

# INFORMATION OF PRUDENTIAL RELEVANCE

31 December 2018

## 1. GENERAL INFORMATION REQUIREMENTS

- 1.1 Introduction
- 1.2 Instituto de Crédito Oficial Consolidated Group
- 1.3 Other general information

## 2. RISK MANAGEMENT POLICIES AND OBJECTIVES

## 3. INFORMATION ON ELIGIBLE OWN FUNDS

- 3.1 Summary of the main characteristics and conditions of the items recorded as own funds of Tier 1 and Tier 2 capital
- 3.2 Total amount of own funds
- 3.3 Reconciliation of shareholders' equity with regulatory capital

## 4. INFORMATION ON MINIMUM OWN FUNDS REQUIREMENTS

- 4.1 Minimum own funds requirements for credit, counterparty credit, dilution and delivery risks and free deliveries
- 4.2 Minimum own funds requirements for settlement and delivery risks
- 4.3 Minimum own funds requirements for position, currency and commodity risks (market risk). Market risk of the trading portfolio
- 4.4 Minimum own funds requirements for operational risk
- 4.5 Minimum own funds requirements for credit valuation adjustment risk
- 4.6 Procedures applied for the assessment of internal capital adequacy

## 5. INFORMATION ON CREDIT RISKS

- 5.1 Accounting definitions and description of methods used to determine impairment corrections
- 5.2 Exposure to credit risk and average value of exposures for the year
- 5.3 Geographical distribution of exposures
- 5.4 Residual maturity of exposures
- 5.5 Counterparts and geographical distribution of defaulted positions
- 5.6 Variations during the year in impairment losses and provisions for contingent risks and commitments for credit risk
- 5.7 Information on the Group's counterparty credit risk

## **6. CREDIT RISK: CREDIT RATINGS**

- 6.1 Identification of internal rating agencies used
- 6.2 Description of the process of assigning external credit ratings for the determination of credit risk weighted exposures

## **7. CREDIT RISK: CREDIT RISK MITIGATION TECHNIQUES**

- 7.1 General information for credit risk
- 7.2 Policies and processes for netting of positions and collateral valuation for counterparty risk
- 7.3 Quantitative information
- 7.4 Effect on risk exposures of the application of risk mitigation techniques and exposures deducted directly from own funds

## **8. SECURITISATION TRANSACTIONS**

- 8.1 General information on securitisation activity
- 8.2 Exposures in securitisation transactions and amount of securitised assets

## **9. MARKET INFORMATION REQUIREMENTS: INFORMATION ON REMUNERATIONS**

## **10. INFORMATION ON SHARES AND EQUITY INSTRUMENTS NOT INCLUDED IN THE TRADING PORTFOLIO**

## **11. INTEREST RATE RISK. MARKET RISK**

## **12. CAPITAL BUFFERS**

## **13. INFORMATION ON UNENCUMBERED ASSETS**

## **14. INFORMATION ON LEVERAGE**

## **1. GENERAL INFORMATION REQUIREMENTS**

### **1.1. INTRODUCTION**

The objective of this report is to comply with the market reporting requirements of the Instituto de Crédito Oficial Consolidated Group, as set out in Part Eight of Regulation EU 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms (hereinafter “the Solvency Regulation”).

Law 10/2014 of 26 June on the organisation, supervision and solvency of credit institutions replaced, as from 1 January 2014, the previous legal text on prudential banking regulation (Law 13/1985 of 25 May and Bank of Spain Circular 3/2008). The main purpose of Law 10/2014, of 26 June, was to adapt the Spanish legal system to the regulatory changes imposed at international and European Union level, directly incorporating the provisions of Regulation (EU) 575/2013, of 26 June (CRR), and duly transposing Directive 2013/36/EU, of 26 June (CRD4). These Community regulations have substantially altered the applicable legislation for credit institutions, since aspects such as the supervisory regime, the capital requirements and the sanctioning regime have been extensively modified.

Pursuant to Additional Provision 8 of Law 10/2014 of 26 June on the organisation, supervision and solvency of credit institutions, the Instituto de Crédito Oficial will be subject to Titles II (Solvency of credit institutions), III (Supervision) and IV (Sanctioning Regime) of said Law, with the exceptions determined by regulation, and the provisions concerning information confidentiality.

In accordance with the information disclosure policies approved by the Institute, this report has been prepared on an annual basis by the Institute's Directorate General of Risks and Financial Control and approved by its President, after verification by the Internal Audit Department.

Certain information required by the regulations in force that must be included in this report is presented, in accordance with said regulations, referenced to the consolidated annual accounts of the ICO Group for the financial year 2018, as it is contained therein and being redundant with it. The aforementioned annual accounts, as well as this document on "Information of prudential relevance" can be consulted on the ICO website ([www.ico.es](http://www.ico.es)).

## **1.2. INSTITUTO DE CRÉDITO OFICIAL CONSOLIDATED GROUP**

The information presented in this report corresponds to the Consolidated Group of Credit Institutions whose dominant entity is the Instituto de Crédito Oficial (hereinafter, the Group or ICO Group).

Subsidiaries are those entities over which the Bank has control. It is considered that an entity controls an investee when it is exposed or entitled to variable returns because of its involvement in the investee and has the ability to influence those returns through the power it exercises over the investee.

In order to be considered as subsidiaries, it must concur:

- Power: An investor has power over an investee when the former has rights in force that give it the capacity to manage the relevant activities, i.e. those that significantly affect the investee's returns;
- Returns: An investor is exposed to, or is entitled to, variable returns for his involvement in the investee when the returns obtained by the investor for such involvement may vary depending on the economic evolution of the investee. The investor's returns may be only positive, only negative or both positive and negative.

Relationship between power and returns: An investor controls an investee if the investor not only has power over the investee and is exposed to, or is entitled to, variable returns for his involvement in the investee, but also has the ability to use his power to influence the returns he obtains from that involvement in the investee.

The annual accounts of the subsidiaries are consolidated with those of the Institute using the full integration method as defined in the regulations. Consequently, all significant balances arising from transactions carried out between the consolidated companies using this method have been eliminated in the consolidation process. The Institute, the Group's dominant entity, accounts for 99% of the Group.

In addition, the participation of third parties in:

- The Group's equity: is presented under "Minority Interests" in the consolidated balance sheets. As at 31 December 2018, there were no minority interests.
- The consolidated results for the year: are presented under the "Income Attributable to Minority Interests" heading in the consolidated income statement. As at 31 December 2018, there were no results attributed to minority interests.



The consolidation of the results generated by the subsidiaries acquired in a given year is carried out taking into account only those relating to the period between the acquisition date and the year-end.

On the other hand, "associates" are those entities over which the Institute has the capacity to exercise significant influence, although they do not constitute a decision-making unit with the Institute nor are they under joint control. Usually, this capacity is manifested in a participation (direct or indirect) equal to or greater than 20% of the voting rights of the investee.

Investments in entities considered as "associates" are presented in the consolidated annual accounts recorded under the heading "Investments in Subsidiaries, Joint Ventures and Investees - Associates" in the consolidated balance sheet, valued at acquisition cost, net of any impairment losses that may have been suffered by such investments.

The results generated by transactions between the associate and Group entities are eliminated by the percentage represented by the Group's share in the associate.

The results obtained by the associate during the year, after the elimination referred to in the previous section, increase or reduce, as the case may be, the value of the investment in the consolidated annual accounts. The amount of these results is recorded under the heading "Share of profit or loss of entities accounted for using the equity method" in the consolidated income statement.

Changes in the associate's valuation adjustments after the acquisition date are recorded as an increase or decrease in the value of the shareholding. The amount of these changes is recorded under "Accumulated other comprehensive income" as valuation adjustments of consolidated equity.

There are no "jointly-controlled institutions" included in the Consolidation Group.

The following is a summary of the main differences regarding the scope of consolidation and the different consolidation methods applied between the Consolidated Group of Credit Institutions Instituto de Crédito Oficial, for which the information contained in this report is presented, and the Group of Credit Institutions ICO, defined in accordance with Rule 3 of Bank of Spain Circular 4/2017, of 27 November.

In the preparation of the consolidated annual accounts of the ICO Group of Credit Institutions, all subsidiaries have been consolidated applying the global integration method, as they meet the requirements to be considered as consolidable due to their activity. Therefore, there are no differences in the scope of consolidation for the purposes of applying the solvency requirements.

For the purposes of preparing the consolidated financial statements of the ICO Group of Credit Institutions, investments in financial institutions that do not meet the requirements to be considered as subsidiaries, jointly controlled entities or associates are considered financial instruments and are valued in accordance with the criteria established in Rule 22 of Bank of Spain Circular 4/2017, of 27 November.

However, for the purposes of applying the solvency requirements, financial entities that have not been classified as subsidiaries, jointly controlled entities or associates pursuant to Rule 47 of Bank of Spain Circular 4/2017, of 27 November, in which at least 20% of their capital or voting rights are owned or controlled, are valued by the equity method for the purposes of preparing the information of the Consolidated Group.

In accordance with the criteria indicated above, the following is a detail as at 31 December 2018 of the subsidiaries of the Consolidated Group to which the global integration method has been applied for the purposes of preparing the consolidated information thereof:

ENTITY: AXIS PARTICIPACIONES EMPRESARIALES, S.G.E.I.C, S.A S.M.E.

Annex I to the Institute's consolidated financial statements contains relevant information on the associates included in the Group.

### **1.3 OTHER GENERAL INFORMATION**

As at 31 December 2018, there is no material, practical or legal impediment to the immediate transfer of own funds or reimbursement of liabilities between the Group's subsidiaries and the Instituto de Crédito Oficial, and there is nothing to suggest that such impediments may exist in the future.

As at 31 December 2018, there are no entities belonging to the economic Group and not included in the consolidated Group that are subject to minimum own funds requirements at individual level, in accordance with the various regulations applicable to them.

As at 31 December 2018, the stake in AXIS PARTICIPACIONES EMPRESARIALES, S.G.E.I.C, S.A S.M.E. included in the Consolidated Group is not subject to the calculation of own funds requirements in individual terms and is included in the ICO consolidated group, which is subject to such requirements.

All the amounts contained in this report are expressed in thousands of euros.

The ICO is not considered a Global Systemic Entity.

## **2. RISK MANAGEMENT POLICIES AND OBJECTIVES**

The information on risk management policies and objectives that the Regulations require to be provided to the market can be found in Note 5 (Risk Exposure) of the Consolidated Report included in the consolidated annual accounts of the Instituto de Crédito Oficial Group for 2018, published on the ICO website. ([www.ico.es](http://www.ico.es)).

## **3. INFORMATION ON ELIGIBLE OWN FUNDS**

### **3.1 SUMMARY OF THE MAIN CHARACTERISTICS AND CONDITIONS OF THE ITEMS ACCOUNTED FOR AS OWN FUNDS OF TIER 1 AND TIER CAPITAL**

For the purposes of calculating its minimum own funds requirements, the Group considers as own funds of Tier 1 capital the items defined as such, considering the corresponding deductions, in Part Two, Title I, Chapters 1 to 3, of the Solvency Regulation.

Own funds of Tier 1 capital are characterised by being components that can be used immediately and without restriction to hedge risks or losses as soon as they occur, the amount being recorded

free of any foreseeable tax at the time it is calculated. These elements show stability and permanence over time, a priori higher than that of own funds of Tier 2 capital as explained below. As indicated in section 3.2 below, the Group's own funds of Tier 1 capital as at 31 December 2018 are basically made up of the Institute's equity and the retained profits and undisclosed reserves.

On the other hand, own funds of Tier 2 capital are considered to be those defined in Part Two, Title I, Chapter 4 of the Solvency Regulation, with the limits and deductions established in said Regulation. Although these own funds comply with the definition of own funds established in the current regulations, they are characterised by having, a priori, a lower volatility or degree of permanence than the elements considered as own funds of Tier 1 capital. As indicated in section 3.2 below, as at 31 December 2018 there were no Group's own funds of Tier 2 capital.

All the concepts which, in accordance with the provisions of the Solvency Regulation, are part of are part of ICO Group's eligible own funds, have homogeneous characteristics as far as their definition and characteristics are concerned, so that their content is not described individually.

**3.2 TOTAL AMOUNT OF OWN FUNDS**

Below is a detail as at 31 December 2018 of the Consolidated Group's eligible own funds, indicating each of its components and deductions, and broken down into own funds of Tier 1 and Tier 2 capital:

	Amount (thousands of euros)
Total Eligible Own Funds	5,179,437
Tier 1 capital	5,179,437
Common Tier 1 capital	5,179,437
Capital instruments eligible as Common Tier 1 capital	4,313,744
Retained earnings	935,176
Other reserves	-73,435
Common Tier 1 capital adjustments due to prudential filters	67,901
Other intangible assets	-7,005
Common Tier 1 capital elements or deductions - Capital instruments Financial Sector Entities with significant investment	-73,197
Elements or deductions from Common Tier 1 capital - Others	16,253
Additional Tier 1 capital	0
Tier 2 capital	0
Adjustments for general credit risk using the standard method	0

### 3.3 RECONCILIATION OF SHAREHOLDERS' EQUITY TO REGULATORY CAPITAL

The reconciliation between the Institute's shareholders' equity reflected in the financial statements and the regulatory capital for solvency purposes as at 31 December 2018 is presented below:

CONCEPT	<i>(Thousands of Euros)</i>
	<b>2018</b>
Capital	4,313,744
Reserves	954,531
Net attributable profit	75,671
<b>TOTAL OWN FUNDS IN PUBLIC BALANCE SHEET</b>	<b>5,343,946</b>
Valuation adjustments	-57,182
<b>TOTAL EQUITY PUBLIC BALANCE SHEET</b>	<b>5,286,764</b>
Other adjustments to basic capital	-
Tier 1 capital deductions	-107,327
<b>TIER 1 CAPITAL</b>	<b>5,179,437</b>

### 4. INFORMATION ON MINIMUM OWN FUNDS REQUIREMENTS

The summary of the total minimum own funds requirements as at 31 December 2018, by type of risk, is shown below:

TOTAL OWN FUNDS REQUIREMENTS	<i>(Thousands of Euros)</i>
	<b>2018</b>
For credit, counterparty credit and dilution risks, and free deliveries	982,938
For settlement and delivery risk	0
For position, currency and commodity risks	8,954
For operational risk	6,452
For credit valuation adjustment risk	19,794
<b>TOTAL REQUIREMENTS</b>	<b>1,018,138</b>

**4.1 MINIMUM OWN FUNDS REQUIREMENTS FOR CREDIT, COUNTERPARTY CREDIT, DILUTION AND DELIVERY RISKS AND FREE DELIVERIES**

Below is the amount of the minimum own funds requirements of the Consolidated Group for credit risk as at 31 December 2018, calculated for each of the categories to which the standard method has been applied (Part 3, Title II, Chapter 2, of the Solvency Regulation), as 8% of the risk-weighted exposures:

*Amounts in thousands of euros*

Total amount of requirements for credit, counterparty credit and dilution risks and free deliveries	982,938
Standard method	982,938
Categories of exposure of the standard method excluding securitisation positions	982,938
Central governments or central banks	22,724
Regional administrations or local authorities	
Public sector entities	191,167
Multilateral development banks	4,347
International organisations	
Entities	262,256
Companies	375,016
Retail exposures	2,130
Exposures secured by mortgages on immovable property	
Exposures in default	5,210
Exposures associated with particularly high risk	
Covered bonds	
Exposures to institutions and corporates with a short-term credit assessment	
Shares in collective investment undertakings (CIUs)	
Equity instruments	109,784
Others	10,304
Securitisation positions according to the standard method	
*Of which: re-securitisation	

#### 4.2 MINIMUM OWN FUNDS REQUIREMENTS FOR SETTLEMENT AND DELIVERY RISK

There are no Group own funds requirements for settlement/delivery risk (Part 3, Title V of the Solvency Regulation).

*Amounts in thousands of euros*

Total amount of requirements for settlement/delivery risk	
Settlement/delivery risk in the investment portfolio	
Settlement/delivery risk in the trading portfolio	

#### 4.3 MINIMUM OWN FUNDS REQUIREMENTS FOR POSITION, CURRENCY AND COMMODITY RISKS (MARKET RISK). MARKET RISK OF THE TRADING PORTFOLIO

*Amounts in thousands of euros*

Total amount of requirements for position, currency and commodity risks	8,954
Amount of requirements for position, currency and commodity risks according to standard methods	8,954
Negotiable debt instruments	8,129
Equity instruments	
Currency	825
Commodities	

The calculation is made in accordance with the provisions of Part 3, Title IV, of the Solvency Regulation.

With respect to the market risk associated with the trading portfolio, it should be noted that the Group considers as such those positions in financial instruments that are held with the intention of trading or that serve as hedges for the elements of said portfolio. In this regard, there are no differences between the trading portfolio for the purposes of calculating the Group's own funds requirements and the trading portfolio defined in accordance with Bank of Spain Circular 4/2017, of 27 November, with respect to debt securities and capital instruments.

The total amount of the own funds requirements associated with the trading portfolio as at 31 December 2018 corresponds to the position risk of negotiable debt instruments.

**4.4 MINIMUM OWN FUNDS REQUIREMENTS FOR OPERATIONAL RISK**

*Amounts in thousands of euros*

Total amount of requirements for operational risk	6,452
Operational risk - Basic indicator method	6,452
Operational risk - Standard/standard alternative methods	
Operational risk - Advanced calculation methods	

The Group uses the relevant indicator (or basic indicator) method to determine the own funds requirements associated with operating risk (Part 3, Title III of the Solvency Regulation).

**4.5 MINIMUM OWN FUNDS REQUIREMENTS FOR CREDIT VALUATION ADJUSTMENT RISK**

*Amounts in thousands of euros*

Total amount of requirements for credit valuation adjustment risk	19,794
Advanced method	
Standard method	19,794
Based on the original exposure method	

The Group uses the standard method for determining the own funds requirements associated with credit valuation risk (Part 3, Title IV of the Solvency Regulation).

**4.6 PROCEDURES APPLIED FOR THE ASSESSMENT OF INTERNAL CAPITAL ADEQUACY**

In accordance with the provisions of the Solvency Regulation, the Consolidated Group applies a series of risk identification, measurement and aggregation procedures that allow it to define and maintain a level of own funds in accordance with the risks inherent to its activity, to the economic environment in which it operates, to the management and control it carries out of these risks, to the governance systems at its disposal, to its strategic business plan and to its real possibilities of obtaining greater own funds, in other words, it carries out an assessment of internal capital, both at the present time and in the projected future based on its planning.

In assessing its internal capital, the Group applies the following procedures related to each of its risks:

- Assessment of capital needs for credit risk: the standard method established in the Solvency Regulation was applied to calculate the minimum own funds requirements associated with this risk.

- Assessment of capital needs for liquidity risk: The Group does not foresee capital needs associated with this risk, once its liquidity policy, liquidity control systems and contingency

plans have been analysed, which show that it enjoys an adequate liquidity situation and, therefore, does not require capital to cover this risk.

- Assessment of capital needs by market risk: the standard method established in the Solvency Regulation was used to estimate the minimum own funds requirements associated with this risk.

- Assessment of capital needs for operational risk: the basic approach is being applied.

- Assessment of capital needs for credit valuation adjustment risk: the standard methodology for calculating the capital required for this risk is being applied.

The Group's total capital requirement has been estimated by aggregating the capital needs associated with each risk, obtained in accordance with the methods indicated above.

In addition, in order to adequately plan the Group's future capital requirements, it is carried out the corresponding projections of profits assigned to reserves and capital consumption derived from expected activity growth in different scenarios that contemplate, among others, stress situations.

The capital planning process seeks to determine the future capital requirements of ICO in a given time horizon. For the purposes of this report, three years are considered. To this end, the sources and consumptions of capital are estimated for the next three financial years, considering as a base for this financial year the forecasts of the Institute for the considered horizon, which will be the base scenario.

In addition to the base scenario, the Institute has estimated what its capital needs would be under an adverse macroeconomic scenario and under various additional stress scenarios, in line with the provisions of the PAC (Capital Self-Assessment Process) and PAL (Liquidity Self-Assessment Process) Guidelines.

The results of the capital planning process include, for all scenarios, the following information:

- Projected evolution of the main balance sheet and income statement masses.
- Calculation of required capital and risk-weighted assets (RWA) for each of the Pillar I risk types in each year.
- Contrast between capital requirements and available capital (in a phase-in scenario and a fully-loaded scenario).
- Action Plan to cover eventual capital needs (if applicable).

In all cases, it is confirmed that the Institute has a capital figure that is expected to enable it to meet the legally required minimums, even in crisis scenarios.

## 5. INFORMATION ON CREDIT RISKS

### 5.1 ACCOUNTING DEFINITIONS AND DESCRIPTION OF THE METHODS USED TO DETERMINE IMPAIRMENT CORRECTIONS

The concepts of positions in default and impairment corrections referred to in this document are based on the definitions in the Solvency Regulation and Annex IX of Bank of Spain Circular 4/2017.

Note 2.7 of the consolidated report forming part of the 2018 financial statements of the ICO Group describes the methods used by the Group in determining the provisions for impairment due to credit risk and in calculating the provisions for contingent risks and commitments associated with that risk.

### 5.2 EXPOSURE TO CREDIT RISK AND AVERAGE VALUE OF EXPOSURES FOR THE YEAR

The total value of risk-weighted exposures, as at 31 December 2018, for credit risk of the Consolidated Group, and their distribution by counterparty class, is as follows:

Amounts in thousands of euros

Risk-weighted exposure amounts for credit, counterparty credit and dilution risks and free deliveries	12,286,726
Standard method	12,286,726
Categories of exposure of the standard method excluding securitisation positions	12,286,726
Central governments or central banks	284,049
Regional administrations or local authorities	
Public sector entities	2,389,587
Multilateral development banks	54,339
International organisations	
Entities	3,278,183
Companies	4,687,706
Retail exposures	26,629
Exposures secured by mortgages on immovable property	
Exposures in default	65,124
Exposures associated with particularly high risk	
Covered bonds	
Exposures to institutions and corporates with a short-term credit assessment	
Shares in collective investment undertakings (CIUs)	
Equity instruments	1,372,304
Others	128,805
Securitisation positions according to the standard method	
*Of which: re-securitisation	

The average value of risk-weighted exposures in 2018, for credit risk of the Consolidated Group and their distribution by counterparty class, is as follows:

*Amounts in thousands of euros*

Average amount of risk-weighted exposures for credit, counterparty credit and dilution risks and free deliveries		13,505,326
Standard method		13,505,326
Categories of exposure of the standard method excluding securitisation positions		13,505,326
Central governments or central banks		850,927
Regional administrations or local authorities		
Public sector entities		2,833,381
Multilateral development banks		37,599
International organisations		
Entities		3,298,445
Companies		4,770,173
Retail exposures		28,851
Exposures secured by mortgages on immovable property		
Exposures in default		96,446
Exposures associated with particularly high risk		
Covered bonds		
Exposures to institutions and corporates with a short-term credit assessment		
Shares in collective investment undertakings (CIUs)		
Equity instruments		1,461,800
Others		127,704
Securitisation positions according to the standard method		
*Of which: re-securitisation		

### 5.3 GEOGRAPHICAL DISTRIBUTION OF EXPOSURES

The detail of risk-weighted exposures, to credit risk of the Consolidated Group as at 31 December 2018, broken down by geographical area, is shown below:

Geographical Area	Exposure amount
	(Thousands of Euros)
	<b>2018</b>
Spain	11,466,231
Other countries of the European Union	428,834
Latin America	288,108
United States	37,219
Rest of Europe (non-EU)	14
Rest of the world	66,320
<b>Exposure as at 31 December 2018</b>	<b>12,286,726</b>

### 5.4 RESIDUAL MATURITY OF EXPOSURES

The distribution by residual maturity of the Consolidated Group's risk-weighted exposure to credit risk as at 31 December 2018, using the standard method for calculating own funds requirements, is presented below:

# INFORMATION OF PRUDENTIAL RELEVANCE

## 31 December 2018



Risk category	Residual maturity as at 31 December 2018						
	<i>(Thousands of euros)</i>						
	Up to 1 year	From 1 to 2 years	From 2 to 3 years	From 3 to 4 years	From 4 to 5 years	More than 5 years	Total
<b>2018</b>							
A) Central governments and central banks	39,877	26,316	29,424	38,793	28,769	120,870	284,049
B) Regional administrations and local authorities	-	-	-	-	-	-	-
C) Public sector entities	335,465	221,389	247,530	326,354	242,023	1,016,826	2,389,587
D) Multilateral development banks	7,628	5,034	5,629	7,421	5,504	23,123	54,339
E) International organisations							
F) Entities	460,212	303,715	339,577	447,712	332,022	1,394,945	3,278,183
G) Companies	658,090	434,303	485,586	640,215	474,782	1,994,730	4,687,706
H) Retail exposures	3,738	2,467	2,758	3,637	2,697	11,331	26,629
I) Exposures secured by immovable property							
J) Exposures in default	9,143	6,034	6,746	8,894	6,596	27,712	65,124
K) High risk exposures.							
L) Covered bonds.							
M) Short-term exposures to institutions and companies							
N) Exposures to collective investment institutions							
Ñ) Equity Instruments						1,372,304	1,372,304
O) Other exposures	18,082	11,933	13,343	17,591	13,046	54,810	128,805
<b>Exposure as at 31 December 2018</b>	<b>1,532,235</b>	<b>1,011,191</b>	<b>1,130,593</b>	<b>1,490,617</b>	<b>1,105,439</b>	<b>6,016,651</b>	<b>12,286,726</b>

## 5.5 DISTRIBUTION BY COUNTERPARTIES AND GEOGRAPHICAL AREA OF EXPOSURES IN DEFAULT

### Exposures in default by counterparty

The following table presents the value of original exposures for default risk (impaired and in default) as at 31 December 2018, before adjustments and provisions, broken down by type of counterparty, together with the amount of impairment losses and provisions for contingent risks and commitments established in relation to those exposures at that date and the amount of impairment losses and provisions for contingent risks and commitments recognised, on a net basis, during the 2018 financial

year (standard method for determining own funds requirements for credit risk):

Counterparty	Total Impaired exposures	Of which: Exposures in default status	Impairment losses and provisions for contingent risks and commitments	Provisions to impairment losses and contingent risks and commitments for the year (net)
	<i>(Thousands of Euros)</i>			
	<b>2018</b>			
A) Central Governments and Central Banks				
B) Regional Administrations and Local Authorities				
C) Public sector entities				
D) Multilateral Development Banks				
E) International organisations				
F) Credit institutions and Investment Services companies				
G) Companies	636,897	240,466	597,041	-94.679
H) Retail exposures				
I) Exposures secured by mortgages on immovable property				
J) High risk exposures				
K) Covered bonds				
L) Short-term exposures with regard to Institutions and Companies				
M) Exposures to Collective Investment Institutions				
N) Equity Instruments				
Ñ) Other exposures				
Amounts as at 31 December 2018	636,897	240,466	597,041	-94,679

Exposures in default status by geographical area

Also, below is a detail, by significant geographical area, of the value of original impaired exposures and of those in default as at 31 December 2018, together with the amount of impairment losses and the provisions for contingent risks and commitments established in relation to these exposures:

Geographical Area	<i>(Thousands of Euros)</i>		
	Total Impaired exposures	Of which: Exposures in default status	Impairment losses and provisions for contingent risks and commitments
			<b>2018</b>
Spain	483,838	202,577	467,914
Other countries of the European Union	134,859	37,889	110,927
Latin America	18,200	-	18,200
United States			
Rest of Europe (non-EU)			
Rest of the world			
Amount as at 31 December 2018	636,897	240,466	597,041

**5.6 VARIATIONS OCCURRED DURING THE YEAR IN IMPAIRMENT LOSSES AND PROVISIONS FOR CONTINGENT RISKS AND COMMITMENTS FOR CREDIT RISK**

The changes in 2018 in the impairment losses due to credit risk accounted for by the Group and in the provisions for contingent risks and commitments due to credit risk are in accordance with Bank of Spain Circular 4/2017, both in the type of losses and provisions constituted and in the methodology applied to calculate them (see section 5.1 above in this report).

The detail of the changes made in 2018 in the value adjustments for impairment of financial assets (including provisions for normal risk under special surveillance) and in the provisions for contingent risks and commitments due to credit risk is shown below:

	Impairment losses on financial assets	Provisions for contingent risks and commitments
	<i>(Thousands of Euros)</i>	
Balance as at 1 January 2018	1,072,370	23
Provisions charged to income	-	
Recovery with credit to income	-94,679	
Amounts applied in the year	-286,406	
Effect of foreign currency exchange differences	33	
Changes due to business combinations		
Changes in the scope of consolidation		
First application Circular 4/2017	124,373	43
Other movements	2,469	
<b>Balances as at 31 December 2018</b>	<b>818,160</b>	<b>66</b>

In addition, the expenses recognised in the consolidated income statement of the ICO Group in 2018 for items transferred directly to written-off assets are nil, whereas the credit recorded in the consolidated income statement for the year for the recovery of assets previously recorded as written-off amounted to 3,770 thousand euros.

## **5.7 INFORMATION ON THE COUNTERPARTY CREDIT RISK OF THE GROUP**

Counterparty credit risk is considered to be the credit risk incurred by the Group in the operations it carries out with derivative financial instruments and in the operations with repurchase commitments, securities or commodities lending commitments, in deferred settlement operations and guarantee financing operations.

It is controlled by means of a system that integrates the management of transactions and the risks arising therefrom in real time, providing operators with updated information on the credit lines available at any given time.

A methodology for the consumption of counterparty lines based on the valuation of transactions at market prices plus a potential future risk or "add-on" has been defined for derivatives and has been approved by the competent bodies of ICO, which is measured as a percentage of the nominal value of the transaction and is calculated as the maximum potential loss (95% confidence) over the life of the transaction. The methodology is reviewed periodically (at least once a year) and the add-ons are adjusted at least semi-annually.

The basic criteria for establishing the counterparty lines are approved by the ICO General Council. These counterparty lines are subdivided into two main groups as a result of ICO's operational characteristics. On the one hand, the counterparty lines for treasury operations. On the other hand, the counterparty lines for mediation operations, operations in which ICO finances different investment projects through framework programmes signed with different entities operating in Spain, such as, for example, the SME Lines.

In order to mitigate exposure to counterparty risk, the Group signs ISDA and CMOF contracts with the counterparties and, where appropriate, the corresponding collateral annexes.

With respect to the management of collaterals, in the case of derivatives, for entities subject to collateral agreements, the position is periodically valued (normally on a day-to-day basis) and, on this valuation, the parameters agreed in the collateral agreement are applied, so that a collateral amount (cash) to be received or returned from the counterparty is obtained.

These amounts ("margin calls") are made on a weekly basis. The counterparty that receives the collateral payment request reviews the valuation, and discrepancies may arise in this process. If these discrepancies are material, they are analysed in detail.

The collaterals signed by ICO with the counterparties have the differential characteristic of being "one way", so that only the counterparties of ICO are obliged to deposit collateral.

As 100% of collaterals received are in cash, value corrections for collateral impairment are not applicable.

With respect to the correlation between the guarantee and the guarantor in derivatives, since cash is received as collateral, there is no risk of adverse effects due to the existence of correlations.

Following is a detail of the Group's credit exposure to counterparty risk due to its operation in derivatives as at 31 December 2018, valuation method at market prices, estimated as the amount of the Group's credit exposure for these financial instruments, net of the guarantees received from the counterparties of the operations:

*Amount (Thousands of Euros)*

**2018**

Exposure value: method of valuation at market prices	580,686
Less: Effect of guarantees received	-7,378
Credit exposure in derivatives after guarantees as at 31 December 2017	573,308

The value of the exposure has been calculated according to the method of valuation at market prices (Part 3, Title II, Chapter 6 of the Solvency Regulation).

## 6. CREDIT RISK: CREDIT RATINGS

### 6.1 IDENTIFICATION OF THE INTERNAL RATING AGENCIES USED

For all categories of credit risk exposure to which the standard method is being applied, the external and export credit rating agencies whose ratings are being used by the Group as at 31 December 2018 are as follows (ECAIs recognised by the Bank of Spain):

- Moody's
- Standard & Poor's
- Fitch Ratings
- D.B.R.S.

### 6.2 DESCRIPTION OF THE PROCESS OF ASSIGNING EXTERNAL CREDIT RATINGS FOR THE DETERMINATION OF CREDIT RISK WEIGHTED EXPOSURES

The allocation rules defined in the Solvency Regulation apply:

- When, for a rated exposure, only one credit rating is available, this rating will be used to determine the risk weighting.
- When, for a rated exposure, two credit ratings are available and these ratings correspond to two different risk weightings, the highest risk weighting shall be applied to the exposure.
- When, for a rated exposure, more than two credit ratings are available, the two credit ratings that provide the lowest weightings are used. In the event that they do not match, the higher of the two will be applied.

## **7. CREDIT RISK: CREDIT RISK MITIGATION TECHNIQUES**

### **7.1 GENERAL INFORMATION FOR CREDIT RISK**

The Group applies in general terms the credit risk mitigation techniques referred to in the Solvency Regulation (Part 3, Title II, Chapter 4), depending on the guarantees received on the risk positions.

These guarantees may be personal (including credit derivatives) or collateral (including those of a financial nature), being valued for these purposes by the credit enhancement incorporated in the external rating of the guarantor (personal guarantees) or by market parameters in the case of collaterals.

### **7.2. POLICIES AND PROCESSES FOR POSITION NETTING AND VALUATION OF COLLATERAL FOR COUNTERPARTY RISK**

Netting refers to the possibility of offsetting between contracts of the same type under the umbrella of a framework agreement such as ISDA or similar. It consists of offsetting the positive and negative market values of derivative transactions executed with a given counterparty, so that in the event of default, a single flow to be paid or received is generated and not a set of positive or negative values corresponding to each transaction. In this way, and given that one of the components of counterparty risk is the market value, obtaining a net market value of the transactions reduces the risk.

An important aspect of framework contracts is that they involve a single legal obligation encompassing all the transactions covered by them; this makes it possible to offset the risks of all the transactions covered by the framework contract with the same counterparty.

The netting clauses are included independently of the possibility of their direct execution, in order to be able to apply the different applicable laws, so that the inclusion of these agreements does not imply the automatic consideration of netting for the calculation of the exposure to counterparty risk with the different counterparties. These exposures are calculated in accordance with the regulations applicable in each of the jurisdictions involved.

With regard to collateral, the Group enters into collateral agreements for the management of its counterparty risk exposures. These agreements involve a set of instruments, in the form of cash deposits, deposited by one counterparty in favour of another in order to guarantee/reduce the counterparty credit risk that may exist, resulting from the portfolios of transactions with risk existing between them.

The nature of such agreements is diverse and the ultimate objective, as in the netting technique, is to reduce counterparty risk by recovering part or all of the benefits (credit granted to the counterparty) generated at one point in time by the transaction (valued at market prices).

### 7.3. QUANTITATIVE INFORMATION

The following detail shows the distribution of the Group's credit risk exposure as at 31 December 2018, broken down according to whether or not credit risk mitigation techniques have been applied and, where applicable, according to the mitigation technique applied (exposure data refer to exposures prior to the application of risk mitigation):

EXPOSURE VALUE	(Thousands of Euros)
	<b>2018</b>
A) Exposures to which no credit risk mitigation technique is applied	39,737,990
B) Exposures to which a credit risk mitigation technique is applied	164,077
- Netting agreements for balance sheet transactions	-
- Netting framework agreements relating to repurchase agreements, securities or commodities lending or other capital market transactions	-
- Collateral (1)	
- Other collateral (2)	
- Personal guarantees	164,077
- Credit derivatives	-

(1) It includes transactions guaranteed by means of debt securities, shares, collection rights and rights in rem in immovable property admitted by the Solvency Regulation as a technique for reducing credit risk.

(2) It includes cash deposits, certificates of deposit and similar instruments held by third parties other than the Group pledged in favour of Group entities, life insurance policies pledged in favour of Group entities issued by insurance entities recognised as protection providers and by debt securities issued by other institutions not included in number (1) above that would receive a maximum weighting of 50%, which must be repurchased at a predetermined price by the issuing institutions at the request of the security holder.

The exposures to which risk reduction techniques are applied, classified by risk category, are the following:

Risk category	Covered with other collateral	Covered with personal guarantees	TOTAL
<i>Thousands of euros 2018</i>			
Central governments and central banks			
Regional administrations and local authorities			
Public sector entities			
Multilateral Development Banks			
International organisations			
Entities			
Companies		95,786	95,786
Retail exposures		3,708	3,708
High risk exposures			
Covered bonds			
Short-term Exposures Institutions and Companies			
Exposures in default		10,646	10,646
CIUs Exposures			
Equity instruments		53,937	53,937
Other exposures			
<b>TOTAL EXPOSURES</b>	-	<b>164,077</b>	<b>164,077</b>

#### 7.4 EFFECT ON RISK EXPOSURES OF THE APPLICATION OF RISK REDUCTION TECHNIQUES AND EXPOSURES DEDUCTED DIRECTLY FROM OWN FUNDS

Below is a detail of the Group's credit risk exposures as at 31 December 2018 to which the standard method has been applied for their estimation, before and after applying the risk reduction techniques allowed by the Solvency Regulation, broken down by exposure categories and by degrees of credit quality (measured as a function of the percentage applied for the purpose of calculating the value of the risk weighted exposure):

Risk category	Positions before applying risk reduction techniques	<i>(thousands of euros)</i>	
		Positions after applying risk reduction techniques	2018
Central governments and central banks	13,793,809	13,957,886	
Regional administrations and local authorities	1,582,451	1,582,451	
Public sector entities	2,396,957	2,396,957	
Multilateral Development Banks	150,952	150,952	
International organisations			
Entities	15,476,044	15,476,044	
Companies	5,608,889	5,513,103	
Retail exposures	51,036	47,328	
High risk exposures			
Covered bonds			
Short-term exposures to Institutions and Companies			
Exposures in default	75,770	65,124	
CIUs Exposures			
Equity instruments	637,340	583,403	
Other exposures	128,819	128,819	
<b>TOTAL EXPOSURES</b>	<b>39,902,067</b>	<b>39,902,067</b>	

Risk weightings	<i>(thousands of euros)</i>	
	Positions before applying risk reduction techniques	Positions after applying risk reduction techniques
Weighting 0%	14,972,030	15,136,107
Weighting 10%		
Weighting 20%	15,576,012	15,576,012
Weighting 35%		
Weighting 50%	671,032	671,032
Weighting 75%	51,036	47,328
Weighting 100%	8,052,087	7,945,655
Weighting 150%		
Weighting 250%	579,870	525,933
<b>TOTAL EXPOSURES</b>	<b>39,902,067</b>	<b>39,902,067</b>

As at 31 December 2018 there were certain elements deducted directly from own funds. These are significant shareholdings in Financial Sector Entities, for the part that exceeds 10% of eligible own funds, in accordance with the provisions of Section 3 of Chapter 2 of Title I of Regulation EU 575/2013.

## **8. SECURITISATION TRANSACTIONS**

### **8.1 GENERAL INFORMATION ON SECURITISATION ACTIVITY**

As at 31 December 2018 the Institute does not have in its balance sheet securitisation positions (Part 3, Title II, Chapter V of the Solvency Regulation).

### **8.2 EXPOSURES IN SECURITISATION TRANSACTIONS AND AMOUNT OF SECURITISED ASSETS**

As at 31 December 2018, the Group does not hold positions in securitisation transactions to which the Group applies, for the purposes of calculating its own funds requirements for credit risk, the treatment set out in Section Four of Chapter Four of the Circular on Solvency.

## **9. MARKET INFORMATION REQUIREMENTS: INFORMATION ON REMUNERATIONS**

ICO is configured as a Public Business Entity and, consequently, is subject to Royal Decree 451/2012, of 5 March, which regulates the remuneration system for senior managers and directors of the public business sector and other entities. It is also subject to the approval of the CIR Executive Committee (Interministerial Remuneration Committee) regarding the determination of remuneration for personnel not covered by the Entity's agreement. As a result of the foregoing, the remuneration of ICO executives is limited by the aforementioned rules, which prevents the competent bodies from approving different remuneration measures.

Pursuant to the 8th additional provision of Law 10/2014, of 26 June, on the organisation, supervision and solvency of credit institutions, Title I of said Law will not apply to the Instituto de Crédito Oficial, which includes the rules of Corporate Government and the remuneration policy.

**10. INFORMATION ON SHARES AND EQUITY INSTRUMENTS NOT INCLUDED IN THE TRADING PORTFOLIO**

Note 2.1 to the Group's consolidated report for 2018 includes a description of the portfolios in which the Group's investments and equity instruments are classified, together with the accounting policies for recognition and measurement applied to each of them. The Note also indicates the models and assumptions used to determine the value of the instruments included in each portfolio. During the 2018 financial year there were no changes that significantly affect the practices and assumptions used by the Group in the valuation of its investments and equity instruments.

The Group has investments and equity instruments with different objectives. In this sense, it has investments in entities in which it intervenes to a greater or lesser extent in their management and decision-making processes, with which it pursues the attainment of objectives that form part of the strategy and objectives of the Group as a whole and/or in which there is an intention to maintain a permanent relationship with its shareholders ("strategic investments"). It also has investments in other entities with different objectives, basically consisting of maximising the results obtained through their management, in coordination with the Group's risk management objectives and strategies ("portfolios held with a view to sale").

Investments and equity instruments owned by the Group for strategic purposes are generally classified for accounting purposes in the category of Group companies, associates and jointly controlled entities, whereas investments held with a view to sale and which do not form part of the trading portfolio are classified in the category of financial assets at fair value with changes in other comprehensive income.

Annex I to the 2018 consolidated financial statements includes a detailed description of the investments of the ICO Group, with information on the investees, the book value of these investments and their fair value.

Note 9 to the Group's consolidated financial statements for 2018 includes an indication of the types, nature and amounts of exposures in investments and equity instruments measured at fair value with changes in other comprehensive income.

The unrealised gains or losses recognised in equity during the period are included in notes 9 and 21 to the Group's consolidated financial statements for 2018.

Actual gains or losses recognised in income during the year as a result of the sale or settlement of equity instruments not included in the trading portfolio are disclosed in note 29 to the Group's consolidated financial statements for 2018.

## 11. INTEREST RATE RISK. MARKET RISK.

Interest rate risk is the risk to which the Group is exposed in its activity because it has asset and liability transactions with different interest rates (fixed and variable interest rates or referenced to different indices) and with different maturities, so that changes in the reference interest rates of these transactions upwards or downwards may have asymmetrical effects on its assets and liabilities with an effect on the Group's income statement and equity.

Interest rate risk is managed by the Group in an integrated manner for all Group entities with significant positions exposed to this risk. The Group's measurement and analysis of this risk is performed considering the following aspects and in accordance with the following premises:

- Risk measurement and analysis is performed on a permanent basis.
- The effects that variations in interest rates in the different currencies in which significant exposures are held could have on the Group's income and on the various margins in the profit and loss account are analysed.
- The analyses include all positions that are sensitive to interest rate risk, including both implicit and explicit interest rate derivatives.
- As a measure of risk, an analysis is made of the effects/deviations that the intermediation margin and the net asset value can adopt, on the value of the central scenario calculated from the base curve and, by means of value simulation, now calculated from variations on the base curve of +/- 200 b.p. with a floor at 0% in each relevant currency.
- Separate interest rate risk measurements are performed for each of the positions held in each currency, as well as aggregated interest rate measurements for all of them.

On the basis of the foregoing analyses, the Group adopts the necessary measures to guarantee optimum management of this risk.

Note 5.4 of the notes to the Group's financial statements for 2018 includes information on market risk management.

## **12. CAPITAL BUFFERS**

As at 31 December 2018, the Bank of Spain had not made it compulsory for ICO to comply with the requirement to have an anticyclical capital buffer, in accordance with Title VII, Chapter 4, of Directive 36/2013/EU.

Bank of Spain Circular 2/2016, of 2 February, to credit institutions, on supervision and solvency, which completes the adaptation of the Spanish legal system to Directive 2013/36/EU and EU Regulation 575/2013, regulates, in chapter 3, capital buffers as from its entry into force (February 2016). In this sense:

- A common capital buffer of 2.5% is established, which the Institute complies with as at 31 December 2018;
- An anti-cyclical capital buffer is established in accordance with the requirements established for this purpose. For 2018, the quarterly percentage established for this buffer by the Bank of Spain is 0% for credit exposures in Spain;
- The Institute is not subject to the buffers for entities of global systemic importance or for other entities of systemic importance;
- No systemic risk buffer has been established by the Bank of Spain.

### 13. INFORMATION ON UNENCUMBERED ASSETS

Below is information on the Group's unencumbered and encumbered assets as at 31 December 2018 (Recommendation JERS/2012/2):

	Carrying amount of Unencumbered Assets		Fair Value of Unencumbered Assets	
		Of which: issued by other entities in the group	Of which: eligible by central banks	Of which: eligible by central banks
				<b>2018</b>
				<i>Thousands of euros</i>
Assets of the Declarant Entity	36,251,045			
Demand Loans	1,669,474			
Equity instruments	663,670		663,670	
Debt securities	10,533,087		10,533,087	
of which: Covered bonds				
of which: Asset-backed securities				
of which: issued by Public Administrations	8,879,556		8,879,556	
of which: issued by financial corporations	1,623,902		1,623,902	
of which: issued by non-financial corporations	29,629		29,629	
Loans and advances other than demand loans	22,497,970			
of which: mortgage loans	260,987			
Other Assets	886,844			

As at 31 December 2018 there are no encumbered assets.

## 14. INFORMATION ON LEVERAGE

Below is information on the Group's leverage ratio as at 31 December 2018:

Exposure corresponding to the leverage ratio	(Thousands of Euros)
<b>Exposure values</b>	
Derivatives: current replacement cost	795,881
Derivatives: addition using the valuation method at market prices	201,019
Off-balance-sheet items conversion factor 10%	
Off-balance-sheet items conversion factor 20%	
Off-balance-sheet items conversion factor 50%	3,123,061
Off-balance-sheet items conversion factor 100%	473,683
Other assets	36,658,395
Assets deducted from Tier 1 capital (according to the definition to be applied upon completion of the phasing-in process)	-74,906
Assets deducted from Tier 1 capital (according to the transitory definition)	-74,906
TOTAL LEVERAGE RATIO EXPOSURE (according to the definition to be applied upon completion of the phasing-in process)	41,177,133
TOTAL LEVERAGE RATIO EXPOSURE (according to the transitory definition)	41,177,133
<b>Capital</b>	
Tier 1 capital (according to the definition to be applied upon completion of the phasing-in process)	5,179,437
Tier 1 capital (according to the transitory definition)	5,179,437
<b>Leverage ratio</b>	
Leverage ratio (according to the definition to be applied upon completion of the phasing-in process)	12.58%
Leverage ratio (according to the transitory definition)	12.58%

The detail of the exposure values considered is as follows:

	Leverage ratio exposure according to the standard method	Risk-weighted assets: exposure standard method
<b>Exposures treated as exposures to central governments</b>	<b>14,131,856</b>	<b>2,618,349</b>
Central Administrations and Central Banks	11,735,949	257,726
Regional administrations and local authorities treated as central governments		
Multilateral development banks and international organisations treated as central governments		
Public Sector Entities treated as central governments	2,395,907	2,360,623
<b>Exposures to regional governments, multilateral development banks, international organisations and public sector bodies not treated as central governments</b>	<b>1,755,467</b>	<b>42,339</b>
Regional administrations and local authorities NOT treated as central governments	1,628,233	0
Multilateral development banks NOT treated as central governments	127,234	42,339
Public Sector Entities NOT treated as central governments		
<b>Entities</b>	<b>14,362,946</b>	<b>3,074,924</b>
Secured by mortgages on immovable property, of which		
Secured by mortgages on residential property		
<b>Retail exposures</b>	<b>42,440</b>	<b>23,539</b>
Retail exposures to SMEs	38,203	15,397
<b>Companies</b>	<b>4,852,473</b>	<b>4,193,112</b>
Financial		
Non-financial	4,852,473	4,193,112
Exposures to SMEs	1,222,040	1,143,038
Exposures to non-SME companies	3,630,432	3,050,075
<b>Exposures in default</b>	<b>672,810</b>	<b>65,124</b>
<b>Other exposures (e.g. equities and other assets other than credit obligations), of which:</b>	<b>840,403</b>	<b>1,501,110</b>
Securitisation exposures	-	-
<b>Trade finance (memo item), of which:</b>	-	-
In the framework of an official export credit insurance scheme		

The leverage ratio as at 31 December 2018 was 12.58%. Management is informed on a monthly basis of the leverage ratio and its evolution.



PASEO DEL PRADO 4 – 28014

[www.ico.es](http://www.ico.es)