 December 2018
Nostro accounts	155	2,706
Term deposits	17,412	58,967
Accrued interest for the period	-	6
IFRS 9 impairment	(1)	(15)
Total	**17,566**	**61,664**

16 SECURITIES AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	31 December 2019	31 December 2018
Hungarian Government bonds	30,900	152,995
Hungarian Discount Treasury bills	-	12,409
Domestic issued bonds	12,826	18,712
Mortgage bonds	-	5,600
Investment funds	-	443
Foreign bank bonds	-	1,705
Equity investments classified as FVOCI	10	292
IFRS 9 impairment	(2)	(15)
Total	**43,734**	**192,142**

Equity investments include shares of SZHISZ for HUF 10 million as at 31 December 2019. (2018: HUF 292 million, shares of SZHISZ for 20 million, shares of Garantiqa Creditqurantee Ltd. for HUF 30 million, as well as SWIFT shares for HUF 1 million and VISA Europe shares for HUF 241 million). The investments represent less than 1% stake in the companies, these securities are classified as FVOCI category in 31 December 2019.

All figures in tables are in HUF million except otherwise noted

17 SALE AND PURCHASE OF SUBSIDIARIES, CHANGE IN THE GROUP OWNERSHIP INTEREST IN SUBSIDIARIES

Purchase of subsidiaries, change in the group ownership interest in subsidiaries

The Takarék Commercial Bank Ltd - amortised cost as at 1 January 2018 35,282 HUF million, impairment 3,304 HUF million – sold. During the reporting period, the subsidiary was sold at book value

Takarek Commercial Bank Ltd.

31 October 2019	Book value
Assets	
Cash, cash balances at central banks and other demand deposits	14,651
Financial assets held for trading	33
Non-trading financial assets mandatorily at fair value through profit or loss	130
Financial assets at fair value through other comprehensive income	72,324
Financial assets at amortised cost	446,413-
Derivatives – Hedge accounting	8
Investments in subsidiaries, joint ventures and associates	350
Tangible assets	2,562
Goodwill and other intangible assets	3
Tax assets	344
Other asset	3,343
Liabilities	
Financial liabilities held for trading	44
Financial liabilities measured at amortised cost	503,912
Derivatives - Hedge accounting	2,281
Provisions	3,736
Tax liabilities	13
Other liabilities	2,815
Net assets disposed of	**27,360**

Notes to the Consolidated Financial Statements

31 October 2019	Book value
Consideration received in cash	31,978

Net cash inflow on disposal of a subsidiary

Net assets disposed of	27,360
Consideration received in cash	31,978
Net cash inflow	**4,618**

The combined result of the discontinued operations included in the profit for the year is set out below. The comparative profit and cash flows from the discontinued operations have been re-presented to include those operations classified as discontinued at the end of current year.

Profit for the year of discontinued operations 2019:

31 October 2019	Takarek Commercial Bank Ltd.
Net interest income	9,789
Net fee and commission income	5,257
Operating Income, net	16,494
Profit before tax	1,713
Attributable income tax expenses	-
Profit after tax	1,713
Consolidation profit*	2,669
Reverse of non- controlling interest*	12,517
Gain on disposal of operation	4,618
Profit for the year from discontinued operations	**21,517**

* Consolidated figures

All figures in tables are in HUF million except otherwise noted

Profit for the year of discontinued operations 2018:

31 December 2018	Takarek Commercial Bank Ltd.
Net interest income	12,455
Net fee and commission income	6,052
Operating Income, net	19,851
Profit before tax	1,560
Attributable income tax expenses	(570)
Profit after tax	990
Consolidation profit*	974
Profit for the year from discontinued operations	**1,964**

* Consolidated figures

18 SECURITIES AT AMORTIZED COSTS

	31 December 2019	31 December 2018
Domestic issued bonds	999	-
Total	**999**	**-**

19 REFINANCED MORTGAGE LOANS

Act L of 2001, which amended other acts providing for financial organizations, introduced substantial changes to Act XXX of 1997 on Mortgage Loan Companies and Mortgage Bonds, modifying the role of commercial banks in the provision of mortgage loans. The substance of the amendment was, that the self-lien backed receivables appeared as collateral for mortgage bonds, parallel the modified act allowed the sale and purchase of these self-liens themselves. Thus mortgage banks are able to refinance the mortgage loans of commercial banks.

The Bank signed contracts with several major Hungarian commercial banks to refinance mortgage loans; hence state subsidized the mortgage loans are available through the entire network of these commercial banks. Later, Takarék Mortgage Bank refinanced also market rate (not supported) mortgage loans. In 2018, the refinanced portfolio changed significantly due to the MFAR (Mortgage funding adequacy ratio) indicator coming into force on 1 April 2017 (20/2015 and 6/2016 NBH decrees), as a result the refinancing activity of Takarék Mortgage Bank has been highly active. By the end of 2019 the number of refinanced bank partners increased to 11. As a result, the refinanced loan portfolio of the Mortgage Bank increased by 28.12% and amounted to HUF 216.98 billion (without the refinanced loan portfolio of Takarék Commercial Bank) at the end of the year.

All figures in tables are in HUF million except otherwise noted

20 LOANS AND ADVANCES TO CUSTOMERS

	31 December 2019	31 December 2018
Housing loans	48,588	130,261
General purpose mortgage loans	9,455	65,438
Customer loans and overdrafts	-	13,062
Loans to employees	764	923
Loans to companies at amortised cost	9	169,641
Loans and advances to customers at amortised cost gross subtotal	**58,816**	**379,325**
Loans to companies at fair value	-	164
Loans gross subtotal	**58,816**	**379,489**
Fair value adjustment of hedged items	-	240
Accrued part of disbursed loans under Funding of Growth Scheme*	-	-
Derecognition**	-	(336)
Accrued interest**	-	5,206
Amortized origination cost**	-	610
Loans gross total	**58,816**	**385,209**
Loan impairment	(988)	(12,615)
Loan portfolio reported	**57,828**	**372,594**

*The disbursed loans under Funding for Growth Scheme started in June 2013. Related to Funding of Growth Scheme the total disbursed loan is HUF 28.5 billion at the end of year 2016. The Bank booked these disbursed loans and the liabilities to NBH at fair value at initial recognition, and accrued the difference between fair value and contractual value until the end of maturity in line with IFRS 9.B5.1.2A. The Accrued part of disbursed loans under Funding of Growth Scheme is reported in other assets in 2018.

** These are the part of loans and advances to customers at amortised cost gross at 31 December 2019.

Loan impairment based on individual rating: HUF 377 million (2018: HUF 2,468 million), based on portfolio rating: HUF 611 million (2018: HUF 10,147 million).

The aggregate amount of stage 3 loans was HUF 2,784 million as of 31 December 2019 (31 December 2018: HUF 22,495 million the non-performing loans).

Within the total balance of mortgage loans 99.98% have maturity over five years (2018: 99.46%), exceeding the minimum level of 80% that is required by the Section 5(1) of Act XXX of 1997 on Mortgage Loan companies.

The total outstanding mortgage loan principal does not exceed 70% of the aggregate collateral value of real estate determined at loan disbursement that is required by the Section 5(3) of Act XXX of 1997 on Mortgage Loan Companies. As of 31 December 2019, loan to value is 32.28% (31 December 2018: 29.38%).

All figures in tables are in HUF million except otherwise noted

21 TANGIBLE ASSETS 31 DECEMBER 2019

	Property and Leasehold improvement	Office equipment	Total
Gross value			
Opening balance	3,409	1,132	4,541
Increase	24	30	54
Decrease	(26)	(156)	(182)
Discontinued operations adjustment	(3,049)	(586)	(3,635)
Closing balance	**358**	**420**	**778**
Depreciation			
Opening balance	1,038	724	1,762
Annual depreciation from continuing operation	53	23	76
Annual depreciation from discontinued operation	82	31	113
Decrease	(27)	(11)	(38)
Discontinued operation adjustment	(798)	(438)	(1,236)
Closing balance	**348**	**329**	**677**
Impairment			
Opening balance	484	124	608
Increase*	-	-	0
Decrease			0
Discontinued operations adjustment	(484)	(124)	(608)
Closing balance	**-**	**-**	**-**
Net value	**10**	**91**	**101**

*The Bank estimates the recoverable amount of the tangible asset. Recoverable amount is the fair value of the asset net of the costs of sale, or the value in use, whichever is higher. Where the carrying amount of an asset exceeds its recoverable amount, the Bank recognises impairment on the asset, by this the carrying amount is written down to the recoverable amount.

The tangible assets in the Consolidated Statement of Financial Position contain the right-of use assets according to IFRS 16. The right-of use assets carrying amount are 56 million HUF as at 31 December 2019. (see note 23)

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

TANGIBLE ASSETS 31 December 2018

	Property and Leasehold improvement	Office equipment	Total
Gross value			
Opening balance	3,515	1,390	4,905
Increase	58	142	200
Decrease	(164)	(400)	(564)
Closing balance	**3,409**	**1,132**	**4,541**
Depreciation			
Opening balance	918	806	1,724
Annual depreciation	139	73	212
Decrease	(19)	(155)	(174)
Closing balance	**1,038**	**724**	**1,762**
Impairment			
Opening balance	210	124	334
Increase*	274	-	274
Decrease	-	-	-
Closing balance	**484**	**124**	**608**
Net value	**1,887**	**284**	**2,171**

*The Bank estimates the recoverable amount of the tangible asset. Recoverable amount is the fair value of the asset net of the costs of sale, or the value in use, whichever is higher. Where the carrying amount of an asset exceeds its recoverable amount, the Bank recognises impairment on the asset, by this the carrying amount is written down to the recoverable amount.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

22 INTANGIBLE ASSETS 31 DECEMBER 2019

	Software	Other intangible assets	Total
Gross value			
Opening balance	2,181	163	2,344
Increase	-	-	-
Decrease	(321)	-	(321)
Discontinued operations adjustment	(622)	(99)	(721)
Closing balance	**1,238**	**64**	**1,302**
Depreciation			
Opening balance	1,602	6	1,608
Annual depreciation from continuing operation	36	-	36
Annual depreciation from discontinued operation	-	1	1
Increase/ (-)Decrease	(123)	153	30
Discontinued operation adjustment	(622)	(96)	(718)
Closing balance	**893**	**64**	**957**
Impairment			
Opening balance	579	122	701
Increase	104	-	104
Decrease	-		0
Discontinued operations adjustment	(579)	(122)	(701)
Closing balance	**104**	**-**	**104**
Net value	**241**	**-**	**241**

In the context of the impairment test of intangible assets the Bank reviewed projects in the course of construction but not yet capitalized by 31 December 2019.

The Bank estimates the recoverable amount of the intangible asset. The impairment of this year connected to IT sotware where the recoverable amount is lower than the net assets. The impairment is presented on the “Other operating expense” line in the Consolidated Statement of Profit or Loss in 2019.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

INTANGIBLE ASSETS 31 December 2018

	Software	Other intangible assets	Agency cooperation	Total
Gross value				
Opening balance	2,738	429	645	3,812
Increase	-	2	-	2
Decrease	(557)	(268)	-	(825)
Derecognize of intangible assets due to disposal	-	-	-	-
Closing balance	**2,181**	**163**	**645**	**2,989**
Amortisation				
Opening balance	1,602	150	231	1,983
Annual amortisation	42	2	32	76
Decrease	(363)	(178)	-	(541)
Closing balance	**1,281**	**(26)**	**263**	**1,518**
Impairment				
Opening balance	579	122	-	701
Increase	-	-	382	382
Reversal	-	-	-	-
Closing balance	**579**	**122**	**382**	**1,083**
Net value	**321**	**67**	**-**	**388**

In the context of the impairment test of intangible assets the Bank reviewed projects in the course of construction but not yet capitalized by 31 December 2018.

The Bank estimates the recoverable amount of the intangible asset. The impairment of 2018 connected to the agency cooperation where the recoverable amount is lower than the net assets. The impairment is presented on the “Other operating expense” line in the Consolidated Statement of Profit or Loss in 2018.

23 IFRS 16 LEASES

Right-of-use asset

	31 December 2019	1 January 2019
Owned property, plant and equipment	101	2,171
Right-of-use assets, other than investment properties	56	1,264
Total property, plant and equipment	**157**	**3,435**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Lease liability

Lease liabilities presented in the statement of financial position

	31 December 2019	1 January 2019
Short term	21	717
Long term	49	560
Total lease liabilities	**70**	**1,277**

Maturity analysis - undiscounted contractual payments

	31 December 2019	31 December 2018
up to 1 year	21	728
1 year to 5 years	49	500
over 5 years	0	81
Total undiscounted lease liabilities	**70**	**1,309**

Right-of-use asset

	Property	Company Car	Total
Opening balance at 1 January 2019	**1,253**	**11**	**1,264**
Increase	70	19	89
Annual amortization from continuing operation	(54)	-	(54)
Annual amortization from discontinued operation	(560)	(1)	(561)
Decrease	(25)	(10)	(35)
Discontinued operation adjustment	(629)	(18)	(647)
Balance at 31 December 2019	**55**	**1**	**56**

Total cash outflow for leases

	2019
Cash outflow from continuing operation	(42)
Cash outflow form discontinued operation	(571)
Total cash outflow for leases	(613)

All figures in tables are in HUF million except otherwise noted

Items related to lease liabilities presented in profit or loss

	31 December 2019
Interest expense on the lease liabilities from continuing operation	(1)
Interest expense on the lease liabilities from discontinued operation	(10)
Expenses related to variable lease payments not included in the measurement of the lease liabilities	-
Income from subleasing right-of-use assets	-
Expenses related to short-term leases	-
Expenses related to leases of low-value assets, expect the expense relating to short-term leases of low-value assets	-
Gains or losses arising from sale and leaseback transactions	-
Total	**(11)**

Items presented in the statement of cash flows

	31 December 2019
Interest expense on the lease liabilities	(11)
Cash payments for the principal portion of the lease liability	(613)

24 OTHER ASSETS

	31 December 2019	31 December 2018
Prepaid expenses	222	1,362
Reclaimable taxes	1	845
Settlements with the Hungarian State	414	124
Repossessed collateral	2	103
Debtors	629	499
Deposits	260	3,354
Accrued part of disbursed loans under Funding of Growth Scheme*	-	2,944
Other	93	1,158
Total	**1,621**	**10,390**

* The Accrued part of disbursed loans under Funding of Growth Scheme is reported in other assets in 2018.
In case of properties held for sale and repossessed collaterals the Group endeavours to sell the properties as soon as possible.

All figures in tables are in HUF million except otherwise noted

25 DUE TO BANKS

	31 December 2019	31 December 2018
Long term loans received	-	17,193
Short term loans received	3,119	139,465
Accrued interest	-	1
Total	**3,119**	**156,659**

26 ISSUED SECURITIES

The Group reports mortgage bonds and bonds that are recognised at amortised cost on 'Issued securities' line in the statement of financial position.

	31 December 2019		31 December 2018	
	Gross book value	Face value	Gross book value	Face value
Non-listed mortgage bonds				
Fixed interest	3,972	3,824	16,480	16,449
Floating interest	-	-	-	-
Listed mortgage bonds				
Fixed interest	218,819	214,137	177,406	176,200
Floating interest	43,138	43,017	10,067	10,072
Total mortgage bonds	**265,929**	**260,978**	**203,953**	**202,721**
Non-listed bonds				
Fixed interest	-	-	-	-
Floating interest	-	-	-	-
Subordinated bonds	-	-	-	-
Listed bonds				
Fixed interest	-	-	5,836	5,786
Floating interest	-	-	-	-
Total bonds	**-**	**-**	**5,836**	**5,786**
Accrued interest (*mortgage bonds*)*	-	-	4,431	-
Accrued interest (*bonds*)	-	-	169	-
Total issued securities	**265,929**	**260,978**	**214,389**	**208,507**

**These are part of gross book value of mortgage bonds.*

All figures in tables are in HUF million except otherwise noted

Mortgage bonds

Mortgage bonds are transferable registered or bearer securities and, pursuant to Act XXX of 1997 on Mortgage Loan Companies and on Mortgage Bonds, can be issued only by mortgage banks. Prior to their issue, a property supervisor reviews if the Bank has adequate collateral for the issue. These collaterals may be (i) ordinary collaterals such as the principal and interest receivable (including interest subsidies) from mortgage loans provided in accordance with the standard collateral requirements, the repurchase price of an independent lien and the related refinancing interest, and (ii) additional collateral such as, typically, government bonds and related interest and any principal and interest receivable guaranteed by the government. According to the Act, if the amount of principal receivable exceeds 60% of the collateral value of related property offered, only the principal receivable amounting to 60% of the collateral value and the proportionate amount of interest can be considered as an ordinary collateral.
The Act governs the proportionate between ordinary and additional collaterals: at least 80% of all collateral must be ordinary collateral. In accordance with the requirements set forth in the Jht, the Bank shall at all times maintain:

(i) Cover for the nominal value: the nominal value of the ordinary collateral (the underlying principal excluding the provision for any impairment loss and interest) should exceed 100% of the not yet repaid nominal value of the mortgage bonds outstanding,

(ii) If point (i) is not met, the Bank has to acquire additional collateral to the extent that the sum of the nominal values of the ordinary and additional collaterals always exceed 100% of the not yet repaid minimal value of the mortgage bonds outstanding,

(iii) Cover for the interest: the interest on the nominal value of the ordinary and supplementary collaterals should exceed 100% of the interest on the not yet repaid nominal value of the mortgage bonds outstanding.

In addition to assessment of the nominal value of the cover for mortgage bonds the Mortgage Loans Act also provides for assessment of mortgage bonds cover at present value. The fair value of collateral exceeded the present value of mortgage bonds outstanding not yet repaid throughout the period.

Bonds

From 2007 the Group launched bonds in addition to mortgage bonds.

Bonds are registered dematerialized securities. Pursuant to the provisions of Act CXX of 2001 on Capital Markets as amended and of Government Decree No. 285 of 2001 (26 December) the Group generates a document containing the data of the bond series. The document, which itself is not a security, is then deposited with Central Clearing House and Depository Ltd. (KELER).

Bonds incorporate the Group’s direct, unconditional, non-subordinate unsecured liabilities. Bonds are equal in rank to the Group’s other outstanding unsecured non-subordinate liabilities at any time in the hierarchy of repayment in the event of bankruptcy, voluntary liquidation or foreclosure except for liabilities, which have precedence on the basis of the governing laws on voluntary liquidation or other relevant statutory provisions.

27 FINANCIAL LIABILITIES AT FAIR VALUE THROUGH PROFIT OR LOSS, EXCEPT DERIVATIVES

The Group reports mainly mortgage bonds and bonds measured at fair value on ‘Financial liabilities at fair value through profit or loss’ line in the statement of financial position. (Description is included in Point 26 of Notes.)
Such financial liabilities are issued mortgage bonds, bonds and interbank loans (that are economically closely related to the swaps, which are entered to mitigate risks and not classified as the hedged item in hedging). The contractually required payment at maturity to the holder of the obligation is the face value of these financial liabilities. Interest is earned or incurred is accrued in ‘Interest income’ or ‘Interest expense’, respectively, using the effective interest rate. The change in fair value other than attributable to change in market conditions, that give right to market risk represent credit risk.

	31 December 2019		31 December 2018	
	Fair value	Face value	Fair value	Face value
Listed mortgage bonds				
Fixed interest	6,552	5,768	6,693	5,787
Floating interest	-	-	-	-
Total mortgage bonds	**6,552**	**5,768**	**6,693**	**5,787**
Total Financial liabilities at fair value through profit or loss, except derivatives	**6,552**	**5,768**	**6,693**	**5,787**

The total credit risk which is due to financial liabilities through profit or loss was HUF 197.6 million as of 31 December 2019 (31 December 2018: HUF 80.9 million).

28 DEPOSITS FROM CUSTOMERS

As a lending institution the Bank holds deposits from clients. The deposit portfolio is as follows:

	31 December 2019	31 December 2018
Current accounts	-	198,416
Term deposits	-	105,839
Accrued interest	-	78
Total	**-**	**304,333**

These deposit agreements are connected to Takarék Commercial Bank Ltd., the investment in this subsidiary are sold in 2019, so the deposits reduce to zero.

All figures in tables are in HUF million except otherwise noted

29 PROVISIONS

Provisions are set up mainly for current and contractual obligation. Provision is also set up for a pending lawsuit. The changes in provisions are accounted for in credit loss expense (Note 36) or in other operating expense (Note 7).

2019	Credit risk provision	Contractual obligation	Other provision	Expected costs of legal cases	Total
Opening balance	1,267	2,122	583	16	3,988
Increase in the period continuing operation	2	-	9	-	11
Increase in the period discontinued operation	390	12	91	9	502
Utilization in the period continuing operation	(10)	(56)	(6)	(2)	(74)
Utilization in the period discontinued operation	(75)	-	(93)	(13)	(181)
Discontinued operations adjustment	(1,571)	(1,581)	(575)	(10)	(3,737)
Closing balance	**3**	**497**	**9**	**-**	**509**

The credit risk provision in 2019 is attributable to the off-balance sheet items.

All figures in tables are in HUF million except otherwise noted

2018	Credit risk provision	Contractual obligation	Other provision	Expected costs of legal cases	Total
Opening balance	674	4,905	630	42	6,251
Increase in the period	1,472	2,123	572	10	4,177
Utilization in the period	(879)	(4,906)	(619)	(36)	(6,440)
Closing balance	**1,267**	**2,122**	**583**	**16**	**3,988**

30 OTHER LIABILITIES

	31 December 2019	31 December 2018
Taxes payable	-	512
Creditors	73	107
Accrued expenses	328	1,736
Liability from investments services	-	4
Customer loan prepayments	591	840
Repo liability	-	3,767
Accrued part of disbursed liabilities under Funding for Growth Scheme*	-	2,061
Other	167	1,820
Total	**1,159**	**10,847**

* The Accrued part of disbursed loans under Funding of Growth Scheme is reported in other liabilities in 2018, it has been reclassified from Due to banks

All figures in tables are in HUF million except otherwise noted

31 SHARE CAPITAL

In the year of 2018 the ownership structure of the Bank Group was significantly altered. The MTB Magyar Takarékszövetkezeti Bank Ltd. purchased the majority of the Bank's shares, as a result of these transaction it has the sole managing owner.

As of 31 December 2019 the Bank's share capital consists of series "A", "B" and "C" shares.
The ownership structure of the Bank as at 31 December 2019 and 31 December 2018 was as follows:

	31 December 2019		31 December 2018	
Shareholder	Holding %	Number of shares	Holding %	Number of shares
Ordinary shares (Series "A" listed)				
Domestic institutional investors	52.6	57,069,304	50.45	54,735,748
Foreign institutional investors	0.02	20,576	0.02	126,899
Domestic private investors	3.47	3,759,643	3.47	5,750,222
Foreign private investors	0.06	60,400	0.06	39,388
Employees, directors and senior management	0.0	-	0.0	-
Government held owner	4.46	4,832,225	4.46	4,832,225
Treasury shares	0.23	253,601	0.23	253,601
Other	0.0	4,261	0.23	250,410
Subtotal	*60.84*	*66,000,010*	*60.84*	*66,000,010*
Dividend preference shares (Series "B" non- listed)				
Domestic institutional investors	13.05	14,163,430	13.05	14,163,430
Subtotal	*13.05*	*14,163,430*	*13.05*	*14,163,430*
Ordinary shares (Series "C" non-listed)				
Domestic institutional investors	26.11	2,832,686	26.11	2,832,686
Subtotal	*26.11*	*2,832,686*	*26.11*	*2,832,686*
	100.0	***82,996,126***	***100.0***	***82,996,126***

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

31.1 The following amounts were used in the calculation of earnings per share:

	31 December 2019	31 December 2018
Profit of shareholders of the Bank from continuing operation	789	4,935
Change of general reserve	(215)	(252)
Attributable profit	**574**	**4,683**
Weighted average number of shares	108 236 699	108 236 699

Earnings per share ratio is calculated as the profit attributable to shareholders of the Bank divided by the weighted average number of shares outstanding during the period excluding treasury shares. For the diluted earnings per share figure the profit attributable to shareholders and the weighted average number of shares outstanding needs to be adjusted by all of the potentially diluting securities. For the normal earnings per share figure the profit attributable to shareholders means the result for the year decreased by the amount of the general reserves which is divided by the number of the shares excluding the number of the treasury shares by the Bank. Shares to managers on the context of the share-based payment are allocated from Treasury shares and require no new issues and thus have no diluting effect on EPS. The Bank has no dilutive potential ordinary shares. Earnings per share figure therefore equals to the diluted earnings per share figure.

31.2 Treasury shares purchased

	31 December 2019	31 December 2018
Opening balance	207	207
Purchase	-	-
Closing balance	**207**	**207**

31.3 Other reserves

	Note	31 December 2019	31 December 2018
Share premium		27,926	27,926
General reserve	33	927	712
Cash-flow hedge reserve		-	28
Change in fair value of financial assets at fair value through other comprehensive	31	992	932
Total other reserves		**29,845**	**29,598**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

31.4 Securities at fair value through other comprehensive income reserve

	31 December 2019	31 December 2018
Opening balance	932	1,267
Net unrealised gains on securities at fair value through other comprehensive income	(665)	(502)
Net realised losses on securities at fair value through other comprehensive income	731	136
Deferred tax	(6)	31
Closing balance	**992**	**932**

31.5 Non-controlling interest

	31 December 2019	31 December 2018
Opening balance	12,517	12,828
Dividend payment to NCI	-	-
Share of profit/(loss) of the year	-	(311)
Selling of subsidiary Takarék Commercial Bank Ltd	(12,517)	-
Closing balance	**0**	**932**

Non-controlling interest detailed by subsidiaries at 2018

Name of the subsidiary	The proportion of ownership interests held by non-controlling interests	The profit or loss allocated to non-controlling interests of the subsidiary during the reporting period	Accumulated non-controlling interests of the subsidiary at the end of the reporting period
Takarék Commercial Bank Ltd.	49%	(315)	12,517
Magyar Kártya Szolgáltató Ltd.	1%	4	-
Total	**-**	**(311)**	**12,517**

All figures in tables are in HUF million except otherwise noted

32 SHARE-BASED PAYMENTS

Share options are granted to employees and also others providing similar services, it is difficult to estimate the fair value of those benefits that are coming from these services, therefore the Group measures the fair value by reference to the fair value of the equity instruments granted.
The Group hasn't got approved share based incentive scheme in 2019 and in 2018.

33 GENERAL RESERVE

In accordance with statutory requirements, the Bank and other credit institutions within the Group are required to set up a non-distributable general reserve equal to 10% of statutory profit after tax. Increases in the general risk reserve are separated from retained earnings, as calculated under Hungarian regulatory rules, and thus are not charged against income. According to the Section 13 (8) of the Government Decree No. 250/2000 (XII.24.) on the specifics of the annual reporting and bookkeeping tasks of investment companies are required to release the general reserve when loss after tax deduction occurs. The amount of the General reserve is HUF 927 million as at 31 December 2018 (General reserve was HUF 712 million as at 31 December 2018). The other reserves are presented in Notes 31.

34 COMMITMENTS

To meet the financial needs of customers, the Bank enters into various irrevocable commitments and contingent liabilities. Even though these obligations may not be recognised on the statement of financial position, they do contain credit risk and are therefore part of the overall risk of the bank.

Off-balance sheet commitments comprise of loans not drawn and other contracted future payments to suppliers of the Group:

	31 December 2019	31 December 2018
Guarantees	-	5,414
Granted bail	110	-
Loan commitments	18,094	99,445
Total	**18,204**	**104,859**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

35 FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of the on- and off-balance sheet financial assets and liabilities:

Financial instruments stated at amortized cost: due to short-term maturity profiles, the carrying values of certain financial assets and liabilities were assumed to approximate their fair values. These include cash and due from banks and with the National Bank of Hungary as well as deposits.

The following shares disclosed under investment.
Equity investments include shares of SZHISZ for HUF 10 million (2018: HUF 292 million, shares of Garantiqa Creditgurantee Ltd. for HUF 30 million, as well as SWIFT shares for HUF 1 million and VISA Europe shares for HUF 241 million)

Securities at fair value through other comprehensive income: Securities at fair value through other comprehensive income held for liquidity purposes are marked to market. For investments traded in organised financial markets, fair value is determined by reference to Stock Exchange quoted market bid prices at the close of business on the balance sheet date. For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another instrument which is substantially the same, or is based on the expected discounted cash flows.

35.1 Loans and advances to customers at amortised cost and refinanced mortgage loans:

The Bank calculates the fair value of loans and advances to customers and refinanced loans at amortized cost on an individual basis.
The applied valuation model takes into account the following:

- The scheduled and calculated repayments, with certain restrictions
- In case of loan repricing events the model recalculates the interest cash flow
- In case of loans where amortized cost is calculated with simplified approach no FV correction is applied

The cash flow series calculated in this way are discounted with the yield curve applied in the Bank's evaluation, which contains the following components:

- Relevant market yield curve
- Spread implied by the annual risk cost
- Spread implied by the capital allocated to the loans (regulatory minimum requirement and all addons)
- Allocated operational costs

The net value of assets, i.e. the fair value of the total portfolio of loans is determined by combining and exchanging to HUF the FX values.

	31 December 2019		31 December 2018	
	Carrying amount	Fair value	Carrying amount	Fair value
Refinanced mortgage loans	217,205	217,205	105,296	105,296
Loans and advances to customers at amortised cost	57,828	64,016	372,737	373,918

35.2 Fair value of mortgage bonds and bonds carried at amortised cost

The fair value of mortgage bonds and bonds is calculated by the Bank on a cash flow basis. In the calculations the Bank identifies the cash flows of the mortgage bonds discounted by the valuation yield curve. This is considered as the fair value of mortgage bonds.

In case of floating rate mortgage bonds the expected interest rates are estimated on a forward basis including interest premium. The interest cash flow calculated and the principal repayments are discounted to present value using the valuation yield curve.

For the valuation yield curve the Bank calculates the yield of own securities – denominated in Hungarian forint and Euro taking into account secondary market quotations, the yields of the secondary deals and the spreads regarding to the issues on primary markets. Based on these yields the Bank position management system calculates the yield curves for the different currencies and bond types (mortgage bond and several unsecured bonds).

The change in fair value is mainly due to the changes in market conditions. Based on this the change in fair value attributable to credit risk is not material.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

	31 December 2019		31 December 2018	
	Bookvalue	Fair value	Book value	Fair value
Non-listed mortgage bonds				
Fixed interest	3,972	3,977	17,528	17,955
Floating interest	-	-	-	-
Listed mortgage bonds				
Fixed interest	218,819	225,475	180,772	182,491
Floating interest	43,139	42,988	10,086	10,107
Total mortgage bonds	**265,929**	**272,440**	**208,385**	**210,553**
Non-listed bonds				
Fixed interest	-	-	-	-
Floating interest	-	-	-	-
Listed bonds				
Fixed interest	-	-	6,004	6,153
Floating interest	-	-	-	-
Total bonds	**-**	**-**	**6,004**	**6,153**
Total issued security	**265,929**	**272,440**	**214,389**	**216,706**

Book value also includes the accrued interests.

35.3 Fair value of other items in the statement of financial position

No estimation is made in respect of the fair value of assets and liabilities that are not considered to be financial instruments, such as fixed assets and other assets and liabilities. Given the use of subjective judgement and uncertainties, the fair values should not be interpreted as being realisable in an immediate settlement of the instruments.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

35.4 Fair value of derivative transactions

Swap transactions are contracts between two parties to swap the differences of interests or exchange rates for a fixed amount. In case of interest rate swap (IRS) transactions, parties usually swap the fixed and variable interest payments of a given currency. In FXS, they swap fixed payments and given amounts of different currencies. CCIRSs are swap transactions where parties swap fix amounts in different currencies as well as fixed and variable interest payments.

	Fair value		Notional amount	
	31 December 2019	31 December 2018	31 December 2019	31 December 2018
Derivatives designated as cash-flow hedges				
Positive fair value of cash flow hedges	-	1	-	33
Including: CCIRS	-	1	-	33
Swap deals classified as HFT				
Positive fair value of trading swaps	175	3,961	15,294	103,796
Including: CCIRS	22	-	2,342	-
Including: IRS	97	3,941	4,841	103,153
Including: FXS	56	20	8,111	643
Fair value hedge				
Positive fair value of IRS fair value hedge	2,676	-	49,650	-
Including: CCIRS	-	-	-	-
Including: IRS	2,676	-	49,650	-
Forward deals				
Positive fair value of forward deals	-	-	-	-
Total derivative financial assets	**2,851**	**3,962**	**64,944**	**103,828**

All figures in tables are in HUF million except otherwise noted

	31 December 2019	31 December 2018	31 December 2019	31 December 2018
Derivatives designated as cash-flow hedges				
Negative fair value of cash flow hedges	-	(11)	-	1,475
Including: CCIRS	-	(11)	-	1,475
Swap deals classified as HFT				
Negative fair value of trading swaps	(136)	(1,896)	12,952	127,286
Including: CCIRS	-	-	-	-
Including: IRS	(39)	(1,896)	7,960	127,286
Including: FXS	(97)	-	4,992	-
Fair value hedge				
Negative fair value of fair value hedges	(287)	(464)	4,799	29,577
Including: CCIRS	-	-	-	-
Including: IRS	(287)	(464)	4,799	29,577
Forward deals				
Negative fair value of forward deals	-	-	-	26
Total derivative financial liabilities	**(423)**	**(2,371)**	**17,751**	**158,363**

The fair value of derivative deals is also calculated based on a cash flow basis by the Bank, the derivatives are broken down to elementary cash flows and the present value is calculated.
The present value of the future cash flows of fixed interest rate deals is calculated by the Bank using the zero-coupon swap yield curve corresponding to the appropriate currency. The fair value of swap deals is the difference of the present value of the two series of cash flows not yet due (incoming and outgoing).

In the case of floating rate deals the expected interest rates are estimated on a forward basis including interest premium. The interest cash flow calculated and the principal payments are discounted to present value using the multi-level yield curve (forward yield curve, and discounting curve). The fair value of the deal is the aggregate of the present values.

The risk premium is significant and permanent, it is justified to incorporate it into the evaluation method of swaps. The yield curve is adjusted with the risk premium. The application of the appropriate risk premium enhances the accuracy of the fair value calculation (please also refer to Note 3) taking counterparty and own credit risk into amount (CVA/DVA) in accordance with IFRS 13.

All figures in tables are in HUF million except otherwise noted

For the Bank's existing derivative contracts designated as fair value hedges, the purpose of the transaction is to exchange fixed interest rate contracts for floating rate transactions and to hedge the resulting fair value risk. The parameters of the hedging instrument (maturity, amount, currency, interest rate, etc.) and thus its cash flow are the same as the parameters of the hedged security and the cash flow of capital and interest.

In the valuation of hedging transactions, the Bank establishes a so-called hypothetical swap and measures its efficiency accordingly. The Bank introduced hedge accounting in the second quarter of 2019 for swap transactions in the individual IFRS financial statements of Takarék Mortgage Bank. The effect of this is shown in the table on December 31, 2019. (The table as at December 31, 2018 contains consolidated data.)

35.5 Fair value hedge transactions

31 December 2019

Description of the hedging instrument	Types of hedged items	Fair value of the hedging instrument	Fair value of the hedged items	Losses on the hedging instrument	Gains on the hedged items
MIRS	Issued mortgage bonds	2,676	(64,353)	301	(304)
MIRS	Government bonds	(288)	5,832	(208)	186

In 2018 two new IRS was designated as hedging instrument in fair value hedge connection.

31 December 2018

Description of the hedging instrument	Types of hedged items	Fair value of the hedging instrument	Fair value of the hedged items	Gains on the hedging instrument	Losses on the hedged items
IRS	loans and advances to customers	(262)	15,575	(240)	240
IRS	available-for-sale asset	(202)	11,029	(99)	99

All figures in tables are in HUF million except otherwise noted

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35.6 Fair value of financial instruments carried at fair value

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:
Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and
Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments carried at fair value.

	31 December 2019		
	Level 1	Level 2	Level 3
Assets			
Securities at fair value through other comprehensive income	43,734	-	-
Derivative financial assets	-	2,851	-
Total assets carried at fair value	**43,734**	**2,851**	**-**
Liabilities			
Derivative financial liabilities	-	423	-
Financial liabilities at fair value through profit or loss, except derivatives	-	6,552	-
Total liabilities carried at fair value	**-**	**6,976**	**-**

	31 December 2018		
	Level 1	Level 2	Level 3
Assets			
Securities at fair value through other comprehensive income	191,699	443	-
Derivative financial assets	-	3,961	1
Total assets carried at fair value	**191,699**	**4,404**	**1**
Liabilities			
Derivative financial liabilities	-	2,360	11
Financial liabilities at fair value through profit or loss, except derivatives	-	6,693	-
Total liabilities carried at fair value	**-**	**9,053**	**11**

All figures in tables are in HUF million except otherwise noted

36 RISK MANAGEMENT

36.1 Overview

Takarék Mortgage Bank Plc. is member of Integration Organisation of Cooperative Credit Institution (SZHISZ). Due to the membership of Integration the scope of the risk management policies of the Integration, as well as risk strategy have been extended to the bank.

Based on the Section 5 of Article 1 of the Act CXXXV of 2013 on integration of cooperative financial institutions and modification of certain rules on economic issues (Szhitv) the Integration Organisation and its members are required to accept joint and several responsibility for each other's obligations according to Ptk. The joint and several responsibility system cover also all the receivables to Integration Organisation and its members, independently the date of its occurrence.

Based on the Section 5 of Article 1 of Szhitv the Integration Organisation and its members are under the combined supervision according to Hpt.

If the conditions are met in the Article 10 of the EU Regulation No 575/2013 (CRR) of the European Parliament and of the Council based on the Section 5 of Article 1 of Szhitv the integration of cooperative financial istitutions is exempted from individual applying of the requirements are defined in the Section (2)-(8) of CRR. According to the resolution no. H-JÉ-I-209/2014 (on 3 March 2014) the National Bank of Hungary authorized the members of the Integration to apply individual exemption based on the Article 10 of CRR.

Risk Strategy – approved by the Board of Directors of MTB Magyar Takarékszövetkezeti Bank Zrt. is mandatory for credit institutions and companies under consolidated supervision led by MTB Magyar Takarékszövetkezeti Bank Zrt. – cover: risk culture, risk taking principles, objectives, risk types, significant risks, risk appetite and risk capacity, risk structure, risk management, the structure and organization of risk management.

The Integration and its member institutions seek to create an integrated risk culture which covering the whole Integration and which is in line with their risk appetite, and their risk tolerance ensure the identification, measurement and management of the emerged risks. The primary tools for creating a risk culture are internal policies, strategies, regulations and guidelines, communication and training of employees.

The risk capacity of Takarék Mortgage Bank Plc. should be in line with the financial resources that are available to cover potential losses. In order to this the current and future economic, capital requirements and the capital requirements under Pillar 1 for quantifiable risk types are calculated.

Prudent risk taking is a fundamental value for the Bank. In order to this risk management identifies, evaluates and analyses the exposures. It processes the information gained, develops risk guidelines, and operates risk management systems.

The Risk Strategy is based on the following main pillars:

- in risk management application of the best approaches and methods applied in market practice

- identification of risk and yield profile of segments, products and risk positions and continuous monitoring
- consideration of the risks in business decisions
- separation the risk management organisation from the business division
- the importance of all stages of the risk management process
- the risk management process is the part of the Bank Group's management system, its aspects are integrated into the strategic and annual planning.

The exposure is basically credit-, liquidity-, market- and operational risks.

36.2 RISK MANAGEMENT STRUCTURE

Board of Directors
The Boards of Directors of the banks are responsible for the Takarék Mortgage Bank's and Takarék Commercial Bank's risk management policy and strategy. The Boards of Directors approve the basic framework rules for risk management and guidelines of applicable methodologies. Due to the Integration Membership the Banks follow the risk strategy, apply the uniform risk management policies of the Integration and report about their risks to the central bodies of the Integration – to the MTB Magyar Takarékszövetkezeti Bank Zrt., and the Integration Organisation of Cooperative Credit Institution (SZHISZ).
Based on regular risk exposure reports, the Boards of Directors evaluate the risk management activities and the level of exposure of the banks. If the level of exposure undertaken by the banks does not correspond to the strategy the Board takes measures to contain risks.

Supervisory Board
The Supervisory Boards of the banks are responsible for monitoring the overall risk and risk management processes within the Bank. In this context they supervise and monitor the suitability of methods and systems applied by the Banks in order to ensure compliance with the statutory capital adequacy requirements.

Refinancing Lending Committee
The purpose of the operation of the Refinancing Lending Committee is to make the necessary decisions to establish certain terms and conditions of the Bank's refinancing business that will be concluded with a particular partner bank (framework agreement).

Assets and Liabilities Committe
The Assets and Liabilities Committee is exercised its authority on an individual level referring to the Bank.
The Assets and Liabilities Committee is exercised its authority relating to the asset and liability management, liquidity risk management, market risk management, issue and pricing of mortgage bonds and bonds, and categories defined in the internal policies for the Committee.

Risk Control Board
The Risk Control Board is exercised its authority on an individual level referring to the Bank.
The Risk Control Board is exercised its authority relating to operational risk, risk policy / risk strategy, capital management, and categories defined in the internal policies for the Board.

Department of Risk Management is responsible for determining the requirements necessary for the prudent operation. They develop the risk guidelines and manage credit, liquidity, market and operational risk.

Internal Audit

The elements of the internal control system (management control and management information system incorporated in processes, and an independent internal control unit function) cover the Bank's all organizational units and are incorporated in day-to-day operation. They are traceable and provide feedback to the appropriate levels of management and control.

Risk management processes are audited regularly by the internal audit organization that examines both the adequacy of the procedures and the compliance with the procedures. Internal Audit reports its findings to the Supervisory Boards and the Managements of the banks.

Risk evaluation and reporting system

The Bank is measured the risk exposure in accordance with the methods defined in laws and integration policies.

In terms of liquidity as well as interest and exchange rate risks, risks are essentially monitored and controlled by means of setting up limits of acceptable exposure. The limits reflect the willingness to undertake risks, and the market environment. The Bank collects and analyses data about events and losses related to risk from operation. As a result of risk assessment the Bank determines the level of capital justified by the level of acceptable exposure.

The Boards of Directors and The Supervisory Board evaluate the reports on risks on a quarterly basis.

36.3 RISK MITIGATION

Interest rate and exchange rate risks

To minimize the risk of interest- and foreign exchange rate risks the Banks manage their asset and liability structure.

Credit risk

Credit risk is the risk of the Bank suffering losses because the borrowers (clients or partners) fail to meet their contractual obligation to the Bank.

The Bank is suspended the new loan placement activity based on strategy decision during 2018, keep handling the existing loan portfolio. Therethrough the Bank monitors client and partner rating on an ongoing basis.

The Bank rates the creditworthiness of their clients and partners and classifys them into client or partner categories. Risk is only accepted if the client's or partner's rating is appropriate. The Bank monitors client and partner rating on an ongoing basis.

Notes to the Consolidated Financial Statements

Risk taking to retail clients is based on the use of standardized loan schemes and lending processes, resulting in a portfolio characterized by high number of customers, small amounts of individual loans and diversification.
Corporate lending is based on individual assessment and the continuous monitoring is in focus.
The Bank applied strict regulations to determine the scope of eligible collaterals, their valuation method and the coverage ratio.

Maximum credit risk exposure based on gross outstanding balances:

	31 December 2019	31 December 2018
Balances with the National Bank of Hungary	915	2,073
Dues from banks	17,566	61,664
Financial assets at fair value through profit or loss	-	-
Securities at fair value through other comprehensive income	43,734	192,142
Derivative financial assets	2,851	3,962
Refinanced mortgage loans	217,205	105,296
Loans and advances to customers at amortised cost and fair value	58,596	379,489
Other assets	1,621	10,390
Total	**342,488**	**755,016**
Off-balance sheet commitments	18,204	104,859
Total	**18,204**	**104,859**
Total credit risk exposure	**360,692**	**859,875**

36.4 CREDIT RISK

IFRS 9 replaces the rules under IAS 39 for impairment. IFRS 9 is effective for annual periods beginning on or after January 1, 2018. The standard has been endorsed by the European Union (EU).

Impairment

The impairment requirements of IFRS 9 apply to all debt instruments that are measured at amortized cost or FVOCI, and to off balance sheet lending commitments such as loan commitments and financial guarantees (hereafter collectively referred to as “Financial Assets”). This contrasts to the IAS 39 impairment model which was not applicable to loan commitments and financial guarantee contracts, as these were instead covered by International Accounting Standard 37: “Provisions, Contingent Liabilities and Contingent Assets” (IAS 37).

Under IFRS 9, the Bank first evaluates individually the Financial Assets whether objective evidence of impairment exists for loans that are individually significant. It then collectively assesses loans that are not individually significant and loans which are significant but for which there is no objective evidence of impairment available under the individual assessment.

All figures in tables are in HUF million except otherwise noted

Staged Approach to the Determination of Expected Credit Losses

IFRS 9 introduces a three stage approach to impairment for Financial Assets that are performing at the date of origination or purchase. This approach is summarised as follows:

- ***Stage 1***: The Bank recognizes a credit loss allowance at an amount equal to 12-month expected credit losses. This represents the portion of lifetime expected credit losses from default events that are expected within 12 months of the reporting date, assuming that credit risk has not increased significantly after initial recognition.
- ***Stage 2:*** The Bank recognizes a credit loss allowance at an amount equal to lifetime expected credit losses (LTECL) for those Financial Assets which are considered to have experienced a significant increase in credit risk since initial recognition. This requires the computation of ECL based on lifetime probability of default (LTPD) that represents the probability of default occurring over the remaining lifetime of the Financial Asset. Allowance for credit losses are higher in this stage because of an increase in credit risk and the impact of a longer time horizon being considered compared to 12 months in Stage 1.
- ***Stage 3:*** The Bank recognizes a loss allowance at an amount equal to lifetime expected credit losses, reflecting a Probability of Default (PD) of 100 %, via the recoverable cash flows for the asset, for those Financial Assets that are credit-impaired. The Bank definition of default is aligned with the regulatory definition. The treatment of loans in Stage 3 remains substantially the same as the treatment of impaired loans under IAS 39 except for homogeneous portfolios as described below.

Financial Assets that are credit impaired upon initial recognition are categorised purchased or originated credit-impaired (POCI) with a carrying value already reflecting the lifetime expected credit losses. The accounting treatment for these (POCI) assets is discussed further below.

Significant Increase in Credit Risk

Under IFRS 9, when determining whether the credit risk (i.e., risk of default) of a Financial Asset has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes quantitative and qualitative information based on the Bank historical experience, credit risk assessment and forward-looking information (including macro-economic factors). The assessment of significant credit deterioration is key in determining when to move from measuring an allowance based on 12-month ECLs to one that is based on lifetime ECLs (i.e., Stage 1 to Stage 2). The Bank's framework aligns with the internal Credit Risk Management process and covers rating related and process related indicators which are discussed further in the section below on Model Descriptions.

Credit Impaired Financial Assets in Stage 3

The Bank has aligned its definition of credit impaired under IFRS 9 to when a Financial Asset has defaulted for regulatory purposes, according to the Capital Requirements Regulation (CRR) under Art. 178.

Notes to the Consolidated Financial Statements

The determination of whether a Financial Asset is credit impaired focusses exclusively on default risk, without taking into consideration the effects of credit risk mitigants such as collateral or guarantees. Specifically, a Financial Asset is credit impaired and in Stage 3 when:

- The Bank considers the obligor is unlikely to pay its credit obligations. Determination may include forbearance actions, where a concession has been granted to the borrower or economic or legal reasons that are qualitative indicators of credit impairment; or
- Contractual payments of either principal or interest by the obligor are past due by more than 90 days.

For Financial Assets considered to be credit impaired, the ECL allowance covers the amount of loss the Bank is expected to suffer. The estimation of ECLs is done on a case-by-case basis for non-homogeneous portfolios, or by applying portfolio based parameters to individual Financial Assets in these portfolios via the Bank's ECL model for homogeneous portfolios.

Forecasts of future economic conditions when calculating ECLs are considered. The lifetime expected losses are estimated based on the probability-weighted present value of the difference between 1) the contractual cash flows that are due to the Bank under the contract; and 2) the cash flows that the Group expects to receive.

A Financial Asset can be classified as in default but without an allowance for credit losses (i.e., no impairment loss is expected). This may be due to the value of collateral. The Bank's ECL calculation is conducted on a quarterly basis.

Default

The bank uses the CRR definition of default as a primary indicator of loss events. Default, as a loss event occure when:

- the obiligiation is more then 90 days past due on any material credit obligation;
- as a result of specific information or an event, the obligor is unlikely to fulfil its credit obligation in full, without recourse to actions such as realising security;
- the obligor is subject to distressed restructuring, i.e. a change in cotract terms, for the clients in financial difficulties, resulting in a material loss;
- the obligor is subject to bankruptcy or similar protection proceedings

Purchased or Originated Credit Impaired Financial Assets

A Financial Asset is considered purchased or originated credit-impaired if there is objective evidence of impairment at the time of initial recognition (i.e., rated in default by Credit Risk Management). Such defaulted Financial Assets are termed POCI Financial Assets. Typically the purchase price or fair value at origination embeds expectations of lifetime expected credit losses and therefore no separate credit loss allowance is recognised on initial recognition. Subsequently, POCI Financial Assets are measured to reflect lifetime expected credit losses, and all subsequent changes in lifetime expected credit losses, whether positive or negative, are recognised in the income statement as a component of the provision for credit losses.

Notes to the Consolidated Financial Statements

Writte off
Loans and debt securities are written off when the Bank has no reasonable expectations of recovering the financial asset (either in its entirety or a portion of it). This is the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. A write-off constitutes a derecognition event. The Bank may apply enforcement activities to financial assets written off. Recoveries resulting from the Group's enforcement activities will result in impairment gains, which will be presented in Provision for impairment losses in the consolidated statement of Profit or Loss.

Model Descriptions - Expected Credit Loss

Stage Determination

At initial recognition, Financial Assets which are not POCI are reflected in Stage 1. If there is a significant increase in credit risk, the Financial Asset is transferred to Stage 2. Significant increase in credit risk is determined by using rating-related and process- related indicators as discussed below. In contrast, the assignment of a financial instrument to Stage 3 is based on the status of the obligor being in default.

Rating-Related Indicators: Based on a dynamic change in counterparty PDs that is linked to all transactions with the counter- party, the Bank compares lifetime PD at the reporting date, with expectations at the date of initial recognition. Based on historically observed migration behaviour and available forward-looking information, an expected forward rating distribution is obtained. A quantile of this distribution, which is defined for each counterparty class, is chosen as the threshold. If for the remaining lifetime the PD of a transaction given current expectations exceeds the PD of the relevant threshold rating, the Financial Asset is considered as significantly deteriorated. The thresholds used to determine Stage 2 indicators are determined using expert judgment and validated annually.

Process-Related Indicators: Process-related indicators are derived via usage of existing risk management indicators, which allow the Bank to identify whether the credit risk of Financial Assets has significantly increased. These include obligors being added mandatorily to a credit watchlist, being mandatorily transferred to workout status, payments being 30 days or more overdue or in forbearance.

On an ongoing basis, as long as the condition for one or more of the indicators is fulfilled and the Financial Asset is not recognized as defaulted, the asset will remain in Stage 2. If none of the indicator conditions is any longer fulfilled and the Financial Asset is not defaulted, the asset transfers back to Stage 1. In case of a default, the Financial Asset is allocated to Stage 3.

Expected Lifetime model

The expected lifetime of a Financial Asset is a key factor in determining the lifetime expected credit losses. Lifetime expected credit losses represent default events over the expected life of a Financial Asset. The Bank measures expected credit losses considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk.

Retail overdrafts, credit card facilities and certain corporate revolving facilities typically include both a loan and an undrawn commitment component. The expected lifetime of such on-demand facilities exceeds their contractual life as they are typically cancelled only when the Bank becomes aware of an increase in credit risk. The expected lifetime is estimated by taking into consideration historical information and the Bank's Credit Risk Management actions such as credit limit reductions and facility cancellation. Where such facilities are subject to an individual review by Credit Risk Management, the lifetime for calculating expected credit losses.

Notes to the Consolidated Financial Statements

Forward-Looking Information

Under IFRS 9, the allowance for credit losses is based on reasonable and supportable forward looking information obtainable, which takes into consideration past events, current conditions and forecasts of future economic conditions.

To incorporate forward-looking information into allowance for credit losses, the Group uses two key elements: As its base scenario, the Bank uses the macroeconomic forecasts provided by Hunarian National Bank. These forecasts cover a number of macroeconomic variables (e.g., GDP, unemployment rates) and reflect Regulator search's view as to the most likely development of those variables, typically over a two year period and updated quarterly.

This base scenario is then translated into a multiple scenario analysis by leveraging the stress test environment. This environment generates the impact of a multitude of economic scenarios and is used as basis for deriving multi-year PD curves for different rating and counterparty classes, which are applied in the calculation of expected credit losses and in the identification of significant deterioration in credit quality of Financial Assets.

The general use of forward-looking information, including macro-economic factors, as well as adjustments taking into account extraordinary factors, are monitored by the Bank's Risk Management.

Assumptions and the Estimation Techniques

IFRS 9 does not distinguish between individually significant or not individually significant Financial Assets and as such the Bank calculates expected credit losses for each Financial Asset individually. Similarly, the determination of the need to transfer between stages is made on an individual asset basis.

The Bank uses three main components to measure ECL. These are PD, Loss Given Default (LGD) and Exposure at Default (EAD). Incorporating forecasts of future economic conditions into the measurement of expected credit losses influences the allowance for credit losses for each stage. In order to calculate lifetime expected credit losses, the Bank's calculation includes deriving the corresponding lifetime PDs from migration matrices that reflect economic forecasts.

The expected credit loss calculation for stage 3 distinguishes between transactions in homogeneous and non-homogenous port- folios, and purchased or originated credit-impaired transactions. For transactions that are in Stage 3 and in a homogeneous portfolio, a similar approach as for Stage 1 and 2 transactions is taken. Since a Stage 3 transaction is defaulted, the probability of default is equal to 100 %.

Below the estimation techniques for the input factors are described in more detail.

The one-year PD for counterparties is derived from our internal PD model. The Bank assigns a PD to each relevant counterparty credit exposure for our exposure.

The counterparty ratings assigned are derived based on internally developed rating models which specify consistent and distinct customer-relevant criteria and assign a rating grade based on a specific set of criteria as given for a certain customer. The set of criteria is generated from information sets relevant for the respective customer segments including general customer behaviour, financial and external data. The methods in use range from statistical scoring models to expert-based models taking into account the relevant available quantitative and qualitative information. Expert-based models are usually applied for counterparties in the exposure classes "Central governments and central banks ", "Institutions " and "Corporates " with the exception of those "Corporates " segments . For the latter as well as for the retail segment statistical scoring or hybrid models combining both approaches are commonly used. Quantitative rating methodologies are developed based on applicable statistical modelling techniques, such as logistic regression.

One-year PDs are extended to multi-year PD curves using conditional transition matrices. The first step in the estimation process is the calculation of through-the-cycle (TTC) matrices, which are derived from a multi-year rating history. For the next two years, economic forecasts are available. These forecasts are used to transform the TTC matrices into point-in-time (PIT) rating migration matrices.

LGD is defined as the likely loss intensity in case of a counterparty default. It provides an estimation of the exposure that cannot be recovered in a default event and therefore captures the severity of a loss. Conceptually, LGD estimates are independent of a customer’s probability of default. The LGD models ensure that the main drivers for losses (i.e., different levels and quality of collateralization and customer or product types or seniority of facility) are reflected in specific LGD factors. In our LGD models we assign collateral type specific LGD parameters to the collateralized exposure.

The EAD over the lifetime of a Financial Asset is modelled taking into account expected repayment profiles. We apply specific Credit Conversion Factors (CCFs) in order to calculate an EAD value. Conceptually, the EAD is defined as the expected amount of the credit exposure to a counterparty at the time of its default. In instances where a transaction involves an unused limit, a percentage share of this unused limit is added to the outstanding amount in order to appropriately reflect the expected outstanding amount in case of a counterparty default.

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IFRS 9 credit risk tables are presented below.

Gross carrying amount movement table- Balance Sheet - 31 December 2019

Asset type	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	POCI Purchased or originated credit-impaired	Total
Gross carrying amount as at 1 January 2019	**715,497**	**11,047**	**22,495**	**353**	**749,392**
Transfers:					
Transfer from Stage 1 to Stage 2	(818)	741	-	-	(77)
Transfer from Stage 1 to Stage 3	(233)	-	206	-	(27)
Transfer from Stage 2 to Stage 3	-	(242)	235	-	(7)
Transfer from Stage 3 to Stage 2	-	107	(118)	-	(11)
Transfer from Stage 2 to Stage 1	191	(221)	-	-	(30)
Transfer from Stage 3 to Stage 1	419	-	(462)	-	(43)
Changes in EAD	42,672	460	(98)	-	43,034
Financial assets derecognised during the period other than write-offs	(18,115)	(312)	(3,627)	-	(22,054)
New financial assets originated or purchased	18,613	92	-	-	18,705
Termination due to discontinued operations	(429,519)	(4,154)	(15,847)	(353)	(449,873)
Gross carrying amount as at 31 December 2019	**328,707**	**7,518**	**2,784**	**-**	**339,009**

Asset type	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	POCI Purchased or originated credit-impaired	Total
Gross carrying amount as at 1 January 2018	561,349	11,627	30,311	330	603,617
Transfers:					
Transfer from Stage 1 to Stage 2	-	(606)	-	-	(606)
Transfer from Stage 1 to Stage 3	-	-	(722)	-	(722)
Transfer from Stage 2 to Stage 3	-	-	(67)	-	(67)
Transfer from Stage 3 to Stage 2	-	(26)	-	-	(26)
Transfer from Stage 2 to Stage 1	(78)	-	-	-	(78)
Transfer from Stage 3 to Stage 1	19	-	-	-	19
Changes in EAD	(9,831)	(37)	3,065	234	(6,569)
Financial assets derecognised during the period other than write-offs	(184,679)	(231)	(11,311)	(250)	(196,471)
New financial assets originated or purchased	349,636	320	1,399	39	351,394
FX and other movements	(919)	-	(180)	-	(1,099)
Gross carrying amount as at 31 December 2018	**715,497**	**11,047**	**22,495**	**353**	**749,392**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Impairment- Credit risk exposure- Gross carrying amount per asset type, and loss allowance

31 December 2019	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	POCI Purchased or originated credit-impaired	Total
Gross carrying amount per asset type					
Cash on hand	-	-	-	-	-
Investment grade	-	-	-	-	-
Balances with the National Bank of Hungary	915	-	-	-	915
Investment grade	*915*	-	-	-	*915*
Due from banks	17,566	-	-	-	17,566
Investment grade	*17,566*	-	-	-	*17,566*
Securities at fair value through other comprehensive income	43,726	-	-	-	43,726
Investment grade	*43,726*	-	-	-	*43,726*
Securities at amortised cost	999	-	-	-	999
Investment grade	*999*	-	-	-	*999*
Refinanced mortgage loans	217,205	-	-	-	217,205
Investment grade	*217,205*	-	-	-	*217,205*
Retail mortgage loans	*49,375*	*6,650*	*2,784*	-	*58,809*
Investment grade	*46,986*	*5,755*	-	-	*52,752*
Default grade	419	107	2,784	-	3,310
Non-investment grade	*1,959*	*788*	-	-	*2,747*
Corporate mortgage loans	9	-	-	-	9
Investment grade	*9*	-	-	-	-
Default grade	-	-	-	-	-
Non-investment grade	-	-	-	-	-
Total gross carrying amount	329,795	6,650	2,784	-	339,2299
Loss allowance	25	405	560	-	990
Carrying amount	**329,770**	**6,245**	**2,224**	**-**	**338,239**

All figures in tables are in HUF million except otherwise noted

The Notes comprising a summary of significant accounting policies and other explanatory information form an integral part of the Financial Statements

Notes to the Consolidated Financial Statements

Impairment- Credit risk exposure- Gross carrying amount per asset type, and loss allowance

31 December 2018	Stage 1	Stage 2	Stage 3	POCI	Total
	12-month ECL	Lifetime ECL	Lifetime ECL	Purchased or originated credit-impaired	
Gross carrying amount per asset type					
Cash on hand	3,157	-	-	-	3,157
Investment grade	*3,157*	-	-	-	*3,157*
Balances with the National Bank of Hungary	2,073	-	-	-	2,073
Investment grade	*2,073*	-	-	-	*2,073*
Due from banks	61,679	-	-	-	61,679
Investment grade	*61,679*	-	-	-	*61,679*
Securities at fair value through other comprehensive income	192,142	-	-	-	192,142
Investment grade	*192,142*	-	-	-	*192,142*
Refinanced mortgage loans	105,296	-	-	-	105,296
Investment grade	*105,296*	-	-	-	*105,296*
Retail mortgage loans	169,738	10,646	11,756	292	192,432
Investment grade	*680*	*5,518*	-	-	*6,198*
Default grade	-	-	*11,756*	*292*	*12,048*
Non-investment grade	*169,058*	*5,128*	-	-	*174,186*
Retail other loans	34,836	295	3,465	61	38,657
Investment grade	*26,107*	*239*	-	-	*26,346*
Default grade	-	-	*3,465*	*61*	*3,526*
Non-investment grade	*8,729*	*56*	-	-	*8,785*
Corporate mortgage loans	36,030	106	4,701	-	40,837
Investment grade	*36,030*	*106*	-	-	*36,136*
Default grade	-	-	*4,701*	-	*4,701*
Corporate other loans	110,546	-	2,573	-	113,119
Investment grade	*25,208*	-	-	-	*25,208*
Default grade	-	-	*2,573*	-	*2,573*
Non-investment grade	*85,338*	-	-	-	*85,338*
Total gross carrying amount	**715,497**	**11,047**	**22,495**	**353**	**749,392**
Loss allowance	1,411	679	10,326	229	12,645
Carrying amount	**714,086**	**10,368**	**12,169**	**124**	**736,747**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Impairment movement table

Asset type	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	POCI Purchased or originated credit-impaired	Total
Impairment loss as at 1 January 2019	**1,411**	**679**	**10,326**	**229**	**12,645**
Movements with P&L impact					
Transfers:					
Transfers from Stage 1 to Stage 2	(24)	116	-	-	92
Transfers from Stage 1 to Stage 3	(31)	-	693	-	662
Transfers from Stage 2 to Stage 1	17	(122)	-	-	(105)
Transfers from Stage 3 to Stage 1	55	-	(1,100)	-	(1,045)
Transfers from Stage 3 to Stage 2	-	12	(38)	-	(26)
Transfers from Stage 2 to Stage 3	-	(63)	137	-	74
New financial assets originated or purchased	608	8	-	-	616
Changes in PDs/LGDs/EADs	1,269	(66)	(199)	(229)	775
FX and other movements	-	-	-	-	-
Other movements with no P&L impact					
Financial assets derecognised during the period other than write-offs	(313)	0	(4,595)	-	(4,908)
Termination due to discontinued operations	(2,967)	(159)	(4,664)	-	(7,790)
Impairment loss as at 31 December 2019	**25**	**405**	**560**	**-**	**990**

Asset type	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	POCI Purchased or originated credit-impaired	Total
Impairment loss as at 1 January 2018	**2,680**	**318**	**14,693**	**109**	**17,800**
Movements with P&L impact					
Transfers:					
Transfers from Stage 1 to Stage 2	-	503	-	-	503
Transfers from Stage 1 to Stage 3	-	-	1,561	-	1,561
Transfers from Stage 2 to Stage 1	(122)	-	-	-	(122)
Transfers from Stage 3 to Stage 1	(795)	-	-	-	(795)
Transfers from Stage 3 to Stage 2	-	(99)	-	-	(99)
Transfers from Stage 2 to Stage 3	-	-	34	-	34
New financial assets originated or purchased	365	13	640	28	1,046
Changes in PDs/LGDs/EADs	(420)	(23)	(710)	177	(976)
FX and other movements	(13)	-	748	-	735
Other movements with no P&L impact					
Financial assets derecognised during the period other than write-offs	(284)	(33)	(6,640)	(85)	(7,042)
Impairment loss as at 31 December 2018	**1,411**	**679**	**10,326**	**229**	**12,645**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Provision movement table

Asset type	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
Provision as at 1 January 2019	**1,154**	**9**	**104**	**1,267**
Movements with P&L impact				
Transfers:				
Transfers from Stage 1 to Stage 2	-	-	-	-
Transfers from Stage 1 to Stage 3	-	-	3	3
Transfers from Stage 2 to Stage 1	-	(1)	-	(1)
Transfers from Stage 3 to Stage 1	-	-	(1)	(1)
Transfers from Stage 3 to Stage 2	4	-	(38)	(34)
New financial assets originated or purchased	1,042	-	-	1,042
Changes in PDs/LGDs/EADs	(226)	(5)	(31)	(262)
Other movements with no P&L impact				
Financial assets derecognised during the period other than write-offs	(47)	-	(29)	(76)
Termination due to discontinued operations	(1,926)	(2)	(7)	(1,935)
Impairment loss as at 31 December 2019	**1**	**1**	**1**	**3**

Asset type	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
Provision as at 1 January 2018	**750**	**11**	**91**	**852**
Movements with P&L impact				
Transfers:				
Transfers from Stage 1 to Stage 2		6	-	6
Transfers from Stage 1 to Stage 3	(2)	-	39	37
Transfers from Stage 2 to Stage 1	(2)	-	-	(2)
Transfers from Stage 3 to Stage 1	(21)	-	-	(21)
Transfers from Stage 3 to Stage 2	-	(6)	-	(6)
New financial assets originated or purchased	790	1	41	832
Changes in PDs/LGDs/EADs	97	(1)	(40)	56
Other movements with no P&L impact				
Financial assets derecognised during the period other than write-offs	(458)	(2)	(27)	(487)
Impairment loss as at 31 December 2018	**1,154**	**9**	**104**	**1,267**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Exposure to credit risk on loan commitments and financial guarantees

31 December 2019	Stage 1	Stage 2	Stage 3	POCI	Total
	12-month ECL	Lifetime ECL	Lifetime ECL	Purchased or originated credit-impaired	
Loan commitment	470	4	64	-	538
Bank guarantees	-	-	-	-	-
Total exposure	**470**	**4**	**64**	**-**	**538**

31 December 2018	Stage 1	Stage 2	Stage 3	POCI	Total
	12-month ECL	Lifetime ECL	Lifetime ECL	Purchased or originated credit-impaired	
Loan commitment	98,967	146	333	-	99,446
Bank guarantees	5,378	-	35	-	5,413
Total exposure	**104,345**	**146**	**368**	**-**	**104,859**

Impairment

31 December 2019	Gross exposure	Impairment allowance	Carrying amount
Credit-impaired assets (stage 3)			
Retail mortgage loans	1,938	281	1,657
Retail other loans	846	279	567
Total credit-impaired assets	**2,784**	**560**	**2,224**

All figures in tables are in HUF million except otherwise noted

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Lending risk exposure of the Bank in terms of internal risk classification

Class	Historic default rate 31.12.2018 (%)	Uncovered 31.12.2018 HUF million	Total 31.12.2018 HUF million
Class 1	0.00	182,678	182,678
Class 2	0.00	1,094	1,094
Class 3	0.00	8,527	10,335
Class 4	0.27	20,344	109,819
Class 5-7	3.38	105,075	224,394

The table shows the Bank gross outstanding loans portfolio (dues from banks, refinanced mortgage loans and other mortgage and unsecured loans and bonds).
In the calculation of risk capital, in accordance with its internal risk management policy, the Bank classifies its loan portfolio and its weighted off-balance items in different rating categories. Consolidated data based on the International Financial Reporting Standards (IFRS) are used in the classification. Retail customers are rated into seventeen categories (classes). Other partners (mainly credit institutions) are rated into seven categories. The classes are determined based on customer rating policy. The Bank consolidated the two sets of classes in the above table, in this way the historical default rates of the entire portfolio are combined and broken down in terms of rating classes.
The classification of credit assets into risk grades is based on Takarék Group's internal rating system. Internal rating models and risk parameters are developed by internal specialist team. Rating development follows internal methodology, which is controlled continuously by the Internal Audit as well as by the supervisory authorities.
The Bank applies different rating scales in different segments, but applies a standardized framework for external reporting, which is mapping the risk classes to the following categories.

Class 1: In practice, only risk-free exposures, governments fall into this category

Class 2: includes first class, nearly risk-free institutional (bank) exposures, which estimated default rate is close to zero. These institutions have typically high (AA) rating from well-known credit rating institutions.

Class 3: includes institutional (bank) low risk exposures, which are not included in previous classes, and their estimated average PD is very low. They are also financially strong, reputed financial institutions that have a good rating.

Class 4:
In this category are included the best qualified retail and corporate customers which default rate is low. These customers have excellent credit history, and a balanced business management (in case of companies).
In case of institutional exposures those exposures which are not included in previous classes and their estimated default rate are low have to be classified to this category.

Class 5-7:
All exposures which are not included in classes 1-4, have to be classified to this category.

36.4.1 Forborne loans

Forbearance measures occur in situations in which the contract – receivable is originated from – is modified on the debtor or the Group's initiative, basically based on the fact that the borrower is considered to be unable to service the debt or refinance the contract according to the original terms and conditions because of the debtor's financial difficulties and significant deterioration of ability to pay.
Furthermore buffer account loans granted within the framework of the FX rate protection scheme are qualified as forborne as loans, as well as ones concerning to the buffer account loan has been opened.

In comparison with the original term and conditions, essentially more favourable conditions are arising for clients by modification of contract.
Modifications of the terms and conditions can be the following:

- rescheduling the payment
- modification of foreign exchange
- forbearing from collaterals
- capitalization of interest

Rating of forborne loans:

1. If the loans are classified as forborne loans the classification category can not be better than it was before.
2. The forborne loans are classified as "to-be- monitored" if the original loan was classified as "problem-free" or "to-be- monitored" and following the forbearance, the number of days past due did not exceed 15 days in case of corporate loans or 30 days in case of retail loan, respectively, during 180 days without break.
3. The forborne loans are possible to be classified as "problem free" after one year of the forbearance if the number of days past due did not exceed 15 days in case of corporate loans or 30 days in case of retail loan, respectively, during 365 days without break.

An analysis of forborne gross loan portfolio by loan types as 31 December 2019 and 2018

Loan type	31 December 2019	31 December 2018
Individual loans	2,830	13,562
Fx rate protection scheme (original loan)	680	3,430
Fx rate protection scheme (buffer account)	29	305
Corporate loans	343	611
Total	**3,173**	**14,173**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

An analysis of impaired forborne loan portfolio by loan types as 31 December 2019 and 2018

Loan type	31 December 2019	31 December 2018
Individual loans	708	13,562
Fx rate protection scheme (original loan)	97	3,430
Fx rate protection scheme (buffer account)	7	305
Corporate loans	343	611
Total	**1,051**	**14,173**

An analysis of forborne loan portfolio by loan types and risk classes as 31 December 2019

Loan type	Not past due	1-30 DPD	31-60 DPD	61-90 DPD	91-360 DPD	360+DPD	Total
Individual loans	1,834	331	111	69	173	312	2,830
allowance	*11*	*4*	*2*	*3*	*16*	*62*	*98*
Corporate loans	342	0	0	0	0	0	342
allowance	*39*	*0*	*0*	*0*	*0*	*0*	*39*
Total capital of loans	**2,176**	**331**	**111**	**69**	**173**	**312**	**3,172**
Total allowance	***50***	***4***	***2***	***3***	***16***	***62***	***137***

** the table shows just the multiple-forborne loans*

An analysis of forborne loan portfolio by loan types and risk classes as 31 December 2018

Loan type	Not past due	1-30 DPD	31-60 DPD	61-90 DPD	91-360 DPD	360+DPD	Total
Individual loans	7,280	1,139	384	293	544	3,922	13,562
allowance	*145*	*104*	*43*	*49*	*158*	*1,970*	*2,469*
Corporate loans	478	-	-	-	-	133	611
allowance	*56*	-	-	-	-	*115*	*171*
Total capital of loans	**7,758**	**1,139**	**384**	**293**	**544**	**4,055**	**14,173**
Total allowance	***201***	***104***	***43***	***49***	***158***	***2,085***	***2,640***

** the table shows just the multiple-forborne loans*

All figures in tables are in HUF million except otherwise noted

An analysis of forborne loan portfolio impaired and not impaired by loan types and risk classes as 31 December 2019

Loan type	Not past due			Past due			Total
	Impaired	Not impaired	Total	Impaired	Not impaired	Total	
Individual loans	199	1,703	1,902	509	419	928	2,830
allowance	*8*	*8*	*16*	*89*	*13*	*102*	*118*
collateral	-	-	-	-	-	-	-
Corporate loans	343	-	343	-	-	-	343
allowance	*39*	-	*39*	-	-	-	*39*
collateral	-	-	-	-	-	-	-
Total capital of loans	**542**	**1,703**	**2,245**	**509**	**419**	**928**	**3,173**
Total allowance	***48***	***8***	***55***	***89***	***13***	***102***	***157***
Total collateral	-	-	-	-	-	-	-

** the table shows just the multiple-forborne loans*

An analysis of forborne loan portfolio impaired and not impaired by loan types and risk classes as 31 December 2018

Loan type	Not past due			Past due			Total
	Impaired	Not impaired	Total	Impaired	Not impaired	Total	
Individual loans	7,280	-	7,280	6,282	-	6,282	13,562
allowance	*145*	-	*145*	*2,324*	-	*2,324*	*2,469*
collateral	*13,352*	*5*	*13,357*	*7,342*	-	*7,342*	*20,699*
Corporate loans	478	-	478	133	-	133	611
allowance	*56*	-	*56*	*115*	-	*115*	*171*
collateral	*981*	-	*981*	*21*	-	*21*	*1,002*
Total capital of loans	**7,758**	-	**7,758**	**6,415**	-	**6,415**	**14,173**
Total allowance	***201***	-	***201***	***2,439***	-	***2,439***	***2,640***
Total collateral	***14,333***	***5***	***14,338***	***7,363***	-	***7,363***	***21,701***

** the table shows just the multiple-forborne loans*

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

An analysis of forborne loan portfolio by type of forbearance as 31 December 2019 and 31 December 2018

	31 December 2019		31 December 2018	
	capital	allowance	capital	allowance
Retail loans	2,830	98	13,562	2,469
bridge loan	*1,310*	*59*	7,995	1,669
Fx rate protection scheme (original loan)	*680*	*12*	3,430	467
Fx rate protection scheme (buffer account)	*29*	*1*	305	34
Fx housing loan converted to HUF	*75*	*5*	307	99
other	737	21	1,525	199
Corporate loans	343	39	611	171
Total	**3,173**	**137**	**14,173**	**2,640**

Changes in impairment of forborne loan portfolio

	31 December 2019
Impairment as at 1 January	472
Provision for impairment in the period	15
Reverse of impairment for the period	(82)
Derecognition due to sale of assets	(268)
Impairment as at end of period	**137**

Changes in impairment of forborne loan portfolio

	31 December 2018
Impairment as at 1 January	7,152
Provision for impairment in the period	214
Reverse of impairment for the period	(416)
Derecognition due to sale of assets	(4,310)
Impairment as at end of period	**2,640**

All figures in tables are in HUF million except otherwise noted

36.4.2 COLLATERALS AND OTHER MEANS FOR IMPROVING THE LOANS PORTFOLIO

Collaterals for lending risk applied by the Bank:

Real estate
The Takarék Mortgage Bank Plc. accepts as collateral mortgages, independent or separated liens established on such real estate that is registered in Hungary and have long live stable value.
Real estate is valued by independent appraisers who are not involved in decision-making regarding the loan and who establish the collateral value conservatively.

State guarantee
All instances of State guarantee accepted by the Banks involve joint and several liability set forth by law. The rules governing the guarantee are laid down in statutory provisions.

Deposit
Deposit can take the form of cash, bank deposit or securities.

Other
In addition to the above the Banks also accept joint and several guarantee by third party (where the third party is other than the Hungarian State), assigned claims, lien on claims.

The table below shows the structure of the collaterals in 2019 and 2018:

	31 December 2019	31 December 2018
Mortgage	719,055	837,126
Bail	12	16,392
Guarantee	14,158	7,447
Other collaterals	-	1,938
Total	**733,225**	**862,903**

The above detailed collaterals cover fully the amount of the loans and refinanced mortgage loans.

Among the collaterals the value of mortgage represents the collateral value allocated to the mortgage at disbursement (market value less discount factor) in case of Customer loans. In case of refinanced mortgage loans, mortgage is the lower of the collateral value or the receivable. All other items are valued at their own value (for example the assignment is valued at the amount which was assigned). The category of other collaterals contains the insurances.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

36.5 MARKET RISK

Takarék Mortgage Bank Plc. maintains low the maturity-, interest rate- and foreign exchange rate risk derive from the asset, liability and off balance sheet commitments.

36.6 INTEREST RATE RISK

Interest rate risk derives from interest rate changes, which affect the value of financial instruments. A bank is also exposed to interest rate risk when the amounts of assets, liabilities and off-balance sheet instruments maturing or re-priced in a particular period are not in harmony. The Bank assess interest rate risk on a continuous basis with the help of Gap-analysis, VaR calculations and sensitivity analysis. The Bank manages market risk mainly by natural hedging. In addition, active management tools such as repurchase of mortgage bonds, swap transactions as well as issued bonds maturities and interest rates suited to assets are also involved in order to ensure the harmony between assets and liabilities.

Average portfolio of interest earning assets and interest bearing liabilities of the Group in the period:

	31 December 2019		31 December 2018	
	Average net A/L	Average interest rate %	Average net A/L	Average interest rate %
Interest earning assets				
Dues from banks and Balances with the National Bank of Hungary	1,192	0.04	43,239	1.17
Securities at fair value through profit or loss and at fair value through other comprehensive income	41,520	1.98	32,513	1.53
Refinanced mortgage loans	193,106	1.86	91,842	2.60
Loans and advances to customers at amortised cost and fair value	82,164	5.08	315,331	5.24
Total interest earning assets	**317,982**	**2.7**	**482,925**	**4.12**
Interest bearing liabilities				
Due to banks	8,264	0.01	34,505	0.14
Deposits	-	-	278,384	0.16
Issued securities and Financial liabilities at fair value through profit or loss, except derivatives	263,873	3.54	189,307	3.57
Total interest bearing liabilities	**272,137**	**3.43**	**502,196**	**1.44**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Interest rate risk exposure – sensitivity analysis (figures in HUF million)

	Sensitivity of interest income 2019	Sensitivity of interest income 2018	Sensitivity of interest income (2019) +10 bp	Sensitivity of interest income (2019) +25bp
HUF	(11)	6	(109)	(273)
EUR	1	(1)	14	36
CHF	-	-	-	-

The sensitivity analysis is performed according to the standard method of using 1 base point increase in interest rates, the excursion is symmetric meaning 1 base point decrease in interest rates would result in the same figures with opposite sign.

Sensitivity of net income is the estimated effect of one base point increase in interest rates to net interest income realized in advance over a period of one year, based on floating rate financial assets and liabilities or those financial assets and liabilities to be re-priced next year carried as of the last day of the given year. It means that if interest increase by one basis point from the close of business 31 December 2019 net interest income would increase by HUF 190 million in case of HUF, it would increase by HUF 14 million in case of EUR.

36.7 EXCHANGE RATE RISK MANAGEMENT

The Mortgage Bank is a specialized credit institution, which narrows the scope of business where exchange rate-related risks may arise. Moreover, the business policy of the Banks is to keep exchange rate risk at a low level.

The Banks strive to immediately hedge the exchange risks related to its core business as allowed by market circumstances. Therefore an open FX position can serve primarily for the purpose of liquidity management, settlements related to lending and refinancing, or active and passive accruals.

FX risk (in the case of 1% increase in exchange rate) in HUF hundred

FX	Effect on earning before income tax (31 December 2019)	Effect on capital (31 December 2019)	Effect on earning before income tax (31 December 2018)	Effect on capital (31 December 2018)
EUR	(850)	(850)	(2,610)	(2,610)
CHF	(110)	(110)	(10)	(10)

Notes to the Consolidated Financial Statements

The sensitivity analysis is performed according to the standard method of using 1% increase in foreign exchange rates, the excursion is symmetric meaning 1% decrease in foreign exchange rates would result in the same figures with opposite sign.

Due to the Bank's currency position 1 percent increase in the exchange rate in case of EUR items the estimated net earnings before tax could decrease with 850 hundred HUF, in case of CHF items it could decrease with 110 hundred HUF. The similar effect for the capital could mean an decrease of 850 hundred HUF in case of EUR items and 110 hundred HUF decrease in case of CHF items. (The sensitivity of the equity means the re-evaluation of the all-currency financial assets and the off-balance sheet positions.)

Consolidated FX financial position of the group in terms of main currencies:

31 December 2019	CHF	EUR	HUF	Total
Assets				
Balances with the National Bank of Hungary	-	-	915	915
Due from Banks	48	5,310	12,208	17,566
Securities at fair value through other comprehensive income	-	-	43,734	43,734
Derivative financial assets	-	(2)	2,853	2,851
Securities at amortised cos	-	-	999	999
Refinanced mortgage loans	-	4,669	212,536	217,205
Loans and advances to customers at amortised cost and	400	-	57,428	57,828
Tangible assets	-	-	157	157
Goodwill and other intangibles	-	-	241	241
Other assets	-	68	1,333	1,401
Total assets	**448**	**10,045**	**332,404**	**342,897**
Nominal values of derivative	-	-	49,650	49,650
Total assets incl. derivatives	**448**	**10,045**	**382,054**	**392,547**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

31 December 2019	CHF	EUR	HUF	Total
Liabilities				
Due to banks	457	1,176	1,486	3,119
Derivative financial liabilities	-	-	423	423
Issued securities	-	-	265,929	265,929
Financial liabilities at fair value through profit or loss, except derivatives	-	6,552	-	6,552
Leasing liability	-	70	-	70
Current tax liability	-	-	93	93
Provisions	-	-	509	509
Other liabilities	2	-	1,157	1,159
Total liabilities	**459**	**7,798**	**269,597**	**277,854**

31 December 2019	CHF	EUR	HUF	Total
Shareholders' equity	**-**	**-**	**65,043**	**65,043**
Total liabilities and shareholders' equity	**459**	**7,798**	**334,640**	**342,897**
Nominal values of derivative liabilities	-	-	4,799	4,799
Total liabilities incl. derivatives	**459**	**7,798**	**339,439**	**347,696**
Position	11	(2,247)	(42,615)	(44,851)

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

31 December 2018	CHF	EUR	HUF	Total
Assets				
Cash on hand	47	405	2,705	3,157
Balances with the National Bank of Hungary	-	-	2,073	2,073
Due from Banks	163	15,049	46,452	61,664
Securities at fair value through other comprehensive income	-	11,693	180,449	192,142
Derivative financial assets	-	-	3,962	3,962
Refinanced mortgage loans	-	-	105,296	105,296
Loans and advances to customers at amortised cost and fair value	1,381	43,192	328,021	372,594
Investment property	-	-	-	-
Tangible assets	-	-	2,171	2,171
Goodwill and other intangibles	-	-	388	388
Deferred tax asset	-	-	679	679
Other assets	-	575	9,815	10,390
Total assets	**1,591**	**70,914**	**682,011**	**754,516**
Nominal values of derivative assets	-	949	239	1,188
Total assets incl. derivatives	**1,591**	**71,863**	**682,250**	**755,704**

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

31 December 2018	CHF	EUR	HUF	Total
Liabilities				
Due to banks	1,283	5,069	150,307	156,659
Deposits	328	53,834	250,171	304,333
Derivative financial liabilities	-	-	2,371	2,371
Issued securities	-	2,491	211,898	214,389
Financial liabilities at fair value through profit or loss, except	-	6,693	-	6,693
Leasing liability	-	-	-	-
Current tax liability	-	-	-	-
Deferred tax liability	-	-	-	-
Provisions	-	-	3,988	3,988
Other liabilities	-	1,208	9,639	10,847
Total liabilities	**1,611**	**69,295**	**628,374**	**699,280**

31 December 2018	CHF	EUR	HUF	Total
Shareholders' equity	**-**	**-**	**55,236**	**55,236**
Total liabilities and shareholders' equity	**1,611**	**69,295**	**683,610**	**754,516**
Nominal values of derivative liabilities	-	125	1,044	1,169
Total liabilities incl. derivatives	**1,611**	**69,420**	**684,654**	**755,685**
Position	20	(2,443)	2,404	(19)

36.8 LIQUIDITY AND MATURITY RISK

Liquidity risk is defined as the risk that the Bank will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Maintaining liquidity is an essential element of banking, which can be ensured by coordinating the maturity of receivables and payables. At the same time, the Bank applys maturity transformation regulated by limits in order to improve profitability while maintaining solvency at all times.
The Banks regularly review prepayments by clients prior to term and takes into consideration their impact in managing market and liquidity risks.

The Bank prepares their liquidity plans and financing position based on different scenarios, also including effects coming from stress tests. The Bank maintains a high level of liquid asset portfolio consisting of mainly government securities and deposits with MTB.
Off-balance sheet liabilities are presented at their latest date to be drawn (contractual maturity) in the table below. They would be presented in the first category if their earliest date to be drawn were to be taken.

All figures in tables are in HUF million except otherwise noted

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Contractual maturities of undiscounted cash flows of financial liabilities as of 31 December 2019

	On demand	Within 3 months	3 - 12 months	1 –5 years	5 – 10 years	10 – 15 years	Total
Banking liabilities							
Due to banks	-	3,119	-	-	-	-	3,119
Deposits	-	-	-	-	-	-	-
Derivative financial liabilities	-		423			-	423
Issued securities	-	5,219	30,069	196,436	34,205	-	265,929
Financial liabilities at fair value through profit or loss, except derivatives	-	591	-	5,961	-	-	6,552
Off balance sheet commitments	180	110	-	4	64	18,026	18,204
Total banking liabilities	**180**	**9,033**	**30,102**	**196,489**	**34,269**	**18,026**	**288,099**

	On demand	Within 3 months	3 - 12 months	1 –5 years	5 – 10 years	10 – 15 years	Total
Receivables from derivatives	-	24,961	832	5,946	1,641	-	33,380
Liabilities from derivatives	-	(24,503)	(442)	(4,973)	(1,503)	-	(31,421)
Net value of derivatives	**-**	**458**	**390**	**973**	**138**	**-**	**1,959**

In the table, the undiscounted interest cash flows includes not only the accrued interest but also the interest payments in the given period.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Contractual maturities of undiscounted cash flows of financial liabilities as of 31 December 2018

	On demand	Within 3 months	3 - 12 months	1 –5 years	5 – 10 years	10 – 15 years	Total
Banking liabilities							
Due to banks	4,029	135,106	331	11,452	5,741	-	156,659
Deposits	198,505	84,230	20,615	983	-	-	304,333
Derivative financial liabilities	-	115	28	664	1,564	-	2,371
Issued securities	-	637	26,707	149,087	60,156	-	236,587
Financial liabilities at fair value through profit or loss, except derivatives	-	259	-	6,434	-	-	6,693
Off balance sheet commitments	3,169	3,667	38,306	59,393	271	53	104,859
Total banking liabilities	**205,703**	**224,014**	**85,987**	**228,013**	**67,732**	**53**	**811,502**

	On demand	Within 3 months	3 - 12 months	1 –5 years	5 – 10 years	10 – 15 years	Total
Receivables from derivatives	-	418	1,399	6,101	3,120	-	11,038
Liabilities from derivatives	-	2,457	1,349	4,490	1,262	-	9,558
Net value of derivatives	**-**	**(2,039)**	**50**	**1,611**	**1,858**	**-**	**1,480**

In the table, the undiscounted interest cash flows includes not only the accrued interest but also the interest payments in the given period.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

The liability structure is managed by the Bank in the following ways:

- in accordance with the possibilities (demand) of the Hungarian mortgage bond market the Bank is aiming to maximize the maturity of its issued mortgage bonds;
- concentration of the maturity of the mortgage bonds is restricted by limits set in the Bank's internal regulations;
- the Bank is an active player of the mortgage bond markets (repurchasing bonds issued by the Bank).

The table above shows an age analysis of the Bank's liabilities based on the remaining maturity calculated from the balance sheet date. The mortgage bonds and bonds issued by the Bank are presented at actual due principal amounts and increased by the interest payments expected to be paid disclosed in the related information memoranda and programs and are not affected by exchange rate gains and losses or by any valuation difference arising on derivatives. In practice, the maturity of liabilities may depart from the contracted terms.

Maturity analysis of assets and liabilities as of 31 December 2019

	Less than 12 months	Over 12 months
Assets		
Cash on hand	-	-
Balances with the National Bank of Hungary	915	-
Due from banks	17,566	-
Securities at fair value through other comprehensive income	-	43,734
Derivative financial assets	2,851	-
Securities at amortised cost	-	999
Refinanced mortgage loans	16,463	200,742
Loans and advances to customers at amortised cost and fair value	11,590	46,238
Tangible assets	-	157
Intangible assets	-	241
Other assets	1,152	250
Total assets	**50,537**	**292,360**

All figures in tables are in HUF million except otherwise noted

	Less than 12 months	Over 12 months
Liabilities		
Due to banks	3,119	-
Derivative financial liabilities	423	-
Issued securities	35,288	230,641
Financial liabilities at fair value through profit or loss, except derivatives	591	5,961
Lease liability	21	49
Current tax liability	-	93
Provisions	9	500
Other liabilities	568	591
Total liabilities	**40,019**	**237,835**

Maturity analysis of assets and liabilities as of 31 December 2018

	Less than 12 months	Over 12 months
Assets		
Cash on hand	3,157	-
Balances with the National Bank of Hungary	2,073	-
Due from banks	6,546	55,118
Securities at fair value through profit or loss	-	-
Securities at fair value through other comprehensive income	38,546	153,596
Derivative financial assets	121	3,841
Refinanced mortgage loans	9,191	96,105
Loans and advances to customers	39,555	333,039
Tangible assets	-	2,171
Goodwill and other intangible assets	-	388
Deferred tax assets	-	679
Other assets	10,390	-
Total assets	**109,579**	**644,937**

All figures in tables are in HUF million except otherwise noted

	Less than 12 months	Over 12 months
Liabilities		
Due to banks	139,466	17,193
Deposits from customers	303,350	983
Derivative financial liabilities	143	2,228
Issued securities	27,344	187,045
Financial liabilities at fair value through profit or loss, except derivatives	259	6,434
Provisions	3,988	-
Other liabilities	10,847	-
Total liabilities	**485,397**	**213,883**

The members of Integration Organisation of Cooperative Credit Institution (SZHISZ) should – with regard to the several responsibility system of the Integration – examine the prudential requirements on consolidation bases. The exemption of individual compliance is ensured for the members of SZHISZ by the relevant statutory and resolution of the National Bank of Hungary. The Takarék Mortgage Bank Ltd is member of the SZHISZ, as a result above exemption also applies to them, according to this the individual liquidity ratios (LCR and NSFR) are not published in the separate final statements.
According to this in the next table includes the liquidity ratio of the whole members of Integration Organisation of Cooperative Credit Institution.:

	31 December 2019	31 December 2018
LCR (liquidity coverage ratio)	134.05%	192.11%
NSFR (net stable funding ratio)	136.79%	111.32%

36.9 MANAGEMENT OF OPERATIONAL RISK

Operational risk is managed primarily by improving internal rules and regulations, training of staff involved in the various processes, and further enhancement of built-in control mechanisms. The exploration and measurement of the risks is performed by the Bank through the collection of the data of the operational risk events and losses, the monitoring of Key Risk Indicators and the implementation of risk self-assessment. The Bank's management considers feedback to be particularly important in terms of operations-related risk management, as this is the tool to check the effectiveness of measures taken to eliminate risks.

All figures in tables are in HUF million except otherwise noted

36.10 TREATMENT OF RISK CONCENTRATION

The Banks are significantly exposed to the status of real estate market regarding the high proportion of real estate in securities. This concentration risk is mitigated by applying conservative method in collateral values and cover rate and also by diversifying their product portfolio from collateral perspective (meaning to increase the proportion of other than real estate securities). Taking risk in corporate segment can do in compliance with the sectoral limits.

37 CALCULATION OF REGULATORY CAPITAL, CAPITAL ADEQUACY AND ROAE

The calculation of regulatory capital based on the Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 the cash flow security reserve should be ignored, thus ensuring the soundness of the comparison with previous periods.
The Group applied (a) the IRB (Internal Rating Based) method for credit risk from 1 July 2008 and (b) the AMA (Advanced Measurement Method) for operational risk from 31 December 2011 regarding the calculation of capital requirements. The National Bank of Hungary at the application of MTB Magyar Takarékszövetkezeti Bank Zrt. permitted to Takarék Mortgage Bank and Takarék Commercial Bank to use the same approaches applied by the members of Integration, namely the standard method for credit risk and BIA (Basic Indicator Approach) for operational risk from 30 June 2018.

According to the resolution no. H-EN-I-36./2017 (on 1 January 2017) the National Bank of Hungary – with the acceptance of application provided by SZHISZ, MTB Magyar Takarékszövetkezeti Bank Zrt., and Takarék Mortgage Bank - authorized Takarék to apply individual exemption and terminated the obligation for compliance with sub-consolidated level requirements.
The members of Integration Organisation of Cooperative Credit Institution (SZHISZ) should – with regard to the several responsibility system of the Integration – examine the prudential requirements on consolidation bases. The exemption of individual compliance is ensured for the members of SZHISZ by the relevant statutory and resolution of the National Bank of Hungary. The Takarék Mortgage Bank Ltd and the Takarék Commercial Bank Ltd are members of the SZHISZ, as a result above exemption also applies to them.
According to this in the next table the regulatory capital of the members of Integration Organisation of Cooperative Credit Institution includes the following elements: share capital – repurchased treasury shares + share premium + general reserve + share option reserve + retained earnings – intangible assets.

	31 December 2019	31 December 2018
Own Funds	251,451	233,499
TIER 1 Capital	251,451	233,499
Common Equity TIER 1 Capital	251,451	233,499

	31 December 2019	31 December 2018
ROAE (return on average equity %)	1.7	6.3

38 RELATED PARTY TRANSACTIONS

For the purpose of the financial statements, Group identified related parties based on definition of IAS 24 including all the enterprises that directly or indirectly through one or more intermediaries are controlled by

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

the reporting enterprise (this includes parents and subsidiaries) and key management personnel, including the member of the Board and Supervisory Board. For the purposes of this Report, related parties also include shareholders whose holding in the Bank exceeds 10% (from 14.10.2016. Fókusz Takarékszövetkezet, and from 09.12.2016. MTB Magyar Takarékszövetkezeti Bank Zrt. Related parties have the power of control over or have a significant influence in, decisions relating to the finances and operation of another enterprise. The Group enters into transactions with related parties under market conditions.

The satellite financial entities of the Takarék Group, including the fund management, the leasing and factoring services and the centralized debt collection were taken over in December 2017 by the MTB Magyar Takarékszövetkezeti Bank Zrt., see notes 17.
The list of the related parties, -including the subsidiaries and joint ventures (joint control with Hungarian Post Ltd.) and associates of the MTB Magyar Takarékszövetkezeti Bank Zrt. as at 31 December 2019 is the following:

Companies included in the consolidation*	Main shareholder***	Core business
Bóly és Vidéke Takarékszövetkezet	MTB Magyar Takarékszövetkezeti Bank Zrt. 0%	Savings Cooperative
Takarék Real Estate Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 100%	Real estate valuation services, real estate agency and sales
Takarék INVEST Befektetési és Ingatlankezelő Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 100%	Own property management, leasing, and operating , facility management
Diófa Alapkezelő Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 88.29%	Fund and property management
Takarék Lízing Ltd.	Takarék INVEST Befektetési és Ingatlankezelő Ltd. 100%	Lending and leasing
Central European Credit d.d. (Croatia)	Takarék Lízing Ltd. 100%	Lending
Diófa Ingatlankezelő Ltd.	Diófa Alapkezelő Ltd. Ltd. 100%	Real estate management
Diófa TM1 Ingatlan Befektetési Alap	Takarékbank 24 %, Takarék Zártkörű Befektetési Alap 76%	Real estate management
Díjbeszedő Faktorház Ltd.	Takarék INVEST Befektetési és Ingatlankezelő Ltd. 51%	Purchasing, handling and collection receivables of retail customers
Díjbeszedő Informatikai Ltd.	Takarék INVEST Befektetési és Ingatlankezelő Ltd. 50%, Díjbeszedő Holding Ltd. 50%	Providing IT services primarily to the members of Díjbeszedő Group
Takarék Kockázati Tőkealap	MTB Magyar Takarékszövetkezeti Bank Zrt. 77%	Hedge Fund

Companies included in the consolidation*	Main shareholder***	Core business

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DÍJNET Ltd.	Takarék INVEST Befektetési és Ingatlankezelő Ltd. 51%	Providing electronic bill payment services
Takarékbank Zrt.	MTB Magyar Takarékszövetkezeti Bank Zrt. 73%	Credit institution
Takarék Mezőgazdasági és Fejlesztési Magántőkealap	MTB Magyar Takarékszövetkezeti Bank Zrt. 100%	Investment Fund
Magyar Posta Befektetési Szolgáltató Ltd.	Takarék INVEST Befektetési és Ingatlankezelő Ltd. 50%, Magyar Posta Ltd. 50%	Selling investment products
Takarék Zártkörű Befektetési Alap	MTB Magyar Takarékszövetkezeti Bank Zrt. 92%, Takarék INVEST 8%	Investment Fund
Takarék Faktorház Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 100%	Providing full factoring services
Takarékszövetkezeti Informatikai Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 52.38% SZHISZ** 47.62%	The leading IT service provider of the integration of Savings Cooperatives – as outsourced activity – primarily provides IT system operation and system integration services in the field of banking IT
Tak-Invest Zrt.	MTB Magyar Takarékszövetkezeti Bank Zrt. 100%	IT service provider
Takarék Központi Követeléskezelő Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 100%	Debt collection, debt recovery, intermediation of financial services
TKK Ingatlan Ltd.	Takarék Központi Követeléskezelő Ltd. 100%	Sale of properties
MA-TAK-EL Magyar Takarék Ellátó Ltd.	MTB Magyar Takarékszövetkezeti Bank Zrt. 59.09% and Magyar Takarék Befektetési és Vagyongazdálkodási Ltd. 40.91%	Providing bank security, facility management and other operating services excluding IT services
DBH Investment Zrt.	MTB Magyar Takarékszövetkezeti Bank Zrt. 99,5%	Fund and property management
TIFOR Takarék Ingatlanforgalmazó Zrt.	Takarékbank 100 %	Sale of properties
TIHASZ Takarék Ingatlanhasznosító Zrt.	Takarékbank 100 %	Renting and operating of real estate
TKK Csoport Ingatlankezelő Ltd.	Takarék Központi Követeléskezelő Ltd. 100 %	Sale of properties
Takarékinfo Központi Adatfeldolgozó Zrt.	MTB Magyar Takarékszövetkezeti Bank Zrt. 13,91 %,Takarék INVEST Befektetési és Ingatlankezelő Kft. 13,91 %, SZHISZ 20,00%	data processing, web-hosting service

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Companies included in the consolidation*	Main shareholder***	Core business
MPT Security Zrt.	MTB Magyar Takarékszövetkezeti Bank Zrt. 40,00 %,Takarék INVEST Befektetési és Ingatlankezelő Kft. 10,00 %	securitiy service
TKK Takarék Követelésbehajtó Zrt.	Takarék Központi Követeléskezelő Ltd. 100 %	Collection receivables

* From the point of view of MTB Magyar Takarékszövetkezeti Bank Zrt., as parent company of Takarék Group (including Takarék Mortgage Bank and Takarékbank).
** “SZHISZ” = Integration of Savings Cooperatives
*** % in the column = the ownership of the main shareholder

	31 December 2019	31 December 2018
Loans to executives, members of the Board of Directors and Supervisory Board	-	-
Gross remuneration		74
Total remuneration	**69**	**74**

Balances and transactions between the Group and its subsidiaries, which are related parties of the Group, have been eliminated on consolidation and are not disclosed in this note. Details of transaction in 2019 and 2018 between the Group and other related parties are disclosed on the next page.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

Details of transactions as of 31 December 2019

	Parent	Associates and joint ventures	Key management
Due from banks	17,955	94,473-	-
Loans and advances to customers at amortised cost	-	1,003	-
Other assets	1,593	92	-
Total assets	**19,548**	**95,568**	**-**
Due to banks	456	-	-
Deposits from customers	-	-	-
Other liabilities	6,763	14,063	-
Total liabilities	**7,219**	**14,063**	**-**
Interest income	235	1,510	-
Interest expense	(615)	(479)	-
Net interest income	**(380)**	**1,031**	**-**
Fee and commission income	1,484	239	-
Fee and commission expense	-	(246)	-
Net fee and commission income	**1,484**	**(7)**	**-**
Other operating income	1,381	899	-
Other operating expense	(790)	(599)	-
Operating income	**591**	**300**	**-**
Operating expense	(11)	(263)	(69)
Profit/loss on transactions with related parties	**1,684**	**(1,061)**	**(69)**

Details of transactions as of 31 December 2018

	Parent	Associates and joint ventures	Key management
Due from banks	60,066	-	-
Loans and advances to customers	-	17,789	2
Other assets	77	14	-
Total assets	**60,143**	**17,803**	**2**
Due to banks	134,068	4,000	-
Deposits from customers	-	11,496	-
Other liabilities	-	56	-
Total liabilities	**134,068**	**15,552**	**-**
Interest income	922	275	-
Interest expense	(1,148)	(12)	-
Net interest income	**(226)**	**263**	**-**
Fee and commission income	4	78	-
Fee and commission expense	(218)	(582)	-
Net fee and commission income	**(214)**	**(504)**	**0**
Other operating income	1,124	54	-
Other operating expense	-	-	-
Operating income	**684**	**(186)**	**0**
Operating expense	(1)	(439)	(48)
Profit/loss on transactions with related parties	(1,105)	(5,892)	(74)

All figures in tables are in HUF million except otherwise noted

39 NET GAINS

The allocation of operating income to financial instrument categories excluding gains from foreign exchange transactions:

2019	Derivative financial assets and liabilities	Securities at fair value through other comprehensive income	Loans and advances to customers at amortised cost and at fair value	Financial liabilities at fair value through profit or loss	Financial liabilities at amortised cost	Not linked to financial instruments	Total
Interest income	1,756	549	6,594	-	-	-	8,899
Interest expense	(803)	-	-	(271)	(6,539)	-	(7,613)
Net interest income	**953**	**549**	**6,594**	**(271)**	**(6,539)**	**-**	**1,286**
Fee and commission income	1,407	-	406	-	-	-	1,813
Fee and commission expense	(78)	-	(311)	-	-	-	(389)
Net fee and commission income	**1,329**	**-**	**95**	**-**	**-**	**-**	**1,424**
Change in fair value of derivatives	58	-	-	-	-	-	58
Gains from securities	-	588	-	134	11	-	733
Other operating income	-	-	-	-	-	841	841
Other operating expense	-	-	-	-	-	(902)	(902)
Operating income	**2,340**	**1,137**	**6,689**	**(137)**	**(6,528)**	**(61)**	**3,440**

All figures in tables are in HUF million except otherwise noted

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2018	Securities at fair value through profit or loss	Securities at fair value through other comprehensive income	Loans and advances to customers at amortised cost and at fair value	Financial liabilities at fair value through profit or loss	Financial liabilities at amortised cost	Not linked to financial instruments	Total
Interest income	1,139	759	7,795	-	-	-	9,693
Interest expense	-	-	-	(1,438)	(6,462)	-	(7,900)
Net interest income	**1,139**	**759**	**7,795**	**(1,438)**	**(6,462)**	**-**	**1,793**
Fee and commission income	-	-	383	-	-	-	383
Fee and commission expense	(181)	-	(301)	-	-	(20)	(502)
Net fee and commission income	**(181)**	**-**	**82**	**-**	**-**	**-**	**(119)**
Change in fair value of derivatives	2,045	-	-	-	-	-	2,045
Gains from securities	-	(153)	-	1,630	89	-	1,566
Other operating income	-	-	-	-		1,821	1,821
Other operating expense	-	-	-	-		(692)	(692)
Operating income	**3,003**	**606**	**7,877**	**192**	**(6,373)**	**1,109**	**6,414**

All figures in tables are in HUF million except otherwise noted

40 SEGMENT REPORTING BY BUSINESS SEGMENTS

The Group distinguishes business segments according to the organizational structure of the company. The profitability of the company is presented based on this structure. The segments have separable and assignable income, expense, assets and liabilities.

The reportable segments of the Group on the base of IFRS 8 are the following:

- **Retail:** the Bank provides a wide range of services to its retail customers (retail bank accounts, deposits, savings, loans) through the branch network and with the collaboration of the Hungarian Post. Retail bank accounts, deposits, savings, loans of the Takarék Mortgage Bank continue to be included as part of the retail segment.
- **Corporate:** the Bank is trying to satisfy not only the retail but the corporate customers' financial needs providing corporate accounts, deposits, loans in different type, size with different collaterals, guarantees.(The corporate segment is not significant after the selling of share of Takarek Kereskedelmi Bank.)
- **Treasury:** the segment's responsiblities include liquidity management, asset and liability management, and security issue on behalf of the Takarék Mortgage Bank.
- **Refinancing:** refinancing mortgage loans to Takarék Commercial Bank and other partner institutions
- **Other:** the Bank's core business is supported by subsidiary, which profitability's is reported in this category.

Segment report, 31 December 2019	Retail	Treasury	Banks	Refinancing	Other	Total
Net interest income	4,013	1,327	(33)	(4,043)	22	1,268
Other net income	1,434	801	-	(9)	-	2,226
Provision for impairment on loan losses	155	-	-	-	-	155
Direct expense	(1,896)	(60)	-	(702)	-	(2,658)
Operating result	3,706	2,068	(33)	(4,754)	22	1,008
Profit before tax	3,706	2,068	(33)	(4,754)	22	1,008
Segment assets	57,608	46,585	18,481	217,205	3,018	342,897
Segment liabilities and equity	-	423	3,119	265,929	73,426	342,897

All figures in tables are in HUF million except otherwise noted

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Segment report, 31 December 2018	Retail	Corporate	Treasury	Refinancing	Other	Total
Net interest income	10,487	2,768	519	917	0	14,691
Other net income	3,060	1,971	4,944	(70)	1	9,906
Provision for impairment on loan losses	709	205	1	-	0	915
Direct expense	(15,715)	(1,902)	(361)	(627)	0	(18,605)
Operating result	(1,459)	3,042	5,103	220	1	6,907
Profit before tax	(1,459)	3,042	5,103	220	1	6,907
Segment assets	201,263	171,459	259,857	105,296	16,769	754,644
Segment liabilities and equity	128,917	175,416	161,091	214,389	74,831	754,644

41 IMPACTS OF IMPLEMENTATION OF IFRS 16

General impact of application of IFRS 16 Leases

IFRS 16 provides a comprehensive model for the identification of lease arrangements and their treatment in the financial statements for both lessors and lessees. IFRS 16 becomes effective for accounting periods beginning on or after 1 January 2019 and superseded the current lease guidance including IAS 17 'Leases' and related interpretations: IFRIC 4 'Determining Whether an Arrangement Contains a Lease', SIC 15 'Operating Leases – Incentives' and SIC 27 'Evaluating the Substance of Transactions in the Legal Form of a Lease'.
The purpose of the new standard is to ease the comparability of the financial statements, presenting both financial and operating leases in the statement of financial position of the lessees, and providing corresponding information to the users of the financial statements about the risks associated with the agreements. In contrast to a lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17.
The date of initial application of IFRS 16 for the Bank was 1 January 2019.
The Bank has chosen the modified retrospective application (cumulative catch-up approach) of IFRS 16 in accordance with IFRS 16:C5(b). Consequently, the Bank restated its comparative figures but recognized the cumulative effect of adopting IFRS 16 as an adjustment to equity (retained earnings) at the date of the initial application.

Impact of the new definition of a lease

IFRS 16 provides a new definition of a lease. The essential element differentiating the definition of a lease under IAS 17 and under IFRS 16 is the concept of control. Pursuant to IFRS 16, an agreement is a lease or contains a lease if it transfers the rights to control the use of an identified asset for a given period in exchange for compensation. Control is considered to exist if the customer has:

- The right to obtain substantially all of the economic benefits from the use of an identified asset; and
- The right to direct the use of that asset.

All figures in tables are in HUF million except otherwise noted

Notes to the Consolidated Financial Statements

The Bank applied the new definition of a lease and related guidance set out in IFRS 16 to all lease contracts entered into or modified before and on or after 1 January 2019.

In preparation for the first-time application of IFRS 16, the Bank has carried out an implementation project. The project has shown that the new definition in IFRS 16 changed significantly the scope of contracts that meet the definition of a lease for the Bank.

Impact on lessee accounting

The new standard discontinues the differentiation between operating and finance leases in the lessee's books, and requires to recognise a right-of-use asset and lease liability regarding all of the lesses's lease agreements except for short-term leases and low asset value leases which are subject to exemptions.
On initial application of IFRS 16, for leases previously classified as operating leases (except as noted below), the Bank recognised right-of-use assets and lease liabilities in the consolidated statement of financial position. The paragraphs below explain the measurement methods that was applied to those leases.
On initial application of IFRS 16, for each lease separately, the lease liability was initially measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate at the date of initial application. Additionally, the Bank decided to use following practical expedients in respect of the measurement of these lease liabilities:

- apply a single discount rate to a portfolio of leases with reasonably similar characteristics;
- use hindsight, such as in determining the lease term if the contract contains options to extend or terminate the lease.

On initial application of IFRS 16, the right-of-use asset, was initially measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.

Additionally, when initially measuring the right-of-use assets, the Bank

- Relied on its assessment of whether leases are onerous applying IAS 37 Provisions, Contingent Liabilities and Contingent Assets immediately before the date of initial application as an alternative to performing an impairment review of the right-of-use asset on a date of initial application. As a consequence, the right-of-use asset recognised at the date of initial application will be adjusted by the amount of any provision for onerous leases recognised in the statement of financial position immediately before the date of initial application.
- Excluded initial direct costs from the measurement of the right-of-use asset at the date of initial application.

Subsequently, the Bank :
(a) Recognised depreciation of right-of-use assets and interest on lease liabilities in the consolidated statement of profit or loss;
(b) Not separated the total amount of cash paid into a principal portion and interest in the cash flow statement/consolidated cash flow statement.

No changes in accounting had been made in case of operating leases which as at 1 January 2019 will have the remaining lease period of 12 months or less, and leases of low-value assets (such as personal computers and office furniture. In those cases, the Bank opted to recognise a lease expense on a straight-line basis as permitted by IFRS 16.

As at 31 December 2018, the Bank 21 has non-cancellable operating lease commitments that are related to leases other than short-term leases and leases of low-value assets. Summary of the related contracts:

Leased asset category	Number of contracts
Properties	20
- with indefinite term	11
- with definite term	1
Company car	1
- with indefinite term	0
- with definite term	1
Total	**21**

The Bank recognised a right-of-use asset of HUF 1,263 million and a corresponding lease liability of HUF 1,278 million in respect of all these leases. The estimate impact on profit or loss in 2019 is to decrease rental fees by HUF 736 million, to increase depreciation by HUF 723 million, and to increase interest expense by HUF 12 million.
The Bank has no provision for onerous lease contracts or lease liability incentives as at 31 December 2018 that should be derecognised and considered in measurement of the right-of-use assets and lease liabilities.

Under IAS 17, all lease payments on operating leases are presented as part of cash flows from operating activities. The impact of the changes under IFRS 16 would be to increase the cash generated by operating activities by HUF 735 million and to decrease net cash used in financing activities by the same amount.

The summary of the financial impact on adopting IFRS 16 is presented in the table below (related only to leases entered or modified before 1 January 2019):

in million HUF	01 January 2019	31 December 2019
Right-of-use asset	1 264	56
Lease liability	1 278	70
Provision for onerous contracts	-	-
Other items	-	-
Cumulative impact recognized as an adjustment to the equity at the date of initial application	(14)	
Expected impact on statement of comprehensive income from continuing operation:		12
Expected impact on statement of comprehensive income from discontinued operation:	-	-

- Increase of depreciation from continuing operation	-	(54)
-Increase of depreciation from discontinued operation		(561)
- Increase of interest expense from continuing operation	-	(1)
-Increase of interest expense from discontinued operation		(10)
- Decrease of rental fee from continuing operation	-	42
- Decrease of rental fee from continuing operation		571
Expected impact on statement of cash flows:	-	0
- Increase of net cash-flow from operating activities	-	613
- Decrease of net cash-flow from financing activities	-	(613)

Estimated impact on financial ratios, bank covenants and other arrangements

Adopting IFRS 16 had no material impact on financial ratios, bank covenants and other arrangements.

42 SIGNIFICANT EVENTS AFTER BALANCE SHEET DATE

The Takarek Mortgage Bank Co. Plc. (TMB) has won the Budapest Stock Exchange BÉT LEGEK (BSE BESTS)'s Award of Best Mortgage Bonds Issuer of the Year 2019 based on TMB's very active capital market acitivity. The reason behind the decision is that Takarek Mortgage Bank issued nearly 60 billion nominal mortgage bonds and listed them on the stock exchange. The TMB organized 15 public auctions on the BSE auction modul, with the participation of the entire consortium of the Mortgage Bank (MTB Magyar Takarékszövetkezeti Bank Zrt., MKB Nyrt., Concorde Securities Zrt. and Erste Securities Zrt.) during 2019. TMB as a pure mortgage bank (refinancing and covered bond issuance) continues to regularly issue mortgage bonds through regular auctions and to offer competitive assets to investors, and to provide adequate long term funding for the refinancing partners.

S&P Global Ratings (Madrid) announced on February 28, 2020 that it affirmed the „BBB" foreign and local currency ratings to Takarék Mortgage Bank Co. Plc's mortgage covered bond program and all outstanding covered bond issuances, while the outlook on the covered bond rating was revised to positive from stable. The rating action follows the February 14, 2020 revision of Hungary's long term sovereign rating outlook to positive from stable.

The Budapest Stock Exchange (BSE) published the new composition of the BUX and BUMIX baskets - valid from March 23, 2020 - on March 12, 2020. The CEO of the Budapest Stock Exchange Ltd. adopted the resolution 117/2020 and decided based on Point 3.3.6.1 a) the exclusion of the shares of the Company from the BUX basket and from the BUMIX basket.

On March 11, 2020, the Management Board of the Takarek Group approved the Pandemic Plan and the Amendment of the Business Continuity Policy, and the Pandemic Operational Staff (POT) was established. From this time the POT coordinates in close cooperation with the Management Board and other relevant

All figures in tables are in HUF million except otherwise noted

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departments the tasks of the Takarék Group in relation to the coronavirus crisis. The POT continually formulates instructions and recommendations to all employees and about this send information to the meetings at appropriate intervals.
The management regularly monitors the impact of the crisis on equity and profit or loss and decides on appropriate actions which it also informs the National Bank of Hungary.

This situation is expected to have an impact on macroeconomic circumstances in the future (e.g. GDP growth, unemployment, inflation), which indicators were taken into account for the purpose of the IFRS9 models; the impairment and provisioning levels are expected to increase in 2020 and 2021.

If current economic processes are sustained, payment facilities may be introduced to help clients who are defaulting on payment moratorium on repayments based on the Bank's own decisions, and these influence the classification of loans and guarantees, potentially causing an increase in impairment and provisions. See credit risk at the balance sheet date in note 36.4.

Liquidity shortage is expected in the financial markets; therefore the renewal of existing derivative contracts, government securities and mortgage bonds will potentially be subject to less favourable terms than in 2019 depending on the crisis and the responses of the central bank.