

# **BANCA VALSABBINA - DIRECTORS' REPORT ON OPERATIONS**

## **FINANCIAL STATEMENTS AS AT 31 DECEMBER 2013**

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## INTRODUCTION

*Dear Shareholders,*

The drafting of the report which accompanies the financial statements for each year is always a moment of great importance since it offers the opportunity to relate, via numbers and regulated information, the background, the events and the results of an entire year of work. And 2013 was a long and arduous year, due to not only the economic and financial tensions which continued to affect vast areas of the planet but also the repercussions with regard to political, social and values-related stability and the equilibriums within the sphere of interpersonal relations.

We thought - and we were not alone in believing - that the year just ended would be that of a turning point, of a way out of the deep and endless crisis which has severely damaged the economic, social and political fabric of Italy and many other countries, at least in the Euro Zone. But this failed to happen: however - even if the industrial production index of the Euro Zone underwent, in contrast to expectations, a icy drop in the very last month of the year - certain signs of improvement were however seen and were seized upon with greater readiness and sensitivity by those who reacted, opposing first of all that sense of retreat which itself risks becoming a crisis factor.

We are among those who have put into practice that wise teaching, referred to in the report some years ago, according to which *“we cannot expect things to change if we keep doing the same things”*. And so we turned to account even the weakest signs of recovery so as to turn them into a renewed boost to work harder and with greater pride, within the dignity of a convincing idea: if the Bank has overcome the most difficult points of the crisis, it cannot fail to recoup those operational assertions which have characterised the growth profile in the years prior to 2008.

The path towards a new corporate season thus continued for the whole of 2013 without hiccups or slowdowns, sustained by ventures and programmes aimed at surmounting the obstacles which intervene in the economic pick up and the risks which are typical and characteristic of the banking business. But also supported by a positive state of mind and awareness of being able to count on the wealth of a wider market served and on the consensus of the shareholders and the customers who assign Valsabbina the institutional and social responsibility of interpreting a Bank model with a truly co-operative vocation.

The bottom line of the income statement, that relating to the profit or loss for the year, discloses a net profit of considerable improvement with respect to 2012, but cannot express - unless it explains them - the strategies and the dynamics which have led to the same, to that precise extent. Certainly, the result could also have been greater if we had not interpreted the mutual spirit of the Bank to its utmost, listening to the requests, often entreaties, of the individuals and the businesses brought to their knees by the crisis; but it could have been lower if we had not implemented - with a reasoned and non-dogmatic approach - new governance strategies, effective initiatives with regard to commercial matters and shared resource management and development policies: human, technological and organisational.

This task of this Report is to explain and make sense of the numbers which characterise the size-related and production profiles of the business: and it is the task of this shareholders' meeting to judge and possibly approve the conduct of the Directors, presented on the pages which follow and commented on in the salient points so as to provide account of the choices made in the weekly meeting of the board.

The commitment which we undertake from this point on is that of reporting in a simple and balance manner on the work carried out in the 116th financial year, without wallowing in congratulations - since the re-equilibrium of the quality of the assets is still far off - but without however keeping quiet, when the figures are indisputable and the progress achieved projects the

confidence in seeing the improvement indices consolidated in the year underway and in those to come.

The premise contained in this first section would not be complete if we failed to say also that towards the end of the year, a three-year Strategic Plan was approved which commits the Company and all its components, truly all, in a growth projects - parallel to that which is awaited for the economy of the country - and which is able to develop the role, identity and the image of Valsabbina as an industrial co-operative reference Bank for its area, at present extended to the provinces of Brescia, Trento, Mantua and Verona. An in-depth review will be dedicated to the importance of the figures of this document on the pages which we are preparing to examine after having carried out, as is customary, a preliminary summary on the mixed profile of the international and Italian economy during 2013.

## **1 THE INTERNATIONAL ECONOMIC AND FINANCIAL SCENARIO**

The global economy in 2013 progressively improved with connotations not dissimilar to those of the previous year: the forecasts formulated by the leading research centres and institutes were essentially confirmed, especially with regard to the heavy characterisation of the weight and the economic cycle of the various powers.

In the majority of the advanced economies, a constant strengthening of the growth ratios was witnessed, encouraged above all else by moderation in the fiscal policies and even further by the accommodating stance of the monetary policies.

In emerging countries, the growth rate by contrast lost vitality after years of strong bullish intonation. The abundant liquidity introduced by the central banks worldwide ensured the emerging countries florid expansive conditions, but the launch of the reduction in the monetary stimulus by the Federal Reserve led to the adoption of more critical and selective policies. The imbalances in the accounts with abroad, the slowdown in growth and the whittling down of the currency reserves then joined in as new factors which proceed to create a different profile of the global economy: these countries, despite in fact remaining a strong driving force in the dynamics of global development, are losing a great deal of their verve.

With regard to the so-called Brics - whose economies appear overall to be more better equipped to resist the pressures of the markets - the growth rates of the past are revealing themselves to be unsustainable.

For three decades, China - the strongest among the countries in the group - chalked up an average annual expansion rate of close to 10%, while now that rate has dropped to 7.7%. And according to the calculations of the International Monetary Fund, "one point less in growth of investments in China takes away almost one point from the growth in the added value of the regional supply chain". If Indonesia, Malaysia and Thailand are increasingly dependent on Beijing, it should not be forgotten that on the other side of the world, in Africa and South America, China is the leading purchaser of raw materials; if it imports less, countries such as Brazil, Argentina and Chile will feel the effect.

Again with reference to the Brics, this also explains why India is growing at a rate 5% while South Africa, Brazil and Russia have seen growth of between 2 and 3%.

The halt is substantial, such as to squeeze the rate of global growth, and above all else has structural-type characteristics: we are certainly not in the presence of a cyclical situation, bearing in mind that it was the drop in prices of raw materials and the considerable lack of investments which caused the same - with the exception of China - investments which were inadequate for meeting the increasingly sharper demand for consumables.

On the other side of the Atlantic, among the advanced economies, America in the last quarter of 2013 consolidated a positive trend which started back in the previous year; authoritative

estimates, presented what is more in the ECB's February monthly Bulletin, placed the GDP growth rate at 3.2% on an annual basis with particularly robust rates in the last two quarters; the performance is attributable to a rise in consumptions and exports, but also to the accumulation of stock whose pace remained high in all four quarters.

The growth in GDP was accompanied by the positive trend of the employment market, in the sense of a consistent reduction on the unemployment rate, and a significant drop in inflation, from 2.1% in 2012 to the 1.5%.

The general improvement in the profiles of the real economy had repercussions on the policy of monetary stimulus, so much so that the Federal Reserve announced during its first meeting in January 2014 a gradual reduction in the monthly rate of purchases of American treasury securities, and also in securitised loans. Further reductions may take place during the year if the unemployment rate drops under the scheduled level of 6.5% and if the inflationary projections remain under 2%.

The performance of the economy in Japan was positive, in third place worldwide after the USA and China, even if the significant monetary and fiscal boosts applied by the new Government and the Central Bank leave us to imagine a more solid overtone. During the last quarter, the Gross domestic product rose just 0.3% on the previous figure, while expectations were for a more significant 0.7%. Abenomics Japan (taken from the name of the prime minister Abe) has thus started to delude the expectations on the macro-economic front and consistently with regard to the important stock market sector with repercussions extending to other markets: the causes are mainly attributable to a much more contained pick-up in exports than envisaged, having taken into account the heavy and sought-after weakening of the Yen. And what is more, on an annual basis the real GDP reported growth of 1.6%, without doubt lower than that of the USA, but considerably higher than the -0.4% of the Euro Zone and the situation for the year underway could improve in the presence of a second governmental manoeuvre of the public incentives capable of neutralising the rise in taxes on consumption from 5% to 8% as early as April.

With regard to the European economy, GDP underwent an average decline of 0.4% with respect to 2012 with also with considerable differences between the healthier countries. While Germany and France command a visible pick up with positive rates of 0.4% and 0.2% respectively, Italy, Spain and the Netherlands remain in negative waters.

Italy, despite having found appreciation in the last quarter for an inversion in the cycle by means of a mini-revival of 0.1%, ended 2013 with a negative result of -1.8%. Spain and the Netherlands did better, limiting the drop in gross domestic product, respectively, to -1.3% and -1.1%.

In conclusion, with regard to global inflation, 2013 reported overall moderate dynamics: the slowdown in the level of the prices in the emerging economies and the forecasts of an economic trend with an uncertain profile contributed towards maintaining the conditions and the prospects of the phenomenon stable; a not dissimilar trend occurred, albeit with different overtones, also within the sphere of the advanced economies in which - both due to the continuation of large margins of unused production capacity and the absence of pressure on the cost of energy goods - inflation remained well under the objectives set by the central banks.

Also with regard to the Euro Zone, the inflationary trend remained on average at around 1% with somewhat lower points in some countries due to the elevated unemployment rate, the consequent drop in consumption and, in general, the low levels of economic activities.

## **2 THE PERFORMANCE OF THE MONETARY AND THE FINANCIAL MARKETS**

If we think back to what happened on that unforgettable day, 9 November 2011, with the spread at 575 base points and a return on government securities above the threshold of 7%, it is possible

to comprehend how devastating the effects of international speculation can be, also beyond the logics which underlie the fundamentals of the real economy.

We were overwhelmed by a financial and monetary storm caused by the inability to govern the fate of the real economy, and above all else an authentic confidence crisis with regard to sovereign debt. We were not alone in experiencing the long-lasting effects of the crisis which exploded towards the end of 2007: there were also other countries in the Euro Zone inside that deep-seated devastation of rules and conduct of the markets, the Mediterranean ones in particular, but without doubt Italy experienced the worst crisis since after the war and saw the deterioration of the most serious of its problems, the high level of public debt, with implications which even made the risk of default realistic.

Just over two years have passed and the situation in Europe, as it has in Italy, has radically changed.

Speculation has changed direction, after the European Central Bank energetically neutralised the risks of dissolution of the Euro: first of all, at the start of 2012, with the loan to the European banks of around Euro 1,000 billion, a quarter of which ended up with the Italian banks which had mainly purchased Italian government securities offsetting the drop in foreign demand. And subsequently, midway through the year, with the declaration of Mario Draghi that “everything would be done to save the single currency”.

2013 was therefore a year of consolidation for the new set-ups of the financial and monetary markets. Precisely at the moment when Europe returned to being more secure and the FED had launched, albeit gradually, the announced tapering policy, the immense liquidity fuelled by the injections of the central banks worldwide abandoned emerging countries, considered too hazardous, to return to Europe. Mainly the countries of the south benefited - Italy, Spain, Portugal, Greece - where the returns on sovereign debt securities fell progressively and to a significant extent.

This was precisely the case of Italy where in 2013 the weighted average return on government securities dropped no less to 2.08% to reach in the first few weeks of the year underway 1.66% in the wake of a spread progressively decreasing under 200 base points. And thus also if the economy shows lasting symptoms of the crisis: very low consumption, high levels of unemployment, sky-high taxation, all-time highs in bankruptcies and the flight of businesses towards eastern shores. All factors which would seem to justify the fact that the businesses, individuals and ideas are leaving Italy. Within the apparent contradiction, the fact that the risk/return ratio of our country is considered interesting for those who have liquidity to invest is certainly not bad news.

The repercussions of the afore-mentioned expansive monetary policies of the Federal Reserve, the European Central Bank and, at the beginning of Spring 2013, also the Japanese Central Bank on the structure of the interest rates and the performance of the stock markets, were immediate, important and positive.

With regard to the former, the FED maintained the reference rates stable, at a standstill since 2010, to the extent of 0.75%. The ECB, in turn, took steps on two occasions, in Spring and Autumn, to reduce the discount rate, still today at 0.25%. The correlated effects on the stock markets were significant; the S&P index earned 26% and the European DJ Stoxx 18%.

With a 16.50% performance of the share prices, compared with 6.6% in 2012, the Italian stock market certainly did not cut a poor figure in comparison. In volume terms, nearly 60 million contracts were traded for an equivalent value of Euro 540 billion; not a great deal, but it should also be considered that the array of listed Italian companies - 326 in all - is somewhat restricted if compared with that of the main European stock markets.

By contrast, the volume of net bond issues decreased, both in Italy and in the Euro area, within more significant dimensions in the banking sector with respect to that of non-financial companies.

### 3 THE ITALIAN ECONOMIC SCENARIO

For years we have been saying that the economic situation in Italy, the second manufacturing power in Europe, has been heading towards critical and unsettling conditions, at times dramatic: in the assessment of the indicators which sum up the state of the economy, it is sufficient to distract oneself for a moment to register shocking deteriorations. Since 2007, the year which heralded the outbreak of the crisis, the industrial base decreased by more than 20% leading to the loss of nine percentage points of the Gross domestic product, despite the brief respite granted by the fleeting recovery registered in 2010. The number of those in work - indicator which, together with the percentage figure of the gross domestic product, effectively portrays the picture of the economic recession underway - has fallen by one million, while the unemployment rate is close to 13% and touched the 41% mark amongst youngsters.

In 2013 alone, despite the very slight decrease seen in December, the unemployment rate in fact stood at 12.7%, compared with an average in the Euro Zone of 12%, and a growth trend of 1.2 percentage points; during the 12-month period, the number out of work rose 10%, equal to 293 thousand more.

The snap shot developed by ISTAT at the beginning of the year reveals that the number of unemployed at the end of 2013 reached 3 million and 230 thousand individuals, also including those who - discouraged by the difficulties - ceased looking for a employment launch-pad. The unemployment figure relating to youngsters between 15 and 24, equating to 671 thousand (+48 thousand over the 12 months) was merciless.

Such negative trends are the repercussion of the heavy retreat suffered by the production sector, the leading “employer” of the Italian economy, also considering that the public administration authorities have maybe slowed down the rate of employment absorption, but have certainly not implemented “lay-off” policies within its structures.

Italian industry has in fact once again suffered in 2013 the heavy backlashes of the crisis, dragging all the related indicators downwards: the most expressive - that of the “turnover”, or the aggregate revenues - dropped from Euro 907 billion in 2008 to Euro 774 in 2013, Euro 24 billion less with respect to 2012. And behind each billion of sales revenue lost, there are companies closing down, thousand of bankruptcies, a collapse in investments, job losses, consumption down even further, rising indebtedness which does not allow a glimpse of a possibility for recovery of the minimum conditions of financial balance. From the start of the crisis, the industrial system has burnt enormous figures: more than Euro 130 billion, behind which a vertical drop in the profit margins is found. In 2008, profits generated by Italian industry came to more or less 18 billion, at the end of 2013 just 4.1 billion: a shocking figure if one considers that in any event production intended for exports have maintained positive margins and rates of around 1%.

The agricultural sector and that of services performed even worse than industry, affected by a cyclical drop in private consumption and, with regard to the former, also by the negative climatic conditions.

In a situation such as that described, it is not surprising than the performance of the prices reported considerable slowdowns: inflation in Italy continued in fact to decrease, more than forecast a few months ago, dropping to 0.7% in December. The weakness in demand, caused by the drop in consumption, in fact contained the prices fixed by the businesses to a more emphasised extent than in the past and the October increase in VAT was re-assigned only to a small extent to the end prices. The annual rate of inflation therefore dropped by 3.3% in 2012, to 1.2% last year.

The level of public deficit by contrast fell: the requirement of the state sector in fact rose considerably, albeit as a consequence of extraordinary factors such as the payment of a significant part of the prior debts of the public administration authorities. According to the Bank of Italy, on the basis of available data, the net indebtedness of the public administration authorities remains around the threshold of 3%, it only being possible to foresee its containment as from 2014.

By contrast, the trend in external foreign accounts was positive during the year; the balance of the current part of the balance of payments, thanks to the drop in imports and the simultaneous increase in exports, was once again positive and is destined to grow on a parallel with the envisaged gradual strengthening of economic activities.

An aspect which closely concerns us, completing the summaries on the main aggregates of the Italian economy, is that relating to the credit situation and the risk profiles by means of which the banks - including ours - have had to daily measure up to during this difficult 2013.

The afore-mentioned financial fragility of the businesses - caused by the contained degree of capitalisation and the historic dependence on bank lending in the absence of bond and share markets supplementary or alternative for the funding of investments and working capital - has manifested it all its glory precisely in the period under review with an upsurge of the stocks of uncollectable receivables which discloses a new record since 1998.

Non-performing bank loans in fact exceeded Euro 155 billion in December 2013, with growth of 24.6% when compared with the same month in 2012, in the presence - above all else - of a generalised decrease in loans due to the low demand for credit for investments by companies and, with regard to supply, by the high credit risk and the pressure applied by the recession on the financial statements of banking intermediaries.

In the continuation of this report, we will see the profiles of the credit policies implemented by the banking system in a more in-depth form, with particular reference to co-operative banks and we will be able to comment in terms of what the dynamics of the lending aggregate have been along with the repercussions in terms of quality of the assets within our business entity.

#### **4 THE ECONOMY IN THE BRESCIA AND VERONA AREA**

Dealing, as we have done, with the evolution and the main events affecting the economy and finance in the world and in Italy during 2013, one almost has the sensation of dedicating oneself to school exercises or relating events occurring elsewhere, far away and extraneous to the interests and the pressures of the Italian environmental and operating context. But in reality we are well aware that it is not exactly so: the long-lasting effects of the subprime loans, the subsequent crisis affecting the real economy, have generated a merciless contagion which has reached our region from the financial centres and global markets, infiltrating the most remote corners where one can hear the rich variety of church bells and dialects of our plain and our valleys.

The expansion of the area of influence of the Bank to the nearby province of Verona has led to the need to extend attention and our observation beyond the specificities of the respective markets to study the effects of synergy and complementary nature between the area in which the bank's presence may encourage opportunities in the field of production, exchanges, close integration between economies which are amongst the richest in the country. Opportunities which - irrespective of the difficult economic moment - may evolve on a parallel with an exit from the crisis, permitting the Bank to concentrate itself on a formidable market positioning perimeter: a powerful strategic asset which reduces the distances from the wealth and draws closer the possibility of re-engaging the positive results of the excellent entrepreneurial policies.

For the drafting of the summary on the features of the economy of the provinces of Brescia and Verona, we availed ourselves of the economic cycle analysis developed by the Chambers of Commerce and by the category and trade association bodies, the publication of whose data relieves us from the concern of reporting imprecise or out-of-date information.

Therefore, we would like to make a preliminary comment: the trends revealed by the figures - pertaining to production, turnover, employment, commercial rather than services - have an almost mirror-like correspondence in the phenomena observed by the Bank via its everyday operational dealings with its customers; none of the data or indicators provided by the aforementioned sources have surprised us or left us perplexed. Rather, in the role of community bank we have filtered the difficulties and the insecurities of the businesses and households bearing in mind - due to participation which could not fail to be emotive as well, and somewhat in advance - what the final balance of the various economic sectors might be.

For a sense of realism, suggested by the awareness that the presence of our Bank in the Verona area is still somewhat marginal from the standpoint of the market shares, we have limited ourselves to presenting a number of summary notes, reserving greater space for the extended area of choice, in which the signs of our branches have a much different presence and strong evocatory power.

Rather than number or indicators, to which we will by contrast make abundant recourse in the examination of the Brescia economic situation, we will instead refer to qualitative aspects and the singularly managerial stamp of the Scaligera entrepreneurial class; not without however having revealed that its history and its dynamics lie within a region - Veneto - amongst the most industrialised in Europe, with a weight of the manufacturing industry which touches 30% of the economy and which exits the fourth quarter of 2013 with growth of 1.4%, albeit boosted by exports.

Concentrated more on the expectations of a new season of growth rather than on the reports of the crisis, it seems auspicious to resume a passage from a recent presentation by Giulio Pedrollo, leader of the Verona industrialists society, according to whom: *“The crisis has also been beneficial because it has provided an occasion to cast off old mechanisms and allow one’s outlook to grow. In many companies, generational changeovers have become obligatory and with the new generations at the helm not only has the company acquired a greater boost and velocity in perceiving the market needs, but has also grown with regard to financial awareness, capitalising itself in the right way”*. And Verona, in any event, reported an increase in production during the fourth quarter of 2013, of 1.55% when compared with the previous quarter.

With regard to the province of Brescia, 2013 was not a negative year all told, even if the forecasts and the auspices justified more decisive improvements in the various local production and economic components.

On the other hand, the inequalities in the distribution of wealth, held in Italy in 2008 by 10% of the population for 43% and today for 47%, have grown more emphasised, revealing new phenomena of poverty, generators of social hardship never so keenly felt or piercing also in the traditionally wealthy provincial context.

This circumstance, which we witness with joint and several concern, maybe unwittingly provoke negative perceptions, whilst - and fortunately - some progress in the direction of a pick up can be effectively documented and may represent the premise for a rebalancing of the distribution curves.

Industrial production, in fact, which thus has a large part in the fortunes of the provincial economy, has reported the best performance in the last two years with an economic cycle increase of 1.1%, despite the presence of an unchanged rate of use of the plants at 70.5%



The trend-based result, obtained by comparing the fourth quarter of 2013 with 2012, came to 4.2%, placing the province of Brescia in second place in Lombardy after Lecco.

Larger companies did better than medium-sized or small ones: among the sectors, drawing along the positive result were those involved in transport, skins and hides, footwear and rubber - plastic; the chemicals and clothing industries were by contract negative.

Likewise positive, higher than the regional average, was the sign provided by the manufacturing cottage industries in the textiles, foodstuffs and engineering sectors, but also in the skins and hides and the footwear area; production in the fourth quarter of 2013 increased with respect to the same period in the previous year by 3.63%, as did the sales turnover, up on average 2.93% thanks to the contribution from exports, up 4.18%.

Orders also disclosed a significant annual increase, equal to 4%, of which 6.8% obtained by the foreign component and 2.1% by the internal component after ten negative quarters.

By contrast, the result of the orders in the manufacturing cottage industry sector was essentially stable.

The indicators relating to employment, in truth, were contrasting. While in relation to industry, the last quarter of 2013 was posted as positive, albeit by just a few fractions of a point, criticalities remained in employment levels for the manufacturing cottage industry sector in the last quarter, down 1.14%.

The commerce sector remains negative: particularly affected by the drop in business turnover were the smaller businesses, who declared a decrease of 3.7%. The services sector, which in the whole of the Lombardy region repeats the lasting difficulties reported at national level, closed the last quarter of the year with a slight increase in business turnover (+0.7%) after many quarters under a negative sign. The prospects for the first quarter of the current year disclose small signs of confidence with regard to the business turnover of both commerce and services, while the prospects regarding employment levels remain negative.

It does not seem to us either premature or undue to make reference at this precise point in our report to the important date with Expo 2015 which will take place next year in Milan between 1 May and 31 October. The work for the achievement of such a far-reaching venture in terms of the responsibilities and the aspects of our country and our Region are proceedings swiftly in observance of the agenda and on a parallel with another great infrastructural project which closely concerns our city: the Brebemi, the Brescia-Bergamo-Milan motorway.

That which is taking place less than 100 km from our city, has positive repercussions and reflections also for the provincial economy, since the production units in the area involved for various reasons in the projects and the supply of goods and services are by no means just a few. And the returns for the tourism and commercial sector will be no less significant, during the event, even if just a small portion of the 20 million visitors expected at Expo will decide to acquaint themselves with the beauties of our province, staying or passing through the same to reach another destination, also important for us: Verona, Unesco World heritage Site.

Concluding the summary review on the state of the Brescia economy in 2013, it appears pertinent to refer to an in-depth survey into the future of local manufacturing, drawn up by the Brescia Industrial Society and presented at the end of February this year: we have referred to two steps as salient because we believe they are indicators of the entrepreneurial manner of the category.

The first refers to the dimensional feature layout of the local production systems, in other words its powerful numbers: the province of Brescia alone represents the GDP of an entire region such as the Marches or Liguria and exports the same as two average-sized Italian regions put together. This favourable starting point is the ideal incubation ground - and is the second important step - for an exacting repositioning strategy for the sector on more structured internationalisation methods.

The possible future scenarios drawn up on conclusion of the survey are three. According to the first, considered “basic”, the manufacturing industry will not be able to make “new leaps forward” of an intensity identical to that pre-crisis and will limit itself to re-proposing current strategies. The second - entitled “fall back scenario” - is worse and pessimistic because it would imply a drop in sales revenues of 3%.

Hope is entrusted to an “advancement” scenario, which puts forward the possibility of 6% growth, and which is energetically supported by the Chairman of the Association, Marco Bonometti.

Why have we presented the framework of this survey? Because it is that more innate in the disposition and the implementation abilities of the operators in our area and because - in the role of representatives of the “Household Bank” - we feel we are in a position to share and support, ideally participating for the part we are responsible for, in the arduous commitments of overcoming the challenge. And from our standpoint, this appears realistic.

## **5 OUTLOOK FOR THE ECONOMIC AND FINANCIAL SCENARIO**

The comment made last year with regard to this same section was marked by moderation and prudence which we can certainly not regret. We resisted the temptation of believing that 2013 would have seen a turning point, trusting more humbly in the launch of a normalisation of the fundamental parameters which describe the state of the economy and we have shaped the guidelines of the management policies to a scenario of essential economic “neutrality”.

2014 opens however with different prospects, positive and encouraging starting off from the convergence of the forecasts regarding a recovery in GDP, a sign expressive of the turn around after years of retreat which - at least for Italy - has led to a significant destruction of wealth: now all needs to be rebuilt, but favourable conditions are required which cannot leave aside the still complex picture which characterises the European economy.

The strong Euro, even if weakened at the start of the year vis-à-vis the Yen and the Sterling, represents a risk for recovery since it curbs exports; unemployment levels remain high especially in certain peripheral countries, such as Spain and Italy, where the estimates indicate figures of around 26% and 12% respectively; the balancing of public finances remains, in turn, a crucial condition for the consolidation of a pick up, especially in those countries, such as ours, characterised by a high debt/GDP ratio which however obtain by no means insignificant advantages on the cost of the debt from the low level of the interest rates.

During 2013, the ECB cut the interest rates twice and President Draghi reconfirmed, again recently, the intention to adopt every additional and appropriate monetary policy initiative for maintaining a low level of the rates. New measures in this sense should not be excluded since the financial fragmentation of the entire Euro Zone has prevented a full and systematic transmission of the expected boosts of the monetary policy to the development of the real and financial one.

The difference between the bank interest rates between Germany and peripheral countries in fact fluctuates between 80 basis points for loans involving a high amount and 180 for those with a lower balance; with regard to Italy, this difference stands at around 130 basis points and this circumstance confirms how the relatively high cost of bank credit can have heavy repercussions on the financial equilibrium of the companies granted credit facilities, especially when it is not possible - due to size or organisational and operating profiles - to access alternative sources of funding such as recourse to the share or bond market.

Confirmation has been seen in the dynamic of bankruptcies, whose upsurge continued in Italy during 2013 with a total of 14 thousand declarations, more than 12% more with respect to the 12,332 in the previous year and 15% on the 12,154 in 2011. And even further confirmation has been provided by the shocking number of businesses which have closed down: 111 thousand, of

which 94 thousand further to voluntary closures, in other words “performing” businesses without previous insolvency proceedings.

Also within the sphere of the business crisis, some glimmers of hope however have started to appear if one observes the downwards trend in bankruptcy petitions presented at the courts in the main Italian cities: in Milan, for example, there were 250 in the first month and a half of the year, a good 100 less than in the same period last year, thus confirming the drop already noted to an albeit more modest extent in 2013.

Again with regard to the financial stability of the business, an incisive excerpt contained in the Consob’s “Risk outlook” report from last February: “The sustainability of the debt continues to represent a significant problematic for Italian businesses. During the first half of 2013, around 50% of listed companies registered a coverage of the financial charges by means of operating income less than the long-term average, while financial leverage remains at significantly higher levels than that of European competitors. Also in terms of profitability, the leading Italian listed companies remain fragile: in the first half of 2013, the percentage of companies which reported a negative EBIT came to 15% (25% at the end of 2012)”. Much more emphatic fragility remains in unlisted companies and in medium-to-small sized ones where, obviously, banking finance is required to substitute alternative sources of funding.

And this specific topic couples with that closer to home regarding the stability and profitability of another important category of businesses: banking concerns, crushed by a mountain of non-performing positions which, albeit having increased in 2012 at a lower rate than in the previous year, continued the upsurge surpassing the amount of Euro 155 billion at the end of 2013.

The low level of interest rates, the heavy adjustments caused by the deterioration of the quality of the loans and the widespread need for recapitalisation, already made evident by means of the heralded share capital increase projects of numerous banks in the country, represent central themes on which the game of recovery will be played, no longer possible to put off, to regain margins of efficiency and operational cost effectiveness heavily compromised by the continuation of the crisis.

The summary contained in the afore-mentioned Consob report is illuminating in this connection, with regard to the new scenario in which the set-ups of the banks will bustle in 2014. “The levels of capitalisation improve for all the leading European banks, but new capital requirements could emerge further to the Asset quality review and the Stress tests which the ECB and the EBA are undertaking to achieve in view of the launch of the Single Supervisory Mechanism system. These supervisory initiatives will be joined by the uncertainties associated with regulatory innovations being defined (Directive on the resolution of the banking crisis) or which have already taken place (such as the regulation concerning Government aid).

The new rules make reference to the principle of burden sharing aimed at correcting moral hazard phenomena by banks and at reducing the entity of any public measure.

However, this principle makes bank funding via certain types of financial instruments more expensive (i.e. unsubordinated bonds, hybrid instruments and subordinated liabilities) since it makes the holders of these instruments responsible for any recapitalisations of the lending institutions, before these can access public funds. The impact on the overall cost of funding is difficult to quantify, since it depends - among other aspects - on the structure of the liabilities and the systemic importance of the banks. On the other hand, a more intense regulation of the market could reduce the undertaking of risks by the lending institutions and, accordingly, contain the rise in the cost of funding”.

Despite being affected by these problematics, the Italian banks look to 2014 with certain confidence in the hope of revenues on the up.

Besides a widespread sentiment, this would be confirmed by the outcome of a survey of an important consultancy multinational, Roland Berger, according to which - and the estimate appears reliable - 78% of Italian managers interviewed expect growth, albeit modest, in total

revenues. Growth first and foremost determined by a careful review of the supply conditions, both with regard to loans and deposits, but also by a pick up in profitability by means of active management of impaired credit and the search for new growth. The latter could find application in different customer service models, created with greater recourse to the multi-channel aspect in view of a significant reduction in the number of branches: the branches, according to 67% of those interviewed, should in fact be whittled down by 5 - 10% while Internet, POS, tablets and smartphones will adopt growing importance with regard to commission-related profiles to an extent of 10- 20%.

If the forecasts are confirmed - with the benefit of the doubt in relation to an effective reduction of the number of bank branches, at least with reference to the local situations - it does not appear unrealistic - working at the same time on margins and on a greater efficiency in the handling of the enormous stocks of impaired credit - to consolidate new results in terms of profitability, drawing the cost/income ratio even closer to the much more contained levels of the best European banking economies.

Encouragements in the direction of a more relaxed climate and context in any event derive on the eve of this general meeting season from the more or less unanimous assessment that maybe the crisis has not ended, but that without doubt one of the most acute market phases in Italian economic and financial history has been surmounted. This is also our position: which ranges from the realistic observation of the events and which turns the same to account - as already mentioned - with positive attitudes and with the reinvigorated awareness of great ability and the will to achieve.

## **6 SHAREHOLDING STRUCTURE AND SHARE TRENDS**

Every time we talk about our shareholding structure, we express satisfaction and pride in referring to a community of individuals which recognise, in the characteristic co-operative set-up of the industrial co-operative Bank, the most efficient lending model closest to the needs of the reference area.

The consensus granted over time to co-operative banks in the context of a diversified national banking system has always been wide, but it has continued to grow further in these latter years of deep economic crisis, so much so that a quarter of the entire Italian lending market is brokered precisely by banks in our category. And the reasons for this success are easy to recognise. Co-operative banks, mainly addressing the shareholder - customer and the area in which they spring up, give priority importance to the person rather than to the capital, supporting the development of the individuals and the communities and in this manner activating a virtuous circle which develops the social relationships with equal attention and intensity with respect to the economic and commercial ones.

Demonstration of the efficacy of the model is confirmed, in the specific case of the Bank, by the constant growth of the market shares, the volumes brokered, the number of customers and shareholders who, in an extraordinarily complex period full of difficulties, have confidently relied on the bank, asking to be able to share their projects, be supported with regard to their needs, to be able to entrust their savings relying on professional competence.

Respect for the value and aspiring principles of co-operative governance has been valid for increasing the currents of affinity and work with customers and shareholders: old and new.

We will deal with the customers further on in the section concerning commercial policies: with regard to the shareholders, we can straightaway say that they have increased in number, from 36,574 at the end of 2012 to 38,194 as at 31 December 2013 and 38,559 in the first two months of 2014. Nearly two thousand individuals have joined an array, mainly made up of the same customers of the bank, which characterises Valsabbina as one of the most invested in entities among industrial co-operative banks. Each one of them contributes to the company a more or

less large part of their savings, investing them confidently, taking part in the association activities and enjoying the benefits effectively measurable in the prices of the services used and the extent of the interest rates paid on deposits rather than on those applied to loan transactions. But, among the benefits, the aspect of seeing one's investment grow over time under the form of an increase in the value of the security, rather than remuneration in dividend form, is by no means negligible. Irrespective of the difficult economic period experienced during these years of crisis, the investment in Valsabbina shares has always revealed itself to be interesting, partly because it is shielded from the risks which are characteristic to those speculative transactions which, if on the one hand may promise attractive returns, on the other without doubt cannot exclude bitter disappointment.

During 2013, around 1.2 million shares of the Bank were traded in the trading system managed by Istituto Centrale delle Banche Popolari Italiane. The price remained firm at Euro 18.

During the year, the Bank carried out the following transactions on own shares, starting off from a balance at the beginning of the year of 366,000:

- it purchased 464,570 shares at an average price of Euro 18 for Euro 8,362 thousand by virtue of the general meeting authorisations in 2012 and 2013;
- it assigned shareholders 516,600 shares at an average price of Euro 18 for a total of Euro 9,298 thousand as a dividend for 2012;
- it sold 223 shares for Euro 4 thousand.

As at 31 December 2013, own shares in the portfolio amounted to 313,747 for an equivalent value of Euro 5,664 thousand.

## **7 CAPITAL AND CAPITAL RATIOS**

Again in 2013, due to the tensions on financial markets and in view of the future enforcement of the Basel 3 rules, the degree of capitalisation of Italian banks represented a crucial element for the purposes of the stability and staying power of the national banking system.

In this context, it should be emphasised that the Bank's levels of capitalisation, after the consistent enhancement achieved by the share capital increase fully subscribed by the shareholders during 2011, also remained high in 2013, fully maintaining the ability of the Bank to ensure decisive support for the real economy also in the future, despite conditions of continuing criticality with regard to the economic and financial context.

At 31 December 2013, on the basis of the profit allocation proposal, the book value of the shareholders' equity, net of own shares held in the portfolio, amounted to Euro 382 million, more or less unchanged with respect to the previous year.

The Tier 1 regulatory capital decreased during the year from Euro 373.6 million to Euro 371.6 million due to the negative effect of the purchases of own shares in the year for Euro 5.7 million and other adjustments for Euro 0.3 million and as a result of the positive effect of the capitalisation of the profit for Euro 3.3 million and minor intangible fixed assets for Euro 0.7 million. The Tier 2 capital, which included Euro 25 million of the new subordinated loan issued, amounted to Euro 26 million.

At year end, therefore, the regulatory capital used for the purpose of calculating the capital ratios came to Euro 397.6 million. The regulatory capital, as already occurred in the last two years, benefits from the exercise by the Bank of the option permitted by the Provision issued by the Bank of Italy on 18 May 2010, which permits - for the sole purposes of calculating said regulatory capital and limited to the securities issued by European Union nations - the neutralisation of the capital losses relating to securities falling within the portfolio of available-for-sale financial assets ("AFS"). In detail, in the event of capital losses of the EU nation

securities segment, this method makes it possible not to detract the negative valuation reserve from the Tier 1 capital.

For greater disclosure details regarding the evolution of the aggregates which make up the regulatory capital, please see section F of the explanatory notes.

On a parallel, the risk-weighted assets at the end of 2013 amounted to Euro 2,726 million, which compared with the balance of Euro 2,856 million in risk assets as at 31 December 2012.

The Tier 1 capital ratio, established on the basis of the ratio between the Tier 1 capital and the risk-weighted assets, came to 13.63% at year end and the Total capital ratio - which is calculated using the total regulatory capital as the numerator - came to 14.59%, a level much higher than the minimum of 8% required by sector legislation and comfortably above the average of the entire banking system.

The change in the main capitalisation indices during the last five years presents the following trend:

	31 December 2013	31 December 2012
shareholders' equity / customer deposits	11.98%	12.20%
shareholders' equity/amounts due from customers	12.80%	12.38%
shareholders' equity/total assets	9.00%	9.23%
impaired loans/regulatory capital	101.48%	90.37%
net non-performing positions/regulatory capital	42.19%	36.31%
regulatory capital/risk-weighted assets (1)	14.58%	14.10%
core tier one	13.63%	13.08%

The entity of the equity and the ample surplus of the capital ratios with respect to the minimums required, together with the forecasts of growth in the risk-weighted assets more contained than in the more recent past - in relation to the minor demand for credit caused by the continuation of the economic crisis - makes it possible to plan harmonious growth in the dimensions of the business operations, leaving the share capital unchanged.

## 8 DEPOSITS

During 2013, the tensions seen in the previous two years with regard to funding from customers were partially diluted. The context conditions became less competitive both on the retail market and the wholesale one, mainly for two reasons: due to the minor requirements felt by companies for the funding of investments and due to the possibility of accessing instruments with an exceptional profile and range made available by the ECB within the sphere of the monetary policy guidelines.

The Bank resorted to these instruments during the moments of greatest tension at the end of 2011 and in the first few months of 2012, taking part in the LTRO programme implemented in fact by the European Central Bank: this involves 3-year loans maturing at the end of 2014 and in February 2015. At the time of presentation of the applications for both maturities, the Bank requested and obtained loans for a total of Euro 500 million, 100 million of which was repaid in advance during the first few months of 2013 due to the improved liquidity conditions.

Despite the difficult market context which characterised the whole of 2013, Banca Valsabbina once again confirmed its vocation as deposit-taking bank, deeply entrenched in its area, achieving appreciable results both with respect to the average of the small and medium-sized banks and with respect to the large banking groups of national importance, the attention of which with regard to retail customers is focused on offsetting the difficulties of funding on international markets, whose costs - unfortunately - suffer the Italy risk.

Total direct deposits thus rose in 2013, on a like-for-like basis, by 1.5%, reaching a total of Euro 3,185 million; this result was made possible thanks to the considerable efforts made by the area network, directed in particular at restricted time deposits represented by both bonds and time deposits, by now recognised and having made a name for themselves on the market due to the simplicity and immediacy of their technical structure.

This result appears even more significant if one considers that in 2013, in the presence of the already stiff competition within the banking sphere, the powerful supply capacity of the Government continued, placing public debt securities granting the subscribers significant returns, made even more interesting by the preferential tax regime.

With regard to the evolution of the aggregates referring to the individual technical forms of funding, emphasis should be made of the positive increase in current accounts with a balance of Euro 1,532 million, (+9.6%), which bears further witness to the favour granted by the customers vis-à-vis the Bank, and the appreciable staying power of the bonds at Euro 1,229 million (-3.1%), thanks to the attention paid during the year to the new issues, mainly fixed rate, so as to take into account both the need to safeguard suitable balances in the structure of the rates and the need to achieve a lengthening of the maturities. The result is even more appreciable since during the year subordinated bonds issued in 2008 for a total of Euro 140 million matured.

Within the sphere of the subordinated bonds issue programme, amounting in total to Euro 150 million for the purpose of a further capital enhancement, Euro 25 million in subordinated bonds were placed in December. Another Euro 35 million were placed at the end of February 2014.

As of 31 December 2013, the breakdown of funding was as follows:

Customer deposits (Euro 000s)	31 Dec. 2013	31 Dec. 2012	Change	
			Amount	%
Savings deposits	44,446	55,498	(11,052)	(19.91%)
Current accounts	1,531,697	1,398,126	133,571	9.55%
Bonds	1,228,746	1,268,310	(39,564)	(3.12%)
<i>of which: Subordinated bonds</i>	<i>25,003</i>	<i>139,283</i>	<i>(114,280)</i>	<i>(82.05%)</i>
Certificates of deposit	8,709	3,436	5,273	NS
Time deposits	370,285	411,764	(41,479)	(10.07%)
Other funding	691	681	10	1.47%
<b>Total direct funding</b>	<b>3,184,574</b>	<b>3,137,815</b>	<b>46,759</b>	<b>1.49%</b>

The change in bonds during the year, at face value, discloses issues for Euro 448 million and redemptions for Euro 522 million. The balance of Euro 1,216 million differs from the previous table, which states the bonds at amortised cost, because gross of the bonds repurchased and net of the interest accrual maturing.

Change in bond issues at face value (Euro 000s)				
		2013		2012
<b>Bonds in circulation at 1 Jan. 2013</b>		<b>1,289,897</b>		<b>1,233,173</b>
Bonds issued:		448,083		354,985
of which: fixed rate	428,114		294,761	
step up			58,044	
mixed rate	19,969		2,180	
Matured bonds		(521,642)		(298,261)
of which: fixed rate	(343,494)		(247,061)	
floating rate	(147,700)		(48,200)	
step up	(11,924)			
mixed rate - zero coupon	(18,524)		(3,000)	
<b>Bonds in circulation at 31 Dec. 2013</b>		<b>1,216,338</b>		<b>1,289,897</b>

Indirect deposits also disclosed a positive trend. At the end of 2013, they amounted to Euro 1,162 million compared with Euro 1,073 million as at 31 December 2012 (+ Euro 90 million or 8.4%). The increase is partly attributable to the improvement in the stock market value of the shares, but above all else it is the result of a careful commercial policy aimed at asset management in mutual funds and that which is insurance-related. The two segments achieved 29% of the total of indirect deposits, compared with 25% last year, leading to an increase in mutual funds of 20.2% and insurance asset management of 32.4%.

Total funding therefore rose at the end of 2013 to Euro 4,347 million, with an annual increase of 3.2%.

## 9 LOANS

With regard to loans, the Bank was also affected by the system dynamics. At the end of November, the drop in bank loans to businesses came to 5.8% when compared with the previous November. Demand for credit remained weak. At the end of 2013, the mass of receivables amounted to around Euro 3 billion, disclosing a decrease, what is more lower than the national average, of 3.5% when compared with 31 December 2012, of which in relation to businesses - 5.2% and in relation to households -1.4%. Irrespective of any emphatic representation, the figures show how - especially at times of recognised “credit crunch” - Banca Valsabbina has been in a position to remain faithful to its commitments to support the manufacturing system and accompany households in projects which require the support of the bank close at hand in the area and the sensitivity of the relationship with the customer.

The particular attention paid to the needs of the companies in one of the areas of greatest entrepreneurial vocation in the country - and therefore with more intense demand for credit and lending services - is proven by the promptness and versatility with which the Bank has activated its own or system instruments so as to permit customers in temporary difficulty, but worthy of trust, to deal with the negative effects of the serious economic crisis. In this context, having verified the compliance with the requirements established at system level, the Bank has accepted further applications from businesses in difficulty within the sphere of the moratorium of the debts of small and medium-sized companies furthered by ABI (Italian Banking Association), the Ministry of the Economy and finance and the trade and consumer associations. Again with a view to providing support and assistance in company situations of greatest criticality, the Bank has subsequently facilitated - for the part it is responsible for - access to regulated procedures which permit them to overcome the state of crisis: unconditional arrangement with creditors (Art. 161 of It. Bankruptcy Law), debt restructuring agreements as per Article 182 *bis* of It. Bankruptcy Law and arrangement with the business as going-concern (Art. 186 *bis* of It. Bankruptcy Law) as well as the turnaround plans (Art. 67 of It. Bankruptcy Law).

Passing on to examine the change in the composition of loans by technical form, at the end of 2013 current accounts in credit and advances subject to due reserve amounted to Euro 611 million, while mortgage loans totalled Euro 1,675 million.

The change in the composition of loans by technical form in 2013 is presented as follows:

Loans to customers (Euro 000s)	31 Dec. 2013	31 Dec. 2012	Change	
			Amount	%
Current accounts	610,895	677,265	(66,370)	(9.80%)
Mortgage loans	1,675,305	1,746,795	(71,490)	(4.09%)
Personal loans	3,643	8,315	(4,672)	(56.19%)
Other financing	288,800	294,635	(5,835)	(1.98%)
Impaired loans	403,527	363,811	39,716	10.92%
<b>Total loans to customers</b>	<b>2,982,170</b>	<b>3,090,821</b>	<b>(108,651)</b>	<b>(3.52%)</b>



During 2013, the effective initiative continued in the specific sector of microcredit addressing business in the Brescia and Verona areas who are not customers, who in fact bear the features of micro-businesses: turnover no higher than Euro 2 million and a maximum of nine employees; by means of this initiative, 343 procedures were finalised for a total of Euro 16.7 million, for unit amounts ranging between Euro 20 thousand and Euro 100 thousand, backed by government guarantees up to 70% of the amount via Mediocredito Centrale.

The loans granted with government backing via Mediocredito Centrale came to 618 in number for a total amount of Euro 80.5 million.

Lending support for households also continued at significant levels. Mortgage loans granted to the same for the purchase of their first home numbered 365, for a total of Euro 51 million.

<b>MEDIUM/LONG-TERM DISBURSEMENTS (amounts)</b>	<b>2013</b>		<b>2012</b>	
<b>A) Directly using funds of the Bank</b>	<b>Trans. No.</b>	<b>Amount</b>	<b>Trans. No.</b>	<b>Amount</b>
Loans with Mediocredito Centrale backing made available	618	80,475	577	80,831
Former Artigiancassa loans	-		4	734
Artisan loans backed by surety of the Credit Guarantee	198	10,337	224	14,454
Ordinary mortgage, building and land loans	795	184,524	1,067	250,285
Loans and mortgages to Shareholders of the Bank	754	11,071	715	10,730
Mortgage-secured current accounts	8	8,710	3	1,990
<b>B) Indirectly as intermediary of specialised Institutes</b>				
Leasing transactions	134	12,307	77	9,027

The breakdown of customers granted credit by category of credit facility confirms the strategy adopted by the Bank of pursuing a suitable fractioning of the loan portfolio and preferring credit to households and small-to-medium-sized companies which represent the reference customers in the area of choice.

<b>Number of customers granted credit facilities broken down by credit facility category</b>						
	<b>2013</b>	<b>% of total</b>	<b>2012</b>	<b>% of total</b>	<b>2011</b>	<b>% of total</b>
Up to Euro 40,000	13,939	4.0	13,591	3.7	12,798	3.5
Between Euro 40,001 and Euro	5,743	11.8	5,532	10.8	4,918	9.8
Between Euro 125,001 and Euro	2,950	13.6	3,004	13.0	2,690	11.9
Between Euro 250,001 and Euro	1,310	12.2	1,482	13.0	1,321	12
Between Euro 500,001 and Euro	722	13.2	791	13.8	756	13.6
Between Euro 1,000,001 and	559	27.9	613	28.7	622	30.8
Over Euro 5,000,001	67	17.3	72	17.0	74	18.4
<b>Total</b>	<b>25,290</b>	<b>100.0</b>	<b>25,085</b>	<b>100.0</b>	<b>23,179</b>	<b>100</b>

The numbers shown in the table are the result of the lending policy pursued and implemented during the year, aimed at the expansion of the customer base and the reduction of the risk concentration: the customers with loans under the threshold of Euro 500 thousand rose during the year from 40.5% to 41.6% (37.2% in 2011) and those with credit facilities over Euro 1 million fell from 45.7% to 45.2% (49.2% in 2011).

Also the breakdown of the loan portfolio by business activities shows itself to be balanced, taking into account the average system figures referring to the areas in which the Bank is present:

	Sectors of business activities	2013	2012	2011	2010	2009
1	Private concerns	23.30	22.64	22.29	20.74	21.34
2	Other services	18.07	17.91	19.41	19.19	20.99
3	Sundry engineering services	10.25	10.73	11.26	11.15	10.14
4	Wholesale commerce	9.11	8.90	8.67	9.11	7.98
5	Construction and public works	8.72	9.16	9.79	9.51	9.88
6	Retail commerce and public service	4.99	4.92	4.81	4.71	4.67
7	Agriculture, forestry and fishing	2.57	2.57	2.38	2.16	2.35
8	Financial companies	2.56	2.23	0.44	1.64	1.86
9	Foodstuffs and beverages	2.42	2.62	2.19	2.29	2.2
10	Agricultural and industrial machinery	2.17	2.05	2.30	2.43	2.82
11	Textile products and clothing	1.88	2.08	2.10	2.02	2.11
12	Wood, furniture and other industrial	1.83	1.91	2.06	2.24	2.1
13	Construction materials	1.73	1.57	1.69	1.41	1.62
14	Transport services	1.51	1.52	1.33	1.30	1.38
15	Iron and steel industries	1.44	1.30	1.53	2.29	1.62
16	Electricity, energy and chemical products	1.40	1.60	1.33	0.92	0.85
17	Rubber and plastic products	1.39	1.45	1.55	1.80	1.4
18	Electrical supplies and materials	1.13	1.18	1.02	1.16	1.05
19	Public administration authorities	0.75	0.75	0.92	0.51	0.1
20	Vehicle repairs and sundry articles	0.72	0.68	0.68	0.79	0.64
21	Glass and ceramic industries	0.60	0.60	0.69	0.67	0.67
22	Paper and publishing	0.55	0.63	0.52	0.65	0.5
23	Means of transport	0.44	0.49	0.62	0.63	0.77
24	Non-ferrous metal industries	0.32	0.34	0.25	0.48	0.41
25	Fine and precision engineering	0.15	0.17	0.17	0.20	0.55
		100.00	100.00	100.00	100.00	100.00

During the year, the policies for selecting and handling the credit facilities were appropriately reviewed and streamlined so as to deal with the generalised decline in the loan portfolio, caused by the considerable deterioration of the economic operating context, especially in those sectors where the local economy is more inclined and the bank consequently committed; in this sense, additional procedural and organisational stratagems have been adopted suitable for intensifying the efficacy of the monitoring and the accuracy of the control safeguards on the facilities granted, which are of particular importance for limiting the rise in loans at risk as far as possible. Thus, despite the continuation of the economic crisis which has led to the further weakening of the traditional solidity of the fabric of small-to-medium-sized business also in our area - in particular in the construction sector and related side-lines, the engineering and transformer machinery sectors - it has inevitably had repercussions on the risk profile of the Bank's loan portfolio.

The overall incidence of net impaired loans - which rose to Euro 403.5 million (+10.9%) - out of total net loans, in fact increased from 11.77% at the end of 2012 to 13.53%, also if with respect to recent years a certain slowdown can be seen in the related growth rate.

During 2013, the total net amount of non-performing positions passed from Euro 146.2 million to Euro 167.8 million, equal to 5.62% of net loans.

Within this sphere, suitable disclosure must be provided on the decision of the Board of Directors to carry out without recourse factoring of 1,114 non-performing positions for a gross value of Euro 65.4 million, for the purpose of simplifying the legal and administrative activities for debt recovery reducing the related management costs. The assignment, which concerned loans almost entirely written down, penalised the percentage rate of coverage of the non-performing positions which fell from 40.8% to 34.9%. The coverage, in the absence of the

transaction, would have been 40.85% and, also including positions written off during the year, 46.42%.

The coverage reflects the presence, for the majority of these loans, of suitable secured guarantees valued in relation to the consistency and quality of the underlying assets and the related estimated realisable value. Net non-performing loans, backed by secured guarantee and by government guarantee via Mediocredito Centrale, represent 69% of the net non-performing positions.

With regard to watchlist and restructured loans, these were essentially unchanged, having increased from 5.74% to 6.01% of total net loans, while the related degree of coverage prudently rose from 9.24% to 9.8%. 62% of the watchlist loans are backed by secured collateral.

The increase in past due positions, in conclusion, from Euro 40.1 million to Euro 56.6 million, is attributable to the difficult economic situation. These are positions persistently in overdraft or with instalments past due by more than 90 days.

The following table shows the breakdown of impaired loans, with disaggregation of the figures for the individual categories envisaged by supervisory legislation, and the related percentage out of total net loans, compared with 2012:

<b>31 December 2013</b>					
<b>Type of exposure/values (amounts in Euro 000s)</b>	<b>Gross exposure</b>	<b>Specific adjustments</b>	<b>Forfeit adjustments</b>	<b>Net exposure</b>	<b>% of total</b>
a) Non-performing	257,599	89,834	-	167,765	5.62%
b) Watchlist	179,518	17,252	-	162,266	5.44%
c) Restructured exposures	19,070	2,201	-	16,869	0.57%
d) Past due exposures	58,802	2175	-	56,627	1.90%
Total impaired loans	514,989	111,462	-	403,527	13.53%
e) Performing loans	2,594,561	-	15,918	2,578,643	
Total	3,109,550	111,462	15,918	2,982,170	

<b>31 December 2012</b>					
<b>Type of exposure/values (amounts in Euro 000s)</b>	<b>Gross exposure</b>	<b>Specific adjustments</b>	<b>Forfeit adjustments</b>	<b>Net exposure</b>	<b>% of total</b>
a) Non-performing	246,803	100,605	-	146,198	4.73%
b) Watchlist	181,555	16,792	-	164,763	5.33%
c) Restructured exposures	13,997	1,279	-	12,718	0.41%
d) Past due exposures	40,928	796	-	40,132	1.30%
Total impaired loans	483,283	119,472	-	363,811	11.77%
e) Performing loans	2,741,745	-	14,735	2,727,010	
Total	3,225,028	119,472	14,735	3,090,821	

Also “performing” loans, which amounted to Euro 2,579 million at the end of 2013, compared with Euro 2,727 million as at 31 December 2012 (-5.7%), were subject to forfeit write-down which was raised in the year to 0.61%, compared with 0.54% in the previous year - for a total of Euro 16 million.

The total amount of the value adjustments appears suitable for covering the risks inherent in the entire loan portfolio, having taken into account its structure and composition, the features of the customers granted credit - mainly private individuals, professional and small-to-medium sized businesses - and the related guarantees.

The loan cost, amounting to the ratio between losses and write-downs booked to the income statement and the loans recognised in the financial statements, came to 1.53% compared with 1.83% in the previous year.

The change in the last five years with regard to the balances of the various categories of loans at risk, the related indicators and the respective degrees of coverage, is presented below:

<b>Net exposure (amounts in Euro 000s)</b>	<b>31 December 2013</b>	<b>31 December 2012</b>
Non-performing loans	167,765	146,198
Watchlist and restructured loans	179,135	177,481
Past due exposures	56,627	40,132
<b>Total</b>	<b>403,527</b>	<b>363,811</b>
<b>Performing loans</b>	<b>2,578,643</b>	<b>2,727,010</b>
<b>Total net loans</b>	<b>2,982,170</b>	<b>3,090,821</b>

<b>LOAN QUALITY RATIOS</b>	<b>31 Dec. 2013</b>	<b>31 Dec. 2012</b>
<b>on gross loans</b>		
% of non-performing positions out of total gross	8.28%	7.65%
% of watchlist and restructured positions out of	6.39%	6.06%
% of past due positions out of total gross loans	1.89%	1.27%
% of doubtful positions out of total gross loans	16.56%	14.99%
<b>coverage percentages</b>		
Non-performing loans	34.87%**	40.76%
Watchlist and restructured loans	9.80%	9.24%
Past due exposures	3.70%	1.94%
Total out of impaired loans	21.64%**	24.72%
Performing loans	0.61%	0.54%

\*\* reduction to be ascribed to the disposal of more than Euro 65 million in non-performing loans

<b>percentages on net loans</b>		
% of non-performing positions out of total net	5.62%	4.73%
% of watchlist and restructured positions out of	6.01%	5.74%
% of past due positions out of total net loans	1.90%	1.30%
<b>% of doubtful positions out of total net loans</b>	<b>13.53%</b>	<b>11.77%</b>

## **10 FINANCIAL ASSETS AND TREASURY ACTIVITIES AND THE EQUITY INVESTMENTS**

With reference to the initial section of this report, the accommodating monetary policy of the European Central Bank represented, for all the banks, a favourable opportunity for the positive repercussions caused on the income statements in periods of significant difficulty for the core management of the banks. Using the sums made available by the ECB, in fact, correlated investments were made in Italian government securities considering the weak demand for credit shown by the economy and pending a new expansive phase. The greater entity of the portfolio made it possible to benefit from the improvement in share prices which, with alternating movements, consolidated towards the end of the year, making it possible to generate profits on the disposal of financial assets for Euro 26.4 million (Euro 31.7 million in 2012).

Financial assets and liabilities comprise:

Financial assets and liabilities (amounts in Euro 000s)	31 December 2013	31 December 2012
20 Financial assets held for trading	197	157
40 Available-for-sale financial assets	1,012,280	845,165
60 Amounts due from banks	114,234	91,273
100 Equity investments	1,375	170
<b>Total</b>	<b>1,128,086</b>	<b>936,765</b>
10 Amounts due to banks	(585,598)	(522,492)

Available-for-sale financial assets rose from Euro 845 million at the end of 2012 to Euro 1,012 million and mainly comprise government securities, essentially fixed rate. In detail, BTPs (long-term treasury bonds) represent 71.56% of the aggregate, CCTs (treasury certificates) 7.13%, BOTs (treasury bills) and CTZ (zero coupon treasury certificates) 21.31%

(amounts in Euro 000s)	31 Dec. 2012	% of portfolio	31 Dec. 2012	% of portfolio
Italian government securities	978,744	96.69%	787,894	93.22%
Other bonds	4,437	0.44%	17,461	2.07%
Units of mutual investment funds	13,676	1.35%	15,787	1.87%
Equities	15,423	1.52%	24,023	2.84%
<b>Total</b>	<b>1,012,280</b>	<b>100.00</b>	<b>845,165</b>	<b>100.00%</b>

On the basis of their maturity, Italian government securities (sovereign debt) are broken down as follows (amounts in Euro 000s):

Duration	31 Dec. 2013	% of aggregate	31 Dec. 2012	% of aggregate
up to one year	266,210	27.20%	210,621	26.73%
between 1 and 2 years	74,374	7.60%	149,313	18.95%
between 2 and 3 years	57,870	5.91%	87,137	11.06%
between 3 and 5 years	211,259	21.59%	156,308	19.84%
between 6 and 10 years	241,068	24.63%	132,280	16.79%
beyond 10 years	127,963	13.07%	52,235	6.63%
<b>Total government securities</b>	<b>978,744</b>	<b>100.00%</b>	<b>787,894</b>	<b>100.00%</b>

The average duration of the Bank's portfolio as at 31 December 2013 came to 3.88 compared with 2.87 as at 31 December 2012.

The list of the equities held by the Bank for the purpose of long-term investment, with the changes with respect to the previous year, is presented in the following table.

Description (amounts in Euro 000s)	Balance as at 31 Dec. 2012	Purchases	Sales	Impairment	Impairment	Balance as of 31 Dec. 2013	No. of shares or holdings	% holding
				to income statement	to shareholders' equity			
Ist. Centr. Banche Pop.	673					673	12,162	0.08%
UBI Leasing SpA	2,609			(476)		2,133	405,550	1.01%
Unione Fiduciaria SpA	28					28	4,320	0.40%
Swift SC	1					1	2	0.02%
SSB SpA	1					1	8,147	0.01%
Consulting SpA	24					24	22,500	15.00%
Gruppo Azione Locale	1					1	1	1.53%
Arca Sgr Spa	288					288	590,000	
Cedacri Spa	2,754	324			(301)	2,777	292	2.32%
Pieffe assicurazioni srl	3					3	1	15.00%
Consorzio servizi srl	2					2	1	
Banca Popolare Cividale	2,070					2,070	84,500	
Carife	9,433			(5,048)		4,385	476,190	1.13%
Banca Popolare di	2,026	101				2,127	34,029	
Banca Etruria	145	1,530			(765)	910	1,769,418	
Aedes	573		(573)			0		
Credito Valtellinese	1,749		(1,749)			0		
UBI Banca ScpA	739		(739)			0		
Intesa - San Paolo SpA	39		(39)			0		
Deutsche Bank	660		(660)			0		
Telecom	205		(205)			0		
<b>TOTAL SHARES</b>	<b>24,023</b>	<b>1,955</b>	<b>(3,965)</b>	<b>(5,524)</b>	<b>(1,066)</b>	<b>15,423</b>		

The equity investments increased from Euro 171 thousand to Euro 1,375 thousand due to the purchase of 9.8% of Polis Fondi Immobiliari di Banche popolari Sgr p.A.. The acquisition was made for the prospective interest in the evolution of the real estate property sector which at present is particularly depressed.

### Equity investment in Valsabbina Real Estate

As at 31 December 2013, the fourth accounting period of Valsabbina Real Estate closed, during which a number of initiatives were put together to support the non-performing loans of the Bank. During the year, Valsabbina Real Estate obtained 18 properties for industrial, non-industrial and commercial use; as at 31 December 2013, the amounts recorded under the balance sheet receivables, since there is still not any justification to record them under the inventory properties, amounted to Euro 3,892 thousand, while the transfer deeds were issued relating to 7 assets for Euro 5,070 thousand.

The overall value of the properties recorded under inventories amounted to Euro 5,760 thousand compared with Euro 2,269 thousand as at 31 December 2012 due to:

- the assignment of 7 properties for Euro 5,070 thousand;
- the disposal of an industrial property for Euro 1,175 thousand, generating a capital gain of around Euro 190 thousand;
- the conferral of two of the properties assigned under auction to the real estate property fund "Fondo Asset Bancari IV", managed by Polis Fondi Immobiliari di Banche Popolari Sgr p.A., for a total of Euro 580 thousand.

As a result of the conferral, 3 units of the fund were received, for an overall value of Euro 750 thousand, supplemented by a cash payment of Euro 170 thousand. The three units were sold at the same time at the same value to the group parent Banca Valsabbina.

The properties were acquired using the opening of current account credit, granted by Banca Valsabbina and regulated at market rates, which at 31 December 2013, presented use of Euro 9,526 thousand.

The shareholders' equity of the subsidiary, inclusive of the loss, amounts to Euro 131 thousand.

With regard to the income statement, the value of production amounted to Euro 1,766 thousand, of which Euro 1,755 thousand for the sale of properties and Euro 11 thousand for leasing fees.

2013 closed with a loss of Euro 25 thousand as indicated below:

Value of production	Euro 1,766
Costs for services	- Euro 77
Operating expense	- Euro 25
Difference between costs for purchases of properties and the	- Euro 1,580
Gross result net of interest and taxes	Euro 84
Interest expense	- Euro 92
Tax	- Euro 17
Loss for the year	- Euro 25

Consolidated financial statements are not drawn up due to the limited significance and relevance of the balances of the subsidiary with respect to those of the parent company, as emerges from the "Systematic framework for the preparation and presentation of the financial statements", which represents the conceptual model underlying the IAS standards. The financial statement total of the subsidiary (Euro 9.6 million) is also lower than the limits envisaged by the Supervisory instructions for exemption from the consolidated indications (financial statement assets less than Euro 10 million).

## 11 BUSINESS STRATEGIES

On the first page of this report we disclosed that on 27 November 2013 the Bank's Board of Directors had approved the 2014-2016 Strategic Plan, which outlines the business development policies for the three-year period and identifies the measures to be adopted for the achievement of important efficiency, profitability and competitiveness objectives in a scenario of growth aimed at the creation of value over time for the shareholders, the customers and the entire reference community.

The fundamental assumptions which enliven and develop the dimension of the Plan are ingrained in the valorisation of the people's and industrial co-operative Bank model: a model which, as already indicated, has shown a great ability to deal with the stress caused by five years of financial and structural-debt crisis and has made the competitive and positioning profiles recognisable, entirely singular, with respect to all the other categories of intermediaries.

The Plan takes into account important system events - such as the new Basel 3 regulatory set up which, besides higher levels of capital, introduces limits to the financial leverage and new liquidity requirements to ensure a bank financial statement structure which is more resistant over the short term and more balanced over the mid-term - and the profound changes underway in a still unsettled economic and financial context. It also takes into account, with regard to the



internal management profiles, the reshaping of the organisational set ups resolved last Spring further to the events affecting senior Executives.

In light of such fundamental premises, the Plan has identified the following strategic lines:

- Geographic development by internal lines
- Commercial policies with attention to qualitative and price of the services profiles
- The improvement in the profitability
- The maintenance of a balance in the structural liquidity
- The maintenance of a more than adequate level of Regulatory capital
- The handling of the risks with particular focus on the credit risk.

The importance of the stated programmatic lines, also from the point of view of the project-related and organisational commitment for their implementation, prompts us to develop a number of summary notes commenting in the individual spheres.

With regard to geographic development, over the last few years the Bank has seen growth in the commercial network, achieved both by internal lines with the 2007 - 2009 branches plan and external lines via the acquisition of Credito Veronese. The current structure of the sales network, based on 61 branches located in the provinces of Brescia (50), Verona (7), Trento (3) and Mantua (1), appears suitable for ensuring an effective coverage of the area, also due to the consistency of the logics which have supported the decisions to expand and cover the areas served over the years. Nevertheless - in light of the lengthening of the timescales for achievement of the break-even in the opening of new branches - areas have been identified for a rationalisation of said network, or rather for an improvement in the efficiency profiles. In this sense, the closure of the Ponte Caffaro branch has been envisaged, counting on the vicinity of the neighbouring branch in Lodrone.

In April, following the closure of Ponte Caffaro, the opening of a new branch in Corso Milano, Verona is envisaged.

The financial centers in which to locate the newly-opened branches are being pin-pointed.

For such purposes, a branch plan for the opening of 4 new branches will be presented.

The subject of geographic organisation links up closely to the second point of the Plan, that relating to the sales policies which - confirming the target of households and small-to-medium sized businesses as that closest to the history and the background of the economic reference market - focus on the consolidation of the volumes brokered, the expansion of the number of shareholders and customers and the specialisation of the services with a view to the emancipation of the operational relationships. The funding policies will comply with criteria which show preference for the maintenance of a strong component of the aggregate over the mid-term, while those regarding loans are aimed at splitting the risk and the further development of the channel of micro-credit and the loans backed by Mediocredito Centrale with regard to businesses, and home mortgage loans for households.

A precise commitment - which has taken on substance with the creation of a new specialist division - will be dedicated to the foreign intermediation sector, in tune with the strong vocation in this sense expressed by the local manufacturing industry.

Again with reference to industrial customers, the Bank then deems that it can reserve, via partnership agreements with selected counterparts, assistance and consulting in services with greater value and qualification such as generational changeovers, the restructuring plans and the extraordinary finance projects.

The analysis carried out at the time the Plan was drawn up, also supported by the studies of the leading research companies which we mentioned in the initial part of this report, subsequently confirmed the need to ensure suitable investments, economic but above all else involving entrepreneurial logic, for the “On-line Bank” channels, the Bankassurance division and the enhancement of the commercial offer within the sphere of the products and investment services:



from this point of view, the provision of the financial advisory service will be extended to private customers, since the Bank is able to count on trained professionals and on method-based and IT supports widely experimented.

The strategic way of thinking which animates the policies just outlined certainly does not neglect the aim, inalienable for the stability of the equity and financial set ups, of developing suitable levels of profitability in periods characterised by low interest rates, and therefore margins, and by great needs for requalification of loan assets. The Plan policies envisage in this connection structured measures which range from the balanced re-drafting of the pricing of the loans, for the purpose of correctly pricing the risk containing the related cost, an increase in the commission-based contributions and measures for the active management of the liquidity and cash management which permit greater margins in the financial component.

The streamlining of the management (application approval and monitoring) and recovery stage for the stocks of impaired loans, liable to produce the most significant effects for the improvement of the profitability, complete the structured framework of the initiatives on which the specialist divisions, as much as the network structures will be employed over the coming years.

In detail, for the purpose of containing the negative effects of the current economic cycle phase on the quality of the assets, back in 2013 the Board of Directors, upon the proposal of General Management, launched an in-depth review of the loan monitoring process, with the creation of a specialist division and the adoption of an *ad hoc* procedure, for the purpose of picking up on the signs of deterioration in lending relationships in time.

Another line of the Plan is represented by the subject of liquidity, with regard to which the objective of maintaining a prudent profile is preliminarily undertaken, via a ratio between loans and funding lower than the unit. Direct deposits from retail customers, whose balances are traditionally more stable also in periods of more acute stress, and the maintenance of the current loans with the ECB - appeased by the expectations of stability in the monetary policies - will play an important role in the achievement of the sought-after structural balances of the liquidity.

The subject of the regulatory capital thus adopts entirely singular importance in the three-year Strategic plan, whose dimensions give rise to the development abilities under conditions of safety, stability, and safeguarding of the correlated economic and financial balances. We have reported with candid satisfaction on the previous page with regard to the consistency of the assets which make up the regulatory capital and we can add here that the objective of consolidating the appreciable parameters which have from time immemorial characterised the positioning of the bank with respect to many competitors on the national and local scene is truly strategic. The achievement of this priority objective lies in the forecast of contained growth of the exposures to risks, correlated exclusively to the rise in business volumes. With regard to the section on risks, whose supervision the three-year Strategic Plan dedicates ample space to since their dynamics directly affect the capital consumption, we will make reference in the specific comments made further on the report.

For the entire duration of the Plan - partly thanks to a subordinated issues programme with direct placement care of customers - the Bank believes that it will thus be able to maintain the capital requirements higher than the more stringent ones which will enter into force in 2019 with Basel 3. In proximity to the expiry of the Plan and on an consistent basis with the evolution of the economic scenario, also the appropriateness of a capital enhancement may possibly be assessed, via means of the classic instrument of the share capital increase, rather than with the issue of convertible bonds.

On conclusion of the summary review carried out with regard to the business strategies, we can ensure in this venue that Senior Management will dedicate constant and systematic support activities to the implementation and co-ordination effort which the entire structure - involved as from the analysis stages and until those for presentation and discussion of the Plan - is required to make in this period of challenges and changes.

## **12 THE NEW ORGANISATIONAL SET-UPS**

In continuity with the handling of the topics of significant strategic importance, we believe it appropriate to disclose in this section the important decisions adopted last Spring by the Board of Directors with regard to organisational set ups.

As already mentioned in the context of the previous Report, Mr. Spartaco Gafforini had communicated his decision to conclude his working activities at the end of April 2013 after managing the bank for many years.

The need, unanimously agreed on, to ensure continuity for the management policies - clearly without prejudice to the natural diversities in approach caused by the speed and intensity of the change in the rules and the market - guided the Board of Directors, for the replacement of the General Manager, towards an internal-type of solution, shielded from those risks which businesses frequently run into when the value and the qualities of the individuals who have grown within their senior management teams are unknown.

In the specific case, the Deputy General Manager Mr. Barbieri was identified, due to his professional and human traits, but also the managerial versatility tried and tested over ten years in his current role, the feature most in keeping with the profile sought for heading up the Executives.

The new General Manager undertook responsibility for the office as from 1 May 2013 and, as is common practice at the time of any change in the senior management of companies, the Board of Directors examined and unanimously agreed on the proposal made by Mr. Barbieri for a new General Management set up - also having been determined by the need to cover the position left vacant - and for a reshaping of the senior level of the organisational structures again within the sphere of the professional expertise already present in-house.

The head of Internal Auditing Mr. Tonino Fornari was thus called to cover the position of Deputy General Manager, an individual of proven management expertise and sensitivity due to the experience accrued in specialist spheres and, more recently, in the delicate and extended areas of auditing.

The distinct complementary nature of expertise and aptitude harmoniously created during years of respectful collaboration are the basis for a promising entente between the two highest executives who have launched a new course providing proof of ability, spirit of initiative and managerial method.

At the same time as the appointments mentioned, the Board of Directors implemented a reshaping of the main organisational positions, creating two new central Divisions which report directly to General Management and which have been assigned to the responsibility of an equal number of executives with sure experience and decision-making ability.

The first is the Market Division, run by Mr. Marco Bonetti, who in fact oversees the governance of the production departments and the sales network by means of the co-ordination of the Commercial, Loans, Financial, Foreign Goods Sectors, the Strategic Marketing, Planning and Products Sectors as well as the Trend Monitoring Service.

Particular significance is undertaken within Division by the role undertaken by the Commercial Sector, entrusted to Pierangelo Fanelli, enhanced so as to ensure an incisive operating presence in the area.

The second is the General Affairs and Organisation Division, run by Mr. Walter Piccini, which ensures the delicate relationship between company bodies and departments, in observance of the supervisory regulations concerning corporate governance, and which implements the role for co-ordination of important departments, such as Personnel and Organisation.

The innovation introduced in the organisational scheme has revealed itself, at a distance of nearly a year, to be efficient and productive of tangible results, above all else because it has been accompanied and supported by an accurate review - also in terms of scaling and qualification of the staff - of the functional sphere of the entire structure with a view to improvement of the efficiency, efficacy and operational cost-effectiveness profiles of both the production and sales apparatus and of those dedicated to the system of controls, as we will see in the section will follow.

### **13 THE INTERNAL CONTROLS SYSTEM**

A clear and timely identification of the risks which the Bank is potentially exposed to is an indispensable condition for the informed undertaking and accurate valuation of said risks, implemented by means of the use of effective instruments and appropriate techniques for gauging, mitigation and handling. Once again in 2013, the Board of Directors dedicated particular attention and sensitivity to internal controls, convinced that the competitiveness of the company and its stability over the mid/long-term cannot do without - in observance of the principles of sound and prudent management - an integrated and efficient system which involves - according to skills which are the prerogative of the various roles - the management body, the board of statutory auditors, general management, the departments appointed due to specific legislative provisions and the staff. All and at every level, if it is true - as it is within our company - that the audit system represents an integral part of daily operations.

Within this fundamental assumption, the array of business risks is overseen within the context of precise organisational references according to a model which uses methods and procedures aimed at ensuring the efficacy and efficiency of the operating processes, guaranteeing the reliability and integrity of the information and checking the observance of legislation in recurrent operations.

Outlining the profiles and the features of the bodies and the internal control divisions, we cannot fail to remember preliminarily that following the merger via incorporation of Credito Veronese S.p.A., in December 2012, the Banca Valsabbina Group is currently made up of the group parent Banca Valsabbina S.C.p.A. and the subsidiary Valsabbina Real Estate S.r.l., an operating company active in the real estate sector, whose share capital is wholly-owned by the group parent.

With reference to this scope, the Bank's organisational structure envisages, within the specific sphere of the internal controls, the following departments:

- The internal audit department (known as the Internal Audit Service)
- The compliance control department (known as the Compliance Service)
- The risk management department (known as the Risk Management Service)
- The department tasked with preventing and fighting the achievement of laundering and terrorism funding transactions (known as the Anti-money Laundering Service), whose Head is assigned the appointment of "Appointee as per Article 42 of It. leg. Decree No. 231/2007" in relation to the reporting of suspect transactions, as well as reference individual for aggregate anti-money laundering reports (S.ar.a.).

In relation to the activities carried out by the control departments, the Compliance Service continued with the activities aimed at ensuring the compliance of the policies and the internal procedures concerning the provision of investments and accessory services, with particular reference to the checking of observance of the provisions regarding conflicts of interest, incentives and execution of orders. The service has also dedicated specific sections of intervention to numerous compliance profiles regarding transparency and correctness of dealings with customers, as well as the checking, in as far as it is responsible, of the compliance of the remuneration and incentive systems adopted by the Bank with the supervisory provisions and the specific recommendations made by the Bank of Italy to the entire banking system in relation to the various spheres of operations. The Compliance Service subsequently carried out, as envisaged by legislation, an important assistance function in the prior definition of the adaptations of the internal regulations to the new legislation which came into force during the year.

The risk management department, known as Risk Management, is by contrast the unit responsible for the assessment and gauging of the risks, in an aggregate logic, aimed at the determination of the overall internal capital. Within the sphere of responsibility, the department further streamlined the methods and the instruments to support the monitoring of the coherence of the Bank's evolution in terms of equity and financial balance on the basis of the Supervisory indications of the Bank of Italy and the limits established by the Board of Directors.

The activities carried out by Risk Management within the context of the discipline of the internal controls system will find accurate representation in the following section reserved for risk management.

Also the Internal Audit Service, which in the hierarchy of the apparatus performs a third level function role, has carried out - in observance of the agenda established in the annual plan - a wide programme of checks, both remote and care of the various operating units; checks which concerned the main activities carried out in central services and the operations of the sales network.

The controls carried out on the central departments were mainly concentrated on the loan sector, on the administration sector, on the commercial sector and on the financial one. The main verification measures inherent to specific operating processes by contrast concerned the adequacy and efficacy of the anti-money laundering safeguards - which will be dealt with in more detail in the following section concerning legislative innovations - the register, the loans process, the handling of checks, credit transfer, debit and credit cards, current accounts, savings deposits, sundry operations and securities. Within the sphere of the checks carried out, besides the operating regularity, the adequacy and efficacy of the line and procedure controls were ascertained, which are the typical first level controls, in addition to the second level ones, entrusted to other control departments, in other words Compliance, Risk Management and Anti-money Laundering.

The controls *in situ* on the distribution network carried out during the year concerned 25 branches. On the basis of the results of the checks carried out, the Internal Audit Service as and when drew up proposals and recommendations aimed at overcoming the shortfalls noted, with a view to strengthening the safeguards in the various operating sectors.

For the whole of 2013, remote controls continued, appropriately structured to identify and look in-depth at the operations of specific management spheres exposed to elevated risk profiles, both effective and potential. The related activities availed themselves of the help of a specific IT application supplied by Cedacri which guarantees high flexibility in the performance of certain controls and makes it possible to obtain prompt reports on the operations carried out which exceed the pre-established attention thresholds; the versatility of the instrument in conclusion facilitates the identification of the necessary corrective measures and the prompt adoption of the appropriate measures.

The results of the checks carried out by the control units - which directly report to the corporate bodies - have been analysed in-depth using the internal apparatus concerned and subsequently submitted to General Management and the Board of Statutory Auditors and formed the subject matter of systematic reporting to the Board of Directors within the sphere of the information flows, as envisaged by current legislation.

In conclusion, it should be pointed out that the internal control units actively took part in the work group set up specifically for carrying out the self-assessment process regarding the adequacy of the company situation with respect to the provisions introduced by the Bank of Italy with the 15th up-date of Circular 263/06 concerning the “New prudent supervisory instructions for banks” relating to internal control systems, information systems and operational continuity.

The outcome of the complex preparatory and cognitive activities was presented in an extensive and systematic report, submitted for the examination of the corporate bodies, and sent to the Bank of Italy.

## **14 THE RISK MANAGEMENT SYSTEM**

The risk management system adopted by the Bank reflects the structure required by the prudent supervisory instructions for banks as per the Bank of Italy Circular No. 263 dated 27 December 2006.

The adequacy of the risk management process has been subject during the year to in-depth internal analysis, during the self-assessment process carried out by the Bank with regard to the compliance of its corporate situation, with respect to the provisions introduced by the 15th up-date of Circular No. 263/06.

The instructions contained in the afore-mentioned provision require the adoption of specific risk monitoring and control methods and the development of instruments and processes for the detection and assessment of the current and forecast exposure to the various types of risk, effective and potential, which the Bank is exposed to when carrying out its activities.

The 15th up-date issued in July 2013 systematically reviewed the legislative framework relating to the system of controls, internalising and furthering best practices, with the aim of getting the banks to further strengthen their business risk management abilities; and confirmed how the system of internal controls must check the implementation of the corporate strategies and policies, ensuring the containment of the risk within the limits indicated in the reference framework for the determination of the Bank’s propensity to risk (Risk Appetite Framework, abbreviated to RAF).

The Document which describes the internal Risk Appetite Framework is currently being drawn up by the Risk Management, Planning and Control Service, with the aid of a specific work group and the technical committees established within the Bank (Finance Committee, Risks Committee, Steering Committee), and will shortly be submitted for the examination of the Board of Directors for approval.

The regulations are based on three Pillars. The first envisages specific capital requirements for dealing with the risks typical to banking and financial activities (credit, counterpart, market and operational); in order to quantify these risks, alternative calculation methods were requested, characterised by different levels of gauging and control complexity, to be adopted by the banks according to the principle of proportionality in relation to the company dimensions.

Within the sphere of the operational risk, the recent legislative up-date placed particular emphasis on the IT risk, assigning the internal controls system the task of assessing the reliability and security of the company information and the IT procedures.

The second pillar requires the banks to endow themselves with suitable strategies and an intricate self-assessment process for the capital adequacy, current and forecast (ICAAP - Internal Capital Adequacy Assessment Process), to be formalised in the “ICAAP Report” to be sent periodically

to the Bank of Italy. In this sphere, an accurate identification must be carried out of the risks which the Bank is exposed to in relation to its operations and the reference markets, considering - in addition to the first pillar risks - also other types of risk of growing importance in the current market context. Amongst these, the “New Prudent Supervisory Instructions” include the rate, concentration, liquidity, excessive financial leverage, residual, strategic and reputational risks. The identification of all the risks undertaken or which can be undertaken also requires the valuation of the Bank’s positioning with respect also to other types of risk which are not subject to specific gaugings such as for example country risk, transfer risk, model risk and macroeconomic risk. In conclusion, the third pillar introduced public disclosure obligations on the capital adequacy, on the exposure to the risks and on the organisational methods for the identification, monitoring and gauging of the same.

Over the years the Bank had adopted and developed a series of organisational structures, processes and detection, monitoring and handling policies for the exposure to the various types of risk, established in the respective general guidelines by the Board of Directors. The performance of the second level controls regarding the implementation of the governance of the risks is entrusted to the Risk Management, Planning and Control Service, while the Compliance Service is tasked with ensuring the compliance of the business operations with the regulations.

The gauging, handling and mitigation methods for the Bank’s exposure to the various types of risk are illustrated below, risks which, on the basis of the internal self-assessment process, have been identified as significant in light of the operations and the contained degree of complexity of the Bank. Section E of the Explanatory Notes “Information on the risks and the related hedging policies” provides additional information of a qualitative and quantitative nature on the risks, while section F “Information on the capital” includes information relating to the Regulatory capital.

### **Credit risk**

The analysis of the risk associated with the disbursement of credit - which represents the main activity carried out - undertakes particular importance and is aimed at assessing the ability of the Bank to suitably select its customers and the economic initiatives which are credit worthy, as well as the efficacy of the disbursement, handling, monitoring and trend control process for the loans disbursed. In quantitative terms, the credit risk represents the most significant risk, in light of the elevated incidence of loans to customers with respect to total balance sheet assets.

The Bank gauges the capital requirement relating to the credit risk using the standardised method, which envisages the application of different weighting ratios for the portfolio loans according to the segment the counterparty granted credit belongs, the credit worthiness and the type of guarantees possibly acquired. For the analysis and accurate and constant monitoring of the credit risk, the Bank avails itself of a management system, known as “Credit Rating System - CRS”, which classifies the customers on the basis of credit worthiness, via an internal scoring system. The system comprises a statistical-type insolvency risk gauging model which, by means of fundamental and trend analysis of the main economic - financial indicators of the counterparty, makes it possible to assess the main relationship data. The Credit Rating System also represents the reference basis for the calculation of the estimated loss used for the quantification of the adjustments (forfeit write-down) of performing loans, together with the estimates of probability of default (PD - Probability of Default) and loss in the event of default (LGD -Loss Given Default).

During 2013, the Bank launched the process for the adoption of the second generation rating models developed by the outsourcer Cedacri. The backtesting analysis carried out with regard to the probability of default assigned by the new model to the loan exposures has revealed how the latter perform better, with respect to the previous ones, with regard to the identification of signs of deterioration in the loan quality.

The Bank also uses the “Collateral” procedure provided by the outsourcer Cedacri for the purpose of checking all the conditions of general and specific admissibility of the mortgage guarantees, as defined by prudent supervisory legislation, so as to benefit from a minor capital absorption in the presence of credit risk and avail of an efficient system for managing the mortgage guarantees. This procedure represents a valid safeguard to the residual risk, or the risk that a minor amount than that envisaged is obtained from the enforcement of a guarantee.

The Bank launched the process relating to the monitoring of problem loans during the year, whose activities are currently entrusted to the “Trend Monitoring” Service, set up and regulated specifically during the year. In detail, this Service, besides seeing to the trend-related monitoring of the relationships, handles the performing positions and the positions persistently non-performing (past due), while the watchlist positions, including objective watchlist) and restructured positions are handled by the Pre-dispute Service.

Within the sphere of the loan monitoring activities, the Bank adopted, during the year, a new application provided by Cedacri: “Quality Credit Management”, replacing the previous instruments ICC (Credit Control Process) and Watchlist Management. The new procedure has the aim of identifying the counterparts to be subjected to monitoring and of handling the positions in which anomalies have already manifested, with the end purpose of containing the credit risk.

The new IT platform makes it possible to divide the customers up into monitoring sub-portfolios according to the Bank’s strategic guidelines; for each customer “cluster” identified, it is possible to associate different lending strategies, with a customisation of the process chosen in terms of players involved and actions to be undertaken.

The concentration risk per individual borrower and the concentration risk vis-à-vis counterparts belonging to the same business sector or the same geographic area (geo-sectoral concentration) represent specific interpretations of the credit risk.

The concentration risk per individual borrower is monitored examining - with specific methods - the exposures involving a significant amount vis-à-vis individual counterparts and between those associated legally and/or economically, while the gauging of the risk takes place using a model on the entire loan portfolio based on the Herfindahl index, in line with the matters envisaged by the supervisory instructions. The checks are carried out promptly, for the purpose of maintaining the degree of concentration within thresholds consistent with the diversified allocation policy of the loan portfolio established by the Board of Directors. With regard to the gauging of the geo-sectoral concentration risk, within the ICAAP process the Bank uses the valuation model proposed by the work group specifically set up within ABI (Italian Banking Association).

The Bank also avails itself of the procedure entitled C.C.M. (Credit Capital Management), made available by the outsourcer Cedacri, with the aim of providing support for the calculation of the prudent requirements (First Pillar), the prudent control process (Second Pillar) and the drafting of reports for public disclosure (Third Pillar).

Each year, the Board of Directors defines the lending policies overseeing the quality of the loans both at the time for initial resolution and in the subsequent management of the relationship, taking into due consideration the Bank’s economic/equity situation and the related economic context. The policies in the last few years have seen the splitting of the credit risk as the prevailing strategic approach.

### **Market risk**

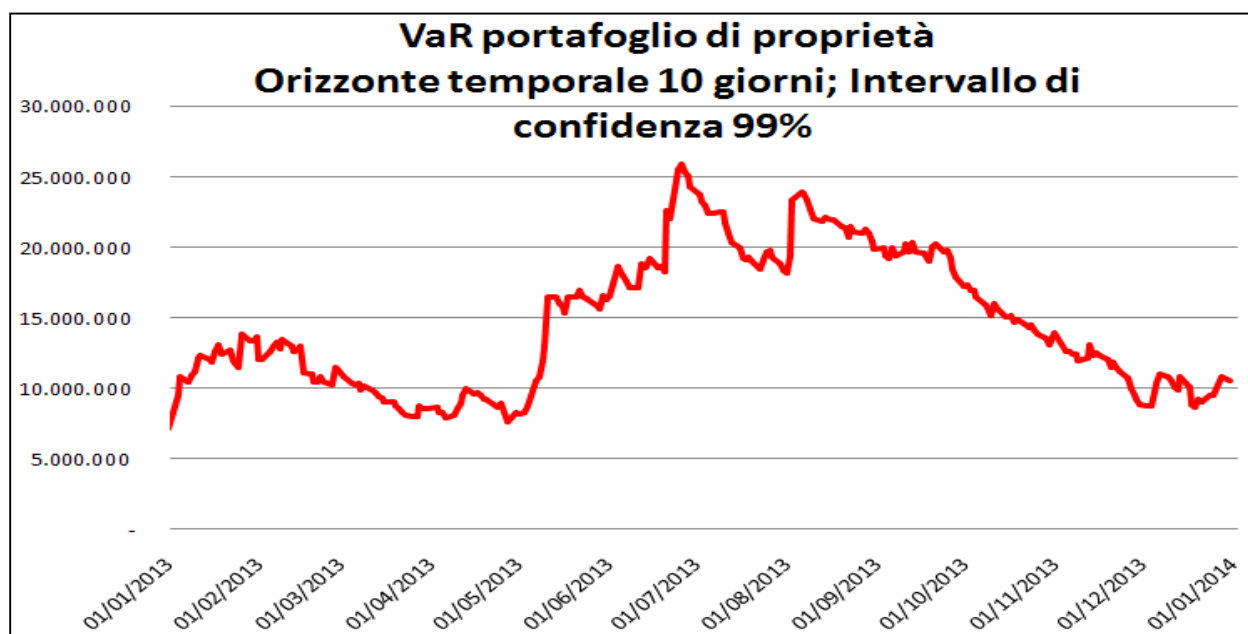
The Bank has developed methods for the detection of market risks which include price, interest and exchange risk on a consistent basis with the strategies adopted and with the features of the financial assets held.

The pre-existing strategies of prudent management of the financial portfolio were confirmed in 2013, mainly addressing the government security bond market and, only marginally, the share market; steps were also taken to constantly balance the positions in foreign currency.

With regard to the gauging of the price risk on the securities portfolio, a management model is used based in the Value at Risk (VaR), capable of summarily expressing the maximum possible loss of a static portfolio also in monetary terms, in relation to a timescale and a confidence level chosen prudently.

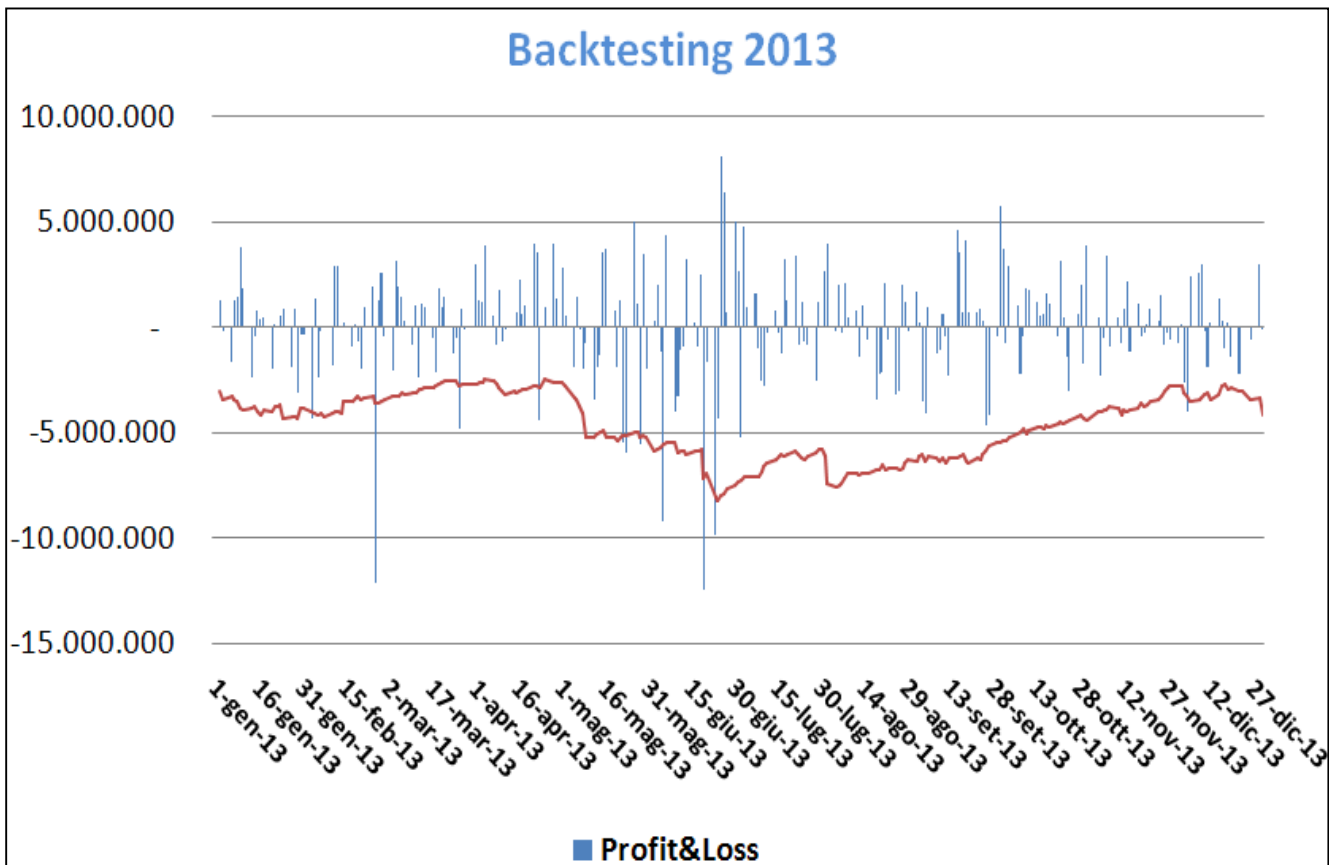
For the calculation of the VaR, the Risk Management, Planning and Control Service used both the ALMpro application and the ERMAS application, both provided by Prometeia, on a parallel. The financial information necessary for the determination of the VaR (volatility, correlations, forward structure of the interest rates, exchange rates, shares indexes and benchmark indices) are provided to both applications by the Risk Size product. The VaR model adopted is parametric in type and a confidence interval of 99% and a timescale of 10 days are prudently used.

The trend in the bank's exposure to the market risk during the year, relating to its securities portfolio, gauged according to the VaR method described above, presents itself as follows:



The VaR trend, from the moment that the securities portfolio is almost entirely made up of Italian government securities, has aligned itself with the fluctuations registered on the related markets. In detail, it disclosed the maximum value at the end of June when, further to the communications of the Federal Reserve (FED) with regard to the possible progressive reduction of the measures supporting the American Treasuries, the market revealed a generalised reduction in the prices of bonds. The subsequent stabilisation of the markets and the maintenance of an expansive policy by all the Central Banks permitted a progressive reduction of the spread of government securities, leading to the reduction of the VaR of the Bank's securities portfolio. The overall VaR in absolute value has aligned with the values at the start of the year, in the presence of a securities portfolio which by contrast has increased by around Euro 140 million, also further to the optimum liquidity situation reported by the Bank. The average duration of the bonds has always remained under the maximum limits established by the Board of Directors (5 years). The backtesting analysis carried out in 2013 revealed 11 cases of exceeding of the calculated VaR, 10 of which concentrated in the first half of the year, further demonstrating the progressive return to normal of the financial markets.





### Operational risk

Operational risk is represented by the possibility of suffering losses due to inadequacy or failures of procedures, human resources and internal systems, or as a result of external events.

The Bank sees to the determination of the capital requirement in the presence of operational risk, using the B.I.A. method (Basic Indicator Approach), according to which the capital covering this type of risk equates to 15% of the average of the net interest and other banking income generated in the last three years.

The supervision of the operational risk, in any event, is subject to constant attention both in the various phases of the operational processes and procedures and within the sphere of the periodic adequacy checks on the system adopted, carried out with the contribution of the various company departments involved in the processes.

The Bank has defined a series of organisational processes for the supervision and handling of the types of operational risk, within the sphere of which it avails itself - together with the competent Risk Management unit - of the Internal Audit and Compliance Services and the Supervisory Body established in accordance with Italian Leg. Decree No. 231/2001. In order to contain the negative consequences, in economic and reputational terms, deriving from the occurrence of types of operational risk, the Bank has also adopted the Operational Continuity Plan, aimed at safeguarding the Bank in the presence of critical events which may invalidate full operations and has also carried out the mapping of the main operating processes. The implementation of the new branch procedure, in conclusion, has permitted a more efficient automation of the anti-money laundering surveys, thereby guaranteeing improved supervision in the prevention and fighting of money-laundering and terrorism funding.

For the purpose of improving the operational risk management process, the Bank has adopted an integrated detection, assessment, monitoring, mitigation and control system for this risk. In this connection, a system has been created for the collation and conservation of the data relating to operational events and losses, which permits the creation of a database for the detection of the operational losses care of each central and network organisational unit. Cedacri's LDC (Loss Data Collection) procedure has been adopted to support this system, making it possible to gather together the data relating to the operational losses and classify the same according the Basel 2 logics.

The collation of the events which have led to operational losses permits the Bank to promptly identify the reiteration of negative events or conduct, thus encouraging appropriate corrective measures.

### **Interest rate risk**

The interest rate risk is generated by the imbalance between the maturities (repricing) and the asset and liability items belonging to the bank book, which is made up of all the financial assets and liabilities not included in the trading portfolio as per supervisory legislation.

The mitigation of the interest rate risk takes place by means of the integrated handling of the bank assets and liabilities, aimed at stabilisation of the interest margin and the safeguarding of the economic value of the bank book.

The gauging of the interest rate risk is carried out by the Risk Management, Planning and Control Service. The assessment takes place monthly according to a dynamic approach; therefore, for each sensitive item identified in the time period chosen for the analysis, account is taken of the specific repricing methods.

The ERMAS procedure makes it possible to monitor all the Bank's activities associated with the transformation of the maturities of the assets and liabilities and to quantify the effects, balance sheet and income statement in type, induced by hypothetic shocks of the market rates. Said shocks are processed within the sphere of macro-economic scenarios, or rather theoretic shifts of the market rate curves.

For the purpose of gauging the variability of the interest margin, determined by positive and negative changes in the rates over a time period of 365 days, monitoring of the differences between asset and liability items of the financial statements is carried out, grouped according to the maturity or rate redefinition date; the method used is "gap analysis", via several approaches which make it possible to achieve increasingly accurate estimates. The rate risk gauging techniques were implemented during the year, also including the estimate of the effect linked to the core component of the "on demand" items in the registrations.

The gauging of the variability of the economic value of the Bank's assets and liabilities to monitor the current value of the equity is carried out via Duration Gap analysis and Sensitivity Analysis, which make it possible to check the sensitivity of the Bank's economic value with regard to the change in the interest rates.

The calculation of the exposure to the rate risk is also carried out on the basis of the standard algorithm envisaged by the afore-mentioned Circular No. 263/2006, by means of the creation of a summary index which expresses the ratio between the change in the economic value of the bank book in the presence of a rate shock (+/- 200 base points) and the regulatory capital. The Bank has always maintained the risk index under the maximum threshold established by legislation (20%). The change in the economic value of the bank book is also calculated in the presence of a rate shock which represents the 1st percentile (downward) and the 99th percentile (upward) of the changes in the market rates in the last 6 years.

### **Liquidity risk**

The liquidity risk is represented by the risk that the bank is unable to efficiently cover the expected and unexpected cash outflows without risking its ordinary operations and its financial equilibrium.

The overall model adopted by the bank for the handling and monitoring of the liquidity risk is divided up into three distinct spheres according to the reference scope, the timescale and the analysis frequency:

- the management of the intraday liquidity, or rather the management of the daily settlements of the debit and credit positions in the various settlement, payment and clearing systems which the Bank takes part in;
- the management of the operating liquidity, or rather the management of the most volatile events which impact the Bank's liquidity position over a period between 1 day and up to 6 months, with the primary objective of maintaining the Bank's ability to meet its ordinary and extraordinary payment commitments, minimising the related costs. Within this sphere, the registrations of the imbalances between incoming and outgoing sources and the related system of supervisory limits and thresholds, focus in particular on the maturities up to six months;
- the management of the structural liquidity, or rather the management of all the events of the bank book which impact the Bank's overall liquidity position in the period beyond 6 months, with the primary objective of maintaining a balanced dynamic ratio between medium/long-term assets and liabilities.

The model adopted by the Bank for the management and monitoring of the liquidity risk is based on the construction of the maturity ladder and on the allocation of the certain and estimated flows to the various time brackets of the same, for the purpose of proceeding with the calculation of the cumulative gap for each maturity bracket.

The Bank has established a number of operating limits for the management of the liquidity in both spheres: operational and structural. In particular, with regard to the management of the operational liquidity the limits are defined in terms of absolute value of the cumulative GAPS, on the various maturities, while with regard to the management of the structural liquidity the limit adopted is defined in terms of ratio between the assets and liabilities with a maturity of more than one year.

Safeguarding the liquidity risk, the Bank continually monitors the value of the Counterbalancing capacities (CBC), understood as the availability of assets which can be promptly reimbursed, sold or used in refinancing transactions with the interbank system and which therefore make it possible to generate liquidity rapidly and efficiently.

The bank has also drawn up a "Contingency Funding Plan", as an instrument for mitigating the liquidity risk which indicates, in detail, the individuals and the units responsible for the implementation of the extraordinary funding policies in the event of need, as well as the action to be adopted to remedy the same, in accordance with the legislative requirements envisaged by the new regulations on the subject.

During 2013, the Bank launched the gauging, using the Jcompass application issued by the outsourcer Cedacri, of the "Liquidity Coverage Ratio" (in short LCR) and "Net Stable Funding Ratio" (NSFR) indicators envisaged by the Basel III Framework. The calculation of the indicators will be further implemented on the basis of the matters envisaged by the specific legislation contained in the EU Regulation No. 575 dated 26 June 2013 of the European Parliament (CRR Legislation).

### **Risk of excessive financial leverage**

The bank pursues sustainable growth policies containing recourse to financial leverage.

The duties and the responsibilities of the Risk Management, Planning and Control Service include the quarterly monitoring of the risk of excessive financial leverage by means of the

calculation of the financial leverage indicators estimated on the basis of the indications of the Basel III Framework.

This gauging aims to capture the risk aspects which are not included in the gauging of the Supervisory ratios (Tier 1 and Tier Total).

### **Strategic risk**

The strategic risk is represented by the risk, both current and forecast, of coming across a drop in the profits or the capital of the Bank deriving from changes in the operating context or from erroneous business decisions, the unsuitable implementation of decisions, as well as the scant reactivity to change in the competitive context.

The Bank has adopted a mitigation policy for the strategic risk which is mainly based on the formalisation of an analytical, prudent and shared decision-making process, on the careful and constant observation of the reference market, on the gradual activation of new services and/or products, on a formalised operational and strategic planning process and on constant detection and monitoring activities for the company performance and the related differences with respect to the pre-established objectives.

### **Reputational risk**

The reputational risk is represented by the risk, current and forecast, of a drop in the profits or the capital deriving from a negative perception of the Bank's image by customers, counterparts, shareholders, investors or the Supervisory Authority. The reputational risk is triggered off by original factors attributable, mainly, to the operational risk; the losses associated with the reputational risk may be higher than those attributable to the original risk event.

By means of interviews with the heads of the units involved in the handling of the risks and the processes, the Bank carries out a self-diagnostic assessment of the forecast exposure to reputational risk, with the intention of monitoring the areas of operations most exposed to this risk and raising the awareness of the main players involved.

## **15 COMMERCIAL ACTIVITIES**

These are not superfluous: it is a necessary extension to repeat that the commercial activities are at the heart of banking activities; the core management takes place within this function, that of funding and lending, and also all the services area, which has expanded enormously further to the increasingly common practice of distributing third party products via its own network - among which insurance products and those linked to investment services undertake particular importance - and the development of the technology applied to the system of payments and to the speed and security of the transactions.

In the history of Valsabbina, the emphasis given to the development of the commercial activities is almost an automatic given of the specificity of the chosen area, characterised by the presence of a manufacturing sector which has created generations of entrepreneurs, vivacity of trade, enterprise in the development of research and innovation; and consequently economic culture, employment and wealth. In this favourable context, the Bank has itself been an enterprise of equal vivacity, exercised by a virtuous delivery which has produced a positive bank - customer relationship, almost exclusive, because it is favoured by the diffusion of its branches, the knowledge of the locations, the confidence in the projects and in the individuals which to a large extent are also the shareholders.

The responsibility of maintaining this commercial and entrepreneurial trait - which also has repercussions on the plan of the social relationships - has encouraged the Bank to up-date and

streamline its policies so as to be increasingly a genuine “Household Bank” amongst the many competitors.

As a sign of this awareness, among the rationalisation measures in the organisational set ups implemented in 2013, mention is made of the creation within the new Market Division of a specialist unit known as “strategic, marketing and product planning” aimed at co-ordinating in a systematic and unitary manner, the policies for the development of the balance sheet aggregates and the sale of the services by means of method-based, IT and training supports for the sales network.

At the same time, the structure of the Commercial Areas was reviewed, reducing their number from eight to six and the commercial co-ordination role of the Area Head was enhanced and qualified, which will be accompanied by an equipped operational team, supporting the activities and the administrative-type fulfilments, so as to permit a greater concentration on the singular production functions associated with the role.

Together with the redrafting of a new monitoring and reporting system, the afore-mentioned measures made the decision-making process more fluid and made it possible to more incisively oversee the performance-related profiles of the network activities, being able to intervene more effectively in the corrective action.

The product catalogue was thus implemented also during 2013, making competitive instruments available to the customer with regard to funding, loans and, undergoing constant growth, services - own and third party - with the aim of increasing the market shares, in particular in the areas of most recent acquisition, especially in the province of Verona, on the branches deriving from the purchase of the former Credito Veronese, Again in this new context, the business strategy has aimed to consolidate the institutional identity of industrial co-operative and peoples Bank and has focused on the completeness of the supply and the speed in responding to the needs of the customers.

With regard to the products, the “Shareholders & Customer Programme” continued briskly, via which our shareholders avail of particular advantageous contractual conditions.

The facilities reserved for the Shareholders in fact envisage not only an interesting return on current account deposits, but also a fixed monthly fee for the use of a series of services- international cash card, credit card, securities dossier, accident and injury insurance policies and internet banking - but also a facilitated regime for other loans and banking products, both traditional and innovative.

The consensus created around the initiative is confirmed by the extended array of those who use the “Socio & Cliente” package: more than 21,000 account holders, 30% of all our current account holders. Again in this case, the responsibility for keeping the contents of the proposal high and attractive has induced us to extend the scope of use by means of two new formulas “Socio & Cliente Plus” and “Socio Azienda” which will be launched in the first half of 2014.

With the support of targeted initiatives and advantageous conditions, the offer of current account deals continued which envisage the fruition of non-banking services, such as the Conto Rosa or the Conto Evergreen, rather than the traditional ones like Conto Light and Conto Nuovo.

The accurate planning phase of the new “Conto Giovani” also concluded, an account intended for the under 30s, which debuted at the beginning of 2014 among the new products of the list and which envisages, together with a prize competition reserved for all the new participants, benefits and discounts for those who become account holders.

With the chief purpose of furthering the acquisition of new customers, the Bank then organised a new initiative via the competition known as “Vieni, Vedi e Vinci”, with the collaboration of a specialised company. All the individuals who, in the duration of the same - from 16 December 2013 and 16 June 2014 - open one or more current accounts and all those who, already account holders, present the Bank with new customers, are admitted to the competition.

There are two possibilities of winning: the first, which is an “instant-type win”, makes it possible to compete for prizes directly in the branch via scratch and win cards. The second envisages the final extraction from among all the participants of 50 TOP Star prizes comprising useful and valuable objectives: ranging from cameras to LCD TVs. In order to be entitled to the TOP Star prizes, the winning Customer will have to be the holder of an active current account at the time of extraction.

By way of confirmation of the quality of the services offered and the promotional ventures which support the same, current accounts reported an increase of more than 2,000, rising from 66,456 to 68,483, with annual growth of 3%.

Despite a year which saw a drop in the overall volume of the loans due to the minor demand for credit by companies, the Bank’s vicinity to the area was not lacking, complying with the requests of the customers deserving support, albeit using selective criteria also with regard to the technical forms.

New medium-term disbursements at the end of 2013 amounted to around Euro 380 million, of which 80 concerned more than 600 loans to SMEs, 70% guaranteed by the guarantee fund of Mediocredito Centrale; the “micro businesses”, in other words the companies with sales revenues of up to Euro 2 million and with a number of employees no more than nine, where subject to particular attention as always.

Again in 2013, the Bank granted the possibility of suspending the payment of mortgage and unsecured loan instalments for businesses and households in temporary difficulty for a total of 400 positions and an equivalent value of Euro 100 million and also permitted the renegotiation of the conditions rather than the restructuring of the repayment plans. Within the sphere of medium/long-term loans, 365 new mortgage loans were granted to households for the purchase of their first home, for a total of Euro 51 million.

As is known, during 2013 new tax incentives were launched, confirmed by the stability law also for 2014, for building renovation and for energy saving measures. In order to permit households and businesses to access such incentives, the Bank created and offered its customers specific concessions via dedicated products, such as “Mutuo Incentivi Casa” and “Prestito Incentivi Casa”, which join the traditional range of mortgages and loans all of which featuring truly competitive conditions. More than 100 customers have already benefited from the new loans introduced into the Bank’s product range, for a total of around Euro 18 million.

With regard to the leasing sector, where the Bank’s operations involve the channelling of the transactions care of specialist financial brokers in this form of funding, during the year 134 contracts were finalised for an equivalent value of Euro 12 million.

Another chapter of significant interest for the development of the commercial policies was that of the financial products intended for savers. Bonds issued by the Bank merit indication amongst these products, representing a traditional and stable source of direct funding largely appreciated by customers due to the simplicity and linear nature of their technical and trading structure; by way of confirmation of the appreciation and, at the same time, confidence granted to the Bank, in December 2013 and January 2014 new subordinated bonds were subscribed by customers, in just a few days, for Euro 60 million, issued within the sphere of the annual programme which envisages the issue of a further Euro 90 million.

The overall stock of bonds exceeded Euro one billion and two hundred million, despite the important maturities during the year for around Euro 500 million, with new placements for around Euro 450 million, almost exclusively fixed rate and step up: an excellent result, considering the tensions on financial markets and the preference of the investors for liquidity.

Placement continued - so as to meet half way the desire of the investors to remain with shorter maturities than those of bonds - of time deposits, with a time restriction of up to 24 months. The stock at year end came to over Euro 360 million.

Within the sphere of asset management, collaboration was intensified with qualified brokers in the sector, aimed at further extending the range of products to offer to customers. The Bank has agreements with Arca sgr, Azimut sgr, Eurizon sgr, Templeton, Anima sgr, Aletti Gestielle, Amundi funds, Fortis&Parvest Sicav, Generali Sicav, Nordea funds, Raiffeisen funds, Pictet Sicav and DWS, which make it possible to offer the customers a wide choice among the numerous and diversified lines of mutual investment funds; the stock at the end of 2013 touched the Euro 170 million mark, disclosing growth in the segment of 20% with respect to the previous year.

With regard to “bankassurance” services, the positive trend in the sale of the life and non-life class policies continued throughout the year, with the by now long-term partnership with the Zurich Italia Group.

The collaboration relationship, tried and test over years of operational agreement, envisaged the distribution of standardised policies and otherwise, as well as exclusive coverage - collective policies - which ensure the customers the maximum insurance protection while reducing the costs to a minimum.

At year end, the stock of Zurich products for savings purposes placed care of our customers amounted to Euro 168 million, with growth of 32.4% compared with last year. Besides the placement of traditional separate products (Zil Performance, Zil Flash, Zil Coupon Plus, ZilInvest, Somilia and Zil Capital - which due to legal obligations are at least 80% invested in government securities), the Z-Platform product was particularly successful: a full life unit-linked type product which permits the customer to choose from among the 60 best mutual investment funds (UCITs), selected by the insurance company and issued by leading market players. The contract is based on two fundamental services; one insurance-related, in the event of demise of the insured party, and one financial, linked to the performance of the mutual funds chosen in the validity period of the policy.

During the year, the range of products distributed was once again enhanced by the offer of Accident and injury policies for Accumulation Plans, subscribed in just December by more than 300 counterparts.

Alongside the already well-known insurance formulas regarding life and non-life pure risks - such as TCM (temp in event of demise), fire, legal protection, accident, injury and health - the D&O revealed itself to be effective and innovative.

But the wide panorama of insurance products offered by the Bank does not end there. In 2013, 1,200 “Credit Life” policies, 360 “TCM “ (Temporary in the Event of Demise - known as Taboo)” policies and 590 fire and explosion (For Family or Metro x Metro) policies were placed. The placement of 1,250 contracts of the policy known as “Protection-Fidi” was also positive, linked to current account credit facilities, alongside the policy “Vita Privata” (civil liability and legal protection): the related new contracts were 815. Very important, also due to the rising sensitivity and culture of the topic, was the placement of the pension product “Vipensiono” with 280 new subscriptions for an overall stock of Euro 4 million.

With regard to the sphere of the non-life products offered to businesses who are our customers, mention should be made of the growth in commission of the Bank for the sale of Business Protection policies, 270 new contracts, and 70 D&O contracts. Thanks to Zurich’s recognised experience in the area of insurance products, the later are among the best products existing on the market with regard to the quality of the coverage provided.

The positive results achieved in the last few years in the product partnerships - within the insurance sphere, in that of pensions, but also in that of services for the individual and leisure time - have encouraged us to intensify the internal marketing activities so as to up-date and extend the range of products which may usefully accompany our customers in the recurrent and new needs of their working, profession and family lives. Further developments in the profiles of

the range are in fact envisaged also during 2014, in the awareness that, as in any business segment, also the banking industry is the market which selects the best.

Completing the report on the commercial ventures aimed at enhancing the range and encouraging the inclusion in the shareholding structure of new shareholders and new customers, the important and highly topical section of virtual bank services remains.

It is entirely normal - we wrote last year - that the policies for the diffusion of banking services on the web occupy a significant space among the business strategies, from the standpoint of the organisational commitment required, from that for the possible containment of the production costs and from that of the returns in terms of quality of the service provided. Judging by the growth in the number of customers, private individuals and businesses, enabled to use the services of the “Virtual Bank” and by the volumes of the instructions imparted, the internet channel accompanies the traditional contact methods of the Bank as a powerful communication and operative linking instrument.

At the end of 2013, users of the “Banca Virtuale” -“Valsabbina on-line” and “Valsabbina corporate” services, numbered in total around 24,000, compared with 23,122 at the end of 2012, involving an increase of 3.6% per annum thanks in part to the boost which the Bank wished to give in terms of divulgation and promotion.

During 2013, more than 20,000 private users of the Valsabbina Home Banking service had the possibility of migrating to a new platform featuring higher quality and security standards.

Given the by now universal spread of smartphones and tablets, during 2013 an app was developed which makes it possible to use the home banking services also via said instruments.

The launch is envisaged during the first few months of 2014.

A mention, at the end of our review, is also due to the somewhat fast growth in payment instruments represented by credit and debit cards. The following table provides an account of the trend in POS and automatic teller machine points, the number of transactions and the balances involved:

	2009	2010	2011	2012	2013
<b>ATM points</b>	<b>60</b>	<b>60</b>	<b>60</b>	<b>68</b>	<b>66</b>
Number of transactions carried out	759,948	786,021	807,558	862,254	875,207
Amounts transacted (in millions of Euro)	116	125	133	148	153
<b>POS</b>	<b>1,187</b>	<b>1,343</b>	<b>1,484</b>	<b>1,937</b>	<b>1,799</b>
Number of transactions carried out	898,231	1,133,437	1,321,361	1,645,407	1,867,782
Amounts transacted (in millions of Euro)	74	89	108	133	140

With regard to the POS, in 2013 a stock of 1,799 was achieved. The reduction in the stock is attributable to the re-contractualisation of the service, which led to the cancellation of more than 300 connections inactive for some time. A new boost to the segment is expected further to the initiative linked to the sale of the new Mobile POS service, which will be distributed in 2014 in collaboration with Cartasì.

Supplementing the numbers in the table, we can state that the stock of debit, credit and prepaid cards in circulation at year end came to 70 thousand, with an increase of 2%, while transactions carried out touched the Euro 68 million mark in total.

Together with “Carta Libera”, the international cash withdrawal/POS card used by around 40 thousand current account holders, Valsabbina also distributes CartaSì credit cards, issued by Istituto Centrale delle Banche Popolari Italiane, as well as the American Express card.



With regard to the “prepaid cards” segment - a recent service but evolving rapidly due to its practical and reliable features - the Bank has placed around 700 of the “Carta Chiara”, endowed with high quality and security standards.

During the second half of 2013, a new product was developed known as Ci-Conto which makes it possible to unite the benefits - also real from the point of view of the moderation of the conditions - of the target of youngsters.

With regard to car-owning customers, in conclusion, an agreement was recently signed for the direct distribution of the Telepass family product for the payment of tolls at the motorway booths and a series of services of sure utility including roadside assistance.

These last few pages have related how the boost given to commercial activities, on a consistent basis with the programmatic policies defined for 2013, have produced important results with regard to volumes, contributions of commission and the market shares held by the company; the importance is judged, first of all, by means of quantitative type gaugings, but another assessment is by no means extraneous, that of the ability of the entire structure to provide itself with goals, as a rule ambitious, and achieve them. This ability is an component of extraordinary value, because it transmits assurance and awareness in outlining the scenarios and in getting them to exist effectively in the discipline of the daily commitment. If it is true that the future has an ancient heart, the hypotheses of development which support the structure of layout of the three-year strategic Plan which we have dealt with extensively, thus appear without doubt plausible and realistic. If that which we have spoken of comes about - and this is valid as an auspice - Banca Valsabbina will have turned very significant pages in its age-long history as “Household Bank

## **16 HUMAN RESOURCES**

Graph showing trend in employee numbers

As we have already indicated also on previous occasions, the Staff represent the most important resource on which the Bank can count: in fact, they play a fundamental role in looking after daily relations with the customers and the shareholders, in securely handling the operational complexities, in translating the logics of the commercial policy in observance of the rules of transparency and correctness, in creating confidence around the business. The commitment of our workers gives rise to the business results and their singular abilities and expertise originates the effective expression of the values which enhance the reputational profile of the Bank.

Individuals well-integrated in the area in which they operate lead to the best expression of those principles of industriousness and positivity which identify them and contribute in a substantial manner to the maintenance of its identity and progressive development of its economy.

The graph shown above confirms the gradual consolidation of the human resources employed in the business; as 31 December 2013 the staff increased by 10 with respect to the previous year, due to 19 new recruits and 9 leavers. This increase should be placed in relation with the development of the volumes of activities on the network, characterised by an increasing technical and operational complexity, and above all else the measures for the re-organisation and enhancement of the central structures which concerned, as already mentioned, the control units and the commercial, loans, planning and marketing sectors: these being spheres of strategic importance, especially in periods of lasting economic crisis.

The constant and disciplined development of the activities of the Bank is confirmed by the satisfactory positions reached in the classifications of the productivity and efficiency published in sector studies and is without doubt attributable to the contribution offered by the staff for

achieving the planned growth objectives, each within the sphere of the respective roles and responsibilities.

In this connection, it is worth remembering that among the priority action to be implemented in the next three years to achieve the profitability, liquidity and capitalisation objectives envisaged by the Strategic Plan, the Bank identifies - among other aspects - the geographic development by internal lines and the growth of the funding and lending balance sheet aggregates.

The objectives are ambitious and certainly have repercussions and fallouts in the Staff management policies with regard to organisation of the work, production processes and, naturally, also costs. But we know that we have capable, responsible and highly motivated individuals with us, endowed with professional skills and a style which fully complies with the features of the area: and for such reasons, we feel equipped to deal with the exacting work programmes, also facilitated by an appropriate configuration of the hierarchical and functional profiles of the structure.

The table relating to the distribution of the staff by grade is presented below.

<b>Distribution of the staff by grade</b>						
	<b>2013</b>	<b>%</b>	<b>2012</b>	<b>%</b>	<b>2011</b>	<b>%</b>
<b>Executives</b>	<b>9</b>	1.9%	<b>9</b>	2.0%	<b>9</b>	2.2
<b>3rd and 4th level middle management</b>	<b>100</b>	21.1%	<b>96</b>	20.7%	<b>82</b>	<b>19.8</b>
<b>1st and 2nd level middle management</b>	<b>69</b>	14.6%	<b>63</b>	13.6%	<b>52</b>	<b>12.5</b>
<b>Remaining staff:</b>	<b>295</b>	62.4%	<b>295</b>	63.7%	<b>272</b>	65.5
<b>of which: professional training</b>	<b>1</b>	0.0%	<b>1</b>	0.2%	<b>8</b>	1.9
<b>under staff leasing</b>	<b>5</b>	1.1%	<b>4</b>	0.9%	<b>3</b>	0.7
<b>TOTAL</b>	<b>473</b>	100.0	<b>463</b>	100.0	<b>415</b>	100.0

Of the 473 staff in the workforce at year end, 145 carry out their activities at the head offices and 328 operate in the sales network, made up of 61 branches distributed throughout the provinces of Brescia, Trento, Verona and Mantua. The staff who operate on the market come to around 70% of the entire workforce.

The remuneration policies, characterised from time immemorial by simplicity and equilibrium starting from the emolument reserved for senior figures, has formed the subject matter of constant and responsible attention with the aim of containing the costs, but safeguarding the correct recognition, in terms of promotions, gifts or similar, of the responsibility and the commitment provided by the staff.

The average cost per employee came to Euro 69 thousand, while the corresponding system figure has pushed forward to the level of Euro 75 thousand.

Proceeding with an examination of the qualitative-quantitative profiles, it should be observed that the female component continues to represent almost a third of the entire workforce, being made up of 151 workers, also involved in roles of responsibility both in the network and the central units: the female component includes all 12 figures who work part-time.

With regard to the registry aspects, at the end of 2013 the overall average age was 40 (37.8 for just the female component) and the length of service was 11.2 years (for both components), figures which characterise an on-average young "team" therefore capable of providing fresh energy in the daily work activities.

<b>Distribution of the staff by age, length of service and gender</b>					
	<b>2013</b>	<b>2012</b>	<b>2011</b>	<b>2010</b>	<b>2009</b>
average age	40	39.1	38.3	37.7	37.2
length of service	11.2	10.8	10.8	10.25	9.8

males	322	313	283	282	276
females	151	150	132	131	123
total	473	463	415	413	399

The level of education within Banca Valsabbina is very high: the employees in possession of a degree in fact come to 44.4%, while the average system figure stops at 35.9%, and those with a high school leaving diploma come to 53.7%. The female component in turn discloses a level of education comparatively high, with a portion of graduates equal to 49% while those with a high school leaving diploma come to 50.3%. (Staff education level table)

But the achievement of a high quality level of the staff presupposes, together with the presence of solid human and cultural bases, also the adoption of effective management processes capable of ensuring constant evolution with regard to learning. A genuine internal school which transmits ability, openness to change, willingness to discuss and which educates as per the spirit of service vis-à-vis the customers. And these values are usually transferred, also by means of example, by the mature and competent elements to the newly recruited resources, selected, according to a consolidated and precise business approach, from among youngsters who have brilliantly concluded their high school or university studies with a predominantly technical and economic bent.

In a context of change which what is more requires increasingly fewer bank tellers and increasingly more qualified professionals, once again in 2013 the Bank renewed a significant and agreed on commitment at all levels with regard to the training policies. A commitment also in economic terms, albeit moderated by the recourse to the funding granted, as in previous years, by Fondo Banche Assicurazioni further to the approval of the training projects presented.

The structure of the training plans thus involved a good 434 individuals, corresponding to more than 91% of the entire internal population, with the disbursement of 18,700 hours in total, corresponding to an average of more than 39 hours of training per head. In the previous year, the beneficiaries of at least one training course came to 84% of the total, while 37 average hours of training per head were provided.

In order to define the plan of the training measures to be implemented, once again in 2013 reference was made to the guidelines of the company strategy, aimed at turning to account the quality of the relationship with the customer as an instrument for achieving both the core business objectives and the development of the services and the products proposed to the market. The identification of the specific training and educational needs of the various internal figures took place by means of a constant and accurate process for the assessment of the skills and the individual potential, compared with the professional profiles requested.

And in the planning of the training measures, looked after by both the company specialists and qualified outside teaching staff, constant reference was made to the characteristics of our reference market and the needs and expectations - often undergoing rapid change, especially in the current critical market phase - of our customers.

The areas in which training action has developed in particular were - besides those relating to the obligatory topics - the specialist ones regarding the commercial division, the sales techniques, the credit management and control methods, as well as the characteristic skills of the most senior individuals in the network. In detail, "training labs" were set up in which the commercial staff were required to streamline their abilities to professionally handle the dealings with the customers, aware that the sales action must mainly be directed at satisfying the authentic needs of said customers.

Experimental action was launched during the year for the Bank - with truly positive results - aimed at increasing the managerial, organisational and commercial skills of the Branch Managers, by means of a training and “on the job” consulting process which met with the full appreciation of the individuals involved.

A great commitment was also dedicated to training in the lending area, addressing branch and head office figures with the aim of increasing the efficacy of the management and control of the risk, improving discussion between the various internal components involved in the lending process, as well as developing knowledge of the instruments for efficiently handling the dealings with customers in difficulty as well. Furthermore, the investee company Consulting planned and organised a Mini Masters course of particular training valence, destined to provide the Area Managers - also via dialogue and discussion with qualified professionals - with instruments and models for developing the characteristic managerial abilities of the role covered.

With regard to mandatory training, the new rules concerning anti-money laundering have been subject to targeted and extended in-depth analysis, in the conviction that the correct application of the fulfilments presupposes a deep business culture of prevention and aware that the IT procedures are only aids but cannot replace the human factor, specifically in this sphere.

Also remote training continued to be used within the sphere in which teaching activities can usefully be realised also by means of alternative methods to the typical classroom ones, as well as the so-called “relational training”, involving periodic operational meetings and encounters, work agendas dedicated to the branch and the area, convivial moments, such as company Conventions, during which information is transmitted, elements of reflection are gathered and those present educate themselves reciprocally by discussion.

It is no wonder, after all that has been said that the attention reserved for senior management and the development of the human resources has been perceived at all levels, including that of trade union relations, as a distinctive and systematic component of the business philosophy. The friendly closeness to each worker, the openness with regard to the individual needs and aspirations, the satisfaction - each time this is possible - of the requests motivated by personal or family reasons are principles applied by the company with absolute spontaneity: they form part of a historic culture, without doubt encouraged by the contained dimension of the structure of the workforces, which recognises the importance of a good internal climate as an irremissible factor for the individual motivations and for the affirmations of the entire group.

As satisfied worker who is listened to and valorised works better and with greater profit, for themselves, for the customer and for the company: this is a merely apparent obviousness, since it is not difficult to observe how, in large and more verticalised entities, management styles which are obliged to be less inclined to the individual may fail to provide that sense of identification and belonging which distinguishes the companies also according to emotive categories.

Outside of any rhetoric, we can conclude this section by maintaining with pride and a vivid sense of recognition that our Staff are truly very prepared and esteemed: the results tell us so, the warmth of the interpersonal relations tells us so, the customers tell us so and even our competitors tell us so - or rather they let us understand as so.

## **17 LEGISLATIVE AND REGULATORY INNOVATIONS**

During 2013, the Authorities, at both EU and Italian level, continued to issue significant measures for the up-dating and amendment of the legislative and regulatory framework regarding the banking and financial system, which for the Bank led to the development of

important internal reorganisation projects - whose performance will also extend to 2014 - and the adoption of intricate and complex structural and procedural adaptations.

During the year, in detail, the Bank of Italy adapted the supervisory legislative framework to the progressive evolution of the EU legal system regarding prudent supervision of banks introduced by means of EU Regulation No. 575/2013 and Directive 2013/36/EU, better known respectively as “CRR” and CRD IV”.

The new reference legislative framework of the European Union - whose enforcement is set for 1 January 2014 - renders the new rules defined by the Basel Committee for banking supervision in December 2010 and subsequent amendments and additions (“Basel 3”) operative, with the aim of furthering a more solid banking system resistant to financial shocks at EU level. The new rules will be the legislative setting in which the new single supervisory mechanism will have to operate, and which will represent a main element of the European banking union.

The supervisory instructions issued by the Bank of Italy in acknowledgement of the CRR and CRD IV introduced significant innovations with respect to the legislation previously in force regarding capital adequacy, the risk management system, leverage ratios, management of the liquidity risk and disclosure obligations for all the banks.

At the beginning of 2013, the consulting procedure on the new supervisory instructions regarding authorisation to carry out banking activities also concluded; the new final provisions, issued in April 2013, now take into account the evolution of the regulatory framework which took place recently (Basel 3, organisation and internal controls, administrative proceedings, compliance).

The most recent regulatory measures issued by the Bank of Italy also concerned, to a significant extent, the supervisory regulations relating to corporate governance and the system of internal controls. During the year, in particular, the new supervisory provisions relating to the system of internal controls, the disclosure system and the operating continuity of the banks and the banking groups were issued, with the aim of strengthening the ability of the banks to handle the business risks.

Within a systematic framework, the new provisions disciplined the general principles to which the system of internal controls must aspire and introduced a number of specific innovations on the subject, with particular reference to the obligation by the body with strategic supervision functions to define the overall risk level tolerated and the provision of the need for a more integrated approach to the management of business risks, envisaging the strengthening of the risk management structures, obliged to provide prior opinions on the coherence of the most significant transactions with the company risk management policy. Among the other innovations introduced by the new provisions, there is the extension of the sphere of compliance activities to compliance with tax provisions, the introduction of specific regulations regarding the outsourcing of the company functions and the enhancement of the regulations related to the functioning of the IT system and to operating continuity.

Also in relation to the remuneration and incentive practices - disciplined within the European sphere by the legislation issued by the EBA - the Bank of Italy, after having launched the first survey on pay at the end of 2012, confirmed in March 2013, with a new communication to the banking system, the indications regarding remuneration already formulated last year and drew attention to the need to adopt particularly prudent conduct.

Again with regard to governance, the Bank of Italy, recently, submitted a document for consultation in December 2013, inherent to the up-dating of the provisions regarding corporate governance; as of the date this report was drawn up, the consulting stage had not yet concluded.

Reviewing the other legislative measures of the Bank of Italy, it is emphasised that by means of measure dated 28 March 2013, the Supervisory Authority implemented EU directive No. 90 dated 14 November 2011, which amended the hypotheses for the calculation of the TAEG

(annual percentage rate) so as to take into account any problems emerging during initial application.

In March 2013, the formats for the reporting by banks and banking groups of activities at risk and conflicts of interests vis-à-vis associated parties were published; these models also incorporate a number of interpretative stances on the application of the new regulations.

In conclusion, on 1 January 2014 new instructions came into force with regard to suitable checking of the customers, which represent the last element of the secondary legislation regarding anti-money laundering, changing the operating methods inherent to the identification and verification of the data of the effective account holder, in other words the individual to whom the operations of the customers are attributable in the last instance.

The measures led to an exacting work programme for the various functions involved in the adaptation processes. In this context:

- the Anti-money Laundering Policy was approved which gathers together the guiding principles for the action of all the Bank staff involved in the prevention of the risk of involvement in laundering and international terrorism funding activities;
- steps were taken to supplement the internal regulations (Anti-money Laundering Manual) for the acknowledgment of the new supervisory provisions and the other operating instructions regarding the prevention of the laundering risk contained in the formats representative of anomalous conduct of the FIU;
- questionnaires were updated for the profiling of the money laundering risk of the customers, having taken into account the risk categories indicated in the Policy, and the periodic monitoring activities were consistently enhanced;
- the internal Regulation Manual of the Anti-money Laundering Service was adopted, containing responsibilities, duties, operating formalities, information flows and scheduling of the control activities.

The operating control activities carried out by the Audit service, in the year just ended, confirmed that the activities for the suitable checking of the new customers are carried out promptly, in compliance with the provisions of the law and internal regulations, and also that the recurrent reporting activities, or specific activities in relation to the anomalies detected, are carried out regularly, promptly and with increasing efficacy.

The care and exactitude by means of which the activities for the implementation of the legislation have been carried out derive from awareness that the action for preventing the risk of involvement in laundering activities is an on-going challenge. The risk prevention action therefore remains a high priority once again in 2014, in the conviction that the same represents and is consolidated by means of a constant operational practice, to be adopted efficiently according to an approach based on the risk.

Also with regard to tax-related aspects, a number of new regulations came into force during 2013, which introduced innovative elements with respect to the past:

- Italian Law No. 228/2012 (so-called 2013 stability law) introduced as from 2013 a tax on financial transactions (Tobin Tax) which concerns the purchase of shares issued by companies resident in Italy, the trading of derivative financial instruments referring to share-based or investment securities and the so-called “high frequency” trading of shares, investment instruments or derivatives which relate to share-based or investment securities. The tax is formulated to a proportional extent or by classes and is payable by the purchaser, by both the parties or by the financial broker depending on the subject matter of the transaction. A great many situations of exemption or exclusion from the tax are envisaged, what is more linked to the subject matter of the individual transaction. The applicability of the new tax, fixed for 1 March 2013, was deferred until 1 September 2013 for derivative products, with postponement

of the first payment until 16 October 2013. Only on 18 July 2013 was the last of the awaited implementing measures issued.

- as from 2013, the extent of the stamp duty on communications sent to customers relating to financial products was once again amended, the rate of which passing from 0.1% in 2012 to 0.15%, with a maximum extent of Euro 4,500 if the party is not an individual, and the maximum amount of Euro 1,200 fixed for 2012 with regard to just individuals was abolished.
- Italian Decree Law No. 133/2013 introduces for just the 2013 tax period an IRES (company earnings' tax) surtax of 8.5%; this essentially takes the IRES rate for 2013 to 36%. The portion of the write-downs and loan losses which exceeds the limit fixed by Article 106.3 of the ITCA is excluded from the surtax, the deduction of which has been deferred to the next four years.
- Italian Law dated 27 December 2013 (so-called "Stability Law for 2014") amended, as from the 2013 tax period, the deductibility regime for write-downs and losses on customer loans. Both for IRES and IRAP (regional business tax) purposes, they become deductible on a straight-line basis, over five years, as from the year when said liabilities are recorded and in the following four. The losses on the afore-said loans generated by means of factoring against payment are an exception to this rule which, for IRES purposes, become fully deductible in the year of registration on a par with what has already occurred for IRAP.

On the basis of the new provisions, the losses on customer loans are no longer subject to the disputed application of Article 101.5 of the ITCA if the deductibility is subordinate to the presence of certain and precise elements, bankruptcy proceedings, etc..

The regime in force of deduction over eighteen years for write-downs made up until 2012 remains in force.

These innovations permit a greater fiscal certainty on the operations of the banks and considerably reduce the financial recovery timescales for the associated prepaid taxes. The unjustifiable non-deductibility of these liabilities for IRAP purposes has also been removed.

On the same basis as the IRES, the transformability in tax credit of the prepaid IRAP (DTA) recorded in the financial statements with reference to (i) the write-downs/losses on customer loans not deducted in accordance with Article 106.3 of the ITCA and (ii) the realignment of the value of the goodwill and the other intangible assets, has been acknowledged.

The transformation of the DTA into a tax credit occurs if the annual financial statements disclose a statutory loss as well as if the IRAP tax declaration discloses a negative value of production. In this latter case, the IRAP DTA referable to the afore-mentioned components which have contributed towards the formation of the negative production result are transformed into tax credits. The provision has positive effects also for the purposes of the regulatory capital.

## **18 RELATED-PARTY TRANSACTION**

Related-party transactions are disciplined by specific internal regulations pursuant to Article 2391 *bis* of the Italian Civil Code, Consob Resolution No. 17221 dated 12 March 2010 and subsequent amendments and additions and Section V, Chapter 5 of the Bank of Italy Circular No. 263/2006.

The internal regulations, published on the Bank's website as required by legislation - discipline the identification, approval and execution of the transactions entered into by the Bank with related parties and parties associated with the same, -  
establish suitable rules for ensuring the transparency and essential and procedural correctness of the transactions,

- define the operating procedures regarding the monitoring and handling of the transactions with related parties and the discipline of the checks and the reports required by the new supervisory instructions.

It is hereby specified that all the transactions carried out by Banca Valsabbina and the group companies with related parties and parties associated with the same have been performed in observance of the criteria of essential and procedural correctness and under conditions identical to those applied for the transactions concluded with other parties; furthermore, no atypical and/or unusual transactions have been entered into, either with related parties or with the other parties, these being understood to be transactions which due to significance and/or importance, nature of the counterparts, subject matter of the transaction, method for determining the price and timescale may give rise to doubts in terms of the correctness and/or completeness of the financial statement disclosure, conflicts of interest, the safeguarding of the integrity of the company assets and the safeguarding of the shareholders.

In conclusion, during the year no transactions were carried out with related parties and/or parties associated with the same which significantly influenced the balance sheet or the Bank's results, nor have there been any changes to or developments of transactions with these parties which could have a significant effect in this sense.

With regard to the data and information relating to:

- remuneration paid to members of General Management and the Executives with strategic responsibilities;
  - dealings with Group companies;
  - parties associated with the related parties;
- please see Section H - Related-party transactions in the Explanatory Notes.

## **19 SUPERVISORY BODY**

The Supervisory Body, established in accordance with Article 6 of Italian Legislative Decree No. 231/2001 (hereinafter for the sake of brevity also the “231 Body”), was appointed by the Board of Directors on 24 March 2004. The Supervisory Body has the task of assessing the correct functioning of the organisational safeguards adopted by the Bank so as to avoid involvement in events which could be subject to sanction pursuant to and for the purposes of Italian Law No. 231 dated 2001. As established by the Organisational Model, it periodically reports to the Bank's Board of Directors.

During 2013, the composition of the Body was changed and it is now made up of an external member of proven experience who covers the role of Chairman, by the Chairman of the Board of Statutory Auditors, by the Head of the Internal Audit Service, by the Head of the Anti-money Laundering Service, by the Head of the Compliance Service, by the Head of the Risk Management, Planning and Control Service and by the Head of the Environmental Monitoring Service.

The changed composition provides even further assurance of the necessary link between the Body and the control units which the Bank has endowed itself with and more fully complies with the necessary exchange of information flows envisaged by Bank of Italy legislation contained in circular 263, as amended and supplemented in July 2013.

During 2013, the activities of the Supervisory Body focused on the one hand on the checking and up-dating of the Organisational Model which the Bank has endowed itself with in accordance with the afore-mentioned Law 231 in line with the most recent legislative innovations introduced and on the other hand on the verification of the existence of the necessary organisational and/or control safeguards.



During the four meetings held in the year, the Body was in a position to then stop and look at, with greater attention, the adoption by the Bank of the necessary organisational measures advised by the Bank of Italy and in particular those associated with the application of the legislation contrasting money laundering and the funding of international terrorism.

The Body also examined and discussed the annual reports of the various control units of the Bank, in particular evaluating any critical aspects emerging and the related measures adopted and/or planned by the Bank for the removal of the same.

Copies of the reports of the Body, which are recorded in the specific stamped and dated book, are sent to the Chairman of the Board of Directors and the Chairman of the Board of Statutory Auditors.

You are hereby reminded that the company website, corporate documents section, contains all the information regarding the Organisational Model adopted by the Bank as well as the composition of the Supervisory Body.

## 20 ECONOMIC PERFORMANCE

For the purpose of comprehending the dynamics which have characterised the 2013 income statement, the highlights are summarised below; a review of the same reveals that, with respect to last year - besides the staying power of the interest margin, net commission, net interest and other banking income and the careful control of the general expenses - the incidence of value adjustments has decreased. Therefore, the net profit rose from Euro 3 million to Euro 7.7 million.

<b>RECLASSIFIED INCOME STATEMENT</b> (amounts in Euro 000s)	<b>2013</b>	<b>2012</b>	<b>% change</b>
Interest margin	65,468	66,427	(1.44%)
Net commission	21,516	23,157	(7.09%)
Dividends and trading and other income	24,981	32,102	(22.18%)
Net interest and other banking income	111,965	121,686	(7.99%)
Net value adjustments on loans and held-for-sale financial assets and other	(50,075)	(60,551)	(17.30%)
<b>Net profit (loss) from financial operations</b>	<b>61,890</b>	<b>61,135</b>	<b>1.23%</b>
Payroll and related costs	(32,201)	(30,514)	5.53%
Other administrative expenses	(26,940)	(26,519)	1.59%
Net allocations to provisions for risks and charges	(284)	(651)	(56.37%)
Net value adjustments on tangible and intangible assets	(2,564)	(2,529)	1.38%
Other operating income/expense / gains or losses	11,410	6,022	89.47%
<b>Operating costs</b>	<b>(50,579)</b>	<b>(54,191)</b>	<b>(6.67%)</b>
Profit before tax from continuing operations	11,311	6,944	62.89%
Income tax for the year	(3,626)	(3,904)	(7.12%)
<b>Profit for the year</b>	<b>7,685</b>	<b>3,040</b>	<b>152.80%</b>

### The interest margin

The interest margin discloses a slight reduction of 1.4%, equal to Euro 959 thousand, due to the different composition of both the interest-bearing assets influenced by the reduction in the interest rates - with fractional drop in customer loans and an increase in the securities portfolio - and the deposits which disclosed a greater incidence of the interest expense for the restricted portion.

Interest income consequently fell from Euro 149.1 million to Euro 148.6 million, while interest expense rose from Euro 82.7 million to Euro 83.2 million. The comparison of the separated data

relating to the contribution provided to the interest margin of the various components with respect to 2012 bears witness to said trends:

<b>INTEREST MARGIN (amounts in Euro 000s)</b>	<b>2013</b>	<b>2012</b>	<b>% change</b>
<b>Interest income and similar revenues</b>	<b>148,660</b>	<b>149,137</b>	<b>(0.32%)</b>
- on financial assets	25,559	24,010	6.45%
- on amounts due from banks	1,130	1,345	(15.99%)
- on amounts due from customers	122,604	124,993	(1.91%)
-on FV adjustment of receivables of former Credito Veronese	(633)	(1,211)	(47.73%)
<b>Interest expense</b>	<b>(83,192)</b>	<b>(82,710)</b>	<b>0.58%</b>
- on amounts due to banks	(2,688)	(4,361)	(38.36%)
- on amounts due to customers	(35,496)	(36,052)	(1.54%)
- on securities issued	(45,008)	(42,297)	6.41%
<b>Interest margin</b>	<b>65,468</b>	<b>66,427</b>	<b>(1.44%)</b>

### **The margin from services**

Net commission disclosed a reduction of 7.09% due to the different classification in 2013 of “Fast credit processing fees” (Euro 3,260 thousand) in the item “other operating income”; on a like-for-like basis, the aggregate would disclose an increase of 7%, mainly attributable to the rise in the commission deriving from the placement of mutual funds and insurance products. In detail, commission on the placement of mutual funds reached a total Euro 2.1 million (+ Euro 0.6 million), while commission on the distribution of third party services - which exclusively comprise the commission relating to insurance policies - amounts to Euro 3.3 million, compared with Euro 2.2 million in 2012.

The commission relating to traditional services remained more or less unchanged. In detail, the decrease in commission for “other services”, down from Euro 6.5 million to Euro 3 million, is due to the afore-mentioned differing classification of the Fast credit processing fees (CIV), in replacement of the overdraft commission, which, according to the Bank of Italy Instructions, should be recorded in income statement item 190: “Other operating income/expense, since it is similar to that relating to cost recovery.

With regard to commission expense, the most significant item is made up of “guarantees given” for Euro 1.6 million compared with Euro 2 million in 2012. This is commission acknowledged by the government for the guarantee given on securities issued by the Bank deposited care of the ECB as collateral on the loans received. At the end of 2013, the guarantee given, maturing in February 2015, amounted to Euro 150 million and envisages annual commission of 1.05%. The additional expense in 2012 refers to the guarantee of Euro 150 million received at the end of 2011 maturing in June 2012, not renewed.

<b>NET COMMISSION FROM SERVICES (amounts in Euro 000s)</b>	<b>2013</b>	<b>2012</b>	<b>% change</b>
<b>COMMISSION INCOME</b>			
Guarantees given	1,174	1,259	(6.75%)
Management and trading services:	7,145	5,412	32.02%
- <i>foreign exchange dealing</i>	301	225	33.78%
	-	-	
- <i>custody and administration of securities</i>	94	76	23.68%
- <i>placement of securities</i>	2,098	1,483	41.47%
- <i>stock market instructions</i>	1,329	1,408	(5.61%)
- <i>distribution of third party services</i>	3,323	2,220	49.68%
Collection and payment services	5,549	5,478	1.30%
Servicer activities for securitisation transactions	130	163	(20.25%)
Account keeping and management	8,265	8,311	(0.55%)
Other services	2,993	6,507	(54.00%)
<b>Total</b>	<b>25,256</b>	<b>27,130</b>	<b>(6.91%)</b>
<b>COMMISSION EXPENSE</b>			
Guarantees given	(1,580)	(2,012)	(21.47%)
Management and trading services	(120)	(104)	15.38%
Collection and payment services	(1,443)	(1,388)	3.96%
Other services	(597)	(469)	27.29%
<b>Total</b>	<b>(3,740)</b>	<b>(3,973)</b>	<b>(5.86%)</b>
<b>TOTAL NET COMMISSION</b>	<b>21,516</b>	<b>23,157</b>	<b>(7.09%)</b>

## Net interest and other banking income

Besides the interest margin and net commission, the following contribute towards the formation of net interest and other banking income:

- dividends for Euro 179 thousand (compared with Euro 166 thousand);
- the gain/loss from trading activities for Euro 347 thousand (compared with Euro 197 thousand), almost entirely made up of the gain on foreign currency assets (Euro 331 thousand);
- the loss on the receivable factoring transaction for Euro 2,437 thousand, already commented on previously;
- gains on available-for-sale financial assets for Euro 26,423 thousand (compared with Euro 31,101 thousand);
- gains on the disposal and repurchase of Bank bonds for Euro 469 thousand (compared with Euro 638 thousand).

Overall, net interest and other banking income presented a balance of Euro 112 million.

## Value adjustments

Value adjustments, net of write-backs, amounted in total to Euro 50,074 thousand, compared with Euro 60,551 thousand in 2012.

The situation of doubtful loans and receivables at year end, consequent to the serious financial crisis underway and the related repercussions on the economic fabric of the area - as occurred for the entire Italian banking system - required, also due to the request of the supervisory bodies, particular attention for the assessment of the loans and receivables: an assessment which led to total net value adjustments (including those relating to non-performing positions factored) recorded for Euro 45.6 million, compared with Euro 56.6 million in 2012.

In addition, adjustments were made on available-for-sale financial assets for Euro 6,788 thousand (compared with Euro 3,990 thousand) and on guarantees given for Euro 65 thousand (in 2012 there were value write-backs for Euro 52 thousand).

The value adjustments on loans and receivables include both the specific adjustment on impaired positions and the losses indicated on positions which are subject to bankruptcy proceedings. Euro 1,183 thousand has been provided on performing loans.

The cost of credit, represented by the percentage-based incidence of the losses and the value adjustments on loans and receivables with respect to the amount of the net loans and receivables recorded in the financial statements, amounts to 1.53%, compared with 1.83% in 2012.

The provisions emerged as appropriate both with regard to the new non-performing positions emerging during the year - especially due to the decreased ability to reimburse by debtors - and with regard to the negative performance of the listings of the real estate property sector: this latter circumstance has triggered off a drop in the value of properties guaranteeing the credit positions.

As already mentioned, for the purpose of mitigating the credit risk as far as possible, the Bank reinforced the supervisory and safeguard measures on the dynamics of the aggregate in every direction, resorting to the various possible instruments including the subsidiary Valsabbina Real Estate which, intensifying the effectiveness of its role, took part in 18 property auctions, backed both by CTU (court-appointed expert) appraisals and by appraisals up-dated by the surveyors of Polis Fondi Immobiliari sgr.

In conclusion, the remaining value adjustments almost exclusively concerned the available-for-sale financial assets (Euro 6.7 million) and mainly refer to the write-down of the investments in Cassa di Risparmio di Ferrara and UBI Leasing.

As a result of the aforesaid entries, the net result from financial operations amounted to Euro 61.9 million, compared with Euro 61.1 million in the previous year.

## **Operating costs**

The strategy for containing the operating costs - which has always been a distinctive trait of the Bank's management policies - continued once again in 2013 with an increasingly disciplined approach and consequently appreciable results in more or less all the expenditure spheres; what is more, the cost synergies revealed themselves to be particularly significant, generated further to the incorporation of Credito Veronese.

The operating costs amount in total to Euro 50.6 million, compared with Euro 54.2 million last year; the drop therefore came to Euro 3.6 million, corresponding to a significant 6.7% decrease. Also without the effect of the classification of the Fast credit processing fees (Euro 3.3 million), the operating costs would have been lower than those last year.

Payroll and related costs amount to Euro 32.2 million, compared with Euro 30.5 million in 2012 (+ Euro 1.7 million or 5.5%), above all else due to the increase in the number of employees from 463 to 473. The item also includes the remuneration acknowledged, under the form of emoluments, to the members of the Board of Directors and the Board of Statutory Auditors.

Other administrative expenses rose during the year from Euro 26.5 million to Euro 26.9 million, disclosing a modest increase of 1.6%. However, excluding the expense related to stamp duty, whose recovery from customers is booked under other operating income/expense, said costs would amount to Euro 19.6 million compared with Euro 21.5 million in 2012 with a drop, in turn, of 8.8%.

It should be pointed out, since these are non-recurrent events, that as from 1 October 2013 VAT - which due to the tax regime applied to banks represents an additional cost component - underwent an increase in rate from 21 to 22% and that the administrative expenses for 2012

include charges, of an extraordinary nature, regarding the securitisation transaction for Euro 467 thousand.

The operating costs also include the value adjustments on tangible and intangible assets - respectively totalling Euro 1,700 thousand (-2.3%) and Euro 864 thousand (+9.5%) - and the net provisions to allowances for risks and charges, amounting to Euro 284 thousand, provided to cover typical banking disputes.

In conclusion, the positive balance between the other operating income /expense rose from Euro 6 million to Euro 11.4 million, due to the additional income deriving from the afore-mentioned recovery of the stamp duty, up from Euro 4,989 to Euro 7,318 thousand, and the recording of Fast credit processing fees in the item for Euro 3,260 thousand. Other operating expense includes the annual portion of the costs associated with improvements made to leased properties for Euro 212 thousand (Euro 329 thousand in 2012) and the amount requested by the Interbank Guarantee Fund for the measure in favour of banks in difficulty for Euro 576 thousand (Euro 155 thousand in 2012).

Further to the performances described above, the cost/income ratio - which expresses the ratio between the operating costs and net interest and other banking income - was confirmed as highly performing, at 45.2%.

### **Profitability performance**

The evolution of the profit margin illustrated above made it possible to stem the negative effects deriving from the important net value adjustment on loans and receivables recorded during the year, a phenomenon common to the entire banking system.

Profit from continuing operations gross of tax came to Euro 11.3 million, compared with Euro 6.9 million in 2012.

The tax burden amounted to Euro 3.6 million, compared with Euro 3.9 million in the previous year.

With regard to 2013, pursuant to Article 2.2 of Italian Decree Law No. 133/2013, banks are obliged to pay a surtax of 8.5% to be calculated on the taxable IRES adjusted by the increase of 4/5ths of the net adjustments relating to customer loans; the effect of the surtax amounts to Euro 1,003 thousand.

The deductibility for IRAP purposes, envisaged by Article 1.158 of Italian Law No. 147/2013, of the net value adjustments and write-backs due to impairment of loans and receivables had a positive impact on taxation for Euro 2,407 thousand.

The tax burden also benefited from the reversal to the income statement of Euro 885 thousand in deferred taxes already recorded in the financial statements further to the release of the difference between the book value of the tax value which formed with the valuation of the property at the time of initial application of the IAS, in addition to Euro 376 thousand deriving from the adjustment to the declarations presented for the releases of goodwill and other intangible assets recorded in previous years.

The ROE, which expresses the remuneration of the invested capital, stand at around 2.02% and should be considered to be positive in overall terms in light of the difficult reference context.

### **Financial statement ratios**

Closing and completing the analytical examination of the income statement items, the main balance sheet, productivity, efficiency and profitability ratios for the last few years are presented as follow, in accordance with Article 2428 of the Italian Civil Code.

<b>RATIOS</b>	<b>31 Dec. 2013</b>	<b>31 Dec. 2012</b>
<b>STRUCTURE RATIOS</b>		
Loans/Tot. assets	70.3%	74.5%
Loans /Direct deposits	93.6%	98.5%
Average employees per branch (No. employees /No. branches)	7.7	7.6
<b>PROFITABILITY RATIOS</b>		
Net interest and other banking income/total assets	2.6%	2.9%
Net profit/average shareholders' equity	2.02%	0.80%
Net profit/average total assets	0.18%	0.08%
Net interest and other banking income/banking product (1)	1.53%	1.67%
Value adjustments to loans/net interest and other banking	38.6%	46.5%
Tax rate	32.1%	56.2%
Earnings per Share	0.21	0.08
<b>PRODUCTIVITY RATIOS (in Euro 000s)</b>		
Banking product per employee (average)	16,038	15,907
Loans per employee (average)	6,526	6,734
Direct deposits per employee (average)	6,968	6,836
Indirect deposits per employee (average)	2,544	2,337
Net interest and other banking income per employee (average)	245	265
<b>EFFICIENCY RATIOS</b>		
Admin. expenses/average total assets	1.41%	1.51%
Admin. expenses/net interest and other banking income	52.8%	46.9%
Operating costs / Net interest and other banking income	45.2%	44.5%
Adjusted cost/income (2)	50.0%	46.6%
Admin. expenses/banking product	0.81%	0.78%
Payroll and related costs/average number of employees (in Euro	68.55	64.48
<b>ASSET QUALITY RATIOS</b>		
Net impaired loans/net loans	13.53%	11.77%
Non-performing loans/net loans	5.63%	4.73%
Value adjustments and losses on loans and receivables /net loans	1.53%	1.83%
Adjustments on non-performing loans/gross non-performing	34.87%	40.76%
Adjustments on impaired receivables and loans/gross impaired	21.64%	24.72%
<b>CAPITAL RATIOS</b>		
Tier 1	13.63%	13.08%
Total capital ratio	14.58%	14.10%

1. Direct and indirect deposits of customers plus customer loans
2. Ratio between income statement item 150 + 170 + 180 and 120 + 190

## 21 SIGNIFICANT EVENTS AFTER THE END OF THE YEAR

In compliance with a precise dictate of current legislation - Article 3 of Italian Legislative Decree No .87 dated 27 January 1992 - we hereby specify that after the year end date and up until approval of the draft financial statements by the Board of Directors, no significant events took place capable of influencing or affecting the balance sheet or income statement and on a more general note all the aspects which have been illustrated in this document.

## 22 BUSINESS OUTLOOK

The economic situation in Italy, and that of the Euro Zone which we are part of, realistically foresees - after years of heavy retreat of the growth rates - the prospect of a slow and gradual return to normality which what is more does not yet seem to authorise professions of optimism.

That which appears without doubt foreseeable for the Italian situation, is the continuation in the coming months of an economic situation and financial markets which at the most grant an interruption for 2014 to the negative sign in the product accounts and, therefore, the gross Italian profit.

The measures undertaken at political level for the adoption of structural reforms which permit, together with the restructuring of public finances, the re-launch of the economy as well, is still in a embryo state and, even if they bode as effective and liable to generate positive repercussions also for the banking system, they may disclose their effects in a somewhat lengthy manner.

Within this context, the adoption of the policies and the measures envisaged in the 2014 - 2016 Strategic Plan, which we have illustrated in-depth, legitimate - albeit very prudently - the expectation for 2014 of a moderate pick up in the levels of profitability, based essentially on the containment of the cost of credit and on the improvement of the core business margins.

## 23 PROPOSAL FOR APPROVAL OF THE FINANCIAL STATEMENTS

With regard to the distribution of the profit for the year of Euro 7,685,141, the Board of Directors proposes to the shareholders' meeting the payment of a cash dividend of Euro 0.12 per share, according to the following allocation:

<b>Net profit for the year</b>		<b>7,685,141</b>
10% to the legal reserve	(768,514)	
15% to the extraordinary reserve	(1,152,771)	
Portion allocated to the reserves		(1,921,285)
to the shareholders to the extent of Euro 0.12 per each of the 35,796,827 shares which represent the share capital		(4,295,619)
to the Charity Fund		(60,000)
Additional allocation to extraordinary reserve		(1,408,237)
Total		(7,685,141)

The dividend proposed corresponds to a pay out of 56% of the entire profit. No cash dividend

was paid in 2012.

If this proposal is approved, the shareholders' equity will amount to Euro 381,614 thousand.



## 24 THANKS

Dear shareholders, we have come to the end of our report which year by year becomes more extensive so as to contain the information and comments on a Bank which, despite the difficulties of the economic context, has grown both in numbers and the responsibility to govern the same.

We hope that our report may have demonstrated the immense commitment of all the components of the Bank to the growth of the business and for keeping it sound and autonomous in the area as a reference industrial co-operative bank for businesses, households and the institutions in our community.

If it true that the commitment has been intense and absorbing, it is also true that we have however felt supported by a loyal shareholding structure, which promptly responds and which supports us also in moments of particular severity, and by a wide array of customers who have shown us their preference, inducing us to improve and stand out in the crowded market of competitors. Genuine and heartfelt thanks therefore go to all our shareholders and customers.

We would also like to acknowledge our appreciation of General Management and all the workers who have done all they can day after day dedicating their best energies to the bank. We also thank the Board of Statutory Auditors for the commitment and sensitivity with which it has carried out its demanding appointment.

Our thoughts are also with the shareholders, customers and friends who are no longer with us, having left us this year, once again sending our condolences to their families. We would like - in particular - to affectionately remember our young and appreciated worker, Marta Lazzari, who prematurely left us leaving a void as deep as her presence and her memory today was sweet: once again our condolences to her children and family.

In conclusion, we thank the central and peripheral supervisory authorities and, in particular, the Management of the Brescia branch of the Bank of Italy, Consob and all the other bodies and associations which follow us with attention, expertise and co-operation.

The undersigned, Mr. Ezio Soardi, in his capacity as Chairman and Legal Representative of Banca Valsabbina Scpa, hereby certifies the correspondence of this document with that filed with the company's deeds.

The Chairman Legal Representative

(Ezio Soardi)