

**BANCO LA HIPOTECARIA, S. A.
AND SUBSIDIARIES**
(Panama, Republic of Panama)

**Consolidated Financial Statements
and Consolidated Information**

June 30, 2018

(With Authorized Public Accountant Report)

(FREE ENGLISH LANGUAGE TRANSLATION
FROM SPANISH VERSION)

BANCO LA HIPOTECARIA, S. A. AND SUBSIDIARIES
(Panama, Republic of Panama)

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FREE ENGLISH LANGUAGE TRANSLATION FROM SPANISH VERSION

AUTHORIZED PUBLIC ACCOUNTANT CERTIFICATION

We have prepared the consolidated financial statements of Banco La Hipotecaria, S. A. and subsidiaries ("the Bank"), which comprise the consolidated statement of financial position as of June 30, 2018, the consolidated statements of income, comprehensive income, changes in equity and cash flows for the period, and notes, comprising a summary of significant accounting policies and other explanatory information.

We believe that the internal control procedures established in the Bank, allows us to prepare and present fairly, in all material respects, the consolidated financial position of the Bank, free from material misstatement, whether due to fraud or error.

The supplementary information included in Schedules 1 and 2 is presented for purposes of additional analysis of the consolidated financial statements and not to present the financial position nor the operational results or changes in equity of the individual companies.

The consolidated financial statements of Banco La Hipotecaria, S.A. and subsidiaries as of June 30, 2018 have been prepared internally in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Committee ("IASC").


Bolivar A. Gallardo
CPA 123-2004

June 30, 2018
Panama, Republic of Panama

BANCO LA HIPOTECARIA, S. A. AND SUBSIDIARIES

(Panama, Republic of Panama)

Consolidated Statement of Financial Position

Period ended June 30, 2018

(Stated in Balboas)

<u>Assets</u>	<u>Note</u>	<u>2018</u>	<u>2017</u>
Cash and cash equivalents		214,345	337,800
Deposits in banks:			
Demand deposits in local banks		17,049,782	17,340,520
Demand deposits in foreign banks		3,132,485	5,128,017
Savings deposits in local banks		3,529,420	1,071,053
Savings deposits in foreign banks		754,067	3,656,794
Time deposits in local banks		2,200,000	0
Time deposits in foreign banks		0	0
Total deposits in banks		26,665,754	27,196,384
Total of cash, cash equivalents and deposits in banks	7, 28	26,880,099	27,534,184
Investments in securities	8, 28	58,771,506	59,512,559
Less: Investments reserves		1,312	0
Investments, net		58,770,194	59,512,559
Loans	9, 28	635,707,559	595,098,106
Less: Allowance for loan losses	9, 28	580,996	313,625
Loans, net		635,126,563	594,784,481
Furniture, equipment and improvements, net	10	2,388,989	2,230,664
Accounts and interests receivable	11	3,462,290	3,675,649
Accounts receivable related companies		30,000	0
Tax credit	30	5,053,326	8,479,096
Deferred tax	25	1,080,062	987,891
Other assets	12	3,869,082	2,618,923
Total assets		736,660,605	699,823,447

The consolidated statement of financial position should be read along with the accompanying notes which are an integral part of the consolidated financial statements.

<u>Liabilities and Equity</u>	<u>Note</u>	<u>2018</u>	<u>2017</u>
Liabilities:			
Deposits from customers:			
Local savings	6, 28	928,170	851,096
Foreign savings	6, 28	191,414	139,388
Local time	6, 28	199,502,700	189,621,270
Foreign time	6, 28	20,165,865	17,934,223
Total deposits from customers:		<u>220,788,149</u>	<u>208,545,977</u>
Negotiable commercial papers	13, 28	85,144,947	82,931,225
Negotiable commercial notes	14, 28	102,848,222	96,309,431
Ordinary bonds	15	12,152,920	14,310,229
Investment certificates	16, 28	9,600,000	13,600,000
Other negotiable debts	17, 28	24,436,597	13,840,047
Borrowed funds	18	198,850,071	187,147,534
Deferred tax	25	0	0
Income tax payable	25	879,088	1,143,500
Accounts payable-related parties		0	0
Other liabilities	19	11,464,733	11,407,593
Total liabilities		<u>666,164,727</u>	<u>629,235,536</u>
Equity:			
Common shares	20	15,000,000	15,000,000
Treasury shares		(727,000)	0
Additional paid-in capital		25,025,329	26,300,000
Capital reserve		1,800,000	1,800,000
Fair value reserve		1,334,368	1,738,846
Currency translation reserve		(4,271,446)	(4,640,024)
Regulatory reserves		7,818,936	7,564,524
Retained earnings		23,591,482	21,932,674
Total equity of the controlling interest		<u>69,571,669</u>	<u>69,696,020</u>
Non-controlling interest	1	924,209	891,891
Total equity		<u>70,495,878</u>	<u>70,587,911</u>
Commitments and contingencies	27		
Total liabilities and equity		<u><u>736,660,605</u></u>	<u><u>699,823,447</u></u>

BANCO LA HIPOTECARIA, S. A. AND SUBSIDIARIES

(Panama, Republic of Panama)

Consolidated Statement of Income

Period ended June 30, 2018

(Stated in Balboas)

	<u>Note</u>	<u>2018</u>	<u>2017</u>
Interest and commissions income:			
Interest on:			
Loans		20,795,846	17,585,989
Investment securities		1,102,384	2,138,403
Deposits in banks		64,622	409,005
		<u>21,962,852</u>	<u>20,133,397</u>
Commission on:			
Management and servicing, net	22	2,768,803	2,749,840
Loan granting		1,215,271	1,139,594
Total interest and commissions income		<u>25,946,926</u>	<u>24,022,831</u>
Interest and commissions expense:			
Deposits		5,079,385	4,492,454
Borrowed funds		9,848,257	8,609,469
Commissions	23	616,163	782,588
Total interest expenses and commissions		<u>15,543,805</u>	<u>13,884,511</u>
Net interest and commissions income		<u>10,403,121</u>	<u>10,138,320</u>
Provision for loan losses	9	497,319	151,494
Provision for investments		51,085	0
Net interest and commission income, after provision		<u>9,854,717</u>	<u>9,986,826</u>
Income from banking services and others:			
Gain (loss) on investments, net		843,053	647,212
Other income	6, 22	1,429,596	494,539
Total income from banking services and others, net		<u>2,272,649</u>	<u>1,141,751</u>
General and administrative expenses:			
Salaries and other personnel expenses	6, 24	4,508,621	4,430,489
Depreciation and amortization	10	414,903	338,904
Professional and legal fees		1,034,856	933,949
Taxes		1,079,229	983,259
Other expenses	6, 24	2,118,952	1,972,445
Total general and administrative expenses		<u>9,156,561</u>	<u>8,659,046</u>
Net income before income tax		<u>2,970,805</u>	<u>2,469,531</u>
Income tax	25	836,644	729,744
Net income		<u>2,134,161</u>	<u>1,739,787</u>
Income attributable to:			
Controlling interest		2,116,227	1,741,376
Non-controlling interest		17,934	(1,589)
		<u>2,134,161</u>	<u>1,739,787</u>
Income per share		<u>149.52</u>	<u>115.98</u>
Diluted income per share		<u>149.52</u>	<u>115.98</u>

The consolidated statement of income should be read along with the accompanying notes which are an integral part of the consolidated financial statements.

BANCO LA HIPOTECARIA, S. A. AND SUBSIDIARIES

(Panama, Republic of Panama)

Consolidated Statement of Comprehensive Income

Period ended June 30, 2018

(Stated in Balboas)

	<u>Note</u>	<u>2018</u>	<u>2017</u>
Net income		<u>2,134,161</u>	<u>1,739,787</u>
Other comprehensive income:			
Items that are or may be reclassified to statement of income			
Fair value reserve:			
Fair value of loan portfolio acquired:			
Amortization		(39,670)	(39,761)
Valuation reserve of available for sale securities:			
Trasferred to profit or loss	8	(168,666)	(542,162)
Investment reserves		50,656	
Net change in fair value		(252,544)	1,160
Foreign currency translation differences for foreign operations		<u>382,962</u>	<u>(203,667)</u>
		<u>(27,262)</u>	<u>(784,430)</u>
Total other comprehensive income		<u>2,106,899</u>	<u>955,357</u>
Comprehensive income attributable to:			
Controlling interest		2,074,581	964,604
Non-controlling interest		<u>32,318</u>	<u>(9,247)</u>
Total comprehensive income		<u>2,106,899</u>	<u>955,357</u>

The consolidated statement of comprehensive income should be read along with the accompanying notes which are an integral part of the consolidated financial statements.

Consolidated Statement of Changes in Equity

Period ended June 30, 2018

(Stated in Balboas)

Note	Attributable to the Controlling Interest										Total equity	
	Common shares	Treasury Shares	Additional paid-in capital	Capital reserve	Investments reserve	Fair value reserve	Currency translation reserve	Regulatory reserves		Non-controlling interest		
								Dynamic provision	Specific provision in excess			Retained earnings
Balance at December 31, 2016	15,000,000	0	26,300,000	1,800,000	0	3,410,751	(4,680,536)	5,946,794	646,657	17,605,388	701,675	66,721,029
Net income	0	0	0	0	0	0	0	0	0	1,741,376	(1,569)	1,739,767
Other comprehensive income (loss):												
Fair value reserve:												
Fair value of loan portfolio acquired, net	0	0	0	0	0	(39,781)	0	0	0	0	0	(39,781)
Net change in fair value	0	0	0	0	0	(541,002)	0	0	0	0	0	(541,002)
Foreign currency translation differences for foreign operations	0	0	0	0	0	0	(196,009)	0	0	0	0	(196,009)
Total other comprehensive income (loss)	0	0	0	0	0	(580,783)	(196,009)	0	0	0	(7,658)	(784,430)
Total comprehensive income	0	0	0	0	0	(580,783)	(196,009)	0	0	1,741,376	(9,247)	955,357
Other changes in equity												
Constitution of reserves	0	0	0	0	0	0	0	0	152,499	(152,499)	0	0
Transactions with the shareholders of the Bank:												
Contributions, distributions and change in participations:												
Additional paid-in capital	0	0	0	0	0	0	0	0	0	0	0	0
Complementary tax	0	0	0	0	0	0	0	0	0	(64,112)	0	(64,112)
Non-controlling interest	0	0	0	0	0	0	0	0	0	159,770	0	159,770
Total of contributions and distributions	0	0	0	0	0	0	0	0	0	(64,112)	159,770	95,658
Balance at June 30, 2017	15,000,000	0	26,300,000	1,800,000	0	2,829,968	(4,886,545)	5,946,794	798,156	19,130,153	852,498	67,772,044
Balance at December 31, 2017	15,000,000	0	26,300,000	1,800,000	0	1,738,846	(4,640,024)	6,863,256	701,268	21,932,674	891,891	70,567,911
Impact on adopting IFRS 9												
Balance at January 1, 2018	15,000,000	0	26,300,000	1,800,000	5,746	1,738,846	(4,640,024)	6,863,256	701,268	21,824,024	891,891	70,465,007
Net income	0	0	0	0	0	0	0	0	0	2,116,227	17,934	2,134,161
Other comprehensive income (loss):												
Fair value reserve:												
Fair value of loan portfolio acquired, net	0	0	0	0	0	(39,670)	0	0	0	0	0	(39,670)
Net change in fair value	0	0	0	0	0	(421,210)	0	0	0	0	0	(421,210)
Foreign currency translation differences for foreign operations	0	0	0	0	0	0	968,578	0	0	0	14,384	382,962
Total other comprehensive income (loss)	0	0	0	0	0	(460,880)	968,578	0	0	0	14,384	(77,918)
Total comprehensive income	0	0	0	0	0	(460,880)	968,578	0	0	2,116,227	32,318	2,056,243
Other changes in equity												
Constitution of reserves	0	0	0	0	50,656	0	0	0	264,472	(264,472)	0	50,656
Transactions with the shareholders of the Bank:												
Contributions, distributions and change in participations:												
Additional paid-in capital	0	0	0	0	0	0	0	0	0	0	0	0
Decrease on additional paid-in capital	0	0	(1,274,671)	0	0	0	0	0	0	0	0	(1,274,671)
Treasury shares	0	(727,000)	0	0	0	0	0	0	0	(94,357)	0	(94,357)
Complementary tax	0	0	0	0	0	0	0	0	0	0	0	0
Non-controlling interest	0	0	0	0	0	0	0	0	0	0	0	0
Total of contributions and distributions	0	(727,000)	0	0	0	0	0	0	0	(94,357)	0	(821,357)
Balance at June 30, 2018	15,000,000	(727,000)	25,025,329	1,800,000	56,402	1,277,966	(4,271,446)	6,863,256	955,680	23,591,482	924,209	70,495,678

The consolidated statement of changes in equity should be read along with the accompanying notes which are an integral part of the consolidated financial statements.

BANCO LA HIPOTECARIA, S. A. AND SUBSIDIARIES

(Panama, Republic of Panama)

Consolidated Statement of Cash Flows

Period ended June 30, 2018

(Stated in Balboas)

	<u>Note</u>	<u>2018</u>	<u>2017</u>
Operating activities:			
Net income		2,134,161	1,739,787
Adjustments to reconcile net income and cash from operating activities:			
Provision for loan losses		497,319	151,494
Provision for investment losses		51,085	0
Realized gain on investment at fair value		(552,699)	(105,050)
(Gain) loss on sale of financial instruments		(168,656)	(542,163)
Depreciation and amortization		414,903	338,904
Gain on sale of fixed assets		0	1,714
Interest income		(21,962,852)	(20,133,072)
Interest expense		14,927,642	13,101,923
Income tax expense		836,644	729,744
Changes in operating assets and liabilities:			
Loans		(40,879,071)	(31,704,214)
Accounts receivable		(175,195)	63,961
Accounts receivable related companies		(30,000)	0
Accrual of tax credits		3,425,770	1,028,920
Other assets		(1,342,330)	(4,756,046)
Time deposits		12,113,072	7,252,123
Saving deposits		129,100	(162,216)
Other liabilities		(456,039)	71,012
Cash generated from operations:			
Interest received		22,351,406	20,143,725
Interest paid		(15,200,669)	(13,013,248)
Income tax paid		(314,850)	(462,350)
Cash flows from operating activities		<u>(24,201,259)</u>	<u>(26,255,052)</u>
Investing activities:			
Purchase of investment securities		(12,334,033)	(4,912,310)
Sale of available for sale securities		11,374,951	4,786,714
Redemption of investment securities		1,898,259	1,620,817
Purchases of furniture and equipments		(588,458)	(855,883)
Cash flows from investing activities		<u>350,719</u>	<u>639,338</u>
Financing activities:			
Proceeds of borrowed funds		47,500,000	47,450,000
Payment of borrowed funds		(35,797,463)	(19,240,536)
Proceeds from issuance of negotiable commercial papers		56,927,722	54,798,000
Redemption of negotiable commercial papers		(54,714,000)	(41,304,975)
Proceeds of issuance of negotiable commercial notes		29,167,791	20,534,000
Redemption of commercial notes		(22,629,000)	(25,372,040)
Issuance of investment certificate		0	0
Redemption of investment certificate		(4,000,000)	23,505
Issuance of negotiable debts		19,734,550	5,451,000
Redemption of negotiable debts		(9,138,000)	(7,454,819)
Redemption of ordinary bonds		(2,157,309)	(190,141)
Additional paid-in capital		(1,274,671)	0
Common shares		(727,000)	0
Non-controlling interest		14,384	152,112
Complementary tax		(94,357)	(64,112)
Cash flows from financing activities		<u>22,812,647</u>	<u>34,781,994</u>
Effect on the fluctuation of exchange rates on cash held		383,808	(190,780)
Net (decrease) increase on cash		(1,037,893)	9,166,280
Cash and cash equivalents at the beginning of the year		27,534,184	31,306,633
Cash and cash equivalents at the end of the year	7	<u>26,880,099</u>	<u>40,282,133</u>

The consolidated statement of cash flows should be read along with the accompanying notes which are an integral part of the consolidated financial statements.

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(Panama, Republic of Panama)

Notes to the Consolidated Financial Statements

June 30, 2018

(in Balboas)

(1) General information

Banco La Hipotecaria, S. A. and Subsidiaries before La Hipotecaria, S.A., was incorporated on November 7, 1996 under the law of companies of the Republic of Panama. According to Resolution S. B. P. No. 127-2010 of June 4, 2010, the Superintendence of Banks of Panama granted a General Banking License to start operations as a Bank on June 7, 2010, which allows it to carry out banking transactions in Panama and the abroad in addition to any other activity authorized by this Superintendence.

Banco La Hipotecaria, S.A. is a private bank whose shareholder is La Hipotecaria (Holding), Inc. a company incorporated under the laws of the British Virgin Islands whose main shareholder is Grupo Assa, S. A. in 69.01% (2016: 69.01%).

Through Resolution FID No. 3-97 of August 6, 1997, the Superintendence of Banks granted the Bank a fiduciary license that allows it to conduct trust business in or from the Republic of Panama. The Bank is registered with the Superintendence of the Securities Market by means of Resolution No.487-01 of December 14, 2001.

The following table provides the detail of the Bank's significant subsidiaries:

	<u>Activity</u>	<u>Country of Incorporation</u>	<u>Controlling Interest</u>	
			<u>2017</u>	<u>2016</u>
La Hipotecaria Compañía de Financiamiento, S. A.	Grant residential mortgage loans, administer residential mortgage loans in the Republic of Colombia.	Colombia	94.99%	94.99%
La Hipotecaria, S. A. de C. V.	Grant residential and personal mortgage loans, manage residential and personal mortgage loans in the Republic of El Salvador.	El Salvador	99.98%	99.98%

The main office is located on Via España, Plaza Regency, floor No. 13, Panama City.

Thereafter, Banco La Hipotecaria, S. A and its subsidiaries will be referred to as "the Bank".

(2) Basis of Preparation

(a) Statement of Compliance

These consolidated financial statements of the Bank have been prepared in conformity with International Financial Reporting Standards (IFRS) No. 34.

The Audit Committee of the Bank reviewed and authorized the issuance of these consolidated financial statements on June 30, 2018.

(b) Basis of Measurement

The consolidated financial statements have been prepared on a historical cost basis, except for the following items:

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(2) Basis of Preparation, continued

<u>Item</u>	<u>Basis of Measurement</u>
Investment in securities with changes in fair value through profit or loss (FVTPL)	Fair value
Investment in securities with changes in other comprehensive income (FVOCI) – after January 1 st , 2018	Fair value
Investment available for sale – before January 1, 2018	Fair value

(c) Functional and Presentation Currency

The consolidated financial statements are expressed in Balboas (B/) the monetary unit of the Republic of Panama, which is at par and freely exchangeable with the United States of America Dollar (US\$). The Republic of Panama does not issue its own paper currency and, instead, the United States of America Dollar is used as a legal tender. The functional currency of the subsidiary in Colombia is the Colombian peso (COP), and the functional currency of the subsidiary in El Salvador is the United States of America Dollar (US\$).

(3) Summary of Significant Accounting Policies

Except for the changes explained in the Note 3(c.2), Note 3(e) Note, 3(h), Note 3(j) and Note 3(r), the accounting policies set out below have been applied by the Bank consistently to all periods presented in these consolidated financial statements.

(a) Consolidation Basis

(a.1) Subsidiaries

The subsidiaries are participated entities controlled by the Bank. The Bank controls a subsidiary as it is exposed, or has rights, to variable returns from its involvement in the subsidiary and has the ability to affect those returns through its power over the investee. The Bank reassesses whether it has control over a participated entity if there are changes to one or more of the three elements of control. The financial statements of subsidiaries, as described in Note 1, are included in the consolidated financial statements from the date on which control commences until the date when control ceases.

(a.2) Structured Entities

A structured entity, is an entity that has been designed so that the rights to vote or similar they are not the determinant factor to decide who controls the entity, as when the rights to vote are related only to the administrative tasks and the relevant activities are directed by contractual agreements. In the evaluation to determine if

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Notes to the Consolidated Financial Statements

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(3) Summary of Significant Accounting Policies, continued

the Bank has sufficient rights to give power on these participated entities, the Bank considers factors of the participated entity; such as, its intention and design; its present aptitude to direct the relevant activities; the nature of its relation with other parts; and the exposition to the implication in the participated entity.

(a.3) Non-controlling Interests

Changes in the Bank's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

(a.4) Loss of Control

When the Bank loses control over a subsidiary, it derecognizes the assets and liabilities of the subsidiary, and any related non-controlling interest and other components of equity. Any resulting gain or loss is recognized in the statement of income. Whether the Bank retains any interest in the former subsidiary is measured at fair value when control is lost.

(a.5) Transactions Eliminated on Consolidation

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(a.6) Funds Administration

A subsidiary of the Bank acts as administrator and trustee of trust contracts at the risk of customers. The financial statements of these entities are not part of these consolidated financial statements except when the Bank has control over the entity.

(b) Foreign Currency

(b.1) Foreign Currency Transactions

Transactions in foreign currencies are translated into the respective functional currency at the current exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the current exchange rate at that date. Foreign currency differences arising on translation are generally recognized in the statement of income. However, foreign currency differences arising from the translation of available-for-sale equity instruments are recognized in after comprehensive income.

(b.2) Foreign Operations

The financial position and the results of any subsidiary in a different functional currency are translated to the presentation currency as follows:

- Assets and liabilities, at the current exchange rate at the end of the year.

Notes to the Consolidated Financial Statements

June 30, 2018

(in Balboas)

(3) Summary of Significant Accounting Policies, continued

- Revenue and expenses, at the monthly average exchange rate of the year.
- Equity accounts are measured at historical cost, at relevant exchange rate at the time of each transaction.

The resulting adjustments due to translation are recorded in a separate account directly in the consolidated statement of changes in equity, under currency translation reserve.

(c) Financial Assets and Liabilities

(c.1) Recognition

The Bank initially recognizes loans, receivables, investments, deposits, debt instruments issued, and borrowing on the date on which they are originated or date of settlement.

(c.2) Classification

Financial Assets - Policy applicable since January 1, 2018

The Bank classifies its financial assets as they are subsequently measured at amortized cost (AC), at fair value through changes in other comprehensive income (FVOCI), and at fair value through profit or loss (FVTPL), based on the business model for the management of financial assets and the contractual cash flow characteristics of financial assets.

A financial asset is measured to the AC if it meets the following two conditions and is not designated as fair value with changes in results:

- the asset is maintained within a business model whose objective is to maintain the assets to collect the contractual cash flows; and
- the contractual terms of the financial asset give rise on specific dates to the cash flows that are only payments of the principal and interest on the amount of the outstanding principal.

A debt instrument is measured at FVOCI only if it meets the following two conditions and is not designated as fair value with changes in results:

- the asset is maintained within a business model whose objective is achieved both by the collection of contractual cash flows and the sale of financial assets; and

-

Notes to the Consolidated Financial Statements

June 30, 2018

(in Balboas)

(3) Summary of Significant Accounting Policies, continued

- the contractual terms of the financial asset give rise on specific dates to the cash flows that are only payments of the principal and interest on the amount of the outstanding principal.

In the initial recognition of an equity investment that is not held for trading, the Bank may irrevocably choose to present subsequent changes in fair value in other comprehensive income. This choice is made investment by investment. All other financial assets are classified as measured at FVTPL.

In addition, in the initial recognition, the Bank can irrevocably designate a financial asset that otherwise meets the requirements to be measured at the AC or at FVOCI, as at fair value with changes in result if doing so eliminates or significantly reduces an accounting mismatch that otherwise it would arise.

Evaluation of the business model

The Bank evaluates the objective of the business model in which financial instruments are maintained at the portfolio level to reflect, in the best way, the way in which the business is managed and in which the information is provided to management. The information that was considered included:

- The policies and objectives indicated for the portfolio and the operation of those policies in practice. These include whether management's strategy focuses on collecting revenue from contractual interests, maintaining a specific interest rate profile or coordinating the duration of the financial assets with the liabilities that said assets are financing or the expected cash outflows or realize cash flows through the sale of the assets;
- The frequency, value and timing of sales in previous periods, the reasons for those sales and expectations about future sales activity.

Financial assets that are held for trading or are managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are not held to collect contractual cash flows.

Evaluation if the contractual cash flows are only capital and interest payments

For the purpose of this evaluation, "principal" is defined as the fair value of the financial asset at the time of initial recognition. "Interest" is defined as the consideration of the value of money over time and the credit risk associated with the principal amount in force at a particular time period and other basic risks of a loan agreement.

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(3) Summary of Significant Accounting Policies, continued

When evaluating whether the contractual cash flows are only principal and interest payments, the Bank will consider the contractual terms of the instrument. This includes the evaluation to determine whether the financial asset contains a contractual term that could change the period or amount of the contractual cash flows in such a way that it does not comply with this condition.

- Investments in securities held to maturity measured at amortized cost under IAS 39 will generally maintain this measurement under IFRS 9.
- Investments in equity classified as available for sale under IAS 39 will generally be measured at FVTPL under IFRS 9.

Reclassification

Financial assets are not reclassified after their initial recognition, except in the period following the modification of the business model for the administration of financial assets.

Financial Assets - Policy applicable before January 1, 2018

The Company classified its financial assets into one of the following categories:

- Loans and accounts receivable
- Maintained until expiration
- Available for sale
- Values at fair value with changes in result (VFTPL)

See note 3: f, h, e.

Financial liabilities

The Bank classifies all financial liabilities at amortized cost.

(c.3) Derecognition of financial assets and liabilities

Financial Assets

The Bank derecognizes a financial asset when the contractual rights to the cash flows of the financial asset expire, or transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the asset are transferred or in which the Bank does not transfer or substantially retain all the risks and advantages of the property and does not retain control of the financial asset.

When deregistering a financial asset, the difference between the book value of the asset (or the book value assigned to the portion of the asset derecognized) and the sum of (i) the consideration received (including any new asset obtained less any new liabilities assumed) and (ii) any accumulated gain or loss that has been recognized in other comprehensive income is recognized in results.

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(3) Summary of Significant Accounting Policies, continued

The continuous participation that takes the form of a guarantee on the transferred asset is measured by the lower of the original book value of the asset and the maximum amount of consideration that the Bank could be obliged to pay.

Financial liabilities

A financial liability is written off when the obligation extinguishes, by virtue of liability, when the obligation specified in the contract has been paid or canceled, or has expired.

(c.4) Modification of Financial Assets

Financial assets

If the terms of a financial asset are modified, the Bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to the cash flows of the original financial asset are considered expired. In this case, the original financial asset is written off in accounts and a new financial asset is recognized at its fair value

(c.5) *Offsetting Financial Assets and Liabilities*

Financial assets and liabilities are offset only for purposes of presentation in the consolidated statement of financial position when the Bank has a legally enforceable right to set off the amounts and intends either to settle them on a net basis, or to realize the asset and settle the liability simultaneously. Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions derived from financial instruments at FVTPL

(d) *Fair Value Measurement*

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When applicable, the Bank measures fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active, if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

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(3) Summary of Significant Accounting Policies, continued

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price. If the Bank determines that the fair value in the initial recognition differs from the transaction price and the fair value is not evidenced by a quoted price in an active market for an identical asset or liability, nor is it based on a valuation technique for which is judged to be insignificant in relation to measurement, then the financial instrument is measured initially at its fair value, adjusted to defer the difference between the fair value at the initial recognition and the transaction price. Subsequently, that difference will be recognized in results on an adequate basis over the useful life of the instrument, but at the latest when the valuation is fully supported by observable market data or when the transaction is closed.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Bank recognizes transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

(e) Deterioration

Policy applicable since January 1, 2018

The Bank recognizes the reserve for expected credit losses (ECL) in the following financial instruments that are not measured at FVTPL:

- Loans receivable
- Debt instruments

Loss due to impairment in equity investments is not recognized.

The Bank measures reserves for losses in an amount equal to the expected credit losses during the life time, with the exception of the following ones, for which they are measured as expected credit losses during the next 12 months:

- Investments in debt instruments that are determined to reflect low credit risk at the reporting date; and
- Other financial instruments over which the credit risk has not increased significantly since its initial recognition.

The 12-month ECL is the portion of the ECL that results from loss events that are possible on a financial instrument within a period of 12 months after the reporting date.

Measurement of the ECL

The ECL is the estimated weighted probability of credit loss and is measured as follows:

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Notes to the Consolidated Financial Statements

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(3) Summary of Significant Accounting Policies, continued

- Financial assets that do not show credit deterioration at the reporting date: the present value of all arrears of contractual cash payments (eg the difference between the cash flows owed to the Bank according to the contract and the cash flows that the Bank expects to receive);
- Financial assets that are impaired at the reporting date: the difference between the book value and the present value of the estimated future cash flows;

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced by a new one due to financial difficulties of the debtor, then an assessment is made as to whether the financial asset should be derecognized and PCEs measured. as follows.

- If the expected restructuring does not result in the derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included when calculating the cash deficits of the existing asset.
- If the expected restructuring will result in the derecognition of existing assets, then the expected fair value of the new asset is treated as the final cash flow of the existing financial asset at the time of derecognition. This amount is included when calculating the cash deficits of the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Financial assets with credit deterioration

At each reporting date, the Bank evaluates whether the financial assets accounted for by AC and the financial assets measured by FVOCI have credit impairment. A financial asset has "credit deterioration" when one or more events occur that have a negative impact on the expected future cash flows of the financial asset.

Evidence that a financial asset has credit impairment includes the following observable data:

- Significant financial difficulty of the debtor or issuer;
- A breach of contract, such as an event of non-payment or default;
- The restructuring of a loan or advance from the Bank in terms that the Bank would not consider otherwise;

evaluates whether the financial assets accounted for to AC and the financial assets measured to FVOCI have credit deterioration. A financial asset has "credit deterioration" when one or more events occur that have a negative impact on the expected future cash flows of the financial asset.

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(3) Summary of Significant Accounting Policies, continued

When evaluating whether an investment in sovereign debt has credit deterioration, the Bank considers the following factors.

- The evaluation of the market on solvency reflected in the yields of the bonds.
- The solvency assessments of rating agencies.
- The capacity of the country to access the capital markets for the issuance of new debts.
- The probability that the debt will be restructured, which causes the holders to suffer losses through the cancellation of the voluntary or mandatory debt.

Presentation of the reserve for ECL in the consolidated statement of financial position

The reserves for ECL are presented in the consolidated statement of financial position as follows:

- Measured financial assets AV: as a deduction from the gross book value of the assets;
- Financial assets measured at FVTPL: no loss is recognized in the consolidated statement of financial position because the carrying amount of these assets is their fair value. However, the reserve for ECL is disclosed and recognized in the fair value reserve.

Impairment losses - Write-offs

Loans and investments in securities are written off (either partially or totally) when there is no reasonable expectation of recovery. This is generally the case when the Bank determines that the debtor has no assets or sources of income that could generate sufficient cash flows to pay the amounts owed subject to the impairment loss, without the Bank's course of action to recover the collateral (in the case that they maintain). However, financial assets that are written off may still be subject to legal actions for the recovery of the amounts owed.

Deterioration - Policy applicable before January 1, 2018

The Company evaluates, at each reporting date, whether there is any objective evidence of impairment of a loan or loan portfolio. The amount of losses on loans determined during the period is recognized as a provision expense in the consolidated statement of income and increases an account of allowance for loan losses. The reserve is presented deducted from the loans receivable in the consolidated statement of financial position. When a loan is determined as uncollectible, the irrecoverable amount is reduced from the aforementioned reserve account.

Impairment losses are determined using two methodologies to determine whether there is objective evidence of impairment, that is, individually for loans that are individually significant and collectively for loans that are not individually significant.

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(3) Summary of Significant Accounting Policies, continued

- Individually Evaluated Loans

Impairment losses on individually assessed loans are determined based on an exposure assessment on a case-by-case basis. If it is determined that there is no objective evidence of impairment, for an individually significant loan, it is included in a group of loans with similar characteristics and is evaluated collectively for impairment. The impairment loss is calculated by comparing the present value of the expected future cash flows, discounted at the original effective rate of the loan, against its current carrying amount and the amount of any loss is recognized as a provision for loan losses in the consolidated statement of results. The book value of the impaired loans is reduced from the reserve account.

- Collectively Evaluated Loans

For the purposes of a collective assessment of impairment, the Company primarily uses statistical models of historical trends of probability of default, the timing of recoveries and the amount of the loss incurred, and makes an adjustment if current economic and credit conditions are such that the real losses are likely to be greater or less than those suggested by historical trends. The default rates, loss rates and the expected term of future recoveries are regularly compared against actual results to ensure that they remain appropriate.

- Reversal due to deterioration

If in a subsequent period, the amount of the impairment loss decreases and the decrease could be objectively related to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed by decreasing the reserve account for loan impairment. The amount of any reversal is recognized in the consolidated statement of income.

- Reserve for Contingent Loans Risk

The Bank uses the reserve method to provide for possible losses on contingencies of a credit nature. The reserve is increased based on a provision that is recognized as a provision expense in the consolidated statement of income and is reduced by write off related to these contingencies of a credit nature.

- Renegotiated or Restructured Loans

The renegotiated or restructured loans are those to which a renegotiation or restructuring has been made due to any deterioration in the debtor's financial condition, and where the Bank considers granting a change in the credit parameters.

Designation at fair value with changes in results
Financial assets

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(3) Summary of Significant Accounting Policies, continued

In the initial recognition, the Bank has designated certain financial assets as FVTPL because this designation eliminates or significantly reduces an accounting asymmetry, which would otherwise increase.

Prior to January 1, 2018, the Bank also designated certain financial assets as measured at FVTPL because the assets were managed, evaluated and reported internally.

(f) Cash and Cash Equivalents

For purpose of the consolidated statement of cash flows, cash equivalents include demand deposits with banks and term deposits with original maturities of three months or less, excluding restricted deposits.

(g) Negotiable assets and liabilities

Negotiable assets and liabilities are those that the Bank acquires or contracts mainly for the purpose of selling or repurchasing in the short term, or they are maintained as part of a portfolio that is jointly administered for taking positions or short-term gains.

Negotiable assets and liabilities are initially recognized and subsequently measured at fair value in the consolidated statement of financial position, with transaction costs recognized in profit or loss. All changes in fair value are recognized as part of net marketable income in results.

(h) Loans

Policy applicable since January 1, 2018

Loans are non-derivative financial assets with fixed determinable payments that are not quoted in the active market, and are generally originated by providing funds to debtors and the Bank does not intend to sell immediately or in the near term. Loans are reported at their principal amounts outstanding, less unearned interest and the allowance for impairment. Unearned interest on loans are accrued to income during the life of the loans under the effective interest method.

Loans are presented at amortized cost considering the principal amount outstanding, less unearned interest and the allowance for expected losses. Loans are initially measured at fair value plus the incremental direct cost attributable to the transaction and later carried at amortized cost under the effective interest method.

Policy applicable before January 1, 2018

Loans are non-derivative financial assets with fixed determinable payments that are not quoted in the active market, and are generally originated by providing funds to debtors and the Bank does not intend to sell immediately or in the near term. Loans are reported at their principal amounts outstanding, less unearned interest and the allowance for impairment. Unearned interest on loans is accrued to income during the life of the loans under the effective interest method.

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(3) Summary of Significant Accounting Policies, continued

(i) Allowance for Expected Credit Losses

The allowance for credit losses is set up to cover the losses arising from the credit origination process, inherent to the portfolio of loans and loan commitments, as well as the portfolio of investment securities measured at AC and FVOCI, using the reserve method for ECL. The increases to the reserve for ECL are made with charge to results. The ECL are deducted from the reserve, and subsequent recoveries are added. The reserve is also reduced by reversals of the reserve with credit to results.

The reserve attributable to the financial instruments measured to AC is presented as a deduction to the loans, the reserve for ECL. The reserve for ECL of the investment in securities measured at FVOCI is presented in the fair value reserve in other comprehensive income.

The Bank measures the ECL in a way that reflects: a) an unbiased weighted probability amount that is determined by evaluating a range of possible outcomes; b) the value of money over time; and c) reasonable and sustainable information that is available without cost or disproportionate effort on the date of the presentation about past events, current conditions and the forecast of future economic conditions.

The ECL model reflects the general pattern of deterioration or improvement in the credit quality of financial assets. The amount of ECL recognized as a reserve or provision depends on the degree of credit deterioration since the initial recognition. There are two evaluation criteria:

- 12-month PCE (stage 1), which applies to all financial assets (on initial recognition), provided there is no significant deterioration in credit quality, and
- ECL during the life time (stages 2 and 3), which is applied when there has been a significant increase in credit risk individually or collectively. In these stages 2 and 3 interest income is recognized. In stage 2 (as in stage 1), there is a total dissociation between the recognition of interest and impairment and the interest income is calculated on the gross amount in books. In stage 3, when the financial asset subsequently becomes impaired (where a credit event has occurred),

The provision for PCE includes a specific active component and a component based on a formula.

The specific active component, or of the specific assignment, refers to the provision for losses in financial assets considered impaired and evaluated individually, case by case. A specific provision is established when the discounted cash flows (or observable fair value of collateral) of the financial asset is less than the book value of that asset. The component based on the formula (collective tax base) covers the normal credit portfolio of El Banco and is established based on a process that estimates the probable loss inherent in the portfolio, based on the statistical analysis and qualitative judgment of the administration. This analysis takes into account the complete

Summary of Significant Accounting Policies, continued

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(3) Summary of Significant Accounting Policies, continued

information that incorporates not only default data, but other relevant credit information, such as prospective macroeconomic information.

In order to determine whether there has been a significant increase in the credit risk of the financial asset, the evaluation is based on quantitative information and qualitative information. The Bank considers the following factors, although not exhaustive, in measuring the significant increase in credit risk:

- a) Significant changes in credit risk indicators as a result of a change in credit risk from the beginning;
- b) Significant changes in the indicators of the external credit risk market for a specific financial instrument or similar financial instruments with the same expected life;
- c) A real or expected significant change in the external credit rating of the financial instrument;
- d) Significant changes in the value of collateral that supports the obligation;

As a cap, the Bank considers that a significant increase in credit risk occurs when an asset has more than 90 days delinquent, for personal loans or, for Mortgage loans, more than 180 days past due. The days due are determined by counting the number of days elapsed since the oldest due date with respect to which the total payment has not been received. The due dates are determined without considering any grace period that may be available to the debtor.

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk through periodic reviews, to confirm that:

The balances of the reserves for PCE are calculated by applying the following formula:

$$\text{PCE} = \Sigma (\text{ED} \times \text{PD} \times \text{LD}); \text{ where:}$$

- Exposure to default (ED): is defined as the current balance of the principal at the date of the statement of financial position. In the case of credits or loans that include a line of credit with a quota that can be used in its entirety in the form of loan contracts, this parameter includes the Bank's expectations of future disbursements incorporating a credit conversion factor (CCF).
- Probability of default (PD): the probability that a client will not comply with the total and timely payment of credit obligations within a one-year horizon. The estimated PD for a period of 12 months is adjusted by the loss identification period (LIP) to estimate the probability of default

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(3) Summary of Significant Accounting Policies, continued

- The probability of default of one year applied to the portfolio for expected losses for less than 12 months and during the life time for expected losses greater than 12 months. The default rates are based on the historical performance of the Bank's portfolio by rating category, supplemented by the probabilities of default of an International Risk Rating Agency.
- Loss of non-compliance (LD) = a factor based on historical information is used.

(j) Investments in Securities

Policy applicable since January 1, 2018

Investments in securities presented in the consolidated statement of financial position include:

- Investment in securities in debt instruments measured to the AC. These are initially measured at fair value plus the incremental direct costs of the transaction, and subsequently at their amortized cost using the effective interest method;
- Investment in securities in debt and equity instruments mandatorily designated and measured at FVTPL. These are measured at fair value with changes recognized immediately in results;
- Investment in securities in instruments measured at FVOCI

For the debt instruments measured at FVOCI, gains and losses are recognized in the consolidated statement of comprehensive income, except for the following, which are recognized in results in the same way as for financial assets measured at amortized cost:

- Interest income using the effective interest method;
- Reserves and reversals of expected credit losses.

When the investments in securities measured at the FVOCI are derecognised, the accumulated gain or loss previously recognized in the consolidated statement of comprehensive income is reclassified from equity to income.

Policy applicable before January 1, 2018

Investment securities are initially measured at fair value plus, incremental costs related to the transaction, except for securities at fair value through profit or loss, and subsequently accounted based on the maintained classifications according to the characteristics of the instrument and purpose for which its acquisition was determined. The classifications used by the Bank are detailed below:

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(3) Summary of Significant Accounting Policies, continued

- *Held-to-Maturity*

Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank's has the positive intent and ability to hold to maturity.

Held-to-maturity investments owned by the Bank consist of debt instruments, which are carried at amortized cost using the effective interest method, less any impairment losses. A sale or reclassification that is not insignificant in relation to the amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale, and would prevent the Bank from classifying investment securities as held-to-maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- Sales or reclassifications that are close to the maturity date or the redemption date of the financial asset because changes in the market interest rate would not have a significant effect on the financial asset's fair value.
- Sales or reclassifications after the Bank has collected substantially all of the asset's original principal.
- Sales or reclassifications that are attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

- *Securities at Fair Value through Profit or Loss*

This category includes those investments securities acquired mainly for the purpose of generating a profit from short - term fluctuations in the price of the instrument. These securities are measured at fair value and changes in fair value are recognized in the consolidated statement of income in the period in which they are generated.

- *Securities Available-for-Sale*

This category includes those investments securities acquired with the intention to be held for an indefinite period of time, which may be sold in response to the needs of liquidity or changes in interest rates, exchange rates or equity prices. These securities are measured at fair value and changes in fair value are recognized in consolidated statement of changes in equity and presented in the fair value reserve within equity, until these securities are sold, redeemed, or impaired, in which case, the accumulated gain or loss in other comprehensive income is reclassified the consolidated statement of income.

When the fair value of investments in equity instruments cannot be reliable, investments remain at cost.

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(3) Summary of Significant Accounting Policies, continued

Impairment of Securities Available for Sale

The Bank assesses at each consolidated statement of financial position date whether there is objective evidence that investment securities are impaired. In the case, of securities classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired.

If any such evidence exists for securities available-for-sale, the losses accumulated is reclassified from equity to the consolidated statement of income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized then the impairment loss is reversed through the consolidated statement of income.

(k) Furniture, Equipment and Improvements

Furniture, equipment and improvements include buildings, furniture and equipment used by branches and offices of the Bank. All furniture, equipment and improvements are measured at cost less accumulated depreciation and amortization. The historic cost includes the expense that is directly attributable to the acquisition of the asset.

Subsequent expenditure is capitalized only when it is probable that the future economic benefits of the expenditure will flow to the Bank. Ongoing repairs and maintenance are expensed as incurred. Cost considered as repairs and maintenance is charged to the consolidated income statement during the financial period that they are incurred.

The depreciation expense of furniture and equipment, and amortization of improvements to the leased property is charged to current period using the straight-line method over the estimated useful life. The estimated useful life of assets is summarized as follows:

- Furniture and equipment	3 - 10 years
- Vehicles	5 years
- Improvements	3 - 10 years

The assets' useful lives and residual value are reviewed, and adjusted if appropriate, at each consolidated statement of financial position date. Furniture and equipment are subject to review for impairment when there are events or changes in the circumstances that indicate that the carrying value may not be recoverable. An asset's carrying amount is written-down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

(l) Assets Classified as Held for Sale

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(3) Summary of Significant Accounting Policies, continued

Non-current assets, or disposal groups comprising assets and liabilities, that are expected to be recovered primarily through sale rather than through continuing use, are classified as held for sale. Immediately before classification as held for sale, the assets, or components of a disposal group, are remeasured in accordance with the Bank's accounting policies. Thereafter generally the assets, or disposal group, are measured at the lower of their carrying amount and fair value less cost to sell. An impairment loss is recognized due to reductions in the initial value of such assets. Impairment losses on initial and subsequent classification as held for sale are recognized in the consolidated statement of income.

(m) Deposits, Borrowed Funds and Debt Securities Issued

These financial liabilities correspond to the Bank's main sources of debt funding. They are initially measured at fair value less incremental direct transaction costs, and subsequently are measured at amortized cost using the method of effective interest rate.

(n) Share based payments

The fair value at the date of granting options of the Holding's share purchase plan of Bank employees is recognized as a personnel expense, with the corresponding increase in the account payable to the Holding, within the vesting period in which employees acquire unconditional rights over the shares. The amount recognized as an expense is adjusted to reflect the amount of concessions, which will effectively meet the conditions of service.

(o) Employee Benefits

(o.1) Termination Benefits

Termination benefits are recognized as expenses between whichever occurs first when the Bank can no longer withdraw the offer of those benefits and when the Bank recognizes costs for a restructuring. If benefits are not expected to be wholly settled within twelve months of the consolidated statement of financial position, then such benefits are discounted to determine their present value.

(o.2) Short-term Employee Benefits

Short-term employee benefits are expensed as the related service is provided. A liability is recognized for the amount expected to be paid if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(p) Earnings per Share

Basic earnings per share is calculated by dividing the profit or loss that is attributable to ordinary shareholders of the Bank by the weighted-average number of ordinary shares outstanding during the period.

(q) Segment Reporting

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(3) Summary of Significant Accounting Policies, continued

A business segment is a main component of the Bank, whose operating results are regularly reviewed by management for decision making about resources to be allocated to the segment and evaluate its performance, and for which we have available financial information for this purpose.

The business segments presented in the consolidated financial statements correspond to a main component of the Bank responsible for providing a single product or service or a group of related products or services within a particular economic environment and that is subject to risks and returns that are different from the other business segments.

(r) Interest Income and Expense

Policy applicable since January 1, 2018

Effective interest rate

Interest income and expenses are recognized in income using the effective interest method. The "effective interest rate" is the rate that accurately discounts estimated future cash payments or collections over the expected life of the financial instrument for:

- The gross carrying amount of the financial asset; or
- The amortized cost of the financial liability.

When calculating the effective interest rate for financial instruments other than assets with credit deterioration, the Bank estimates the future cash flows considering all the contractual terms of the financial instrument, but not the ECL. In the case of financial assets with credit impairment, the effective interest rate adjusted for the credit is calculated using the estimated future cash flows including the ECL.

The calculation of the effective interest rate includes the transaction costs, fees and premiums or discounts paid or received which are integral parts of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issuance of a financial asset or a financial liability.

Amortized cost and gross balance in books

The amortized cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured in the initial recognition less the payments to principal, plus or minus the accumulated amortization using the effective interest method of any difference between the initial amount and the amount at maturity and, for financial assets, adjusted for any expected credit loss.

The gross carrying amount of a financial asset is the amortized cost of a financial asset before adjusting for any reserve for ECL.

Calculation of interest income and expenses

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(3) Summary of Significant Accounting Policies, continued

When calculating interest income and expenses, the effective interest rate is applied to the gross carrying amount of the asset (when the asset has no credit impairment) or to the amortized cost of the liability.

For financial assets that present a deteriorated credit after their initial recognition, interest income is calculated by applying the effective interest rate on the gross amount of the financial asset.

Presentation

The income and interest expenses presented in the consolidated statement of income and in the consolidated statement of comprehensive income include:

- Interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis;
- Interest on debt instruments measured at fair value with changes in other comprehensive income calculated on an effective interest basis;

Interest income and expenses on all negotiable assets and liabilities are considered incidental to the Bank's trading operations and are presented together with all other changes in the fair value of the assets and liabilities in the net income.

Interest income and expenses on other financial assets and financial liabilities at FCTPL are presented in the net income of other financial instruments measured at FVTPL.

Policy applicable before January 1st, 2018

Interest income and expense are recognized in the consolidated statement of income using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes commissions, transaction costs and fees, and any premium paid or discount received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue or disposal of a financial asset or financial liability.

Interest income and expense presented in the consolidated statement of income and include:

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(3) Summary of Significant Accounting Policies, continued

- Interest on financial assets and financial liabilities measured at amortized cost calculated on an effective interest basis.
- Interest on available-for-sale investment securities calculated on an effective interest basis.

(s) Fees and Commission

Income and expenses from fees and commissions, both paid and received, other than those included in determining the effective interest rate, include banking services, premium and other service fees, administration and management of accounts which are recognized as the related services are performed or received.

The Bank receives recurrent income related to management services of trusts. These incomes are registered under the accrual method. Its obligation of the Bank to manage the resources of the trusts in conformity with the contracts and independent of its equity.

(t) Trusts Operations

Assets held on trusts or in function of the trustee are not considered part of the Bank and therefore, those assets and its corresponding income are not included in the consolidated financial statements presented. Its obligation of the Bank to manage the resources of the trusts in conformity with the contracts and independent of its equity.

The Bank charges a commission for the trust management of the funds in the trusts, which is paid by the trustees under the basis of the balance that the trusts have or with an agreement between the parties. These commissions are recognized to income under the terms of the trusts contracts monthly, quarterly, or annually under the accrual basis.

(u) Net Income from as Financial Instruments at Fair Value through Profit or Loss

Net income from other financial instruments at fair value through profit or loss relates to non-trading derivatives held for risk management purposes that do not form part of qualifying hedge relationships and financial assets and financial liabilities designated at fair value through profit or loss. It includes all realized and unrealized fair value changes, interest, dividends and foreign exchange differences.

(v) Income tax

Current income tax is the expected tax payable on the taxable income for the year using tax rates enacted at the consolidated statement of financial position date, and any adjustment to the tax payable in respect of previous years.

Deferred income tax represents the amount of income tax payable and/or receivable in future years resulting from temporary differences between the carrying accounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, using the tax rates enacted at the consolidated statement of financial position

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(3) Summary of Significant Accounting Policies, continued

date. These temporary differences are expected to be reversed in future years. If it is determined that the deferred tax would not be realized in future years, the deferred tax will be totally or partially reduced.

(w) New IFRSs and Interpretations that have not been yet adopted

To the date of these consolidated financial statements, there are IFRS that have not been applied in the preparation of the statements:

- IFRS 16 "Leases". On January 13, 2016, IFRS 16 "Leases", which replaces the current, IAS 17 "Leases" was issued. IFRS 16 eliminates classification of leases either as operating leases or finance leases for the lessee. Instead, all leases are recognized similarly to finance leases under IAS 17. Leases are measured at the present value of future lease payments and are presented as either leased assets (right of use assets) or along with property, furniture and equipment. IFRS 16 is effective for annual periods beginning on or after January 1, 2019. Early adoption is permitted for entities that also adopt IFRS 15 "Revenue from Contracts with Customers".

Due to the nature of the financial operations of the Bank, the adoption of this norm will not have a significant impact on the financial statements, an aspect that is under evaluation by the administration.

(4) Financial Risk Management

A financial instrument is any contract that originates a financial asset in one entity and a financial liability or equity instrument in another entity. The Bank's activities are mainly related to the use of derivative financial instruments and therefore, the consolidated statement of financial position is comprised mainly of financial instruments. These instruments expose the Bank to various types of risk, for which the Bank Board has established certain committees for administration and regular monitoring of risks to which the Bank is exposed. To manage and monitor these risk, the Board has established the following committees, which are the following:

- Credit Committee
- Collections Committee
- Audit Committee
- Compliance Committee
- Risk Committee
- Asset and Liability Committee (ALCO)

The Audit Committee of the Bank supervises the way in which Management monitors the compliance of the policies and procedures of risk management and reviews if the risk management framework is appropriate in respect of the risks that the Bank confronts.

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(4) Financial Risk Management, continued

This Committee is assisted by Internal Audit in its supervision role. Internal Audit makes periodic revisions of the controls and procedures of risk management, and these results are reported to the Audit Committee.

The Bank's Risk Committee main responsibilities are the following:

1. Oversight of the performance and independence of the Risk Department of the Bank, according to its role.
2. To monitor the risk expositions and compare those expositions to the risk limits approved by the Board of Directors; as to bring to the Board of Directors the presented results.
3. To develop and to propose methodologies, procedures, limits and strategies for the administration of the risks; as well as to propose improvements to the risk management policies.
4. Issue recommendations to support the maintenance and/or improvement of the risk qualification of the Bank.
5. Periodically, as well as prior to performing assets and liabilities operations with large entities, to help management quantify the possible losses which the Bank might incur, in case of an operation is carried out.
6. To propose contingency plans on the risks subject, which will be submitted to the approval of the Board of Directors and to recommend courses of action or mechanisms which can normalize any situation in which the Bank has left of the established limits.
7. To watch that the management of the Bank promotes the culture of risk management.
8. Develop and maintain the Bank's risk classifications to categorize exposures according to the degree of default risk. The current risk rating framework consists of 8 levels on default that reflect different degrees of default risk for the loan portfolio segments. These ratings are associated or related to the delinquency presented by the loan instrument. While the Bank adopts the inclusion of a behavioral credit scoring, the ratings will be based on the delinquency.
9. Develop and maintain Bank processes to measure ECL, this includes processes for initial approval, regular validation and retrospective testing of the models used; and incorporation of prospective information.

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(4) Financial Risk Management, continued

The main risks identified by the Bank are credit, liquidity, market and operational risk, which are described as follows:

(a) Credit Risk:

Is the risk that the debtor, issuer or counterpart of a financial asset owned by the Bank does not fully and timely comply with any payment due to the Bank, in conformity with the agreed upon terms and conditions, when the financial asset was acquired or originated by the Bank. Also this risk is conceived as an impairment in the credit quality of the counterpart, of the collateral and/or of the guarantee agreed initially.

To mitigate the credit risk, the risk management policies establish processes and controls to follow for loans approvals or credit facilities. The Bank structures the levels of credit risk acceptable by the establishment of limits over the quantity of accepted risk in relation to only one borrower, or group of borrowers, and geographic segment. These credits are controlled constantly and subject to a periodic revision.

Exposure to credit risk is also managed through a periodic analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits when appropriate. The exposure to credit risk is also mitigated through collaterals, corporate, and personals obtained by the Bank.

Risk management is carried out under policies approved by the Board of Directors; these policies are reviewed and modified to reflect changes in markets, regulations, and other factors to consider in the formulation of these policies.

The Bank has several risk assessment reports to evaluate the performance of their credit portfolio, allowance requirements, and especially to anticipate the circumstances that can affect the repayment ability of their borrowers.

The Board of Directors has delegated the responsibility for the management of the credit risk in the Credit Committee, Administration of Credit Committee, Risk Committee, Collections Committee which watch periodically the financial condition of the debtors and respective issuers, who involve a credit risk for the Bank.

Credit Quality Analysis

The following table presents information on the credit quality of the financial assets measured to the AC and the investments in securities measured to the FVOCI. Unless specifically indicated, for financial assets, the amounts in the table represent the gross book values. For the promissory letters, the amounts in the table represent the amounts committed:

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(4) Financial Risk Management, continued

	2018			2017	
	ECL next 12 months	ECLPCE during life (not impaired)	ELC during life (impaired)	Total	Total
Loans					
Low-fair risk	612,891,498	0	0	612,891,498	576,584,739
Watch list	15,914,896	0	0	15,914,896	12,839,884
Substandard	0	868,288	274,038	1,142,326	1,272,508
Doubtful	0	2,128,168	429,337	2,557,505	1,567,064
Loss	0	0	3,201,334	3,201,334	2,833,911
Gross Amount	628,806,394	2,996,456	3,904,709	635,707,559	595,098,106
Allowance for impairment	(161,814)	(119,732)	(299,450)	(580,996)	(313,625)
Net carrying amount	<u>628,644,580</u>	<u>2,876,724</u>	<u>3,605,259</u>	<u>635,126,563</u>	<u>594,784,481</u>
Investment in securities at AC					
Low-fair risk	430,337	0	0	430,337	442,132
Gross Amount	430,337	0	0	430,337	442,132
Allowance for impairment	(1,312)	0	0	(1,312)	0
Net carrying amount	<u>429,025</u>	<u>0</u>	<u>0</u>	<u>429,025</u>	<u>442,132</u>
Investment in securities at FVOCI					
Low-fair risk	42,772,492	0	0	42,772,492	43,933,581
Promissory Letters					
Low-fair risk	73,902,870	0	0	73,902,870	77,155,573

At June 30, 2018, the Bank made the analysis based on the required on the Agreement No.4-2013 which regulates off-balance accounts. Of the total off-balance accounts, 100% correspond to revocable promissory letters. The total of the promissory letters are classified in the low-fair risk category.

Deposits placed in banks

As June 30, 2018, the Bank held deposits placed in banks for B/.26,665,754 (2017: B/.27,196,384). These deposits are held with banks and financial institutions that are rated with investment grade of at least BBB- and BBB+, based on Fitch Ratings Inc., Moodys and Standard & Poors.

Collateral held and Other Credit improvement and their Financial Effect

The Bank held collateral and other credit to secure the payment of its financial assets exposed to credit risk improvements. The table below presents the main types of collateral held by different types of financial assets.

	% of coverage subject to requirements of Collaterals		Type of Collateral
	2017	2016	
Loans	92%	92%	Properties
Investment securities	76%	77%	Mortgage loans

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(4) Financial Risk Management, continued

Residential mortgage loans

The tables below stratify credit exposures from mortgage loans by ranges of loan-to-value (LTV) ratio. LTV is calculated as the ratio of the gross amount of the loan to the value of the collateral. The value of the collateral for residential mortgage loans is based on the collateral value at origination and generally is not updated.

<u>LTV ranges</u>	<u>2018</u>	<u>2017</u>
0-20%	564,902	500,763
20-40%	5,135,460	4,810,538
40-60%	27,079,154	24,400,710
60-80%	184,646,835	168,193,621
80-100%	364,853,825	349,265,979
Total	582,280,176	547,171,611

The Bank does not update its collateral valuation routinely. The appraisals on the collaterals are updated when the credit risk of a loan becomes significantly impaired and the loan is under close supervision. For loans that are doubtful to recover, the Bank obtains appraisals for collaterals because it is an input for measuring impairment.

Assets obtained by taking possession of collateral

Details of non-financial assets obtained by the Bank during the period by taking possession of collateral held as security against loans and advances as well as calls made on credit enhancements and held at period end are shown below:

	<u>2017</u>	<u>2016</u>
Properties	<u>279,839</u>	<u>270,110</u>

Amounts arising from expected credit losses

Significant increase in credit risk

In assessing whether the credit risk of the loan portfolio has increased significantly, the Bank considers the change in default risk that occurs since the initial recognition. For a financial instrument that incurs an event of default, the management will consider the criteria based on the different defaulting states as established for the implementation of the Expected Loss, while evaluating the application of other criteria used in the internal credit risk model such as behavior scoring, bureau score and / or aspects and qualitative factors, when appropriate. At each reporting date, the Bank evaluates whether there is a significant increase in credit risk based on the change in default risk that occurs during the expected life of the loan instrument. In order to assess whether significant credit deterioration has occurred, the Bank considers reasonable and sustainable information that is available without cost or disproportionate effort, comparing:

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(4) Financial Risk Management, continued

- The default risk that occurs in the financial instrument on the reporting date,

Degree of credit risk for the credit portfolio

The Bank assigns a credit risk rating to each exposure based on the delinquency transitions that the operation generates. These migrations are assigned a Probability of Default based on the results of 66 transition matrixes that were reviewed at 1, 2 and 3 years, which gives a real default rate based on the default of the operation. As explained above, the Bank is in the process of adapting other variables in addition to the actual default rate, such as credit behavior scoring, bureau scoring and / or collective factors depending on the economic events that can be registered in sectors of the economy.

Credit risk ratings are defined and calibrated so that default risk increases exponentially as credit risk deteriorates, for example, the difference in default risk between credit risk grades 1 and 2 is lower than the difference between grades 2 and 3.

A credit risk rating is assigned to each exposure on the initial recognition based on the information available about the debtor. Exposures are subject to continuous monitoring, which may cause an exposure to move to a different credit risk rating.

Consequently, and according to the impairment of risk suffered by each instrument throughout its residual life, the Bank periodically from the date of the initial recognition, will establish the differences in the risk status of that exposure with the registered in the initial recognition. Based on the evaluation carried out, the Bank will assign each instrument to 3 stages of deterioration (buckets):

- a) Bucket 1 (B1): Instruments with low credit risk
- b) Bucket 2 (B2): Instruments with significant impairment of credit risk
- c) Bucket 3 (B3): Impaired instruments (high credit risk)

The objective of the assignment to different credit risk stages is the adjustment of the expected loss calculation algorithm, so that when the instruments have been assigned to Bucket 1, these losses will be determined for a 12-month horizon. The losses for instruments assigned to Bucket 2 or 3, will be calculated for the residual life of the instruments, which is until their maturity or lifetime.

The Bank, in the first phase of application of the Standard, as long as it did not have a structure of internal qualifications that would allow to assess the impairment, will adopt, as a general criterion, the one established by the Standard in B5.5.17 (p). : "Information about delinquency, including the rebuttable presumption [...]"

The foregoing implies that the Bank will use the schedule of arrears ranges for the allocation, according to the following order of ratings:

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(4) Financial Risk Management, continued

- A1 - Current range (current, no delay) and 1 to 30 days
- A2 - 31 to 60 days range
- B1 - 61 to 90 days range
- B2 - 91 to 120 days range
- C1 - 121 to 150 days range
- C2 - 151 to 180 days range
- D - Greater than 180 days range

Construction of the term of probability of default (PD) of the credit portfolio

Instrument treatment approach

Given the homogeneity of the profiles of borrowers in the Bank's credit portfolios, in order to determine the credit deterioration of the instruments that constitute them, it was established that in a general manner, with exceptions, they will be treated under a collective approach. For practical purposes this implies that the determined PD and LGD values will be shared collectively, either partially or totally, by all the instruments that participate in each identified segment.

The Bank has identified that its instruments present similar risk profiles in relation to the amount of exposure, interest rate, guarantees or other factors within the group to which they belong.

For this purpose, dispersion statistics (volatility) of the values of said profiles were determined around average values. Until the closing date of this preliminary document, no instruments of the loan portfolio were identified to be treated individually.

Consequently, the convenience of grouping the financial instruments that make up the Bank's credit portfolios by country and by segments according to their guarantee was determined.

Consequently, two (2) segments were defined per country:

a) Mortgage loans with mortgage guarantee and personal loans with mortgage guarantee-CLMG;

b) Personal loans without Mortgage Guarantee-CLNMG

The adoption of this instrument grouping criterion derives, not only from the risk sharing requirement, but also from the need to facilitate the subsequent calculation of the Loss Rate given the Non-compliance of the segments, a parameter significantly associated with the guarantees of the instruments.

In the case of the CLNMG, the rate of loss includes in the calculation the value of recoveries derived from the execution of mortgages and deed in lieu, which explains the

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(4) Financial Risk Management, continued

importance of its disaggregation with respect to another type of recoveries that do not present this quality of guarantees. In the specific case of the CLMNG, the main risk factor they share is, in addition to the volatility of the value of the mortgaged property, the moral hazard, as the houses financed by the Bank are residential type for the use of low and middle income families. The LGD of the CLNMG segment will be determined through the recoveries which process is described below in the corresponding section in this document.

In order to determine the probability of default of the segments identified, and in the context of the collective treatment of the credit portfolios, the Bank will focus the measurement based on the processes denominated Markov Chains, through which the probability (conditional) that an instrument, which is at a certain moment in a certain risk category, migrate to another in a time horizon also determined. Mathematically, it is expressed as the probability that an event A will occur, given another event B. In the Bank's calculation process, the probability that an instrument that at the reporting date presents a certain rating, will default in a time horizon.

For the calculation of the PD, transition matrices have been structured that reflect the annual migration of the risk categories of the instruments, taken monthly. For structuring the matrix, the historical series of ratings of each instrument that makes up each portfolio segment of each country will be used, which will be available in historical series of five (5) years for each instrument. With this database, the rating (risk category) of an instrument is compared monthly at the end of a given month, with the category of that same instrument for the same months of different time horizons (1, 2, 3 or more years).

Through the process described, "pairs" of categories corresponding to a historical period of five years will be formed within each segment. Each "pair" represents the risk rating of each instrument for a given month (T) and the same month of the following year (T + 12), the same month as other years (T + 24, T + 36, T + n), depending on the time horizon analyzed). Arranging matrix pairs and calculating the frequencies of their occurrence, we obtain the conditional probability of migration between the current category of risk of the instrument and the category of non-compliance for different time horizons. The table presents the example of the 1-year peer-training mechanism 13,14 based on the analysis of risk ratings.

The Bank uses statistical models to analyze the data collected and generate PD estimates of the remaining life of the exposures and how they are expected to change as the passage of time.

General approach for determining non-compliance and rebutting of assumptions.

The behavior and payment commitment of the clients when it comes to taking care of their home, makes that the default of the loans granted by the Banco is very low in

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(4) Financial Risk Management, continued

comparison with the behavior of other types of loans. Even unsecured personal loans granted by the Bank remain below the market default curves. It is estimated that this behavior is due to the fact that the Bank only offers personal or consumer loans to clients who have their mortgages with the Bank.

The previous hypothesis is reinforced by the implementation of adequate origination policies and an effective collection strategy. Undoubtedly, another important aspect about low delinquency is the high number of clients that pay for Direct Discount, which is one of the conditions for the approval of a credit in the Bank.

To define default in each segment of each country, the different transitions of delinquency shown by the credits according to delinquency ranges have been analyzed.

As a first approach to the identification of the level of non-compliance, defaults (by days of arrears) of each operation in each segment (Mortgage Loan and Personal Credit) was included, taking as a basis the historical series of each one, for Panama, El Salvador and Colombia.

Under this statistical approach, 66 intermediate matrices have been prepared, corresponding to each month for each segment and country between January 2012 and July 2017, containing the monthly roll-rates of delinquency of the loans granted by the Bank according to their rates of delay of payment or delinquency. From these matrices, 2 matrices with average data were drawn up, corresponding to each credit segment by country, in such a way as to reflect a probability of occurrence of the arrears according to delinquency ranges.

The horizontal lines of the tables show the probabilities that an instrument reaches a certain default according to the range of delay of payment or delinquency at the beginning of the period in a horizon of 1 year. The accumulated percentages of arrears in which the instruments of the segment fall within a horizon of 12 months, after the beginning month of the count, are shown in the columns to the right.

The values allow, in each segment, to determine the range of delay in which it is estimated that the default would occur from a percentage considered as acceptance limit. Based on this information, the Bank has decided that the default would be established from 180 days for the segments of financial instruments with mortgage guarantee and 90 days for the segments of personal credit instruments without mortgage guarantee.

The Bank intends to implement or incorporate other variables and elements to complement the Probability of Non-compliance or real rate of default. These elements may include the incorporation of credit behavioral scoring, the incorporation of credit bureau scores and / or collective elements associated with economic situations.

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(4) Financial Risk Management, continued

Modified financial assets

The contractual terms of a loan can be modified for several reasons, including changes in market conditions, customer retention and other factors not related to current or potential customer credit deterioration. An existing loan whose terms have been modified can be derecognized and the renegotiated loan is recognized as a new loan at fair value in accordance with the accounting policy established in Note 3.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination if the asset's credit risk has increased significantly reflects the comparison of:

- the risk of non-compliance with the remaining life on the reporting date based on the modified terms; with
- the risk of non-compliance with the remaining lifetime estimated on the basis of the data in the initial recognition and the original contractual terms.

Definition of deterioration

The Bank considers that a financial asset is impaired when:

- It is unlikely that the debtor will pay its credit obligations to the Bank in its entirety, without the Bank resorting to actions such as the performance of the guarantees (if applicable); or
- The debtor is over 90 days behind in personal loans and more than 180 days in mortgage loans.
- Significant changes in credit risk indicators as a result of a change in credit risk from the beginning;
- Significant changes in the indicators of the external credit risk market for a specific financial instrument or similar financial instruments with the same expected life;
- A real or expected significant change in the external credit rating of the financial instrument;

In assessing whether a debtor is in default, the Bank considers indicators that are:

- qualitative - breaches of contractual clauses.
- quantitative - default status and non-payment of another obligation of the same debtor to the Bank; and based on data developed internally

The inputs used to assess whether a financial instrument is impaired and its importance may vary over time to reflect changes in circumstances.

The definition of impairment for the loan portfolio is aligned to a great extent with that applied by the Bank for regulatory capital purposes.

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(4) Financial Risk Management, continued

Incorporation of prospective information

The incorporation into the calculation process of Expected Losses in the Bank of prospective aspects will be made based on the possible impact that could be recorded in the value of those losses, caused by expected changes in the short and medium term of the behavior of macroeconomic variables that could affect the flow of payment of the instruments.

In the Central American region and especially in the countries where the Bank operates, statistics on macroeconomic factors are provided almost exclusively by government agencies, and in practice they constitute the main source of information for obtaining values of macroeconomic indicators. In view of such limitations, the Bank, in order to identify those parameters that could have an impact on the payment behavior of financial instruments, established that those that complied with at least one series of profiles that would make them suitable for this type of measurement would be used, as: a) that are available regularly; b) that are accessible to the public in a relatively simple way; b) that are reasonably reliable. While there are no alternative sources to confirm or validate the information indicated in order to have acceptable data for the analysis, it was necessary to select among all the available variables, those that presented the indicated profiles of regularity, accessibility and reliability, and that were:

- a) Inflation (IPC)
- b) Unemployment
- c) Social security contributors
- d) Gross Domestic Product
- e) Imae / Ivae
- f) TRM
- g) Bank's past due portfolio
- h) Past due loan portfolio of the financial system.

The methodology used in the Bank to identify the forward-looking variables (FL) that will participate in the process of incorporating these to the determination of the expected losses, is based on the calculation of the Multiple Correlation Coefficient. The process of defining the most significant variables among the universe of those available, consists of three steps:

The Multiple Correlation and Explanation coefficients were calculated between the historical series of the annual percentage variations of the value of the Past Due Portfolio of Banco La Hipotecaria (taken as a dependent variable), and the historical series of the values of the interannual variations of GDP, IMAE, Inflation and Unemployment (considered independent variables). This calculation allows to determine if those last ones could explain and / or reasonably infer the possible impacts on the payment behavior of the instruments in the future.

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(4) Financial Risk Management, continued

Once the existence of an acceptable degree of association between these variables was determined, we proceeded to calculate the marginal contribution of each, separately, to the value of the multiple correlation, by neglecting the contribution of each one to the value of that correlation. This is achieved by recalculating the multiple correlation, by sequentially eliminating each variable that participates in the original series. The new multiple correlation value after these eliminations, would allow to infer the contribution of each elimination to the originally calculated correlation value.

Finally, the results were compared with those corresponding to the existing correlation between the past due loans of the Bank and those of the financial system of each country, in order to confirm the meaning of the associations.

As a result of the application of the methodology exposed in historical series corresponding to annual periods between 2012 and 2016, the following variables were identified by country and segment:

Panama Operations with Guarantees (Unemployment)
Panama Operations without Guarantee (Inflation).

El Salvador Operations with Guarantees (Unemployment)
El Salvador Operations without Guarantee (IVAE).

Measurement of estimated credit losses

The key inputs in the measurement of credit losses are the structure terms of the following variables:

- Probability of non-compliance or default (PD)
- Loss Given Default (LGD)
- Exposure at Default (EAD)

These parameters are usually derived from internally developed statistical models and other historical data. They are adjusted to reflect the forward-looking information as described above.

For the determination of the PD of the identified segments, and in the context of the collective treatment of the credit portfolios, the Bank will focus the measurement from the processes denominated Markov Chains, through which the probability is calculated that an instrument, which is at a certain moment in a certain risk category, migrates to another within a certain time horizon. Mathematically, it is expressed as the probability that an event A will occur, given another event B. In the Bank's calculation process, the probability will be determined that an instrument that at the reporting date presents a certain rating, will default in a time horizon.

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(4) Financial Risk Management, continued

The Bank estimates the LGD parameters based on the history of recovery rates of the claims against the impaired debtors or counterparts. The LGD models consider the structure, the guarantee, the age of the claim, the counterpart industry and the recovery costs of any guarantee that is integral to the financial asset. For mortgage loan, LTV ratios are a key parameter for determining LGD.

Estimation of the LGD

The calculation of the LGD is implemented for each segment identified in each country, and it requires comparing the amounts recovered in each of those against the unpaid amounts. The convenience of providing information on "closed" cases was established, that is, the data of noncompliance and recoveries will correspond to specific events, whose collection has been terminated by the management, either by the total recovery of the amounts owed or due to justified withdrawal from collection process according to approved credit management policies. The final objective of the calculation is to establish the percentage of recoveries over the value of unfulfilled exposures. The following are definitions relevant to the calculation of LGD in the Bank.

LGD of Mortgage operations that have gone through judicial process and / or deed in lieu

For the calculation, a database called Historical Recoveries was used. In this, all the operations where the Bank has received the asset have been registered, either by means of deed in lieu or repossessed via judicial process (real estate owned). In this report is recorded when the loan starts the process and the repossessed asset is received until it is sold, or is placed again in the figure of a credit to another customer. It also takes into account the legal expenses and repairs that brought us the recovery of that good. This will allow calculating the PDI of operations received as dation in payment or via judicial process.

LGD of operations that reached more than 90 days for personal loans, which were canceled or written off

For this case, the personal loan operations that reach the number of days in arrears indicated above and that ended up canceled or in the default portfolio are averaged, that is, the recoveries of the personal loans that were written off are obtained and also those of the personnel that having reached the point of default were canceled. Then the average of both LGD is obtained and averaged to obtain the LGD of the Personal segment. In the case of personal loans, due to their nature, legal recovery expenses are not incurred.

Mortgage LGD for the Colombian operation

For the mortgage portfolio of Colombia, the bank does not have historical data on recoveries of residential mortgage loans that allow estimating the LGD. Therefore, to obtain the LGD we took into account figures related to the increase of property value

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(4) Financial Risk Management, continued

in Colombia, the current housing deficit, and the LTV of the loan disbursements and of the average LTV of the portfolio.

Exposure at Default (EAD)

EAD represents the expected exposure in case of non-compliance. The Bank determines the EAD of the current exposure of the counterparty and the possible changes in the current amount allowed under the contract, including amortization. The EAD of a financial asset is its gross value in books. For loan commitments and financial guarantees, the EAD includes the amount used, as well as the potential future amounts that may be used from the contract, which are estimated based on historical observations and forward-looking forecasts. For some financial assets, the EAD is determined by modeling the range of possible exposure results at various points in time using scenarios and statistical techniques.

The EAD is the amortized cost of the exposed balances. The Bank determines the annual EAD over the remaining life of the instruments for subsequent weighting due to the respective marginal annual default probability.

At the Bank, the value of the nominal annual EAD will be calculated from the projection of the balances at amortized cost of the instruments. In order to calculate the EAD, the Bank periodically performs a projection of the amortization tables of the loans of each segment until their cancellation. Based on the above, the annual average of the residual (projected) capital balances is obtained annually, a value that is used as the annual EAD exposure projected for the life of the instruments. Finally, said balances are discounted at the annual effective rate.

Clusters are subject to periodic review to ensure that exposures within a particular group remain appropriately homogenous.

Concentration of Credit risk

The Bank monitors concentrations of credit risk by sector and by geographic location. An analysis of concentrations of credit risk at the date of the consolidated financial statements is as follows:

	<u>Loans</u>		<u>Investments in Securities</u>	
	<u>June 30,</u> <u>2017</u>	<u>June 30,</u> <u>2016</u>	<u>June 30,</u> <u>2017</u>	<u>June 30,</u> <u>2016</u>
Concentration by Sector:				
Mortgage banking	582,280,176	547,171,611	43,919,935	44,029,545
Personal banking	53,427,383	47,926,495	0	0
Other sectors	<u>0</u>	<u>0</u>	<u>14,851,571</u>	<u>15,513,014</u>
	<u>635,707,559</u>	<u>595,098,106</u>	<u>58,771,506</u>	<u>59,542,559</u>

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Geographic:

Panama	461,815,889	435,069,985	44,137,727	44,283,233
El Salvador	119,834,783	111,726,941	0	0
Colombia	54,056,887	48,301,180	5,108,467	5,364,951
United States of America	0	0	9,525,312	9,864,375
Caribbean islands	0	0	0	0
	<u>635,707,559</u>	<u>595,098,106</u>	<u>58,771,506</u>	<u>59,512,559</u>

Concentration by location for loans is based on the customer's country of domicile. Concentration by location for investment in securities is based on the country of domicile of the issuer of the security.

(b) Liquidity Risk

The liquidity risk consists of two definitions and depends on its origination:

Funding Liquidity Risk:

It represents the difficulty of an entity to obtain the resources necessary to comply with all its obligations, through the income generated by their assets or by the acquisition of new liabilities. This type of risk, generally, is occasioned by a drastic and sudden deterioration of the quality of the assets which originates an extreme difficulty to turn them into liquid resources.

Market Liquidity Risk:

It is the probability of economic loss due to the difficulty of disposing assets without a significant reduction in its price. It is incurred in this class of risk as a result of changes in the market (prices, rates, etc.), or when investments realized are in markets or instruments for which does not exist an ample offer and demand.

Liquidity Risk Management

The Bank monitors this risk with sufficient and appropriate liquid funds and assets that can easily be liquidated, usually at level required by the regulator and maintains an adequate gap between maturities of assets and liabilities which is reviewed regularly.

The ALCO Committee is in charge of the management of the liquidity risk in order to assure the Bank can respond in case of unexpected cash withdrawals of deposits or unscheduled loans commitments.

Bank's management and the ALCO Committee is responsible to monitor the liquidity position through an analysis of the contractual maturity are structure, stability of deposits by type of customer, and the compliance with regulations and corporate policies.

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(4) Financial Risk Management, continued

Exposure to Liquidity Risk

The key measure used by the Bank for managing liquidity risk is the index of net liquid assets to deposits from customers. The net liquid assets are considered as including cash and cash equivalents and debt securities for which there is an active and liquid market less any deposit from banks, debt securities issued and other borrowings.

The index of net liquid assets on deposits from customers of the Bank reported to the Superintendencia of Banks of Panama; this index should not be less than 30%:

	<u>2018</u>	<u>2017</u>
At June 30	68.00%	59.25%
Average of the year	56.59%	87.14%
Maximum of the year	75.77%	146.68%
Minimum of the year	40.13%	43.61%

The table below set out the undiscounted cash flows of the financial assets and liabilities of the Bank and its loan commitments not recognized.

<u>2018</u>	<u>Carrying amount</u>	<u>Gross nominal (outflow)/inflow</u>	<u>Up to 1 year</u>	<u>From 1 to 5 years</u>	<u>From 5 to 10 years</u>	<u>More than 10 years</u>
Financial Liabilities:						
Saving deposits	1,119,584	(1,119,584)	(1,119,584)	0	0	0
Time deposits	219,668,565	(234,485,857)	(116,260,487)	(118,225,370)	0	0
Negotiable commercial papers	85,144,947	(87,019,513)	(87,019,513)	0	0	0
Negotiable commercial notes	102,848,222	(107,104,466)	(25,331,538)	(81,772,928)	0	0
Ordinary bonds	12,152,920	(13,778,373)	(616,086)	(13,162,287)	0	0
Investment certificates	9,600,000	(10,124,826)	(5,192,187)	(4,932,639)	0	0
Other negotiable debts	24,436,597	(25,163,869)	(25,163,869)	0	0	0
Borrowed funds	198,850,071	(220,292,471)	(54,411,612)	(127,514,886)	(38,365,973)	0
Total financial liabilities	<u>653,820,906</u>	<u>(699,088,959)</u>	<u>(315,114,876)</u>	<u>(345,608,110)</u>	<u>(38,365,973)</u>	<u>0</u>
Financial Assets:						
Cash	214,345	214,345	214,345	0	0	0
Demand deposits	26,665,754	26,665,754	26,665,754	0	0	0
Investment securities	58,770,194	109,367,173	3,141,483	11,717,917	17,028,088	77,479,885
Loans	635,126,563	1,248,247,634	62,046,435	241,322,342	279,849,330	665,029,527
Total financial assets	<u>720,776,856</u>	<u>1,384,494,906</u>	<u>92,068,017</u>	<u>253,040,259</u>	<u>296,877,418</u>	<u>742,509,212</u>
Commitments and contingencies						
Loan commitments	0	(73,902,870)	(73,902,870)	0	0	0
<u>2017</u>	<u>Carrying amount</u>	<u>Gross nominal (outflow)/inflow</u>	<u>Up to 1 year</u>	<u>From 1 to 5 years</u>	<u>From 5 to 10 years</u>	<u>More than 10 years</u>
Financial Liabilities:						
Saving deposits	923,276	(923,276)	(923,276)	0	0	0
Time deposits	207,555,493	(222,571,814)	(103,518,484)	(119,053,330)	0	0
Negotiable commercial papers	82,931,225	(84,302,996)	(84,302,996)	0	0	0

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Negotiable commercial notes	96,309,431	(98,446,601)	(33,152,509)	(65,294,092)	0	0
Ordinary bonds	14,310,229	(16,583,965)	(725,449)	(15,858,516)	0	0
Investment certificates	13,600,000	(14,534,160)	(6,173,639)	(8,630,521)	0	0
Other negotiable debts	13,840,047	(13,880,549)	(13,880,549)	0	0	0
Borrowed funds	<u>187,147,534</u>	<u>(208,045,893)</u>	<u>(35,143,214)</u>	<u>(152,708,564)</u>	<u>(20,194,115)</u>	<u>0</u>
Total financial liabilities	<u>616,617,235</u>	<u>(659,289,254)</u>	<u>(277,820,116)</u>	<u>(361,275,023)</u>	<u>(20,194,115)</u>	<u>0</u>
Financial Assets:						
Cash	337,800	337,800	337,800	0	0	0
Demand deposits	29,093,301	29,093,301	29,093,301	0	0	0
Investment securities	59,477,544	109,513,433	2,785,384	11,556,148	15,730,586	79,441,315
Loans	<u>595,098,106</u>	<u>1,168,695,681</u>	<u>57,578,383</u>	<u>224,700,582</u>	<u>280,412,642</u>	<u>626,004,094</u>
Total financial assets	<u>684,006,751</u>	<u>1,307,640,215</u>	<u>89,794,868</u>	<u>236,256,710</u>	<u>276,143,228</u>	<u>705,445,409</u>
Commitments and contingencies						
Loan commitments	<u>0</u>	<u>(77,155,573)</u>	<u>(77,155,573)</u>	<u>0</u>	<u>0</u>	<u>0</u>

For financial assets and liabilities that are non-derivatives, the gross nominal amount is measured based on undiscounted cash flows of comprising cash and include estimated interest payable and receivable, therefore they differ from the amounts presented in the consolidated statement of financial position.

The table below sets out the carrying amounts of financial liabilities expected to be settled more than twelve months after the reporting date:

	<u>2018</u>	<u>2017</u>
Financial Liabilities:		
Time deposits	<u>105,835,400</u>	<u>106,568,404</u>
Borrowed funds	<u>146,522,254</u>	<u>153,842,987</u>
Negotiable commercial notes	<u>70,467,000</u>	<u>63,902,000</u>
Ordinary bonds	<u>12,152,920</u>	<u>14,310,229</u>
Investment certificates	<u>4,600,000</u>	<u>7,600,000</u>

The Bank is dedicated to generate mortgage and personal loans and is capable of securitize part of its loans in accordance with its liquidity needs. Mortgage loans reflect a monthly flow in capital installments and interest payments which are not listed in the table above.

The table below shows the Bank's commitment and available assets as collateral in connection with any financial liability or other compromise, and represent those financial assets available to support future commitments or borrowed funds:

	<u>2018</u>	<u>Pledged as Collateral</u>	<u>Available as Collateral</u>	<u>Total</u>
Cash and cash equivalent	0	0	26,880,099	26,880,099
Investment securities	0	0	58,770,194	58,770,194
Loans, net	181,432,579	181,432,579	453,693,984	635,126,563
Non-financial assets	0	0	<u>15,883,749</u>	<u>15,883,749</u>

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	<u>181,432,579</u>	<u>555,228,026</u>	<u>736,660,605</u>
<u>2017</u>	<u>Pledged as Collateral</u>	<u>Available as Collateral</u>	<u>Total</u>
Cash and cash equivalent	0	27,534,184	27,534,184
Investment securities	0	59,512,559	59,512,559
Loans, net	158,173,667	436,610,814	594,784,481
Non-financial assets	<u>0</u>	<u>17,992,223</u>	<u>17,992,223</u>
	<u>158,173,667</u>	<u>541,649,780</u>	<u>699,823,447</u>

(c) *Market Risk:*

It is the risk that the value of a financial asset is reduced as a result of changes in interest rates, in monetary exchange rates, stock prices and other financial variables, as well as the reaction of market participants to political and economic events. These elements cause that the Bank is subject to latent losses as to potential profit. The objective of market risk management is of managing and watching the risk exposures and that the same ones are supported inside the acceptable parameters optimizing the risk return.

Market Risk Management:

The management of this risk is supervised constantly by the General Management. To mitigate this risk, the Bank has documented in its control policies related to investment limits, classification and valuation of investments, qualification of portfolio, cross-check of interest payments, sensibility and stress tests.

Below are detailed the composition and analysis of each of the types of market risk:

Exchange Rate Risk

Is the risk that the value of a financial instrument fluctuates as a consequence of changes in exchange rates of foreign currencies and other financial variables, and the reaction of market participants to political and economic events. For purposes of IFRS 7, this risk does not derive from financial instruments that are not monetary items, nor for financial instruments denominated in the functional currency.

The Bank holds and makes loans in Colombian Pesos, the national currency of Colombia. The value of positions fluctuates as a result of changes in the prices of the exchange rate.

The sensibility analysis for the risk of exchange rate, is considered principally in the measurement of the position inside a specific currency. The analysis consists of verifying how much would represent the position in the functional currency on the currency to which it would be converting and therefore the mix of the exchange rate risk.

The currency position is presented in its equivalent in dollars as follows:

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(4) Financial Risk Management, continued

<u>Colombian Pesos</u>	<u>2018</u>	<u>2017</u>
Assets		
Cash and cash equivalent	3,733,789	4,802,534
Loans, net	53,966,218	48,301,180
Other assets	<u>7,111,765</u>	<u>7,067,252</u>
Total assets	<u>64,811,772</u>	<u>60,170,966</u>
Liabilities		
Time deposits	27,310,291	19,159,683
Ordinary bonds	12,152,920	14,310,229
Borrowed funds	625,440	2,770,331
Other liabilities	<u>653,396</u>	<u>634,166</u>
Total liabilities	<u>40,742,047</u>	<u>36,874,409</u>
Net position	<u>24,069,725</u>	<u>23,296,557</u>

Interest Rate Risk

Interest rate risk is the financial exposure (net margin and equity market value) of the Bank to possible losses in the event of unexpected movement in the interest rates.

The Board of Directors establishes that the ALCO Committee has the responsibility to analyze the sensibility to interest rate fluctuations, statement of financial position structure, transaction terms and investment strategies.

The basic analysis carried out every month by management consists in determining the impact caused on financial assets and liabilities by increases or decreases of 25 and 50 basis points in interest rates, considering as a premise, the minimum rate of 0.005% in cases that their results yield negative values to raise the actual values. The impact is summarized as follows:

	<u>Increase of 25 bp</u>	<u>Decrease of 25 bp</u>	<u>Increase of 50 bp</u>	<u>Decrease of 50 bp</u>
Sensitivity of projected net <u>interest income</u>				
2018	121,420	(121,420)	242,840	(242,840)
2017	86,075	(88,357)	173,905	(169,569)
Sensitivity of projected net <u>equity</u>				
2018	(1,153,222)	1,153,222	(2,306,444)	2,306,444
2017	(1,217,299)	1,217,299	(2,434,599)	2,434,599

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(4) Financial Risk Management, continued

The table below summarizes the Bank's exposure to interest rate risk. It includes the Bank's assets and liabilities at carrying value, categorized by the earlier of contractual reprising rate or maturity.

<u>2018</u>	<u>Up to 1 year</u>	<u>From 1 to 5 years</u>	<u>From 5 to 10 years</u>	<u>More than 10 years</u>	<u>Total</u>
Assets:					
Demand deposits	17,206,357	0	0	0	17,206,357
Time deposits	2,200,000	0	0	0	2,200,000
Investment in securities at FVOCI	26,028,423	0	13,182,283	0	39,210,706
Investments held to maturity	211,340	0	0	218,997	430,337
Investments in securities at FVTLP	1,240,263	0	0	17,890,200	19,30,463
Loans	<u>635,707,559</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>635,707,559</u>
Total de activos	<u>682,593,942</u>	<u>0</u>	<u>13,182,283</u>	<u>18,109,197</u>	<u>713,885,422</u>
Liabilities:					
Saving deposits	1,119,584	0	0	0	1,119,584
Time deposits	112,261,215	107,407,350	0	0	219,668,565
Borrowed funds	198,850,071	0	0	0	198,850,071
Issued debt	<u>147,229,544</u>	<u>86,953,142</u>	<u>0</u>	<u>0</u>	<u>234,182,686</u>
Total liabilities	<u>459,460,414</u>	<u>194,360,492</u>	<u>0</u>	<u>0</u>	<u>653,820,906</u>
Interest rate sensitivity, net	<u>223,133,528</u>	<u>(194,360,492)</u>	<u>13,182,283</u>	<u>18,109,197</u>	<u>60,064,516</u>
<u>2017</u>	<u>Up to 1 year</u>	<u>From 1 to 5 years</u>	<u>From 5 to 10 years</u>	<u>More than 10 years</u>	<u>Total</u>
Assets:					
Demand deposits	17,180,807	0	0	0	17,180,807
Time deposits	0	0	0	0	0
Investment in securities at FVOCI	43,887,069	0	0	0	43,887,069
Investments held to maturity	223,459	0	0	218,673	442,132
Investments in securities at FVTLP	1,362,746	0	0	13,774,100	15,136,846
Loans	<u>595,098,106</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>595,098,106</u>
Total assets	<u>657,752,187</u>	<u>0</u>	<u>0</u>	<u>13,992,773</u>	<u>671,744,960</u>
Liabilities:					
Saving deposits	990,484	0	0	0	990,484
Time deposits	100,840,995	106,714,498	0	0	207,555,493
Borrowed funds	187,147,534	0	0	0	187,147,534
Issued debt	<u>135,390,272</u>	<u>85,600,660</u>	<u>0</u>	<u>0</u>	<u>220,990,932</u>
Total liabilities	<u>424,369,285</u>	<u>192,315,158</u>	<u>0</u>	<u>0</u>	<u>616,684,443</u>
Interest rate sensitivity, net	<u>233,382,902</u>	<u>(192,315,158)</u>	<u>0</u>	<u>13,992,773</u>	<u>55,060,517</u>

To evaluate the interest rate risk and its impact in the fair value of financial assets and liabilities, management of the Bank makes stress tests to determine the sensibility of financial assets and liabilities.

Price Risk:

Is the risk that the value of a financial instrument fluctuates due to changes in market prices, independently that they are caused by specific factors related to the particular

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(4) Financial Risk Management, continued

instrument or its issuer, or factors that affect all securities traded on the market.

The Bank is exposed to price risk of financial instruments classified at FVOCI or securities at FVTPL. To mitigate the price risk in equity or debt instruments, the Bank diversifies its portfolio according to the established limits.

(d) Operational Risk

Operational risk involves potential losses, directly or indirectly related to the banking process. It could be caused by personnel, technology, infrastructure, as well as external factors that are not related to credit, market and liquidity risks. These external factors involve government legal requirements and regulatory requirements and generally accepted standards of corporate behavior.

The model of Operative Risk Management covers as principal points:

- Identification and evaluation of the risks.
- Report of events of losses and incidents.
- Definition of mitigating actions.
- Proper follow up to the execution of plans of actions defined by new initiatives of the Bank, products and/or services and significant improvements to the processes.
- To evaluate the operative risk level in the initiatory piece of news of the Bank, products and/or services and significant progress to the processes.
- Development of trainings.
- Participation in the design of policies and procedures.

The different areas that take part in joint form for the ideal management of the operative risk are:

- Unit of Administration of Risk.
- Technology of Information.
- Unit of Computer Security.
- Monitoring and Prevention of Frauds.
- Unit of Internal control.

As part of the model of Corporate Government, the strategy, methodology of work and follow up to the plans of actions defined for the events and risks valued as critical and high are brought to the Top Management and in turn to the Risk Committee of the Board of Directors every three months.

The Department of Internal Audit checks and validates the fulfillment of the policies and definite methodologies and that these go according to the existing regulation, the results of this review are presented to the Audit Committee.

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(4) Financial Risk Management, continued

(e) Capital Management:

One of the policies of the Bank is to maintain a level of capital to accompanying credit business and investment growth in the market, maintaining a balance between the return on investments, and the adequacy of capital required by regulators.

The Bank is subject to the Panamanian Banking Law, which states that the total capital adequacy ratio shall not be less than 8% of its total weighted assets and off-balance accounts which represent an irrevocable contingency, weighted based on their risks.

Based in the Agreements No. 1-2015 and its amendments and No. 3-2016, issued by the Superintendence of Banks of Panama, as of June 30, 2018, the Bank held a regulatory capital position that is comprised as follows:

	<u>2018</u>	<u>2017</u>
Capital Primario Ordinario		
Common shares	15,000,000	15,000,000
Additional paid in capital	25,025,329	26,300,000
Less: Treasury Shares	(727,000)	0
Capital reserves	1,800,000	1,800,000
Other items of comprehensive income (1)		
Gain in available for sale securities	37,223	571,834
Adjust for translation of foreign currency	(4,271,446)	(4,640,024)
Retained earnings	23,595,482	21,932,674
Non-controlling interests	924,209	891,891
Less: Deferred tax	<u>(1,080,062)</u>	<u>(987,891)</u>
Total Primary Ordinary Capital	<u>60,303,735</u>	<u>60,868,484</u>
Dynamic provision	<u>6,863,256</u>	<u>6,863,256</u>
Total Regulatory Capital	<u>67,166,991</u>	<u>67,731,740</u>
Total of Risk weighed assets	<u>448,907,908</u>	<u>429,296,001</u>

	<u>Minimum requested</u>		
Ratios:			
Capital Adequacy ratio	<u>8.00%</u>	<u>14.96%</u>	<u>15.78%</u>
Primary Ordinary Capital Ratio	<u>3.75%</u>	<u>13.42%</u>	<u>14.18%</u>
Primary Capital Ratio	<u>5.25%</u>	<u>13.42%</u>	<u>14.18%</u>

(1) Excludes the fair value of the portfolio acquired

(5) Use of Estimates and Judgments in Applying Accounting Policies

The management of the Bank prepares the consolidated financial statements in accordance with International Financial Reporting Standards. They have applied judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of

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(5) Use of Estimates and Judgments in Applying Accounting Policies, continued

assets, liabilities, income and expenses during the period. Actual results may differ from these estimates.

The assumptions and decisions are continuously evaluated and are based on the historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The management of the Bank evaluates the selection, disclosures and application of critical accounting policies in the mayor uncertain estimates. The information related to the related to the presumptions and estimates that affect the reported amounts of assets and liabilities under the next fiscal year and critical judgments in the selection and application of the accounting policies detailed as follows:

(a) Classification of financial assets

When determining the classification of financial assets, the Bank uses its judgment to evaluate the business model within which the assets are held and whether the contractual terms of the financial asset are only payments of the principal and interest on the outstanding principal amount.

(b) Impairment of financial instruments

The Bank review its financial assets on the date of each consolidated statement of financial position to determine whether the credit risk of a financial instrument has increased significantly since its initial recognition.

(c) Income tax

The Bank is subject to income taxes under the jurisdictions of the Republic of Panama, Colombia, and El Salvador. Significant estimates are required in determining the provision for income taxes. Estimates are made through a tax projection to determine the provision for income taxes and the liabilities resulting from said estimation are recognized. When the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the provision for income taxes and deferred taxes in the period in which such determination was made.

(d) Non-consolidated structured entities

The Bank's management conducted an analysis of their structured entities, and in turn concluded that the same should not be consolidated because the Bank performs the function of an agent and not principal. An agent act on behalf and for the benefit of another party or parties (the principal or principals) and therefore does not control an investee when exercising its authority to make decisions. Therefore, sometimes the power of a principal can be maintained and exercised by an agent, but on behalf of the principal.

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(6) Balances and Transactions with Related Parties

The consolidated statement of financial position and the consolidated statement of income include balances and transactions with related parties, which are summarized as follows:

	<u>2018</u>	<u>2017</u>
Assets:		
Demand deposits	72,435	117,026
Account receivable related parties	30,000	0
Liabilities:		
Savings deposits	685,430	681,277
Time deposits	5,818,578	5,989,191
Accrued interest	0	0
Account payable related parties	0	0
Other income (expenses):		
Interest expense on deposits	(126,614)	(122,593)
Short-term benefits to executives	(509,621)	(560,004)

Transactions with Directors and Executives

As of June 30, 2018, the Bank has paid fees for B/.18,992 (2016: B/.34,031) to Directors that attend the meetings of the Board of Directors and Committees.

The Bank has paid salaries and other benefits such as life insurance, bonus, and salaries in species to the executives for B/.509,621 (2016: B/.560,004).

(7) Cash and Cash Equivalents

The cash and cash equivalents are detailed as follows for purposes of reconciliation with the consolidated statement of cash flows:

	<u>2018</u>	<u>2017</u>
Cash and cash effects	214,345	337,800
Demand deposits	20,182,267	22,468,538
Saving deposits	4,283,487	4,727,846
Time deposits	2,200,000	0
Cash and cash equivalents in the consolidated statement of cash flows	<u>26,880,099</u>	<u>27,534,184</u>

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(8) Investment in Securities

The investment securities and other financial assets are classified as follows:

	<u>June 30, 2018</u>	<u>December 30, 2017</u>
Investments in securities at FVOCI	39,210,706	0
Investments in securities at FVTPL	19,130,463	15,136,846
Investments at amortized cost	430,337	0
Investments available for sale	0	43,933,581
Investments held to maturity	0	442,132
Total investments in securities	<u>58,771,506</u>	<u>59,512,559</u>
Reserves for investments at amortized cost	<u>(1,312)</u>	<u>0</u>
	<u>58,770,194</u>	<u>59,512,559</u>

Investments in securities at FVOCI

These securities are detailed as follows:

30 de junio de 2018			
	Republic of Colombia	United States of America	
<u>Mortgage Bonds</u>	<u>Treasury Bonds</u>	<u>Treasury Bonds</u>	<u>Total</u>
26,028,423	3,656,971	9,525,312	39,210,706
<u>26,028,423</u>	<u>3,656,971</u>	<u>9,525,312</u>	<u>39,210,706</u>

The Bank made sales of investments in securities at FVOCI of B/.11,404,951, these sales generated a gain of B/.168,656.

Changes to the allowance for ECL related to investment in securities at FVOCI are detailed as follows:

	2018			
	<u>ECL next 12 months</u>	<u>ECL during life time (not impaired – collective assessment)</u>	<u>ECL during life time (impaired – individual assessment)</u>	<u>Total</u>
At January 1st	23,191	95,956	0	119,147
Remeasurement net of allowance for losses	16,272	34,384	0	50,656

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Purchase of new financial assets	20,216	0	0	20,216
Disposal of Financial instruments during the period	(20,216)	0	0	(20,216)
At the end of period	<u>39,463</u>	<u>130,340</u>	<u>0</u>	<u>169,803</u>

Allowance for ECL mentioned above is not recognized in the consolidated statement of financial position because the carrying amount of the investment in debt instruments at FVOCI for \$39,210,706 (2017:\$43,963,581) is its fair value.

Investment in Securities at Fair Value through Profit or Loss - FVTPL

These securities consist of residual interests that the Bank has retained as part of the securitization of their portfolios, and are detailed as follows:

	<u>Maturity</u>	<u>June 20 2018</u>	<u>December 31 2017</u>
Residual interest of eighth trust	December 2036	2,428,414	2,573,532
Residual interest of ninth trust	December 2022	572,627	573,964
Residual interest of tenth trust	September 2039	5,483,836	5,107,150
Residual interest of eleventh trust	October 2041	2,874,685	2,725,621
Residual interest of twelfth trust	November 2042	1,599,991	1,574,304
Residual interest of thirteenth trust	December 2045	1,368,861	1,219,529
Mortgage bond eleventh trust	October 2041	1,848,927	0
Mortgage bond twelfth trust	November 2042	784,828	0
Mortgage bond thirteenth trust	December 2045	928,031	0
Agricultural development securities	October 2018	565,220	180,373
Time deposit certificate	February 2018	0	1,182,373
Mutual funds	At call	675,043	0
Total		<u>19,130,463</u>	<u>15,136,846</u>

The trust's residual interests were determined by discounting the future cash flows as trustee commissions and incentives that will receive the Bank from these trusts. At the time of origination of these trusts, it was estimated that the realization of values was 30 years for the Eighth, Ninth, Tenth, Eleventh, Twelfth, and Thirteenth Mortgage Bonds Trust: (maturing in 2036, 2022, 2039, 2041, 2042 and 2045 respectively).

Securities at amortized cost

The Bank maintains bonds of the Republic of Panama with a nominal value of B/.225,000, which are recorded at amortized cost of B/.218,673 (2017: B/.218,673) with a fair value of B/.302,625 (2017: B/.327,645). These bonds have an interest rate of 8.875% (2017: 8.875%) and maturity date on December 31, 2027. These bonds are held in the Banco Nacional de Panama and are at the disposition of the Superintendence of Banks of Panama, in order to

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(8) Investment in Securities, continued

guarantee proper compliance with the fiduciary obligations of the Bank. Similarly the Bank maintain Colombian agricultural development securities (TDA and TDB) with a carrying amount of B/.211,340 (2016: B/.223,459) a fair value of B/.211,340 (2016: B/.223,459) with maturity on July 2018.

Securities at amortized cost per issuer are detailed below:

June 30, 2018		
Republic of Panama Bonds	Colombian Agricultural Development Securities	Total
218,997	211,340	430,337
<u>218,997</u>	<u>211,340</u>	<u>430,337</u>

The movement of the allowance for expected credit losses related to investments in securities at amortized cost is detailed below.

	2018			Total
	ECL Next 12 months	ECL During life time (not impaired – collective assessment)	ECL during life time (impaired – individual assessment)	
At January 1st	884	0	0	884
Remeasurement net of allowance for losses	(89)	0	0	(89)
Purchase of new financial assets	547	0	0	547
Disposal of Financial instruments during the period	(30)	0	0	(30)
At the end of period	<u>1,312</u>	<u>0</u>	<u>0</u>	<u>1,312</u>

Securities Available-for-Sale

The investments in securities available for sale are detailed as follows:

December 31, 2017					
Mortgage Bonds	Republic of Colombia Treasury Bonds	United States of America Treasury Bonds	Mutual Funds	Shares	Total
30,255,445	3,767,249	9,864,375	11,497	35,015	43,933,581
<u>30,255,455</u>	<u>3,767,249</u>	<u>9,864,375</u>	<u>11,497</u>	<u>35,015</u>	<u>43,933,581</u>

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(8) Investment in Securities, continued

The Bank maintains an investment in shares in the amount of \$ 0 (2017: \$ 35,015), to which the Bank could not reliably calculate fair value.

As of June 30, 2017, the Bank sold investments registered as available for sale for \$ 1,972,163, generating a gain of \$ 542,163.

Securities Held to Maturity

Investments in securities held to maturity are detailed as follows:

December 31, 2017		
<u>Republic of Panama Bonds</u>	<u>Colombian Agricultural Development Securities</u>	<u>Total</u>
218,673	223,459	442,132
<u>218,673</u>	<u>223,459</u>	<u>442,132</u>

(9) Loans, Net

The composition of the loans portfolio is summarized as follows:

	<u>2018</u>	<u>2017</u>
Local loans:		
Personal	37,606,324	35,268,757
Residential mortgages	424,209,564	399,801,228
Total local loans	<u>461,815,888</u>	<u>435,069,985</u>
Foreign loans:		
Personal	12,657,738	9,778,345
Residential mortgages	147,370,383	131,819,917
Total foreign loans	<u>160,028,121</u>	<u>141,598,262</u>
Total loans	<u>595,098,106</u>	<u>505,818,303</u>

The movements of the allowance for expected credit loan losses are detailed as follows. The comparative amounts for 2017 represent the allowance for credit losses and reflect the measurement basis according to IAS 39:

	2018			Total	December 31,2017
	ECL next 12 months	ECL during life time (not impaired – collective assessment)	ECL during life time (impaired – individual assessment)		
As January 1st, 2018	134,341	81,847	239,478	455,666	300,664

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- Transfer to expected credit losses during the next 12 months	247,031	(118,672)	(128,359)	0	0
- Transfer to expected credit losses during life time- not impaired	(62,632)	137,233	(74,601)	0	0
- Transfer to expected credit losses during life time-impaired	(1,821)	(115,622)	117,443	0	0
- Remeasurement net of the allowance for credit losses	(146,129)	138,182	249,656	241,709	512,648
- Origination of new financial assets	18,189	0	0	18,189	0
- Financial instruments that have been written off during the period	(27,609)	(3,234)	(49,831)	(80,674)	0
Written off	0	0	(53,894)	(53,894)	(499,687)
As June 30, 2018	<u>161,370</u>	<u>119,734</u>	<u>299,892</u>	<u>580,996</u>	<u>313,625</u>

In June and September 2015, the Bank purchased the residential mortgage portfolio from the Sixth and Seventh Mortgage Loan Bonds with a fair value of \$ 4,517,878 and \$ 4,773,715, respectively. The difference between the amount paid and the fair value of these purchases was \$ 1,325,034 and was recorded in the fair value reserve account in the consolidated statement of changes in equity. The amount pending amortization to date is B / .1,127,342 (2017: B / .1,167,013).

(10) Furniture, Equipment and Improvements, net

Furniture, equipment and improvements are summarized as follows:

<u>2018</u>	<u>Furniture</u>	<u>Office Equipment</u>	<u>Vehicles</u>	<u>Leasehold Improvements</u>	<u>Total</u>
Cost:					
At the beginning of the year	776,290	2,996,040	399,691	1,974,438	6,146,459
Purchases	21,337	212,295	233,323	121,503	588,458
Sales and disposals	<u>(7,973)</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>(7,973)</u>
At the end of the year	<u>789,654</u>	<u>3,208,335</u>	<u>633,014</u>	<u>2,095,941</u>	<u>6,726,944</u>
Accumulated depreciation:					
At the beginning of the year	553,078	2,270,510	324,870	767,337	3,915,795
Expense for the year	58,088	210,604	38,349	107,862	414,903
Sales and disposals	(7,973)	0	0	0	(7,973)
Adjustment for conversion	<u>(11,183)</u>	<u>26,413</u>	<u>0</u>	<u>0</u>	<u>15,230</u>
At the end of the year	<u>592,010</u>	<u>2,507,527</u>	<u>363,219</u>	<u>875,199</u>	<u>4,337,955</u>
Net balances	<u>197,644</u>	<u>700,808</u>	<u>269,795</u>	<u>1,220,742</u>	<u>2,388,989</u>
<u>2017</u>	<u>Mobiliario</u>	<u>Equipo de oficina</u>	<u>Equipo rodante</u>	<u>Mejoras a la propiedad</u>	<u>Total</u>
Cost:					
At the beginning of the year	690,970	2,526,661	385,673	1,136,160	4,739,464
Purchases	171,047	547,177	14,018	838,278	1,570,520
Sales and disposals	(85,727)	(77,798)	0	0	(163,525)

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Adjustment for conversion					
Adjustment and reclassification					
At the end of the year	0	0	0	0	0
Cost:	(17,180)	25,477	0	0	8,297
At the beginning of the year	<u>759,110</u>	<u>3,021,517</u>	<u>399,691</u>	<u>1,974,438</u>	<u>6,154,756</u>
Accumulated depreciation:					
At the beginning of the year	506,329	1,893,130	264,988	608,239	3,272,686
Expense for the year	101,336	441,048	59,882	159,098	761,364
Sales and disposals	(84,055)	(77,755)	0	0	(161,810)
Adjustment for conversion	473	16,628	0	0	17,101
Adjustment for origination	11,815	22,936	0	0	34,751
At the end of the year	<u>535,898</u>	<u>2,295,987</u>	<u>324,870</u>	<u>767,337</u>	<u>3,924,092</u>
Net balances	<u>223,212</u>	<u>725,530</u>	<u>74,821</u>	<u>1,207,101</u>	<u>2,230,664</u>

(11) Accounts and Interests Receivable

The following is a detail of accounts and interests receivable:

	<u>2018</u>	<u>2017</u>
Accounts receivable:		
Clients	1,306,836	1,199,257
Employees	31,073	16,188
Insurance	34,891	652,184
Others	468,353	59,456
	<u>1,841,153</u>	<u>1,927,085</u>
Interests receivable:		
Loans	1,360,510	1,477,991
Bonds	260,627	270,573
	<u>1,621,137</u>	<u>1,748,564</u>
	<u>3,462,290</u>	<u>3,675,649</u>

(12) Other Assets

The other assets are detailed as follows:

	<u>2018</u>	<u>2017</u>
Guarantee deposits	57,633	57,303
Bond of trust license	25,000	25,000
Severance fund	637,817	616,887
Various prepaid	1,821,916	840,133
Advance to assets purchase	420,786	312,616
Foreclosed assets	279,839	234,239
Other	626,091	532,677
Total	<u>3,869,082</u>	<u>2,618,923</u>

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(13) Negotiable Commercial Papers

The Bank is authorized by the Superintendence of the Securities Market of Panama five rotating programs up to B/.200,000,000 in negotiable commercial papers which are backed up by the general credit of the Bank. Of these programs, two for the amount of B/.40,000,000 are backed by Grupo ASSA, S. A. as solidary Surety. At this date those two programs has no papers issued.

		<u>2018</u>		
	<u>Type</u>	<u>Interest rate</u>	<u>Maturity</u>	<u>Amount</u>
	Series DCF	3.8750%	July-18	3,000,000
	Series DCG	3.8750%	July-18	2,500,000
	Series BCK	3.8750%	August-18	1,000,000
	Series BCL	3.8750%	August-18	1,629,000
	Series BCM	3.8750%	August-18	5,410,000
	Series BCN	3.8750%	August-18	1,590,000
	Series O	3.0000%	September-18	1,606,000
	Series BCP	3.8750%	September-18	2,770,000
	Series DCH	3.2500%	September-18	2,279,000
	Series BCR	3.8750%	September-18	2,505,000
	Series A	3.8750%	October-18	300,000
	Series B	3.8750%	October-18	2,000,000
	Series C	3.8750%	November-18	4,390,000
	Series D	3.8750%	December-18	2,450,000
	Series E	3.8750%	December-18	1,775,000
	Series F	3.8750%	December-18	3,000,000
	Series G	3.8750%	January-19	2,000,000
	Series H	3.8750%	January-19	1,000,000
	Series I	3.8750%	January-19	2,014,000
	Series J	3.8750%	January-19	2,306,000
	Series K	3.8750%	February-19	5,283,000
	Series L	3.8750%	February-19	2,854,000
	Series M	3.8750%	February-19	2,584,000
	Series N	3.8750%	February-19	2,500,000
	Series P	3.8750%	March-19	1,185,000
	Series Q	3.8750%	March-19	858,000
	Series DCI	4.0000%	March-19	3,890,000
	Series DCJ	4.0000%	April-19	1,864,000
	Series DCK	4.0000%	April-19	2,000,000
	Series DCL	4.0000%	April-19	959,000
	Series DCM	4.0000%	April-19	1,210,000
	Series DCN	4.0000%	April-19	1,300,000
	Series DCO	4.0000%	May-19	1,936,000
	Series DCP	4.0000%	May-19	1,000,000
	Series DCQ	4.0000%	May-19	2,064,000
	Series CDK	4.0000%	May-19	1,980,000
	Series CDL	4.0000%	June-19	4,000,000
	Series CDM	4.0000%	June-19	1,845,000
	Series CDN	4.0000%	June-19	410,000
				85,246,000
	Less issuance cost			(101,053)
				85,144,947

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<u>Type</u>	<u>Interest rate</u>	<u>2017</u> <u>Maturity</u>	<u>Amount</u>
Series CCZ	3.8750%	January, 2018	3,000,000
Series CDA	3.8750%	January, 2018	2,000,000
Series CDB	3.8750%	January, 2018	1,000,000
Series DBW	3.8750%	January, 2018	2,143,000
Series BCJ	3.0000%	February, 2018	1,000,000
Series DBX	3.8750%	February, 2018	1,482,000
Series CDC	3.8750%	February, 2018	3,600,000
Series DBZ	3.8750%	March, 2018	2,723,000
Series DCA	3.8750%	March, 2018	2,500,000
Series BCO	3.8750%	March, 2018	2,000,000
Series BCC	3.8750%	March, 2018	1,225,000
Series BCD	3.8750%	March, 2018	1,000,000
Series BCQ	3.8750%	April, 2018	3,000,000
Series CDD	3.8750%	April, 2018	4,085,000
Series CDE	3.8750%	April, 2018	2,004,000
Series BCG	3.8750%	April, 2018	2,000,000
Series BCF	3.8750%	April, 2018	1,459,000
Series BCH	3.8750%	April, 2018	2,240,000
Series BCI	3.8750%	May, 2018	1,300,000
Series DCD	3.8750%	May, 2018	1,898,000
Series CDF	3.8750%	May, 2018	1,000,000
Series CDJ	3.8750%	May, 2018	3,000,000
Series CDG	3.8750%	June, 2018	980,000
Series DCE	3.8750%	June, 2018	2,000,000
Series CDH	3.8750%	June, 2018	1,000,000
Series CDI	3.8750%	June, 2018	4,000,000
Series DCF	3.8750%	July, 2018	3,000,000
Series DCG	3.8750%	July, 2018	2,500,000
Series BCK	3.8750%	August, 2018	900,000
Series BCL	3.8750%	August, 2018	1,629,000
Series BCN	3.8750%	August, 2018	1,590,000
Series BCM	3.8750%	August, 2018	5,410,000
Series BCP	3.8750%	September, 2018	2,770,000
Series BCR	3.8750%	September, 2018	2,505,000
Series A	3.8750%	October, 2018	300,000
Series B	3.8750%	October, 2018	2,000,000
Series C	3.8750%	November, 2018	4,390,000
Series D	3.8750%	December, 2018	<u>2,350,000</u>
			82,983,000
Less issuance costs			<u>(51,775)</u>
			<u>82,931,225</u>

As of June 30, 2018 and 2017, there have been no defaults in the payment of principal and interest in relation to negotiable commercial securities.

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(14) Negotiable Commercial Notes

The Bank has been authorized by the Securities Market Superintendence of Panama of three programs totaling B/.190,000,000 in Negotiable Commercial Notes (NCN). The placements of the first issuance for B/.40,000,000 are supported by the general credit of the Bank, a guarantee trust made up of mortgage loans and a solidary surety of Grupo ASSA, S. A. that will cover any difference not covered with the proceeds from the sale of the mortgage loans.

The placements of the other two programs of B/.50,000,000 and B/.100,000,000, respectively, are only supported by the general credit of the Bank.

<u>Tipo</u>	<u>Interest rate</u>	<u>Maturity</u>	<u>2018</u>	<u>2017</u>
SERIES S	4.00%	June-18	0	2,060,000
SERIES D	4.00%	February-18	0	355,000
SERIES I	4.25%	April-18	0	2,880,000
SERIES H	4.25%	April -18	0	2,996,000
SERIES K	4.25%	April -18	0	4,991,000
SERIES M	4.25%	May-18	0	1,000,000
SERIES Q	4.25%	May-18	0	5,000,000
SERIES R	4.25%	May-18	0	1,000,000
SERIES N	4.25%	May-18	0	75,000
SERIES R	4.25%	Juli-18	2,000,000	2,000,000
SERIES Y	4.25%	November-18	2,999,000	2,999,000
SERIES AB	4.50%	January-19	3,451,000	3,451,000
SERIES A	4.50%	January-19	2,500,000	0
SERIES C	4.50%	January-19	2,000,000	2,000,000
SERIES Z	4.25%	February-19	2,000,000	2,000,000
SERIES V	4.38%	February-19	4,239,000	0
SERIES AB	4.25%	March-19	3,090,000	3,090,000
SERIES AD	4.25%	March-19	2,250,000	2,250,000
SERIES M	4.25%	March-19	2,150,000	2,150,000
SERIES N	4.25%	April-19	500,000	500,000
SERIES AE	4.25%	April-19	1,000,000	1,000,000
SERIES AF	4.25%	May-19	2,469,000	2,469,000
SERIES AG	4.25%	June-19	2,000,000	2,000,000
SERIES AH	4.25%	July-19	1,500,000	1,500,000
SERIES AO	4.00%	July-19	4,000,000	0
SERIES AJ	4.25%	July-19	3,000,000	3,000,000
SERIES AS	4.00%	August-19	355,000	0
SERIES U	4.50%	August-19	1,250,000	1,250,000
SERIES AT	4.00%	August-19	622,000	0
SERIES AV	4.00%	September-19	1,464,000	0
SERIES AK	4.25%	September-19	3,000,000	3,000,000
SERIES AA	4.50%	September-19	720,000	720,000
SERIES W	4.50%	October-19	1,990,000	1,990,000
SERIES AL	4.50%	March-20	1,000,000	1,000,000
SERIES AM	4.50%	March-20	5,000,000	5,000,000
SERIES AN	4.50%	March-20	2,000,000	2,000,000
SERIES AC	4.50%	March-20	1,500,000	1,500,000
SERIES AQ	4.25%	January-20	2,000,000	0
SERIES AU	4.25%	March -20	1,378,000	0
SERIESAW	4.25%	March -20	210,000	0
SERIES BD	4.50%	March -20	1,100,000	0
SERIES AY	4.25%	April-20	1,155,000	0
SERIES AZ	4.25%	April-20	1,300,000	0
SERIES BA	4.25%	May-20	2,250,000	0
SERIES BB	4.25%	May-20	780,000	0
SERIES BC	4.25%	May-20	3,900,000	0
SERIES BE	4.25%	June-20	849,000	0
SERIES BF	4.25%	June-20	2,870,000	0

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SERIES BG	4.25%	June-20	530,000	0
SERIES AP	4.38%	July-20	960,000	0
SERIES T	4.50%	July-20	1,800,000	1,800,000
SERIES AR	4.50%	February-21	2,000,000	0
SERIES AA	4.50%	February -21	1,761,000	1,761,000
SERIES E	5.00%	February -21	7,017,000	7,017,000
SERIES K	5.00%	February -21	4,991,000	0
SERIES AI	4.75%	July-21	1,200,000	1,200,000
SERIES U	5.00%	September-21	1,858,000	1,858,000
SERIES X	5.00%	November-21	<u>1,657,000</u>	<u>1,657,000</u>
			103,115,000	96,521,000
		Less issuance cost	<u>(266,778)</u>	<u>(211,569)</u>
			<u>102,848,222</u>	<u>96,309,431</u>

As of June 30, 2018 and 2017, there have been no defaults in the payment of principal and interest in relation to negotiable commercial notes.

(15) Ordinary Bonds

The Financial Superintendence of Colombia through Resolution 015094871-006-000 of October 8, 2015 authorized the incorporation of Ordinary Bonds in the National Registration of Securities and Issuers and its public offer.

As of June 30, 2018, the subsidiary in Colombia has issued medium-term ordinary bonds by B/.12,152,920 (2017: B/.14,310,229) at a rate of 10.05% (2017: 10.05%) for 5 years term, its maturity are December 10, 2020.

As of June 30, 2018 and 2017, there have been no defaults in the payment of principal and interest in relation to ordinary bonds.

(16) Investment Certificates

The Bank is authorized by the Superintendence of Securities Market of El Salvador for an issuance of B/.30,000,000 in Investments Certificates (IC).

<u>Type</u>	<u>Interest rate</u>	<u>Maturity</u>	<u>2018</u>	<u>2017</u>
Tranche 7	6.00%	June-18	0	2,000,000
Tranche 8	6.00%	June -18	0	2,000,000
Tranche 9	6.25%	June -19	3,000,000	3,000,000
Tranche 10	6.25%	July -18	2,000,000	2,000,000
Tranche 11	6.25%	August-19	3,000,000	3,000,000
Tranche 12	6.25%	August-19	<u>1,600,000</u>	<u>1,600,000</u>
			9,600,000	13,600,000
		Less issuance costs	<u>(0)</u>	<u>(0)</u>
			<u>9,600,000</u>	<u>13,600,000</u>

As of June 30, 2018 and 2017, there have been no defaults in the payment of principal and interest in investment certificates.

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(17) Other Negotiable Debts

The Bank was authorized by the Superintendence of Securities of El Salvador for one revolving plan of up to B/.35,000,000 of Negotiable Debt (stock market paper).

	<u>2018</u>			
<u>Tipo</u>	<u>Tasa de interés</u>	<u>Vencimiento</u>	<u>Valor</u>	
Tranche 22	4.5000%	Agugust-18	2,000,000	
Tranche 25	4.2500%	October-18	2,000,000	
Tranche 26	4.2500%	October-18	300,000	
Tranche 27	4.2500%	October-18	1,000,000	
Tranche 28	4.2500%	November-18	3,000,000	
Tranche 35	5.0000%	November-18	1,000,000	
Tranche 40	5.0000%	diciembre-18	630,000	
Tranche 29	5.0000%	February-19	1,000,000	
Tranche 30	5.0000%	February-19	1,000,000	
Tranche 31	5.0000%	March-19	2,000,000	
Tranche 32	5.0000%	March-19	1,000,000	
Tranche 33	5.0000%	March-19	1,000,000	
Tranche 34	5.0000%	March-19	3,000,000	
Tranche 36	5.0000%	May-19	1,000,000	
Tranche 37	5.0000%	May-19	1,000,000	
Tranche 38	5.0000%	May-19	1,000,000	
Tranche 39	5.0000%	June-19	1,553,000	
Tranche 41	5.0000%	June-19	<u>1,000,000</u>	
			24,483,000	
Less issuance costs			<u>(46,403)</u>	
			<u>24,436,597</u>	

	<u>2017</u>			
<u>Type</u>	<u>Interest Rate</u>	<u>Maturity</u>	<u>Amount</u>	
Tranche 19	4.75%	March, 2018	3,000,000	
Tranche 20	4.50%	May, 2018	1,000,000	
Tranche 21	4.50%	June, 2018	1,000,000	
Tranche 23	4.25%	April, 2018	85,000	
Tranche 24	4.25%	April, 2018	1,000,000	
Tranche 22	4.50%	August, 2018	2,000,000	
Tranche 25	4.25%	October, 2018	2,000,000	
Tranche 26	4.25%	October, 2018	300,000	
Tranche 27	4.25%	October, 2018	1,000,000	
Tranche 28	4.25%	November, 2018	<u>2,480,000</u>	
			13,865,000	
Less issuance costs			<u>(24,953)</u>	
			<u>13,840,047</u>	

As of June 30, 2018 and 2017, there have been no defaults in the payment of principal and interest in other negotiable debts.

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(18) Borrowed Funds

Borrowed funds are summarized as follows:

	<u>2018</u>	<u>2017</u>
Line of credit for working capital for B/.5,000,000, with maturity the year 2020 renewable at the parties' option and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	5,000,000	1,500,000
Line of credit for working capital for B/.30,000,000, with maturity the year 2021 and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	12,051,375	13,773,000
Line of credit for working capital for B/.10,000,000, with maturity the year 2019 renewable at the parties option and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	0	8,000,000
Revolving line of credit for working capital for B/.20,000,000, with maturity the year 2020 renewable at the parties option and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	18,500,000	12,500,000
Line of credit for working capital for B/.5,000,000, with maturity the year 2020, renewable at the parties' option and fixed annual interest rate backed by a portfolio of residential mortgage loans.	5,000,000	0
Line of credit for working capital for B/.12,000,000, with maturity the year 2019 and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	2,000,000	1,450,000
Line of credit for working capital for B/.13,000,000, with maturity the year 2018 renewable at the parties option and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans	8,692,308	9,923,077
Line of credit for working capital for B/.25,000,000, with maturity the year 2019 and annual Libor interest rate plus a margin backed by a portfolio of residential mortgage loans.	25,000,000	25,000,000
Line of credit for working capital for B/.25,000,000, with maturity the year 2019 and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	<u>16,850,000</u>	<u>19,633,333</u>
Sub - total going to next page	<u>88,996,077</u>	<u>68,848,509</u>

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(18) Borrowed Funds, continued

	<u>2018</u>	<u>2017</u>
Sub - total coming from previous page	<u>88,996,077</u>	<u>68,848,509</u>
Line of credit for working capital for B/.35,000,000, with maturity the year 2020 and fixed rate.	35,000,000	40,000,000
Line of credit for working capital for B/.15,000,000, with maturity the year 2021 and fixed rate annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	6,966,666	2,616,666
Line of credit for working capital for B/.25,000,000, with maturity the year 2022 and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	16,071,429	17,857,143
Line of credit for working capital for B/.32,000,000, with maturity the year 2024 and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	30,857,143	16,000,000
Line of credit for working capital for B/.17,000,000, with maturity the year 2020 and annual Libor interest rate plus a margin, backed by a portfolio of residential mortgage loans.	17,000,000	17,000,000
Line of credit for working capital for B/.4,000,000 (COP 12 thousand millions), with maturity the year 2019 renewable at the parties' option and annual interest rate DTF plus a margin.	113,735	1,429,848
Revolving line of credit for working capital up to approximately B/.4,000,000 (COP 12 thousand millions), with maturity the year 2019 renewable at the parties' option and annual interest rate DTF plus a margin.	<u>511,795</u>	<u>1,340,483</u>
Total	199,614,360	188,023,550
Less issuance costs	<u>(764,289)</u>	<u>(876,016)</u>
Total of borrowed funds	<u>198,850,071</u>	<u>187,147,534</u>

As at June 30, 2017 and 2017, there has no defaults in the payment of capital and interest in relation to the borrowings.

(19) Other Liabilities

The other liabilities are detailed as follows:

	<u>2018</u>	<u>2017</u>
Accrued interest payable of deposits, borrowed funds and other obligations	3,805,470	3,532,444
Allowance for employee benefits and other benefits	1,097,031	831,344
Cashier's checks	1,604,853	1,179,951
Others	<u>4,957,379</u>	<u>5,863,854</u>
	<u>11,464,733</u>	<u>11,407,593</u>

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(20) Capital and Reserves

The composition of common shares is detailed as follows:

	<u>2018</u>	<u>2017</u>
Authorized shares with nominal value B/.1,000	<u>15,000</u>	<u>15,000</u>
Shares issued and paid on January 1st and at the end of the period	15,000	15,000
Treasury Shares	<u>(727)</u>	<u>0</u>
Carrying amount of the shares at the end of the period	<u>14,273,000</u>	<u>15,000,000</u>

Reserves

Nature and purpose of reserves:

Capital Reserve

One of the subsidiaries constitutes a reserve to support any loans portfolio's impairment loss considering the country risks in which the debtors are located. This reserve is established from the retained earnings.

Fair Value Reserve

Comprises the cumulative net change in the fair value of available-for-sale financial assets, until the assets is derecognized, redeemed, or impaired. In addition, includes the net amount of the loan portfolio acquired fair value, which will be amortized during the remaining life of the loans or until been cancelled.

Currency Conversion Reserve

Comprises all foreign exchange differences arising on foreign currency translation to the currency presented in the financial statements of foreign subsidiaries with a functional currency different from the presentation currency for purposes of presentation of the consolidated financial statements.

Dynamic Provision

Is constituted according to prudential criteria on all credit facilities that lack specific provision allocated, i.e. on credit facilities classified in the Normal category, as defined in the Agreement No. 004-2013 issued by the Superintendence of Banks of Panama. It corresponds to an equity account presented under the heading of regulatory reserve in the statement of changes in equity and appropriates retained earnings.

Specific Provision in Excess

Provisions that are to be constituted on the basis of the classification of credit facilities in the risk categories Watch list, Substandard, Doubtful or Loss, as provided in the Agreement No. 004-2013 issued by the Superintendence of Banks of Panama. They are for individual credit facilities as for a group of these. For a group corresponds to circumstances indicating the existence of deterioration in credit quality, although it is not yet possible the individual

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(20) Capital and Reserves, continued

identification. It corresponds to an equity account that is presented under the heading of regulatory reserve in the statement of changes in equity and appropriates retained earnings.

(21) Income per Share

The calculation of basic income per share is based on net income attributable to common shareholders by the weighted average number of common shares outstanding.

Attributable income to common shareholders:

	<u>2018</u>	<u>2017</u>
Net income for the year	2,134,161	1,739,787
Attributable net income to the common shareholders	2,134,161	1,739,787

Weighted average of common shares:

	<u>2018</u>	<u>2017</u>
Issued shares at January 1st	15,000	15,000
Weighted average of common shares	14,273	15,000

Net income attributable to common stockholders is as follows:

	<u>2018</u>	<u>2017</u>
Attributable income to common shareholders	2,134,161	1,739,787
Weighted average of common shares (basics)	14,273	15,000
Income per share basic and diluted	149.52	115.99

(22) Service Commissions, Net and Other Income

The breakdown of service commissions and other income are detailed as follows:

	<u>2018</u>	<u>2017</u>
Commissions for administration and management:		
Trusts administration	765,166	826,758
Management collection	1,057,204	987,086
Insurance management	194,037	363,660
Others	752,396	572,336
	<u>2,768,803</u>	<u>2,749,840</u>

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Other income:

Income on sale of tax credit	553,034	65,887
Trusts	1,513	1,669
Insurance	75,997	75,116
Sale of foreclosed assets	24,795	25,318
Other income	<u>774,257</u>	<u>326,549</u>
	<u>1,429,596</u>	<u>494,539</u>

(23) Commission Expenses

The detail of commission expenses are detailed as follows:

	<u>2018</u>	<u>2017</u>
Commissions expenses:		
NCP commissions	84,246	249,209
NCN commissions	73,222	152,957
Line of credit commissions	160,729	194,545
Other commissions	<u>297,966</u>	<u>185,877</u>
	<u>616,163</u>	<u>782,588</u>

(24) Salaries, Other Personnel Expenses, and Other Operating Expenses

Salaries, other personnel expenses, and other operating expenses are detailed as follows:

	<u>2018</u>	<u>2017</u>
Salaries and other personnel expenses:		
Wages, thirteenth month and vacations	2,730,254	2,568,059
Representation expenses	480,255	451,245
Bonuses	301,482	494,249
Social security costs	386,204	335,813
Severance costs	163,355	115,211
Travel, allowances and fuel	69,221	78,728
Others	<u>377,850</u>	<u>387,184</u>
	<u>4,508,621</u>	<u>4,430,489</u>

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(24) Salaries, Other Personnel Expenses, and Other Operating Expenses, continued

	<u>2017</u>	<u>2016</u>
Other operational expenses:		
Rent	390,334	304,297
Advertising	378,686	353,288
Equipment maintenance	420,048	340,853
Office supplies	59,050	62,982
Utilities expenses	147,114	140,230
Bank charges	77,554	55,147
Other expenses	<u>646,166</u>	<u>715,648</u>
	<u>2,118,952</u>	<u>1,972,445</u>

Options Plan of Purchase of Shares

In 2014 and 2012, the Board of La Hipotecaria (Holding), Inc. approved plans to grant options to executives of the Bank for 15,200 options with a unit fair value of B/.8.591 and 19,290 options with a unit fair value of B/.3.694, respectively, with exercise maturity in 10 years for each plan. As of June 30, 2017, there are 29,491 options outstanding (2017: 29,491), has not been cancelled options (2017: 0) and at the reporting date no options has been exercised. These options has a weighted-average price of exercise of B/.27.13 (2017: B/.27.13). The plans gives the executive the right to exercise the options over La Hipotecaria (Holding), Inc. shares, at the time of the first anniversary of both plans. In 2018 the Bank has not recorded any expense for options issuance (2017: B/.0).

(25) Income Tax

The statements of income tax of the Bank incorporated in the Republic of Panama, according to current tax regulations are subject to review by tax authorities for up to three (3) years. According to current tax regulations, companies incorporated in Panama are exempt of income tax for earnings from foreign operations, interest earned on deposits in local banks, government securities and debt Panama investments in securities listed with the Superintendence of stock market securities and traded on the Bolsa de Valores de Panama, S. A. (Stock Exchange of Panama).

According as required by Article 699 of the Tax Code, as amended by Article 9 of Law 8 of March 15, 2010 with effect from January 1, 2010, the income tax for legal entities engaged in the business banking in the Republic of Panama, they should calculate the tax according to the rate of 25%.

Additionally, legal entities whose taxable income exceeds one million five hundred thousand dollars (B/.1,500,000) annually, will pay tax by the applicable income tax rate to the taxable net income according to current legislation in the Republic of Panama or the alternative calculation, which results higher.

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(25) Income Tax, continued

Act 52 of August 28, 2012, restored the payment of estimated income tax from September 2012. According to this law, the estimated income tax payable in three equal amounts over June, September and December each year.

The Bank's subsidiaries shall calculate the income tax according the following rates:

	<u>Colombia</u>	<u>El Salvador</u>
Current rates	34%	30%

The Congress of the Republic of Colombia, enacted the 1607 Act on December 26, 2012, introducing major reforms to the Colombian tax system, mainly the following:

- Taxpayers of income tax for equity are not required to pay contributions to SENA and ICBF for employees earning less than 10 minimum monthly wages; this exemption will be extended for the contributions to the contributory health scheme from the first of January 2014.
- The concept of permanent establishment is defined, which is identified as a fixed place through which a foreign Bank develops business in the country.
- The method on how to calculate the taxable and non-taxable profits for companies that distribute profits to its partners or shareholders is amended.
- New rules are introduced on the transfer pricing regime. Among others, the scope of the transactions with related parties located in free zones is increased and some operations from taxpayers with foreign entities related to a permanent establishment in Colombia or abroad are regulated.

For this purpose, the Technical Board of Public Accountancy of Colombia, through the strategic management directions classified the companies in groups according to our analysis with cutoff date of December 31, 2013, the subsidiaries in Colombia belong to Group 2, classified as SMEs, in which transition period begins on January 1, 2015 and the issuance of the financial statements under International financial Reporting Standards in 2016.

The total expense on income tax as at December 31, 2017 is detailed is follows:

	<u>2018</u>	<u>2017</u>
Estimated income tax	872,480	723,028
Deferred tax temporary differences	(35,836)	6,716
Total income tax costs	<u>836,644</u>	<u>729,744</u>

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(25) Income Tax, continued

The effective rate of the estimated income tax is detailed as follows:

	<u>2018</u>	<u>2017</u>
Profit before income taxes	2,970,805	2,469,531
Income tax expense	<u>836,644</u>	<u>729,744</u>
Effective rate of income tax	<u>28.16%</u>	<u>29.55%</u>

The deferred income tax arises from temporary differences relating to the provision for loan losses and the operative losses carry forward. Deferred tax asset is included as part of other assets in the consolidated statement of financial position.

Deferred income tax is comprised as follows:

	<u>2018</u>		<u>2017</u>	
	<u>Temporary differences</u>	<u>Deferred tax</u>	<u>Temporary differences</u>	<u>Deferred tax</u>
Deferred tax assets				
Allowance for loan losses	580,994	164,930	309,028	77,257
Operative losses carry forward (1)	<u>2,691,565</u>	<u>915,132</u>	<u>1,860,288</u>	<u>465,072</u>
	<u>3,272,559</u>	<u>1,080,062</u>	<u>2,169,316</u>	<u>542,329</u>

(1) Correspond to losses carry forward in Colombia, without expiration date.

Deferred tax movement is as follows:

	<u>2018</u>	<u>2017</u>
Beginning Balance	987,891	554,811
Adjustment under IFRS 9	40,019	0
Balance as of January 1st, 2018	1,027,910	554,811
Provision for loan losses	35,836	(6,717)
Operative losses carry forward	16,316	(5,765)
Deferred tax at period end	<u>1,080,062</u>	<u>542,329</u>

The conciliation between financial income before income tax and net income tax as at December 31, 2017, is a follows:

	<u>2018</u>	<u>2017</u>
Net financial income before income tax	2,970,805	2,469,531
Calculation of "expected" income tax expense	742,701	617,383
Non-deductible expenses	369,478	492,038
Income and expense from foreign and exempt sources, net	(433,525)	(511,929)
Change for temporary differences	(52,152)	(6,716)
Difference in foreign tax rates	<u>210,142</u>	<u>125,537</u>
Total income tax	<u>836,644</u>	<u>729,744</u>

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(25) Income Tax, continued

As of December 31, 2017, the Bank has not recognized a liability for deferred income tax of approximately B/.531,510 (2017: B/.497,503) for the retained earnings of its operations abroad, due to the Bank considers that approximately B/.10,630,206 (2017: B/.9,950,063) of its earnings will be reinvested indefinitely.

(26) Trusts under Management

The Bank held in trust management contracts at customer risk amounted to B/.208,153,626 (2017: B/.225,153,486). Considering the nature of these services, management believes that there are not significant risks for the Bank.

(27) Commitments and Contingencies

The Bank has subscribed lease contracts, for terms of up to five (5) years, related to the use of properties where its offices operate. A detail of annual lease payments that the Bank have to pay for the next five years according the lease contracts is as follows:

<u>Year</u>	<u>Amount</u>
2,019	736,800
2,020	736,800
2,021	736,800
2,022	736,800
2,023	736,800

As of June 30, 2018, there is an ongoing complaint filed against the subsidiary of El Salvador by the Consumer Advocacy. The Bank's management and its legal counsel believe it is not expected that the result of this process have a material adverse effect on the financial position of the Bank.

In the normal course of business, the Bank held financial instruments without-balance sheet risk to cover the financial needs of its customers. As of June 30, 2018, the Bank has issued promise letters for B/.73,902,870 (2016: B/.77,155,573).

(28) Fair value of financial instruments

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Bank determines fair value using other valuation techniques

For financial instruments that are traded on a low frequency and have few availability of pricing information, the fair value is less objective, and its determination requires the use of varying degrees of judgment that depend on liquidity, geographical concentration, uncertainty of market assumptions factors in determining prices and other risks affecting the specific instrument.

The Bank establishes a fair value hierarchy that categorizes into three levels the input data valuation techniques used in measure fair value:

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(28) Fair Value of Financial Instruments, continued

- Level 1: inputs that are quoted market prices (unadjusted) in active markets for identical instruments
- Level 2: Inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Other valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which observable market prices exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premise used in estimating discount rates.

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The following table presents the carrying value and fair value of financial assets and liabilities, by the level in the fair value hierarchy into which the fair value measurement is categorized. This table does not include information on the fair value of financial assets and liabilities measured at fair value when its carrying approximates their fair value.

<u>2018</u>	<u>Carrying amount</u>	<u>Fair Value</u>			<u>Total</u>
		<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:					
Financial assets at fair value:					
Securities – FVOCI	39,210,706	13,182,283	0	26,028,423	39,210,706
Securities – FVTPL	19,130,463	0	565,220	18,565,243	19,130,463
Financial assets not measured at fair value:					
Loans	635,707,559	0	0	662,258,292	662,258,292
Assets - AC	430,337	0	513,965	0	513,965
Liabilities:					
Financial liabilities not measured at fair value:					
Deposits from customer - time	219,668,565	0	0	220,941,930	220,941,930
Negotiable comercial paper	85,144,947	0	0	83,519,436	83,519,436
Negotiable comercial notes	102,848,222	0	0	103,406,776	103,406,776
Ordinary bonds	12,152,920	0	0	12,152,920	12,152,920
Investment certificate	9,600,000	0	0	9,599,882	9,599,882
Other negotiable debt	24,436,597	0	0	24,481,754	24,481,754
Borrowed funds	198,850,071	0	0	198,555,294	198,555,294

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	<u>2017</u>	<u>Carrying amount</u>	<u>Fair Value</u>			<u>Total</u>
			<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:						
Financial assets measured at fair value:						
Securities available for sale		43,898,566	9,864,375	3,767,239	30,266,952	43,898,566
Securities at fair value through profit or loss		15,136,846	0	1,362,746	13,774,100	15,136,846
Financial assets not measured at fair value:						
Loans		595,098,106	0	0	655,644,039	655,644,039
Securities held to maturity		442,132	0	442,132	0	442,132
Liabilities:						
Financial liabilities not measured at fair value:						
Deposits from customers – time		207,555,493	0	0	197,975,512	197,975,512
Negotiable commercial paper		82,931,225	0	0	81,688,132	81,688,132
Negotiable commercial notes		96,309,431	0	0	96,746,641	96,746,641
Ordinary bonds		14,310,229	0	0	14,310,229	14,310,229
Investment certificate		13,600,000	0	0	13,593,290	13,593,290
Other negotiable debt		13,840,047	0	0	13,851,192	13,851,192
Borrowed funds		187,147,534	0	0	182,123,169	182,123,169

As of June 30, 2018, there were not transfers of fair value hierarchy on securities at FVOCI and securities at FVFPL.

The following table shows the valuation technique the input data used and significant unobservable inputs when measuring the fair value of the instruments classified in Level 3 as of June 30, 2018 and as of December 31, 2017:

		<u>Quantitative information Level 3 fair values</u>			
	<u>Valuation technique</u>	<u>Unobservable inputs</u>	<u>2018</u>	<u>Range (weighted average) 2017</u>	
Mortgage bonds	Discounted cash flows	Cumulative Default Assumptions ("SDA")	2.43% - 0.13% (0.76%)	4.48% - 0.14% (1.26%)	
		Cumulative Speed Assumptions and Prepayment rate ("PSA" and "CPR")	49.11% - 19.28% (42.19%)	48.95% - 21.01% (42.66%)	
		Recoveries percentage		90%	
		Estimated time to perform the recoveries	90% 12 months	12 months	
Residual Interests of trust	Discounted cash flows	Cumulative Default Assumptions ("SDA")	2.43% - 0.13% (0.68%)	4.48% - 0.14% (0.84%)	
		Cumulative Speed Assumptions and Prepayment rate ("PSA" and "CPR")	49.11% - 19.28% (42.42%)	48.95% - 21.01% (41.42%)	
		Recoveries percentage		90%	
		Estimated time to perform the recoveries	90% 12 months	12 months	
Government Bonds	The valuation model is based on different prices of observable references on an active market. Present value of the flows of a title, discounting them with the reference rate and the corresponding margin.	N/A	N/A	N/A	

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(28) Fair Value of Financial Instruments, continued

Financial Instrument	Valuation Technique and Observable Input Used
Not measured at fair value:	
Deposits from customers	For saving deposits its fair value represents the outstanding amount expected to receive/pay at reporting date. For time deposits its fair value is determined using discounted cash flows at market interest rate.
Securities held to maturity	Fair value represents the amount receivable / payable at the reporting date.
Loans	The fair value of loans represent the discounted expected cash flow to receive. The cash flows are discounted at market interest rates to assess its fair value.
Repurchase agreements	The value of the future cash flows is discounted using a discount rate that represents the present interest rate of market for financings of new debts with maturity similar surplus.
Borrowed funds	The fair value for loans payable in semiannual interest rate adjustments are determined using the future cash flows discounted at the current market interest rate.
Ordinary bonds	The fair value for ordinary bonds are determined using the future cash flows discounted at the current market interest rate.
Negotiable commercial papers	The fair value for negotiable commercial papers are determined using the future cash flows discounted at the current market interest rate.
Other negotiable debts	The fair value for other negotiable debt are determined using the future cash flows discounted at the current market interest rate.
Negotiable commercial notes and investment certificate	Fair value for the negotiable commercial notes is determined using future cash flows discounted at the current interest rate of the market.

The table below presents the reconciliation as of June 30, 2018 for financial instruments categorized as Level 3 in the hierarchy of levels of fair value:

	<u>2018</u>	<u>2017</u>
Balance at the beginning of the year	44,041,052	45,752,935
Total income or (loss):		
In the consolidated statement of income	624,700	970,056
In the consolidated statement of comprehensive income	(40,917)	(389,310)
Purchases	4,344,253	922,246
Sales	<u>(4,375,422)</u>	<u>(3,214,875)</u>
Balance at the end of the year	<u>44,593,666</u>	<u>44,041,052</u>

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(28) Fair Value of Financial Instruments, continued

Although the Bank believes that its estimates of fair value are appropriate, the use of different methodologies or assumptions could lead to different measurements of fair value. For fair value measurements in Level 3, changing one or more assumptions to reflect reasonable alternative assumptions would have the following effects:

	<u>2018</u>		Effect on Other	
	Effect on Consolidated		Comprehensive Income	
	Statement of Income		(Loss)	
	<u>Favorable</u>	<u>(Unfavorable)</u>	<u>Favorable</u>	<u>(Unfavorable)</u>
Investments at fair value through profit or loss	1,144,806	(744,303)	0	0
Securities at FVOCI	<u>0</u>	<u>0</u>	<u>1,069,805</u>	<u>(850,351)</u>
	<u>1,144,806</u>	<u>(744,303)</u>	<u>1,069,805</u>	<u>(850,351)</u>

	<u>2017</u>		Effect on Other	
	Effect on Consolidated		Comprehensive Income	
	Statement of Income		(Loss)	
	<u>Favorable</u>	<u>(Unfavorable)</u>	<u>Favorable</u>	<u>(Unfavorable)</u>
Investments at fair value through profit or loss	1,106,247	(761,940)	0	0
Securities at FVOCI	<u>0</u>	<u>0</u>	<u>1,101,706</u>	<u>(921,133)</u>
	<u>1,106,247</u>	<u>(761,940)</u>	<u>1,101,706</u>	<u>(921,133)</u>

Favorable and unfavorable effects of using reasonably possible alternative assumptions for the valuation of mortgage bonds and bonds of residual interests in securitizations are calculated recalibrating the values of the models, using methods based on possible estimates of unobservable inputs of the Bank.

The most important unobservable data inputs refer to the risk discount rates. The reasonable alternative assumptions are 0.5% below and 0.5% higher, respectively, of discount rates used in the models.

The Bank has established a control framework with respect to the measurement of fair values. This control framework includes a separate management unit reporting directly to the Executive Vice President of Finance, and has independent responsibility to verify the results of the operations of investment and significant fair value measurements.

Specific controls include:

- Checking the quoted prices;
- Validation or "re-performance" of valuation models;

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(28) Fair Value of Financial Instruments, continued

- Review and approval of the processes for new models and changes to existing valuation models;
- Review of significant unobservable data; adjustments and significant changes in fair value of Level 3 compared with the previous month.

The Bank uses a third party, as a service provider for this control unit evaluates and documents the evidence obtained from such third parties that support the conclusion that such assessments meet the requirements of IFRS. This review includes:

- Verify that the vendor price is approved by the Bank;
- Obtain an understanding of how the fair value has been determining and whether it reflects current market transactions;
- When similar instruments are used to determine fair value, how these prices have been adjusted to reflect the characteristics of the instrument being measured.

This process is also monitored by the Audit Committee through Internal Audit.

(29) Segment Information

The segment information of the Bank is presented regarding its business lines and has been determined by management based on reports by senior management for decision making.

The composition of the business segments is described as follows:

- *Trust Administration:* This segment includes commissions earned by management and collection of mortgage and personal loans belonging to third parties, which hires the Bank under management contracts to carry out such function.
- *Mortgages as assets:* Within this concept interest income is recognized less costs *generated* by financing mortgages loans that Bank hold as assets, plus commissions for disbursements and the proportional share of the commissions from collections and reinsurance services from the insurance Bank to which it provides the service of reinsurance.
- *Personal loans as assets:* Within this concept interest income is recognized less costs generated by financing personal loans that Bank hold as assets, plus commissions for granted and the proportional share of the commissions from collections and reinsurance services from the insurance Bank to which it provides the service of reinsurance.
- *Other investments:* This concept includes the income generated by other investments of the Bank.

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(29) Segment Information, continued

<u>2018</u>	<u>Trust administration</u>	<u>Mortgage as assets</u>	<u>Personal loans as assets</u>	<u>Other investments</u>	<u>Total</u>
Interest income	0	18,779,832	2,510,494	672,526	21,962,852
Commission on management and servicing, net	1,109,987	1,530,377	128,439	0	2,768,803
Commission on loan granting	0	923,725	291,546	0	1,215,271
Interest and commission expense	0	(13,647,640)	(853,731)	(1,042,434)	(15,543,805)
Provision for loan losses	0	(409,831)	(138,573)	0	(548,404)
Gain on investments, net	0	0	0	843,053	843,053
Other income	0	1,255,202	78,519	95,875	1,429,596
Operating expenses	<u>(787,890)</u>	<u>(6,217,944)</u>	<u>(1,724,840)</u>	<u>(425,887)</u>	<u>(9,156,561)</u>
Profit by segment before tax	<u>322,097</u>	<u>2,213,721</u>	<u>291,854</u>	<u>143,133</u>	<u>2,970,805</u>
Segment assets					
Segment liabilities	<u>0</u>	<u>618,801,384</u>	<u>53,065,065</u>	<u>64,794,157</u>	<u>736,660,605</u>
<u>2017</u>	<u>Trust administration</u>	<u>Mortgage as assets</u>	<u>Personal loans as assets</u>	<u>Other investments</u>	<u>Total</u>
Interest income	0	15,532,854	2,053,135	2,547,408	20,133,397
Commission on management and servicing, net	564,625	2,069,972	115,243	0	2,749,840
Commission on loan granting	0	813,731	325,863	0	1,139,594
Interest and commission expense	0	(12,249,310)	(723,384)	(911,816)	(13,884,511)
Provision for loan losses	0	(66,751)	(84,743)	0	(151,494)
Gain on investments, net	0	0	0	647,212	647,212
Other income	0	436,296	25,766	32,477	494,539
Operating expenses	<u>(907,326)</u>	<u>(5,759,548)</u>	<u>(1,597,683)</u>	<u>(394,490)</u>	<u>(8,659,046)</u>
Profit by segment before tax	<u>(342,701)</u>	<u>777,244</u>	<u>114,196</u>	<u>1,920,791</u>	<u>2,469,531</u>
Segment assets	<u>0</u>	<u>544,969,073</u>	<u>48,216,352</u>	<u>60,776,056</u>	<u>653,961,482</u>
Segment liabilities	<u>0</u>	<u>517,152,988</u>	<u>30,540,529</u>	<u>38,495,921</u>	<u>586,189,438</u>

The composition of the geographic segments is described as follows:

<u>2018</u>	<u>Panama</u>	<u>El Salvador</u>	<u>Colombia</u>	<u>Total</u>
Interest income	14,489,689	4,471,329	3,001,834	21,962,852
Commission on management and servicing, net	2,198,634	510,179	59,990	2,768,803
Commission on loan granting	972,599	242,672	0	1,215,271
Interest and commission expense	(11,368,254)	(2,598,658)	(1,576,893)	(15,543,805)
Provision for loan losses	(344,946)	(167,736)	(35,722)	(548,404)
Gain on investments, net	674,397	0	168,656	843,053
Other income	1,251,196	123,784	54,616	1,429,596
Operating expenses	<u>(6,483,727)</u>	<u>(1,493,074)</u>	<u>(1,179,760)</u>	<u>(9,156,561)</u>
Profit by segment before tax	<u>1,389,588</u>	<u>1,088,496</u>	<u>492,721</u>	<u>2,970,805</u>
Segment assets				
Segment liabilities	<u>546,614,079</u>	<u>125,234,754</u>	<u>64,811,772</u>	<u>736,660,605</u>

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(29) Segment Information, continued

<u>2017</u>	<u>Panama</u>	<u>El Salvador</u>	<u>Colombia</u>	<u>Total</u>
Interest income	13,385,666	3,995,078	2,752,653	20,133,397
Commission on management and servicing, net	2,107,016	581,270	61,554	2,749,840
Commission on loan granting	931,137	208,457	0	1,139,594
Interest and commission expense	(9,876,302)	(2,175,497)	(1,832,712)	(13,884,511)
Provision for loan losses	(158,923)	(24,546)	31,975	(151,494)
Gain on investments, net	647,212	0	0	647,212
Other income	397,598	95,928	1,013	494,539
Operating expenses	<u>(6,244,797)</u>	<u>(1,441,205)</u>	<u>(973,044)</u>	<u>(8,659,046)</u>
Profit by segment before tax	<u>1,188,607</u>	<u>1,239,485</u>	<u>41,439</u>	<u>2,469,531</u>
Segment assets	<u>483,516,111</u>	<u>114,825,795</u>	<u>55,619,576</u>	<u>653,961,482</u>
Segment liabilities	<u>457,775,794</u>	<u>95,304,216</u>	<u>33,109,428</u>	<u>586,189,438</u>

(30) Preferential Interests on Mortgage Loans

According to current fiscal regulations in Panama, the financial institutions that grant mortgage loans not exceeding B/.120,000 with preferential interest, receive the benefit of an annual fiscal credit. From July 2010 according to the law 8 of 15 March 2010 repealing Article 6 of Act 3 of 1985, it increases the benefit of a tax credit of ten (10) years, to, the first (15) years for new loans for the purpose of new houses in the amount equal to the difference between the income that the lender would have received if you have taken the benchmark interest rate market, which has been in effect during that year and the actual income received in interest in relation to each preferential mortgage loans.

Law No. 3 of May, 1985 in the Republic of Panama establishes that fiscal credit can be used for payment of national taxes, including income tax. The fiscal credit, under Law No. 11 of September, 1990, which extends the previous law, and Law No. 28 of June, 1995, establishes that it can be used only for payment of income tax. If in any fiscal year the financial institution cannot effectively use the entire fiscal credits to which it is entitled, then it can use the excess credit over the next three years, at their convenience, or transfer, in whole or in part, to another taxpayer.

As of June 30, 2018, the Bank recorded, net of reserve, B/.5,053,330 (2017: B/.4,041,565), as preferential interest income on the portfolio of residential mortgage loans. During the same period, a subsidiary of the Bank sold to third parties prior years' fiscal credits for B/.8,709,954 (2017: B/.87,494), which generated an income of B/.553,034 (2017: B/.1,313).

As of June 30, 2018, the accumulated fiscal credit is included in the consolidated statement of financial position for the amount of B/.5,053,326 (2017: B/.8,479,096).

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(31) Participations in Non-Consolidated Structured Entities

The following table describes the types of structured entities in which the Bank holds a participation and acts as an agent thereof. (See Note 3 a5).

<u>Type</u>	<u>Nature and purpose</u>	<u>Participation maintained by the Bank</u>
Loan Securitization Trusts	Generate: <ul style="list-style-type: none">Funds for lending activities of the BankCommission for administration and management of loan portfolio <p>These trusts are financed by the sale of debt instruments.</p>	Investments in the mortgage bonds issued by the trusts

The participation maintained by the Bank in the non-consolidated structured entities represents 10%, 3% and 5% (2017: 10%, 3% y 5%) in three trusts.

(32) Main Applicable Laws and Regulations

The principal laws and regulations applicable in the Republic of Panama are:

(a) *Banking Law*

Banking operations in the Republic of Panama, are regulated and supervised by the Superintendence of Banks of the Republic of Panama, according to the laws established by Executive Decree No.52 of April 30, 2008, which adopts the only text Decree Law 9 of February 26, 1998, as amended by Decree Law 2 of 22 February 2008, by which the banking system in Panama is established and the Superintendence of Banks and the rules that govern it is created.

(b) *Trust Law*

Trust operations in Panama are regulated by the Superintendence of Banks of Panama in accordance with the legislation established in Law No. 1 of January 5, 1984.

(c) *Securities Law*

The operations brokerage firm in Panama are regulated by the Superintendence of the share market in accordance with the legislation established in Decree Law No.1 of July 8, 1999, reformed by Act No. 67 of September 1, 2011.

The operations of brokerage houses are in the process of adaptation to the Agreement No.4-2011, amended certain provisions by Agreement 8-2013, established by the Superintendence of the share market, which indicate that they have to comply with the capital adequacy rules and modalities.

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(32) Main Applicable Laws and Regulations, continued

The main regulations or norms in the Republic of Panama, which have an effect on the preparation of these consolidated financial statements are described below:

- (a) *General Board Resolution SBP-GJD-0003-2013 issued by the Superintendence of Banks of Panama on July 9, 2013*

This resolution establishes the accounting treatment for those differences arising between prudential standards issued by the Superintendence of Banks and International Financial Reporting Standards (IFRS), such that 1) the accounting records and financial statements are prepared in accordance with IFRS as required by the Agreement No.006 - 2012 December 18, 2012 and 2) in the event that the calculation of a provision or reserve under prudential rules applicable to banks to submit additional accounting specific aspects required IFRS, is greater than the respective calculation under IFRS oversupply or under prudential reserves is recognized in a regulatory reserve in equity.

Prior authorization of the Superintendence of Banks, banks shall be able to partially or totally reverse the provision established, after submitting due justification before the Superintendence of Bank.

- (b) *Agreement No. 003 – 2009 Dispositions on Acquired Foreclosed Assets, issued by the Superintendence of Banks of Panama on May 12, 2009*

For regulatory purposes, the Superintendence sets a term of five (5) years, effective the date of registration before the Public Registry to sell immovable goods acquired for the payment of past due credits. If after that term the Bank has not sold the property acquired, it shall conduct an independent appraisal to determine if its value has decreased, by applying in such case the provisions of IFRS.

Likewise, the Bank shall create a reserve in equity, through the appropriation in the following order of: a) undistributed earnings; b) profits for the period, to which the following value of the foreclosed asset will be transferred:

First year:	10%
Second year:	20%
Third year:	35%
Fourth year:	15%
Fifth year:	10%

The aforementioned reserves shall maintain until the acquired asset is actually transferred, and it shall not be considered a regulatory reserve for purposes of calculating the equity ratio.

- (c) *Agreement No. 004-2013, "Whereby provisions on credit risk management inherent of in credit portfolio and off-balance sheet transactions are established", issued by the Superintendence of Banks of Panama on May 28, 2013.*

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(32) Main Applicable Laws and Regulations, continued

Sets forth general classification criteria for credit facilities in order to determine the specific and dynamic provisions to cover the Bank's credit risk. Additionally, this Agreement establishes certain required minimum disclosures, in line with IFRS disclosure requirements about credit risk management and administration.

This Agreement is effective as of June 30, 2014 and repeals all parts of the Agreement No. 6-2000 of June 28, 2000 and all amendments, Agreement No. 6-2002 of August 12, 2002 and Article 7 of Agreement No. 2-2003 of March 12, 2003.

Specific Provisions

Agreement No.004-2013 sets forth that specific provisions are generated by any objective and concrete evidence of impairment. These provisions shall be recorded for credit facilities classified in the risk categories named: special-mention, substandard, doubtful or loss, both for individual or collective credit facilities.

Banks shall calculate and maintain the amount of the specific provisions determined through the methodology explained in this Agreement, which takes into consideration the balance owed by each credit facility classified in any of the categories subjected to provision, mentioned in the preceding paragraph; the present value of each collateral available as risk mitigating, as established per type of collateral in this Agreement, and a table of estimates applied to the net balance exposed to losses for such credit facilities.

In case of a surplus in the specific provision, calculated in conformity with this Agreement, over the provision calculated in conformity to IFRS; this surplus shall be accounted for in a regulatory reserve in equity increasing or decreasing through allocations from or to retained earnings. The balance of the regulatory reserve shall not be considered as capital funds for purposes of calculating certain indices or ratios mentioned in this Agreement.

The table below summarizes the loans at amortized cost of the Panamanian Bank classified according this Agreement and the specific provision:

<u>Classification</u>	<u>2018</u>		<u>2017</u>	
	<u>Balance</u>	<u>Allowance</u>	<u>Balance</u>	<u>Allowance</u>
Normal	452,388,541	0	429,229,393	0
Watch list	4,619,718	266,977	2,400,218	131,800
Substandard	1,438,374	213,698	1,502,959	228,404
Doubtful	2,077,943	490,082	1,306,821	344,905
Loss	<u>1,291,313</u>	<u>244,825</u>	<u>630,594</u>	<u>111,779</u>
Total	<u>461,815,889</u>	<u>1,215,582</u>	<u>435,069,985</u>	<u>816,888</u>

The table below summarizes the balances of past due and default loans for the principal categories:

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(32) Main Applicable Laws and Regulations, continued

<u>2018</u>	<u>Current</u>	<u>Past due</u>	<u>Default</u>	<u>Total</u>
Loans to customers	<u>447,485,341</u>	<u>10,750,409</u>	<u>3,580,139</u>	<u>461,815,889</u>
<u>2017</u>	<u>Current</u>	<u>Past due</u>	<u>Default</u>	<u>Total</u>
Loans to customers	<u>424,221,337</u>	<u>7,966,451</u>	<u>2,882,197</u>	<u>435,069,985</u>

As of June 30, 2018, the balances of the loans which accumulation of interests has been suspended due to an impairment in the quality of the credit or for the nonperformance of payment in accordance with the indicated in the Agreement No. 4-2013 was of B/.1,615,393 (2017: B/.1,342,105).

Dynamic Provision

Agreement No. 004 - 2013 indicates that the dynamic provision is a reserve established to meet possible future needs for establishment of specific provisions, which is governed by its own prudential bank regulation criteria. The dynamic provision constitutes at quarterly basis on credit facilities that lack specific provision allocated, i.e. on credit facilities normally classified category.

The dynamic provisioning is a heritage item that increases or decreases with assignments to or from retained earnings. The credit balance of this provision is part of dynamic regulatory capital but does not replace or offset the capital adequacy requirements established by the Superintendence.

The balance of dynamic provision of the Bank is as follows

	<u>2018</u>	<u>2017</u>
Banco La Hipotecaria, S. A.	4,844,652	4,844,652
La Hipotecaria, S. A. de C.V.	1,416,926	1,416,926
La Hipotecaria C. F., S. A.	<u>601,678</u>	<u>601,678</u>
Total	<u>6,863,256</u>	<u>6,863,256</u>

With this Agreement is established a dynamic provision which will not be less of 1.25%, nor higher to 2.50% of the risk weighed assets corresponding to credit facilities classified as normal.

By requirements of Agreement No.004-2013, is constituted a regulatory provision of B/.955,681 (2017: B/.701,268) which represents the excess of regulatory provision over the allowance for loan losses according IFRS.

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(32) Main Applicable Laws and Regulations, continued

The principal laws and regulations applicable in the Republic of El Salvador are:

- (a) *Law of the Superintendence of Corporate Obligations (formerly Business Enterprises)*
The operations of business enterprises in El Salvador are regulated by the Superintendence of Companies and Corporations, contained in Legislative Decree No.448 of 09 October 1973.
- (b) *Securities Law*
The operations of issuers and brokerage positions in El Salvador are regulated by the Securities in accordance with the procedures established in the Decree Law No.809 of April 31, 1994. According to Legislative Decree No.592 of 14 January 2011, the Securities ceased to exist as of August 2, 2011, which contains the Law on Regulation and Supervision of the Financial System, published in Official Journal No.23 of February 2, 2011, which became effective on August 2, 2011, and gave birth to the new Financial System Superintendence as single supervisory body that integrates the functions of the former Superintendence of the Financial System, Pensions and Securities.

The principal laws and regulations applicable in the Republic of Colombia are:

- (a) *Laws for Commercial Business*
The operations of commercial business in Colombia are regulated by the Superintendence of Companies in accordance with the laws established in the Decree Law No.222 of December 20, 1995.
- (b) *Equity Tax*
According to Decree 4825 of December 29, 2010, issued by the Ministry of Finance and Public Credit, establishing the state tax applicable to juridical persons, natural and indeed societies. This tax is generated by the possession of wealth by January 1st of 2011, whose value equals or exceeds one billion dollars and less than three billion pesos. The tax rate ranges from 1% to 1.4% and added a surcharge of 25% of the estate tax result. The estate tax is presented in the consolidated statement of comprehensive income in the area of taxes.

(33) Changes in accounting policies

Except for the changes below, the Bank has consistently applied the accounting policies established in Note 3 to all the periods presented in these consolidated financial statements.

IFRS 9 – Financial Instruments Financieros

The Bank has adopted IFRS 9 Financial Instruments issued in July 2014 with an initial application date of January 1, 2018. The requirements of IFRS 9 represent a significant change in IAS 39 Financial Instruments: Recognition and Measurement. The new standard brings fundamental changes in the accounting of financial assets and in certain aspects of the accounting of financial liabilities.

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(33) Changes in accounting policies, continued

The key changes in the Bank's accounting policies resulting from its adoption of IFRS 9 are summarized below:

Classification of financial assets and financial liabilities

IFRS 9 contains three main categories of classification for financial assets: measured at amortized cost (CA), fair value with changes in other comprehensive income (VRCOUI), and fair value through profit or loss (VRCR). The classification of IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates existing categories of IAS 39 as held-to-maturity, loans and accounts receivable and securities available for sale. Under IFRS 9, derivatives implicit in contracts where the receiver is a financial asset within the scope of the Standard it is not divided. In contrast, the complete hybrid instrument is evaluated for classification. See Note 3, for an explanation of how the Bank classifies financial assets according to IFRS 9.

IFRS 9 retains to a large extent the requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all changes in the fair value of the liabilities designated under the fair value option were recognized in profit or loss, in accordance with IFRS 9, changes in fair value are generally presented as follows:

- The amount of the change in fair value attributable to changes in the credit risk of the liability is presented in other comprehensive income, and
- The remaining amount of change in fair value is presented in profit or loss. See Note 3, for an explanation of how the Company classifies financial liabilities according to IFRS 9.

Impairment of financial assets

IFRS 9 replaces the "incurred loss" model in IAS 39 with an "expected credit loss" (ECL) model. The new impairment model also applies to certain loan commitments and financial guarantee contracts, but not to equity investments.

According to IFRS 9, credit losses are recognized before compared to IAS 39. See Note 3, for an explanation of how the Bank applies the impairment requirements of IFRS 9.

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retroactively, except as described below.

- Comparative periods have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognized in retained earnings and reserves as of January 1, 2018. Consequently, the information presented for 2017 does not reflect the requirements of IFRS 9 and, therefore, is not comparable to the information presented for 2018 under IFRS 9.

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- The following evaluations have been made based on the facts and circumstances that existed on the date of the initial application:
 - The determination of the business model within which a financial asset is maintained.
 - The designation and revocation of previous designations of certain financial assets and financial liabilities measured at FVTPL.
 - The designation of certain investments in equity instruments not held for trading as in FVOCI.
- If an investment in debt securities had a low credit risk at the date of initial application of IFRS 9, then the Bank has assumed that the credit risk on the asset has not increased significantly since its initial recognition.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, see Note 34.

(34) Financial Assets and Financial Liabilities

Classification of financial assets and financial liabilities

The following table provides a reconciliation between line items in the consolidated statement of financial position and categories of financial instruments:

June 30, 2018	<u>Mandatory to FVTPL</u>	<u>Investment in securities at FVOCI</u>	<u>Amortized cost</u>	<u>Carrying amount</u>
Financial assets				
Cash and cash equivalent				
Deposits in banks:			26,880,099	26,880,099
Investment in securities:				
Measurement at amortized cost	0	0	430,337	430,337
Measurement at fair value	19,130,463	39,210,706	0	58,341,169
Loans at amortized cost	<u>0</u>	<u>0</u>	<u>635,126,563</u>	<u>635,126,563</u>
Total financial assets	<u>19,130,463</u>	<u>39,210,706</u>	<u>662,436,999</u>	<u>721,359,164</u>
Financial liabilities				
Deposits from customer:				
Local savings			928,170	928,170
Foreign savings			191,414	191,414
Local time			199,502,700	199,502,700
Foreign time			20,165,865	20,165,865
Negotiable commercial paper			85,144,947	85,144,947
Negotiable commercial notes			102,848,222	102,848,222
Ordinary bonds			12,152,920	12,152,920
Investment certificates			9,600,000	9,600,000
Investment certificates			24,436,597	24,436,597
Borrowed funds			198,850,071	198,850,071
Total financial liabilities			<u>653,820,906</u>	<u>653,820,906</u>

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(34) Financial Assets and Financial Liabilities, continued

	<u>Negotiable</u>	<u>Amortized cost</u>	<u>Held to maturity</u>	<u>Loans and accounts receivable</u>	<u>Available for sale</u>	<u>Carrying amount</u>
December 30, 2017						
<u>Financial assets</u>						
Cash and cash equivalent						
Deposit in banks				27,534,184		27,534,184
Investment in securities:						
Measurement at amortized cost			442,132			442,132
Measurement at fair value	15,136,846				43,933,581	59,070,427
Loans at amortized cost				<u>594,784,481</u>		<u>594,784,481</u>
Total financial assets	<u>15,136,846</u>		<u>442,132</u>	<u>622,318,665</u>	<u>43,933,581</u>	<u>681,831,224</u>
<u>Financial liabilities</u>						
Deposits from customer:						
Local savings		139,388				139,388
Foreign savings		189,621,270				189,621,270
Local time		17,934,223				17,934,223
Foreign time		851,096				851,096
Negotiable commercial paper		82,931,225				82,931,225
Negotiable commercial notes		96,309,431				96,309,431
Ordinary bonds		14,310,229				14,310,229
Investment certificates		13,600,000				13,600,000
Investment certificates		13,840,047				13,840,047
Borrowed funds		187,147,534				187,147,534
Total financial liabilities		<u>616,684,443</u>				<u>616,684,443</u>

Classification of financial assets and financial liabilities as of the date of the adoption of IFRS 9.

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories according to IFRS 9 for the financial assets and liabilities of the Bank as of January 1, 2018.

	<u>Original classification under IAS 39</u>	<u>New classification under IFRS 9</u>	<u>Original carrying amount under IAS 39</u>	<u>New carrying amount under IFRS 9</u>
<u>Financial assets</u>				
Cash and cash equivalent				
Deposits in banks:	Loans and account receivable	Amortized cost	27,534,184	27,534,184
Investment in securities:				
Measurement at amortized cost	Investments held to maturity	Amortized cost	442,132	441,248
Measurement at fair value	Available for sale	FVOCI	43,933,581	40,323,668
Measurement at fair value	FVTPL	FVTPL	15,136,846	18,776,759

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	Loans and account receivable	Amortized cost		
Loans at amortized cost			594,784,481	594,642,440
			<u>681,831,224</u>	<u>681,831,224</u>
Financial liabilities				
Deposits from customer:				
Local savings	Amortized cost	Amortized cost	851,096	851,096
Foreign savings	Amortized cost	Amortized cost	139,388	139,388
Local time	Amortized cost	Amortized cost	189,621,270	189,621,270
Foreign time	Amortized cost	Amortized cost	17,934,223	17,934,223
Negotiable commercial paper	Amortized cost	Amortized cost	82,931,225	82,931,225
Negotiable commercial notes	Amortized cost	Amortized cost	96,309,431	96,309,431
Ordinary bonds	Amortized cost	Amortized cost	14,310,229	14,310,229
Investment certificates	Amortized cost	Amortized cost	13,600,000	13,600,000
Other negotiable debt	Amortized cost	Amortized cost	13,840,047	13,840,047
Borrowed funds	Amortized cost	Amortized cost	187,147,534	187,147,534
Total financial liabilities			<u>616,684,443</u>	<u>616,684,443</u>

The accounting policies of the Bank on the classification of financial instruments in accordance with IFRS 9 are presented in Note 3. The application of these policies resulted in the reclassifications established in the previous table and explained below.

The following table reconciles the carrying amounts under IAS 39 with the carrying amounts under IFRS 9, in the transition to IFRS 9 on January 1, 2018:

	December 31, 2017 IAS 39	Reclassification	Remeasurement	January 1st IFRS 9
Financial assets				
At amortized cost				
Cash and cash equivalent				
Beginning balance	27,534,184	0	0	27,534,184
Ending balance	<u>27,534,184</u>	<u>0</u>	<u>0</u>	<u>27,534,184</u>
Loans				
Beginning balance	594,784,481	0	0	594,784,481
Remeasurement	0	0	(142,041)	(142,041)
Ending balance	<u>594,784,481</u>	<u>0</u>	<u>(142,041)</u>	<u>594,642,440</u>
Inversiones en valores				
Beginning balance	442,132	0	0	442,132
Remeasurement	0	0	(884)	(884)
Ending balance	<u>442,132</u>	<u>0</u>	<u>(884)</u>	<u>441,248</u>
Total at amortized cost	<u>624,657,714</u>	<u>0</u>	<u>(142,925)</u>	<u>624,514,789</u>
Available for sale				
Investments in securities:				
Beginning balance	43,933,581	0	0	43,963,581
A VRCOUI – instrumento de deuda	0	(40,323,668)	0	(40,323,668)

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A VRRCR	0	(3,609,913)	0	(3,609,913)
Ending balance	<u>43,933,581</u>	<u>(43,933,581)</u>	<u>0</u>	<u>0</u>
FVOCI – debt instruments				
Investments in securities:				
Beginning balance	0	0	0	0
From available for sale	<u>0</u>	<u>40,323,668</u>	<u>0</u>	<u>40,323,668</u>
Ending balance	<u>0</u>	<u>40,323,668</u>	<u>0</u>	<u>40,323,668</u>
Total FVOCI	<u>0</u>	<u>40,323,668</u>	<u>0</u>	<u>40,323,668</u>
FVTPL				
Investments in securities:				
Beginning balance	15,136,846	0	0	0
From available for sale	<u>0</u>	<u>3,609,913</u>	<u>0</u>	<u>18,746,759</u>
Ending balance	<u>0</u>	<u>3,609,913</u>	<u>0</u>	<u>18,746,759</u>
Total FVTPL	<u>0</u>	<u>3,609,913</u>	<u>0</u>	<u>18,746,759</u>
Total financial assets	<u>683,728,141</u>	<u>0</u>	<u>(142,925)</u>	<u>683,585,216</u>

	December 31, 2017 <u>IAS 39</u>	<u>Reclassification</u>	<u>Remeasurement</u>	January 1st <u>IFRS 9</u>
Financial liabilities				
At amortized cost				
Deposits from customer	208,545,977	0	0	208,545,977
Debt issuances	220,990,932	0	0	220,990,932
Borrowed funds				
Beginning balance	<u>187,147,534</u>	<u>0</u>	<u>0</u>	<u>187,147,534</u>
Total amortized cost	<u>616,684,443</u>	<u>0</u>	<u>0</u>	<u>616,684,443</u>

The following table analyzes the impact, net of taxes, of the transition to IFRS 9 regarding reserves and retained earnings. The impact is related to the reserve of fair value and the retained earnings. There is no impact on other components of equity.

	Impact on the adoption of IFRS 9 January 1st, 2018
Reserve for fair value	
Ending balance under IAS 39 (December 31, 2017)	1,738,846
Change of classification from investments available for sale to FVTPL	(113,401)
ECL recognition under IFRS 9 for investments in securities at FVOCI	119,147
Beginning balance under IFRS 9 (January 1st, 2018)	<u>1,744,592</u>
Retained Earnings	
Ending balance under IAS 39 (December 31, 2017)	21,932,674
Change of classification from investments available for sale to FVTPL	113,401
Deferred taxes	40,020
ECL recognition for loans under IFRS 9	(142,041)
ECL recognition for investments at FVOCI under IFRS 9	(119,147)
ECL recognition for investments at AC under IFRS 9	(883)
Beginning balance under IFRS (January 1st, 2019)	<u>21,824,024</u>

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(34) Financial Assets and Financial Liabilities, continued

The following table is reconciled:

- Provision for closing impairment for financial assets in accordance with IAS 39.
- The initial allowance for ECL determined in accordance with IFRS 9 as of January 1st, 2018.

	December 31, 2017 <u>IAS 39/IAC 37</u>	<u>Reclassification</u>	<u>Remeasurement</u>	January 1st <u>IFRS 9</u>
Allowance for loan losses according to IAS 39 / financial assets at amortized cost according to IFRS 9.	313,625	0	142,925	456,550
Investment in securities available for sale according to IAS 39 / debt financial instruments at FVOCI according to IFRS 9.	<u>0</u>	<u>0</u>	<u>119,147</u>	<u>119,147</u>
Total	<u><u>313,625</u></u>	<u><u>0</u></u>	<u><u>262,072</u></u>	<u><u>575,697</u></u>

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Consolidated Schedule - Information of the Consolidated Statement of Financial Position

Period ended June 30, 2018

(Stated in Balboas)

Assets	Consolidated	Eliminations	Sub-total	Banco	La	La
	Total			La Hipotecaria, S. A.	Hipotecaria de Colombia, C. F.	Hipotecaria El Salvador de C. V.
Cash and cash equivalents	214,345	0	214,345	212,712	683	950
Deposits in banks:						
Demand deposits in local banks	17,049,782	(2,574,948)	19,624,730	14,999,236	1,493,009	3,132,485
Demand deposits in foreign banks	3,132,485	2,574,948	557,537	0	0	557,537
Savings deposits in local banks	3,529,420	106,868	3,422,552	1,073,685	2,240,097	108,770
Savings deposits in foreign banks	754,067	(108,770)	862,837	860,935	0	1,902
Time deposits in local banks	2,200,000	0	2,200,000	2,200,000	0	0
Time deposits in foreign banks	0	0	0	0	0	0
Total deposits in banks	26,665,754	(1,902)	26,667,856	19,139,856	3,733,106	3,800,894
Total of cash, cash equivalents and deposits in banks	26,880,099	(1,902)	26,882,001	19,346,568	3,733,789	3,801,644
Investments in securities	58,771,506	0	58,771,506	53,662,932	5,108,574	0
Less: Investment reserves	1,312	0	1,312	1,205	107	0
Investment in securities, net	58,770,194	0	58,770,194	53,661,727	5,108,467	0
Investments in affiliates	0	(33,646,744)	33,646,744	33,284,484	0	362,260
Loans	635,707,559	0	635,707,559	461,815,889	54,056,887	119,834,783
Less: Allowance for loan losses	580,996	0	580,996	259,902	90,669	230,425
Loans, net	635,126,563	0	635,126,563	461,555,987	53,966,218	119,604,358
Furniture, equipment and improvements, net	2,388,989	0	2,388,989	1,950,439	196,804	241,746
Accounts and interests receivable	3,462,290	0	3,462,290	2,318,548	331,272	812,470
Accounts receivable from related companies	30,000	0	30,000	30,000	0	0
Tax credit	5,053,326	0	5,053,326	5,053,326	0	0
Deferred tax	1,080,062	0	1,080,062	64,975	945,959	69,128
Other assets	3,869,082	0	3,869,082	2,994,769	529,263	345,050
Total assets	736,660,605	(33,648,646)	770,309,251	580,260,823	64,811,772	125,236,656
Liabilities and Equity						
Liabilities:						
Deposits from customers:						
Local savings	928,170	(1,902)	930,072	930,072	0	0
Foreign savings	191,414	0	191,414	191,414	0	0
Local time	199,502,700	0	199,502,700	172,192,409	27,310,291	0
Foreign time	20,165,865	0	20,165,865	20,165,865	0	0
Total deposits from customers	220,788,149	(1,902)	220,790,051	193,479,760	27,310,291	0
Negotiable commercial papers	85,144,947	0	85,144,947	85,144,947	0	0
Negotiable commercial notes	102,848,222	0	102,848,222	102,848,222	0	0
Ordinary bonds	12,152,920	0	12,152,920	0	12,152,920	0
Investment certificates	9,600,000	0	9,600,000	0	0	9,600,000
Other negotiable debts	24,436,597	0	24,436,597	0	0	24,436,597
Accounts payable to related parties	0	0	0	0	0	0
Borrowed funds	198,850,071	0	198,850,071	129,194,651	625,440	69,029,980
Income tax payable	879,088	0	879,088	421,628	0	457,460
Other liabilities	11,464,733	0	11,464,733	8,744,850	653,396	2,066,487
Total liabilities	666,164,727	(1,902)	666,166,629	519,834,058	40,742,047	105,590,524
Equity:						
Common shares	15,000,000	(12,000)	15,012,000	15,000,000	0	12,000
Additional paid-in capital	25,025,329	(34,721,546)	59,746,875	25,025,329	28,934,546	5,787,000
Treasury shares	(727,000)	0	(727,000)	(727,000)	0	0
Capital reserve	1,800,000	0	1,800,000	0	0	1,800,000
Fair value reserve	1,164,565	0	1,164,565	1,170,037	(5,472)	0
Regulatory reserves	7,818,936	0	7,818,936	5,800,332	601,678	1,416,926
Investments reserve	169,803	0	169,803	149,587	20,216	0
Currency translation reserve	(4,271,446)	150,825	(4,422,271)	0	(4,422,271)	0
Retained earnings	23,591,482	11,768	23,579,714	14,008,480	(1,058,972)	10,630,206
Total equity attributable to the controlling interest	69,571,669	(34,570,953)	104,142,622	60,426,765	24,069,725	19,646,132
Non-controlling interest	924,209	924,209	0	0	0	0
Total equity	70,495,878	(33,646,744)	104,142,622	60,426,765	24,069,725	19,646,132
Total liabilities and equity	736,660,605	(33,648,646)	770,309,251	580,260,823	64,811,772	125,236,656

See the accompanying independent auditors' report.

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Consolidated Schedule - Information of the Consolidated Statement of Income and Other Comprehensive Income

Period ended June 30, 2018

(Stated in Balboas)

	Consolidated <u>Total</u>	<u>Eliminations</u>	<u>Sub-total</u>	Banco <u>La Hipotecaria, S. A.</u>	La Hipotecaria de <u>Colombia, C. F.</u>	La Hipotecaria <u>El Salvador de C.V.</u>
Interest and commissions income:						
Interest on:						
Loans	20,795,846	0	20,795,846	13,405,126	2,921,356	4,469,364
Investment securities	1,102,384	0	1,102,384	1,060,132	42,252	0
Deposits in banks	64,622	0	64,622	24,431	38,226	1,965
	<u>21,962,852</u>	<u>0</u>	<u>21,962,852</u>	<u>14,489,689</u>	<u>3,001,834</u>	<u>4,471,329</u>
Commission on:						
Management and servicing, net	2,766,803	0	2,766,803	2,198,634	59,890	510,179
Loan granting	1,215,271	0	1,215,271	972,599	0	242,672
Total interest and commissions income	<u>25,946,928</u>	<u>0</u>	<u>25,946,928</u>	<u>17,660,922</u>	<u>3,061,824</u>	<u>5,224,180</u>
Interest and commissions expense:						
Deposits	5,079,385	0	5,079,385	4,305,023	774,362	0
Borrowed funds	9,848,257	0	9,848,257	6,616,761	750,556	2,480,940
Commissions	616,163	0	616,163	446,469	51,975	117,719
Total interest expenses and commissions	<u>15,543,805</u>	<u>0</u>	<u>15,543,805</u>	<u>11,368,253</u>	<u>1,576,893</u>	<u>2,598,659</u>
Net interest and commissions income	<u>10,403,121</u>	<u>0</u>	<u>10,403,121</u>	<u>6,292,669</u>	<u>1,484,931</u>	<u>2,625,521</u>
Provision for loan losses	497,319	0	497,319	292,505	37,078	167,736
Provision for investments	51,085	0	51,085	52,441	(1,356)	0
Net interest and commission income, after provision	<u>9,854,717</u>	<u>0</u>	<u>9,854,717</u>	<u>5,947,723</u>	<u>1,449,209</u>	<u>2,457,785</u>
Income from banking services and others:						
Gain (loss) on investments, net	843,053	0	843,053	674,397	168,656	0
Other income	1,429,596	0	1,429,596	1,251,196	54,616	123,784
Total income from banking services and others, net	<u>2,272,649</u>	<u>0</u>	<u>2,272,649</u>	<u>1,925,593</u>	<u>223,272</u>	<u>123,784</u>
General and administrative expenses:						
Salaries and other personnel expenses	4,508,621	0	4,508,621	3,301,618	606,909	600,094
Depreciation and amortization	414,903	0	414,903	341,905	15,024	57,974
Professional and legal fees	1,034,856	0	1,034,856	766,500	91,229	177,127
Taxes	1,079,229	0	1,079,229	574,623	186,146	318,460
Other expenses	2,118,952	0	2,118,952	1,499,081	290,452	339,419
Total general and administrative expenses	<u>9,156,561</u>	<u>0</u>	<u>9,156,561</u>	<u>6,483,727</u>	<u>1,179,760</u>	<u>1,493,074</u>
Net income before income tax	<u>2,970,805</u>	<u>0</u>	<u>2,970,805</u>	<u>1,389,589</u>	<u>492,721</u>	<u>1,088,495</u>
Income tax	836,644	0	836,644	407,452	29,857	399,335
Net income	<u>2,134,161</u>	<u>0</u>	<u>2,134,161</u>	<u>982,137</u>	<u>462,864</u>	<u>689,160</u>

See the accompanying independent auditors' report.