

# Report of the Supervisory Board of NLB d.d. on the results of examining the NLB Group Annual Report 2018

Pursuant to the provisions of the Companies Act<sup>1</sup> (hereinafter: **the Companies Act**) and the relevant corporate governance codes, the Supervisory Board compiled the written report for the General Meeting of Shareholders of NLB d.d.

## 1.) Report of the Supervisory Board of NLB d.d. on the results of examining the NLB Group Annual Report 2018 and the proposal for the allocation of distributable profit

Pursuant to the provisions of Article 282 of the Companies Act and Article 34 of the Articles of Association of Nova Ljubljanska banka d.d., Ljubljana, the Supervisory Board must check the Annual Report and the proposal for the allocation of distributable profit presented by the Management Board. It must compile a written report for the General Meeting on the findings of the examination referred to in the previous sentence.

On 12/04/2019, the Supervisory Board of NLB d.d. met for its 54th meeting and discussed the NLB Group Annual Report 2018 and the attached auditor's report prepared by Ernst & Young, Revizija, poslovno svetovanje d.o.o., Ljubljana (hereinafter: **Ernst & Young**). The Supervisory Board of NLB d.d. examined the compiled NLB Group Annual Report 2018. After a careful examination, the Supervisory Board of NLB d.d. had no comments to the report and therefore approved it unanimously, which means that the report is, therefore deemed approved.

The NLB Group has continued with the trend of stable and positive performance for the fifth consecutive year. It generated an excellent result in the amount of EUR 203.6 million after tax thanks to a significant contribution of the NLB Group subsidiaries.

All daughter banks on the southeastern European markets operated at a profit and thus contributed significantly to the Group's overall result. In addition to the parent bank, all core banks and the companies NLB Skladi d.o.o., Ljubljana, NLB Vita d.d., Ljubljana and Bankart d.o.o., Ljubljana operated at a profit in 2018.

Total net operating income amounted EUR 493.3 million, representing a 1% increase YoY (2017: EUR 487.7 million), and was driven by higher net interest income (EUR 3.6 million or 1% YoY) and higher regular net fee and commission income (EUR 5.2 million or 3% YoY). Net interest income increased due to loan volume growth and lower interest expenses. Loan growth continued to be solid with 10% YoY growth in strategic foreign markets and a 6% YoY growth in retail segment Slovenia. Group's gross loans exposure has shifted to individuals (to 49 % in 2018 from 45% in 2017) also as a consequence of favourable economic situation and consumer confidence.

Because of successful NPL resolution measures and a supportive macroeconomic environment, our loan portfolio quality continued to improve. Gross NPLs on the Group level were down EUR 222.2 million compared to December 2017, hence the NPL ratio decreased to 6.9%, while the internationally more comparable NPE ratio (based on EBA guidelines) fell to 4.7%. Overall, NLB Group recorded a negative cost of risk in 2018, with a net release of impairments and provisions in the amount of EUR 23.3 million.

The capital ratios (CET1 and total capital ratio) of the NLB Group remained strong, reaching 16.7% (including 1H'18 result), and were well above the regulatory thresholds. As already announced, NLB d.d. is in the process of examining various alternatives for issuing additional Tier2 capital.

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<sup>1</sup> The applicable corporate governance codes: Corporate Governance Code for Listed Companies (October 2016) and Corporate Governance Code for State-Owned Enterprises (May 2017).

In 2018, NLB Group continued focusing attention on finding solutions that best address client needs. NLB d.d. introduced 24/7 chat and video chat functionality through multiple channels and together with NLB Banka AD Skopje launched the mobile wallet 'NLB Pay' – a mobile payment solution with the potential to develop into an e-wallet platform. All banks are investing in upgrading their distribution capabilities with enhanced service offerings such as "Super Fast Cash Loan", POS lending and more targeted sales efforts (CRM). NLB Group is committed to remaining a leader of service innovation in banking for the region.

The Supervisory Board of NLB d.d. expressed its satisfaction with the achieved results. Progress was also noted in the area of digitalisation, simplification and modernisation of the processes and services which confirms that the entire NLB Group accepted the technological development and digitalisation as new opportunities for further growth. The Bank as well as the other members of the NLB Group played an active role of a generator of innovative, advanced and simple solutions for clients on their respective markets. The focus on the client, its needs and satisfaction is shown by the improved user experience and constant availability on the one hand and the in-depth advisory role on the other hand. In addition to the stable, sustainably profitable operations and a clear vision, this is the guarantee for a successful performance of the NLB Group also in the future.

The Supervisory Board of NLB d.d. performed its work in line with the powers vested in it and the Rules of Procedure of the Supervisory Board of NLB d.d. (March 2019). Its function of providing efficient supervision over the management of the bank and the NLB Group and its duty to act with diligence and prudence was performed in accordance with its powers stipulated by the applicable laws (the Companies Act and the Banking Act) and other provisions and in the internal documents of the bank (the Articles of Association of Nova Ljubljanska banka d.d.).

The Supervisory Board of NLB d.d. monitors and supervises the management and operations of the bank. Throughout the year, the Supervisory Board of NLB d.d. maintained a balanced professional relationship with the Management Board of NLB d.d. and received timely, comprehensive and data-supported information from the Management Board which allowed it to adopt decisions in accordance with the Bank's business interests, banking regulations and statutory powers. The Management Board of NLB d.d. regularly and completely informed the Supervisory Board of NLB d.d. of all issues related to the strategy, planning, development, risks and risk management important for the Bank. The co-operation between the Chairman of the Supervisory Board of NLB d.d. and the President of the Management Board of NLB d.d. is continuous and going on also outside the formal meetings, if required. Similarly, the other chairs of the committees cooperate with the relevant members of the Management Board of NLB d.d. outside the formal meetings. The Supervisory Board of NLB d.d. assessed that the Management Board of NLB d.d. worked efficiently in 2018.

Regarding the commitments made by the Republic of Slovenia to the European Commission in August 2018 the Supervisory Board of NLB d.d. monitored the fulfilment of those commitments during the year and also invited a representative of KPMG, poslovno svetovanje d.o.o., Ljubljana in the role of the Monitoring Trustee in charge of supervising the commitments to all its meetings.

In 2018, the General Meeting of NLB d.d. appointed the company Ernst & Young as external auditor for the auditing of the annual financial statements for a five-year period, namely for business years from 2018 to 2022. The co-operation with the external auditor took the form of external auditor's representatives regularly reporting to the Audit Committee of the Supervisory Board of NLB d.d., both on the progress and findings of the audit and on the implementation of external auditor's recommendations.

The auditor's report of the auditing company Ernst & Young was also attached with the NLB Group Annual Report 2018. The Management Board of NLB d.d. submitted to the Supervisory Board of NLB d.d. the NLB Group Annual Report 2018 which includes the business report with audited financial statements of NLB d.d., the consolidated financial statements of the NLB Group and the auditor's opinions. In the auditor's opinion, in all material respects, the individual and the consolidated financial statements enclosed give a true and fair view of the financial position of NLB d.d. and the NLB Group as at 31/12/2018, individual and consolidated income statement, and individual and consolidated cash flows for the year then ended, in accordance with the International Financial Reporting Standards as adopted by the European Union. It was also established on the basis of the audit of the business report that the information contained in the business section of the Annual Report is consistent with

the audited financial statements of the bank and the NLB Group. The Supervisory Board of NLB d.d. acknowledged the report of the auditing company Ernst & Young to the NLB Group Annual Report 2018 and had no comments.

Pursuant to the provisions of the first paragraph of Article 282 of the Companies Act, the Supervisory Board of NLB d.d. also checked the proposal of the Management Board of NLB d.d. for the allocation of distributable profit of NLB d.d. for the business year 2018 and approved it.

The distributable profit of NLB d.d. established as at 31/12/2018 amounted to EUR 194,491,264.58 and comprised the net profit for the business year 2018 in the amount of EUR 165,298,598.13, the effect of the change of the accounting policy due to the migration to the International Financial Reporting Standard IFRS 9: financial instruments in the amount of EUR 29,121,673.23, the transfer of realised profits arising from the surplus revaluation upon the derecognition of capital financial instruments measured at fair value through other comprehensive income in the amount of EUR 44,309.75 and profit brought forward from previous years in the amount of EUR 26,683.47.

Distributable profit in the amount of EUR 194,491,264.58 shall be used as follows:

- the part in total amount of EUR 142,600,000.00 shall be paid out to the shareholders as dividend, which amounts to EUR 7.13 gross per share,
- the part in the amount of EUR 51,891,264.58 shall remain undistributed and become part of the profit brought forward.

Pursuant to Article 272 of the Companies Act and the above report the Supervisory Board of NLB d.d. established and ensured that it regularly and thoroughly monitored the Bank's and the NLB Group's operations in 2018 within its powers and efficiently supervised the Bank's and the NLB Group's management and operations.

## **2. Report in accordance with the applicable corporate governance codes**

Pursuant to the recommendation 6.11 of the Corporate Governance Code for State-Owned Enterprises (May 2017) and the recommendations 5.1 and 12.11 of the Corporate Governance Code for Listed Companies (October 2016)<sup>2</sup>, the Supervisory Board of NLB d.d. also prepared the following report for the Bank's General Meeting:

Throughout 2018 the Supervisory Board of NLB d.d. was composed of eight members, namely: Primož Karpe - Chairman, Andreas Klingen - Deputy Chairman, and the following members: Alexander Bayr, David Eric Simon, László Urbán, Vida Šeme Hočevar, Simona Kozjek and Peter Groznik. On 30/11/2018, the Supervisory Board acknowledged the letter of resignation submitted by the members Simona Kozjek and Vida Šeme Hočevar with a three-month notice period which expired on 28/02/2019.

In accordance with the two-tier governance system and the authorisations for supervising the Management Board, the Bank's Supervisory Board among other issues approves to the Management Board related to the bank's business policy and financial plan, approves the strategy of the bank and the Group, organisation of the internal control system, annual action plan of the Internal Audit and all financial transactions defined in the Articles of Association of Nova Ljubljanska banka d.d. The Supervisory Board of NLB d.d. acts in accordance with the highest ethical standards of management, considering the prevention of conflicts of interest.

In 2018, the Supervisory Board of NLB d.d. met at seven regular and four correspondence sessions. In its work, the Supervisory Board of NLB d.d. received professional assistance from four of its

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<sup>2</sup> In addition to the statutory contents, the report of the Supervisory Board to the General Meeting should also include relevant information on the internal organisation of the Supervisory Board, on the composition of the Supervisory Board from the aspect of the independence of its members, on the (potential) conflict of interest and their settlement, and on procedures for the operation of the Supervisory Board including the indication of how much the self-assessment (i.e., the procedure for the evaluation of efficiency) has contributed to changes.

operational committees, namely the Audit Committee, the Risk Committee, the Nomination Committee and the Remuneration Committee, the composition and tasks of which are presented in the chapter on Corporate Governance in the NLB Group Annual Report 2018. With the aim of improving the bank's corporate governance, the Supervisory Board of NLB d.d. performed its duties in compliance with the relevant Corporate Governance Code for Listed Companies and until 14/11/2018 also in compliance with the Corporate Governance Code for State-Owned Enterprises.

All four committees of the Supervisory Board function as consulting bodies of the Supervisory Board of NLB d.d. and discuss the materials and proposals of the Management Board of NLB d.d. for the meetings of the Supervisory Board of NLB d.d. related to a particular area. Each of the four committees is composed of at least three members of the Supervisory Board. More detailed work of the committees of the Supervisory Board of NLB d.d. is presented in the chapter on Corporate Governance in the NLB Group Annual Report 2018.

In accordance with the recommendation No. 5 of the the Corporate Governance Code for Listed Companies a company must include Corporate Governance Statement into business report of the annual report. Corporate Governance Statement must be drawn up in accordance with the provisions of the Article 70, Paragraph 5 of the Companies Act. In the framework of the adoption of the annual report the Supervisory Board must take a stand on the Corporate Governance Statement as well. The Supervisory Board of NLB d.d. discussed and adopted Corporate Governance Statement of NLB d.d. at its 53rd regular meeting dated 8/3/2019.

In line with the recommendation 14 (in connection with recommendation 12.11) of the Corporate Governance Code for Listed Companies the Supervisory Board of NLB d.d. carried out in the second half of 2018 a self-assessment of its composition, operation, potential conflicts of interest of individual members and the functioning of individual members of the Supervisory Board of NLB d.d. and the Supervisory Board of NLB d.d. as a whole, as well as its cooperation with the Management Board of NLB d.d. In its assessment, the Supervisory Board of NLB d.d. also included the assessment of the work of the committees of the Supervisory Board of NLB d.d. At its meeting held on 30/11/2018 the Supervisory Board of NLB d.d. also acknowledged the results of the self-assessment and adopted the Action plan for the implementation of recommendations and/or findings from the conducted self-assessment. Most of the activities from the Action plan have already been implemented or will be completed shortly. These improvements from the self-assessment will contribute to better functioning of the Supervisory Board of NLB d.d. also in the future.

The members of the Supervisory Board of NLB d.d. have appropriate and complementary knowledge, experience and skills for performing their duties, with different professional, national and educational backgrounds. The Supervisory Board of NLB d.d. is composed of a balanced group of experts who complement each other and focus on the efficiency of performing their basic functions. All members of the Supervisory Board of NLB d.d. have the necessary personal integrity and professional ethics required for their position, which was confirmed by the positive fit&proper assessment prior to their appointment. It is thus ensured that their supervisory roles can be performed in a responsible way and that they are able to pass decisions for the benefit of the Bank. The adoption of critical and determined opinions has always been and will remain the basic principle in the decision-making process which is also based on the expected active involvement of all members at all times.

The members of the Supervisory Board of NLB d.d. signed the Statements of Independence of Supervisory Board member according to the Corporate Governance Code for Listed Companies. Each member of the Supervisory Board of NLB d.d. signs and submits to the Supervisory Board of NLB d.d. a statement on the existence of various conflicts of interest. A member of the Supervisory Board of NLB d.d. must immediately inform the Supervisory Board of NLB d.d. of any new potential conflicts of interest. The Statement on the absence of a conflict of interest of the members of the Supervisory Board of NLB d.d. (in the form of Attachment C to the Corporate Governance Code for Listed Companies) is published on the Bank's Slovenian website.

Throughout the year, the members of the Supervisory Board of NLB d.d. adopted preventive measures to prevent potential conflicts of interest that could affect their decisions. The Supervisory Board of NLB d.d. actively managed the conflicts of interest of its members and gave them consent for assuming positions on the supervisory boards of unrelated companies.

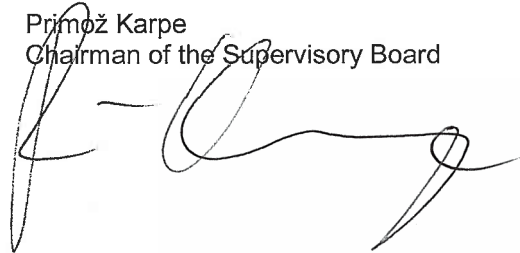
The conflict of interest is regulated by Article 6 of the Rules of Procedure of the Supervisory Board of NLB d.d. (March 2019). When deciding on individual issues at the meetings of the Supervisory Board of NLB d.d., its members followed the general rules of corporate governance concerning conflicts of interests. At the meetings, they informed the Supervisory Board of NLB d.d. of the existence of a conflict of interests in specific cases and excluded themselves from discussion and decision-making on the issue. As a result of the termination of the term of office of a member of the Supervisory Board of NLB d.d. who was a member of the Board of Directors in a Serbian bank and the expiration of the three-month notice of resignation of two members of the Supervisory Board of NLB d.d. on 28/02/2019, potential conflict of interest of members of the Supervisory Board of NLB d.d. does not exist anymore.

**In line with the above, the Supervisory Board of NLB d.d. hereby proposes that the General Meeting of Shareholders of NLB d.d. acknowledges the Report of the Supervisory Board of NLB d.d. on the results of the examination of the NLB Group Annual Report 2018.**

Ljubljana, 28/03/2019

Supervisory Board of NLB d.d.

Primož Karpe  
Chairman of the Supervisory Board

A handwritten signature in black ink, consisting of several loops and a long horizontal stroke, positioned below the printed name and title.

