Risk management within CEC BANK S.A., is coordinated by the Risk Management Committee, set up at the Bank Headquarters. Operation and responsibilities of this permanent committee are governed by the Bank’s Rules of Organization and Operation. The Regulation of the Risk Management Committee and its composition are approved by the Board of Directors of the Bank.

The Bank manages the risks associated with the activities that may be performed in accordance with the CEC BANK - S.A. By-laws and with the legislation specific to credit institutions, according to the authorization of the National Bank of Romania, as those activities are performed.

The significant risks that are taken into account are the following: credit risk and counterparty credit risk, residual risk, concentration risk, securitization risk, market risk, interest rate risk arising from non-trading activities, liquidity risk, operational risk and reputational risk.

Risk exposure limit is the maximum capacity of the Bank to undertake on- and off-balance sheet commitments, within a time period, capacity established in conjunction with:

- The existing and projected level of own funds;
- The structure and level of resources and investments, existing and projected to be achieved;
- The estimated profit to be realized.

Risk exposure objectives and limits established by the Significant risk management strategy and Risk profile for 2012 were determined taking into account the Bank's strategic orientations set out in the Income and Expenditure Budget for 2012 and the correlation of the general objectives foreseen, with the economic and financial market and business environment developments.

In accordance with its mission, the Bank's objectives for 2012 were the following:

- leading provider of banking services for SMEs, agriculture and local government;
- main partner to co-finance the beneficiaries of EU funded projects; in this regard, has developed new dedicated products and services;
- substantially improved banking services provider;
- consolidation of achievements from the previous years, both in the segment of products and services offer as well as of the staff training or technical platform;
- increased product quality and customer service;
- adapting the commercial offer to the economic conditions of 2012, including new solutions for debt restructuring, not ignoring the concern for improved risk management;
- identification of new ways to support the customers facing problems caused by the economic crisis;
- continued funding from its own resources, designed primarily to support and develop the SMEs, agriculture and local government, as well as the bankable projects, which by their nature, contribute to the economic development, job creation and maintenance;
- further involvement in the Romanian development programs;
- maintaining CEC Bank in the top 5 banks in the Romanian banking system;
the keywords in terms of branch network development strategy have been and will remain "efficiency and competitiveness";
- maintaining the bank prudential indicators within the limits imposed by the NBR.

The Significant risk management strategy and Risk profile are reviewed annually or whenever necessary, depending on the evolution of the Bank's prudential indicators, in the context of the financial and banking market development, to achieve the strategic objectives of the Bank.

**Credit Risk Management Strategy**

Bank’s financial stability is directly influenced by the approach of the risk management. Since lending has an important share in the activity of the Bank, the effective credit risk management generates positive effects for both the Bank and for its customers. For the Bank, the positive effects are a decreased level of bad debt losses, optimized revenue and expenses projected when preparing the budget of revenues and expenses, and reduced volatility of the financial results. For customers, the positive effects consist in optimized prices, increased quality and level of diversification of services and their efficient provision, increased degree of protection of the customers’ interests. For this purpose, by the risk profile, the Bank has set limits on the exposure concentration by type of exposure, sectors, categories of customers, geographical areas, currency, loan maturity, estimated profitability of the portfolio, in order to promote certain categories of loans.

Credit risk strategy established the following:

- general requirements for the development of policies and procedures on lending, through the credit risk approach, considering the acceptable ratio between risk and profit, while ensuring sound and prudent business continuity;
- the lines to follow in implementing the chosen risk profile through credit policies and procedures and credit risk management.

Policies and procedures on lending subject to revisions, take into account the following:

- Rigorous procedures of credit application analysis and customer acceptance;
- Adequate scoring system;
- Adequate exposure approval system;
- Establishing an adequate system of signatures for granting and using the loans;
- Adequate protection of exposures;
- Adequate loan tracking system;
- A system establishing the loan approval powers depending on the quality of the loan portfolio and lending performances;
- Management system of limits on the credit risk concentration level, both at the customer level and at credit portfolio level or collateral issuer.

The Bank is not financing:

- operations is violation or breach of legal regulations;
- transactions and customers for which there are well-founded suspicions that obtain material benefits from crimes committed by themselves or within their areas of interest;
- gambling and casinos;
- political organizations and election campaigns;
- activities on the EBRD list, regarding the inconsistency with the regulations relating to environmental protection, including:
  - production or activities involving forms of exploitation, forced or hazardous labour or hazardous labour for minors, discriminatory practices or practices that prevent the
employees to exercise their rights of association and collective bargaining, under the law;
- manufacture, use or sale of asbestos fibres and products containing asbestos;
- activities prohibited by the laws of Romania and international conventions on the protection of resources biodiversity and cultural traditions;
- production or sale of products containing polychlorinated biphenyls;
- production or sale of pesticides, herbicides, pharmaceuticals and other dangerous substances, which are subject to international restrictions, withdrawn from production or prohibited;
- production or distribution of substances that destroy the ozone layer and are subject to international restrictions;
- trade in wild animals and plants regulated by the CITES Convention (Convention on International Trade in Endangered Species)
- sea fishing with floating nets using nets with a length of more than 2.5 km;
- transport of oil by oil tanks, without IMO certification;
- trade in goods without import or export licenses or transit authorizations from the export, import, and transit countries, respectively.

In the process of activities permitted by the Bank's By-laws and credit institutions specific legislation, having as counterparties entities within the credit institutions sector and outside it, activities that generate credit risk and counterparty credit risk, in order to comply with the profile risk undertaken, the Bank took into account the following:

- credit risk management at individual level for customers, individuals and legal entities;
- credit risk management within the Bank, through the quality of the loan portfolio and financial instruments, including derivatives.

**Credit risk management at individual level for customers, individuals and legal entities**

Risk assessment for loans granted within the Bank is done in two steps, both before committing the Bank in performing the operations, and after the approval of operations and is based mainly on:

- not registering exposures to the counterparties which, according to the internal regulations, are considered non-eligible counterparties with high risk, based on the information obtained from the databases of CRC, CIP, Credit bureau, internal databases and / or from insurance companies;
- non-placement of high-yield investments along with a high risk;
- assessing the counterparty and the guarantees given, falling within the eligibility criteria established;
- falling within the maximum exposure level to a group of connected clients;
- exposures approval by decision makers according to predetermined levels of competence;
- monitoring of all counterparties during the loan agreements;
- daily monitoring of the service debt (the number of days of arrears) of the counterparties involved in the lending process;
- monthly assessment of the exposure risk by recording each item from and off the balance sheet assets representing exposure in a classification category, according to the service debt, financial performance categories of the counterparties and the related guarantees, according to the criteria established by the National Bank Romania and with the internal regulations;
- monthly assessment of exposure impairment and determination of impairment adjustments required - on an individual basis for individually significant exposures and on collective basis for those individually insignificant;
- assessment of collaterals accepted in lending, following the principles set out in the internal regulations regarding the determination of fair value of the collateral.
Credit risk management in the Bank, through the quality of the loan portfolio and financial instruments, including derivatives

Risk profile of the Bank's loan portfolio is a distribution process on four levels of credit risk (low, moderate, medium, high).

Besides the risk profile of counterparties that is accepted along with entering into contracts with them, considering the dynamics of the loan portfolio, the Bank also establishes an accepted risk profile of the loan portfolio.

According to the Bank's Business Strategy, was aimed to establish a banking book portfolio by predominant registration of exposures (lending and issuance of guarantees) to the counterparties represented by small and medium enterprises (SMEs), local government and individuals.

Credit risk management in the loan portfolio took into account the risk assessment portfolio of the loan portfolio and financial instruments, including derivatives, and the compliance with the limits for credit risk exposure, including:

a) ceilings and exposure limits to the Romanian and foreign banks, registered in and off the balance sheet;
b) exposure limits to guarantee funds and insurance companies;
c) limits on concentration risk arising from transactions with non-bank customers recorded in and off the balance sheet:
   c1) by categories of clients: individuals and legal entities;
   c2) by geographical areas;
   c3) by currency;
   c4) by product category;
   c5) by category of credit risk;
   c6) by lending period;
   c7) by credit risk levels;
   c8) by sector.
   c9) against the collateral issuers.

The risk profile of the loan portfolio is determined calculating the weight of loans classified in four risk categories (low, moderate, medium and high) in the total loans.

The purpose of introducing the assessment system of the loan portfolio risk profile is to differentiate the levels of risk in the loan portfolio of the Bank to:

- avoid loan portfolio concentration in the high risk profile;
- determine the portfolio quality trends so as to respond appropriately and prevent damaging in time of this quality;
- ensure the credit risk management and adequate protection of the Bank against this risk.

Observing the chosen risk profile is considering including the estimated level of profitability so that the Bank business can be performed respecting the banking prudential indicators.

Taking into account:
- the overall economic situation;
- the adverse perspectives on the economic growth and unemployment;
- the increased cost of credit;
- the currency depreciation;
- the impairment of collateral value,
the Bank shall conduct monthly / quarterly profit forecast scenarios and impact assessment in case of materialization of credit risk on capital requirements in crisis situations, the Risk Management Committee being informed and proposing measures to remedy the situation, including a review of the credit policy.

In terms of residual risk, no relevant issues have been met during 2012.
**Market risk**

In accordance with the NBR Regulation no.18/2009 regarding the administrative framework of credit institutions’ activity, the internal evaluation process for adjusting the capital to risks and the requirements for outsourcing their activities, as amended and supplemented:

- Market risk is the current or future risk of adverse effects on profits caused by market fluctuations of securities’ prices and interest rate, in terms of activities falling within the trading portfolio and fluctuations in currency exchange rates and commodity prices for the entire activity of the Bank;
- Interest rate risk is the current or future risk of adverse effects on profits and capital as a result of adverse changes in interest rates.

**I. Market Risk Management Strategy**

Risk strategy (in terms of market risk) has considered mainly the major components of the market risk, namely:

- risk of interest rate changes;
- currency risk.

The factors affecting mainly the emergence and development of the interest rate changes risk may be:

a) **endogenous factors** (important for the risk management, action on them generating risk exposure minimization): the Bank's strategy, the structure of bank assets and liabilities, the volume and value of loans, loan portfolio quality, loan rescheduling maturities, maturity of funds collected;

b) **exogenous factors** (stemming from the general economic conditions development): economic environment, the type of economic, monetary, financial and currency policy practiced by the authorities, correlation of the monetary policy of the central authority with the government economic policy, interbank market evolution, psychological factors.

The Bank has proposed an adequate management of lending and deposit rates combined with actions to promote active and passive products, to achieve both an increased workload and ensuring an optimal interest rate gap, and a balanced level of the adjusted individual foreign currency positions and of the overall foreign currency position.

The market risk strategy aimed at achieving a portfolio with low sensitivity to changes in interest rate and exchange rate, and achieving the targets set in the risk profile. These targets were achieved by managing the interest margin, the calculation and analysis of the interest rate risk indicators, the Bank's foreign currency position management and currency risk indicators’ analysis.

Through the interest rate risk strategy, the Bank intended to decrease the gap between assets and liabilities sensitive to interest rate changes, both totally and by time horizons, so that the impact of the interest rate changes on the net interest income to be as low as possible.

The Bank developed alternative and contingency plans, if necessary (depending on the intensity of possible events), establishing mainly:

- responsibility of the governing bodies of the Bank;
- procedures to be taken to enable these plans;
- identification of post crisis solutions.

**II. Market risk profile**

The Bank aimed to fall within a low market risk and within the significant risk limits set by the internal regulations and by the NBR limits. In managing the market risk were considered the following:

- identification of potential risk-generating situations;
- monitoring, assessment / analysis of risk exposures;
- reporting risk exposures;
• risk reduction measures;
• tests to assess the impact of various determinants of risk modification;
• scenarios / tests systems for the crisis (stress testing) and procedures to be applied in such cases;
• internal control systems.

II.1. Interest rate risk management

The interest rate risk management was done by the establishment of sensitivity factors to the interest rate changes (G.A.P. ratio) involving the identification of assets / liabilities within and off the balance sheet, sensitive and non-sensitive to interest rate changes, totally and by time horizons.

By the G.A.P. monitoring, the Bank intended to decrease the gap between assets and liabilities sensitive to interest rate changes, totally and by time horizons, so the impact of interest rate changes on the net interest income to be as low as possible.

In order to prevent crisis situations, the Bank has developed scenarios, including "stress testing" scenarios. The simulations were based on the balances of assets and liabilities sensitive to interest rate changes and average interest and were achieved by scenarios involving changes in the Bank's activities in conjunction with upwards and / or downwards changes in the interest rate.

The Bank also tested through simulations, the impact of shocks on the yield curve, resulting from upwards and / or downwards changes in the interest rate, either by constant change or by their differentiated increase / decrease, according to the operating mode specified in the risk management policy.

According to the NBR Order no. 6/2010 on reporting the potential changes in the economic value of credit institutions as a result of changing the interest rate, by applying the standardized calculation methodology provided by the NBR Regulation no. 18/2009, the Bank determined the potential change of the economic value by applying a standard shock, set by the NBR, respectively the alleged change in yield by 200 basis points - for each currency above 5% of its assets and liabilities sensitive to the interest rate (ie RON and EUR) and cumulative for the other currencies.

II.2. Currency Risk Management

Currency risk management has been achieved:
1. by determining the following indicators:
   a) Net open position in each currency (excluding the reporting currency) and in gold;
   b) Total net position;

on which base, the maximum levels of net open positions and the total net position in all own funds were monitored and restricted.

In accordance with the NBR Regulation no. 22/2006 on the capital adequacy of credit institutions and investment firms, the Bank quantified the currency risk undertaken in order to determine the capital requirement for its coverage by:

• determining the net open position of the Bank in each currency portfolio;
• determining the net long and short positions in each currency, other than the reporting currency,

If the total net foreign exchange position exceeded 2% of total own funds, the Bank calculated the own funds requirement to cover the currency risk by multiplying it by 8%.

The Bank conducted quarterly tests regarding the impact of the maximum appreciation / depreciation of the exchange rate on the assets and liabilities in foreign currency, by developing simulations having as premises an exchange rate determined by the 12-month history. Moreover, the potential impact of disturbing factors was assessed monthly using the "stress testing".

To measure the risk of the Bank’s foreign currency portfolio, the VaR (Value at Risk) methodology was used, in order to determine daily the maximum loss expected.
Liquidity risk

Liquidity risk expresses the present or future risk of adverse effects on profits and capital caused by the inability of the Bank to meet its obligations at maturity; liquidity risk lies in the inability of the Bank to meet its payment obligations in the short term without incurring costs or losses that may not be borne by the Bank.

Liquidity risk refers to:
- a) inability of the Bank to fund the assets portfolio on the appropriate maturity dates;
- b) inability of the Bank to liquidate the position at the appropriate time and at a reasonable price.

I. Liquidity Risk Management Strategy

The liquidity risk strategy aimed at achieving the objectives of the risk profile, mainly:

- monitoring the compliance with the significant limits of the liquidity risk management ratios, including early warning indicators;
- achieving a liquidity indicator with values above 1, on RON equivalent (by maturity intervals) to comply with the NBR regulations by monitoring it daily;
- monthly monitoring of the liquidity indicator, analyzing its evolution, the causes that can lead / have led to a deterioration of the indicator and any action proposed;
- monthly monitoring of the liquidity GAP (independent of the liquidity calculation provided by the NBR regulations in force), the analysis of its evolution;
- monthly monitoring of the high risk of liquidity and of the groups of connected clients conducting passive transactions with the Bank.

Moreover, in accordance with the provisions of the NBR Regulation No. 25/2011 on the liquidity of credit institutions (art. 37), as amended and supplemented, and the NBR Regulation No. 18/2009 regarding the administrative framework of credit institutions' activity, the internal evaluation process for adjusting the capital to risks and the requirements for outsourcing their activities, as amended and supplemented, "CEC BANK S.A. Strategy in the liquidity risk management and solutions to overcome crisis situations - financial year 2012" was developed, submitted to the National Bank of Romania.

Given that the crisis situations are determined by factors both endogenous and exogenous to the Bank, they were prevented by measures of permanent monitoring of the liquidity, along with measures to prevent a possible liquidity crisis.

The main objectives of the Bank's strategy focused on liquidity risk management, were:
- a) prevention of crisis situations;

The methods to prevent crisis situations were related to liquidity risk management by:
- defining the liquidity risk profile on a limited time horizon and compliance of the liquidity indicators monitored with the risk level accepted under the NBR regulations and the internal regulations.

- b) development / adoption of alternative plans of action and identification of solutions to overcome / address possible liquidity crisis periods of the Bank;

By the alternative plans for managing liquidity risk during crisis, the Bank has undertaken to maintain the short and medium term liquidity at optimum levels, correlated with its risk strategy, so that it can provide the prudent asset growth and honour its obligations without increased costs that may not be borne by the Bank. The main objective of the Bank in the event of a liquidity crisis is the fulfilment of its commitments in optimal conditions of cost / benefit and ensuring the minimum mandatory reserve.

- c) identification of post-crisis solutions;
In accordance with the NBR Regulation no. 18/2009 regarding the administrative framework of credit institutions’ activity, the internal evaluation process for adjusting the capital to risks and the requirements for outsourcing their activities, as amended and supplemented, the Bank has developed (in the event of a liquidity crisis), a set of guidelines regarding the identification of post-crisis solutions and measures was established, which refers mainly to:

- determine the causes that led to the liquidity crisis;
- analysis of the Bank’s liquidity crisis and obtaining conclusions that lead to improved information / computer, control and risk management systems;
- establishment of new measures to monitor the Bank’s liquidities, depending on the causes of the liquidity crisis.

In the event of a liquidity crisis, the Liquidity Crisis Management Committee provides the Bank’s management, overcoming and minimizing the negative consequences.

II. Liquidity risk profile

In what concerns the liquidity risk, the Bank pursued to fall within a medium risk profile, taking into account the optimal parameters for the Bank.

In order to measure the liquidity risk accepted, liquidity was managed according to:

- CEC BANK S. A. Strategy on liquidity management and solutions for overcoming the crisis - financial year 2012 (which aimed and ensuring the capability of the Bank to meet its obligations under adverse conditions);
- Internal Regulations on management of significant risks within the Bank (developed under the NBR Regulation No. 18/2009 regarding the administrative framework of credit institutions’ activity, the internal evaluation process for adjusting the capital to risks and the requirements for outsourcing their activities, as amended and supplemented and NBR Regulation no. 25/2011 on the liquidity of credit institutions).

Through the risk profile, the Bank monitored:

- monthly liquidity indicator (based on the calculation provided by the NBR Regulation no. 25/2011 on the liquidity of credit institutions) as determined and / or foreseen in static and dynamic meaning;
- daily liquidity indicator;
- high liquidity risk;
- liquidity profile by the GAP analysis (GAP, cumulated GAP and short term current liquidity ratio);
- early warning indicators to identify immediately an increased vulnerability regarding the liquidity position or the financing needs;
- immediate liquidity indicator and the share of non-pledged government securities in the unadjusted balance liabilities;
- liquid assets weight (various levels of liquidity) in the total unadjusted balance liabilities;
- monthly weighted operations denominated in euro in total operations performed in RON equivalent, etc.;
- liquidity reserve, aimed to cover the liquidity risk in unforeseen circumstances, from the liquidity reserve available immediately.

In order to prevent the crisis situations, monthly forecasts were developed on different timelines, on which base assumptions were made about the future direction of the liquidity / liquidity ratio trend.

In terms of liquidity, throughout the year 2012, the Bank was within the limits imposed by the NBR.
In addition, has developed resistance tests of various intensities and on different holding periods, in order to assess the hypothetical losses incurred in the event of unexpected liquidation of funding sources, consisting of deposits, to provide the liquidity needs.

**Operational Risk**

The operational risk is the risk of loss caused either by the use of processes, systems and human resources inadequate or that have not functioned properly, or external events and actions. The operational risk includes the legal risk.

The Bank followed the establishment of an operational risk management framework, covering the operational risk appetite and tolerance, through policies and processes for identifying, assessing, monitoring, reporting, control and mitigation of the operational risk.

**Operational Risk Management Strategy**

Risk management strategy established general requirements for the development of the internal policy and procedures of the Bank, in terms of significant risk approach, considering framing within the risk profile and the acceptable ratio between profit and risk, while ensuring the sound and prudent business continuity.

The operational risk management has considered these events generating operational risk:
- internal fraud;
- external fraud;
- employment and workplace safety practices;
- customers, products and business practices;
- damage to physical assets;
- business disruption and system failures;
- process execution, delivery and management.

CEC BANK - S.A. Strategy for the year 2012 has proposed to monitor and control the operational risk at all levels and in all activities performed, starting from the creation or promotion of a product, service or activity, to fit into a moderate risk class.

The strategic objective of the Bank in terms of operational risk management aimed mainly the following:
- assessment of products and services, activities, processes and systems in order to determine the inherent operational risk;
- implementation of new operational risk indicators, their analysis and monitoring to fall within the set limits;
- updating the thresholds for the operational risk indicators, thresholds used for both monitoring and control of the operational risk faced by the Bank;
- implementation of operational risk indicators that are:
  - **specific**: the operational risk indicators are determined according to the fields, processes, systems and products of the Bank;
  - **measurable**: the operational risk indicators are objectively quantifiable and can be easily verified;
  - **relevant**: being sensitive to risk, operational risk indicators are even more relevant as signal in time the losses that may occur;
  - **with clearly defined alert limits**: the values of the operational risk indicators are kept under observation by certain thresholds used for both monitoring and control.
- establishment of risk control measures to significantly decrease the losses due to the operational risk, namely losses due to inadequate internal processes, human errors and errors of various automated systems, and those due to external factors;
- internal control improvement through continuous adaptation of the internal regulatory framework and internal processes so as to ensure their compliance with the requirements of the National Bank of Romania;
- increased training programs and organizing courses for the professional development of the employees in order to reduce the operational risk;
- operational risk level monitoring in relation to the operational risk profile for more rapid detection of the optimal risk control and mitigation measures;
- assessment of the operational risk exposure using the database on the history of Bank’s losses;
- inclusion in the internal regulations, according to the regulation field, of provisions relating to workflow and documents, clear responsibilities of the personnel involved in carrying out these regulations and the control method thereof;
- monitoring the legal risk, component of the operational risk that arises from the failure to apply or faulty application of laws or contractual provisions, adversely affecting the Bank's operations;
- decisions on:
  - undertaking / accepting certain risks;
  - intensification of control measures to prevent and decrease the operational risk;
  - operational risk transfer (through outsourcing or taking insurance policies);
- periodic review of business continuity plans, in case of its termination due to possible crisis situations, considering the principle of business continuity and minimizing the losses;
- establishment of crisis scenarios, based on historical or hypothetical scenarios, depending on various parameters.

The operational risk strategy aimed to minimize the events generating operational risk, both of the internal and external fraud, and improper processing of data about customers and treatment of customers and commercial counterparties, malfunctions of computer systems.

**Operational risk profile**

The operational risk profile was determined based on two factors:
- probability (low, medium or high) of the operational risk and the total loss expected (estimated) from the operational risk;
- impact (low, moderate, high or medium) of the operational risk on the capital requirement for operational risk, or on the gross income from the banking activity.

CEC BANK-S.A. had in 2012 a low operational risk profile.

The Bank assessed quarterly, based on crisis scenarios, the impact of the operational risk on profitability and capital requirements.

**Reputational risk**

Reputational risk is the current or future risk of adversely affecting the profits and capital caused by unfavourable perception of the image of a bank by customers, counterparties, shareholders, investors and supervisors.
Reputational Risk Management Strategy

The main strategic objectives of the Bank for 2012 aimed at:

- strengthening the position of the oldest bank in Romania as universal commercial bank, competitive, provide the customers with diverse and qualitative products and services;
- promoting the credit for the purchase of land for agricultural production and its rehabilitation in view of farming, credit launched in Nov.2011;
- continuing to offer real estate credit by engaging in the "First House" project and granting loans for thermal rehabilitation;
- promoting new passive products: deposits on 2 or 3 years, unit linked insurance with capital and guaranteed growth (the sources are kept within the bank for a period between 3 and 7 years), PF products package, other types of insurance;
- actively promoting new products: implementation of the loan for studies / medical purpose, fast credit for legal entities, multi-product and multicurrency ceiling for legal entities;
- continuing to access European funds through the “European Funds Bureaus” and supporting the customers in accessing European funds for SMEs and human resources development, environmental protection, development of transport networks and rural development;
- consolidation of the Bank on the banking market by increased volume and complexity of the transactions executed;
- staff behaviour change both within the institution and to customers, and ensuring the highest level of professional training of the staff;
- strengthening the Bank's image on the financial and banking market.

In order to decrease the reputational risk, the Bank has considered the permanent update of the internal regulations on standards and actions to follow in the KYC activities, to prevent money laundering and terrorism financing, to resolve complaints and claims made by some Bank customers.

Reputational risk profile

The reputational risk is directly related to the operational risk, with some common solutions to limit it. Once lost, the image restores hard and the prestige loss can have serious consequences in the activity of a bank.

In 2012, the Bank aimed at a low reputational risk level that does not result in failure to obtain or loss of profits estimated by the Bank. In this regard, the Bank has proposed to prevent and limit the events generating the reputational risk by:

- adapting internal regulations to promote banking products with a positive impact on the market;
- introduction of modern banking products, efficient and in line with the continuously growing requirements of the banking market, crossed by the financial crisis;
- promoting banking products in the media, through all forms of advertising, after becoming operational, or specifying the time when they become operational;
- further development of alternative business continuity plans to ensure the conditions necessary to be implemented urgently in other location than the Bank Headquarters;
- introduction of technologies for processing and security of information.

Risks arising from outsourcing activities

Outsourcing of an activity means use by the bank of an external supplier, in order to carry out, on a contractual basis and continuously, activities that would normally be conducted by the Bank.
The external provider is the provider of goods and services, which may be an entity authorized or not, that is, a related party in a group or outside the group.

The Bank accepts and chain outsourcing, subcontracting being permitted only with the prior approval of the Bank and under the same conditions as those applied to the main external supplier.

In its activities, the Bank may outsource both significant and insignificant activities.

**Strategy for managing the risks of the outsourced activities**

Bank’s strategy on the management of risks of outsourcing is based on the Bank’s policy regarding outsourcing the Bank’s activities and is applied through the internal regulations on the procedure for outsourcing and managing the related risks, according to the NBR.

In reaching its objectives and goals, the Bank has identified (and implemented where applicable) organizational changes that led to improved efficiency, and took into account the possibility of outsourcing activities in cases where outsourcing has led to increased efficiency of the Bank, without prejudice to its main objectives, in accordance with the policy on outsourcing activities within the Bank.

The reasons that have led to the outsourcing of certain activities of the Bank include:
- reduced operational costs and investment efforts of the Bank, while maintaining the control of the risks involved;
- absence of internal resources necessary for the activity in question, or the high response time, in case of adjustment of the existing structure for this purpose;
- reallocation of internal resources for other priority activities, in order to obtain a high efficiency of these resources;
- access to advanced technology and specialized quality services, provided by vendors with experience;
- conducting that activity for a limited period, which does not justify making investments;
- reduction of specific risks or their better control;
- improved processes and their better control, given the large volume of transactions involved the activity for which outsourcing is considered, etc.

The Bank approached rigorously the outsourcing of some activities on the basis of specific internal regulations.

**Outsourcing risk the profile**

In order to manage the significant risks posed by outsourcing, the Bank had regulated outsourcing procedures, including methods for the selection and assessment of external providers of goods and services, monitoring procedures of how the external providers of goods and services carried out the activities outsourced, alternative plans and costs and resources needed to change the supplier.

The Bank constantly ensured that the outsourcing plans have not decreased its ability to meet the obligations to clients and regulatory authorities and have not prevented the regulatory bodies to conduct their supervision.

The Bank is outsourcing activities only under a contract, in writing, with the external suppliers of goods and services, which clearly state all the material aspects of the outsourcing plan, including the rights, responsibilities and expectations of all parties.

The outsourcing of activities of the Bank consider the analysis, management and monitoring of risks generated, not limited to the reputational risk, legal risk, operational risk, country risk, concentration risk, etc.

When outsourcing an activity, the Bank assesses the risks to which it is exposed and seeks framing the outsourced business risks in a low risk level.

Regarding **bank’s own funds**, they include the following:
<table>
<thead>
<tr>
<th>Item Name</th>
<th>Value on 31.12.2012 M RON</th>
<th>Information on the nature of the item</th>
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</thead>
<tbody>
<tr>
<td>Own funds - Tier I</td>
<td>1,346.38</td>
<td>This item includes:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>a) subscribed and paid capital - the Romanian State is the sole shareholder, represented by the Ministry of Public Finance (positive component): RON 1,301.01 million, out of which RON 209.08 million represents the capital adjustment with inflation indices under IAS 29.</td>
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<tr>
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<td>b) Total reserves (positive component): RON 192.38 million total, out of which:</td>
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<tr>
<td></td>
<td></td>
<td>- Legal reserve* (positive component): RON 90.19 million;</td>
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<td></td>
<td>- Reserve for general banking risks* (positive component): RON 57.56 million;</td>
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<td>- Audited profit that was decreased by the amount of the legal reserve (positive component): RON 32.11 million;</td>
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<td></td>
<td></td>
<td>- Other reserves established in the previous years (positive component): RON 121.90 million;</td>
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<td></td>
<td></td>
<td>- Carryforward earnings resulting from the application of IAS 29 for the first time (positive component): RON 0.67 million;</td>
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<tr>
<td></td>
<td></td>
<td>- Carryforward earnings resulting from the application of IAS 29 for the first time - adjustment with the inflation indexes of the social capital (negative component): RON 209.08 million;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Carryforward earnings obtained from the correction of accounting errors (positive component): RON 0.41 million;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Earnings obtained from the revaluation reserve surplus (positive component): RON 18.78 mil;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Carryforward earnings arising from the implementation of IFRS as accounting basis - representing specific provisions* - (positive component): RON 95.28 million;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Assessment differences eligible as own funds of Tier 1 represents exchange differences relating to non-monetary financial assets, differences in fair value changes of the financial assets available for sale and deferred tax for AFS and equity instruments (negative component): RON 15.43 million;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>c) intangible assets** (deduction): RON 16.15 million.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>d) prudential filters* (deduction): RON 130.85 million.</td>
</tr>
<tr>
<td>Own funds - Tier II</td>
<td>322.76</td>
<td>This item includes:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- Reserves from the revaluation of land and buildings owned * (positive component): RON 453.61 million;</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- prudential filters* (deduction): RON 130.85 million.</td>
</tr>
<tr>
<td>Total own funds</td>
<td>1,669.14</td>
<td>-</td>
</tr>
</tbody>
</table>

* These items are presented at their net value, decreased with the related tax calculated in accordance with the regulations in force.
** This item is shown at its net value decreased with the corresponding depreciation calculated according to the regulations in force.
Capital adequacy to risks

The current methodology for determining capital requirements of the Bank, issued in accordance with the NBR regulations, provides a minimum rate of 8% for the capital adequacy to risks for which there is the need of regulatory capital (credit risk, currency risk and operational risk) and risks for which the regulatory capital requirements are not fully covered (risks resulting from the application of less sophisticated approaches for credit risk and operational risk, residual risk related to the credit risk mitigation techniques, risks such as interest rate risk for non-trading activities, concentration risk, reputational risk and the strategic risks, external risks and risks related to the economic regulatory environment or to the Bank operation).

According to the risk management strategy, capital adequacy to risks and the risk profile for 2012, reaching a level of 10% for the capital adequacy ratio, is a warning signal for action, so it does not register an erosion of capital and decreased adequacy ratio below 8%, considering both the risks for which regulatory capital is necessary and risks for which the regulatory capital requirements are not fully comprehensive. Upon reaching the 10% threshold, will be taken steps to remedy the situation by a policy stimulating the investment with lower degrees of risk depending on the counterparty or the security for debts, eliminating or reducing the factors that generate the need for non-regulatory capital requirements and assessment of capital increase possibilities.

On 31.12.2012, the capital adequacy ratio of the risks for which there are regulatory capital requirements was 15.90%.

The internal assessment of capital adequacy was made based on G.E.O. No.99/2006 on credit institutions and capital adequacy, as amended and supplemented, the NBR Regulation No.18/2009 regarding the administrative framework of credit institutions’ activity, the internal evaluation process for adjusting the capital to risks and the requirements for outsourcing their activities, as amended and supplemented, other NBR regulations on capital adequacy to risk within credit institutions and reporting requirements.

The internal assessment process of capital adequacy was formalized during 2012 in the Bank's internal regulations, on the establishment of the Bank's minimum capital requirements to cover the credit risk, currency risk, operational risk and risks for which there are no regulatory capital requirements and in the principles established by the Risk management strategy of capital adequacy to risks and risk profile for the year 2012.

In accordance with the NBR Regulation no.18/2009 regarding the administrative framework of credit institutions’ activity, the internal evaluation process for adjusting the capital to risks and the requirements for outsourcing their activities, as amended and supplemented, the internal assessment of capital adequacy to risks follows:

- Covering the risks for which there are NBR regulatory capital requirements under NBR / NSC Regulation no.13/18/2006 on determining the minimum capital requirements for credit institutions and investment firms (credit risk, currency risk and operational risk);
- Covering the risks for which the regulatory capital requirements are not fully covered, ie.: risks resulting from the application of less sophisticated approaches - underestimating the credit risk (in the context of using the standard approach) and the operational risk (in the context of using the basic approach), residual risk related to the techniques for credit risk mitigation, securitization risk and other risks.

Establishment of the minimum capital requirements to cover the risks

Establishment of the Bank's minimum capital requirements for the credit risk is performed in accordance with the NBR-NSC Regulation no.14/19/2006 on credit risk for credit institutions and investment firms under the standardized approach, as amended and supplemented, respecting and the NBR-NSC Regulation no.13/18/2006 on determining the minimum capital requirements for credit institutions and investment firms, as amended and supplemented.
Minimum capital requirements for credit risk under the standardized approach on 31.12.2012, was RON 685.06 million.

Allocation of capital requirements by exposure classes is as follows:

<table>
<thead>
<tr>
<th>Exposure class pursuant to Article 4 of the NBR-NSC Regulation no.14/19/2006 on credit risk for credit institutions and investment firms standard approach, as amended and supplemented</th>
<th>- RON million- 8% of the risk weighted exposure</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) debts or contingent debts of central governments or central banks;</td>
<td>3.74</td>
</tr>
<tr>
<td>b) debts or contingent debts of regional governments or local authorities;</td>
<td>20.67</td>
</tr>
<tr>
<td>c) debts or contingent debts of administrative bodies and non-profit entities;</td>
<td>0.00</td>
</tr>
<tr>
<td>d) debts or contingent debts of multilateral development banks;</td>
<td>0.00</td>
</tr>
<tr>
<td>e) debts or contingent debts of international organizations;</td>
<td>0.00</td>
</tr>
<tr>
<td>f) debts or contingent debts of institutions and financial institutions;</td>
<td>0.31</td>
</tr>
<tr>
<td>g) debts or contingent debts of companies;</td>
<td>170.53</td>
</tr>
<tr>
<td>h) retail debts or contingent debts;</td>
<td>207.04</td>
</tr>
<tr>
<td>i) debts or contingent debts secured by real estate;</td>
<td>144.45</td>
</tr>
<tr>
<td>j) remaining items;</td>
<td>37.36</td>
</tr>
<tr>
<td>k) items belonging to high-risk categories;</td>
<td>0.00</td>
</tr>
<tr>
<td>l) exposures in the form of covered bonds;</td>
<td>0.00</td>
</tr>
<tr>
<td>m) securitization positions;</td>
<td>-</td>
</tr>
<tr>
<td>n) short-term debt of institutions and companies;</td>
<td>0.00</td>
</tr>
<tr>
<td>a) claims in the form of shares held in collective investment undertakings;</td>
<td>0.00</td>
</tr>
<tr>
<td>p) other items.</td>
<td>100.96</td>
</tr>
</tbody>
</table>

Establishment of the minimum capital requirements for position risk, foreign currency risk, commodity risk and operational risk

Establishment of the minimum Bank’s capital requirements for foreign exchange risk is carried out in accordance with the NBR-NSC Regulation no.22/27/2006 on capital adequacy of credit institutions and investment firms and with the NBR-NSC Regulation no.13/18/2006 on determining the minimum capital requirements for credit institutions and investment firms, as amended and supplemented.

Quarterly, the Bank calculates the capital requirements for foreign exchange and since it was not exposed to such risks, did not calculate capital requirements for position risk and commodity risk.

In addition, to cover the operational risk, the Bank has determined a need for capital in the amount of RON 154.68 million, calculated according to the basic indicator approach provided in the NBR / NSC Regulation No. 24/29/2006 on setting the minimum capital requirements of credit institutions and investment firms for the operational risk.

In the process of quantifying the Bank's exposure to the credit risk and debt decrease risk, for accounting purposes, the following definitions are used:

Non-impaired outstanding exposures - balance sheet exposures that record debts not collected at maturities and for which no indicators of impairment were identified.

Impaired exposures - balance and off-balance exposures for which there are impairment indicators (objective indicators of impairment of a loan or group of loans, including observable information acknowledged by the Bank), established internally in accordance with International Financial Reporting Standards (IAS 39).

Impairment adjustments for loans / investments - impairment adjustments determined according to the International Financial Reporting Standards - IAS 39 and recorded in the accountancy.
In determining the depreciation of assets, the methods outlined by legislation were applied (linear method).

The total amount of exposures and their mean value, after the balance sheet off-setting and before applying the credit risk mitigation techniques, broken down by exposure classes, on 31.12.2012 show the following structure:

<table>
<thead>
<tr>
<th>Exposure class pursuant to Article 4 of the NBR-NSC Regulation no.14/19/2006 on credit risk for credit institutions and investment firms standardized approach</th>
<th>Total exposures</th>
<th>Mean exposures for the period</th>
</tr>
</thead>
<tbody>
<tr>
<td>a) debts or contingent debts of central governments or central banks;</td>
<td>14,946.95</td>
<td>-</td>
</tr>
<tr>
<td>b) debts or contingent debts of regional governments and local authorities;</td>
<td>1,677.65</td>
<td>9.07</td>
</tr>
<tr>
<td>c) debts or contingent debts of administrative bodies and non-profit entities;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>d) debts or contingent debts of multilateral development banks;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>e) debts or contingent debts of international organizations;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>f) debts or contingent debts of institutions and financial institutions;</td>
<td>15.87</td>
<td>0.63</td>
</tr>
<tr>
<td>g) debts or contingent debts of companies;</td>
<td>3,061.13</td>
<td>4.48</td>
</tr>
<tr>
<td>h) retail debts or contingent debts;</td>
<td>4,472.27</td>
<td>0.01</td>
</tr>
<tr>
<td>i) debts or contingent debts secured by real estate;</td>
<td>3,261.39</td>
<td>0.13</td>
</tr>
<tr>
<td>j) remaining items ;</td>
<td>1,931.16</td>
<td>0.05</td>
</tr>
<tr>
<td>k) items belonging to high-risk categories;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>l) exposures in the form of covered bonds;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>m) securitization positions;</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>n) short-term debts of institutions and companies;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>a) claims in the form of shares held in collective investment undertakings;</td>
<td>0.00</td>
<td>0.00</td>
</tr>
<tr>
<td>p) other items.</td>
<td>1,761.02</td>
<td>-</td>
</tr>
</tbody>
</table>

Exposures by geographical areas and the main classes of exposure

<table>
<thead>
<tr>
<th>Geographical area / Exposure class</th>
<th>Regional governments or local authorities</th>
<th>Companies</th>
<th>Retail</th>
<th>Debts secured by real estate</th>
<th>Remaining items</th>
</tr>
</thead>
<tbody>
<tr>
<td>NORTH EAST</td>
<td>236.17</td>
<td>171.94</td>
<td>544.26</td>
<td>329.68</td>
<td>203.26</td>
</tr>
<tr>
<td>SOUTH EAST</td>
<td>147.82</td>
<td>103.80</td>
<td>639.58</td>
<td>484.95</td>
<td>450.11</td>
</tr>
<tr>
<td>SOUTH- MUNTE NIA</td>
<td>147.84</td>
<td>343.03</td>
<td>551.27</td>
<td>432.89</td>
<td>154.98</td>
</tr>
<tr>
<td>SOUTH- WEST OLTENI A</td>
<td>167.27</td>
<td>656.55</td>
<td>466.78</td>
<td>508.28</td>
<td>217.09</td>
</tr>
</tbody>
</table>
Impairment adjustments and impairment adjustments expenses for the main types of customers

<table>
<thead>
<tr>
<th>Type of customer</th>
<th>Impairment adjustments for the initial balances</th>
<th>Impairment adjustments expenses for the period</th>
<th>Impairment adjustments for the final balances</th>
</tr>
</thead>
<tbody>
<tr>
<td>bank customers</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>non-bank customers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- corporate</td>
<td>592.31</td>
<td>330.62</td>
<td>922.93</td>
</tr>
<tr>
<td>non-bank customers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- individuals</td>
<td>510.49</td>
<td>141.72</td>
<td>652.21</td>
</tr>
</tbody>
</table>

The Bank does not use balance compensation and compensation of off-balance items in the credit risk mitigation techniques.

Credit risk mitigation techniques using credit risk mitigation with effect of substitution of exposures is performed by taking into account the type of mortgages as collateral deposits placed with the Bank, using the Financial Collateral Simple Method. Deposits taken into account have at least a maturity equal to the maturity of the exposure and are established in the exposure currency.

Personal guarantees used by the Bank to mitigate the credit risk are irrevocable and unconditional express guarantees issued by the central government of the Romanian State or personal guarantees assimilated thereof.

Values at risk covered with mortgages and personal guarantees described above and divided by classes of exposure:

<table>
<thead>
<tr>
<th>Exposure class</th>
<th>Value at risk collateralised</th>
<th>Value at risk covered by personal guarantees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regional governments</td>
<td>0.00</td>
<td>50.54</td>
</tr>
<tr>
<td>or local authorities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Companies</td>
<td>20.97</td>
<td>654.28</td>
</tr>
<tr>
<td>Retail</td>
<td>16.51</td>
<td>432.25</td>
</tr>
<tr>
<td>Remaining items</td>
<td>0.11</td>
<td>13.12</td>
</tr>
</tbody>
</table>

Real estate collaterals in the form of real estate are recognized by the Bank for the credit risk mitigation if at least the following conditions are met:

- mortgages and privileges are enforceable;
- market value of the properties is determined by an independent evaluator;
• can be capitalized by the Bank within a reasonable time, in accordance with the contract of guarantee;
• the real estate values can be monitored and the need for reassessment can be identified periodically with a frequency according to the NBR regulations and of the Bank;
• are adequately insured against damage for the period of the loans.