GarantiBank International N.V.

REPORT ON CAPITAL ADEQUACY and RISK MANAGEMENT
2013

CONTENTS

1. Introduction

Related to the implementation of the Capital Requirements Directive (CRD), financial institutions have to fulfil several disclosure requirements. The aim is to make information available to the public relating to solvency aspects and the risk profile of the institution. The requirements are part of the so-called Pillar III of the CRD, or Disclosures and Market Discipline and have been included in the Financial Supervision Act (Wet op het financieel toezicht/Wft) in the Netherlands effective as of 1 January 2008. This document contains the Pillar III disclosures of GarantiBank International N.V. (hereafter referred to as "GBI") as at 31 December 2013 and should be read in conjunction with the annual report of GBI.

2. Scope of Application

The scope of application of the Pillar III requirements is confined to GBI and its branch. The information disclosed in this document is not subject to an external audit, but is verified and approved independently within GBI.

3. Risk Governance at GBI

The risk management culture at GBI has been established as a key ingredient of the Bank's strategy, with an emphasis on risk awareness at all levels of the organization. GBI has established an adequate segregation of duties and responsibilities with a view to a controlled pursuit of the business operations. Risk management is structured under various levels within the organization. These levels are composed of committees at the Supervisory Board Level, committees at the Bank level and in the form of separate risk and control division and departments. The committees which form the backbone of risk governance at GBI are established as per the segregation of duties principle and are supported by the supplementary risk management responsibilities of the related division and departments as specified below.

The Supervisory Board (SB) supervises the risk policy pursued by the Bank, and approves the risk appetite proposed by the Managing Board (MB) on at least an annual basis. The Risk Committee of the Supervisory Board (RCSB) advises the SB in the performance of its supervisory role, and also ensures that effective risk management is conducted by the Bank in line with the risk appetite. RCSB is responsible for monitoring all material risks and adequacy of capital and liquidity, at Supervisory Board level. The Audit & Compliance Committee of the Supervisory Board (ACCSB) is the ultimate authority related with the independent function of audit and compliance related issues, at Supervisory Board level. The Risk Management Committee (RMC) is responsible for the coordination and monitoring of risk management activities within the Bank, and reports directly to the RCSB. Other committees are established to manage more specifically the key banking risks; the Credit Committee for credit risk, Asset & Liability Committee (ALCO) for market, interest rate and liquidity risks, Compliance Committee for compliance risks and the New Product Development Committee for risks related to the introduction of new products/services.

The Risk Management Department (RMD) is an independent risk management function, which does not have any involvement in commercial activities and reports directly to RMC and RCSB. RMD is responsible for the quantification and monitoring of the material risks in terms of economic capital and regulatory capital in order to limit the impact of potential events on the financial performance of the Bank. RMD develops and implements risk policies, procedures, methodologies and infrastructures that are consistent with the regulatory requirements, and best market practices. RMD also coordinates all efforts for compliance of the Bank's risk management policies and practices with Basel principles and the Financial Supervision Act (FSA, Wet op het financial toezicht / Wft).

The Internal Control Unit (ICU), under RMD, is involved in the monitoring and reporting of operational risks and establishing preventive control processes.

The Credits Division (CD) is established as a separate risk control function, independent of the business lines, and ensures that effective processes are in place for the continuous administration and monitoring of credit risk and that the composition and the diversification of the loan portfolio are in line with the lending strategy of the Bank. The Internal Audit Department (IAD) is responsible for the monitoring of the proper functioning of the governance framework around risks through regular audits, and reports these to the ACCSB. The Legal and Compliance Department (LCD) operates independently from any commercial unit and reports directly to the Managing Board, Compliance Committee and ACCSB.

Information Security Department (ISD) is an independent risk control department that carries out the monitoring process in a systematic manner related with IT risks. ISD operates independently of any commercial activities.

4. Risk Appetite of GBI

GBI defines risk appetite as a core consideration in quantitative and qualitative indicators as well as meeting the regulatory, corporate governance and stakeholder requirements. The Bank's appetite with respect to risks is defined via a three-layer structure, which translates these objectives into metrics that can be measured and managed. Those layers consist of capital adequacy, return on equity and liquidity. Firstly, GBI prefers to have a strong capital base with a high Tier 1 component. Secondly, the performance aim of the Bank is to have a return on equity (ROE) that is stable in the long term and satisfies the stakeholders, including the shareholders, while maintaining her core competencies and strategic position in the key markets. Thirdly, GBI's liquidity risk policy is to maintain sufficient liquidity in order to ensure safe banking operations and a sound financial condition in normal and stressed financial environments and a stable long term liquidity profile. These three objectives are supported by the limit framework for each risk type.

GBI ensures that the risk strategy and targets are aligned throughout the organisation, from the top down and the bottom up. The high-level management policies, which are also subject to the final approval of the Supervisory Board, outline the framework for translating the Board-approved risk appetite into quantitative limits, and the governance for their monitoring and management.

5. Own Funds

GBI's capital base consists of two parts: Tier 1 (primary) and Tier 2 (supplementary) capital. The Tier 1 capital of GBI consists of fully paid-in capital and retained earnings including current year profit. Deductions from Tier 1 capital includes 50% of the excess[1] of expected loss over provisions, and the intangible fixed assets.

No hybrid Tier 1 capital products are used at GBI. Therefore, the common equity Tier 1 is equal to the Total Tier 1 Capital. Tier 2 capital of GBI consists of subordinated debt. The remaining 50% of the excess of expected loss over provisions is deducted from Tier 2 capital.

In line with article 64, paragraph 3 c) of the directive 2006/48/EG the amount of subordinated debt that is included in the own funds is gradually amortized if its remaining maturity falls below five years.

[1] If the total impairment provisions exceed the expected loss, it is added to Tier 2 capital up to the limit of 0.625% of credit risk weighted assets.

Please find below an overview of GBI's own funds composition as at 31.12.2013.

Table 5-1

(EUR 1,000)	31.12.2013	31.12.2012	Change
Tier 1			
Paid-in and called-up capital	136,836	136,836	-
Eligible reserves	352,089	293,610	58,479
IRB provision shortfall - 50%	-3,670	-5,100	1,430
Deduction of intangible fixed assets	-3,089	-	-3,089
TOTAL Tier 1	**482,166**	**425,346**	**56,820**
Tier 2			
IRB provision shortfall - 50%	-3,670	-5,100	1,430
Subordinated debt	30,000	30,000	-
TOTAL Tier 2	**26,330**	**24,900**	**1,430**
TOTAL Eligible Capital	**508,496**	**450,246**	**58,250**

Total own funds of GBI increased by 13% in 2013 mainly due to the strong profit generation of the Bank. GBI recorded a net profit of EUR 58.5 million in 2013, which is 8% higher than 2012's results. The relationship between GBI's Own Funds and accounting capital is shown in the table below. Further details of the Bank' own funds may be found in GBI's *"Annual Report 2013*".

Table 5-2

(EUR 1,000)	31.12.2013
Tier 1 capital:	
Paid-in and called-up capital	136,836
Other reserves	293,610
Net profit current year	58,479
Shareholders' equity (Accounting Capital)	**488,925**
IRB provision shortfall - 50%	-3,670
Deduction of intangible fixed assets	-3,089
Total tier 1 capital	**482,166**
Tier 2 capital:	
Subordinated debt	30,000
IRB provision shortfall - 50%	-3,670
Total tier 2 capital	**26,330**
Total regulatory capital	**508,496**

6. Regulatory Capital Requirements

Total of Tier 1 and Tier 2 capital should correspond to at least 8% of the Banks' risk weighted assets, of which Tier 1 capital must constitute at least 4%.

GBI applies the Foundation Internal Ratings Based (F-IRB) Approach for credit risk of Corporate, Institution and Sovereign portfolios since 1 January 2008 based on the permission obtained from De Nederlandsche Bank N.V. (DNB). Exposures related with Retail and Private Banking, are subject to permanent exemption from F-IRB and are treated under the Standardised Approach (SA). GBI uses the Standardised Measurement Approach (SMA) for market risk and the Basic Indicator Approach (BIA) for operational risk in the calculation of the minimum level of required capital. In the table below, an overview of the capital requirement and gross credit risk exposure[2] at 31 December 2013 is presented.

Table 6-1

(EUR 1,000)	31.12.2013		31.12.2012		Change	
	Gross Exposure	Capital Req.	Gross Exposure	Capital Req.	Gross Exposure	Capital Req.
Credit Risk	**4,849,351**	**187,730**	**5,094,378**	**170,519**	**-245,027**	**17,211**
F-IRB approach:						
Central Gov. & Central Banks[3]	680,048	14,074	835,280	12,054	- 155,232	2,020
Institutions	1,412,128	64,896	1,465,781	63,335	- 53,653	1,561
Corporates	2,173,520	81,438	2,325,944	77,387	- 152,424	4,051
Corporates (Specialised Lending)	463,619	21,897	387,525	14,628	76,094	7,269
Total F-IRB approach	***4,729,315***	***182,305***	***5,014,530***	***167,404***	***-285,215***	***14,901***
Standardised approach:						
Central Gov. & Central Banks	-	-	-	-	-	-
Institutions	1,699	39	-	-	1,699	39
Corporates	84,709	2,981	48,813	1,003	35,896	1,978
Retail	14,581	881	10,874	499	3,707	382
Equity	250	20	250	20	-	-
Other non credit-obligation assets	18,797	1,504	19,911	1,593	-1,114	-89
Total Standardised approach	***120,036***	***5,425***	***79,848***	***3,115***	***40,188***	***2,310***
Counterparty Credit Risk (CCR)	**686,726**	**6,974**	**198,908**	**1,757**	**487,818**	**5,217**
F-IRB approach:						
Institutions	492,987	1,972	162,037	976	330,950	996
Corporates	4,664	253	2,050	116	2,614	137
Corporates (Specialised Lending)	740	68	524	48	216	20
Total F-IRB approach	***498,391***	***2,293***	***164,611***	***1,140***	***333,780***	***1,153***
Standardised approach:						
Institutions	90,890	628	-	-	90,890	628
Corporates	92,933	3,961	32,345	569	60,588	3,392
Retail	4,512	92	1,952	48	2,560	44
Total Standardised approach	***188,335***	***4,681***	***34,297***	***617***	***154,038***	***4,064***
Total Credit Risk & CCR	**5,536,077**	**194,704**	**5,293,286**	**172,276**	**242,791**	**22,428**
Total Market Risk (SMA)		**118**		**320**		**-202**
Total Operational Risk (BIA)		**14,850**		**14,075**		**775**
Total Capital Requirement		**209,672**		**186,671**		**23,001**
Total RWA		**2,620,900**		**2,333,388**		**287,513**
Tier 1 Ratio		**18.40%**		**18.23%**		**0.17%**
Solvency Ratio		**19.40%**		**19.30%**		**0.10%**

[2] Balance sheet and off balance sheet items, before collateral mitigation and after provisions

[3] As per DNB's national discretion sovereign exposures of EUR 498.4 mio (2012: EUR 656.5 mio) which satisfy the 0% risk weight condition are classified under IRB in this table

The capital requirement under Pillar 1 is EUR 209.7 million. The largest part (93%) of the capital requirement relates to credit risk[4]. 95% of the credit risk weighted assets are treated under F-IRB approach.

GBI operates at a comfortable solvency level of 19.40% with a strong Tier 1 component of 18.40%. This solvency level provides a strong base to the Bank for the implementation of CRD IV. An overview of new regulations is provided in Section 9.

6.1. Credit Risk

The Bank's credit risk perception is in line with international standards. Credit risk is perceived as the volatility in the earnings of the bank due to the losses which arise in the credit portfolio as a result of the default of the counterparty (ies) and/or difficulty in liquidating the collateral(s).

At GBI, credit risk arises mainly, among others, from trade finance lending and fixed income securities portfolio. GBI is mainly involved in low default portfolios such as sovereigns, banks, large corporate companies and trade finance activities. The credit risk framework of GBI is built in a way that allows classifying counterparties, segregating them and subsequently applying specific processes to effectively cope with credit risks. All business flows implying credit risk are routed via the Credit Division that in turn is subdivided into separate teams responsible for assessing and managing credit risks pertinent to corporate counterparties, financial institutions and sovereigns. The aggregation of business flows in the Credit Division allows adequate evaluation of the global balance of risks and exposures.

The risk assessment approaches for different types of counterparties within the above mentioned subdivisions are different and adjusted to the specific properties of each subdivision type (e.g. financial institutions, non-bank financial institutions, commodity trading companies, corporates etc.) and to the variety of transactions typically handled (e.g. trade finance, shipping finance, treasury, private banking etc.).

Being a F-IRB Bank, GBI has dedicated internal rating models for all asset classes to evaluate the creditworthiness of counterparties. The rating models are integrated in the credit allocation and monitoring processes. Risk rating models serve as a basis for the calculation of regulatory capital and economic capital that GBI has to maintain to cover expected and unexpected losses from its lending activities. Ratings are also integral parts of pricing and risk based performance measurement processes. During 2013, all rating models have been validated by independent third party experts. IAD has reviewed the use of the models and the data quality.

The Credit Committee is responsible for the control of all credit risks arising from the banking book and the trading book, i.e. counterparty risks and concentration risks.

The effectiveness of risk monitoring is supported by internal systems ensuring proper compliance with the principle of segregation of duties and authorization levels. Every transaction under approved credit limits requires a number of authorizations and controls prior to execution and cannot be finalized without those processes. Under this structure, every commercial initiative goes through multiple checks and is inputted in the operating system by authorized personnel who are functionally separated from the personnel with commercial targets. Regular monitoring of GBI's exposure and compliance with the established credit limits ensures timely management of credit risk. The exposures to various

[4] Including counterparty credit risk

customers, business lines and geographical locations are monitored on a daily basis by assigned account and credit officers, while compliance with the established limits is controlled by Credits Division that provides independent judgement.

The credit follow-up process is divided into two main parts; follow-up of the customer and follow-up of the credit facility itself. The follow-up of the customer is associated with the credit risk, whereas follow-up of the credit facility (e.g. documentation) is related to credit risk mitigation and operational risk. The credit facility follow-up is a dynamic process and is categorized as; performing, watch list, impaired, provisioned and write-off stages. All shifts within those categories either in the direction of downgrading or upgrading, require the approval of GBI's Credit Committee. A loan may be shifted to the watch list based on the events outlaid in pre-defined warning signals.

The internal information system of GBI offers great possibility in delivering information on a regular and ad-hoc basis and allows producing a variety of daily reports that comprise all exposures and concentrations by geographical location, commodity type, supplier and many other criteria.

6.1.1. Exposure Amounts before Credit Risk Mitigation

The total credit exposure, including off balance sheet liabilities and counterparty credit risk exposure, after provisions and before credit risk mitigation is as follows:

Table 6.1.1

	Average Exposure	Total Exposure			
(EUR 1,000)	2013	Q4-2013	Q3-2013	Q2-2013	Q1-2013
Central Gov. & Central Banks	492,179	680,048	478,548	452,716	357,403
Institutions	1,808,056	1,997,704	1,705,672	1,639,702	1,889,147
Corporate	2,859,482	2,820,185	2,812,792	2,984,215	2,820,736
Retail	17,163	19,093	16,952	15,468	17,138
Equity	250	250	250	250	250
Other non credit-obligation assets	20,055	18,797	20,903	20,919	19,602
Total	**5,197,185**	**5,536,077**	**5,035,117**	**5,113,270**	**5,104,276**

The average exposure remained at similar levels compared to EUR 5,236 thousand in 2012.

6.1.2. Off-Balance Sheet Exposure Amounts

The off-balance sheet exposures are broken down to the transaction types shown in the table below. For regulatory capital calculations, the exposure values of off-balance sheet items are determined by multiplying the notional amounts with a Credit Conversion Factor (CCF), based on a regulatory 'risk classification'. The decrease in total off-balance sheet exposure is mainly driven by the decrease in letters of credit compared to 2012.

Table 6.1.2-1

(EUR 1,000)	31.12.2013	31.12.2012	Difference
Guarantees	**41,077**	**55,745**	**-14,668**
100%	41,077	55,745	-14,668
75%	-	-	-
20%	-	-	-
0%	-	-	-
Irrevocable letters of credit	**256,719**	**312,559**	**-55,840**
100%	6,438	-	6,438
75%	-	-	-
20%	250,281	312,559	-62,278
0%	-	-	-
Other commitments	**87,218**	**105,599**	**-18,381**
100%	3,408	13,790	-10,382
75%	83,392	91,298	-7,906
20%	-	-	-
0%	418	511	-93
Total	**385,014**	**473,903**	**-88,889**

6.1.3. Geographical Breakdown of the Exposures

The following table gives an overview of the geographical breakdown[5] of gross exposure by material exposure classes based on customer residence:

Table 6.1.3

(EUR 1,000)	The Netherlands	Other Europe	Turkey	CIS countries	Rest of the World	Total
31.12.2013						
Central Gov. & Central Banks	483,216	107,199	89,633	-	-	680,048
Institutions	166,965	566,450	884,638	286,816	92,835	1,997,704
Corporates	249,666	864,751	1,091,265	134,425	480,078	2,820,185
Retail	4,413	3,467	9,787	1,426	-	19,093
Equity	250	-	-	-	-	250
Other non credit-obligation assets	16,861	1,936	-	-	-	18,797
Total	**921,371**	**1,543,803**	**2,075,323**	**422,667**	**572,913**	**5,536,077**
Percentage of total	16.64%	27.89%	37.49%	7.63%	10.35%	100.00%

[5] The geographical breakdown of assets and off-balance sheet liabilities is also provided in Section 33.1.a of GBI's *"Annual Report 2013"*. Nevertheless the figures in annual report do not include cash held at the central bank, non-credit obligations together with the counterparty credit risk.

(EUR 1,000)	The Netherlands	Other Europe	Turkey	CIS countries	Rest of the World	Total
31.12.2012						
Central Gov. & Central Banks	641,925	118,777	74,578	-	-	835,280
Institutions	47,584	292,253	884,043	335,570	68,368	1,627,818
Corporates	242,044	665,129	1,331,469	122,270	436,290	2,797,202
Retail	1,283	1,261	10,282	-	-	12,826
Equity	250	-	-	-	-	250
Other non credit-obligation assets	19,737	174	-	-	-	19,911
Total	**952,823**	**1,077,594**	**2,300,372**	**457,840**	**504,658**	**5,293,287**
Percentage of total	18.00%	20.36%	43.46%	8.65%	9.53%	100.00%

6.1.4. Effective Maturity Breakdown

GBI mainly enters into transactions with short maturities as a result of its business model. The vast majority of the exposures are with residual maturity less than one year. The effective maturity breakdown of gross exposure based on exposure classes is as follows:

Table 6.1.4

(EUR 1,000)	< 3 Months	< 6 Months	< 1 Year	< 2 Years	< 3 Years	<= 5 Years	Total
31.12.2013							
Central Gov. & Central Banks	488,695	-	-	-	-	191,353	680,048
Institutions	971,603	254,740	350,802	40,775	7,426	372,358	1,997,704
Corporates	1,429,841	327,724	318,897	302,790	238,448	202,485	2,820,185
Retail	9,787	464	2,664	303	130	5,745	19,093
Equity	250	-	-	-	-	-	250
Other non credit-obligation assets	-	-	-	-	-	18,797	18,797
Total	**2,900,176**	**582,928**	**672,363**	**343,868**	**246,004**	**790,738**	**5,536,077**
Percentage of total	52.39%	10.53%	12.15%	6.21%	4.44%	14.28%	100.00%
31.12.2012							
Central Gov. & Central Banks	544,056	-	-	-	147,998	143,226	835,280
Institutions	568,526	322,337	286,617	127,484	450	322,404	1,627,818
Corporates	1,564,578	332,107	463,441	118,696	155,054	163,326	2,797,202
Retail	5,967	966	1,789	1,789	223	2,092	12,826
Equity	250	-	-	-	-	-	250
Other non credit-obligation assets	-	-	-	-	-	19,911	19,911
Total	**2,683,377**	**655,410**	**751,847**	**247,969**	**303,725**	**650,959**	**5,293,287**
Percentage of total	50.70%	12.40%	14.20%	4.70%	5.70%	12.30%	100.00%

75.1% of the total credit exposures have effective maturity of lower than one year compared to 77.3% in 2012.

6.1.5. Breakdown of the Exposures by Industry

The breakdown of gross exposure[6] by industry and exposure class is as follows:

Table 6.1.5

(EUR 1,000)	31.12.2013		31.12.2012	
	Total	**% of Total**	**Total**	**% of Total**
Central Gov. & Central Banks	**680,048**	**12.28%**	**835,280**	**15.78%**
Institutions	**1,997,705**	**36.09%**	**1,627,818**	**30.75%**
Corporates	**2,820,185**	**50.94%**	**2,797,202**	**52.85%**
Agriculture	171,298	3.09%	179,544	3.39%
Automotive	26,754	0.48%	-	-
Basic materials	461,191	8.33%	545,122	10.30%
Services	3,026	0.05%	4,791	0.09%
Chemicals	274,716	4.96%	251,421	4.75%
Food, beverages and tobacco	92,869	1.68%	31,748	0.60%
Construction	58,148	1.05%	126,179	2.38%
Consumer products	149,185	2.69%	129,695	2.45%
Financial services	619,947	11.20%	655,770	12.39%
Insurance and pension funds	10,057	0.18%	16,263	0.31%
Leisure and Tourism	6,200	0.11%	10,360	0.20%
Media	-	-	1,752	0.03%
Oil and Gas	352,480	6.37%	258,942	4.89%
Other	228,146	4.12%	124,905	2.36%
Wholesale	15,561	0.28%	12,030	0.23%
Telecom	112,291	2.03%	166,004	3.14%
Transport and logistics	209,595	3.79%	251,535	4.75%
Utilities	28,723	0.52%	31,141	0.59%
Retail	**19,093**	**0.34%**	**12,826**	**0.24%**
Equity	**250**	**0.00%**	**250**	**0.00%**
Other non-credit obligation assets	**18,797**	**0.34%**	**19,911**	**0.38%**
Total	**5,536,077**	**100.00%**	**5,293,287**	**100.00%**

6.1.6. Past Due and Impaired Exposures, Provisions and Value Adjustments

A loan is recognized as impaired if there is an objective evidence of impairment. This evidence could be given by, but is not limited to, the events listed below:

- It is probable that the borrower will enter bankruptcy or other financial reorganization.
- The debtor has payment defaults against third parties; customers, banks, employees, etc.
- The debtor has been in arrears for at least 90 days with regard to repayment of principal and/or interest.
- Observable data indicates that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets.
- A breach of contract, such as a default or delinquency in interest or principal payments
- Significant financial difficulty of the issuer or obligor.
- The disappearance of an active market for that financial asset because of financial difficulties.

For impaired loans, GBI attempts to ensure recovery by restructuring, obtaining additional security and/or proceeding with legal actions. Provisions are established by the Credit Committee, for the outstanding amount of the defaulted credit facility after deduction of expected recoveries and/or

[6] Breakdown by industry for loans and advances is also provided in Section 33.1.c of GBI's *"Annual Report 2013*". However, the table above includes all exposures subject to credit risk calculation.

liquidation value of the collaterals. The impaired credit facility is further proposed for write-off after all possible means of recovery have been exhausted. Below table provides information on the impaired loans and provisions by exposure class:

Table 6.1.6-1

(EUR 1,000)	31.12.2013		31.12.2012	
	Impairment[7]	Provisions	Impairment[7]	Provisions
Corporates	85,282	44,711	64,174	30,796
Retail	617	617	746	746
Total	**85,899**	**45,332**	**64,920**	**31,542**
Loan Loss Reserve Ratio	**52.8%**		**48.6%**	

Loan loss provisions are at the 52.8% level and reflect the robust recoveries expected due to the collateralised nature of the credit portfolio. The table below gives an overview of the impaired and past due exposures and the provisions set aside by the residence of the counterparty:

Table 6.1.6-2

(EUR 1,000)	Impaired Exposures	90 Days Past Due[8]	Provisions for Impairment
31.12.2013			
The Netherlands	1,788	-	1,788
Other Europe	34,301	-	20,325
CIS countries	21,667	-	9,514
Rest of the world	27,567	-	13,224
Turkey	576	-	480
Total	**85,899**	**-**	**45,332**
31.12.2012			
The Netherlands	2,891	-	2,481
Other Europe	7,148	2,206	7,148
CIS countries	24,889	-	7,252
Rest of the world	26,761	-	11,597
Turkey	3,231	-	3,064
Total	**64,920**	**2,206**	**31,542**

An exposure is past due if a debtor has failed to make a payment of principal and/or interest when contractually due. There is no 90 days past due amount which is not provisioned at 31.12.2013.

The actual value adjustments in the preceding periods for each exposure class are as follows:

Table 6.1.6-3

(EUR 1,000)	31.12.2013	31.12.2012
Position as of 1 January	31,542	25,544
Additions	20,809	10,785
Write-offs	-437	-2,659
Releases	-5,383	-1,410
Exchange rate differences	-1,199	-718
Position as of 31 December	**45,332**	**31,542**

The net provision for loan losses increased to EUR 45.3 million from EUR 31.5 million.

[7] Impaired exposures after deduction of financial collaterals and including the noncash exposures to the impaired customers.
[8] but not impaired

6.1.7. Counterparty Credit Risk

The exposure value of the counterparty credit risk is calculated according to Section 5 of the DNB's Supervisory Regulation on Solvency Requirements for Credit Risk. Establishment of a credit limit for counterparty credit risk includes, but is not limited to, for the products below:

- Spot and forward foreign exchange (FX) transactions
- Currency transactions including currency swaps
- Options
- Forward rate agreement (FRA)
- Interest rate swaps (IRS)
- Credit default swaps (CDS)
- Securities lending or borrowing transactions (SFTs)

Derivatives transactions with professional market participants are subject to the Credit Support Annex (CSA) of the International Swaps and Derivatives Association (ISDA) derivatives agreements. Therefore the Bank could be in a position to provide or require additional collateral as a result of fluctuations in the market value of derivatives. The amount of collateral provided under these agreements is disclosed under section 32 (Pledged assets) of GBI's "*Annual Report 2013*". For derivatives transactions with clients the Bank is not obliged to provide collateral, but it is entitled to receive collateral from clients, hence there is no potential liquidity risk for the Bank.

The repurchase transactions are subject to the Global Master Repurchase Agreement (GMRA). The increase in the positive replacement value of derivatives together with the increase in the repurchase transactions, have increased the total counterparty credit risk in 2013 compared to 2012. The credit exposures of the derivative transactions are calculated by using Current Exposure Method (CEM) and eligible collaterals are accounted for, where applicable.

Table 6.1.7-1 demonstrates the steps in the calculation of net derivatives credit exposure.

Table 6.1.7-1

(EUR 1,000)	Positive Replacement Value	Potential Future Credit Exposure	Exposure Value[9]	Collateral Held	Net Exposure[10]
31.12.2013					
Repurchase transactions			446,973	333,824	113,149
Interest rate derivatives	844	1,574	2,418	-	2,418
FX derivatives and Options	184,597	52,740	237,337	65,830	171,507
Total	**185,441**	**54,314**	**686,727**	**399,654**	**287,073**
31.12.2012					
Repurchase transactions			182,099	149,754	32,345
Interest rate derivatives	-	1,106	1,106	-	1,106
FX derivatives and Options	75,011	57,455	132,466	26,578	105,888
Total	**75,011**	**58,561**	**315,672**	**176,332**	**139,339**

The distribution of derivatives notional amounts by residual maturity is provided in Section 33.1.e of GBI's "*Annual Report 2013*".

[9] Exposure value refers to the sum of positive replacement cost and potential future credit exposure, however for Repurchased transactions, it includes mark-to-market value of the securities provided as collateral (after application of regulatory volatility haircuts).

[10] Exposure after collateral mitigation

6.1.8. Credit Risk Mitigation

Credit risk mitigants are financial collaterals and guarantees which directly decrease the credit exposure or transfer the credit risk from obligor to guarantor. GBI applies diversified collateral requirements and systematic approaches to collaterals submitted by customers, which depend on the transaction type and purpose, including but not limited to cash margins, physical commodities, receivables, cash flows, guarantees, accounts, financial instruments and immovable or movable assets. The value of collateral is usually monitored on a daily basis to ensure timely measures are taken, if necessary.

The use of collateral to reduce counterparty credit exposure is also embedded in the standard legal agreements used throughout the industry as explained above. For derivative transactions, the legal agreements include the ISDA derivatives agreements with CSA.

The range of collateral that is eligible for the use of credit risk mitigation is based on the regulatory capital calculation method that is used. GBI uses the Comprehensive – IRB method in the calculation of credit risk mitigation factors. The total exposure value that is covered by financial and other collaterals recognized as eligible credit risk mitigation[11] by the capital requirements directive is as follows:

Table 6.1.8-1

(EUR 1,000)	Financial Collateral	Guarantees	Other Collateral	Total
31.12.2013				
Central Gov. & Central Banks	-	-	-	-
Institutions	527,440	9,355	-	**536,795**
Corporates	149,827	168,863	800	**319,490**
Retail	6,936	-	-	**6,936**
Total	**684,203**	**178,218**	**800**	**863,221**
31.12.2012				
Central Gov. & Central Banks	100,000	-	-	**100,000**
Institutions	151,899	-	-	**151,899**
Corporates	279,355	55,302	112,459	**447,116**
Retail	5,985	-	-	**5,985**
Total	**537,239**	**55,302**	**112,459**	**705,000**

6.2. Scope of Acceptance for F-IRB Approach

GBI applies the F-IRB approach for the following exposure classes:

- Central Governments and Central Banks,
- Institutions and
- Corporates (including sub classes; Corporates, Non-Bank Financial Institutions, Specialized Lending exposure classes of Commodity Finance and Shipping Finance).

Retail exposures (including sub classes Retail and Private Banking) are subject to permanent exemption from F-IRB and are treated under SA.

[11] Similar table in Section 33.1.b of GBI's "*Annual Report 2013*" presents the collateral allocated only for loans and advances.

6.2.1. General Description of Models

GBI has dedicated rating models for all the sub-exposure classes mentioned above. The rating models within the scope of F-IRB application can be grouped into two:

- Probability of Default (PD) Models: These models provide obligor grades based on the master scale defined by GBI. The master scale has 22 rating grades and provide sufficient granularity for risk assessment. The rating grades are converted to PD via a master scale. The master scale is reviewed on an annual basis and updated where necessary based on the internal and external changes in observed default rates.

- Supervisory Slotting Criteria (SSC) Models: GBI has developed rating models for Specialized Lending exposure classes of Commodities Finance and Shipping Finance based on the SSC as per the conditions stated in CRD. SSC Models provide 5 grades, which are mapped to risk weights set by the regulation.

All rating models used within GBI have similar and consistent methodologies, which are based on two steps. The first step contains financial and non-financial models that produce a combined score. The models use financial information along with qualitative information that is collected through standard questionnaires. This score is further adjusted for a number of warning signals. The result is an individual rating, which is subject to an override framework in the second step. The override framework has three layers, which are; country layer, parental support and manual override.

The internal models are subject to a regular cycle of validation and review performed by external and internal parties.

6.2.2. Governance Framework around F-IRB Models and Processes

Credit rating models at GBI are based on a model-life cycle framework consisting of the following steps;

- Model development
- Model approval
- Model implementation
- Use and monitoring of model performance
- Model validation

Model development starts with the identification of the model requirement. This may arise from regulatory needs, improving risk management practices, changes in the risk management structure, changes in business structure that might lead to a new business line or a new asset class, a drastic change in macroeconomic or business environment that might affect risk factors, change in market practices and validation results that would necessitate model re-development.

Model approval starts after the completion of model development and model documentation. All the relevant materials regarding the model development are submitted to the RMC for approval. The models are approved based on the criteria that the model should reflect the risk perception of GBI, meet regulatory requirements, have a consistent methodology with the other models used by GBI, and perform adequately for that specific asset class. The proposed model is also subject to supervisory review if the impact of the model on risk weighted assets is significant[12].

[12] As defined by DNB, a change in a rating model is “significant” if it leads to a change in the capital requirement of more than 20% for the related portfolio, and/or 5% for the whole credit risk portfolio.

Model implementation starts once the model is approved by the RMC. IT related issues, data management, business line re-design and training of the user of the models are included in the generic roll-out plan of model implementation.

The models are used within the various levels of the organization. Related business lines initiate the rating process together with the credit proposals. The Credit Division reviews the rating which is then approved by the Credit Committee. The assigned ratings are used for all relevant transactions of the counterparty throughout the whole credit decision making process, including credit allocation, utilization, pricing and performance monitoring.

The correct use of models is audited by IAD within the scope of the regular audit activities. RMD is responsible for the on-going monitoring of the performance of the models. Model accuracy, stability, granularity, use of overrides and the data quality are key performance indicators for model performance. As the Bank mainly works with low default portfolios, the accuracy of the model cannot be measured through predictive power against default experience. Hence, alternative methods are used to ensure that the model performs satisfactorily, such as comparing the model outcomes with internal or external benchmarks and using concordance measures to determine their similarity.

The model validation framework is managed by a validation team that is independent of the model development team. In order to avoid the “Conflict of Interest” adequately, third parties are hired to ensure independence. RMC has the ultimate decision making authority in the formation of the validation team and the selection of the third party. The findings of the validation team are presented in the validation reports. These reports are immediately shared with DNB following the completion of the validation process. Model validation is conducted once a year and may be conducted more frequently based on the model performance.

Model maintenance is an on-going process which follows several steps within the lifecycle of the model. GBI has established procedures in order to support change management. These procedures explain the roles and responsibilities of the related stakeholders during the implementation of a change in the models, including detailed procedures related with the IT infrastructure of the models. These activities are audited by IAD on a regular basis in addition to the independent checks and controls carried out within the scope of the validation process.

6.2.3. Calculation of Risk Weighted Assets for F-IRB Exposure Classes

RWA calculation for credit risk is performed based on a regulatory formula under the F-IRB approach where the Probability of Default (PD), Maturity (M), Exposure at Default (EAD) and Loss given Default (LGD) are the factors. Under the F-IRB approach, PDs are estimated by the institution while M, LGD and EAD are supervisory estimates.

Below is an overview of the portfolios, applicable for F-IRB methodology, excluding specialized lending, as of 31 December 2013.

Table 6.2.3-1

(EUR 1,000)	Gross Exposure[13]	RWA	Average PD[14]
31.12.2013			
Central Gov. & Central Banks	680,048	175,925	0.43%
Institutions	1,896,526	835,850	0.46%
Corporates	2,148,217	1,021,138	0.68%
Total	**4,724,791**	**2,032,913**	**0.58%**
31.12.2012			
Central Gov. & Central Banks	835,280	150,672	0.43%
Institutions	1,617,979	803,877	0.54%
Corporates	2,305,865	968,790	0.65%
Total	**4,759,124**	**1,923,339**	**0.60%**

6.2.4. Specialized Lending

Credit institutions have to distinguish specialized lending exposures within the corporate exposure class. Specialized lending exposures possess the following characteristics:
(a) The exposure is to an entity which was created specifically to finance and/or operate physical assets;
(b) The contractual arrangements give the lender a substantial degree of control over the assets and the income that they generate; and
(c) The primary source of repayment of the obligation is the income generated by the assets being financed, rather than the independent capacity of a broader commercial enterprise.
The following table discloses the gross specialized lending exposures after provisions, assigned to the different risk categories as at 31 December 2013:

Table 6.2.4-1

(EUR 1,000)		31.12.2013		31.12.2012	
Risk Weight Category	**Risk Weight**	**Gross Exposure[15]**	**RWA**	**Gross Exposure[15]**	**RWA**
Strong	50% - 70%	137,367	52,735	189,717	69,171
Good	70% - 90%	239,497	153,728	152,413	87,491
Satisfactory	115%	69,163	60,908	30,660	26,791
Weak	250%	3,875	7,188	-	-
Total		**449,902**	**274,559**	**372,790**	**183,453**

[13] Gross exposure excluding nonperforming loans
[14] Expected probability of default of the performing portfolio
[15] Gross exposure excluding nonperforming loans

6.3. Market Risk

Market risk is defined as the current or prospective threat to GBI's earnings and capital as a result of movements in market factors, i.e. prices of securities, commodities, interest rates and foreign exchange rates.

GBI assumes limited market risk in trading activities by taking positions in debt securities, foreign exchange and commodities as well as in equivalent derivatives. The Bank has historically been conservative while running the trading book. Hence the main strategy is to keep the end of day trading positions at low levels. GBI uses the Standardised Measurement Approach in order to calculate the capital requirement arising from market risk (trading book) under Pillar I, which is generally comprised of foreign exchange risk. The net FX position is calculated using the shorthand method prescribed in the DNB's Supervisory Regulation on Solvency Requirements for Market Risk; the net short and net long position in each currency, including the reporting currency, are converted at spot rates into the reporting currency. They are then summed separately to form the total of the net short positions and the total of the net long positions, respectively. The higher of these two totals is the Bank's overall net foreign exchange position. The below table gives the breakdown of the capital requirement as at 31.12.2013:

Table 6.3-1

(EUR 1,000)	**31.12.2013**	**31.12.2012**
Foreign Exchange Risk	118	320
Total Capital Requirement	**118**	**320**

Value-at-Risk (VaR) analysis is used in order to assess the adequacy of the capital allocated under Pillar I within the scope of ICAAP and in the daily limit monitoring process.

ALCO bears the overall responsibility for the market risk and sets the limits at product and desk levels. Treasury Department actively manages the market risk within the limits provided by ALCO. Middle Office (MO) and Internal Control Unit (ICU), which are both established as independent control bodies, monitor and follow-up all trading transactions and positions on an on-going basis. Trading activities are followed-up as per the position, stop-loss, sensitivity and VaR limits set by ALCO. Single transaction and price tolerance limits have been established in order to minimize the operational risks involved in the trading processes. RMD is responsible for the maintenance of internal models, follow-up of risk based limits and performing stress tests and presenting the results to the related committees.

6.4. Operational Risk

GBI uses the Basic Indicator Approach in order to determine the regulatory capital requirement which arises from operational risk. The capital requirement is equal to 15% of the relevant indicator in this methodology. The relevant indicator is the average over three years of the sum of annual net interest and net non-interest income. The three-year average is calculated on the basis of the last three financial year observations.

Table 6.4-1

(EUR 1,000)	**31.12.2013**	**31.12.2012**	**31.12.2011**	**31.12.2010**
Operational Risk Exposure	91,271	105,311	100,419	75,779
Total Capital Requirement	**14,850**	**14,075**		

The average of the sum of net interest income and net non-interest income over the past three years amounts to EUR 99 million in 2013, which results in a capital requirement of EUR 14.9 million.

7. ICAAP Framework

GBI has designed a comprehensive ICAAP framework by making use of qualitative and quantitative assessment methodologies to assess the adequacy of the Bank's capital to cover various risks. The methodologies used are believed to be the most appropriate ones in line with the risk profile of GBI and they reflect the underlying risks in a prudent manner.

ICAAP starts with the assessment of the capital allocated for Pillar I risks. The capital calculations under Pillar I are referred to as Regulatory Capital (RCAP). GBI has specific assessment methodologies for credit, market and operational risks, which are used to come up with an Economic Capital (ECAP) figure. RCAP and ECAP are compared for each risk type under Pillar I and the maximum of RCAP and ECAP is taken as the outcome of ICAAP. The total of the outcomes for each risk type is the final result of ICAAP for Pillar I risks.

The second step is to take into account the additional capital requirements arising from the risks, which are not taken into account in Pillar I. GBI has a dedicated assessment methodology for each material Pillar II risk. The capital requirement for the concentration risk and interest rate risk in the Banking Book (IRRBB) are calculated through quantitative techniques, whereas the strategic risk is assessed within the scope of capital plan.

The Bank categorizes the materiality of risks as per the groups shown in below. The categorization is made based on an appropriate qualitative or quantitative assessment of the particular risk type.

Table 7-1

Materiality	Definition	Likely Action
1. Material	The probability of a risk event leading to a significant or high impact is material.	Established controls and risk assessments are performed on a regular basis. Mitigating actions shall be taken. Adequate level of capital shall be allocated for the risk type where necessary
2. Immaterial	The probability of a risk event leading to a significant impact is low.	Established controls and risk assessments are performed on a regular basis. Mitigating actions are taken, where necessary. No capital is allocated for the risk type.
3. Not Applicable	Risk is not applicable at all.	No action taken.

GBI is subject to the risk types presented below as a result of the activities pursued by the Bank.

Table 7-2

Risk Type	Covered in
Credit Risk	Pillar I and Pillar II
Concentration Risk	Pillar II
Market Risk	Pillar I and Pillar II
Interest Rate Risk on the Banking Book	Pillar II
Operational Risk	Pillar I and Pillar II
Strategic Risk	Pillar II
Liquidity Risk	ILAAP

7.1. Credit Risk

GBI has a dedicated ECAP model for credit risk, which is used as a benchmark to assess the adequacy of regulatory capital allocated for credit risk under Pillar I. A 99.9% confidence level is used in the ECAP calculations.

7.2. Concentration Risk

Concentration risk is defined as the risk arising from the concentration of credit risk exposure in a group of obligors vulnerable to the same or similar/correlated factors; e.g. industry concentration, country concentration, group concentration.

GBI continuously follows the credit risk positions of all obligors via a comprehensive management information system. Exposures to countries and industries are followed up frequently by the Credit Division and monitored and discussed regularly at the Credit Committee.

Follow-up of large exposures is also an integral part of this process. GBI monitors the large credit exposures to group of customers and proactively manages single name concentration. Large exposures are also reviewed by the Credit Committee and Supervisory Board on a regular basis. RMD monitors the concentration risk, quantifies its impact on the regulatory and economic capital, and reports to RMC and Supervisory Board.

GBI has developed an integrated quantitative methodology for the assessment of concentration risk. The concentration risk model, which is another form of economic capital methodology, takes into account the main concentration elements in the portfolio, namely single name concentration, country concentration and industry concentration, in a more conservative manner. The outcomes of the concentration risk model are supplemented by various stress tests.

The Bank complies with the requirements of the “Policy rule on the treatment of concentration risk in emerging countries”, which is a specific regulation on concentration risk that entered into force in the Netherlands as of July 2010.

7.3. Market Risk

GBI uses VaR as a risk measure for market risk on the trading book, in order to assess the adequacy of the capital allocated under Pillar I. VaR quantifies the maximum loss that could occur due to changes in risk factors (e.g. interest rates, foreign exchange rates, equity prices, etc.) for a time interval of one day, with a confidence level of 99.9%. This amount is multiplied by square root of 10 and multiplication factor of three (as a result of the daily back tests) in order to calculate the required capital. Limits based on VaR are defined and monitored periodically.

VaR is supplemented by stress tests and scenario analyses in order to determine the effects of potential extreme market developments on the value of market risk sensitive exposures. Stress tests have the advantage of out-of-model analyses of the trading book. Hypothetical or historical scenarios are chosen and applied to the Bank's position regularly. These scenarios are reviewed periodically and updated when necessary. Currently the stress tests include 'factor push' types of tests where shocks are applied to the key market factors, as well as stress tests where historical scenarios such as the 2001 crisis in Turkey and the 2008 Lehman collapse are applied to the Bank's current portfolio.

7.4. Interest Rate Risk on the Banking Book (IRRBB)

Interest rate risk is defined as the risk of loss in interest earnings or in the economic value of banking book items as a consequence of fluctuation in interest rates. GBI perceives interest rate risk as a combination of repricing risk, yield curve risk, basis risk and option risk. The asset and liability structure of the Bank creates a certain exposure to IRRBB. Repricing risk is the most important one and the others are at immaterial levels as a result of the business model of the Bank. However all types are monitored and their impact is assessed regularly. Business units are not allowed to run structural interest mismatch positions. As a result of this policy, day-to-day interest rate risk management is carried out by the Treasury Department in line with the policies and limits set by ALCO, with the help of a well-defined internal transfer pricing process.

IRRBB is measured and monitored by using Duration, Repricing Gap and Sensitivity analyses. Sensitivity analyses are based on both economic value and earnings perspectives. Interest sensitivity is measured by applying standard parallel yield curve shifts, historical simulation and user defined yield curve twist scenarios. A full pricing methodology is used for the quantification. All analyses are based on the interest rate repricing maturities. Behavioural analyses are used for the products that do not have contractual maturities, i.e. saving deposits.

The Repricing Gap analysis shows interest bearing balance sheet assets and liabilities broken down by when they are next due for repricing. This analysis is used as a supplementary measure to duration in order to point out interest bearing inflows/outflows and their maturities. Maturity calendar is disclosed under section 33.2.b (Interest Rate Risk) of GBI's *"Annual Report 2013"*.

The Earnings at Risk (EaR) analysis focuses on the effects of interest rate changes on the Bank's reported earnings over one year and two years. The standard gradual shift in the yield curve is applied for the calculation of the regulatory stress test; the interest rates are assumed to increase (or decrease) within one year and to remain at that level in the second year.

Economic Value of Equity (EVE) is defined as the economic value of assets less the economic value of liabilities. The standard parallel shock to yield curve leads to a potential decrease in EVE of EUR 31.5 million (6.20% of the total own funds), which is well below the regulatory threshold of 20%. GBI monitors the present value of her exposures both with risk free curves and spread curves in order to distinguish the impact of credit spread of the yield curves.

GBI also measures interest rate sensitivity by using historical volatility approach. Historical scenarios are applied to the whole banking book in a systematic manner in order to find the day in history which would have the maximum negative impact on the economic value of equity. Scenarios are determined based on the interest rates collected at different currencies and maturities for a 5 year historical period.

Table 7.4-1

Economic Value Sensitivity Analysis[16] (EUR 1,000)	**EUR**	**USD**	**TRY**	**OTHER**	**TOTAL**
31.12.2013					
Shift Up Net[17]	-2,881	-33,222	1,936	2,650	-31,517
Shift Down Net[17]	3,648	42,869	-2,027	-791	43,699
Change in Economic Value					31,517
Own Funds					**508,496**
Change in Economic Value / Own Funds					**6.20%**
31.12.2012					
Shift Up Net[17]	-2,479	-27,583	-109	173	-29,998
Shift Down Net[17]	669	22,167	117	-6	22,947
Change in Economic Value					29,998
Own Funds					**450,246**
Change in Economic Value / Own Funds					**6.66%**

The Bank has a low duration structure. Therefore sensitivity to interest rate shocks is limited. Moreover, the duration mismatch is stable as a natural consequence of the clear business model of the Bank.

All interest rate sensitivity analyses are also used for evaluating hedging strategies, internal limit setting and portfolio monitoring purposes, enabling GBI to manage interest rate risk in a proactive manner.

7.5. Operational Risk

GBI applies the Basel II definition for operational risk, which is 'the risk of direct or indirect loss resulting from inadequate or failed processes or systems, from human error or external events'. It also encompasses IT, legal, business, integrity, reputational, and settlement risk.

The Bank has embedded the 3 Lines of Defence model in its day-to-day activities, with the first line being the business as the experts in their field, controlling functions (Internal Control Unit, Credit Division, Information Security Department, Legal and Compliance Department) as the second line responsible for creating and implementing the relevant tools, in addition to challenging and advising the business, and finally Internal Audit acting as the third line by performing independent audits throughout the year. The operational risk framework of GBI is based on the principle that senior management, in addition to the Managing Board and Supervisory Board, are actively involved in risk management, and that the risk management system is independent, sound and implemented with integrity.

GBI uses policies and procedures to set the rules, and event management to monitor the events that are not in compliance with these rules. The Bank's internal control framework consists of daily controls performed by business lines and by ICU, to ensure that the activities of the Bank are in compliance

[16] Static balance sheet, based on instant liquidation
[17] 200 Bps shock for G10 and 300 Bps shock for non-G10

with the internal policies and that corrections are done in a timely manner on a consolidated basis. Findings of ICU are presented to RMC and RCSB.

GBI follows the Financial Institutions Risk Analysis Method (FIRM) for its operational risk. FIRM questionnaires are also used during the ICAAP via a scoring methodology. The answers to the questions are translated into scores in a similar manner to that explained in the FIRM manual. The score outcomes are reviewed in order to make the necessary decisions (if any) to take mitigating action.

IT risk assessments are performed by an independent external party based on the international Control Objectives for Information and Related Technology (COBIT) and national FIRM standards. The implementation of an Information Security Management System in accordance with internationally recognized standards (ISO 27001) was a key objective in 2013 to demonstrate our commitment to Information Security. This involved the systematic examination of the Bank's information security risks; the identification of threats and vulnerabilities to our information assets and assessment of associated risk exposures to these assets; the implementation of a comprehensive suite of security controls to reduce or mitigate identified information security risks; conducting information security awareness training for all employees; the establishment of information security and information technology policies to manage potential exposures and a robust management process to ensure controls continue to meet the Bank's information security needs; and lastly, centralizing, standardizing and automating identity management services to reduce risk, cost and improve operational efficiency.

7.6. Other Risks

GBI has immaterial or no exposure to business risk, residual risk, pension risk, underwriting risk and securitization risk. Legal risk and settlement risk rare monitored in regular audit activities and by way of applying FIRM assessments, together with operational risk. Strategic risk is taken into account in the capital planning process in order to account for the possible increase in the capital requirement based on the strategies or the business models that are chosen by GBI. The impact of reputation risk is included within the scope of liquidity risk management and contingency funding plan.

7.7. Capital Plan

Capital planning is an integral part of ICAAP. GBI's capital planning structure has been developed based on two scenarios, one of which is in line with the Bank's current expectations and financial budget. The second scenario applies more conservative assumptions in order to assess the future capital adequacy of GBI under stressed economic and financial conditions. Stress test outcomes are used to assess the adequacy of the own funds for potential future capital requirements for the next three years.

The capital plan aims to cover as many aspects as possible, including expected profit liquidity sources, portfolio mix, capital structure and asset quality, in order to reflect the impact of several risk factors on the profitability and the capital adequacy of GBI at the same time. Changes in regulations, timelines, transitions, etc. are taken into account within the scope of the capital planning process.

8. ILAAP Framework

The main objective of GBI's liquidity risk policy is to maintain sufficient liquidity in order to ensure safe operations and a sound financial condition under both normal and stressed market conditions and a stable long term liquidity profile.

To meet this objective, GBI performed an extensive Internal Liquidity Adequacy Assessment Process (ILAAP) in 2013 where all qualitative and quantitative aspects of liquidity risk management at the Bank were reviewed against supervisory recommendations and market best practices. The Framework was approved by the RCSB, which bears the overall responsibility at the Board level for ensuring that effective risk management is conducted by the Bank.

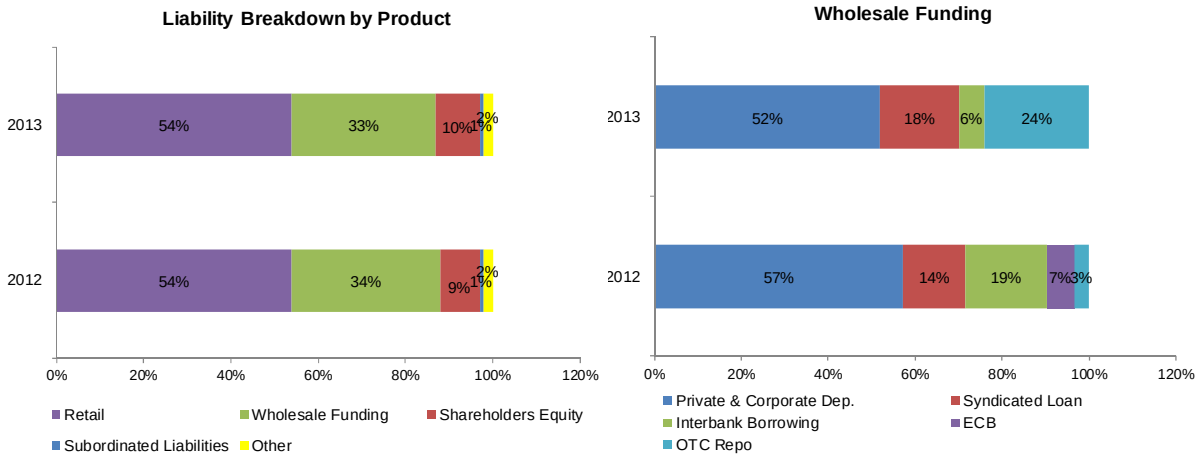
The ILAAP Framework also lays out the Bank's general funding strategy, which is determined in line with the risk appetite. The strategy is reviewed through the budget process while setting the funding plan, another component of the annual ILAAP. The Supervisory Board then monitors whether the Bank remains in line with the strategy and the plan.

At the bank level, ALCO monitors liquidity risk, implements the appropriate policies defined by the ILAAP Framework, makes pricing decisions through the Internal Transfer Pricing (ITP) process and directs the Bank's overall liquidity strategy.

GBI's funding strategy is developed, applied and adapted as necessary using the management's considerable experience and expertise as well as best market practices and regulatory requirements. The Bank aims for a well-diversified mix in terms of instrument types, fund providers, geographic markets and currencies. GBI obtains mainly unsecured funding whilst maintaining and occasionally using secured funding as a secondary option for diversification and cost management reasons. The Bank's unsecured funding comes from a balanced mix of retail and wholesale sources.

Within wholesale funding, the Bank balances the distribution between financial and non-financial counterparties. The non-financial counterparties, with which the Bank has established long lasting relationships through offering various financial services, constitute the major part of the wholesale funding. The remaining portion of wholesale funding is spread across interbank borrowing, secured funding and GBI's syndicated loan. GBI's liabilities to banks include unsecured borrowing facilities from various counterparties. The breakdown of funding sources is provided below.

Table 8-1



In terms of intragroup funding, GBI is not dependent on this funding source and conducts liquidity management independently of the parent company. Group related balances are disclosed under section 35 (Group Related Balances) of GBI's *"Annual Report 2013"*.

GBI's short term lending strategy and stable funding provide a natural mitigant for liquidity risk. The short term lending strategy enables the quick accumulation of a liquidity buffer in stressed financial environments, and the equally efficient build-up of short term assets once the stress is past. The contractual maturity breakdown of assets and liabilities, disclosed under section 33.3 (Liquidity Risk) of GBI's *"Annual Report 2013"*, demonstrates that the Bank does not carry a large maturity mismatch. 84% of loans/advances to corporate and banks, matures in less than one year.

The Bank maintains a high quality liquidity buffer as short term placements to central banks or governments in Europe and to a limited number of creditworthy counterparties, as well as investments in high quality debt securities eligible to be used in repurchase transactions with the Central Bank or in over-the counter repurchase transactions with other counterparties. The liquidity value of the debt securities is calculated using their market value and a conservative assumption of the volatility haircuts applicable in repurchase transactions.

In case of a liquidity squeeze or an emergency situation, GBI has a detailed contingency funding plan, as part of the Recovery Plan prepared by the Bank in 2013, in place to enable the Bank to govern the crisis management.

RMD performs the liquidity risk assessment, develops the required methodologies and conducts regular stress tests to ensure the Bank operates with sufficient liquidity. Liquidity risk is monitored through gap analyses, supplemented by multiple stress tests designed based on different scenarios. These analyses apply shocks with different magnitudes on the liquidity position. Scenarios are set based on bank-specific and market-wide liquidity squeezes. Behavioural analyses of the Bank's liabilities are used to determine some of the stress factors in both of these scenarios.

To ensure stable long-term funding, the Bank's cash capital measure, which shows the excess of long term funds over long term assets, is monitored, and in general, should be positive. In addition to liquidity risk limits, the Bank has established several metrics as 'Early Warning Indicators' (EWIs), which could potentially trigger management action; these include monthly deposit outflows, mismatch in the average maturities of assets and liabilities, and breaches of liquidity risk limits

All EWIs and liquidity analyses are reported to ALCO on a regular basis. ALCO reviews and plans the necessary actions to manage the liquidity gaps, and bears overall responsibility for the liquidity risk strategy. ALCO has delegated day-to-day liquidity management to the Treasury Department, which is responsible for managing the overall liquidity risk position of the Bank, and the intraday liquidity as per the principles of intraday liquidity management, established in the ILAAP Framework. The Treasury Department manages all maturing cash flows along with expected changes in business related funding requirements. The Treasury Operations Department performs the role of collateral management and executes the settlements of all transactions.

9. New Regulatory Standards

With the introduction of the Basel III, the new minimum capital requirements will be in place starting from 2014 and onwards. The Common Equity Tier 1 (CET1) requirement of 2% will be increased to 7% (4.5% plus 2.5% of capital conservation buffer), by the year 2019. In addition to that, the minimum total capital ratio requirement of 8% will be increased to 10.5% (8% plus 2.5% of capital conservation buffer). A countercyclical buffer between 0% and 2.5% will be introduced on top of these required minimums in order to achieve the broader macro-prudential goal of protecting the banking sector from

periods of excess aggregate credit growth. Finally the definition of eligible instruments for capital treatment is changed to increase the loss absorbance quality.

In addition to the changes in the minimum required solvency, a non-risk based measure, namely Leverage ratio, is established in order to limit the excessive leverages created in the financial industry. Moreover short term (Liquidity Coverage Ratio, LCR) and long term (Net Stable Funding Ratio, NSFR) liquidity standards are developed to protect the financial industry from potential liquidity shocks.

GBI has taken part in Basel III Monitoring Exercises since 2011, supervised by DNB and the Basel Committee, and the Bank has prepared a migration plan to outline the projected transition towards Basel III. The results of the monitoring exercises indicate that GBI is well-placed for the regulatory changes, as the Bank already meets the capital (minimum Core Equity Tier 1, Tier 1, Total Capital and Leverage ratios) and liquidity (minimum LCR and NSFR) requirements. The impact of the changes in the definition of capital, as well as the minimum capital requirements, is limited for GBI since the Bank has a high common equity component and no hybrid capital products. Finally, the Bank maintains a high liquidity buffer and given its strong retail funding base, the Bank expects to continue meeting both liquidity requirements.

In this context, the Bank has also prepared for the Capital Requirements Regulation (CRR) and Capital Requirements Directive IV (CRD IV), which will be effective in the European Union from 1st January 2014. GBI is positioned to be fully in line with the applicable capital and liquidity requirements under CRD IV and CRR, as for the Basel III requirements. Related new reporting requirements are being incorporated into the Bank's information systems to meet the first reporting dates in 2014.